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Unless other rules apply, property will be characterized based on the source of funds used to acquire the property.

Wendy and Hal married in 1990. Until 1995, Wendy helped operate the business, but had no ownership interest. It is unclear from the facts whether Wendy's becoming half owner of the business in 1995 was a gift from her father, or (more likely) a reward for past and anticipated future services. If it was a gift, the value at the time would have been Wendy's separate property, but if it was due to Wendy's services, then there would be an allocation--the value prior to marriage would be separate property, and the value from the date of marriage to the date of the agreement would be community property. The interest that Wendy inherited from her father (including the real property and inventory as it existed in late 1999) would be Wendy's separate property.

The value that Wendy's efforts added to the business would be considered community property during the marriage (from the time Wendy obtained an interest in the business in 1995 until the date of separation in 2014). The value added by Wendy's effort after separation would be considered Wendy's separate property.

The court will likely find that the 1/2 interest that Wendy acquired in 1995 was community property. Although Wendy worked in the business prior to the 1990 marriage, there is no indication that the interest was given to her for past services, especially more than five years prior. The interest was acquired during the marriage, and without more, property acquired during the marriage will be presumed to be community property. There is no indication that the interest was given to Wendy as a gift, and it is likely that it was given to her in return for her recent service to the business and in anticipation of her future services. This was borne out by the increase in value of the business. The other half of the business was inherited by Wendy and property acquired through inheritance is the recipient's separate property.

Generally, community property is divided equally between the spouses, and separate property is awarded to the spouse who owns it. But when community funds are used to increase the value of a spouse's separate property, then the property is considered part separate property and part community property. The allocation will be either pursuant to the Pereira or the Van Camp allocation, depending on whether the increase in value is due to the efforts of a spouse or due to appreciation. Here, there is a mixture--the business includes real property, which has historically increased in value significantly in California between 1999 and the present, but the increase in value of the business appears to be substantially due to Wendy's efforts. More facts are needed (discovery? tax returns? was there a mortgage on the real property that was

paid down during the marriage?), but it is likely that the court would find the increase in the value of the business was primarily due to Wendy's efforts. In this case, the increase in value due to appreciation in Wendy's separate property interest in the business would be considered Wendy's separate property, and the remaining value of the separate property interest would be considered community property.

In summary, the 1/2 interest in the business that Wendy obtained by agreement would be community property; the 1/2 interest that Wendy obtained by inheritance would be Wendy's separate property. The increase in value of the separate property not due to appreciation would also be community property. Hal is entitled to the value of 1/4 of the business (1/2 of the 1/2 that is community property) and 1/2 of the increase in value of the other half of the business for the time period from Wendy's father's date of death through the date of separation. Wendy, as the spouse managing the business, should be awarded the business, and Hal should be awarded assets equal to his share of the community property as described above. If there are not sufficient other assets, the court will order Wendy to make an equalizing payment.

Question #3 Final Word Count = 686

END OF EXAM