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Treatment of Community Contributions to Mortgage Payments (Including Principal and Interest on Separate Property)

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THE TREATMENT OF COMMUNITY CONTRIBUTIONS TO MORTGAGE PAYMENTS (INCLUDING PRINCIPAL AND INTEREST) ON SEPARATE PROPERTY

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I. INTRODUCTION

Courts have not been clear on how to treat community contributions to mortgage payments, including interest, on property initially acquired by one spouse prior to the marriage.[1] The confusion derives from the courts' failure to define what is meant by an equitable lien.

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1. In this article I will refer to the spouse who originally acquired the separate property as the "owner spouse," and I will refer to the spouse who did not originally acquire the property but who has contributed community property to the paydown of mortgage principal and interest, "non-owner spouse."

First, the language in the opinions referring to equitable liens does not distinguish between a *pro tanto* lien that attaches at the time the community property contribution is made and a lien granted to secure a reimbursement claim at the time of the dissolution of the marriage.[2] To further compound this problem, some courts have relied on recent California authority without appreciating the extent of ownership rights accorded to the non-owner spouse in that state.[3] Second, courts have been confused over the valuation of the community property interest. While almost all courts giving a reimbursement claim have agreed that community property contributions which reduce the equity on a mortgage of the separate property of one spouse must be reimbursed, the courts have disagreed as to whether community property contributions toward interest must also be reimbursed. Some courts have not permitted reimbursement of the latter expense; others have held that expenses such as interest, taxes and insurance are offset by the benefit received by the community through use of the separate property.

To a large extent, the confusion in the case authority reflects the absence of a consistent approach to, and analysis of, the nature of the contribution of community property to the mortgage on separate property. On the one hand, the contribution of community property to the paydown of a separate property mortgage, including interest, could be viewed as an investment of community property by the husband and wife. If this is the case, one would expect that the husband and wife would actually acquire a community property ownership interest in the property with all the attendant benefits and risks of ownership such as dual management, inheritability and equitable division. Consequently, the spouse's claim should be for a partition of the subject property with the community property interest comprised of the principal and *pro rata* share of the appreciation attributable to the community property contributions, if any. This interest should be treated as an ownership interest from the time the husband and wife begin to make mortgage payments with community property. Furthermore, the community estate would not be entitled to any reimbursement for interest paid because it is part of the necessary cost of maintaining the community's capital investment.

On the other hand, such a contribution could be viewed as a loan thereby placing the husband and wife in the position of creditors of the separate property estate. As such, the community should be enti-

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2. IDAHO LAW FOUNDATION, COMMUNITY PROPERTY LAW OF IDAHO § 5.2, at 2-4 (Joann Henderson ed., 1982); Richard W. Bartke, *Yours, Mine and Ours—Separate Title and Community Funds*, 44 WASH. L. REV. 379, 398-405 (1969); Richard W. Mollerup, Comment, *Improvements to Real Property During Marriage: It's Time for Idaho to Make a Decision*, 28 IDAHO L. REV. 1021, 1026-27 (1992).

3. *See* discussion of Nevada and New Mexico, *infra* notes and accompanying text.

tled to reimbursement of the full amount loaned including that portion of the loan constituting interest on the mortgage. This claim could, of course, be offset by any claims the owner spouse has for non-donative benefits the community estate received from the use of the separate property such as the fair rental value of the separate property.

A combination of the above two approaches seem to hold sway in most jurisdictions. California, New Mexico and Nevada appear to follow an investment approach, treating the interest acquired through community contributions as an ownership interest. However, courts within these jurisdictions have not always been clear about the nature of the interest so acquired during the existence of an ongoing marriage as opposed to at dissolution. Thus, the courts have sometimes characterized the non-owner's claim at dissolution as one for reimbursement as opposed to division, and there has been disagreement about how to value the non-owner spouse's claim in the property.

Idaho, Washington, Arizona, Louisiana, Texas and Wisconsin appear to follow a creditor approach because these jurisdictions treat the non-owner spouse's claim as one for reimbursement rather than apportionment of an ownership interest. The confusion arises, however, because despite the apparent recognition of a creditor's claim, by way of reimbursement, most of these jurisdictions value the reimbursement claim based on an enhancement in value standard and they have discussed the possibility of an equitable lien in inconsistent and confusing ways.

In this article, I will review the approach of each of the nine community property states concerning the use of community property to pay mortgage principal and interest on separate property. I will then argue that the community estate ought to be treated as a creditor of the separate estate and should be entitled to reimbursement of both principal and interest contributed to acquisition of the separate property which may be secured by an equitable lien at the time of judgment, if appropriate. Finally, I will argue that to the extent any offset is permitted for benefits obtained by the community through use of the property, courts should entertain evidence as to the actual value of the benefit received by the community and should consider whether the use of the property was donative in nature.

II. STATE BY STATE APPROACH

A. California, Nevada and New Mexico

Recent California cases have adopted an investment approach to determine the nature and extent of the community property rights created when community property is used to reduce the principal, and pay interest on a separate property mortgage.[4] *Moore v. Moore*[5] culminated the development of the law in this area. In *Moore*, the California Supreme Court concluded that "the rule developed through decisions in California gives to the community a *pro tanto* community property interest in such property in the ratio that the payments on the purchase price with community funds bear to the payments made with separate funds."[6] Consistent with its holding that the community payments are in the nature of an investment and give rise to a present property interest, the court clarified that the community interest was not merely an "equitable charge" but instead should be characterized as "a community property interest in the house."[7] The court's underlying rationale in adopting the *pro rata* ownership approach is clear from its consistent reference to the community interest as an investment.[8] The court concluded that the payment of interest with community funds was not relevant in calculating the share of the community in the underlying property and was not reimbursable because such expenses represented "expenses incurred to maintain the investment."[9] Finally, the court reasoned that to the extent the property in question had increased in value due to market forces, the community and separate estates should share in the increase in value in proportion to their respective contributions to the purchase of the property.[10]

Thus, the *Moore* court calculated the community and separate property interest as follows: The separate property percentage interest consisting of the down payment and the proceeds of the mortgage loan, subtracted by the amount by which the community property reduced the balance of the loan.[11] The resulting sum is divided by

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4. California law has not always been so clear. Prior to the decision in Moore v. Moore, 618 P.2d 208, 210 (Cal. 1980) (en banc), one line of authority even suggested that no right, ownership or otherwise, was created by the expenditure of community funds on separate property. For an interesting discussion of the earlier confusion in California, see Bartke, *supra* note 2, at 405-10. The author notes there that "[t]he law of California must be discussed separately. It defies not only classification, but rationalization as well." *Bartke, supra* note 2, at 405-10.

5. 618 P.2d 208 (Cal. 1980) (en banc).

6. *Id.* at 210 (emphasis added) (quoting Forbes v. Forbes, 257 P.2d 721, 722 (Cal. Dist. Ct. App. 1953)).

7. *Id.* at 210 n.1.

8. *Id.* at 210. *Pro rata* ownership refers to the idea that the present ownership interest is apportioned between the separate and community estates in relation to the amount of consideration provided by each. WILLIAM A. REPPY, JR. & CYNTHIA A. SAMUEL, COMMUNITY PROPERTY IN THE UNITED STATES 6-5 (4th ed. 1994). By contrast, the inception of right doctrine fixes ownership at the time there is a right to acquire title. *Id.* at 6-4. Thereafter, under the inception of right doctrine, contributions of consideration give rise to only a right of reimbursement.

9. *Moore*, 618 P.2d at 211.

10. *Id.* Presumably, if the value of the property had decreased the community and separate share of ownership would also decrease proportionally.

11. *Id.*

the purchase price.[12] The result is the separate property percentage share in the property. Conversely, the community property share is arrived at by dividing the amount the community property payments reduced the principal by the purchase price.[13] The resulting percentages are applied to the fair market value of the property to determine the value of the community property interest in the property.[14]

Like California, Nevada also appears to adopt an investment approach. However, although the case law is fairly consistent, confusing language in the court opinions could lead to conflicting outcomes. Recently, in *Malmquist v. Malmquist*,[15] the Nevada Supreme Court relied extensively on California's *Moore* decision in delineating the nature and extent of the community property interest in real estate acquired by one spouse prior to marriage but where community property was used to reduce the mortgage principal and interest.[16] Unfortunately the clarity and consistency of the California reasoning and approach was not maintained in the Nevada decision because the

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12. *Id.*

13. *Id.*

14. *Id. Moore* has been criticized for assigning the entire value of the outstanding loan balance to the spouse who acquired the property. *See* Peter M. Moldave, Comment, *The Division of the Family Residence Acquired with a Mixture of Separate and Community Funds*, 70 CAL. L. REV. 1263, 1286 (1982) ("The . . . [*Moore*] method is defective, however, as applied to loans which are taken out by one party before marriage and paid by the other or by the community after marriage. The defect is that, as part of its allocation of the appreciation in proportion to the contributions to the purchase price, . . . [*Moore*] treats the loan proceeds as an asset that was contributed entirely as separate or community property. This means that the loan proceeds are misallocated to the extent that principal payments are made by other than the interest taking out the loan.").

15. 792 P.2d 372 (Nev. 1990).

16. *Id.* at 376-77. Consistent with the critique of *Moore* in Moldave, *supra* note 14, at 1286, the Nevada court modified the valuation formula adopted in *Moore* so that the balance of the loan is allocated to the separate and community payments in proportion to the number of payments each interest made as opposed to the amount of principal contributed by the community. *Malmquist*, 792 P.2d at 377.

Despite the *Malmquist* court's extensive reliance on *Moore*, a California case, the concept that community contributions to a mortgage on separate property give rise to a *pro tanto* community property interest in the property had been long recognized by Nevada courts. *See* Barrett v. Franke, 208 P. 435, 437 (Nev. 1922) ("[T]he property would have been community property 'to the extent and in the proportion that the consideration furnished by the community, the spouse supplying the separate funds have a separate interest in the property in proportion to the amount of his or her investment' " (quoting Guye v. Guye, 115 P. 731, 735 (Wash. 1911))); *see also* York v. York, 718 P.2d 670, 671 (Nev. 1986) (holding that if part of separate property is purchased with community funds, the community acquires a *pro tanto* interest in that property); Sly v. Sly, 679 P.2d 1260, 1262 (Nev. 1984) (explaining that the community acquires an interest to the extent of the purchase price contributed by the community); Robison v. Robison, 691 P.2d 451, 453 (Nev. 1984) (concluding that the community is entitled to a *pro tanto* interest in separate property).

court used the terms reimbursement and ownership interchangeably. For example, the Nevada court stated:

> Both parties agree that the community and separate property interests are entitled to *reimbursement* to the extent that those interests actually contributed towards reduction of the principal on the mortgage . . . . Additionally, this court has recognized that the community is entitled to a *pro rata ownership* share in property which community funds have helped to acquire.[17]

The use of the term "reimbursement" by the Nevada court is inconsistent with the basic premise of *Moore* that the community is entitled to an ownership interest. By characterizing the claim as one for reimbursement, the court implies that no right arises unless and until the marriage is dissolved; generally speaking, reimbursement refers to the right of a spouse, upon dissolution of the marriage, to seek an accounting and compensation for contributions to the separate property of the other spouse.[18] While a *pro tanto* ownership right may have to be valued at the time of dissolution in order to facilitate distribution, it is nonetheless a pre-existing right in the property itself. Presumably both spouses would be able to assert ownership rights to the property during the existence of an ongoing marriage, and the rights would be inheritable.[19] Moreover, because a *pro tanto* interest is created the property would presumably be subject to dual management rules and to creditor's claims as community property and not merely the separate property of one spouse. Finally, the property should be subject to equitable division at divorce.

This confusion over the consequence of recognizing an ownership right as opposed to a claim for reimbursement is reflected in other Nevada authority. For example, in *Robison v. Robison*[20] the court refused to consider the benefit the community received in using a residence owned by one spouse prior to marriage as the family residence, analogizing the situation to the implied gift that arises when one spouse uses his or her separate property to pay community expenses.[21] This analogy clearly implies that the court viewed the

17. *Malmquist*, 792 P.2d at 376 (emphasis added).

18. *See, e.g.*; Bartke, *supra* note 2, at 386.

19. California appears to have concluded, consistent with its finding of an ownership interest, that ownership rights exists during an ongoing marriage. In Reiserer v. Foothill Thrift & Loan, 256 Cal. Rptr. 508 (Ct. App. 1989), a court recognizing the creation of such a *pro tanto* community interest, granted a preliminary injunction to a wife seeking to block foreclosure of property acquired by her husband prior to marriage but paid for, in part, by community property contribution to the mortgage. *Id.* at 511. In addition, such ownership rights would include the requirement that both spouses consent to the alienation or encumbrance of community property. *Id.*

20. 691 P.2d 451 (Nev. 1984).

21. *Id.* at 454.

house as the spouse's separate property despite the fact that the court had just concluded that the community contribution to the mortgage payments created a *pro tanto* community property interest in the house.[22]

Thus, while Nevada appears firmly wedded to the same sort of investment approach adopted in California, troubling language in some of the Nevada opinions indicates that the court may not fully recognize the consequences of the ownership interest created by the contribution of community property to a mortgage on one spouse's separate property.

Like Nevada, the New Mexico Supreme Court has followed *Moore*, but has not truly clarified the nature of the interest created when community funds are used to pay the mortgage on property acquired by one spouse prior to marriage. In *Chance v. Kitchell*,[23] the New Mexico Supreme Court treated the surviving spouse as a co-tenant with the deceased spouse's heirs with respect to property acquired by the deceased spouse prior to marriage, but upon which mortgage payments were made with community property.[24] The extent of the surviving spouse's co-tenancy was apparently equal to the contribution of community funds to the reduction of principal on the house.[25] In a subsequent case, *Dorbin v. Dorbin*,[26] the New Mexico Court of Appeals relied on *Moore*, in apportioning the ownership interests in a family home initially acquired by the wife as her separate property but upon which mortgage payments were made with community property.[27]

Chance is a curious case in that the court characterized the community interest as an ownership interest, but employed language suggesting that the community right is in the nature of a reimbursement claim.[28] As the *Dorbin* court recognized, the supreme court implicitly accepted the notion that the community property contributions to equity create a property interest to the extent of the contribution and attributable appreciation. This conclusion logically flows from the *Chance* court's conclusion that the wife was a cotenant with the husband's heirs.[29] Since the husband had initially acquired the

22. *Id.* at 453.

23. 659 P.2d 895 (N.M. 1983).

24. *Id.* at 897.

25. *Id.* The court relied on *Moore* for the proposition that community contributions to interest, taxes and related expenses did not give rise to a community property interest in the property. *Id.* (citing Moore v. Moore, 618 P.2d 208, 210-11 (Cal. 1980)).

26. 731 P.2d 959 (N.M. Ct. App. 1986).

27. *Id.* at 963. Earlier New Mexico cases had reached similar results but were not as clear regarding the method of apportioning ownership. *See, e.g.*, Hertz v. Hertz, 657 P.2d 1169, 1176 (N.M. 1983); Michelson v. Michelson, 551 P.2d 638, 645 (N.M. 1976).

28. *See Chance*, 659 P.2d at 897.

29. *Id.*

property before the marriage with his separate property, the only basis for the wife's cotenancy could be that the community contributions created a community property interest which she then inherited under New Mexico intestacy law when the husband died. In *Dorbin*, the court of appeals recognized the creation a property interest by distinguishing between claims for reimbursement, which, according to the court, arise when community property is used to benefit a separate estate but no asset is acquired, from claims for apportionment, which the arise when mixed community and separate property are used to acquire an asset.[30]

Thus, while the New Mexico Supreme Court does not provide much of a hint about its rationale, it appears certain in light of the court of appeals decision in *Dorbin* that the New Mexico courts will treat community property contributions to mortgage payments on separate property as giving rise to a community interest in the property equal to the reduction in equity and the proportional appreciation.

The investment approach adopted by California has the benefit of treating the community contribution to mortgage payments on separate property in a consistent way. However, courts adopting the approach have not always clarified the full significance of recognizing such ownership rights. None of the jurisdictions adopting the investment approach have fully addressed questions such as whether the interest is subject to the testamentary power of the non-owner spouse, or whether the consent of both spouses is necessary to sell or encumber the property. Moreover, the impact of these unrecorded interests on the claims of bona fide purchasers of the property has not fully explored.

B. Louisiana

The Louisiana Civil Code and Louisiana courts have adopted a creditor approach, by treating the contribution of community property to the reduction of mortgage indebtedness on separate property as giving rise to a claim for reimbursement.[31] This claim is equal to

30. *Dorbin*, 731 P.2d at 964.

31. LA. CIV. CODE ANN. art. 2364 (West 1985). Article 2364 expressly refers to a claim for reimbursement. *See also* Loyacono v. Loyacono, 618 So. 2d 896, 898 (La. Ct. App. 1993) (holding that the non-owner spouse was entitled to reimbursement of one-half of the community property spent on the improvements or the enhanced value of the property); Parker v. Parker, 517 So. 2d 264, 266 (La. Ct. App. 1987) (holding that the non-owner spouse was entitled to reimbursement of one-half of the principal payments on the mortgage); Longo v. Longo, 474 So. 2d 500, 503 (La. Ct. App. 1985) ("[T]he reimbursement should be limited to one-half the amount of principal paid on the mortgage notes."), *cert denied*, 477 So. 2d 711 (La. 1985); Cook v. Cook, 457 So. 2d 235, 241 (La. Ct. App. 1984) (holding that only the principal paid on the mortgage is a debt owed to the community); Willis v. Willis, 454 So. 2d 429, 430-31 (La. Ct. App. 1984) (holding that the non-owner

one-half the amount that the principal is reduced through the use of community property.[32] The primary justification for measuring the reimbursement claim by reduction of principal only and not including interest in the recovery is that the latter is the cost of maintaining the civil fruits of the separate property for the benefit of the community.[33]

The approach of the Louisiana appellate court is puzzling in light of the express language of the 1980 amendments to Louisiana matrimonial regimes law. Prior to 1980, claims for reimbursement for community funds used to reduce a separate property obligation were governed by article 2408 of the Louisiana Civil Code of 1870.[34] Article 2408 provided a right of reimbursement when separate property increased in value as a result of community contributions measured by one-half the enhanced value.[35] Article 2408 was replaced by several new articles that attempted to codify the doctrinal refinements that had developed under article 2408.[36] Even though the primary goal of the revisions regarding reimbursement was to codify the case

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spouse was entitled to reimbursement of one-half of the principal payments on the mortgage).

32. *See* Loyacono v. Loyacono, 618 So. 2d 896, 898 (La. Ct. App. 1993); Parker v. Parker, 517 So. 2d 264, 266 (La. Ct. App. 1987), *writ denied*, 477 So. 2d 711 (La. 1985); Cook v. Cook, 457 So. 2d 235, 241 (La. Ct. App. 1984); Willis v. Willis, 454 So. 2d 429, 430-31 (La. Ct. App. 1984).

33. *Parker*, 517 So. 2d at 266 ("[T]he payment of interest benefited the community because this was a cost of maintaining the natural and civil fruits of this separate property for the community's use. Therefore, the interest cost should not be included in the amount to which the other spouse is entitled to reimbursement."). Apparently the Louisiana courts are ready to presume that the benefits received by the community are equal to interest costs. It does not appear that the independent factual finding regarding the value to the community of residing in the separate property house are necessary to support the courts' conclusion that only principal is reimbursable.

34. 1972 COMPILED EDITION OF THE CIVIL CODES OF LOUISIANA art. 2408 (West 1973) (repealed 1979).

35. *Id.* Article 2408 provided:

> When the separate property of either the husband or the wife has been increased or improved during the marriage, the other spouse, or his or her heirs, shall be entitled to the reward of one half of the value of the increase or ameliorations, if it be proved that the increase of ameliorations be the result of common labor, expenses of industry; but there shall be no reward due, if it be proved that the increase is due only to the ordinary course of things, to the rise in value of the property, or to the chances of trade.

Id. Under this provision the recovery for community contributions that reduced a separate indebtedness was equal to the enhancement in value, or, in other words, one half the reduction in principal. *See* Hurta v. Hurta, 260 So. 2d 324, 327 n.4 (La. Ct. App. 1972).

36. LA. CIV. CODE ANN. arts. 2358-2368 (West 1985 & Supp. 1994); *see also* Katherine S. Spaht & Cynthia Samuel, *Equal Management Revisited: 1979 Legislative Modifications of the 1978 Matrimonial Regimes Law*, 40 LA. L. REV. 83, 141-142 (1979).

law developed under the former provisions, some important changes in the approach to these issues appears to have been intended. In particular, the revisions of article 2408 apparently were intended to change the measure of reimbursement.[37] This intent can be seen in the express language of article 2364 of the revised matrimonial regime law which applies to reductions in separate property obligations with community funds.[38] Article 2364 provides: "If community property has been used to satisfy a separate obligation of a spouse, the other spouse is entitled to reimbursement upon termination of the community property regime for one-half of the *amount or value that the property had at the time it was used.*"[39] This language appears to focus the reimbursement inquiry on the value of the community property used to reduce the indebtedness rather than on the impact of reducing the indebtedness on the underlying separate property. To the extent that a mortgage interest is an obligation of the separate estate, community property used to reduce such indebtedness should rightfully be reimbursed under article 2364. Moreover, the interest obligation would appear to be a separate obligation because the definition of "community obligation" in the Louisiana code does not appear to include obligations acquired prior to the marriage.[40]

The comments to article 2364 also appear to support the idea that the drafters of the provision intended to abandon the enhancement in value test and adopt a different measure of recovery in these sorts of cases. The comments provide:

> Article 2408 of the Louisiana Civil Code of 1870 created a right to reimbursement when separate property increased in value due to community contributions, and the measure of reimbursement was one-half the enhanced value. Article 2364 *instead* treats community property used to satisfy a separate obligation as an interest-free loan.[41]

The language of this comment appears to anticipate that the interest free loan analysis will lead to a different measure of the recovery than did the enhanced value standard. The only way this could be

37. Spaht & Samuel, *supra* note 36, at 142.
38. LA. CIV. CODE ANN. art. 2364.
39. *Id.* (emphasis added).
40. Article 2360 defines community obligations as follows: "An obligation incurred by a spouse *during the existence of a community property regime* for the common interest of the spouses or for the interest of the other spouse is a community obligation." LA. CIV. CODE ANN. art. 2360 (West 1985) (emphasis added). *But see* Spaht & Samuel, *supra* note 36, at 142 ("Under article 2360 . . . the definition of a community obligation includes one incurred during the regime for the common interest of the spouses. The definition in Act 709, however, also includes an obligation incurred for the interest of the other spouse.").
41. LA. CIV. CODE ANN. art 2364 cmt.d (West 1985) (emphasis added).

true is if contributions to interest in addition to principal are reimbursable.

C. Texas and Arizona

Like Louisiana, Texas has adopted a creditor approach for evaluating the interest a spouse has when community property is used to reduce the indebtedness on separate property with the added availability of an equitable lien.[42] Until the Texas Supreme Court's 1990 decision in *Penick v. Penick*,[43] the Texas courts had purported to treat claims for reimbursement based on community contributions to the reduction of separate property indebtedness differently than claims based on community contributions to capital improvements on separate property. Capital improvement claims were reimbursed based on an enhancement of value standard.[44] However, until *Penick*, the lower Texas courts were in complete disarray regarding the method of valuing a reimbursement claim based on reduction of indebtedness.[45] In *Penick*, the Texas Supreme Court resolved the disunity among the lower Texas courts by holding that a reimbursement claim based on community property contributions to the reduction of indebtedness on one spouse's separate property should be treated the same as claims based on capital improvements and that both types of claims should be based on an enhancement in value

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42. *See* Penick v. Penick, 783 S.W.2d 194, 194 (Tex. 1990) ("This divorce case concerns the proper measure for reimbursement when community funds are used to pay a prenuptial, purchase money debt.") Despite the reimbursement language of *Penick* and most other modern Texas cases in this area, early Texas cases speak of the claim arising from community contributions that reduce separate property indebtedness as being in the nature of an "equitable charge" on the subject property. *See, e.g.*, Dakan v. Dakan, 83 S.W.2d 620, 629 (Tex. 1935). Such an equitable charge appears similar in nature to the *pro tanto* community property interest that arises in California under the same circumstances, although California professes to acknowledge a more substantial interest than an equitable charge. *See supra* notes 4-19 and accompanying text. In any case, such a charge would create an interest in the property merely by virtue of the contribution of community property to the reduction of the indebtedness. Such an interest would seem to inconsistent with the language of more modern Texas cases that speak exclusively of a claim for reimbursement. Many of these modern cases result in the placing of a equitable lien on the separate property of the spouse who benefited from the reduction of indebtedness; however, these cases appear clearly to be referring to a lien in the nature of a judgment lien. *See* Mullins v. Mullins, 785 S.W.2d 5, 11-12 (Tex. Ct. App. 1990); Joseph W. McNight, *Family Law: Husband and Wife*, 45 Sw. L.J. 415, 422-23 (1991).

43. 783 S.W.2d 194 (Tex. 1988).

44. *See* Anderson v. Gilliland, 684 S.W.2d 673, 675 (Tex. 1985) ("[A] claim for reimbursement for funds expended by an estate for improvements to another estate is to be measured by the enhancement in value to the benefited estate.").

45. The confusion in the Texas courts is aptly documented in Fred C. Weekley, *Reimbursement Between Separate and Community Estates—The Current Texas View*, 39 BAYLOR L. REV. 945, 963-65 (1987).

measure.[46] Beyond concluding that it could see little distinction between the two types of claims and surmising that the distinction was the result of "historical accident," the court offered little analysis to support its conclusion.[47]

In addition to its reasoning that community claims for reduction of mortgage indebtedness should be measured by an enhancement in value test, the court concluded that the separate estate could offset the reimbursement claim by showing that the community received benefits from the use of the separate property.[48] In *Penick*, specifically, the court upheld the trial court's conclusion that tax advantages obtained by the community as a result of depreciating the husband's separate property real estate should be set off against the wife's reimbursement claim for community contributions to the payment of indebtedness on that property.[49]

Arizona adopts a creditor approach similar to that of Texas. The Arizona courts have been clear that the use of community funds to pay the mortgage on property acquired as the separate property of one spouse does not change the separate character of the property.[50] In *Drahos v. Rens*,[51] the Arizona Court of Appeals held that the community, while not acquiring a property interest in the separate property through the payment of mortgage payments, was entitled to compensation and to an equitable lien against the separate property.[52] Thus, Arizona, like Texas, appears to grant the non-owner spouse some level of interest in the underlying property above and beyond a mere claim for reimbursement.[53]

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46. *Penick*, 783 S.W.2d at 197.
47. *Id.*
48. *Id.* at 197-98.
49. *Id.*
50. *See, e.g.*, Drahos v. Rens, 717 P.2d 927, 928 (Ariz. Ct. App. 1985) ("[A] residence which is separate property does not change its character because it is used as a family home and mortgage payments are made from community funds."); Potthoff v. Potthoff, 627 P.2d 708, 713 (Ariz. Ct. App. 1981) ("If the husband satisfied [a] separate obligation with community funds, then, at most, the community might acquire a claim for reimbursement for such payment in the nature of an equitable lien on the property.").
51. 717 P.2d 927 (Ariz. Ct. App. 1985).
52. *Id.* at 928-29.
53. *See, e.g.*, Horton v. Horton, 278 P. 370, 371 (Ariz. 1929) (recognizing that an equitable lien arises for the amount of community property funds used to pay mortgage on separate property); Wolfswinkel v. Superior Court, 700 P.2d 852, 854 (Ariz. Ct. App. 1984) ("An equitable lien is a right over property constituting an encumbrance, so that the property itself may be proceeded against in an equitable action and either sold or sequestered upon proof of a contract out of which the lien could grow or of a duty on the part of the holder so as to give the other party a charge or lien on it. It is merely floating equity until the time that a judgment or decree is rendered actually subjecting the property to the payment of the debt or claim.").

In addition to Arizona's hybrid reimbursement/equitable lien approach, the courts there have, even more curiously, looked to California to determine the measure of the community claim for reimbursement. *Drahos,* in particular, relied on a California decision that applied the *Moore*[54] formula for *pro tanto* ownership, *In re Marriage of Marsden,*[55] to reach its conclusion that the reimbursement claim should be measured by a "value-at-dissolution/enhanced value" formula.[56]

The analytical basis for the Arizona and Texas approaches to the characterization of community contributions to the reduction of a mortgage on separate property is simply not clear. The use of a reimbursement-oriented theory is inconsistent with the granting of an equitable lien that appears to arise during marriage as community mortgage payments are made. One must ask whether the existence of such a lien would prevent the owner-spouse from alienating the property during the existence of the marriage. Normally the owner of property subject to an equitable lien has the duty to not deal with the property in such a way as to destroy or interfere with the equitable lien.[57] Yet this negative duty could prove to be singularly elusive since, the non-owner spouse may not bring his or her reimbursement claim to effectuate the equitable lien until a divorce is filed. By that time, the property could be long gone!

By granting an equitable lien measured by an enhancement in value standard, Arizona and Texas treat the community property estate as if it were an owner of the property even though one of the spouses does not have any accoutrements of ownership during the existence of the ongoing marriage. Just as the equity only reimbursement cases are inconsistent with the theory of reimbursement, so too are the cases that permit recovery for the appreciation attributable to the reduction in principal associated with payments of community property. Such ownership benefits would include the right to exercise testamentary power over a spouse's share of the community property interest, the availability of equitable division of the asset at divorce,[58] and the applicability of the dual management rules if the

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54. Moore v. Moore, 618 P.2d 208, 212 (Cal. 1980).

55. 181 Cal. Rptr. 910, 915 (Ct. App. 1982) (citing Moore v. Moore, 618 P.2d 208 (Cal. 1980)).

56. *Drahos,* 717 P.2d at 929. In an especially confusing opinion, one Arizona appellate court appears to have endorsed a measure of recovery equal to "community funds expended for the benefit of" the separate estate. Hanrahan v. Sims, 512 P.2d 617, 621 (Ariz. Ct. App. 1973). This language seems to authorize a creditor approach to the resolution of the community claim as opposed to an enhancement in value standard. The opinion is especially confusing because it relies on authority that expressly adopts the enhancement in value standard. In addition, to the extent the opinion appears to authorize a non-enhancement test, the *Drahos* court expressly disavowed it. *Drahos,* 717 P.2d at 929.

57. I AUSTIN W. SCOTT & WILLIAM F. FRATCHER, THE LAW OF TRUSTS §10 (4th ed. 1987).

58. In most community property states, a divorce court only has jurisdiction

property is real estate. Enhancement rules can also be unfair to the spouse who makes his or her separate property available during the marriage for the spouses' use and enjoyment, foregoing the availability of rent and finds that he or she must make substantial restitution to the community in the form of a reimbursement claim.

Measuring the reimbursement claim by an enhancement in value standard is also inconsistent with the theory that the community estate is in the position of a creditor vis a vis the separate property estate. A third-party creditor who loaned money toward the purchase of real estate would not be entitled to share in the appreciation of that real estate during the time of the loan. Little rationale exists for treating spouses who loan assets to one of the spouses for the acquisition of property differently.

D. Idaho and Washington

While apparently also adopting the creditor approach of "reimbursement supported by lien," the Idaho courts have often engaged in confusing and inconsistent analysis of claims involving the expenditure of community funds on a mortgage of separate property. In *Fisher v. Fisher*[59] the Idaho Supreme Court held that the use of community funds to make mortgage payments did not change the character of property acquired by one of the spouses prior to marriage.[60] The court concluded that the non-owner spouse was entitled to "reimbursement for one-half of the community funds applied toward [the payment of the purchase contract price]" on certain property.[61] The court allowed reimbursement based on the amount of community funds expended as opposed to value of the underlying property.[62] This result is completely consistent with a creditor approach to the resolution of the claim. In a later decision, *Griffin v. Griffin*,[63] the Idaho Court of Appeals applied *Fisher*, concluding:

> [T]he use of community funds to make payments on the purchase price [of property initially acquired by one spouse prior to marriage] does not change the character of the property from separate to community. However, the non-owner spouse has the right to reimbursement for *one-half of the community funds* applied toward payments on the property.[64]

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to divide community property and cannot divest a spouse of his or her interest in separate property.

59. 86 Idaho 131, 383 P.2d 840 (1963).
60. *Id.* at 136, 383 P.2d at 842-43.
61. *Id.* at 136, 383 P.2d at 843.
62. *Id.*
63. 102 Idaho 858, 642 P.2d 949 (Ct. App. 1982).
64. *Id.* at 861, 642 P.2d at 952 (emphasis added).

Fisher and *Griffin* appear to be the only Idaho cases that cleanly address the question of the treatment of community funds used to reduce the indebtedness on property acquired prior to marriage by one of the spouses. However, in focusing on the amount of community funds expended, they stand in stark contrast to a line of related Idaho cases dealing with community contribution to the reduction of indebtedness on separate chattel, physical improvements by the community on the separate property of one spouse, and cases where community property has been used for a mixture of making physical improvements and reducing indebtedness on separate property. Cases addressing these issues hold that the community contributions do not change the character of the property, but the community's reimbursement claim is measured by using an enhancement in value formula. *Gapsch v. Gapsch,*[65] a curious case in which the spouses were appealing, in part, the disposition of a $50 increase in value of an antique automobile, is the leading Idaho case.[66] In *Gapsch*, the court set down an approach followed in numerous later cases:

> As a general rule where the separate property of the husband is improved or his equity therein enhanced by community funds the community is entitled to be reimbursed from such separate estate . . . . The claim for reimbursement has been held to be in the nature of a charge or an equitable lien against such separate property so improved or the equity of the husband therein enlarged. It would appear that the measure of the compensation generally is the increased value of the property due to the improvement; in instances where his equity therein has been increased through the application of community funds to the payment of the debt thereon the measure should be the amount by which such equity is enhanced.[67]

Neither *Fisher* nor *Griffin* dealt directly with the issue of how to measure the reimbursement claim. In both cases, the only issue pre-

65. 76 Idaho 44, 277 P.2d 278 (1954).

66. *Id* at 52, 277 P.2d at 282.

67. *Id.* at 53, 277 P.2d at 283. *Gapsch* has been followed in many Idaho cases. *See, e.g.,* Suter v. Suter, 97 Idaho 461, 465, 546 P.2d 1169, 1173 (1976) (holding that non-owner spouse is entitled to reimbursement for community funds used to make physical improvement on husband's separate farm property); Hooker v. Hooker, 95 Idaho 518, 521, 511 P.2d 800, 803 (1972) (holding that enhancement in value is the measure of reimbursement when community funds are used to make physical improvements on separate property); Hiatt v. Hiatt, 94 Idaho 367, 368, 487 P.2d 1121, 1122 (1971) (holding that the reimbursement claim was for the amount of the improvements to husband's business property); Tilton v. Tilton, 85 Idaho 245, 250, 378 P.2d 191, 194 (1963) (holding that the amount of reimbursement to the community is measured by an enhancement in value of the husband's estate).

sented on appeal was whether the community contributions to mortgage payments converted the separate property of one spouse into community property. It is possible that the courts in both cases merely equated community funds contributed to the purchase price to equity. If so, the cases are in accord with *Gapsch* and its progeny. Even so, at best the Idaho authority is comparable to Arizona where an investment oriented measure of recovery is being used in a creditor situation.[68]

The Washington courts have recognized a community claim for reimbursement of funds used to reduce the principal on a mortgage of separate property. The expenditure of community funds on mortgage principal and interest does not change the character of property that was separate at the time it was acquired, and the community reimbursement claim is entitled to be secured through an equitable lien.[69]

While this much is relatively clear from the Washington authority, the measure of the reimbursement claim is not clear. Professor Cross suggests, "[w]hen money has been contributed, the amount advanced has been the measure of the right [or reimbursement], without particular attention being given to the possibility that the use of the money may not have increased the value of the asset by the amount advanced."[70] Professor Cross' general rule does not ap-

68. In Keller v. Rogstad, 112 Idaho 484, 733 P.2d 705 (1987), the court held that certain separate property of the husband could not be transferred without the wife's consent because she had acquired an interest in the property as a result of community contributions to improvements and because of several other factors which should have been insufficient to create such an interest. *Id.* at 487, 733 P.2d at 708. At worst, this recent Idaho case may have recognized a *pro rata* sharing approach. For a thorough discussion see Mollerup, *supra* note 2, at 1034-38.

69. Merkel v. Merkel, 234 P.2d 857, 863 (Wash. 1951); Conley v. Moe, 110 P.2d 172, 174-75 (Wash. 1941); *see also* WASHINGTON STATE BAR ASSOCIATION, WASHINGTON COMMUNITY PROPERTY DESKBOOK § 3.70A.4, at 3-89 to 3-94 (2d ed. 1989) [hereinafter WASHINGTON COMMUNITY PROPERTY DESKBOOK]; Harry M. Cross, *The Community Property Law in Washington (Revised 1985)*, 61 WASH. L. REV. 13, 67 (1986).

70. Cross, *supra* note 69, at 71. Professor Cross propounds a unique position, based on notions of implied consent, that the crucial question is whether a spouse is using community funds with respect to his or her own separate property versus whether a spouse is using community funds to with respect to the other spouse's separate property. Cross, *supra* note 69, at 71. Thus he concludes "if a spouse expends community funds in connection with his or her separate property, the claim for the community estate should be the full expenditure, both because the other spouse's interest in those funds would otherwise be depleted without consent and because the funds could be used to secure a full return by almost any other use." Cross, *supra* note 69, at 71. Whereas, Cross argues, where community funds have been used by one spouse to improve the other spouse's separate property

> only the increased value should be the measure, because the contributing spouse hardly needs to be protected against an unintended use of the community asset, and there would be a danger that a contrary result

pear to be borne out by all the Washington case law. In *Merkel v. Merkel*,[71] for example, the court granted the non-owner spouse a lien equal to one half the value of community funds used to reduce the mortgage principal on certain farm property, noting, "this sum representing one-half of the $4,500 of community funds paid on mortgage principal, it being considered that interest, tax and upkeep payments made by the community represent no more than reasonable rental for the use of the land."[72] This per se attribution of interest, taxes and

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> could involve giving a power to one spouse to 'improve the other out' of his (or her) separate property.

Cross, supra note 67, at 71. Cross' notion seems to be rooted in outmoded notions of male management. Given concepts of equal management it is difficult to draw the conclusion from the payment of a mortgage that one spouse is acting to the exclusion of the other spouse. Moreover since either spouse can seize managerial control of community funds (by marshalling them first) it is hard to see how one would need to be protected after the fact from the managerial power of the other. Finally, to the extent that inequities have controlled the management of marital property it would seem more appropriate to deal with these issues in the context of equitable division rather than in the context of property classification.

71. 234 P.2d 857 (Wash. 1951).

72. *Id.* at 864; *see also In re* Marriage of Harshman, 567 P.2d 667, 671 (Wash. Ct. App. 1977) ("Although the Nevins property must be characterized as the husband's separate property, the community has a right of reimbursement protected by an equitable lien against the property to the extent that community funds were used to discharge *the principal* on the mortgage . . . . ") (emphasis added). Two other Washington cases are frequently cited with *Merkel*, for the proposition that the measure of reimbursement is the value of the funds contributed. Farrow v. Ostrom, 133 P.2d 974 (Wash. 1943) involved an attempt by a tort creditor of the husband to execute against former community property in possession of the wife. *Id.* at 975. The property had been acquired during the marriage by use of a down payment that consisted, in part, of the wife's separate property. *Id.* at 977. The court concluded that he property had been community property and remained subject to execution and attachment for the husband's debt; however, it credited the wife for her separate contributions to the acquisition of the property, supporting this action by analogy to the situation where community funds are used to reduce indebtedness on community property. *Id.* at 977-78. The court did not break down the nature of the wife's contributions to the property into principal and interest; the lion's share of the amount was a contribution to principal.

Fritch v. Fritch, 335 P.2d 43 (Wash. 1959), involved a dispute between a former husband and wife over property acquired during the marriage but not divided by the divorce decree. *Id.* at 45. The court concluded that the property had been community property and that, consequently, the parties held interest as co-tenants. *Id.* at 47. The issue in the case was whether the husband as one co-tenant had ousted the wife so that adverse possession of her interest had taken place. *Id.* at 47-48. The court held that there had been no ouster but impressed the former wife's co-tenancy interest with a lien for one half the value of the taxes, assessments and improvements to the property added by the husband as the amount of contribution he was entitled to as co-tenant. *Id.* at 49. The court also held that the wife has waived her claim as co-tenant to any rents she may have otherwise been entitled to offset this amount. *Id.* Again, the case may be relevant to the extent community property interests are treated similarly to co-tenancy but did not involve any consideration of the unique policies or principals of community property in adjudicating the parties rights.

insurance as fair rental value (apparently without any findings of fact regarding rental values) has the *de facto* result of limiting the recovery of the community estate to the principal reduction or the enhanced value attributable to the community property payments. Later Washington cases have followed Professor Cross' reasoning but are confusing because of the continual citation to the earlier conflicting cases.[73]

The approach adopted by Idaho and Washington have the best possibility of consistently following the creditor approach. The problem is that the courts in both jurisdictions have not worked out the inconsistencies in their authority.

E. Wisconsin

The Supreme Court of Wisconsin has not considered a case in which community funds were used to reduce the indebtedness on separate property since Wisconsin's version of the Uniform Marital Property Act (UMPA) became effective in 1986.[74] Section 766.63 of the Wisconsin Code governs situations in which community and sepa-

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73. *See, e.g.*, *In re* Marriage of Wakefield, 763 P.2d 459, 461 (Wash. Ct. App. 1988) ("If the money was used to pay mortgage expenses that were not met by rental income, *i.e.*, debt reduction as opposed to improvements, it is suggested . . . the measure of recovery is dollar for dollar, rather than a portion of the increase in value." (citing Fritch v. Fritch, 335 P.2d 43, 49 (Wash. 1959))); Pollock v. Pollock, 499 P.2d 231, 237-38 (Wash. Ct. App. 1972) ("If post-marital payments came from community property, the community would have an interest in or with respect to the separate property involved, either for reimbursement of community funds expended or by way of equitable lien to protect the community's interest . . . ." (citing Farrow v. Ostrom 133 P.2d 974, 977 (Wash. 1943))); Merkel v. Merkel, 234 P.2d 857, 864 (Wash. 1951)). One author has concluded, "prior [Washington] case law gave the community a right to reimbursement plus interest for principal payments made on separate mortgage obligations." Martin Gales, Comment, *Serving Two Masters: Expenditure of Community Labor and Assets on Separate Property in Washington*, 19 GONZ. L. REV. 519, 532-33 (1984) (citing Merkel v. Merkel, 234 P.2d 857 (Wash. 1951)). Gales continues by stating that more recent Washington authority such as *In re* Marriage of Elam, 650 P.2d 213 (Wash. 1982), may require a court to apportion increases in value using a formula similar to California' *Moore* formula. *Id.* On the latter point the author seems to be misplaced. The majority of Washington authority has distinguished between situations involving physical improvements to real estate such as *Elam*, and contributions of community funds to the reduction of indebtedness on separate property. *See* WASHINGTON COMMUNITY PROPERTY DESKBOOK, *supra* note 67, § 3.70.A.1, at 3-83; Cross, *supra* note 69, at 71.

74. For reasons of consistency, this article will use the terms community property and separate property to refer to marital and individual property, respectively. The use of the terms "marital" and "individual" in the Uniform Marital Property Act ("UMPA") and in the Wisconsin marital property provisions based on the UMPA did not alter the essential nature of the act as a community property statute. *See* Kornfield, *Uniform Marital Property Act — Prefatory Note* 4 EQUIT. DISTRIBUTION REP. Dec. 1983, at 6, 70-71; James J. Podell, *Impact of Wisconsin's Marital Property Act on Family Law*, 68 MARQ. L. REV. 448, 449 (1985).

rate property are used as consideration in the acquisition of an asset.[75] The section clarifies that if the separate component of an asset cannot be traced the entire asset becomes community property. However, the section does not clarify what the result should be if the separate and community components can be traced; that is, it does not specify whether the asset is owned jointly between the separate and community estates or whether the ownership is fixed and the contributing estate is entitled to reimbursement. In 1991, the federal Bankruptcy Court for the Eastern District of Wisconsin applied California's *Moore*[76] decision to determine whether any community property interest, includable in a bankrupt husband's estate, existed in a house acquired by the wife using her separate funds.[77] After applying *Moore*, however, the court held that the marital property interest in the house ($276.22) was so *de minimus,* relative to the value of the house ($62,000), that apportionment of the interest was not appropriate.[78] More recently, the Wisconsin Court of Appeals considered a case in which community labor and funds were used to make physical improvements on the wife's separate property home which substantially increased the value of the home.[79] In *In re* Estate of Kobylski the Wisconsin court applied Texas law and concluded that when the use of community funds and labor to make physical improvements to separate property a "claim for reimbursement exists in favor of the marital estate measured by the property's enhanced value attributable to the improvements, not the amount of marital funds actually expended."[80]

It's difficult to say whether the Wisconsin Supreme Court would follow the same approach as either *Kobylski* or *In re* Geise in a situation in which community funds are used to reduce indebtedness on separate property. In *Kobylski,* the appellate court recognized that other community property jurisdictions have split on the question of

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75. WIS. STAT. ANN. § 766.63 (West 1993). Section 766.63 provides:

(1) Except as provided otherwise in §§ 766.71 and 766.62, mixing marital property with property other than marital property reclassifies the other property to marital property unless the component of the mixed property which is not marital property can be traced.

(2) Application by one spouse of substantial labor, effort, inventiveness, physical or intellectual skill, creativity or managerial activity to either spouse's property other than marital property creates marital property attributable to that application if both the following apply:

(a) Reasonable compensation is not received for the application.

(b) Substantial appreciation of the property results from the application.

Id.

76. Moore v. Moore, 618 P.2d 208, 212 (Cal. 1980).

77. *In re* Geise, 132 B.R. 908, 914-15 (Bankr. E.D. Wis. 1991).

78. *Id.* at 915.

79. *In re* Estate of Kobylski, 503 N.W.2d 369, 375-76 (Wis. Ct. App. 1993).

80. *Id.* at 376.

whether contribution of community funds to a mortgage on separate property gives rise to an ownership right or a claim of reimbursement.[81] The language of section 766.63[82] and § 14 of the UMPA,[83] on which the cases are based, appears to codify an ownership rationale rather than create a claim for reimbursement. Both the Wisconsin statute and the UMPA focus on tracing property interests and imply that tracing means "unmixing" those interests.[84] Thus, if the separate property component of mixed property is "traced" the result would be the existence of two property interests in the same asset — separate and community. The comments to UMPA section 14 also support the ownership approach. These comments indicate that if community property is used to make mortgage payments on separate property, the result would be a mixture of separate and community property.[85] Finally, prominent commentators on the UMPA also assumed that, while the provisions were ambiguous, mixing under section 14 through use of community property to reduce indebtedness on separate property would create an ownership right and not merely a claim for reimbursement.[86]

Given the adoption of a reimbursement theory in *Kobylski* and the apparent conflict between that approach and the language of the Wisconsin statute and the UMPA comments, Wisconsin's potential approach to community contributions to reduction of indebtedness on separate property is hopelessly unpredictable.

III. APPORTIONMENT

The apportionment approach of California, Nevada and New Mexico is based on the notion that the payment of mortgage payments constitutes providing consideration for the acquisition of the asset and consequently gives rise to an ownership interest in the asset. There are several problems with the approach, however. First, it is inconsistent with the general approach to ownership outside the area of community property. Second, it creates ownership interests

81. *Id.* at 377 n.9; *see supra* notes - and accompanying text.

82. WIS. STAT. ANN. § 766.63.

83. *See* UMPA § 14, 9A U.L.A. 131 (1987).

84. WIS. STAT. ANN. § 766.63; UMPA § 14, 9A U.L.A. at 131.

85. UMPA §14 cmt., 9A U.L.A. at 131.

86. *See* William A. Reppy, Jr., *The Uniform Marital Property Act: Some Suggested Revisions For A Basically Sound Act*, 21 HOUS. L. REV. 679, 705-706 (1984) ("Although the text of the Act is unclear, the comment to section 14 suggests that the Act rejects the inception of title doctrine in favor of *pro rata* sharing of ownership in those cases in which a down payment is made from one estate and at least some subsequent principal payments are made from a different estate."). An inception of right analysis would fix ownership at the original date of acquisition and give the community a claim for reimbursement for subsequent mortgage payments made with community property. *Pro rata* sharing would divide title according to the amount each estate contributed to the consideration.

that are not reflected in the recorded title documentation, casting doubt on the usefulness of the recording system. These interests are especially troubling because unlike equitable liens of the reimbursement states, these unrecorded interests do not fit into an existing category of property rights. Finally, these interests may even survive purchase of the property by a bona fide purchaser.[87]

In general, outside the community property situation, the contribution of assets toward the payment of a mortgage by itself does not give rise to an ownership right in property. For example, parents who help a child make mortgage payments on a home owned by the child would not acquire an ownership interest in the child's home. Rather the contribution of assets would either be treated as a gift or as a loan depending on the intention of the parties and the circumstances at the time the parents contribute to the mortgage. Likewise, even where funds are made available at the time of a purchase of property, the contribution of those funds would not normally, by itself, give rise to an interest in the property unless some intention that an ownership interest exists is present and can be proved.[88]

The policies of marital property law, and particularly of community property law, does not yield a persuasive rationale for treating the contribution of marital assets to the payment of a mortgage on non-marital property any differently. Under Spanish law, title to property was fixed at the time the transaction to acquire the property was initiated and completion of the transaction after marriage, including installment payments made after marriage with community property, did not change the character of the asset as the separate property of the acquiring spouse.[89] Most American jurisdictions followed this rule well into the 20th century.[90] The recent confusion has probably resulted, in some measure, because of the desire of courts to accomplish equity in inflationary real estate markets.

California is a good case study in the abandonment of the principle of inception of right. A hypothetical may help illustrate the problem. Assume that H bought a house on January 1, 1955, in Orange County California. At the time he bought the house he was not married and did not anticipate marriage. The purchase price was

87. *See* Mollerup, *supra* note 2, at 1041.

88. A purchase money resulting trust would not spring up without such an intention. *See* 1 DAN DOBBS, THE LAW OF REMEDIES § 4.3(2), at 600 (2d ed. 1993).

89. WILLIAM Q. DE FUNIAK & MICHAEL J. VAUGHN, PRINCIPLES OF COMMUNITY PROPERTY § 64, at 130-31 (2d ed. 1971).

90. See Bartke, *supra* note 2 for a general discussion of the state of the law in the original eight community property jurisdictions as of 1969. Although Bartke divides the jurisdictions into reimbursement theory versus lien theory states, both theories are based on the original Spanish notion that the separate property character of the property did not change as a result of subsequent community property contributions to mortgage payments. Rather the community estate was entitled to reimbursement, sometimes secured by a *pro tanto* equitable lien in the improved property.

$50,000. H put down $10,000 and financed the remaining $40,000 using a conventional 30 year mortgage at 3.5% interest. Several years later H met W and they got married on January 1, 1961. Prior to the marriage, H made the mortgage payments of $179.62/month using his salary. After the marriage he continued using his salary for mortgage payments. At the time of the marriage, H had $15,112.97 equity in the house and the fair market value of the house was $55,000. W did not work outside the home during the marriage. In 1985, after four children and twenty-five years of marriage, H and W are divorced. The mortgage on the house had just been completely paid off and the fair market value of the house, at the time of divorce was $250,000.

If a pure reimbursement approach, measured by the amount of contributions, is used, at divorce, W will have a claim for reimbursement of one-half the value of the contributions to principal and interest, or $25,865.28.[91] If, on the other hand, a *pro rata* approach is applied, W will have an ownership interest in the house equal to approximately $87,217.57.[92] The difference in these amounts and the apparent unfairness of not allowing W to share in the significant appreciation in the real estate market, combined with the increasing difficulty of dealing with the economic consequences of the divorce on W through alimony[93] apparently motivated courts, particularly in California, to abandoned the notion of inception of right.[94]

If one accepts the abandonment of the inception of right test, the California cases at least have the virtue of internal consistency. That is, the cases have treated the interest created as a full-blown, vested, community property interest.[95] Moreover, the cases have not permitted offsets for rental value, correctly concluding that ownership includes the right to use and occupy the property. However, the abandonment of inception of right is an unprincipled approach to the

91. This amount was calculated by multiplying the monthly payment of $179.62 times the number of months paid with community property (288) and dividing the product ($51,730.56) by two.

92. This amount was arrived at using the *Moore* formula. Thus, the $10,000 down payment was added to the $40,000 in loan proceeds. That sum was reduced by the amount of principal reduction attributable to payments with community property — $34,887.03. The result, $15,112.97, was divided by the purchase price ($50,000) to arrive a percentage of separate property ownership of 30.226%. Thus the community share of the house, based on the present fair market value, would be $174,435.15. W's one-half interest would be $87,217.57.

93. For a thorough discussion of the failure of alimony to address the economic consequences of divorce, see Lenore J. Weitzman, *The Economics of Divorce: Social and Economic Consequences of Property, Alimony and Child Support Awards*, 28 UCLA L. REV. 1181, 1188 (1981).

94. The problem is even more intractable in California because the courts cannot accomplish equity through an equitable division of the community property, but must instead divide the property equally. CAL. FAM. CODE § 2550 (West 1993).

95. *See, e.g.*, Moore v. Moore, 618 P.2d 208, 211 (Cal. 1980).

accomplishment of rough justice in an inflationary real estate market. This approach has both theoretical and practical problems.

The fact is that in most of these cases the property has already been purchased at the time of the marriage and title is vested in the owner spouse. The original investment risk was taken by the spouse who took the initial steps toward acquisition and the lender provided the purchase money necessary at the time the transaction was initiated. One of the fundamental principles of community property has always been that the owner of separate property should be able to preserve the value of that separate property.[96] In an inflationary real estate market, the *pro rata* approach insures that a spouse's separate property will steadily decrease in value as community property contributions and appreciation overtake the original investment. In the previous hypothetical, H's ownership interest decreased from 100% on the date of the marriage to approximately 30% on the date of divorce even though no formal transmutation of the property took place.[97]

A second justification offered for the adoption of the *pro rata* approach is the apparent harshness of the inception of right approach on the non-owner spouse. The problem with this justification is that it fails to consider that because the community resided in the property rent-free, community assets were freed up for other purposes thereby benefitting the community.

If by harshness, courts are referring to the economic consequences of divorce on the parties, and particularly on the wife, confusing ownership concepts of community property is not the appropriate mechanism for dealing with these issues. Rather, equitable divisions of community property or awards of alimony would seem to be better approaches.

IV. REIMBURSEMENT

As the foregoing analysis shows, all the community property jurisdictions except California, Nevada and New Mexico treat the community paydown of mortgage principal and interest on separate property as a loan, giving rise to a claim for reimbursement.[98] Beyond that the similarity among the jurisdictions recognizing reim-

96. In his important work on Idaho community property law, Professor Brockelbank defined two basic elements of community property: 1) Marriage is not a way of acquiring property; and 2) Gains made during the marriage are shared. W.J. BROCKELBANK, THE COMMUNITY PROPERTY LAW OF IDAHO 32-33 (1962). This notion, that the community is only of acquests and gains during the marriage and does not include property acquired by either spouse prior to marriage, is also stressed in DE FUNIAK & VAUGHN, *supra* note 83, § 1 at 1-3.

97. Admittedly, the 100% interest was subject to a mortgage and the 30% interest is not. However, H had the exclusive right to discharge the mortgage as the sole mortgagor.

98. *See supra* part II.A.

bursement ends. Several have adopted a standard of enhancement in value as the measure of the reimbursement claim rather than reimbursing the non-owner spouse for that actual benefit received from the community — mortgage principal and interest.[99] Others have created equitable liens to secure this claim without being clear regarding the nature of the lien and with out questioning its propriety.[100] Finally, these jurisdictions have, in large measure failed to adopt a meaningful approach to assessing the value of the benefit received by the community in the form of rent-free use of the premises where such an assessment is appropriate.

A. Availability of an Equitable Lien

Many jurisdictions adopting the reimbursement approach have also held that an equitable lien arises at the time the payments are made.[101] While, in general, equitable liens are frequently given when benefits are conferred on real estate, rarely do such liens arise under circumstances in which they cannot be enforced.[102] In addition, the courts are anything but clear about the nature of this lien. In 1969, Professor Bartke documented the confusion regarding the nature of the lien created in these cases.[103] While most of the jurisdictions today appear to recognize the *pro tanto* nature of the lien, confusion still abounds. One commentator has even suggested, presumably erroneously, that the remedy of the non-owner spouse is limited to the equitable lien.[104] Even where the courts are careful to describe the lien as a *pro tanto* lien, as opposed to a judgment lien, securing the eventual reimbursement judgment confusion exists. Can this lien be cut off by a bona fide purchaser? Does its existence mean that the property has to be treated as community property for purposes of dual management, inheritance and equitable division? Can it be recorded during the existence of an on-going marriage?

The answers to these questions are complex. At first blush one might answer the bona fide purchaser question in the affirmative because such unrecorded interests generally can be cut off.[105] How-

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99. *See supra* part IV.

100. *See supra* part IV.

101. Texas, Arizona, Idaho and Washington all appear to take this approach. *See supra* parts II.C-D.

102. DAN DOBBS, LAW OF REMEDIES § 4.3(3), at 600 (2d ed. 1993). Dobbs suggests that, in general, the equitable lien places its holder in a better position than a general unsecured creditor because the lienholder has a priority. This is only true to the extent the lienholder can convert her lien into a legal lien. The spouse holding a *pro tanto* equitable lien in community property cannot convert her lien until divorce.

103. *See* Bartke, *supra* note 2, at 385, 397-405.

104. *See* Gales, *supra* note 71, at 527.

105. That is the assumption made by at least two commentators. *See* Bartke, *supra* note 2, at 418; Mollerup, *supra* note 2, at 1041. This assumption is also

ever, when the third party's rights are considered in the context of dual management rules, this equitable lien is, after all, a community property interest in real estate. Generally transfers of community real estate require the consent of both spouses and the transaction is at least voidable by the non-consenting spouse.[106] In most jurisdictions that have broad recording statutes that allow the recording of almost any document relating to land, an affidavit of lien is probably recordable and such recording would resolve much of the bona fide purchaser issue.[107] However, it's not likely that the average married couple would consider recording the fact that they make mortgage payments on a piece of separate property real estate with community property!

The incremental benefit that the *pro tanto* lien adds over and above a reimbursement claim is not always clear. Especially if the lien can be cut off by a bona fide purchaser, it seems to add little protection to the non-owner spouse's interest. The community property interest giving rise to the lien cannot be reduced to judgment and executed upon until divorce. At that time, if sufficient property exists, the lien can attach to that property to secure the reimbursement claim, or, in jurisdictions that permit, an unequal division of community property can be accomplished to set off the reimbursement claim. If there are not enough assets at the time of divorce, the equitable lien won't somehow increase the total asset pool!

B. Measure of Recovery

Some reimbursement jurisdictions measure the reimbursement claim by the enhancement in value of the separate property attributable to the community contributions.[108] That measure has been held by some courts to be equivalent to the amount the equity on the mortgage is reduced,[109] and by others to include, in addition, a *pro rata* share in any appreciation of the underlying property.[110] This

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consistent with general rules of remedies. *See* DOBBS, *supra* note 84, § 4.7(1), at 659.

106. *See* REPPY & SAMUELS, *supra* note 8, at 15-1 (citing IDAHO CODE § 32-912 (1983)). Probably the assumptions of Bartke and Mollerup are correct, but troubling case authority exists. *See* United States v. McConkey, 430 F. 2d 652, 654 (9th Cir. 1970) (purporting to apply Idaho law); REPPY & SAMUELS, *supra* note 8, at 15-10 to 15-11.

107. *But see* Mollerup, *supra* note 2, at 1043 (arguing that the recording of such potentially one-sided documents would detrimentally affect the reliability of recording statutes).

108. *See, e.g.*, Drahos v. Rens, 717 P.2d 927, 928-29 (Ariz. Ct. App. 1985); Longo v. Longo, 474 So. 2d 500, 503 (La. Ct. App. 1985), *cert denied*, 477 So. 2d 711 (1985); Penick v. Penick, 783 S.W.2d 194 (Tex. 1990).

109. This would be the result in Louisiana and possibly Washington, *see infra* parts II.B and II.D, and Texas, *see infra* part II.C.

110. Arizona takes this approach. *See infra* part II.C. In adopting this approach, Arizona relied on California law without addressing the differences between

enhancement in value measure of recovery seems to be inconsistent with principals of restitution which should govern the valuation of the reimbursement claim. Reimbursement is based on the notion that property, once acquired, does not change its character as separate or community property in the absence of a gift or other transmutation. Thus, when property of one estate is used for the benefit of the other estate, a reimbursement claim arises to prevent unjust enrichment by forcing the one spouse to disgorge the benefit received.[111]

This concept of preventing unjust enrichment by requiring one spouse to reimburse the community estate for contributions made by it for the benefit of that spouse's separate property is fundamentally inconsistent with the enhancement in value test. Any appropriate measure of the unjust enrichment action for reimbursement would include not only principal but also interest within the definition of benefit. Certainly the paydown of the loan interest is a benefit received by the separate property estate. Without such interest payments, the loan would have been in default with the possible foreclosure and loss of the property to follow.

Defining benefit to include both principal and interest may not actually be inconsistent with the approach the courts are taking. For example, one Louisiana court appeared to recognize that the payment of interest by the community benefits the separate estate since interest was part of the actual "cost of maintaining the natural and civil fruits of this separate property."[112] However, the court concluded that interest was not reimbursable because the spouses benefitted from residing in the house.[113] Other cases however, do not permit reimbursement of more than the principal and do not discuss the reasons for limiting the claim, giving rise to the appearance that enhancement in value is limited to principal reductions alone.[114] Even

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the apportionment approach of the California courts and the reimbursement approach adopted by the Arizona court.

111. Weekley, *supra* note 45, at 973-74.

112. *See* Parker v. Parker, 517 So. 2d 264, 266 (La. Ct. App. 1987).

113. *Id.* For a discussion of how courts are dealing with this question of offsetting benefits see *infra* notes - and accompanying text.

114. *See* Loyacono v. Loyacono, 618 So. 2d, 896, 898 (La. Ct. App. 1993). Texas law is unclear on this point. The Texas Supreme Court adopted an enhancement in value standard to measure mortgage paydown reimbursement claims and authorized an offsetting benefits approach. Penick v. Penick, 783 S.W.2d 194, 197 (Tex. 1988). However, the court was not clear about whether the enhancement approach would permit reimbursement of contributions to interest as well as principal. *Id.* Earlier Texas cases had held that interest, taxes and insurance were not reimbursable. *See, e.g.,* Cook v. Cook, 665 S.W.2d 161, 164 (Tex. Ct. App. 1983) (holding that the payment of interest from community funds would not create a claim for reimbursement unless it could be proven that expenditures by the community exceeded the benefits received); Hawkins v. Hawkins, 612 S.W.2d 683, 685 (Tex. Ct. App. 1981) (holding that the payment of interest from community funds would not create a claim for reimbursement unless the benefits received were greater than the amount spent by the community).

in courts allowing the reimbursement of both principal and interest, the approach needs to be clarified. Interest, as a benefit received by the separate property estate, is reimbursable. Only when an offsetting claim for fair rental value is made, should the reimbursement claim for both interest and principal be reduced. Language to the contrary in the cases is inconsistent with the theory of reimbursement. The only possible incremental benefit of the *pro tanto* lien approach is that the existence of such a lien subjects the property to equitable division and inheritance rights of both spouses because that position of the property interest encumbered by the lien is community property.

C. Setoffs for Fair Rental Value

Many jurisdictions have recognized that where the community resides in the property, or where the community obtained the benefits of rents,[115] the rental value should be set off against the reimbursement claim.[116] In theory, this is entirely consistent with the law of unjust enrichment. After all, the availability of rent-free housing freed the community assets for other purposes. The problem is that, in the courts of the community property states, this setoff has little content. Many cases that consider a setoff appear to presume, in the absence of any reasonable proof, that the fair rental value of the property is equal to the payment of principal, taxes and insurance.[117] They do not appear to entertain evidence on the question of rental value.

V. CONCLUSION

The most theoretically consistent approach to the mortgage paydown situation is to treat the community claim as one for reimbursement at the time the marriage is terminated. The measure of this reimbursement claim should be the amount of community property contributed to mortgage payments set off by the fair rental value of the property if the spouses resided in it or obtained the benefits of rentals. While a court may choose to secure the reimbursement claim at divorce with a lien on the other spouse's property, it should avoid the *pro tanto* lien with its potential for confusion. This approach best

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115. In Idaho, Texas and Louisiana rents on separate property are community property.

116. Most of the reimbursement jurisdictions have recognized offset in at least some way. *See, e.g.*, Parker v. Parker, 517 So. 2d 264, 266 (La. Ct. App. 1987) (attributing interest to the cost of maintaining property for the community); Penick v. Penick, 783 S.W.2d 194, 197 (Tex. 1990) (permitting the husband to offset community reimbursement claim with the value of tax benefits received by the spouses as a result of depreciating the property); Merkel v. Merkel, 234 P.2d 857, 864 (Wash. 1951) (characterizing interest, taxes and insurance as "reasonable rental").

117. *See, e.g.*, Longo v. Longo, 474 So. 2d 500, 503 (La. Ct. App. 1985).

respects the interests of the spouses within the framework of the community property policy. It avoids unintended transmutation of property yet provides a mechanism by which the true benefit and detriment to the community and separate estates can be considered. Finally it avoids altering ownership rights during marriage for the purpose of effectuating equity at divorce.