


Corpus Christi Estate Planning Council  
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**Marital Property Issues in Drafting  
 Estate Planning Documents**

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**Constitutional Separate Property**

“All property ... of a spouse ...

- **owned or claimed before marriage, [or]**
- **acquired afterward by gift, devise or descent, ...**
- **shall be the separate property of that spouse ....”**

Tex. Const. art. 16, §15.

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**Constitutional Separate Property**

- **The Texas Constitution does not specifically define community property.**
- **It defines separate property and ... by implication ... everything else must, therefore, be community property.**

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**Constitutional Separate Property**

The **constitutional definition of separate property controls** and cannot be impinged upon by either the legislature or the husband and wife.

*Arnold v. Leonard*, 273 S.W.2d 799 (1925);  
*Kellett v. Trice*, 66 S.W.2d 51 (1902).

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**Constitutional Separate Property**

- Property **possessed** by either spouse during or on dissolution of marriage is **presumed to be community property**.

Tex. Fam. Code §3.003.

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**Constitutional Separate Property**

- The degree of proof necessary to establish that property is separate property is **clear and convincing evidence**.

Tex. Fam. Code §3.003.

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### Inception of Title

- The characterization of property as either separate property or community property is fixed at the **moment of inception** measured by the first right that a spouse had to the property.
- If the incipiency of the first right to the property was **before marriage**, the property is **separate property**.

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### Intrinsic Separate Property

**Property Acquired Before Marriage**

- Property claimed or acquired by either spouse **before marriage** is separate property.

- Tex. Const. art. 16, §15;
- Tex. Fam. Code §3.001(1);
- *Jensen v. Jensen*, 665 S.W.2d 107 (Tex.1984).

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### Intrinsic Separate Property

**Property Acquired by Devise or Descent**

- Property acquired by either spouse **by devise or descent** is separate property.

- Tex. Const. art. 16, §15;
- Tex. Fam. Code §3.001(2)

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**Intrinsic Separate Property**

- **Property Acquired by Third-Party Gift**
- Property acquired by either spouse by a **gift from a third party** is separate property.
  - Tex. Const. art. 16, §15;
  - Tex. Fam. Code §3.001(2)

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**Intrinsic Separate Property**

- **Property Arising from Interspousal Gift**
- Property acquired by a spouse by a **gift from the other spouse** is separate property.
  - Tex. Const. art. 16, §15

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**Intrinsic Separate Property**

- **Property Arising from Interspousal Gift**
- A gift from one spouse to the other spouse is **presumed to include a gift of the income from the property.**
  - Tex. Fam. Code § 3.005

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### Intrinsic Separate Property

- **Property Recovered for Personal Injury**
- Generally, property recovered by a spouse for **personal injury**, **excluding** a recovery for **lost earnings** and the **recoupment of medical bills**, is separate property.
  - Tex. Fam. Code §3.001(3)

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### Intrinsic Separate Property

- **Partition/Exchange Agreements**
- Spouses can agree in a **written agreement** that property is separate property and that income arising from a spouse's separate property will be separate property.
  - Tex. Const. art. 16, §15;
  - Tex. Fam. Code §4.102

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### Derivative Separate Property

- **"Derivative" separate property** is property that gets its separate-property character because it has an **intrinsic-separate-property source**.
- The property itself is not defined as separate property, but it is **separate property because it derives from an intrinsic-separate-property source**.

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### Derivative Separate Property

- **Property Acquired in Exchange for Separate Property**
- **Property acquired in exchange for separate property is separate property.**
- *Dixon v. Sanderson*, 10 S.W. 535, 536 (Tex.1888)

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### Derivative Separate Property

- **Property Acquired with Separate Funds**
- **Property acquired with separate property funds is separate property.**
- *Dixon v. Sanderson*, 10 S.W. 535, 536 (Tex.1888)

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### Mutation

Money from an account buys Google stock, which is sold to acquire a house. The money has "mutated" in form from cash in a bank to shares of Google stock to a house.

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### Derivative Separate Property

- **Property Acquired on Separate Credit**
- Property acquired on **separate credit** is separate property.
- *See Whorral v. Whorral*, 691 S.W.2d 32, 35 (Tex. App. – Austin 1985, writ dismissed).

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### Separate Property Credit

- "Lender agrees to look only to the separate estate of Borrower for the repayment of this note."  
... OR ...
- "The obligation to fund the original contribution for an ownership interest in the Partnership shall be a separate property obligation of the Partners and the Partnership will only look to the separate estate of a Partner to enforce the contribution obligations herein established for the acquisition of an interest in the Partnership."

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### The Separate Credit Issue

- **No Supreme Court Case** addressing the issue.
- **Not on the list of what is separate property in the Texas Constitution.**
- **No statutes** dealing with the issue.
- Inconsistent with the **"Rule of Implied Exclusion"** of *Arnold v. Leonard*.

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### A Spouse's Fiduciary Duty

- A spouse who has sole management rights over community property is considered a **trustee** of that property and owes the other spouse a **fiduciary duty** to use **utmost good faith and fairness** when dealing with sole-management community property.
  - See *In re Marriage of DeVine*, 869 S.W.2d 415, 421 (Tex. App. – Amarillo 1993, writ denied).

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### Creating Trusts

- Creating trusts wherein the beneficiary has a *present possessory interest in the corpus*.
  - "Wife" is married to "Husband."
  - Her wealthy uncle leaves \$20,000,000 to her **in trust**.
  - Wife has a **right to demand a distribution of the trust corpus (or a part of the trust corpus)** as a beneficiary.
    - The income from the portion over which the wife can make such a demand can be community property.

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### Creating Trusts

- Giving a married beneficiary a right to withdraw **corpus**, even a percentage of the corpus, (without specific language to the contrary) makes the income related to that corpus **community property**.

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### Creating Trusts

- Put in the trust instrument a statement that **“all income from this trust is a gift from the grantor to such beneficiary and, if the beneficiary is married, shall be that beneficiary’s separate property.”**

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### Partnerships & Tracing

- Spouse enters into a partnership agreement **requiring funding for an interest.**
- The spouse, wanting the partnership interest to be **separate property**, pays for it with his **separate property cash.**
- Possible Theory:** Inception of title is the partnership agreement, which fixes title as community property.

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### Partnerships & Tracing

ARTICLE IV  
CAPITAL CONTRIBUTIONS AND PARTNERSHIP INTERESTS

Definite Contributions

4.01. Upon execution of this Agreement, each partner shall reflect an "initial contribution" to the Partnership as described in Exhibit C, attached to this Agreement and incorporated by reference. Additional contributions are contemplated at this time. The amounts shown in Exhibits C and D reflect the amount of cash contribution made initially. Each Partner shall be personally liable for the contributions to the capital of the Partnership as shown in Exhibits C and D. Upon making the initial contribution as shown in Exhibit C, each Partner shall own the percentage interest in the Partnership as listed in Exhibit D, attached to this Agreement and incorporated by reference.

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### Oil & Gas Royalties


Oil Royalties →


Royalty payments received during marriage from a separate property mineral estate are **separate property**. See *Norris v. Vaughan*, 260 S.W.2d 676, 679 (Tex.1953).

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### Partnership Distributions


Oil Royalties →


Distributed profits from a partnership during marriage are **community property**. See *Marshall v. Marshall*, 735 S.W.2d 587, 594 (Tex. App. – Dallas 1987, writ ref'd n.r.e.).

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### Eggemeyer & Cameron

- When a marriage is being dissolved in Texas by divorce, **the court is required to confirm to each spouse his or her separate property**.
  - See *Cameron v. Cameron*, 641 S.W.2d 210, 214 (Tex.1982); *Eggemeyer v. Eggemeyer*, 554 S.W.2d 137, 139 (Tex.1977) (same); *see also* Tex. Fam. Code §7.002 (confirmation of separate property).

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**“Just & Right”**

- Tex. Fam. Code § 7.001.
- **GENERAL RULE OF PROPERTY DIVISION.**
  - In a decree of divorce or annulment, the court shall order a division of the estate of the parties in a manner that **the court deems just and right**, having due regard for the rights of each party and any children of the marriage.

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**Changing Entity Form**

- Husband has a separate property corporation.
- He wants to change the form of it to a limited partnership.
- He forms an LLC to be the general partner.

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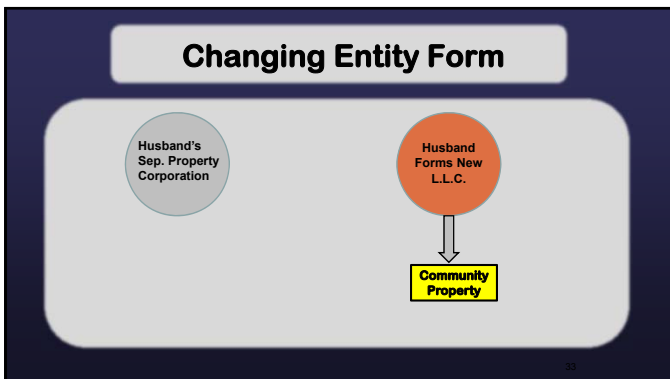
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### Changing Entity Form

- He and the LLC enter into a limited partnership agreement.
- Husband acquires 99% of the new limited partnership by contributing \$990 and is the sole limited partner.
- The new LLC acquires 1% of the new partnership by contributing \$10 and becomes the general partner.

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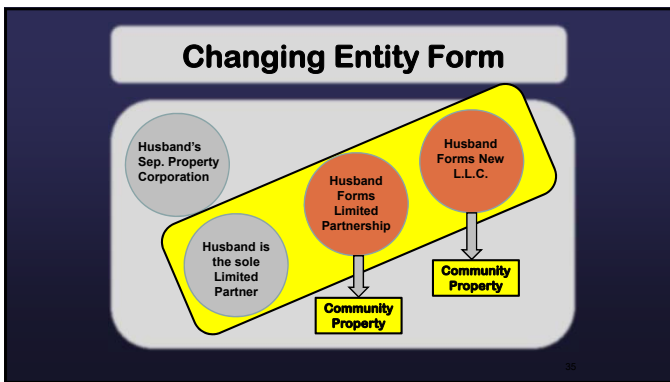
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### Changing Entity Form

- Husband then transfers his separate property corporation (or its assets) to the newly formed limited partnership.

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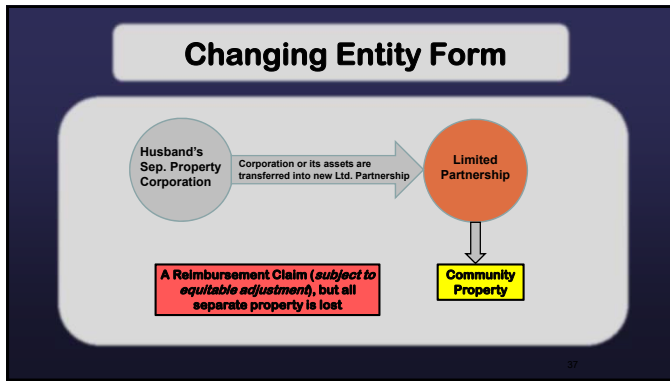
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- ### Starting New Divisions
- Husband has a separate property company.
  - He wants to start **three new divisions: marketing, distribution & finance.**
  - He forms three new companies (using **\$1,000 from his personal checking account (with C/P in it)** to fund the companies.
  - **All three new companies are community property.**

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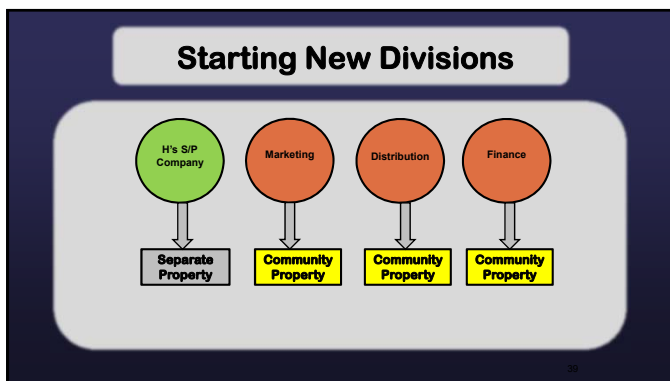
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### Starting New Divisions

- **Alternatives to Consider:**
  - Start **new divisions of the same company**; **no new companies ... or ...**
  - Form **subsidiaries** wholly owned by the separate property parent company ... and ...
  - If necessary or desired, effectuate a **"split-off"** divisive reorganization ... having the parent company transfer the shares of stock in the subsidiaries to the shareholder in exchange for shares of the parent (a mutation).

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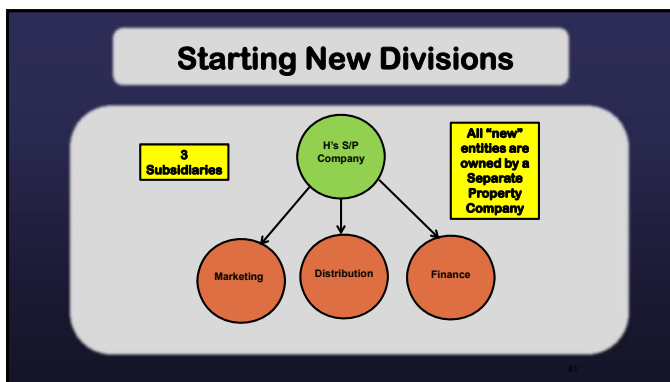
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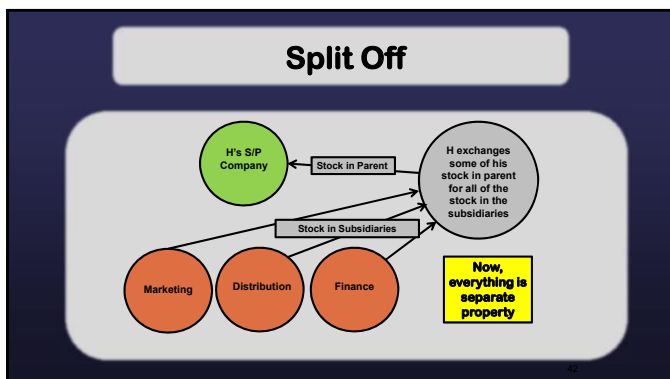
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### Buying Property

- Wife takes a **\$2,000,000 inheritance** (which is her separate property) and **buys a residence**.
- When she and her husband leave the title company, they don't notice it, **but the deed is in both of their names**.
- This is a **presumed gift** of 1/2 of the property to the husband (as his separate property).

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### Buying Property

- **Solutions:**
  - **Marital Agreement** (solves everything).
  - **Make sure the deed is only in the name of the wife, who provided the consideration.**
  - **Issue a statement of declaration of intent as to there not being a gift (even though the title is taken in both names).**

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### Buying Out Your Partner

- Husband owns **65%** of a company as his **separate property**.
- His **35% partner wants to sell** out and retire.

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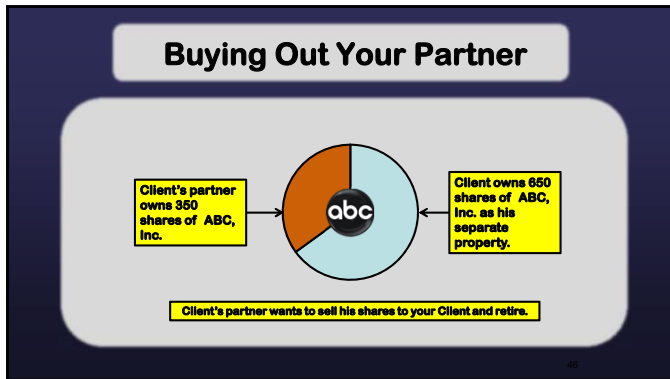
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- ### Buying Out Your Partner
- **Husband buys** his partner's 35%.
  - **Because he buys it during his marriage, unless he's careful, it becomes **community property**.**

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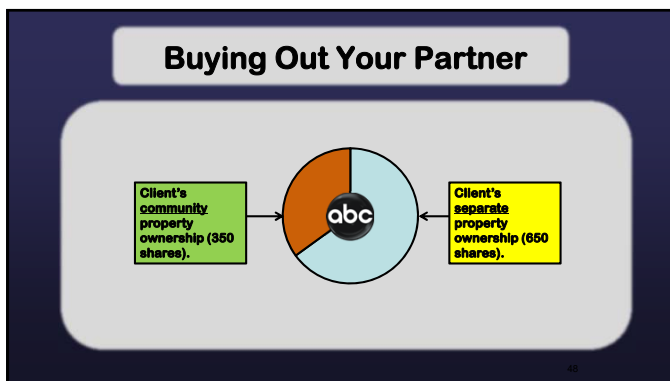
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### Buying Out Your Partner

- Instead, **have the company redeem the 35% partner's shares**, leaving only the husband's remaining shares as the outstanding shares in the company.
- All of the **husband's interest in the company remain his separate property** after the redemption.

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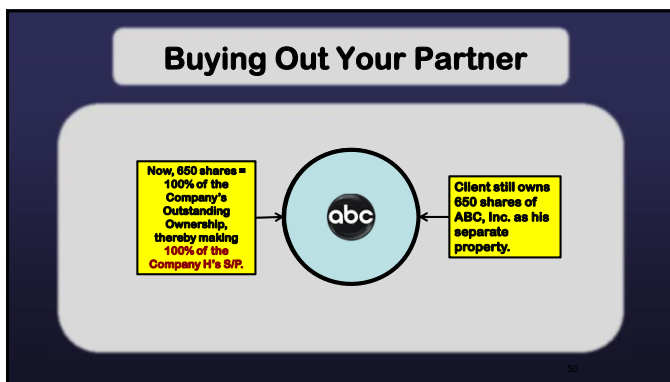
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### Entity to Entity Transfer of Assets

- Husband owns **XYZ, Inc.** as his separate property.
- It has very substantial retained earnings.
- XYZ, Inc. owns **SUB, Inc.**, a wholly-owned subsidiary.
- Husband owns **ABC, Inc.** as his separate property.
- **XYZ, Inc. transfers SUB, Inc. to ABC, Inc.**

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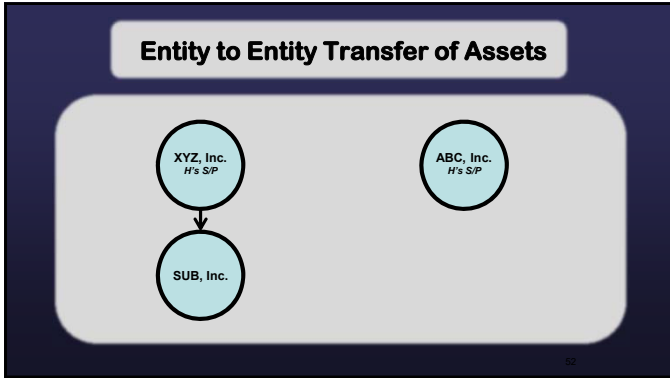
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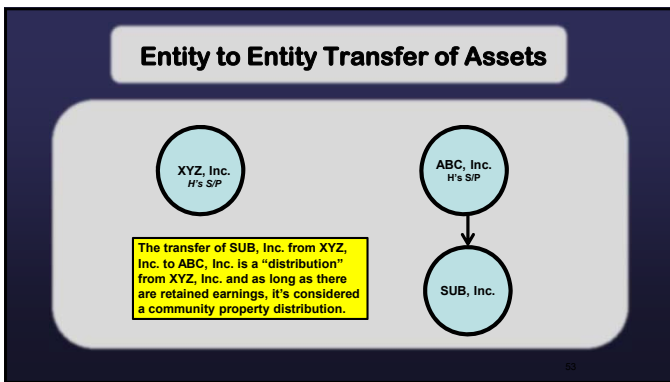
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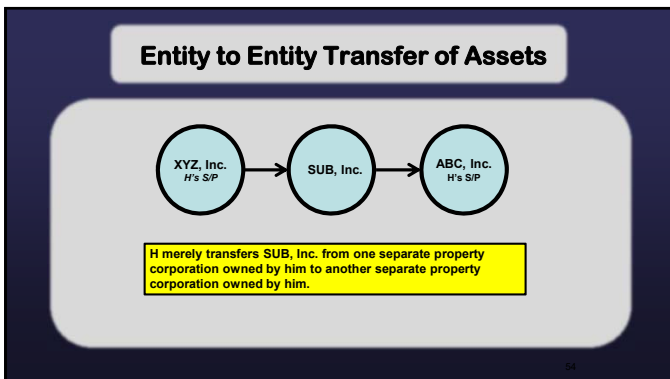
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### Entity to Entity Transfer of Assets

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graph TD
    XYZ((XYZ, Inc.))
    ABC((ABC, Inc.))
    SUB((SUB, Inc.))
    ABC --> SUB
          
```

So, when SUB, Inc. is thereafter acquired by ABC, Inc. it's a deemed transfer of community property to a separate property entity, giving rise to a community property reimbursement claim equal to the value of SUB, Inc.

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### Entity to Entity Transfer of Assets

- **Solution:**
  - Do a **split-off** of SUB, Inc. wherein H gives up some of his S/P stock in XYZ, Inc. in exchange for the stock of SUB, Inc.
  - SUB, Inc. is - at that time - a **mutation in form** of H's XYZ, Inc. stock and, therefore, H's separate property.
  - **Then, H can contribute XYZ, Inc. to ABC, Inc.** and there is no reimbursement claim.

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### Asset Sale

- H owns S/P Company (a pass-thru entity).
- H sells nearly all assets of the Company.
- The Company now has cash.
- H distributes a LOT, but not all, of the cash to himself.
- No shares are redeemed.
- S/P Company keeps on operating, but in a different business area.

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### Another Problem With Conversions

- H owns a S/P Corp. worth \$6,000,000.
- He wants to set up a limited partnership and needs a corporate general partner.
- He forms the limited partnership, and transfers the corporation's assets to the limited partnership.
- The S/P corporation gets .1% of the ownership of the limited partnership for the transfer.

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### Buy-Sell Agreement

- H and his best friend (BF) each own 50% of ABC, Inc.
- H & BF have a buy-sell agreement that says that in the event of divorce and one of their wives get any part of their stock, she has to sell it back to her former spouse **at book value**.
- **The company is worth 8x book value.**

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### Buy-Sell Agreement

- W gets the stock after a trial.
- It's worth 8x of book value.
- She has to sell it to H per the buy-sell agreement **at book value**.
- So, the real value for community property purposes is only book value. **H wins!**
- But ... H's right to buy the stock from W is a community property asset worth 7x book! **(A C/P "stock purchase option")**.

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**Pass Through Entities**

- Husband owns a separate property Subchapter S Corporation.
- The Corporation has income, the taxation of which is passed through to the married couple, which pays tax on the income.
- The income is not all distributed.
- The retained income is Corporate property; a reimbursement claim exists (*theoretically*).

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**The End**

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