The Division of Property Purchased on Credit under California Community Property Law: A Proposal for Reform

Andrew M. Cummings

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The Division of Property Purchased on Credit Under California Community Property Law: A Proposal for Reform

Community property, the "common fund of matrimonial gains," is simply the property that belongs to the association of the husband and wife.¹ Under a community property system, all property acquired during the marriage, with a few exceptions,² will inure to the benefit of the community.³ In a divorce, California community property law gives each spouse the right to an equal share of the community property.⁴

In a marriage dissolution proceeding in California, a court has jurisdiction to divide the existing community property.⁵ Before this division can be made, however, the court must characterize the property owned by the spouses as either community or separate property.⁶ Although property acquired during the marriage is presumed to be community property,⁷ California recognizes the right of either spouse to hold property separately.⁸ In addition, a single asset may be owned proportionately by both the community and one spouse. Property owned in this manner is termed a mixed asset.⁹ If mixed assets are

2. Property acquired during marriage by gift, devise, descent, or from the rents, issues, and profits from separate property is separate property. Cal. Civ. Code §§5107, 5108. California law also provides that property acquired by the spouses during the marriage but while living separate and apart or after legal separation is separate property. Id. §§5118, 5119. See also In re Marriage of Baragry, 73 Cal. App. 3d 444, 448, 140 Cal. Rptr. 779, 781 (1977) (definition of living separate and apart). Throughout this comment, references to the acquisition of property during marriage assume that the spouses are not separated.
3. Cal. Civ. Code §5110; see Wilson v. Wilson, 76 Cal. 2d 119, 125-26, 172 P.2d 568, 572 (1945) (The presumption that all property acquired during marriage is community property is fundamental to the community property system.).
5. Id. §4351.
6. Civil Code section 4800(a) imposes a mandatory obligation on the trial court to ascertain the nature and extent of all assets subject to disposition by the court. In re Marriage of Knickerbocker, 43 Cal. App. 3d 1039, 1048-49, 118 Cal. Rptr. 232, 238 (1974). This obligation includes a duty to identify and value all property owned by the spouses that is community property. Id. The character and value of property for purposes of dissolution is a question of fact. In re Marriage of Lopez, 38 Cal. App. 3d 93, 107, 113 Cal. Rptr. 58, 66 (1974).
included in the property owned by the spouses at the time of divorce, the court must determine the proportional ownership of these assets.10

Problems of determining ownership interests in mixed assets often arise in cases in which property has been acquired on credit and payments have been made over time.11 In this context, two different but interrelated questions arise. The first question is the character of the property at the time of acquisition.12 The initial character may be determined from the form of the title in which the property is held or from an agreement between the spouses.13 If the initial character of the property cannot be determined from the form of title or if no agreement exists between the parties, the courts will determine the character of the property according to the character of the money or property used to make the purchase.14 The portion of the property purchased with a down payment and the portion purchased with the proceeds of a loan must be characterized separately.15 The portion of the property purchased with a down payment, if any, will be characterized according to the character of the money used to make the down payment.16 The portion purchased with the loan proceeds will be characterized according to the character of the loan, which will be determined according to the intent of the lender to rely upon separate or community property in extending the loan.17 This approach is entitled "the intent of the lender test." The intent of the lender test will be explored later in greater detail.18

The second question that will arise at the dissolution proceeding is the effect that subsequent payments will have upon the interest of each spouse in the property.19 This question arises when the character of the loan payments differs from the character of the loan. For example, if the loan proceeds initially are characterized as separate property, repayments may be made from community funds.20 Similarly, loan proceeds initially characterized as community property may be

10. See infra notes 60-86 and accompanying text.
12. See infra notes 40-59 and accompanying text.
13. See infra notes 96-97 and accompanying text.
14. See infra notes 96-98 and accompanying text.
15. Id.
16. Id.
17. Id.
18. See infra notes 102-18 and accompanying text.
19. See infra notes 134-57 and accompanying text.
20. E.g., Moore, 28 Cal. 3d at 370-73, 618 P.2d at 210, 168 Cal. Rptr. at 664.
Division of Credit Purchases

repaid from separate funds. The former situation, in which separate property is contributed toward the purchase of community property, now is governed by California Civil Code section 4800.2. This statutory provision allows a right of reimbursement for specified separate property contributions to the acquisition of community property. When community property is contributed toward the purchase of separate property, the court will apportion ownership of the property in the same proportions as the total contributions made by the community and a separate estate bear to the purchase price.

The distinction between a statutory right of reimbursement and a judicial apportionment of ownership is significant. Reimbursement entitles a spouse to a return of the actual amount contributed. An apportionment of ownership allows a share of the value of the property at the time of divorce. Thus, if the property has appreciated in value, an apportionment will result in a greater return. The new statutory provisions have considerably eased the task of characterizing property purchased on credit during the marriage. In cases in which these new provisions do not apply, however, the law often is unworkable and leads to an unfair result.

The purpose of this comment is to propose reform of the current California law regarding the division of property acquired on credit. This author will argue that the current method of characterizing property acquired on credit for the purpose of division is inappropriate for several reasons. First, the current law does not assess accurately

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23. *Id.; see infra* notes 29-37 and accompanying text. Under California Civil Code section 4800.2, contributions include down payments, payments for improvements, and payments that reduce the principal of a loan used to finance the purchase or the improvement of the property. No right of reimbursement is allowed for payments for interest on the loan or for payments for maintenance, insurance, or taxation of the property.
27. Conversely, if the property decreased in value, reimbursement would yield a greater return. Under California Civil Code section 4800.2, however, the amount of the reimbursement cannot exceed the value of the property at the time of division. *Cal. Civ. Code §4800.2.*
28. Specific criticisms of the current law are discussed *infra.* See *infra* notes 207-46 and accompanying text.
29. *See infra* notes 9-21 and accompanying text.
30. *See infra* notes 52-67 and accompanying text.

131
the contributions made by either spouse or the community to the acquisition of property on credit. Second, the initial characterization of the debt has a greater impact than do the actual loan payments in the final determination of the interests of each party in the property. Furthermore, the law is unclear regarding the cases in which apportionment is applicable. This author will suggest three modifications to the current characterization scheme. First, the intent of the lender test should be discarded in favor of a formula that allocates a rate of return on separate property used to secure a debt. Second, the apportionment formula should be modified to account for all contributions to the acquisition of property, including interest, and should be revised to place greater emphasis on the source of the loan repayments. Third, this author will suggest that recent case law should be interpreted to hold that apportionment is appropriate in all instances in which the community has contributed toward the repayment of a separate property loan. Initially, this author will explore the application of the current law so that the need for reform may be understood more easily.

**CURRENT STATUS OF THE LAW**

The current scheme used in California to divide property purchased on credit at the time of divorce can be illustrated by the following hypothetical. Suppose that during the marriage husband purchased a home for $140,000. He made a $40,000 down payment from separate property accumulated prior to the marriage. The balance of the purchase price was made from the proceeds of a loan obtained at 14.5% interest. At this interest rate, the couple made $1,250 monthly loan payments. The payments were made from the collective earnings of the spouses, which are community property. After ten years, loan payments totaled $144,600 for interest and principal. The principal of the loan was reduced to $95,480. Assume that at the time of divorce, the property had doubled in value to $280,000. In the marriage dissolution proceeding, the court will determine the division of the property.

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31. See infra notes 219, 237-46 and accompanying text.
33. See infra notes 157-205 and accompanying text.
34. See infra notes 68-71 and accompanying text.
35. See infra notes 71-76 and accompanying text.
36. See infra notes 183-200 and accompanying text.
37. These hypothetical figures are taken from Bruch, supra note 9, at 790-94.
by determining the character of the property at the time of acquisition and making adjustment to account for the effect of contributions made with funds that are of a character different from the character of the loan.

A. Initial Character of the Property

Under current California law, the property acquired during marriage in this hypothetical would be characterized initially according to the following analysis. The court first would consider whether the character of the property can be determined from the form of title in which the property is taken. The form of title may support a presumption that the property is community property. A common form of title is joint tenancy. Under California Civil Code section 4800.1, all property acquired during the marriage in joint tenancy is presumed to be community property. This presumption is rebuttable only by a writing to the contrary. Thus, in the above hypothetical, if the property had been acquired in joint tenancy, the entire property would be community property for purposes of dissolution despite the separate property down payment. If, however, the property were taken in the name of the husband alone, the analysis would become more complicated. In California all property acquired during the marriage is presumed to be community property. Unlike this presumption that arises from a joint tenancy title, the presump-

38. The contributions referred to here include both payments made at the time of acquisition that do not affect the initial characterization of the property because of the form of title in which the property is taken and subsequent payments made to repay the loan.

39. See Moore, 28 Cal. 3d at 374, 618 P.2d at 211, 168 Cal. Rptr. at 665.


42. Cal. Civ. Code §4800.1. The presumption of community property arising from the other forms of title is rebuttable by an oral agreement or common understanding. Lucas, 27 Cal. 3d at 815, 614 P.2d at 289, 166 Cal. Rptr. at 857. See also Comment, Form of Title Presumptions in California Community Property Law: The Test for a Common Understanding or Agreement, 15 U.C.D. L. Rev. 95, 97-107 (1981).


tion arising merely from acquisition during the marriage may be rebutted without a writing to the contrary.\textsuperscript{45} The husband in this hypothetical could rebut the community property presumption by showing that the property was acquired entirely or partially with separate funds.\textsuperscript{46} Since the down payment clearly is the separate property of the husband, the husband would have a separate property interest in the property in the proportion that his down payment bears to the total purchase price.\textsuperscript{47} In this hypothetical, the husband would own approximately thirty percent of the property separately as a result of the down payment.\textsuperscript{48} The portion of the property purchased with the loan proceeds presently would be characterized under the intent of the lender test.\textsuperscript{49} The loan proceeds, acquired during marriage, presumptively would be community property.\textsuperscript{50} This presumption, however, is rebuttable by evidence that the lender primarily relied on the separate property of either spouse in extending the loan.\textsuperscript{51} Thus, if the husband can establish that the loan was extended in reliance upon his separate property, the loan proceeds and thus the portion of the property purchased with the loan proceeds also would be the separate property of the husband.\textsuperscript{52} Otherwise, the portion of the property purchased with the loan will be community property.\textsuperscript{53} If the lender did not primarily rely upon the separate property of the husband in extending the loan, the community would have an interest in the property in the proportion that the loan proceeds bear to the total purchase price.\textsuperscript{44} This community property proportion would be approximately seventy percent.\textsuperscript{55}

The above analysis would apply only if, as the facts of the hypothetical indicated, the property were acquired during the marriage. Under California law, if the property were acquired prior to marriage, the entire property would be characterized initially as separate property regardless of the form of the title\textsuperscript{56} or the intent of the

\textsuperscript{45} In re Marriage of Aufmuth, 89 Cal. App. 3d 446, 455, 152 Cal. Rptr. 668, 673 (1979).

\textsuperscript{46} Id.

\textsuperscript{47} Aufmuth, 89 Cal. App. 3d at 457, 152 Cal. Rptr. at 674-75.

\textsuperscript{48} This figure is calculated by dividing the $40,000 down payment by the $140,000 purchase price.

\textsuperscript{49} Gudelj v. Gudelj, 41 Cal. 2d 202, 210, 259 P.2d 656, 661 (1953).

\textsuperscript{50} Id.

\textsuperscript{51} Id.

\textsuperscript{52} Somps v. Somps, 250 Cal. App. 2d 328, 337, 58 Cal. Rptr. 304, 310 (1967).

\textsuperscript{53} Aufmuth, 89 Cal. App. 3d at 456, 152 Cal. Rptr. at 673.

\textsuperscript{54} Id.

\textsuperscript{55} This figure is calculated by dividing the $100,000 loan contribution by the $140,000 purchase price.

\textsuperscript{56} California Civil Code section 4800.1 is not applicable to property acquired in joint
The initial character of the property, however, does not dictate the division of the property at the time of divorce. In the dissolution proceeding, the court must account for contributions made toward the purchase of the property that are of a character different from the initial character of the property.

B. Division of the Property at the Time of Divorce

In dividing property at the time of divorce, courts are guided by the initial character of the property. If the property is community property, a spouse who has made separate property contributions to the purchase is entitled to reimbursement of certain contributions. For example, if in the above hypothetical the property had been acquired in joint tenancy and consequently characterized entirely as community property, the husband would be entitled to a reimbursement of his $40,000 down payment. This reimbursement, however, would not entitle the husband to a proportionate share of the appreciated value. The appreciation would belong entirely to the community.

If community funds are contributed toward the purchase of separate property, however, the court will apportion ownership between the separate and the community estates. This apportionment of ownership entitles each estate to a proportionate share of the property valued at the time of the property division. In the above hypothetical, assume that the property was acquired during marriage and the lender primarily relied upon the separate property of the husband in extending the loan. The property, therefore, was entirely the separate property of tenancy prior to the marriage. In re Marriage of Leversee, 156 Cal. App. 3d 891, 904-96, 203 Cal. Rptr. 481, 483 (1984). Section 4800.1, however, is applicable to property acquired prior to marriage and conveyed to joint tenancy during the marriage. In re Marriage of Benart, 160 Cal. App. 3d 183, 189, 206 Cal. Rptr. 495, 497 (1984); In re Marriage of Anderson, 154 Cal. App. 3d 572, 577-79, 201 Cal. Rptr. 498, 501-2 (1984).

The intent of the lender test will not be applied to characterize property acquired prior to marriage. See, e.g., In re Marriage of Jaffeman, 29 Cal. App. 2d 244, 255, 105 Cal. Rptr. 483, 490 (1972). For a case specifically discussing the different analysis required for property acquired before and after marriage see In re Marriage of Stoner, 147 Cal. App. 3d 858, 862-63, 147 Cal. Rptr. 351, 353-54, 359 (1983).

See infra notes 131-33 and accompanying text.

See infra notes 148-206 and accompanying text.

CAL. CIV. CODE §4800.2.


Moore, 28 Cal. 3d at 371-74, 618 P.2d at 210-11, 168 Cal. Rptr. at 664-65.

Id.

The same apportionment formula would apply to property purchased prior to mar-
the husband at the time of acquisition. The subsequent loan payments from community funds would cause the property to be apportioned according to the formula given by the California Supreme Court in *In re Marriage of Moore.*

Under the *Moore* formula, the separate property interest of the husband would be determined as follows. The proceeds of the loan would be treated as a separate property contribution. The total separate property contribution would be determined by crediting the separate estate with the down payment, $40,000, and the full amount of the loan proceeds less the amount by which the community property payments reduced the balance of the loan, $95,480 in this case. Thus, the total separate property contributions would be $135,480. This sum would be divided by the total purchase price, $140,000, to determine the percentage share of the separate estate.

The percentage share of the community would be determined by dividing the amount of the community contributions by the total purchase price. Only the portion of the loan payments that reduced the principal of the loan would be considered in determining the community contributions. In the above hypothetical, the community contribution would be $4,520 even though the community property payments totaled $144,600. In this hypothetical, the separate estate of the husband received the benefit of the loan proceeds as a contribution even though the loan obligation was satisfied entirely from community funds.

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68. *Id.*
69. The principal of the loan was reduced by $4,520. The initial $100,000 loan minus $4,520 equals $95,480.
70. The $40,000 down payment plus the $95,480 loan principal not paid with community funds equals $135,480.
71. *Moore*, 28 Cal. 3d at 373, 618 P.2d at 211, 168 Cal. Rptr. at 665.
72. *Id.*
74. The distribution of the property would be as follows:

<table>
<thead>
<tr>
<th>PAYMENTS</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Husband</td>
<td></td>
</tr>
<tr>
<td>Down payment</td>
<td>$ 40,000</td>
</tr>
<tr>
<td>Community</td>
<td></td>
</tr>
<tr>
<td>Interest</td>
<td>$140,080</td>
</tr>
<tr>
<td>Principal</td>
<td>4,520</td>
</tr>
<tr>
<td></td>
<td>$144,600</td>
</tr>
</tbody>
</table>
To appreciate the significance of the initial characterization of the loan proceeds, consider the result in the above hypothetical if the lender had not relied primarily upon the separate property of the husband and the loan was characterized as a community contribution. The same formula would be used to determine the proportional ownership interests in the property. The community, however, would have the benefit of the loan proceeds as a contribution to the purchase of the property. Consequently, the resulting value of the community ownership interest would be $110,520 as opposed to $4,520 even though the dollar amount of the contributions would be the same. Thus,

<table>
<thead>
<tr>
<th>RECOGNIZED CONTRIBUTIONS</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Husband</td>
<td></td>
</tr>
<tr>
<td>Down payment</td>
<td>$ 40,000</td>
</tr>
<tr>
<td>Loan Proceeds</td>
<td>95,480</td>
</tr>
<tr>
<td></td>
<td>$135,480</td>
</tr>
<tr>
<td>Community</td>
<td></td>
</tr>
<tr>
<td>Reduction of Loan Principal</td>
<td>$ 4,520</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>OWNERSHIP INTERESTS</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Husband</td>
<td>(appr.) 96.8%</td>
</tr>
<tr>
<td>Community</td>
<td>(appr.) 3.2%</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>PROPERTY DIVISION</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Repayment of Loan</td>
<td>$ 95,480</td>
</tr>
<tr>
<td>Share of Husband</td>
<td></td>
</tr>
<tr>
<td>Separate property</td>
<td>$175,000</td>
</tr>
<tr>
<td>Community property</td>
<td>4,520</td>
</tr>
<tr>
<td></td>
<td>$179,520</td>
</tr>
<tr>
<td>Share of Wife</td>
<td></td>
</tr>
<tr>
<td>Community property</td>
<td>$ 4,520</td>
</tr>
</tbody>
</table>

Bruch, supra note 9, at 791.
75. E.g., Aufmuth, 89 Cal. App. 3d at 456, 152 Cal. Rptr. at 674.
76. Moore, 28 Cal. 3d at 373-4, 618 P.2d at 211, 168 Cal. Rptr. at 665.
77. See infra note 78 and accompanying text.
78. The distribution of the property would be as follows:

<table>
<thead>
<tr>
<th>PAYMENTS</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Husband (down payment)</td>
<td>$ 40,000</td>
</tr>
<tr>
<td>Community</td>
<td></td>
</tr>
<tr>
<td>Interest</td>
<td>$140,080</td>
</tr>
<tr>
<td>Principal</td>
<td>4,520</td>
</tr>
<tr>
<td></td>
<td>$144,600</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>RECOGNIZED CONTRIBUTIONS</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Husband</td>
<td>$ 40,000</td>
</tr>
<tr>
<td>Community</td>
<td>$100,000</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>OWNERSHIP INTERESTS</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Husband</td>
<td>(appr.) 28.6%</td>
</tr>
<tr>
<td>Community</td>
<td>(appr.) 71.4%</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>PROPERTY DIVISION</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Repayment of Loan</td>
<td>$ 95,480</td>
</tr>
</tbody>
</table>
a substantial difference results merely from the characterization of the loan.

In summary, the current scheme of dividing property acquired with credit follows several general rules. First, the form of title may create a presumption that property acquired during marriage is owned by the community. If the form of title, however, does not raise this presumption, the character of the property will be determined according to the character of the funds used to make the purchase. The character of the loan proceeds is determined according to the intent of the lender test. Second, all property acquired prior to marriage is separate property regardless of the form of title or the intent of the lender. Third, separate property contributions to the acquisition of community property result in a right of reimbursement to the contributing spouse, but community property contributions to the acquisition of separate property will result in an apportionment of ownership between the separate and community estates. Fourth, under the apportionment formula, the full amount of the loan is recognized as a contribution, but only the portion of the repayments that reduce the principal of the loan are considered contributions. As a result of this apportionment formula, the community receives a relatively small interest in the property compared to the total dollar amount expended by the community. Moreover, the character of the loan proceeds has a more significant effect upon the property interests of the spouses than the character of the repayments. Since the initial character of the loan proceeds plays an important role in the final determination of the property rights of the spouses, the method by which this determination is made will be explored in greater detail.

<table>
<thead>
<tr>
<th>Share of Husband</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Separate property</td>
<td>$ 80,000</td>
</tr>
<tr>
<td>Community property</td>
<td>$ 52,260</td>
</tr>
<tr>
<td></td>
<td>$132,260</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Share of Wife</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Community property</td>
<td>$ 52,260</td>
</tr>
</tbody>
</table>

Bruch, supra note at 792.
79. See supra note 40 and accompanying text.
80. Aufmuth, 89 Cal. App. 3d at 454, 152 Cal. Rptr. at 673.
82. See supra notes 56, 57 and accompanying text.
83. CAL. CIV. CODE §4800.2.
84. Moore, at 372, 618 P.2d at 211, 168 Cal. Rptr. at 665.
85. See supra notes 68-74 and accompanying text.
86. Id.
INITIAL CHARACTERIZATION OF CREDIT PURCHASES

The initial character of property purchased on credit has been shown to be important in two ways. First, this initial character will determine whether subsequent payments will result in a right of reimbursement or an apportionment of ownership. Second, if an apportionment of ownership is appropriate, the character of the loan proceeds is given greater weight in the determination of contributions to the purchase price than the character of the repayments. For these reasons, the initial characterization must be the starting point in determining the property interests of the spouses.

In making this initial characterization, the court first must consider whether the purchase was made prior to or during the marriage. If the credit purchase was made prior to the marriage, the characterization is straightforward. Property acquired by either spouse prior to the marriage is separate property. Thus, property purchased on credit prior to the marriage will be characterized entirely as separate property at the time of acquisition.

Absent a valid agreement between the parties or a form of title that determines the character of the property, however, more difficult problems arise in making the initial characterization of property purchased during the marriage. By statute in California, all property acquired during the marriage is presumed to be community property. In a credit purchase initiated

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87. See supra notes 60-67 and accompanying text.
88. Id.
89. CAL. CIV. CODE §§5107, 5108.
90. E.g., Moore, 28 Cal. 3d at 373, 618 P.2d at 211, 168 Cal. Rptr. at 665.
91. Spouses may designate the character of their marital property by valid agreement. B. WITKIN, SUMMARY OF CALIFORNIA LAW, Community Property, §71 (1974). If an agreement regarding the character of the property exists, the courts will respect this agreement in dividing the property. Geller v. Anolik, 127 Cal. App. 2d 21, 27, 273 P.2d 29, 33 (1954). An agreement may be made prior to marriage, CAL. CIV. CODE §5133, or during marriage, Id. §5103. An agreement made prior to marriage must be in writing, Id. §5134, and must not by the terms of the agreement promote or encourage divorce. Glickman v. Collins, 13 Cal. 3d 852, 858, 533 P.2d 204, 208, 120 Cal. Rptr. 76, 80 (1975). The writing requirement for antenuptial agreements, however, is dispensible if the agreement is fully executed during marriage, Woods v. Security First National Bank, 46 Cal. 2d 697, 700, 299 P.2d 657, 659 (1956), or if one spouse detrimentally relies upon the oral agreement. Estate of Sheldon, 75 Cal. App. 3d 364, 373, 142 Cal. Rptr. 119, 125 (1975). See generally Monarco v. Lo Greco, 35 Cal. 2d 621, 625, 220 P.2d 737, 741 (1950) (estoppel as an exception to the statute of frauds). Agreements made during marriage must be in writing. CAL. CIV. CODE §5110.730(a). Civil Code section 5110.730, however, is not applicable to agreements made prior to January 1, 1985. Id. §5110.730(e). The law applicable to agreements made prior to January 1, 1985 allows property agreements, except agreements affecting joint tenancy property, see Id. §4800.1, to be made orally. Tomaier v. Tomaier, 23 Cal. 2d 754, 757-58, 146 P.2d 905, 907 (1944).
92. See infra note 40 and accompanying text.
93. CAL. CIV. CODE §5110.
during marriage, two presumptions will arise. First, a down payment presumptively is community property.\textsuperscript{94} Second, the proceeds of a loan or the portion of the property extended on credit presumptively is community property.\textsuperscript{95} The question, then, is whether these presumptions have been rebutted. A spouse may establish that the down payment, and consequently the portion of the property purchased with the down payment, is separate property by tracing the funds used to make the down payment to a separate property source.\textsuperscript{96} To determine the character of the loan proceeds, and consequently the portion of the property purchased with the loan, the court will look to the intent of the lender.\textsuperscript{97} Under this test, the community property presumption may be rebutted by evidence that the lender primarily relied upon separate property in extending the loan.\textsuperscript{98}

Although the intent of the lender test was applied very early in the development of California community property law,\textsuperscript{99} the reliance on the intent of a third party to determine the property rights of the spouses is questionable.\textsuperscript{100} The intent of the lender test is undesirable because the test is difficult to apply and fails to assess accurately the contributions of the spouses to the acquisition of the property.\textsuperscript{101} Before this author proposes a change in the method for initially characterizing property acquired on credit, the intent of the lender test will be examined.

\textit{A. The Intent of the Lender Test}

In 1953, the California Supreme Court in \textit{Gudelj v. Gudelj}\textsuperscript{102} provided a test for determining whether the proceeds of a loan and thus the property acquired with those loan proceeds are separate or community property.\textsuperscript{103} In \textit{Gudelj}, the husband purchased an interest in a business with a separate property down payment and a promissory

\textsuperscript{94} In re Marriage of Aufmuth, 89 Cal. App. 3d 446, 455, 152 Cal. Rptr. 668, 673 (1979).

\textsuperscript{95} Id.

\textsuperscript{96} \textit{Id.} See In re Marriage of Mix, 14 Cal. 3d 604, 611-12, 536 P.2d 479, 484, 122 Cal. Rptr. 79, 84 (1972) (general discussion of the tracing doctrine).

\textsuperscript{97} \textit{Aufmuth}, 89 Cal. App. 3d at 455-56, 152 Cal. Rptr. at 671-72 (citing Gudelj v. Gudelj, 41 Cal. 2d 202, 210, 259 P.2d 656, 661).

\textsuperscript{98} Gudelj v. Gudelj, 41 Cal. 2d 202, 210, 259 P.2d 656, 661 (1953).


\textsuperscript{100} The intent of the lender test has been heavily criticized. \textit{See} Young, \textit{supra} note 11, at 177-226.

\textsuperscript{101} \textit{See infra} note 219 and accompanying text.

\textsuperscript{102} 41 Cal. 2d 202, 259 P.2d 656 (1953).

\textsuperscript{103} \textit{Id.} at 210, 259 P.2d at 661.
note for the balance of the purchase price. The court held that
the character of the down payment could not be used to characterize
the entire property and, therefore, the character of the portion acquired
on credit would have to be determined. The court explained that
the character of the loan proceeds, and thus the character of the por-
tion acquired with credit, must be determined according to the intent
of the lender. The court held that the general presumption that
all property acquired during marriage belongs to the community still
applied, but stated that this presumption could be rebutted by
evidence that the lender, in extending credit, primarily relied upon
the separate property of the borrower. After reviewing evidence of
the lender's intent, the court concluded that the evidence was insuffi-
cient to overcome the community property presumption. The prop-
erty, therefore, was owned proportionately by both the husband and
the community. An application of the intent of the lender test,
however, need not always result in an initial characterization of mixed
separate and community ownership. For example, if the down pay-
ment in Gudelj had been made with community property, the prop-
erty would have been owned entirely by the community. Conversely,
if both the loan proceeds and the down payment were separate
property, the entire property would have been owned by the husband
as separate property.

The intent of the lender test essentially is an application of the
rule that allows a spouse to trace the acquisition of the property to
a separate property source. If the lender relies on the separate prop-
erty of a spouse in extending the loan, the loan proceeds are derived
from separate property and therefore acquire a separate property
character. Since the intent of the lender test is an application of

104. Id. at 209, 259 P.2d at 661.
105. Id. at 210, 259 P.2d at 661.
106. Id.
107. Id.
108. Id. Reliance upon separate property does not necessarily mean that the loan is secured
with separate property. The intent of the lender test applies equally to secured and unsecured
loans. See Bank of California v. Connolly, 36 Cal. App. 3d 350, 375, 111 Cal. Rptr. 468, 485 (1972) (unsecured loan); Estate of Ellis, 203 Cal. 414, 416, 264 P. 743, 744 (1928) (secured
loan).
109. Gudelj, 41 Cal. 2d at 211, 259 P.2d at 661.
110. Id.
111. See, e.g., Ives v. Connacher, 162 Cal. 174, 177, 121 P. 394, 395 (1912).
114. Id.
the tracing doctrine, the test is applicable only in cases in which the community property presumption is properly rebuttable by tracing.\textsuperscript{115} The community property presumption that arises merely because the property is acquired during marriage is rebuttable by tracing.\textsuperscript{116} The community property presumption that arises because of the form of title in which the property is held, however, is not rebuttable by tracing.\textsuperscript{117} Thus, if the form of title controls the initial character of the property, the intent of the lender test is not applicable.\textsuperscript{118} An important form of title presumption arises from California Civil Code Section 4800.1, which affects joint tenancy property. An understanding of this provision and the companion provision, section 4800.2, is important for an understanding of the current method of characterizing credit acquisitions.

B. Application of the Intent of the Lender Test Under Civil Code Sections 4800.1 and 4800.2\textsuperscript{119}

Section 4800.1 of the California Civil Code (hereinafter section 4800.1) limits the application of the intent of the lender test.\textsuperscript{120} Under section 4800.1, all property acquired by husband and wife during marriage in joint tenancy form is presumed to be community property for purposes of dissolution.\textsuperscript{121} This presumption is rebuttable only by a writing to the contrary.\textsuperscript{122} Thus, if a credit purchase is made during marriage and the property is taken in joint tenancy, the intent

\textsuperscript{116} In re Marriage of Mix, 14 Cal. 3d 604, 611-12, 536 P.2d 479, 584, 122 Cal. Rptr. 79, 84 (1979).
\textsuperscript{117} See supra notes 40-42 and accompanying text.
\textsuperscript{118} Lucas, 27 Cal. 3d at 813-15, 614 P.2d at 288-89, 166 Cal. Rptr. at 856-57. An express designation of ownership requires stronger evidence than the source of the funds used to acquire the property to rebut the community property presumption. Id. at 813-14, 614 P.2d at 288, 166 Cal. Rptr. at 857.
\textsuperscript{119} California Civil Code sections 4800.1 and 4800.2 became effective January 1, 1984. 1983 Cal. Stat. c. 342, §§1,2, at 1,2.
\textsuperscript{120} See In re Marriage of Boul, 159 Cal. App. 3d 174, 179, 205 Cal. Rptr. 543, 546-47 (1984). In Boul, the wife financed the purchase of a house taken in joint tenancy with her separate property down payment and two mortgages. The court, without discussion of the intent of the lender, held that the property was entirely separate property under Civil Code section 4800.1. Id.
\textsuperscript{122} Id.; CAL. CIV. CODE §4800.1. Section 4800.1 provides that the community property presumption may be rebutted by one of two means: (1) A clear statement in the deed or other documentary evidence of title by which the property is acquired that the property is not community property, or (2) proof that the parties have made a written agreement that the property is separate property. Id.
of the lender test will not apply and the entire property will be characterized as community property.123

Nevertheless, the intent of the lender still may be applied to determine whether a spouse has made a separate property contribution to the purchase of community property.124 Under California Civil Code section 4800.2 (hereinafter section 4800.2), if one spouse contributes separate funds toward the purchase of a community asset, that spouse is entitled to reimbursement for certain contributions125 upon dissolution of the marriage.126 Thus, if loan proceeds are found to be separate property, the separate estate will be entitled to reimbursement for the amount of the loan even though the entire property is community property.127 In contrast, if title is not taken in joint tenancy, the intent of the lender test is applicable.128 If this test results in a finding that a spouse has made a separate property contribution, that spouse will have a separate property ownership interest in the property rather than simply a right to reimbursement.129 The form of title must be the first inquiry in determining the initial characterization of the property. The initial characterization of the property, however, is not necessarily the character of the property at the time of divorce. Subsequent repayments of the loan may change the proportionate contributions of the separate and community estates.130 Therefore, the court must consider the effect of these subsequent payments.

123.  Boul, 159 Cal. App. 3d at 179, 205 Cal. Rptr. 543, 549-50. Conceivably, the loan agreement could constitute a writing sufficient to rebut the community property presumption under section 4800.1. See CAL. EVID. CODE §250 (definition of a writing). Courts have found some ancillary documents to be sufficient written evidence of the character of property. See, e.g., Estate of Watkins, 16 Cal. 2d 793, 797, 108 P.2d 417, 419 (1940) (joint will executed by husband and wife); Lawatch v. Lawatch, 161 Cal. App. 2d 780, 790, 327 P.2d 603, 608 (1958) (separate federal income tax returns filed by husband and wife). But see In re Estate of Neilson, 57 Cal. 2d 733, 744, 371 P.2d 745, 753, 22 Cal. Rptr. 1, 8 (1962), holding that the designation of earnings as community property in a federal income tax return could be overcome by evidence that the statement was motivated by an attempt to reduce taxes rather than an intent to designate the character of the property. In any event, to overcome the community property presumption, the loan agreement would have to state clearly that the property acquired by the loan is separate property. CAL. CIV. CODE §4800.1; see supra note 122 (discussion of the writing requirement under 4800.1).


125.  See supra note 23.

126.  CAL. CIV. CODE §4800.2.

127.  Id.

128.  See supra notes 44-49 and accompanying text.


CHARACTERIZATION OF THE PROPERTY
AFTER SUBSEQUENT PAYMENTS

The initial character of the loan proceeds and the effect of subsequent payments are two distinct questions. Nevertheless, the character of the proceeds will affect the analysis regarding subsequent payments in two important ways. First, if the loan proceeds are determined to be community property, subsequent payments of separate property will have no effect upon ownership interests in the property. Under section 4800.2, the spouse making the separate property contribution will be entitled to reimbursement only for the contributions. Second, if the loan proceeds are separate property, subsequent payments made from community funds will result in an apportionment of ownership in the proportions that total separate and community contributions bear to the purchase price. In summary, a different analysis is required depending upon the initial character of the loan proceeds. An understanding of these two approaches is important to an understanding of the current scheme of dividing property purchased on credit.

A. Separate Funds Contributed Toward the Payment of a Community Property Loan

Section 4800.2 has been considered previously with respect to separate property down payments. If one spouse makes a separate property down payment and because of a form of title presumption the down payment cannot result in a separate property interest, section 4800.2 provides for reimbursement to the separate estate. Section 4800.2 also applies to separate property payments toward a community property loan. Thus, upon a property division, the spouse who has contributed separate funds will receive the actual dollar amount of those contributions. Again, this right of reimbursement does not entitle the separate estate to a share of the appreciated value of the property. Ownership of the property will not be apportioned

131. CAL. CIV. CODE §4800.2.
133. Moore, 25 Cal. App. 3d at 371-72, 618 P.2d at 210, 168 Cal. Rptr. at 664; see also supra notes 67-74 and accompanying text (analysis of the Moore formula).
134. See supra notes 124-30 and accompanying text.
135. Id.
136. CAL. CIV. CODE §4800.2; Boul, 159 Cal. App. 3d at 183, 205 Cal. Rptr. at 550.
137. Boul, 159 Cal. App. 3d at 183, 205 Cal. Rptr. at 550.
138. Id.
in favor of the separate estate even though the separate estate contributed toward the purchase of the property.\textsuperscript{139} Although section 4800.2 limits the property interest that a separate estate may acquire, this provision allows greater compensation for separate property contributions than was allowed under prior case law.

Prior to the enactment of section 4800.2, the California Supreme Court in \textit{In re Marriage of Lucas}\textsuperscript{140} held that a spouse who contributed separate funds to purchase community property, absent an agreement or understanding between the spouses, had neither a separate property interest in the property nor a right of reimbursement.\textsuperscript{141} The theory underlying this decision was that separate property contributions are presumed to be gifts to the community.\textsuperscript{142} Section 4800.2 was enacted with the express legislative intent to overrule the \textit{Lucas} holding.\textsuperscript{143} Although the California Court of Appeal prior to \textit{Lucas} had decided that separate property contributions created a separate property interest in the property,\textsuperscript{144} the legislature, through section 4800.2, limited recognition of the separate contributions to a right of reimbursement.\textsuperscript{145}

This legislation, however, does not affect the California case law that developed regarding community property contributions toward the repayment of separate property loan proceeds. If the proceeds of the loan are determined to be separate property, either because the credit was extended to one spouse before marriage or because the lender relied upon separate property in extending the loan, California law gives the community an interest in the property in the proportion that the community contributions to equity bear to the total

\textsuperscript{139} Id.
\textsuperscript{140} 27 Cal. 3d 808, 816, 614 P.2d 285, 290, 166 Cal. Rptr. 853, 858 (1980).
\textsuperscript{141} Id. at 815, 614 P.2d at 287, 166 Cal. Rptr. at 855.
\textsuperscript{142} Id. at 816, 614 P.2d at 289, 166 Cal. Rptr. at 858. The source of this gift presumption is \textit{See v. See}, 64 Cal. 2d 778, 785, 415 P.2d 776, 780-81, 51 Cal. Rptr. 888, 892-93 (1966).
\textsuperscript{144} E.g., \textit{Aufmuth}, 89 Cal. App. 3d at 457, 152 Cal. Rptr. at 672. Prior to the \textit{Lucas} decision, California Appellate Courts took conflicting approaches to the effect of separate property contributions to the acquisition of community property. In \textit{In re Marriage of Aufmuth}, 89 Cal. App. 3d 446, 457, 152 Cal. Rptr. 674-75 (1979), the court held that the separate estate acquired a separate property interest in the property as a result of the separate property contributions. In \textit{In re Marriage of Trantafello}, 94 Cal. App. 3d 533, 542-46, 156 Cal. Rptr. 556, 562-64 (1979), the court held that the separate estate was entitled to neither an ownership interest in the property nor reimbursement. In \textit{In re Marriage of Bjornestad}, 38 Cal. App. 3d 801, 806, 113 Cal. Rptr. 576, 578-79 (1979), the court held that the separate estate was not entitled to an ownership interest in the property but was entitled to reimbursement of the separate property contributions.
\textsuperscript{145} \textit{Cal. Civ. Code} §4800.2.
purchase price. \(^{146}\) This formula was developed in the 1980 case of *In re Marriage of Moore*. \(^{147}\)

### B. Community Funds Contributed Toward the Payment of a Separate Property Loan

In *In re Marriage of Moore*, the California Supreme Court provided a formula for determining the interest in separate property acquired by the community as a result of community payments toward the separate property loan. \(^{148}\) The wife purchased a home shortly before her marriage, making a down payment and obtaining a loan for the balance of the purchase price. \(^{149}\) During the marriage, the spouses made payments on the loan from community property. \(^{150}\) The court first concluded that the loan proceeds were separate property because the loan was extended in reliance upon separate property prior to marriage. \(^{151}\) The court further determined that the proportionate interests of the separate and the community estates are determined by dividing the total contributions of each estate by the total purchase price. \(^{152}\) With respect to the community property loan payments, the court held that only the portion of the payment that reduces the principal of the loan should be recognized as a contribution to the purchase of the property. \(^{153}\) In contrast, the court held that the amount of the loan proceeds should be credited as a contribution to the purchase price. \(^{154}\) Thus, under the *Moore* formula, both the loan proceeds and equity contributions in the form of a down payment made at the time of the purchase are recognized, but only the equity portion of subsequent payments is recognized. As a result, the initial character of the loan has a more significant effect upon the final apportionment of interests than do the subsequent payments. \(^{155}\) Since only the equity portion of the repayments is recognized, the community is credited with only a small fraction of the total community payments toward the purchase of the property. \(^{156}\) Despite the harsh

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147. 28 Cal. 3d 366, 618 P.2d 208, 168 Cal. Rptr. 662 (1980).
148. *Id.* at 373-74, 618 P.2d at 211, 168 Cal. Rptr. at 665.
149. *Id.* at 370, 618 P.2d at 209, 168 Cal. Rptr. at 663.
150. *Id.*
151. *Id.* at 373, 618 P.2d at 211, 168 Cal. Rptr. at 665.
152. *Id.*; see also *supra* notes 67-74 and accompanying text.
154. *Id.* at 372-73, 618 P.2d at 210-11, 168 Cal. Rptr. at 664-65.
155. *See supra* notes 74, 78 and accompanying text.
156. *See supra* notes 72-74 and accompanying text.
result, Moore is the definitive rule on the proper method of apportionment. The Moore decision, however, leaves in doubt the proper scope of the apportionment right allowed.

In Moore, the spouses conceded that the community should have an interest in the questioned separate property of the wife. Consequently, the court was not required to discuss the proper application of the apportionment formula. This important question can be resolved by looking to the history of the apportionment theory in California.

C. The Proper Scope of the Moore Decision

Like the case law dealing with separate property contributions to community property prior to the enactment of section 4800.2, the cases prior to Moore relating community property contributions to the acquisition of separate property applied a presumption that these contributions were gifts. Some cases, however, created an exception when the husband used community funds to make payments toward his separate property or toward the separate property of the wife. This exception developed during the period of California

157. Moore, 28 Cal. 3d at 371, 618 P.2d at 209-10, 168 Cal. Rptr. at 663-64.
160. The rationale for this exception was to control the exclusive power of the husband over the community estate. See infra note 165-69 and accompanying text. Theoretically, if the wife acted as manager of the community property, the same exception should have applied. See Wilcox v. Wilcox 21 Cal. App. 3d 458, 459, 98 Cal. Rptr. 319, 320 (1971), holding that the wife as manager owes a fiduciary duty to her husband. Anytime the husband benefitted to the detriment of the wife, however, the courts placed the burden of proof on the husband to show that the wife fully understood the consequences of her transaction. DeFuniaik, Improving Separate Property or Retiring Liens or Paying Taxes on Separate Property with Community Funds, 9 Hastings L.J. 36, 37 (1957).
community property law in which the husband had the exclusive right to manage and control the community estate.\textsuperscript{163} During this period, the courts held that if the husband used community property to make payments toward the acquisition of his separate property, the community had a right to be compensated for this expenditure.\textsuperscript{164} The rationale for this compensation was that the husband owed a fiduciary duty to his wife to avoid misappropriation of community assets.\textsuperscript{165}

The courts reasoned that spending community money on separate property constituted a constructive fraud for which the community was entitled to compensation.\textsuperscript{166} The measure of this compensation was the greater of reimbursement or the increase in the value of the property created by the expenditure.\textsuperscript{167} Similarly, the courts were concerned that the husband could cause a diminution in the value of the separate estate by buying into the separate property with community funds.\textsuperscript{168} Thus, if the husband spent community funds on his separate property or the separate property of the wife, without the consent of the wife, apportionment of ownership was allowed.\textsuperscript{169} Otherwise, payments by the spouses were considered gifts.\textsuperscript{170} In 1975, the California Civil Code was amended to give each spouse equal control over the community property.\textsuperscript{171} Nevertheless, the distinctions that developed under the earlier system of unequal management and control have never been abandoned expressly by either the courts or the California Legislature.\textsuperscript{172} Unless the \textit{Moore} decision was based on the stipulation that a community property interest existed, this decision is inconsistent with the prior case law.

In \textit{Moore}, the separate property in question was owned by the wife.\textsuperscript{173} Under prior law, community property payments made toward

\begin{itemize}
  \item \textsuperscript{163} See DeFuniak, supra note 160, at 37.
  \item \textsuperscript{164} \textit{E.g.} Warren, 28 Cal. App. 3d at 782, 104 Cal. Rptr. at 863; Dunn, 211 Cal. at 590, 296 P.2d 607.
  \item \textsuperscript{165} Warren, 28 Cal. App. 3d at 782, 104 Cal. Rptr. at 863.
  \item \textsuperscript{167} Warren, 28 Cal. App. 3d at 782, 104 Cal. Rptr. at 863-64.
  \item \textsuperscript{168} See Camire, 105 Cal. App. 3d 859, 866-67, 164 Cal. Rptr. at 671.
  \item \textsuperscript{169} Id.
  \item \textsuperscript{170} See supra note 159.
  \item \textsuperscript{171} \textit{CAL. CIV. CODE} §§5125, 5127.
  \item \textsuperscript{172} Bruch, \textit{Management Powers and Duties Under California's Community Property Laws: Recommendations for Reform}, 34 HASTINGS L.J. 229, 262-70 (1982).
  \item \textsuperscript{173} In re Marriage of Moore, 28 Cal. 3d 366, 370, 618 P.2d 208, 209, 168 Cal. Rptr. 662, 663 (1980).
\end{itemize}
the separate property of the wife were presumed to be gifts. If this law had been followed in the Moore case, the husband would not have been entitled to a community property interest in the separate property. Thus, the question that remains after Moore is whether this decision rests on the stipulated community interest or upon an abandonment of the gift presumption. Two possible interpretations exist.

The first is that Moore should be limited to the particular facts of the case. The California Supreme Court did not expressly abandon the prior case law, nor did the court attempt to distinguish Moore from the precedents. Furthermore, the supreme court decision of In re Marriage of Lucas, decided two months before Moore, held that a spouse who made separate contributions to the purchase of a community asset was not entitled to compensation for this expenditure unless the spouses had an agreement or understanding that the separate property contribution would remain separate property. The Lucas court also found evidence that a husband who allowed the wife to trade in a community property automobile to purchase a motor home with separate funds intended to make a gift to the wife. The Lucas decision evidenced a preference to treat contributions during the marriage as gifts. Other cases suggest that the basis for this gift presumption is the inherent generosity present between spouses. Thus, the Lucas case, decided five years after the adoption of the equal management and control statutes in 1975, suggests that the basis for the gift presumption is not the need to prevent misuse of community property by the husband during the period of unequal management and control. If the gift presumption is based not upon outdated concepts of unequal management and control, but upon a presumption of spousal generosity, no reason exists for presuming that the gift presumption has been implicitly overruled by the adoption of the equal management and control provisions. Consequently,

174. See supra notes 159-60 and accompanying text.
175. Id.
176. Moore, 28 Cal. 3d at 371-74, 618 P.2d at 210-11, 168 Cal. Rptr. at 664-65.
177. 27 Cal. 3d 808, 614 P.2d at 287, 166 Cal. Rptr. at 855.
178. Id. at 816, 614 P.2d at 290, 166 Cal. Rptr. at 858.
179. Id.
181. CAL. CIV. CODE §§125 (equal management and control of community personal property). Id. §§127 (equal management and control of community real property).
182. Bruch, supra note 172, at 265.
no reason exists for interpreting Moore beyond the facts of the case.

The other possible interpretation of Moore is that the case represents a subtle departure from the general presumption that community contributions to the acquisition of separate property are gifts. Prior to Moore, numerous California cases had discussed the right of the community to a proportionate share in the separate property of one spouse without regard to the gift presumption. In these cases, however, the community payments had been made by the husband toward his separate property. Therefore, these precedents involved constructive fraud even though the courts did not discuss this theory as the basis for their holdings. Nevertheless, several cases have recited the general rule in California that the community is entitled to a proportionate share in the separate estate whenever the community has contributed toward the acquisition of the separate property. For example, in In re Estate of Neilson, the husband acquired property on credit prior to the marriage. During the marriage, the husband made payments on the loan from community property earnings. The California Supreme Court gave the community an interest in the separate property of the husband. Although the constructive fraud rationale would have been applicable, this theory was not discussed. In Moore the Supreme Court did not explicitly rely upon the stipulation that the community had acquired an interest in the property. In fact, the court relied upon In re Estate of Neilson and other precedent to support the holding. The extension of these cases to a fact pattern to which they technically do not apply can be viewed as

184. See Estate of Bernatas, 162 Cal. App. 2d 693, 697-98, 328 P.2d 539, 541-42 (1958). The Bernatas court criticized prior cases for stating their holdings in language that was too broad to be accurate. Id. The Bernatas court stated that apportionment applies only if the husband spends community property on his own separate property. Id.
186. 57 Cal. 2d 733, 344 P.2d 745, 22 Cal. Rptr. 1, 7 (1962).
187. Id. at 737, 371 P.2d at 751, 22 Cal. Rptr. at 3.
188. Id.
189. Id. at 744, 344 P.2d at 745, 22 Cal. Rptr at 7.
190. Id.
192. In re Estate of Neilson involved a fact pattern in which the traditional elements of constructive fraud were present. Neilson, 57 Cal. 2d at 744, 371 P.2d at 751. Moore did not involve a fact pattern in which constructive fraud was present. 28 Cal. 3d at 370, 618 P.2d at 210, 168 Cal. Rptr. at 663.
a tacit approval of a general right of apportionment and a rejection of the gift presumption. Perhaps the question of whether or not the court intended to discard this presumption is answered best through an examination of the purpose of the gift presumption.

The Lucas decision and other cases suggest that this presumption is based on the inherent generosity of the spouses. Although this theory seems acceptable in the context of separate property contributions to the community, the theory is inapposite in the context of contributions made by the community to the acquisition of separate property. The theory underlying community property law is that wealth generated during marriage should inure to the benefit of both spouses equally. Therefore, the law should favor an apportionment formula that allows for appreciation in the value of property during marriage to inure to the benefit of the community, especially in cases in which the community has contributed to the acquisition of the property. In contrast, the law need not favor a similar aggregation of separate assets.

In In re Marriage of Camire, an appellate case decided prior to Moore, the court suggested that the purpose of the gift presumption is linked to the rules adopted to protect the wife during the period of unequal management and control. The court stated that the gift presumption arose to prevent the husband from creating a diminution in value of the separate estate of the wife by buying into the estate with community funds. If, as the Camire court suggests, the gift presumption is based upon the need to prevent abuses by the husband during the period of unequal management and control, the presumption should have no application subsequent to the adoption of the equal management and control provisions. The Camire rationale for the gift presumption appears to be more consistent with the basic intent of community property law that aggregation of community wealth should be favored. Therefore, the Moore decision

193. See supra notes 178-80 and accompanying text.
198. Id. at 867, 164 Cal. Rptr at 671.
199. Id.
200. See Bruch, supra note 172, at 265-67.
should be interpreted to mean that community property contributions to the acquisition of separate property result in a proportionate community ownership interest regardless of whose separate property is in question and which spouse makes the payments.

In summary, the Moore decision provides the method for analyzing the effect that subsequent payments of the loan have on the character of property acquired on the credit of one spouse separately.\textsuperscript{201} Although Moore leaves unsettled the proper scope of the apportionment right in California, an analysis of the prior case law suggests that Moore should be given an expansive interpretation.\textsuperscript{202} The Moore decision, therefore, has abandoned the rule that community property contributions to the acquisition of separate property are presumed to be gifts. The Moore formula is not the only step in determining the property interests at the time of divorce. Before this formula can be applied, the court first must characterize the property at the time of acquisition.\textsuperscript{203} The initial character of the property then will direct the analysis used to determine the effect of subsequent loan payments.\textsuperscript{204} In the opening hypothetical, this author illustrated the interaction between the intent of the lender test and the Moore formula.\textsuperscript{205} Inequities in the current characterization scheme briefly were mentioned.\textsuperscript{206} The problems associated with the intent of the lender test now will be considered in greater detail.

**CRITICISMS OF THE CURRENT LAW**

Earlier, this author described a hypothetical division of property acquired on credit.\textsuperscript{207} This hypothetical contrasted the result reached if the loan proceeds initially are characterized as separate property with the result reached if the loan proceeds initially are characterized as community property.\textsuperscript{208} The introductory hypothetical revealed that the initial character of the loan proceeds has a significant effect upon the ultimate property division.\textsuperscript{209} For this reason, the merits of the

\textsuperscript{201} See supra notes 148-54 and accompanying text.
\textsuperscript{202} See supra notes 158-205 and accompanying text.
\textsuperscript{203} See supra notes 87-101 and accompanying text.
\textsuperscript{204} See supra notes 131-33 and accompanying text.
\textsuperscript{205} See supra notes 36-78 and accompanying text.
\textsuperscript{206} See supra notes 73-78 and accompanying text.
\textsuperscript{207} See supra notes 68-78 and accompanying text.
\textsuperscript{208} See supra notes 74, 78 and accompanying text.
intent of the lender test as a method of characterization should be examined closely.\textsuperscript{210}

This test is not applied consistently by the California courts. In addition, the standard of proof necessary to establish that the lender relied primarily on separate property is varied and unpredictable. The intent of the lender test announced by the California Supreme Court in \textit{Gudelj v. Gudelj} requires evidence that the lender \textit{in fact} primarily relied upon separate property to establish a separate property character of the loan proceeds.\textsuperscript{211} Subsequent cases, however, have inferred reliance upon separate property from the existence of separate property wealth upon which the lender might have relied.\textsuperscript{212} If reliance upon separate property can be inferred, property acquired during marriage may become separate property simply because one spouse owned sufficient separate property to be credit worthy. By inferring reliance on separate property, the courts too easily rebut the presumption that all property acquired during the marriage is community property.\textsuperscript{213}

Similarly, decisions have varied regarding the type of evidence needed to establish the intent of the lender. Most courts that have decided the issue have held that separate property security alone is not sufficient to establish reliance on separate property.\textsuperscript{214} In one case, however, the court based a finding of separate property solely upon the separate property character of the security.\textsuperscript{215} Confusion also has arisen concerning the evidentiary effect of the signing of the promissory note by the second spouse. As a practical matter, one might expect the signatures of both spouses to evidence reliance upon the community for repayment. The courts, however, have held that the signature of the second spouse should not be considered evidence of the intent of the lender to rely upon the community rather than the separate property of one spouse.\textsuperscript{216} Alternatively, the courts seem willing to

\textsuperscript{210} For a critical analysis of all California cases interpreting the intent of the lender test see Young, \textit{supra} note 11, at 174, 226.

\textsuperscript{211} \textit{Gudelj v. Gudelj}, 41 Cal. 2d 202, 210-11, 259 P.2d 656, 661 (1953).


\textsuperscript{213} One author has argued that only actual monetary contributions should be able to rebut the presumption that all property acquired during the marriage is community property. Bruch, \textit{supra} note 9, at 797.

\textsuperscript{214} \textit{E.g.}, Bank of California v. Connolly, 36 Cal. App. 3d 350, 375, 111 Cal. Rptr. 468, 485 (1972).


infer a separate property characterization from the signature of only one spouse on the loan.\textsuperscript{217} In short, the intent of the lender is difficult to establish and confusing to understand. This difficulty is compounded further by the inconsistent elements of proof that the courts apply.\textsuperscript{218}

Even if the true intent of the lender were easily ascertainable, the intent of this third party, as a means of tracing the acquisition of the property to a separate property source, does not accurately assess the contributions made by the spouses. This inaccuracy primarily results from the fact that the intent of the lender test is limited to a finding that the lender relied primarily upon either separate property or community property but not upon both.\textsuperscript{219} For example, if one spouse owns substantial separate property resources, the court might find that the lender relied primarily upon this separate property even though the lender also relied upon community assets in extending the loan. Alternatively, if one spouse mortgages separate property to secure a loan, the court may find that the lender did not primarily rely upon the security and accordingly find that the loan proceeds are community property. In this instance, the intent of the lender test does not recognize the security as a separate contribution. Upon careful analysis, however, the separate estate has made a significant contribution through a diminution in the value of the property resulting from the encumbrance and by bearing the risk of loss in the event of a default. Thus, under the intent of the lender test, contributions made by one spouse or by the community may go unrecognized.

In addition, the intent of the lender test frustrates the probable expectations of the spouses. If the spouses were to designate the character of the loan proceeds by agreement or understanding, the intent of the lender test would not be applied to characterize the property.\textsuperscript{220} Yet, if no agreement or understanding exists, the courts look to evidence of the intent of a third party rather than to evidence of the intent of the spouses. Property purchased during marriage most

\textsuperscript{217} See Somps 250 Cal. App. 2d at 336-37, 58 Cal. Rptr. at 310 (1967). The court noted that the fact that the wife was not a co-signer was one factor justifying the conclusion by the trial court that the property was separate property. Id.

\textsuperscript{218} See supra notes 214-17 and accompanying text.

\textsuperscript{219} E.g., Bank of California v. Connolly, 36 Cal App. 3d 350, 375, 111 Cal Rptr. 468, 485 (1972).

\textsuperscript{220} See infra note 89 and accompanying text. The understanding regarding the character of the property need not be predicated upon an express agreement. See Nelson v. Nelson, 224 Cal. App. 2d 138, 142, 36 Cal. Rptr. 352, 355 (Treatment of property as community property was sufficient to establish a community property character.).
likely is perceived by the spouses as community property.\textsuperscript{221} This intent does not necessarily change merely because one spouse is in a better financial position than the community. At the time of divorce, however, one spouse may be favored by the testimony of the lender even though the intent of the lender derogates from the expectations and understanding of the spouses at the time of the purchase. A particular example of this problem is \textit{Ford v. Ford}.\textsuperscript{222}

In \textit{Ford}, the husband purchased a farm with a separate property down payment and a loan secured by a deed of trust on other separate property.\textsuperscript{223} Both spouses signed the promissory note.\textsuperscript{224} The profits from the land were sufficient to meet the loan payments.\textsuperscript{225} The court determined that the loan proceeds were separate property even though the wife had signed the promissory note.\textsuperscript{226} Since the payments were made from the separate property of the husband, the court did not need to consider the effect of subsequent payments of a different character.\textsuperscript{227} Upon dissolution of the marriage, the husband received the entire value of the property.\textsuperscript{228} Although the wife argued that the joint signatures evidenced an intent by the spouses to regard the property as a community asset and an intent by the lender to rely upon the community in extending the loan, the court rejected these considerations.\textsuperscript{229} Moreover, in characterizing the loan proceeds, the court did not consider who would be liable for the debt. In this transaction both the community\textsuperscript{230} and the wife\textsuperscript{231} became liable for repayment and consequently could have been compelled to pay for property in which neither had an interest.\textsuperscript{232} The result reached in this case seems inconsistent with the expectations of the spouses. Although

\begin{footnotesize}
\begin{enumerate}
\item[221.] Washington law places greater emphasis upon the intent of the spouses. In Washington, loan proceeds are characterized according to the purpose for which the indebtedness is created. National Bank of Commerce v. Green, 463 P.2d 187, 190-91 (Wash. App. 1969).
\item[222.] 276 Cal. App. 2d 9, 80 Cal. Rptr. 435 (1969).
\item[223.] \textit{Id.} at 10, 80 Cal. Rptr. at 437.
\item[224.] \textit{Id.}
\item[225.] \textit{Id.}
\item[226.] \textit{Id.} at 13, 80 Cal. Rptr. at 438.
\item[227.] \textit{Id.} at 14, 80 Cal. Rptr. at 439.
\item[228.] \textit{Id.}
\item[229.] \textit{Id.}
\item[230.] California Civil Code section 5116 provides, "The property of the community is liable for the contracts of either spouse which are made after marriage...."
\item[231.] The wife became liable as a result of signing the promissory note. CAL. COM. CODE §3118(e).
\item[232.] At least one jurisdiction has recognized the problem of the community becoming liable for separate property debts. In Texas, credit acquisitions during marriage are community property unless the transaction is structured in such a manner that the creditor can reach only separate property. Dillard v. Dillard, 341 S.W. 2d 668, 671 (Tex. 1960).
\end{enumerate}
\end{footnotesize}
the spouses possibly had no expectation that the property in this case would be community property, the possibility also exists that the husband did not really expect that the property would be his separate property. Even if the spouses had no expectations of the character of the property, however, the fact that the wife and the community became liable for the debt and the fact that the property was acquired during marriage without any actual expenditure of separate money militate against a finding that the property is entirely separate property.

The intent of the lender test also may be inconsistent with the expectations of the lender. In granting a loan, a lender expects repayment. The lender does not expect that the debt will be satisfied through a default from the security used for the loan or from an attachment of existing property. In the same sense, a borrower recognizes an obligation to repay the debt. Neither party views the loan proceeds as a contribution to the purchase; each recognizes that the actual contribution is the repayment. Since the expectation of the lender is repayment, the probable source of repayment should have a greater influence upon the character of the property than the character of the loan proceeds. As the law is applied currently, the source of the repayments has relatively little influence upon the initial character of the property. In turn, once the loan proceeds have been characterized, subsequent payments actually made also have relatively little influence on the property interests at the time of divorce. This final result occurs because of the treatment of the subsequent payments under the Moore formula.

Under the Moore formula, the loan proceeds are credited as a contribution to the acquisition of the property. This contribution will be reduced by the amount that community property contributions reduce the principal of the loan. The reduction attributable to community contributions, however, would be relatively small in comparison

233. Young, supra note 11, at 254 (empirical study of California lending practices).
234. The Supreme Court of Idaho expressly rejected the Gudelj rule on this ground. Winn v. Winn, 673 P.2d 411, 414 (Idaho 1983). The court stated that the Gudelj rule is unrealistic because the lender will expect repayment from any source and will not feel bound by the initial reliance in extending the loan. Id. In Idaho, loan proceeds acquired during the marriage are separate property only if the separate estate is the primary source of future repayment. Lepel v. Lepel, 456 P.2d 249, 253 (Idaho 1969).
235. See supra notes 102-108 and accompanying text.
236. See supra notes 68-74 and accompanying text.
238. Id.
to the actual contributions of the community. Only the portion of
the loan payment that reduces the principal is recognized as a
contribution. The effect of this approach is that the loan proceeds
have a greater influence upon the character of the property than do
actual payments. In reaching a final determination of the proper
method to apportion the property, the California Supreme Court in
Moore rejected the method used by the lower court that considered
only the equity contributions with no credit given for the loan
contribution. The court stated that this formula used by the lower
court ignores the importance of the loan in the acquisition of the
property.

A recognition of the importance of the loan, however, should not
result in a disregard of the importance of the loan payments. Without
subsequent repayments to satisfy the periodic obligations of the debt,
the loan would have little value as a contribution to the purchase
of the property. This periodic obligation includes not only principal
but also interest. Several inequities exist with the exclusion of interest
payments as contributions to the purchase of the property. Most
notably, the community may receive recognition for only a fraction
of the total community contributions. With expensive purchases,
like the purchase of a home, a loan is usually a necessary means of
making the acquisition. A necessary incident of the loan is the pay-
ment of interest. Consequently, interest is just as much a contribu-
tion to the acquisition as is the initial purchase price. The supreme
court justified the exclusion of interest payments on the ground that
the value of property ordinarily is measured only by the equity of
the owner and that only contributions to equity should be considered.
This statement, however, seems difficult to reconcile with the view
of the court that the loan proceeds should be considered as contribu-
tions. The debt incurred at the time the property was acquired was
no more a contribution to equity than the subsequent interest payments.

239. See supra notes 68-74 and accompanying text.
240. Moore, 28 Cal. 3d at 373, 618 P.2d at 211, 168 Cal. Rptr. at 665.
241. See supra notes 68-74 and accompanying text.
243. Id.
244. See supra notes 68-74 and accompanying text. The disparity between community con-
tributions and the resulting community interest may not always be as significant as was shown
earlier. See Id. This disparity will be less significant if loan payments are made later in the
repayment schedule when a more substantial portion of the loan payment reduces the principal
of the loan.
245. Moore 28 Cal. 3d at 372, 618 P.2d at 211, 168 Cal. Rptr. at 665.
If the standard for determining the amount contributed is the increase in the equity of the property, the loan proceeds technically should not be considered contributions either. Moreover, the extent of the community interest under the Moore formula depends upon the time during the repayment schedule that the contributions are made. In the typical amortized loan, the payments made early in the repayment schedule are primarily for interest rather than for principal. Therefore, the extent of the community interest depends less upon the amount of the contributions and more upon the time at which they are made. For these reasons, the current scheme of characterizing property acquired on credit should be modified in a manner that results in a more equitable division of the property.

PROPOSAL

This author has demonstrated that the current scheme of dividing assets acquired on credit is, in certain situations, inequitable. As long as the law recognizes the right of a spouse to hold separate property during the marriage, the law regarding the characterization of property owned by the spouses will continue to be a complex matter. Several improvements, however, should be made to both the method of initially characterizing property purchased on credit during marriage and to the method of apportioning ownership after community funds have been spent to satisfy a separate property loan obligation.

A. Characterization of Purchases Made During Marriage

The intent of the lender test should be replaced with a rule that allows a rate of return on property used to secure a loan. This rate of return would be the measure of the contribution made by the separate estate. For example, if a spouse mortgages separate property as security for a loan or credit purchase, the court should measure this contribution by a fair rate of return on the property. This rate should be sufficient to compensate the separate estate for the diminution in the value of the separate property caused by the encumbrance and for the risk of loss from a default. Under this approach, the

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247. See supra notes 207-46 and accompanying text.
248. See infra note 248.
value of the loan would be community property in accordance with the community property presumption except for a portion of the value of the loan attributable to the fair rate of return on the separate property. If the loan is unsecured, the law should find strictly in accordance with the community property presumption. In the case of an unsecured loan, the separate estate has not actually contributed anything to the acquisition of the property or the contribution by the separate estate is insignificant and immeasurable. The separate estate has not incurred an additional risk nor suffered a decrease in value by an encumbrance.

This rate of return theory finds support in other areas of California community property law. The rate of return concept is similar to that used by the courts to apportion the profits from a separate property business. If a spouse owns a separate property business, the court must determine what portion of the profits is due to the property investment and what portion is due to the labor of the spouse. In Pereira v. Pereira, the California Supreme Court developed a rule for making this determination. Under the Pereira rule, the court will allocate to the separate estate a fair rate of return on the property investment. The balance of the profits will be community property. The Pereira situation is similar to the acquisition of property on credit. In both cases, the court determines the contribution that separate property has made to the acquisition of wealth during the marriage.

249. This rate of return also would be used to determine a separate property contribution for purposes of section 4800.2. See supra notes 119-30 and accompanying text.
252. Id.
254. The Pereira formula is one permissible approach to apportioning the profits from a separate property business. In the alternative, courts may apply the approach developed in Van Camp v. Van Camp, 53 Cal. App. 17, 20, 199 P. 885, 887 (1921). The Van Camp approach apportions business profits by allocating to the community the portion of the profits that represents a fair wage for the skill and labor of the spouse owning the business. Id. Courts have discretion to apply the formula that achieves the more equitable result under the circumstances. Beam, 6 Cal. 3d 12, 17-19, 490 P.2d 257, 260-62, 98 Cal. Rptr. 137, 141-42 (1972).
255. Id. at 7-8, 103 P. at 491. The court must select a rate of return that will achieve "substantial justice." Logan v. Forster, 114 Cal. App. 2d 587, 600, 250 P.2d 730, 738 (1952). A trial court has considerable discretion in determining this figure. In re Marriage of Folb, 53 Cal. App. 3d 862, 872, 125 Cal. Rptr. 306, 313 (1975).
256. Id.
If the credit purchase is made prior to the marriage, however, this approach is not applicable. All property acquired before marriage still will be separate property. The Moore formula, however, should be amended to place greater emphasis on the community property contributions to the loan payments.

B. Apportionment of Separate Property Purchased Partially With Community Contributions

In Moore, the court was concerned with maintaining the loan as a contribution to the acquisition of the property. Under the approach proposed by this author, the loan still would be credited as a contribution. The interest portion of the repayments also would be recognized as contribution to the purchase. The proportionate interests of the spouses and the community would be determined by dividing separate and community contributions by the total contributions made. Under this approach, both equity and nonequity contributions would be recognized equally, whether these contributions are made at the time of the initial acquisition or in subsequent payments. The recognition of all contributions made by the community to the acquisition of an asset would be more consistent with other areas of California community property law.

California courts apportion ownership in areas other than credit purchases when both separate and community funds contribute to the acquisition of an asset. Like credit purchases, these cases usually involve the acquisition of property over time. In these cases, the courts have developed a doctrine of equitable apportionment. Under the doctrine of equitable apportionment, whenever separate and community efforts combine to acquire an asset, ownership in that property is shared in the proportion that the contributions of each estate bear to the total purchase contributions.

This approach was taken by the court in Vieux v. Vieux. The

257. Id.
259. Moore, 28 Cal. 3d at 374, 618 P.2d at 211, 168 Cal. Rptr. at 665.
262. Id.
*Vieux* case involved an installment purchase contract. A down payment was made from separate property prior to the marriage. 264 During the marriage, the balance owed on the contract was paid from community property funds. 264 The court apportioned ownership in the property by recognizing the total contributions made by each estate. 265 *Vieux* is apparently distinguishable on the ground that in an installment contract, title is not acquired until after the contract is satisfied. 266 If the courts examined the substance of the transactions rather than the form, however, the same result could be reached in either case.

The current law places undue emphasis on the form of the transaction. Under this proposal, credit purchases and installment purchases would be treated in the same manner. Thus, if community funds are used to repay a separate property loan, the community would be entitled to own the property in the same percentage as community payments bear to total contributions made by both the community and the separate estate. In addition, in determining the total contributions of the community, the law would recognize the payments of interest as well as the payments of principal.

In summary, this proposal would improve the existing case law in several significant respects. First, the evidentiary problems with the

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264. *Id.* at 224, 64 P. at 65.
265. *Id.* The *Vieux* court recognized payments for interest. *Id.*
266. H. Verrall, *supra* note 113, at 242. The significance of this distinction lies in the difference between the inception of right theory and the apportionment theory. Community property systems generally follow either one of these theories. W. DeFunia & M. Vaughn, *supra* note 194, §64, at 130. Under the inception of title theory, the character of the property is determined at the time that title is acquired and does not later change even though payments may be made over time from different sources. *Id.* Under the apportionment approach, title to the property is shared by the community and a separate estate in the proportions that community and separate property payments bear to total contributions made by both the community and the separate estate. In addition, in determining the total contributions of the community, the law would recognize the payments of interest as well as the payments of principal.

In summary, this proposal would improve the existing case law in several significant respects. First, the evidentiary problems with the
intent of the lender test would be eliminated. In addition, this proposed replacement for the intent of the lender test would more accurately measure the contribution that existing separate property may make to the acquisition of a loan. Finally, this proposal treats initial payments and loan payments with equal weight so that the community will acquire an interest in separate property in direct proportion to the total contributions made by the community. Each of these modifications more accurately reflects the intent and expectations of the husband and wife. In addition, these modifications provide a method by which the courts may divide the property more fairly on dissolution of the marriage.

CONCLUSION

The author has described the application of the current scheme used in California to characterize property purchased on credit. Furthermore, the author has noted several inequities that exist under the current law and has provided recommendations for reform. Under the current law, the initial character of the proceeds of a loan or the portion of the property purchased with debt has a substantial effect upon the ultimate property interests of the spouses. First, the initial characterization will dictate the effect that subsequent payments on the loan will have. Contributions of separate property to the acquisition of a community asset now are entitled only to a right of reimbursement. On the other hand, if the community has contributed to the acquisition of separate property, the community will be entitled to an apportioned ownership interest in the property. Second, under the apportionment formula, the amount of subsequent payments may have a relatively small effect upon the contributions since payments of interest are not recognized as contributions. Consequently, upon a divorce, an asset may be deemed substantially separate property even though the property was acquired substantially with community funds. Despite the importance of the initial characterization, the test used to make this characterization does not assess contributions of the parties accurately. Unless title to the property has been taken in joint tenancy, the property initially will be characterized by looking to the subjective intent of a third party. This author has shown that this test may be contrary to the expectations of all the parties to the transaction.

To avoid these inequities, the courts should uphold the community property presumption unless the separate estate has made a measurable
contribution to the acquisition of the loan by securing the loan with separate property. The apportionment formula should be modified to recognize the equity and the nonequity components of all contributions regardless of the time that these contributions are made. By recognizing all contributions made to the acquisition of assets on credit, the law would bring the apportionment of credit purchases more in line with the apportionment doctrine used in other areas of California community property law.

Andrew M. Cummings