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## Rights of Creditors to Collect Marital Debts After Divorce in Community Property Jurisdictions

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## Rights of Creditors to Collect Marital Debts After Divorce in Community Property Jurisdictions

James L. Musselman\*

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## I. Introduction

Creditors who extend credit or otherwise become entitled to payment of obligations owed by debtors have various legal rights and expectations, mostly to collect those obligations in due course based on agreement or operation of law. Debtors are personally and legally obligated to pay the obligations they incur. When debtors default with respect to payment of those obligations, creditors generally have the right to bring a legal cause of action against them and acquire a judgment. Failure by the debtor to pay the judgment gives to the judgment creditor the right to exercise various post-judgment remedies in order to collect the judgment. This includes the attachment and foreclosure of nonexempt property owned by the debtor.

When a debtor is married, issues arise with regard to whether the judgment creditor can attach property owned in whole or in part by the debtor's spouse. There exist two separate types of marital property regimes in the United States. The first and most common type is the *common law property system* adopted from the laws of England. In general, when only one spouse is personally liable for an obligation, a judgment creditor cannot attach property owned by the other spouse to satisfy the judgment.<sup>1</sup> Spouses in common law property jurisdictions are treated as separate persons with regard to obligations incurred by each individual during the marriage.<sup>2</sup>

The second type of marital property regime used by nine of the states is the *community property system*, adopted from Spanish law. In this system, marital property is characterized as either separate property of one spouse or community property. Separate property is treated generally as if the spouses are single and not married.<sup>3</sup> As a consequence, with

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1. See Margaret M. Mahoney, *The Equitable Distribution of Marital Debts*, 79 UMKC L. REV. 445, 449–50 (2010) (explaining that in the forty-one common law property states, liability for unsecured debts is limited to the spouse who incurred the debt).

2. See *id.* at 445 (stating that, in common law property states, spouses retain their separate identity with regard to both debts and ownership of assets).

3. See, e.g., *Cameron v. Cameron*, 641 S.W.2d 210, 223 (Tex. 1982) (stating that separate property owes its existence to things entirely unrelated to the marriage, and the spouses are treated as strangers with regard to that

respect to obligations for which only one spouse is personally liable, separate property in the community property system is treated generally the same as marital property in the common law property system. A judgment creditor cannot attach separate property owned by the other spouse to satisfy the judgment.<sup>4</sup> Community property is treated as if each spouse owns an undivided one-half interest in such property.<sup>5</sup> A significant issue in the community property system is to what extent a judgment creditor can attach community property to satisfy a judgment for which only one spouse is personally liable.

The nine community property states have adopted a variety of distinct rules with regard to this issue. Some jurisdictions have adopted rules that are extremely friendly to creditors, allowing the attachment of virtually any nonexempt community property to satisfy a judgment for which only one spouse is personally liable, regardless of whether the underlying debt was incurred before or during the marriage.<sup>6</sup> Other jurisdictions have adopted rules that are more restrictive with regard to creditors, preventing the attachment of certain community property based on a variety of factors.<sup>7</sup> Part II of this Article will provide a review of the rules that are used in both the common law property states and the community property states with regard to this issue.

A much more troublesome issue has arisen in the community property states when spouses divorce. Namely, to what extent is a creditor allowed to obtain a post-divorce judgment against a spouse who is not personally liable for a debt incurred by the other spouse either before or during the marriage, and attach nonexempt property either received by

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property).

4. See, e.g., TEX. FAM. CODE ANN. § 3.202(a) (West 2006) (providing that a spouse's separate property is not subject to debts for which only the other spouse is personally liable).

5. See Mahoney, *supra* note 1, at 449 (explaining that, as a general rule, each spouse owns half of all community assets).

6. See Andrea B. Carroll, *The Superior Position of the Creditor in the Community Property Regime: Has the Community Become a Mere Creditor Collection Device?*, 47 SANTA CLARA L. REV. 1, 7 (2007) (discussing Louisiana law providing that separate or community obligations may be satisfied from any community property).

7. See *id.* at 8–20 (comparing community property states that use a managerial system of liability with those that use a community debt system).

such spouse in the divorce or subsequently acquired by such spouse. This issue has been dealt with in a variety of ways by the nine community property states. Consistent with the first issue discussed above involving attachment during the marriage of property owned by the non-debtor spouse, some of the states have adopted rules that are extremely friendly to creditors,<sup>8</sup> and others have adopted rules that are more restrictive.<sup>9</sup> In some jurisdictions, creditors acquire greater rights as a result of the divorce than they would have if no divorce had occurred.<sup>10</sup> Part III of this Article will provide a review of the rules that are used in the community property states with regard to this issue.

The primary thrust of this Article is to address the post-divorce liability issue outlined in Part III from the perspective of debtor-creditor law. The rules adopted in most of the community property jurisdictions with respect to this issue appear to be primarily focused on the perspective of marital property and family law without regard to general debtor-creditor law principles and policies. For example, basic fraudulent transfer law has been ignored in those jurisdictions and not applied in the usual manner. As a result, the rules developed in those jurisdictions with regard to the post-divorce liability issue are not consistent with the basic principles and policies of debtor-creditor law. Part IV of this Article will discuss basic debtor-creditor law as it relates to this issue, and will propose a set of rules which could and should be adopted by the community property jurisdictions consistent with debtor-creditor law as it applies generally.

## II. Liability of Marital Property for Obligations for Which Only One Spouse is Personally Liable

Personal liability for obligations is established pursuant to

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8. See James R. Ratner, *Creditor and Debtor Windfalls from Divorce*, 3 EST. PLAN. & COMMUNITY PROP. L.J. 211, 214–23 (2011) (describing the law of community property states, such as Arizona, that actually provide for windfalls to creditors when married couples divorce).

9. See James W. Paulsen, *The Unsecured Texas Creditor's Post-Divorce Claim to Former Community Property*, 63 BAYLOR L. REV. 781, 812–15 (2011) (describing the restrictive approach used in Idaho with regard to this issue).

10. See Ratner, *supra* note 8, at 214–23.

general principles of law based on the type of obligation involved. Executing a contract can cause a person to become contractually obligated for a debt. Committing a tort or crime may cause an obligation to be imposed on a person in court or by a federal, state, or local law—for example, a tax liability. Many possibilities exist by which a person can become liable for some type of obligation. These rules apply in the same way to both single and married persons, with certain exceptions.<sup>11</sup> A married person may be held liable for the acts of his spouse in several situations. First, some community property states recognize the “necessaries doctrine,” in which a spouse is held personally liable for debts incurred by the other spouse for necessities, such as food, clothing, or medical care.<sup>12</sup> In other states, a spouse may be held liable if his or her spouse acts as his or her agent under general agency/principal law.<sup>13</sup> Other legal theories sometimes used to impose liability on a spouse for acts of the other spouse include the doctrines of ratification and unjust enrichment.<sup>14</sup>

It is obvious that obligations incurred *prior to* marriage are the sole obligation of the person incurring them. However, obligations incurred *during* marriage may be the sole obligation of only one spouse, or may be the joint obligation of both spouses. Spouses could be jointly liable under any of the theories discussed above, or because both spouses are jointly liable under the applicable rule of law under which liability for the obligation is based. For example, if both spouses execute a contract, they are both jointly obligated with respect to it. If both spouses are jointly personally liable for an obligation, the creditor can bring a legal cause of action and obtain a judgment against both spouses individually and accordingly exercise post-judgment

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11. See James L. Musselman, *Once Upon a Time in Bankruptcy Court: Sorting Out Liability of Marital Property for Marital Debt Is No Fairy Tale*, 41 FAM. L.Q. 249, 251 (2007) (explaining the manner in which a person could become liable for an obligation).

12. See Carroll, *supra* note 6, at 20–23 (explaining the necessities doctrine as it has been applied in five of the community property states).

13. See *id.* at 23 (explaining the manner in which agency/principal law has been applied in some states to impose liability on a spouse for acts of the other spouse).

14. *Id.* at 24–25 (explaining the manner in which the doctrines of ratification and unjust enrichment have been applied in some states to impose liability on a spouse for acts of the other spouse).

remedies against each of them. If only one spouse is personally liable for an obligation, the issue is whether the judgment creditor can attach property owned in whole or in part by the non-liable spouse.

Generally speaking, in common law property states, when only one spouse is personally liable for an obligation, a judgment creditor cannot attach property owned by the other spouse to satisfy the judgment.<sup>15</sup> Spouses in common law property jurisdictions are treated as separate persons with regard to obligations incurred by only one of them during the marriage.<sup>16</sup>

The nine community property states have adopted a variety of distinct rules with regard to this issue. All nine states are typically categorized into one of two systems regarding marital property liability: (1) the managerial system; or (2) the community debt system.<sup>17</sup>

#### A. The Managerial System

California, Idaho, Louisiana, Nevada, and Texas are typically categorized under the managerial system.<sup>18</sup> The basic concept of a managerial system is that a creditor should be entitled to seize any community property which a spouse personally liable for a debt has the power to manage, and thereby voluntarily alienate to a creditor.<sup>19</sup> It should be noted that the underlying goal of this concept is not entirely achieved in any of the five states that are typically grouped in this category.

In Texas, determining whether a judgment creditor can attach nonexempt property owned in whole or in part by the non-

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15. See Mahoney, *supra* note 1, at 449–50 (explaining that in the forty-one common law property states, liability for unsecured debts is limited to the spouse who incurred the debt).

16. See *id.* at 445 (stating that in the common law property states, spouses retain their separate identity with regard to both debts and ownership of assets).

17. See Carroll, *supra* note 6, at 9–10 (describing the two basic systems for determining marital property liability in the community property states).

18. *Id.* at 11 (stating that these five states are commonly categorized under the management system of liability).

19. *Id.* at 11–12 (explaining the basic rationale for the managerial system of marital property liability).

liable spouse requires that the property first be characterized as separate property or community property. This is because a spouse's separate property is not subject to liabilities incurred solely by the other spouse.<sup>20</sup> Whether community property is subject to attachment by a judgment creditor for an obligation for which only one spouse is personally liable requires a determination of the extent to which the spouses have management power over that particular community property. By statute, each spouse is given the sole power to manage community property constituting (1) that spouse's personal earnings; (2) revenue from that spouse's separate property; (3) recoveries for personal injuries of that spouse; or (4) the increase or mutation of, or the revenue from, that spouse's personal earnings, revenue from separate property, or recoveries for personal injuries.<sup>21</sup> All other community property is subject to the joint management and control of the spouses, unless they agree otherwise as provided in the statute.<sup>22</sup> If a spouse is not personally liable for an obligation incurred solely by the other spouse, any community property over which that non-liable spouse has sole management and control is not subject to that obligation if: (1) the obligation was incurred by the other spouse prior to the marriage; or (2) the obligation was incurred by the other spouse during the marriage and is non-tortious.<sup>23</sup> Community property subject to joint management and control of the spouses can be attached to satisfy any obligation incurred by either of the spouses.<sup>24</sup> Community property is subject to all tortious obligations incurred by either or both spouses during the marriage.<sup>25</sup>

Texas is unique in its treatment of joint management and control over community property. Except in certain specific circumstances provided by statute, each spouse has power to manage his undivided one-half interest in the property, but has no power to manage the interest of the other spouse.<sup>26</sup> Thus,

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20. See TEX. FAM. CODE ANN. § 3.202(a) (West 2006).

21. See *id.* § 3.102(a).

22. See *id.* § 3.102(c).

23. See *id.* § 3.202(b).

24. See *id.* § 3.202(c).

25. See *id.* § 3.202(d).

26. See, e.g., *Williams v. Portland State Bank*, 514 S.W.2d 124, 127 (Tex.

both spouses must participate in and consent to a particular transaction with respect to community property subject to joint management and control.<sup>27</sup>

It is clear then that Texas does not adhere strictly to the basic concept of the managerial system for marital property liability, which is that a creditor should be entitled to seize any community property with respect to which a spouse personally liable for a debt has the power to manage, and thereby voluntarily alienate to a creditor. A spouse lacks the power to alienate to a creditor the other spouse's one-half undivided interest in joint management community property, yet community property subject to joint management and control of the spouses can be attached to satisfy any obligation incurred by either of the spouses. Additionally, all community property is subject to all tortious obligations incurred by either or both spouses during the marriage, regardless of which spouse has management power over the property. However, it is equally clear that Texas comes the closest by far to achieving the goal underlying this basic concept.

The remaining four states that are typically grouped in the managerial system category—California, Idaho, Louisiana, and Nevada—provide rules for determining management and control of community property that seem wholly unrelated to the applicable rules that determine which community property is available to satisfy debts incurred by only one spouse. In fact, it has been suggested that California and Louisiana are included in the managerial system category solely because they determine liability of marital property for debts without regard to whether the debt was incurred in the interest of the family or for the benefit of the community, and thus clearly do not fit into

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App. 1974) (holding that a lien conveyed by husband to bank on real property was not effective with regard to wife's one-half interest in community property because wife did not execute the deed of trust).

27. See WILLIAM A. REPPY, JR., CYNTHIA A. SAMUEL & SALLY BROWN RICHARDSON, *COMMUNITY PROPERTY IN THE UNITED STATES* 255 (8th ed. Carolina Acad. Press 2015) (noting that the Texas statutes dealing with joint management of community property require concurrence of both spouses); see also TEX. FAM. CODE ANN. § 3.104 (West 2006) (providing an important exception allowing a spouse to alienate the entirety of joint management community property titled in that spouse's name or in that spouse's possession (if not subject to evidence of ownership) once certain conditions are met).

the community debt system category.<sup>28</sup> In all four states, the basic rule with respect to management of community personal property is that each spouse has the power unilaterally to manage and alienate all such property;<sup>29</sup> for management of community real property, the basic rule is that both spouses must act together to manage or alienate the property.<sup>30</sup>

With regard to liability of community property for debts solely incurred by one spouse, California and Louisiana, by statute, permit creditors to reach almost any community property for virtually any debt incurred by either spouse regardless of which spouse has management power over that property.<sup>31</sup> California affords a limited exception to that basic rule, providing that earnings during marriage are exempt from

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28. See Carroll, *supra* note 6, at 13–14 (noting that California and Louisiana are grouped with Idaho, Nevada, and Texas under the managerial umbrella because those states determine liability of marital property without regard to whether the particular debt was incurred in the interest of the family or for the benefit of the community, both of which are hallmarks of the community debt system); see also REPPY, SAMUEL & RICHARDSON, *supra* note 27, at 312 (explaining that the current rules in all states which utilize the management system, other than Texas, “make it difficult, if not misleading, to say that management power determines” the right of creditors to seize community property for the debts of only one spouse, “[y]et the chief implication of a managerial system, that the creditor’s right to seize community property does not depend on the classification of the debt as a community debt, is still the rule” in those states).

29. See REPPY, SAMUEL & RICHARDSON, *supra* note 27, at 255 (stating that, in all community property states other than Texas, “the basic rule concerning power to manage and alienate community personal property is equal management based on concurrently possessed power to act unilaterally” (footnote omitted)); CAL. FAM. CODE § 1100(a) (West 2004); IDAHO CODE ANN. § 32-912 (LexisNexis 2006); LA. CIV. CODE ANN. art. 2346 (West 2009); NEV. REV. STAT. ANN. § 123.230 (LexisNexis 2007).

30. See REPPY, SAMUEL & RICHARDSON, *supra* note 27, at 255 n.1 (stating that “[w]ith respect to community realty, the basic rule in equal management jurisdictions is that alienation requires concurrent actions by both spouses . . .”); CAL. FAM. CODE ANN. § 1102(a) (West 2004); IDAHO CODE ANN. § 32-912 (LexisNexis 2006); LA. CIV. CODE ANN. art. 2347 (West 2009); and NEV. REV. STAT. ANN. § 123.230 (LexisNexis 2007).

31. See CAL. FAM. CODE ANN. § 910(a) (West 2004) (providing that, except in limited situations provided specifically by statute, all community property is liable for any debt incurred by either spouse before or during marriage, regardless of which spouse has management rights with respect to the property and which spouse is personally liable for the debt); LA. CIV. CODE ANN. art. 2345 (West 2009) (providing that a separate or community obligation may be satisfied from community property).

debts incurred by the other spouse prior to marriage if certain requirements are met.<sup>32</sup> Idaho has a statute that allows either spouse to “bind the community property by contract.”<sup>33</sup> Moreover, the Supreme Court of Idaho has long held that all “debts of either spouse may be paid from community property.”<sup>34</sup> Courts have similarly held that the basic rule in Nevada is the same as in California, Louisiana, and Idaho—that all community property is within creditor reach for any debt incurred by either of the spouses.<sup>35</sup> Similar to California, Nevada has a statute stating simply that a spouse’s share of community property is exempt from debts of the other spouse contracted for prior to marriage.<sup>36</sup>

## B. The Community Debt System

Arizona, New Mexico, Washington, and Wisconsin are typically categorized under the community debt system.<sup>37</sup> Under this system, determining whether a judgment creditor can attach nonexempt property owned in whole or in part by the non-liable spouse requires that the debt first be classified as a separate or community debt.<sup>38</sup> Classification of debts is determined based on whether the spouse incurring the debt was acting for the benefit of the community.<sup>39</sup> If this is the case, the

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32. See CAL. FAM. CODE ANN. § 911 (West 2004).

33. IDAHO CODE ANN. § 32-912 (LexisNexis 2006) (providing that either spouse may bind the community property by contract).

34. See *Credit Bureau of E. Idaho, Inc., v. Lecheminant*, 235 P.3d 1188, 1192–93 (Idaho 2010) (citations omitted) (explaining that community property is liable for debts of either spouse).

35. See *United States v. ITT Consumer Fin. Corp.*, 816 F.2d 487, 491 n.12 (9th Cir. 1987) (stating that in equal management community property states, including California, Louisiana, Idaho, and Nevada, debts incurred by only one spouse during marriage may be satisfied from community property and from the separate property of the liable spouse).

36. See NEV. REV. STAT. ANN. § 123.050 (LexisNexis 2007).

37. See Carroll, *supra* note 6, at 17 (stating that Arizona, New Mexico, Washington, and Wisconsin have rejected the managerial system and have instead opted for the community debt system); see also REPPY, SAMUEL & RICHARDSON, *supra* note 27, at 327.

38. See REPPY, SAMUEL & RICHARDSON, *supra* note 27, at 327 (stating that those states “require that tort and contract debts be classified as community or separate at the time the creditor seeks to be paid”).

39. See Carroll, *supra* note 6, at 17 (stating that the policy supporting the

debt is classified as a community debt, meaning that community property can be attached to satisfy a judgment obtained with respect to it.<sup>40</sup>

Case law in Arizona, New Mexico, and Washington has created a presumption that all contractual debts incurred during marriage are community debts.<sup>41</sup> Wisconsin has a statute that specifically provides for this presumption and extends to tortious obligations.<sup>42</sup> Each state requires clear and convincing evidence to overcome this presumption.<sup>43</sup> Thus, only in rare instances will a debt incurred during marriage not be classified as a community debt.<sup>44</sup> In Wisconsin, the community debt presumption can be made conclusive if the debtor unilaterally signs a statement before the obligation is incurred stating: “the obligation is or will be incurred in the interest of the marriage or the family.”<sup>45</sup> New Mexico has a statute that allows a spouse and creditor to agree, at the time a debt is incurred, that it will be classified as separate.<sup>46</sup> In Arizona, New Mexico, and Washington, where there is no presumption that tortious obligations incurred during marriage are community debts, courts have generally been willing to find that most such obligations were incurred for the benefit of the community and,

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community debt system is that community property should be held liable only for debts incurred while a spouse is acting for the benefit of the community).

40. *See id.* at 6, 17–18 (explaining that, once a debt is classified as a community debt, in all the community debt states except Wisconsin, “the entirety of the community property between husband and wife . . . could be seized to satisfy the husband’s premarital debt” (footnote omitted)).

41. *See id.* at 18 (stating that those states “employ a presumption that a contractual obligation incurred by a spouse during marriage is one for the benefit of the community, and thus is a community debt” (footnote omitted)); *see also* REPPY, SAMUEL & RICHARDSON, *supra* note 27, at 328.

42. *See* WISC. STAT. ANN. § 766.55(1) (West 2009).

43. *See* Carroll, *supra* note 6, at 18–19 (stating that the clear and convincing evidentiary standard is required to overcome the community debt presumption in every community debt state); *see also* REPPY, SAMUEL & RICHARDSON, *supra* note 27, at 328.

44. *See* REPPY, SAMUEL & RICHARDSON, *supra* note 27, at 328–29 (discussing two Washington cases in which the court held that contractual obligations incurred during marriage were not community debts).

45. WISC. STAT. ANN. § 766.55(1) (West 2009); *see also* Carroll, *supra* note 6, at 19.

46. *See* N.M. STAT. ANN. § 40-3-9(A)(4) (2016); *see also* REPPY, SAMUEL & RICHARDSON, *supra* note 27, at 329.

thus, are community obligations.<sup>47</sup>

Premarital obligations are not community debts. The obligor spouse could not have been acting for the benefit of the community when incurring the debt because the marriage did not yet exist at that time.<sup>48</sup>

After debts have been classified as either separate or community, it can then be determined which marital property is subject to attachment for those debts. The rules differ among the states using the community debt system. New Mexico provides for a statutory scheme by which community debts must be satisfied from the following property in the order stated: first, from all community property and certain other property in which the spouses own an equal interest, except for the spouses' residence; second, from the residence of the spouses except as otherwise provided; third, from the separate property of the spouse who is obligated for the debt.<sup>49</sup> Separate debts must be satisfied from the following property in the order stated: first, from the separate property of the spouse who is obligated for the debt, except for certain property in which the spouses own an equal interest; second, from the obligated spouse's one-half interest in community property and certain other property in which the spouses own an equal interest, except for the spouses' residence; third, from the obligated spouse's interest in the residence of the spouses except as otherwise provided.<sup>50</sup> Thus, in New Mexico, community debts are generally satisfied from community property and from separate property of the obligated spouse. Separate debts, including debts incurred prior to marriage, are satisfied generally from separate property of the obligated spouse and that spouse's one-half interest in community property.

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47. See REPPY, SAMUEL & RICHARDSON, *supra* note 27, at 329 (explaining that, although the burden of proof is on the tort victim/creditor to prove that the tortious activity benefited the community, courts have held that "recreation—just enjoying life—is a community activity," and the resulting tortious obligations were thus community debts).

48. See, e.g., N.M. STAT. ANN. § 40-3-9(A)(1) (2016) (specifically including debts contracted or incurred by a spouse before marriage in the definition of a separate debt).

49. See *id.* § 40-3-11(A).

50. See *id.* § 40-3-10(A).

Arizona's rules are also provided by statute and treat premarital debt in a separate category than debt incurred during marriage. Community property is liable for the premarital debts of a spouse "only to the extent of the value of that spouse's contribution to the community property which would have been such spouse's separate property if single."<sup>51</sup> Community debt incurred during the marriage must be satisfied "first, from the community property, and second, from the separate property of the spouse contracting the debt or obligation."<sup>52</sup> Separate debts can be satisfied only from the separate property of the spouse obligated for the debt.<sup>53</sup>

Wisconsin also provides for a statutory scheme. Wisconsin is similar to Arizona in the manner which it treats premarital debts, which can only be satisfied from the separate property of the spouse obligated for the debt and from that part of the community property "which would have been the property of that spouse but for the enactment of this chapter."<sup>54</sup> Wisconsin differs, however, from New Mexico and Arizona by treating tortious obligations incurred by a spouse during marriage separately from other obligations incurred during marriage. Tortious obligations incurred by a spouse during marriage may be satisfied from the separate property of that spouse and from that spouse's interest in community property.<sup>55</sup> Non-tortious community debts incurred during marriage can be satisfied from all community property and from the separate property of the liable spouse.<sup>56</sup> Non-tortious separate debts incurred during marriage can be satisfied first from the separate property of that spouse, and second from that spouse's interest in community property, in that order.<sup>57</sup>

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51. See ARIZ. REV. STAT. ANN. § 25-215(B) (West 2007).

52. *Id.* § 25-215(D)

53. See REPPY, SAMUEL & RICHARDSON, *supra* note 27, at 327–28 (citing GAF Corp. v. Diamond Carpet Corp., 572 P.2d 125 (Ariz. Ct. App. 1977)).

54. WISC. STAT. ANN. §§ 766.31, 766.55(2)(c)(2) (West 2009) (using and defining the terms *marital property* and *individual property*, which are generally considered substantially similar to *community property* and *separate property*, as those terms are used in the other eight community property states).

55. See *id.* § 766.55(2)(cm).

56. *Id.* § 766.55(2)(b).

57. See *id.* §§ 766.55(2)(d), 766.555 (providing special rules that apply to an *open-end plan*, defined to include credit cards and similar types of credit

The rules in Washington have been established mostly by case law. As in Wisconsin, Washington distinguishes tortious from non-tortious obligations and treats them differently, but in a somewhat more convoluted manner. For tortious obligations which are incurred during marriage and are classified as community debts, creditors can reach the separate property of the obligated spouse and all of the community property.<sup>58</sup> For tortious obligations incurred during marriage that are classified as separate debts, creditors can first reach the separate property of the obligated spouse and then that spouse's one-half interest in community property, in that order.<sup>59</sup> The same rule applies to tortious obligations incurred prior to marriage.<sup>60</sup> For non-tortious debts incurred prior to marriage, Washington has a statute allowing those debts to be satisfied from the earnings and accumulations of the obligated spouse if judgment is obtained within three years of the marriage.<sup>61</sup> For non-tortious debts incurred during the marriage, the rules in Washington are similar to those in Arizona. Community debts can be satisfied from community property and from the separate property of the obligated spouse.<sup>62</sup> Separate debts can be satisfied only from the separate property of the spouse obligated for the debt.<sup>63</sup>

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arrangements if certain conditions are met).

58. See *deElche v. Jacobsen*, 622 P.2d 835, 840 (Wash. 1980) (holding that torts classified as community obligations "will remain community torts with the community and the tortfeasor separately liable").

59. See *id.* (holding that, for torts not classified as community obligations, separate property of the tortfeasor will be primarily liable and, if that property is insufficient to satisfy the obligation, the tortfeasor's one-half interest in community personal property will become liable); see also *Keene v. Edie*, 935 P.2d 588, 594–95 (Wash. 1997) (holding that, for torts not classified as community obligations, the tortfeasor's one-half interest in community real property is liable after exhaustion of the tortfeasor's separate property and one-half interest in community personal property).

60. See *Haley v. Highland*, 12 P.3d 119, 127 (Wash. 2000) (holding that the rules applicable to torts not classified as community obligations apply also to torts committed prior to marriage).

61. See WASH. REV. CODE ANN. § 26.16.200 (West 2005).

62. See REPPY, SAMUEL & RICHARDSON, *supra* note 27, at 328 (stating that the rules in Arizona, New Mexico, and Wisconsin, which allows community creditors to reach both community property and the obligor spouse's separate property, is probably the rule in Washington as well, and citing authority for that proposition).

63. See *Nichols Hills Bank v. McCool*, 701 P.2d 1114 (Wash. 1985) (explaining that the rules adopted in *deElche* for separate tort obligations

### III. Liability of Spouses After Divorce in Community Property Jurisdictions for Debts Solely Incurred by the Other Spouse Prior to or During Marriage

When married couples divorce, new issues arise with respect to obligations one or both of the spouses incurred either prior to or during the marriage. Common law and community property jurisdictions alike have established rules for courts to use in dealing with those obligations in the context of the divorce and in dividing the marital property estate. One issue likely to arise in most situations is to what extent a creditor can bring an action against the spouses after the divorce to collect its debt. A general rule that prevails in all of the common law and community property states is that a divorce decree ordering one spouse to pay a debt is binding only on the spouses and not on a creditor which was not a party to the decree; the divorce decree cannot reduce any rights the creditor had prior to the divorce.<sup>64</sup> Thus, if both spouses are liable for an obligation, the creditor can, either prior to or after divorce, bring an action and obtain a personal judgment against either or both of them.<sup>65</sup>

The particular issue that will be addressed here is one that has become quite troublesome in the community property jurisdictions: namely, to what extent a creditor is allowed to

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constituted a departure from the general rule that a creditor is not allowed to reach community property to satisfy a separate debt).

64. See REPPY, SAMUEL & RICHARDSON, *supra* note 27, at 335 (discussing a general rule that a divorce decree “cannot reduce the rights of pre-divorce creditors of one spouse to reach property awarded the other if that property would have been liable absent the divorce”); see also Margaret M. Mahoney, *Debts, Divorce, and Disarray in Bankruptcy*, 73 UMKC L. REV. 83, 88 (2004) (stating the general rule that rights of a creditor established during the marriage of the debtor is not affected by the debtor’s subsequent divorce).

65. See, e.g., LA. CIV. CODE ANN. art. 2357 (West 2009) (providing that an obligation incurred by a spouse during marriage may be satisfied after divorce from separate property of that spouse); *Sunwest Bank of Albuquerque v. Roderiguez*, 770 P.2d 533, 538 (N.M. 1989) (holding that the spouses’ marriage settlement agreement pursuant to their divorce had no effect on the rights of a pre-divorce creditor who was not a party to the agreement); *Marine Midland Bank v. Monroe*, 756 P.2d 1193, 1194 (Nev. 1988) (holding that a divorce decree to which a creditor was not a party did not divest the creditor of the right to collect its debt from a spouse who was liable); *Broadway Drug Store of Galveston, Inc. v. Trowbridge*, 435 S.W.2d 268, 270 (Tex. Civ. App. 1968) (holding that a “court in a divorce action has no power to disturb the rights which creditors lawfully have against the parties”).

obtain a judgment after divorce against a spouse who is not personally liable for a debt solely incurred by the other spouse either before or during the marriage and, accordingly, to what extent such a creditor is allowed to attach nonexempt property either received by the non-labile spouse in the divorce or subsequently acquired by such spouse.<sup>66</sup> This is not an issue in common law property jurisdictions for the reasons discussed in Part II. Generally, when only one spouse is personally liable for an obligation in common law property states, a judgment creditor cannot attach property owned by the other spouse to satisfy the judgment.<sup>67</sup> Spouses in common law property jurisdictions are treated as separate persons with regard to obligations incurred by only one of them during the marriage.<sup>68</sup> The rules developed by each of the community property jurisdictions with respect to this issue are quite distinct and will be discussed separately for each jurisdiction.

#### A. Idaho

The rules in Idaho for dealing with this issue were explained by the Supreme Court of Idaho in *Twin Falls Bank & Trust Co. v. Holley*.<sup>69</sup> In that case, John Holley (“Husband”) borrowed money from Twin Falls Bank & Trust Co. (“Bank”) for use in a construction business which he operated.<sup>70</sup> On June 26, 1981,

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66. This is not a significant issue in common law property jurisdictions. *See generally* Mahoney, *supra* note 1, at 456 (explaining the post-divorce rights of creditors in common law property jurisdictions, namely that, while courts in common law property states have a certain amount of power in a divorce to allocate marital debts between the spouses, those courts have no power to modify the rights of third-party creditors with respect to the individual spouses, unless the creditors are joined as parties in the divorce proceeding. As a result, a creditor will be entitled after the divorce to proceed against whichever of the spouses is personally liable for the obligation. That is, of course, the same right the creditor has during the marriage in a common law jurisdiction.).

67. *See* Mahoney, *supra* note 1, at 449–50 (explaining that, in the forty-one common law property states, liability for unsecured debts is limited to the spouse who incurred the debt).

68. *See id.* at 445 (noting that in the common law property states, spouses retain their separate identity with regard to both debts and ownership of assets).

69. 723 P.2d 893 (Idaho 1986).

70. *Id.* at 894.

Husband borrowed additional funds from Bank and executed an unsecured promissory note, due on September 28, 1981, for the total amount owed to Bank.<sup>71</sup> Husband was married to Joan Holley (“Wife”) at the time of these events, but Wife did not execute the promissory note.<sup>72</sup> Husband and Wife were divorced on August 28, 1981, pursuant to which Husband was awarded the construction business (a community asset) and assumed liability for payment of the June 26, 1981 promissory note.<sup>73</sup> Husband did not pay that note on its September 28, 1981 due date, instead executing with Bank an agreement extending the due date of the promissory note to November 22, 1981 and granting to Bank a security interest in certain real and personal property to secure the note.<sup>74</sup> Husband was solvent at the time he executed the extension agreement, but subsequently defaulted on his obligation to Bank and filed for bankruptcy.<sup>75</sup> The Bank eventually sued Wife for non-payment of the promissory note.<sup>76</sup>

In its opinion, the Court explained “[t]his case can be resolved based on fundamental principles governing the debtor-creditor relationship.”<sup>77</sup> When a creditor obtains a judgment, he can proceed to collect his judgment by executing on the debtor’s assets. Those rules apply in the same way to married and unmarried debtors.<sup>78</sup> The only difference is that, if the debtor is married, the creditor can execute on community property owned by the debtor and his spouse as well as the debtor’s separate property.<sup>79</sup> In this case, only Husband executed the promissory note and was personally liable for the obligation to Bank.<sup>80</sup> On June 26, 1981, when Bank had a claim against Husband for unpaid obligations due at that time and Husband and Wife were still married, Bank could have brought an action against Husband and Wife, obtained a judgment, and proceeded to

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71. *Id.* at 894–95.

72. *Id.* at 895.

73. *Id.*

74. *Id.*

75. *Twin Falls Bank & Trust Co. v. Holley*, 723 P.2d 893 (Idaho 1986).

76. *Id.*

77. *Id.* at 896.

78. *Id.*

79. *Id.* at 896–97.

80. *Id.* at 897.

collect that judgment from Husband and Wife's community property and Husband's separate property.<sup>81</sup> Instead, Bank chose to have Husband execute a promissory note due September 28, 1981.<sup>82</sup> When that note became due, Husband and Wife were already divorced.<sup>83</sup> The Bank was unsuccessful in its efforts against Husband to fully satisfy Husband's obligation to Bank pursuant to the promissory note.<sup>84</sup>

The issue then became whether Bank could bring an action against Wife, who was not personally liable on the promissory note, obtain a judgment, and collect that judgment from formerly community property received in the divorce by Wife.<sup>85</sup> The Court held that "a creditor may not, with one exception, proceed against community assets distributed to [a spouse] pursuant to a divorce decree" if that spouse is not personally liable for the obligation to that creditor.<sup>86</sup> The Court cited to an earlier case, *Spokane Merchants' Ass'n v. Olmstead*,<sup>87</sup> for the exception: in a divorce, when only one spouse is personally liable for an obligation incurred during the marriage, "but is not awarded sufficient community assets to satisfy such a debt, a creditor may properly seek satisfaction for the debt from community property distributed to the other spouse."<sup>88</sup> The Court explained the purpose for the exception is to prevent spouses from utilizing "divorce proceedings to perpetrate a fraud on creditors of the community."<sup>89</sup> It held that the exception did not apply in *Twin Falls* because the trial record clearly indicated that "sufficient assets were distributed to [Husband] as part of the divorce proceedings which would have enabled him to satisfy the community obligation [to Bank] which he assumed pursuant to the property settlement agreement."<sup>90</sup> Accordingly, the Court

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81. *Twin Falls Bank & Trust Co. v. Holley*, 723 P.2d 893 (Idaho 1986).

82. *Id.* at 894–95.

83. *Id.* at 895.

84. *Id.* at 897.

85. *Id.*

86. *Id.*

87. *Twin Falls Bank & Trust Co. v. Holley*, 723 P.2d 893, 897 (Idaho 1986) (citing 327 P.2d 385 (Idaho 1958)).

88. *Id.* at 897.

89. *Id.*

90. *Id.* at 898.

held in favor of Wife.<sup>91</sup>

The rules in Idaho with respect to this issue are very restrictive with regard to rights of creditors. A creditor who extends credit for which only one spouse is personally liable will potentially have fewer rights to execute on property in a collection action if its debtor spouse is divorced before the creditor brings its action. Any community property that would be available to the creditor for execution during the marriage will not be available if distributed to the non-liable spouse in the divorce, subject to the exception stated in *Twin Falls*.

#### B. California

The rules in California with respect to this issue are provided by statute and are potentially very restrictive as to rights of creditors. The basic premise underlying the statute is that debts owed by the spouses at the time of divorce will be assigned for payment to one of the spouses as part of the division of property in the divorce.<sup>92</sup> The statute provides that such assignment cannot relieve a spouse of personal liability for a debt for which such spouse is personally liable at the time of the divorce.<sup>93</sup> Thus, if both spouses are personally liable for a debt, they will remain personally liable after the divorce, regardless of which spouse was assigned the debt for payment. Likewise, if only one spouse is personally liable for a debt and the debt is assigned to the other spouse, the liable spouse will remain personally liable after the divorce. When a debt for which only one spouse is personally liable is assigned to the non-liable spouse, the effect is to make that non-liable spouse personally liable for the debt;<sup>94</sup> but if that debt is not assigned to the non-liable spouse, none of that spouse's separate property owned at the time of divorce or community property received by that

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91. *Id.*

92. *See* CAL. FAM. CODE § 916(a) (West 2004) (providing that debts be assigned for payment to one of the spouses in a divorce).

93. *Id.* § 916(a)(1) (providing that a spouse remains personally liable for a debt incurred by that spouse before or during marriage regardless of whether the debt was assigned to the other spouse in the divorce).

94. *Id.* § 916(a)(3) (providing that a spouse to whom a debt, incurred by the other spouse before or during marriage, is assigned for payment in the divorce is personally liable for such debt).

spouse in the divorce is liable for that debt, and that spouse has no personal liability for that debt.<sup>95</sup>

Because debts are normally assigned under these provisions to the spouse who is personally liable for the debt, these rules usually have the effect of substantially restricting the rights of creditors subsequent to the divorce.<sup>96</sup> Consistent with Idaho, a creditor who extends credit for which only one spouse is personally liable will potentially have fewer rights to execute on property in a collection action if its debtor-spouse is divorced before the creditor brings its action. Any community property that would be available to the creditor for execution during the marriage will not be available if it is distributed to the non-liable spouse in the divorce and if such non-liable spouse is not assigned the debt for payment. However, if the non-liable spouse is assigned the debt for payment in the divorce, the creditor's rights will actually be increased after the divorce because assignment of the debt to the non-liable spouse will make that spouse personally liable for the debt. The creditor could then execute on separate property of the non-liable spouse, including property acquired by such spouse after the divorce, which the creditor would not have been entitled to do had there been no divorce.<sup>97</sup>

These statutory provisions have been criticized for enabling spouses to agree to the terms of their divorce and utilize strategies that detrimentally affect their creditors.<sup>98</sup> For

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95. *Id.* § 916(a)(2) (providing that a spouse is not liable for a debt incurred by the other spouse before or during marriage unless that debt was assigned for payment to such spouse in the divorce).

96. *See* REPPY, SAMUEL & RICHARDSON, *supra* note 27, at 336 (stating that “in the usual situation where the debt is assigned to the debtor-spouse, divorce will often relegate the creditor of the debtor-spouse to half of the community property he could have reached before the divorce”); *see also* Mejia v. Reed, 74 P.3d 166, 171 (Cal. 2003) (stating that the legislature, in enacting the predecessor statute to Section 916 of the California Family Code, determined that, in most circumstances, after a divorce, it is unwise to continue the liability of spouses for community debts incurred by the other spouse).

97. *See supra* notes 2–3 and accompanying text (explaining that, in the community property jurisdictions, a judgment creditor cannot attach separate property owned by a spouse to satisfy a judgment with respect to an obligation for which only the other spouse is personally liable).

98. *See* Ratner, *supra*, note 8, at 212–13 (describing how the rules in California allowing married couples to decide the manner in which their debts will be assigned has the potential for detrimentally affecting the rights of their

example, assume that only husband is personally liable for all the debts incurred during the marriage; the couple could strategically divorce and assign all the debts to husband and agree that wife will receive all the community property. Husband will have no assets which the creditors can attach after the divorce. California courts have responded to these concerns by identifying an important exception to the statutory provisions for situations in which blind application of the statutory rules would result in substantial unfairness to the rights of creditors.<sup>99</sup> In *Mejia v. Reed*,<sup>100</sup> a husband (“Husband”) had an extramarital relationship, resulting in the birth of a child, and was subsequently ordered to pay child support to the child’s mother (“Creditor”).<sup>101</sup> The Husband and his wife later divorced, the terms of which they memorialized in a marital settlement agreement (“MSA”).<sup>102</sup> The MSA required Husband to transfer all of his interest in jointly owned real property to wife.<sup>103</sup> The property received by husband pursuant to the MSA ultimately proved to be worthless, and husband was subsequently left with no assets and little income with which to pay the child support obligation.<sup>104</sup> Creditor filed an action asserting that the transfer of husband’s interest in the real property to wife under the MSA constituted a fraudulent transfer and requested that a lien be imposed upon the property pursuant to California fraudulent transfer law.<sup>105</sup> In this case of first impression in California, the Court addressed the issue of whether the Uniform Fraudulent Transfer Act (“UFTA”), as adopted by California, applies to transfers of property in a divorce under California Family Code Section 916.<sup>106</sup> The Court was forced to apply established rules of statutory construction to resolve that issue and noted that

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creditors).

99. See REPPY, SAMUEL & RICHARDSON, *supra* note 27, at 336 (discussing situations in which California courts have held that a creditor is not bound by the property division in a divorce).

100. See generally 74 P.3d at 166–176.

101. *Id.* at 169.

102. *Id.*

103. *Id.*

104. *Id.*

105. *Id.*

106. *Mejia v. Reed*, 74 P.3d 166, 169 (Cal. 2003).

neither statute expressly refers to the other.<sup>107</sup> After evaluating the two separate statutory schemes and addressing issues of public policy, the Court determined that the UFTA did, in fact, apply to property transfers in divorce pursuant to marital settlement agreements.<sup>108</sup> The Court then applied the UFTA to the case at bar and determined that whether Husband engaged in actual fraud with regard to the transfer of his interest in the real property to his wife under the MSA was “a triable issue for decision by the trial court,” and accordingly remanded the case for further proceedings.<sup>109</sup>

### C. Louisiana

The rules in Louisiana with respect to this issue are provided by statute. The general rule is mostly neutral with respect to creditors, providing that “[a]n obligation incurred by a spouse before or during the community property regime may be satisfied after termination of the regime from the property of the former community and from the separate property of the spouse who incurred the obligation.”<sup>110</sup> Thus, the general rule extends the rules for liability of marital property for debts incurred prior to or during marriage to the period after divorce.<sup>111</sup> Because creditors can reach the same property after divorce and during the marriage, their rights are typically neither reduced nor enhanced as a result of a divorce. In

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107. *Id.*

108. *Id.* at 170–74 (quoting *Lezine v. Sec. Pac. Fin. Servs., Inc.*, 925 P.2d 1002, 1013 (Cal. 1996)) (explaining that the Court noted California legislative policy requires a court to allocate debts to spouses in a divorce to account for the rights of creditors “so there will be available sufficient property to satisfy the debt by the person to whom the debt is assigned”). In limiting its decision to property transfers pursuant to marital settlement agreements, the Court noted that “when the court divides the marital property in the absence of an agreement by the parties, it must divide the property equally . . . which provides some protection for a creditor of one spouse only.” *Id.* at 173.

109. *Id.* at 174–76.

110. LA. CIV. CODE ANN. art. 2357 (West 2009).

111. *See id.* art. 2345 (providing that a separate or community obligation may be satisfied from community property); *see also supra* notes 2–3 and accompanying text (explaining that, in the community property jurisdictions, a judgment creditor cannot attach separate property owned by a spouse to satisfy a judgment with respect to an obligation for which only the other spouse is personally liable).

addition, the statute provides that “[i]f a spouse disposes of property of the former community for a purpose other than the satisfaction of community obligations, he is liable for all obligations incurred by the other spouse up to the value of that community property.”<sup>112</sup> The term *community obligation* is defined for purposes of this statute as “[a]n obligation incurred by a spouse during the existence of a community property regime for the common interest of the spouses or for the interest of the other spouse.”<sup>113</sup> A spouse can avoid the liability imposed under this statute for disposing of former community property after divorce by assuming, in writing, “responsibility for one-half of each community obligation incurred by the other spouse.”<sup>114</sup>

#### D. Texas

The rules in Texas with respect to this issue have been provided by a majority of the intermediate courts of appeal; the Supreme Court of Texas has not ruled directly on the issue.<sup>115</sup> The existence of the rules provided by the courts of appeal, however, appear to be universally accepted by “respected academicians, continuing legal education speakers, practice guides, and popular bar review outlines.”<sup>116</sup> The general rule is the same as that in Louisiana: unsecured creditors of a spouse are allowed to attach the same property after divorce as they could have attached during the marriage.<sup>117</sup>

The principal decision cited as authority for this rule is *Stewart Title Co. v. Huddleston*,<sup>118</sup> decided by the San Antonio

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112. *Id.* art. 2357.

113. *Id.* art. 2360.

114. *Id.* art. 2357.

115. See Paulsen, *supra* note 9, at 794–810.

116. *Id.* at 794–96 (citations omitted); but see Joseph W. McKnight, *Commentary to Family Code § 5.61*, 21 TEX. TECH. L. REV. 1108, 1110 (1990) (soundly criticizing the rationale for these rules); Paulsen, *supra* note 9, at 815–49 (same).

117. See Paulsen, *supra* note 9, at 794–810 (explaining that “the idea that one spouse’s unsecured creditors can reach the same assets after divorce as those creditors could reach beforehand” has wide support in Texas, and referring to an outstanding and exhaustive discussion of case law underlying and explaining the development of this rule in Texas).

118. 598 S.W.2d 321 (Tex. App. 1980), *writ refused NRE per curiam*, 608 S.W.2d 611 (Tex. 1980).

Court of Appeals. The Court stated that, as a general rule, “a spouse who receives property [in a divorce] which would, absent a divorce, be subject to the claims of creditors remains personally liable, and the property so received remains subject to being taken to satisfy the claims of the community creditors.”<sup>119</sup> Thus, if a spouse not personally liable for a debt owed to a creditor receives property in the divorce that could have been attached by that creditor during the marriage, the creditor is allowed to bring a collections proceeding after divorce to attach that property. That is true even though the spouse who received that property in the divorce is not personally liable for the debt to that creditor.<sup>120</sup> An illustration provided in a previous article published by this author is as follows:

To illustrate, Husband (H) incurs a debt to Creditor (C), for which only H is personally liable. H and Wife (W) own nonexempt land that is subject to the joint management and control of both H and W. H defaults on his debt to C, and C sues H and obtains a judgment. Under the marital property liability rules discussed above, C may attach the land to satisfy the judgment. If, before C either acquires his judgment or attaches the land, H and W are divorced, and W receives the land in the divorce, C may obtain a judgment against W and attach the land, notwithstanding that W has no personal liability to C with respect to the debt. W, however, will have no personal liability with respect to the judgment. The judgment will be ‘in rem’ with respect to the land,

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119. *Id.* at 323 (citations omitted).

120. *See* Musselman, *supra* note 11, at 260 (explaining the circumstances pursuant to which a creditor can bring a collection action post-divorce against a spouse who is not personally liable for the debt owed to that creditor). The right to bring that action by the creditor does not create personal liability for the non-liable spouse receiving the property in the divorce; it is only the property that is liable for the debt. *See id.* (citing *State Farm Lloyds, Inc. v. Williams*, 791 S.W.2d 542 (Tex. App., 1990) *writ denied*, 791 S.W.2d 542 (Tex. App. 1990)) (stating that the creditor can obtain only an “in rem’ judgment against the property as opposed to a personal judgment against the spouse who received that property in the divorce”).

meaning that its sole effect will be to allow C to attach the land to satisfy the judgment.<sup>121</sup>

Thus, the rules in Texas regarding this issue are mostly neutral with respect to creditors. Because creditors can reach the same property after divorce that they can reach during the marriage, their rights are typically neither reduced nor enhanced as a result of a divorce.<sup>122</sup>

#### E. Washington

The rules in Washington for dealing with this issue were explained by the Supreme Court of Washington in *Watters v. Doud*.<sup>123</sup> In that case, Charles Doud (“Husband”), during his marriage to Judith Doud (“Wife”), executed a promissory note payable to Harry Watters (“Creditor”) to evidence a debt in the approximate amount of \$15,000.<sup>124</sup> Husband and Wife subsequently divorced; the property settlement provided that Husband would pay the debt to Creditor and that the community home would be transferred to Wife.<sup>125</sup> Husband eventually defaulted on the debt to Creditor, and Creditor acquired a judgment and attempted to satisfy it by executing on the community home received by Wife in the divorce.<sup>126</sup>

The first issue addressed by the Court—and the only issue relevant here—was “whether after a marriage dissolution, previously community held assets are fully available, including their post-divorce appreciated value, to satisfy debts incurred by the former marital community.”<sup>127</sup> The Court cited to its previous decisions holding that “separate property contributions to an asset previously owned by the marital community, and which were made after the divorce, are not subject to preexisting

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121. *Id.*

122. *But see* Paulsen, *supra* note 9, at 841–42 (describing a situation in which a creditor’s position could be enhanced as a result of a divorce).

123. *See generally* 631 P.2d 369 (Wash. 1981) (en banc).

124. *Id.* at 370.

125. *Id.*

126. *Id.*

127. *Id.*

community debts.”<sup>128</sup> The Court stated that previous cases had held only that property “formerly owned by the community can be levied upon for the community’s debts,”<sup>129</sup> and that the issue regarding post-divorce appreciation in value was one of first impression in Washington.<sup>130</sup> The Court decided the issue by adopting the rule prevailing at that time in California;<sup>131</sup> namely, that “since all property becomes separate upon divorce, all net equity arising thereafter must be separate in character and thus is unavailable to community creditors.”<sup>132</sup> The Court explained that it was adopting that rule because it “is preferable on the basis of equity and generally applicable community property principles,”<sup>133</sup> noting that “[o]ur cases have also exempted separate property and its appreciation from the claims of community creditors.”<sup>134</sup> The Court further justified its decision by explaining that “[c]reditors are adequately protected without making post-divorce equity available to them” because they are permitted “to execute upon formerly community held assets to the extent of the community’s net equity [at the time of divorce].”<sup>135</sup> The Court also noted that creditors have other traditional remedies available to them, such as having “a property settlement agreement set aside by proving the divorce was an attempt to defraud them.”<sup>136</sup>

The rules with respect to this issue are thus somewhat more limited in Washington with regard to the rights of creditors than those in Louisiana and Texas. Creditors in Louisiana and Texas are permitted to attach the same property after divorce that they can during marriage to the full extent of the value of that property at the time of attachment, including any post-divorce appreciation in the value of such property. Creditors in Washington are allowed to attach all property that was formerly part of the community property estate, but only to the extent of the net equity in such property at the time of the divorce.

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128. *Id.*

129. *Watters v. Doud*, 631 P.2d 369, 371 (Wash. 1981) (en banc).

130. *Id.* at 370–71.

131. *Id.* at 371.

132. *Id.* at 370.

133. *Id.* at 371.

134. *Id.*

135. *Watters v. Doud*, 631 P.2d 369, 371 (Wash. 1981) (en banc).

136. *Id.*

## F. Wisconsin

The rules in Wisconsin with respect to this issue are provided by statute. The basic rule is similar to that in Washington: creditors are allowed to attach all property that was formerly part of the community property estate, but only to the extent of the value of such property at the time of the divorce.<sup>137</sup> However, creditors in Wisconsin are provided additional rights post-divorce that are substantially greater than Washington creditors could ever receive. First, the divorce decree may provide that income of a spouse be available after the divorce to satisfy a community debt for which only the other spouse is personally liable; absent such a provision, no such income of the non-liable spouse is available for satisfaction of such a debt.<sup>138</sup> Second, the divorce decree may provide for the imposition of personal liability on a spouse after the divorce for a community debt for which only the other spouse is personally liable.<sup>139</sup>

Thus, creditors in Wisconsin are afforded the same rights as creditors in Washington under the basic rule. If a Wisconsin creditor is provided the right to reach post-divorce income of a non-liable spouse to satisfy a community debt, that creditor is treated similar to creditors in Texas and Louisiana with respect to that particular debt. As discussed earlier, community debts in Wisconsin can be satisfied during marriage from community property, so allowing a creditor to satisfy its obligation from post-divorce income of the non-liable spouse constitutes a limited extension of that creditor's rights during the marriage to the period after divorce. If, however, the divorce decree also provides for the imposition of personal liability for a community debt on a non-liable spouse, that creditor's rights will be significantly enhanced simply because of the divorce, and the creditor will consequently receive a windfall. The creditor will now be entitled to file an action against the previously non-liable spouse and obtain a judgment that is enforceable, not only against community property received in the divorce, but also

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137. See WISC. STAT. ANN. § 766.55(2m) (West 2009).

138. *Id.*

139. *Id.*

against that spouse's separate property owned during the marriage and any property that spouse acquires after the divorce.

#### G. Arizona

Arizona has a statutory scheme providing for the treatment of debts in a divorce proceeding,<sup>140</sup> but that scheme does not specifically resolve this issue.<sup>141</sup> The rules in Arizona with respect to this issue have been provided by the intermediate courts of appeal; the Supreme Court of Arizona has not ruled directly on the issue. In *Community Guardian Bank v. Hamlin*,<sup>142</sup> Jerry Hamlin ("Husband") was solely liable for an obligation to Community Guardian Bank ("Bank").<sup>143</sup> Bank brought an action against both Husband and Janice Hamlin ("Wife") alleging several counts, including unjust enrichment.<sup>144</sup> A default judgment was obtained against Wife on the unjust enrichment count.<sup>145</sup> Bank served a writ of garnishment against Wife's employer, and Husband and Wife subsequently divorced.<sup>146</sup> Wife then moved to quash the writ of garnishment.<sup>147</sup> Wife argued that Bank was not entitled to

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140. See generally ARIZ. REV. STAT. ANN. § 25-318 (West 2007).

141. See Ratner, *supra* note 8, at 215 (referring to the statutory scheme as a "creditors bill of rights" with regard to divorce proceedings); see also ARIZ. REV. STAT. ANN. §§ 25-318(E)(2), (H), (J), (L), (West 2007) (providing that a court may require parties to submit a proposed debt distribution plan which, *inter alia*, states how community creditors will be paid. Additionally, courts are required to reflect, in its orders, the debt distribution plan that it approves. The statute also authorizes a court to impose liens on the separate property of a spouse or on the community property a spouse receives in the divorce to secure the payment of community debts that the court orders that spouse to pay. It does not specify whether that lien would be imposed in favor of the creditor or the other spouse. The statute makes clear, however, that the assignment of community debts to one spouse or the other for payment is binding on the spouses only and not on any creditors. Thus, any such lien would apparently be in favor of the other spouse only). This statutory scheme does not specifically resolve the issue regarding the rights of creditors after divorce with respect to a debt for which only one spouse is liable.

142. See generally 898 P.2d 1005 (Ariz. Ct. App. 1995).

143. *Id.* at 1007.

144. *Id.*

145. *Id.*

146. *Id.*

147. *Id.*

garnish her post-divorce wages because she was not personally liable to Bank for the obligation.<sup>148</sup> The Court first determined that the default judgment against Wife was a community obligation because Bank alleged in its complaint that the obligation was created on behalf of and for the benefit of the community estate.<sup>149</sup> The Court then discussed Arizona law regarding the obligations of spouses after divorce for community debts.<sup>150</sup> The Court stated that “[a] divorce court has the statutory power to divide the community assets and obligations. . . . However, the court’s allocation of community obligations does not affect the rights of third party creditors.”<sup>151</sup> The Court was not at all concerned with how the obligation to Bank was allocated in the divorce; its only concern was that the judgment created a community debt.<sup>152</sup> The Court then stated that the issue of whether a spouse is liable after divorce for community debts is “quite clear in Arizona: both former spouses remain jointly liable for community obligations after divorce.”<sup>153</sup> The Court then held that Wife was personally liable after the divorce for the obligation to Bank, and Bank was thus entitled to garnish her post-divorce wages to satisfy the judgment.<sup>154</sup>

Creditors in Arizona are thus afforded greater rights than creditors in any other state with regard to liability of spouses after divorce for debts incurred during the marriage. Spouses are personally liable after divorce for all community debts. Creditor’s rights in Arizona are significantly enhanced simply because of the divorce, and the creditor will consequently receive a windfall. The creditor will now be entitled to file an action against the previously non-liable spouse and obtain a judgment enforceable not only against community property that spouse

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148. *Cnty. Guardian Bank v. Hamlin*, 898 P.2d 1005, 1008 (Ariz. Ct. App. 1995).

149. *Id.* at 1009.

150. *Id.*

151. *Id.* (citations omitted).

152. *Id.*

153. *Id.*

154. *Cnty. Guardian Bank v. Hamlin*, 898 P.2d 1005, 1009 (Ariz. Ct. App. 1995); *see also In Re Oliphant*, 221 B.R. 506, 509 (D. Ariz. 1998) (citing *Cnty. Guardian Bank*, 898 P.2d at 1009) (interpreting Arizona law and holding that, after divorce, “each former spouse remains individually liable to creditors of the former community”).

receives in the divorce, but also against that spouse's separate property owned during the marriage and any property that spouse acquires after the divorce.<sup>155</sup>

#### H. New Mexico and Nevada

Case law in New Mexico and Nevada is consistent with the generally prevailing rule in all of the common law and community property states, as follows: a divorce decree ordering one spouse to pay a debt is binding only on the spouses and not on a creditor who was not a party to the decree; the divorce decree cannot reduce any rights the creditor had prior to the divorce.<sup>156</sup> Thus, if both spouses are liable for an obligation, the creditor can, either prior to or after the divorce, bring an action and obtain a personal judgment against either or both of them.<sup>157</sup> No statutory or case law exists, however, in either state dealing with the issue regarding liability of spouses after divorce for debts incurred during the marriage by only one spouse.<sup>158</sup>

### IV. Debtor-Creditor Law and Other Policy Considerations

#### A. General

The law of debtors and creditors in the United States has developed over the years into an intricate system that attempts to balance the rights and interests of each of the parties. Some aspects of this legal system favor debtors and other aspects favor

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155. See Ratner, *supra* note 8, at 218–23 (discussing and criticizing the “windfall” that creditors receive under Arizona law when their married debtor divorces his spouse.).

156. See *supra* note 63 and accompanying text.

157. See *Sunwest Bank of Albuquerque v. Roderiguez*, 770 P.2d 533, 538 (N.M. 1989) (holding that the spouses' marriage settlement agreement pursuant to their divorce had no effect on the rights of a pre-divorce creditor who was not a party to the agreement); *Marine Midland Bank v. Monroe*, 756 P.2d 1193, 1194 (Nev. 1988) (holding that a divorce decree to which a creditor was not a party did not divest the creditor of the right to collect its debt from a spouse who was liable).

158. See Paulsen, *supra* note 9, at 811 n.179 (citing to sources and concluding that no statutory or case law exists in New Mexico or Nevada dealing with that issue).

creditors. Creditors have a general expectation that the law will entitle them to be paid according to the terms of their bargain or the rule of law which gave rise to the debt they are owed. Creditors generally have the right in all jurisdictions to bring a legal cause of action and obtain a judgment against a debtor who is personally liable for an obligation to a creditor and has defaulted on payment of such obligation. If the debtor subsequently declines to pay the judgment, the creditor has a range of post-judgment remedies available against the debtor, such as execution on the debtor's assets as necessary to satisfy the judgment.

Debtors are not left without protection in the collection process. Various federal and state laws have been enacted to protect debtors from overreaching and engaging in abusive tactics in attempts to collect debts. Examples of federal law include the Fair Credit Reporting Act<sup>159</sup> and the Fair Debt Collection Practices Act.<sup>160</sup> Many states have enacted their own versions of those laws, as well as deceptive trade practices and other consumer protection legislation.<sup>161</sup>

All jurisdictions have enacted exemption laws to protect certain property of a debtor from the execution process with respect to a judgment. The basic purpose of exemption laws is that creditors cannot "leave the debtor with so little property that the debtor and the debtor's family will become a charge on the community."<sup>162</sup> However, the exemption laws enacted by the various states display a wide range of protection granted to debtors, with some states affording debtors very minimal protection, while others are quite generous with regard to the amount of property that debtors can exempt. Texas is a prime example of a state that affords substantial protection to debtors through its homestead exemption with no dollar limit and its generous protection of a wide range of personal property.<sup>163</sup>

Undoubtedly, the greatest protection afforded to debtors in

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159. 15 U.S.C. § 1681 *et seq.* (2009).

160. *Id.* at § 1692 *et seq.* (2009).

161. *See, e.g.*, TEX. BUS. & COM. CODE ANN. §§ 17.01-17.926 (West 2011).

162. ELIZABETH WARREN & JAY LAWRENCE WESTBROOK, *THE LAW OF DEBTORS AND CREDITORS: TEXT, CASES AND PROBLEMS* 79 (7th ed. Wolters Kluwer Law & Bus. 2014).

163. *See* TEX. PROP. CODE ANN. § 41.001 *et seq.* (West 2006).

the collection process is the federal bankruptcy law.<sup>164</sup> Individual debtors filing for bankruptcy protection generally have a choice between a liquidation or reorganization proceeding.<sup>165</sup> Liquidation involves disposition of all the debtor's nonexempt assets by a trustee appointed to represent the bankruptcy estate and distribution of the proceeds to creditors.<sup>166</sup> In a reorganization bankruptcy, the debtor retains all assets and proposes a plan to the court regarding payment of some portion of his debts over a period of time.<sup>167</sup> In both types of proceedings, however, any debts remaining unpaid at the end of the case are discharged,<sup>168</sup> and a permanent injunction is imposed preventing collection of those debts in the future.<sup>169</sup>

## B. Fraudulent Transfer Law

### 1. History

For as long as there have existed debtors and creditors, debtors have attempted at times to avoid paying their debts. A common avoidance technique has been to transfer nonexempt assets to friends and family members to prevent creditors from executing on those assets to satisfy a judgment. The law has long attempted to prevent debtors from engaging in such transfers for the purpose of defrauding their creditors. Fraudulent transfer doctrines developed under Roman law, which were used as a basis for English common law as early as 1571 in Elizabethan England.<sup>170</sup> The English common law then served as the basis for American fraudulent transfer doctrine.<sup>171</sup>

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164. See 11 U.S.C. §§ 101–1532 (2016).

165. See generally *id.* §§ 701–84 (governing liquidation bankruptcy); *id.* §§ 1301–30 (governing reorganization bankruptcies for individual debtors.).

166. See generally *id.* §§ 701–84.

167. See generally *id.* §§ 1301–30.

168. See generally *id.* § 727, 1328.

169. See generally *id.* § 524.

170. See Kenneth C. Kettering, *The Uniform Voidable Transactions Act; or, the 2014 Amendments to the Uniform Fraudulent Transfer Act*, 70 BUS. LAW. 777, 778 (2015) (explaining that fraudulent transfer “was elaborately developed in Roman law, and English common law borrowed from that source”).

171. See *id.* (stating that “the English Statute of 13 Elizabeth,” enacted

All jurisdictions in the United States have enacted fraudulent transfer laws. The first important codification of fraudulent transfer law in America was the Uniform Fraudulent Conveyance Act (“UFCA”), which was promulgated by the National Conference of Commissioners on Uniform State Laws (“NCCUSL”) in 1918, and which remains current law in Maryland and New York.<sup>172</sup> In 1984, NCCUSL modernized and updated the uniform law by promulgating the Uniform Fraudulent Transfer Act (“UFTA”).<sup>173</sup> As of 2014, the UFTA had been enacted in forty-five jurisdictions and is currently the prevailing fraudulent transfer law in the United States.<sup>174</sup> Five other jurisdictions have enacted fraudulent transfer laws other than the UFCA and the UFTA.<sup>175</sup> In 2014, NCCUSL promulgated amendments to the UFTA, renaming the UFTA as the Uniform Voidable Transactions Act (“UVTA”).<sup>176</sup> These amendments were relatively minor in nature.<sup>177</sup> Because the UFTA currently remains as the prevailing fraudulent transfer in the United States, it will be used for purposes of discussion and analysis of the issues discussed in this Article.

## 2. General Description of UFTA

The basic purpose of the UFTA is to provide a cause of action and specific remedies to creditors when debtors make certain transfers of property that are defined under the UFTA as fraudulent.<sup>178</sup> Those remedies include avoidance of the transfer to the extent necessary to satisfy the creditor’s claim;<sup>179</sup>

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in 1571, “is traditionally referred to as the fountainhead of American law on the subject” (citation omitted)).

172. *See id.* at 779.

173. *See id.*

174. *See id.* at n.11 (noting that these forty-five jurisdictions include forty-three states, the District of Columbia, and the U.S. Virgin Islands).

175. *See id.* (listing these states as Alaska, Kentucky, Louisiana, South Carolina, and Virginia).

176. *See Kettering, supra*, note 170, at 779.

177. *See id.* at 779–80 (stating that “the substantive changes made by the amendments, though significant enough to warrant attention, are . . . light”).

178. *See* Unif. Fraudulent Transfer Act §§ 7, 8 (1984).

179. *See id.* § 7(a)(1).

attachment against the property transferred;<sup>180</sup> execution by levy on the property transferred if the creditor has obtained a judgment against the debtor and the court so orders; and recovery of a judgment against certain transferees for the value of the property transferred.<sup>181</sup>

A *transfer* is defined as “every mode, direct or indirect, absolute or conditional, voluntary or involuntary, of disposing of or parting with an asset or an interest in an asset, and includes payment of money, release, lease, and creation of a lien or other encumbrance.”<sup>182</sup> An *asset* is defined as property of a debtor, but does not include:

- (i) [P]roperty to the extent it is encumbered by a valid lien; (ii) property to the extent it is generally exempt under nonbankruptcy law; or (iii) an interest in property held in tenancy by the entirety to the extent it is not subject to process by a creditor holding a claim against only one tenant.<sup>183</sup>

*Property* is defined as “anything that may be the subject of ownership.”<sup>184</sup> A transfer is *fraudulent* as to a creditor if it is described in either Section 4 or Section 5 of the UFTA.<sup>185</sup> Section 4 applies “whether the creditor’s claim arose before or after the transfer was made,” and makes the transfer fraudulent if the debtor made the transfer:

- (1) [w]ith actual intent to hinder, delay, or defraud any creditor of the debtor; or (2) [w]ithout receiving a reasonably equivalent value in exchange for the transfer or obligation, and the debtor: (i) [w]as engaged or was about to engage in a business or a transaction for which the remaining assets of the debtor were unreasonably

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180. *Id.* § 7(a)(2).

181. *See id.* § 8(b).

182. *Id.* § 1(12).

183. *Id.* § 1(2).

184. Unif. Fraudulent Transfer Act § 1(10) (1984).

185. *See id.* §§ 4, 5.

small in relation to the business or transaction; or  
(ii) [i]ntended to incur, or believed or reasonably  
should have believed, that he [or she] would incur,  
debts beyond his [or her] ability to pay as they  
became due.<sup>186</sup>

Section 4(b) provides a list of factors that may be considered in determining *actual intent* under Section 4(a)(1).

Section 5 applies only to creditors “whose claim arose before the transfer was made.”<sup>187</sup> Section 5(a) makes the transfer fraudulent “if the debtor made the transfer . . . without receiving a reasonably equivalent value in exchange for the transfer or obligation and the debtor was insolvent at that time or the debtor became insolvent as a result of the transfer or obligation.”<sup>188</sup> A debtor is *insolvent* by definition “if the sum of the debtor’s debts is greater than all of the debtor’s assets at a fair valuation.”<sup>189</sup> For purposes of determining whether a debtor is insolvent, assets that have been “transferred, concealed, or removed with intent to hinder, delay, or defraud creditors or that [have] been transferred in a manner making the transfer voidable under this [Act]” are not included in the calculation.<sup>190</sup> Also not included in the calculation are debts “to the extent [they are] secured by a valid lien on property of the debtor.”<sup>191</sup> A debtor “who is generally not paying his [or her] debts as they become due is presumed to be insolvent.”<sup>192</sup>

The term *reasonably equivalent value* is not defined in the UFTA. Section 3(b), however, provides a safe harbor for certain transfers, stating that:

[A] person gives a reasonably equivalent value if  
the person acquires an interest of the debtor in an  
asset pursuant to a regularly conducted,

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186. *Id.* § 4(a).

187. *Id.* § 5(a).

188. *Id.* § 5(a), (b) (making fraudulent certain preferential transfers to creditors).

189. *Id.* § 2(a).

190. Unif. Fraudulent Transfer Act § 2(d) (1984).

191. *Id.* § 2(e).

192. *Id.* § 2(b).

noncollusive foreclosure sale or execution of a power of sale for the acquisition or disposition of the interest of the debtor upon default under a mortgage, deed of trust, or security agreement.<sup>193</sup>

The UFTA applies to a division of property in a divorce only if such a division constitutes a *transfer* of an *asset*, as those terms are defined in the UFTA. Transfers of assets routinely occur in a divorce in common law property jurisdictions, because all property owned at divorce is the property of one of the spouses, or both spouses if it is jointly owned. Division of the marital property necessarily requires the parties or the court to transfer property interests from one spouse to the other. In community property jurisdictions, it is the community property estate that is divided upon divorce. In all community property jurisdictions, the spouses are treated as co-owners of the community property owned during marriage; the spouses' interests in community property are, at least in some respects, similar to a tenancy in common.<sup>194</sup> Division of community property at divorce effectuates a partition of the spouses' co-ownership interests in the property.<sup>195</sup> As a consequence, division of community property at divorce, as in common law property jurisdictions, necessarily requires the parties or the court to transfer property interests from one spouse to the other.

It is not difficult to imagine circumstances in which divorcing spouses who voluntarily divide their marital property pursuant to a property settlement agreement could do so with actual intent to hinder, delay, or defraud a creditor, and thus run afoul of Section 4(a)(1) of the UFTA.<sup>196</sup> In any situation

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193. *Id.* § 3(b).

194. *See generally* REPPY, SAMUEL & RICHARDSON, *supra* note 27, at 18 (stating that the “equality of the interests of spouses is a fundamental principle of community property law which all community property jurisdictions now recognize”). The analogy of community property ownership to a tenancy in common is not entirely accurate, but the conceptual relationship is clearly present. *Id.* at 22 (stating “[s]ome of the rules applicable to co-ownership between unmarried persons do not apply to community co-ownership”).

195. *See generally id.* at 350–53 (discussing the methodologies adopted by the various community property jurisdictions for dividing the community property estate, and the effect of such a division as a partition of the community property).

196. *See* Unif. Fraudulent Transfer Act § 4(a)(1) (1984).

where one spouse is solely liable for a large debt, the spouses could obtain a collusive divorce for the purpose of awarding the nonexempt assets to the non-debtor spouse, thereby preventing the creditor from attaching those assets to satisfy a judgment against the debtor spouse. It is extremely difficult to imagine how that could occur in cases where the trial court divides the marital property at the conclusion of a contested trial. The constructive fraud provisions of the UFTA in Sections 4(a)(2)<sup>197</sup> and 5,<sup>198</sup> however, could result in a division of property being treated as a fraudulent transfer in either situation. A determining factor pursuant to those sections would be whether the debtor spouse received a *reasonably equivalent value* in exchange for the property awarded to the non-debtor spouse. Again, it is easy to imagine how that could occur when the divorcing spouses voluntarily divide their marital property pursuant to a property settlement agreement; however, it could also easily occur in situations where the trial court divides the marital property in jurisdictions that do not require an equal division of marital property in a divorce.<sup>199</sup>

In Texas, for example, the trial court is required to divide the community property estate in a manner that the court deems just and right.<sup>200</sup> The trial court is given extremely wide discretion in making that division, and has made it clear that the division is not required to be equal.<sup>201</sup> There are a large range of factors that the court is allowed to consider in exercising its discretion, including fault in the breakup of the marriage, disparity in earning capacity, and many others.<sup>202</sup> In cases where one spouse has engaged in particularly egregious behavior during the marriage that led to the divorce, courts have awarded very large portions of the community property to the

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197. *See id.* § 4(a)(2).

198. *See id.* § 5.

199. *See generally* REPPY, SAMUEL & RICHARDSON, *supra* note 27, at 350–51 (describing rules in the community property jurisdictions for dividing community property at divorce and noting that some community property jurisdictions require an equal division of community property at divorce while others do not).

200. *See* TEX. FAM. CODE ANN. § 7.001 (West 2006).

201. *See* Murff v. Murff, 615 S.W.2d 696, 698–99 (Tex. 1981).

202. *Id.*

aggrieved spouse.<sup>203</sup> Division of the community property estate in these cases has often resulted in the spouse awarded little or no community property in the divorce receiving less than *reasonably equivalent value* for the community property transferred to the aggrieved spouse. Assuming that spouse has debts that existed at the time of the divorce for which only that spouse is personally liable, those creditors have a potential claim under Sections 4(a)(2)<sup>204</sup> or 5<sup>205</sup> of the UFTA.

At first glance, it would seem that applying the constructive fraud provisions of the UFTA in cases where the trial court orders an unequal division of marital property in a divorce is inconsistent with the statutory authority to make that unequal division of marital property. For example, in Texas, the trial court has wide discretion to make an unequal division of community property in a divorce; but application of the constructive fraud provisions of the UFTA would then allow a creditor to bring an action against a non-liable spouse subsequent to the divorce and recover property, or its value, if the liable spouse received less than reasonably equivalent value in the divorce for the community property transferred to the non-liable spouse. However, application of the constructive fraud provisions of the UFTA in that situation would be no more inconsistent with the statutory authority in Texas to make an unequal division of marital property in a divorce than are the current rules which allow a creditor to attach nonexempt property of a non-liable spouse after divorce to the same extent the creditor could have done so during the marriage, as discussed in Part III(D) of this Article.

### 3. Jurisdictions Applying the UFTA to Division of Marital Property in Divorce Proceedings

There are not a great number of courts that have directly addressed the issue of whether the UFTA applies to a division of

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203. See *Morrison v. Morrison*, 713 S.W.2d 377, 379 (Tex. App. 1986) (trial court awarded 83.5% of the community property estate to wife due to husband's "alcoholism, adultery, and diversion of community assets for the benefit of other women").

204. See Unif. Fraudulent Transfer Act § 4(a)(2) (1984).

205. See *id.* § 5.

marital property in a divorce proceeding; but those that have done so have held uniformly that the UFTA does, in fact, apply.

Michigan is a good example of a common law jurisdiction where this issue has been thoroughly addressed and resolved.<sup>206</sup> In *Estes v. Titus*,<sup>207</sup> the Supreme Court of Michigan held that the UFTA applies to a division of marital property in a divorce judgment that incorporates a property settlement agreement.<sup>208</sup> In that case, Jeff Titus (“Husband”) was convicted of murder and sued for wrongful death by the decedent’s wife, Estes (“Decedent’s Wife”).<sup>209</sup> While that suit was pending, Husband was sued for divorce by his wife, Julie Swabash (“Wife”).<sup>210</sup> In the divorce action, Husband and Wife agreed to unequally divide the marital property pursuant to a property settlement agreement, with the Wife receiving nearly all the marital property, on the ground that Husband was serving a life sentence in prison as a result of his murder conviction.<sup>211</sup> The day following the entry of the divorce judgment, Decedent’s Wife sought to intervene in the divorce action and challenged the distribution of assets to Husband, contending that the property settlement agreement constituted a fraudulent transfer under the UFTA.<sup>212</sup>

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206. See *Citizens State Bank Norwood Young Am. v. Brown*, 849 N.W.2d 55, 61 (Minn. 2014) (holding that a transfer made pursuant to an uncontested marital dissolution decree may be set aside as fraudulent under the UFTA, but reserving opinion as to whether the UFTA applies to contested marital dissolution decrees); *Dowell v. Dennis*, 998 P.2d 206, 209, 212–13 (Okla. Civ. App. 1999) (holding that a creditor may collaterally attack a divorce decree as a fraudulent transfer under the UFTA); *Greeninger v. Cromwell*, 915 P.2d 479, 482 (Or. Ct. App. 1996) (holding that a division of property pursuant to a divorce decree may constitute a fraudulent transfer under the UFTA); see also *Canty v. Otto*, 41 A.3d 280, 289–92 (Conn. 2012) (concluding, after an extensive analysis, that the UFTA applies to property distributions pursuant to a divorce judgment, regardless of whether the distribution is made by the parties pursuant to a property settlement agreement or by the court at the conclusion of a trial and referencing bankruptcy court decisions which held that the distribution of marital assets in a dissolution decree is a transfer for purposes of the federal Bankruptcy Code and noted that the definition of *transfer* in the Bankruptcy Code is similar to that in the UFTA).

207. See generally 751 N.W.2d 493 (Mich. 2008).

208. *Id.* at 503.

209. *Id.* at 495.

210. *Id.*

211. *Id.* at 495–96.

212. *Id.* at 496.

The Court noted that the UFTA applies to any *transfer* of an *asset*, as those terms are defined in the UFTA, quoting the UFTA's definition of transfer as "every mode, direct or indirect, absolute or conditional, voluntary or involuntary, of disposing of or parting with an asset or an interest in an asset, and includes payment of money, release, and creation of a lien or other encumbrance."<sup>213</sup> The Court then explained that a distribution of property made by a court in a divorce judgment "has the same effect as a deed or a bill of sale . . . effectuat[ing] a transfer for purposes of the UFTA when the divorce judgment enters."<sup>214</sup> Thus, "property transferred pursuant to a property settlement agreement incorporated in a divorce judgment is subject to a UFTA action if it meets the definition of an asset."<sup>215</sup>

At this point, California is the only community property jurisdiction that has directly addressed the issue of whether the UFTA applies to a division of marital property in a divorce proceeding. In *Mejia v. Reed*, the Supreme Court of California held that the UFTA applies to a division of marital property in a divorce judgment that incorporates a property settlement agreement.<sup>216</sup> In that case, Danilo Reed ("Husband") had an extramarital affair that resulted in the birth of a child.<sup>217</sup> Husband's wife, Violeta Reed ("Wife"), and Husband subsequently divorced, pursuant to which Husband and Wife agreed to a property settlement agreement providing for the transfer of Husband's interest to Wife in certain jointly held real property.<sup>218</sup> Prior to the divorce, Husband's former mistress, Rhina Mejia ("Mistress"), filed a paternity action against Husband and requested child support.<sup>219</sup> After the divorce decree was finalized, Mistress filed an action claiming that the property settlement agreement was a fraudulent transfer by Husband to Wife to prevent Mistress from collecting child support, and alleged that Husband executed the property settlement agreement with the actual intent to defraud

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213. *Estes*, 751 N.W.2d at 497.

214. *Id.*

215. *Id.*

216. *See generally* 74 P.3d 166 (Cal. 2003).

217. *Id.* at 168.

218. *Id.*

219. *Id.* at 169.

Mistress.<sup>220</sup> One of the primary issues on appeal was whether a transfer of property pursuant to a property settlement agreement in a divorce action could be held invalid under the UFTA.<sup>221</sup>

The Court began its analysis by discussing the statutory tension between the UFTA and California's family code provisions that protect property transferred to a spouse in a divorce proceeding from debts for which only the other spouse is liable.<sup>222</sup> The Supreme Court of California stated that its task was to harmonize those two statutory schemes.<sup>223</sup> The Court's analysis regarding application of the UFTA to a transfer of property pursuant to a property settlement agreement in a divorce action was consistent with the Supreme Court of Michigan's analysis of that issue in *Estes*.<sup>224</sup> The UFTA applies to any *transfer* of an *asset*, as those terms are defined in the UFTA, and a distribution of property made by a court in a divorce judgment pursuant to a property settlement agreement is a transfer of an asset under those definitions.<sup>225</sup> Thus, the Court held that the UFTA applies to a division of marital property in a divorce judgment that incorporates a property settlement agreement.<sup>226</sup>

The Court then turned to the family code provisions dealing with the protection of property transferred to a spouse in a divorce from debts for which only the other spouse is liable. The Court referred to Section 916 of the Family Code, which provides that property received by a spouse in a divorce is exempt from debts incurred by the other spouse before or during marriage, and such spouse is not personally liable for those debts unless they are assigned for payment to such spouse in the divorce.<sup>227</sup> The Court then described the legislative history of the predecessor statute to Section 916, stating that the legislature enacted this statute after determining that it is usually unwise

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220. *Id.*

221. *Id.* at 168.

222. *Mejia v. Reed*, 74 P.3d 166, 169–70 (Cal. 2003); *see also supra* Part III(B) (explaining these family code provisions).

223. *Mejia*, 74 P.3d at 170.

224. *Compare id.*, with *Estes v. Titus*, 751 N.W.2d 493 (Mich. 2008).

225. *Mejia*, 74 P.3d at 170.

226. *Id.* at 174.

227. *Id.* at 171.

to continue, after divorce, the liability of spouses for community debts incurred solely by former spouses.<sup>228</sup> The Court also noted that, in enacting that statute, the legislature contemplated that a divorce court should take the rights of creditors into account in allocating debts to the parties by assuring “there will be available sufficient property to satisfy the debt by the person to whom the debt is assigned, provided the net division is equal.”<sup>229</sup> The Court cited to Section 2550 of the Family Code, providing that the trial court must divide the community property estate of the parties equally, unless the parties agree otherwise in writing or by oral stipulation in open court, but there is no requirement that parties divide the community property equally in a property settlement agreement or that the court scrutinize the agreement to ensure an equal division.<sup>230</sup> Moreover, Section 916 is silent with regard to fraudulent transfers.<sup>231</sup>

Thus, the two statutory schemes are facially inconsistent. The Family Code protects property transferred to a spouse in a divorce proceeding from debts for which only the other spouse is liable, so long as the debt is not assigned for payment to such spouse in the divorce. However, the UFTA allows a creditor to bring an action against a non-liable spouse subsequent to the divorce and recover property, or its value, if the division of marital property pursuant to the divorce is fraudulent under the UFTA. The Court approached its task of harmonizing the two statutory schemes by way of a policy analysis. It explained that a division of community property by the court in the absence of agreement of the parties must be done equally, and that requirement provides some protection for a creditor of only one spouse.<sup>232</sup> For that reason, and because of the legislature’s interest in protecting the rights of creditors, the Court opined that “it is unlikely that the Legislature intended to grant married couples a one-time-only opportunity to defraud creditors by including the fraudulent transfer in” a property settlement agreement.<sup>233</sup> As a result, Section 916 must be

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228. *Id.*

229. *Id.*

230. *Id.* at 171–72.

231. *Mejia*, 74 P.3d at 172.

232. *Id.* at 173.

233. *Id.*

interpreted to mean that property received by a spouse in a divorce is exempt from debts incurred by the other spouse before or during marriage, and such spouse is not personally liable for those debts, unless they are assigned for payment to such spouse in the divorce, and except in cases where the division of marital property pursuant to the divorce is fraudulent under the UFTA. Stated more simply, the UFTA applies to a division of marital property in a divorce judgment that incorporates a property settlement agreement.<sup>234</sup>

The Court, noting that the Appellate Court found triable issues of fact with regard to both actual and constructive fraud, then turned to the question of whether there existed a triable issue of fact under the UFTA as to constructive fraud.<sup>235</sup> The Court determined that whether Husband received reasonably equivalent value in the division of property pursuant to the property settlement agreement was a material disputed fact.<sup>236</sup> However, the Court noted that constructive fraud under Section 5 of the UFTA requires proof that “the transferor was insolvent at the time of the transfer, or rendered insolvent by the transfer,” and determined that there was “no triable issue of fact on the question of insolvency.”<sup>237</sup>

Idaho, a community property jurisdiction, has not directly addressed the issue of whether the UFTA applies to a division of marital property in a divorce proceeding, but has taken an approach that is at least conceptually similar to application of portions of the UFTA. As discussed in Part III(A) of this Article, in *Twin Falls Bank & Trust Co. v. Holley*,<sup>238</sup> the Supreme Court of Idaho applied debtor-creditor principles to the issue of whether a creditor is allowed to obtain a post-divorce judgment against a spouse who is not personally liable for a debt incurred solely by the other spouse, either before or during the marriage, and attach nonexempt property received by the non-liable spouse in the divorce. The Court held that “a creditor may not, with one exception, proceed against community assets distributed to [a spouse] pursuant to a divorce decree” if that

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234. *Id.* at 174.

235. *Id.*

236. *Id.*

237. *Mejia*, 74 P.3d at 174.

238. *See generally* 723 P.2d 893 (Idaho 1986).

spouse is not personally liable for the obligation to that creditor.<sup>239</sup> The Court cited to an earlier case, *Spokane Merchants' Ass'n v. Olmstead*,<sup>240</sup> for the exception: in a divorce, when only one spouse is personally liable for an obligation incurred during the marriage, "but is not awarded sufficient community assets to satisfy such a debt, a creditor may properly seek satisfaction for the debt from community property distributed to the other spouse."<sup>241</sup> The Court explained that the purpose for the exception is to prevent spouses from utilizing "divorce proceedings to perpetrate a fraud on creditors of the community."<sup>242</sup> These rules bear at least some resemblance to the constructive fraud provisions of the UFTA in Sections 4(a)(2)<sup>243</sup> and 5.<sup>244</sup>

### C. Policy Considerations

The basic issue addressed by this Article is to what extent a creditor is allowed to obtain a judgment after divorce against a spouse who is not personally liable for a debt, which has been incurred solely by the other spouse, either before or during the marriage. Accordingly, the question is to what extent is a creditor allowed to attach nonexempt property either received by the non-liable spouse in the divorce or subsequently acquired by such spouse. As discussed earlier in this Article, the rules adopted in most of the community property jurisdictions with respect to this issue appear to be primarily focused on the perspective of marital property and family law without regard to general debtor-creditor law principles and policies. For example, basic fraudulent transfer law has been ignored in those jurisdictions and not applied in the usual manner. As a result, the rules developed in those jurisdictions with regard to the post-divorce liability issue are not consistent with the basic principles and policies of debtor-creditor law. This Section will explore

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239. *Id.* at 897.

240. *See generally* 327 P.2d 385 (Idaho 1958).

241. *Twin Falls Bank*, 723 P.2d at 897 (citing *Spokane Merchants Ass'n*, 327 P.2d 385).

242. *Id.* (citing *Spokane Merchants Ass'n*, 327 P.2d 385).

243. *See* Unif. Fraudulent Transfer Act § 4(a)(2) (1984).

244. *See id.* § 5.

whether valid policy reasons exist for treating creditors differently in this context than creditors in other situations.

The basic right of any creditor is to be paid the full amount they are owed according to the terms and conditions established at the time the obligation is created, either by agreement of the parties or applicable rules of law. If the obligation is created by contractual agreement, the creditor has the ability to evaluate the level of risk that it desires to assume, or even whether to extend credit at all. The creditor has the ability to acquire a substantial amount of information with regard to its debtor. The creditor can obtain the debtor's permission to conduct a credit investigation by the use of credit reporting agencies and determine the debtor's credit score. The creditor certainly can determine whether its debtor is married or single. If the debtor is married, the creditor can demand that the debtor's spouse agree to become jointly liable for the obligation. However, if the debtor owns unencumbered assets, then the creditor can further protect itself by acquiring security interests in those assets to secure the obligation.<sup>245</sup>

Unsecured creditors are generally disfavored under the law and have few rights compared to secured creditors.<sup>246</sup> As discussed earlier in this Article, creditors generally have the right in all jurisdictions to bring a legal cause of action and obtain a judgment against a debtor who is personally liable for an obligation and who has defaulted on payment of such obligation. If the debtor subsequently declines to pay the judgment, the creditor has a range of post-judgment remedies available against the debtor, such as execution on the debtor's assets as necessary to satisfy the judgment. If a creditor who has not yet obtained a judgment is concerned or actually suspects that the debtor will transfer nonexempt assets to avoid satisfaction of any judgment ultimately acquired by the creditor, pre-judgment attachment remedies are available, subject to

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245. See generally Paulsen, *supra* note 9, at 835–37 (discussing rights of creditors and their ability to protect themselves when extending credit).

246. See generally WARREN & WESTBROOK, *supra* note 164, at 40–44, 131–36 (explaining that the rights of secured creditors are vastly superior to the rights of unsecured creditors, and the superior rights of the secured creditor compared to the minimal rights of the unsecured creditor is a paradigm that extends into federal bankruptcy law).

certain procedural and constitutional safeguards.<sup>247</sup> All creditors assume a risk that, subject to application of a jurisdiction's fraudulent transfer law, a debtor will dispose of or otherwise dissipate his nonexempt assets that would be normally available to a creditor in the post-judgment execution process.<sup>248</sup> This could occur whether the debtor is single or married. However, if a debtor is married and his spouse is not personally liable for the obligation, the debtor has the added ability to transfer nonexempt assets to his spouse, thus making them unavailable to his creditors in a collection action.

A transfer of assets to a spouse could be accomplished in a number of different ways, but the usual manner is by making a gift of the assets. In community property jurisdictions, property received by gift is characterized as separate property of the donee spouse,<sup>249</sup> even when the gift is made by the other spouse. Thus, the property is placed *outside* of the creditor's reach in a collection action. The UFTA applies to such a transfer in the same way it applies to transfers of assets outside the marriage, thereby protecting the creditor from transfers that the UFTA describes as fraudulent.

In community property jurisdictions, spouses have the ability to effectively transfer community property assets by entering into an agreement to change the character of property from community property to separate property of one of the spouses.<sup>250</sup> Thus, a debtor spouse could enter into such an agreement to make community property the separate property of the non-debtor spouse, thereby placing such property outside the creditor's reach in a collection action. The extent to which such an agreement is binding on creditors varies significantly among the community property jurisdictions.<sup>251</sup> In Texas, for

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247. See *generally id.* (briefly explaining the legal process required for a creditor to obtain pre-judgment remedies with respect to nonexempt property of a debtor).

248. See *id.* at 841 (discussing risks that all creditors must assume when extending credit).

249. See, Tex. Fam. Code Ann. § 3.001(2) (West 2006).

250. See *generally*, REPPY, SAMUEL & RICHARDSON, *supra* note 27, at 35–43 (discussing the rules applicable in community property jurisdictions for spouses to make express agreements concerning the characterization of property owned during marriage).

251. See *generally id.* at 338–40 (discussing the rules applicable in

example, spouses may enter into pre- and post-marital agreements and agree to change the character of property from community to separate, unless by doing so they intend to defraud pre-existing creditors.<sup>252</sup> At least one community property jurisdiction (Arizona) has recognized that the UFTA applies to agreements to change the character of property from community to separate.<sup>253</sup> In *State ex rel Industrial Commission of Arizona v. Wright*,<sup>254</sup> the Court held that an agreement between spouses to change the character of marital property is a *transfer* as that term is defined in the UFTA.<sup>255</sup> The Court explained that an agreement to change the character of property constitutes the transfer of property rights from one spouse to the other.<sup>256</sup> Thus, the UFTA clearly applies to all transfers of property pursuant to a pre- or post-marital property agreement, protecting creditors from transfers that the UFTA describes as fraudulent.

A transfer of assets can also be accomplished in any jurisdiction by a division of marital property at divorce. As discussed in Part IV(B) of this Article, the UFTA clearly applies to all such transfers, thereby protecting creditors from transfers which the UFTA describes as fraudulent. As such, any transfer of assets from one spouse to another, however structured, is subject to the UFTA in the same way transfers of assets by a single person or by a married person to a non-spouse are. This

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community property jurisdictions with regard to the extent to which marital property agreements are binding on creditors). In Nevada, for example, agreements between spouses to change the character of community property to separate property do not affect creditors, but are binding on creditors in Washington and California. *See id.* at 339. In Wisconsin, such agreements cannot adversely affect a creditor absent such creditor's actual knowledge of the agreement at the time the obligation is incurred. *See id.* In Louisiana, such agreements must be recorded to be effective against subsequent creditors to be effective. *See id.*

252. *See* Paulsen, *supra* note 9, at 826 (explaining the constitutional and statutory limitations with regard to pre- and post-marital property agreements); *see also* TEX. CONST. art. XVI, § 15; TEX. FAM. CODE ANN. § 4.106(a) (West 2006).

253. *See State ex rel. Indus. Comm'n of Ariz. v. Wright*, 43 P.3d 203, 206 (Ariz. Ct. App. 2002) (holding that marital transmutations of community property to separate property are subject to the UFTA).

254. *Id.*

255. *Id.* at 205–06.

256. *Id.* at 206.

results in a logical consistency with respect to the rights of creditors. Creditors should be entitled to the same protection of their right to be paid, regardless of whether their debtor is married or single at any point in the debtor-creditor relationship.

So, what is the purpose for the rules adopted by some of the community property jurisdictions—as described in Part III of this Article—which allow creditors to attach property transferred to the non-debtor spouse post-divorce? As discussed, some of those jurisdictions, such as Louisiana and Texas, simply extend the rules for liability of marital property for debts incurred prior to or during marriage to the period after divorce. However, other jurisdictions, such as Wisconsin and Arizona, go even further by allowing the rights of creditors to be significantly enhanced simply because of divorce, providing creditors with potential windfalls.

The rules adopted by community property jurisdictions regarding whether community property is exempt from debts incurred solely by one spouse—as discussed in Part II of this Article—were critically necessary for protection of creditors during an intact marriage. If community property was exempt from debts incurred solely by one spouse, a creditor would in many cases not be able to collect unless it assured that both spouses were personally liable for it. This would impose a burden on creditors to determine that its debtor is, in fact, married and require his or her spouse to participate in the debt-creating transaction. It would be essentially impossible for a creditor to accomplish this in cases involving involuntary debts, such as an obligation imposed by tort or tax law, for which personal liability only attaches to those on whom the obligation is imposed by law.

However, there is no conceivable purpose in extending these rules to the period after divorce and enabling a creditor to attach former community property which has been transferred in the divorce to the non-debtor spouse.<sup>257</sup> In fact, doing so creates a

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257. Case law in the community property jurisdictions that extend those rules to the period after divorce is devoid of any rationale for doing so. *See, e.g.,* Paulsen, *supra* note 9, at 815–16 (asserting that there is no “clearly articulated rationale” provided in the Texas decisions that extend the rules enacted to protect the rights of creditors during an intact marriage, with regard

serious injustice with regard to a former spouse who was never personally liable for the obligation and received the former community property in exchange for other community property. Furthermore, creditors do not need these rules to be extended to the period after divorce for their rights to be adequately protected. Creditors of single debtors, who default on their obligations and have transferred property to others, are protected by the UFTA. The same is true of creditors of married debtors who default on their obligations and transfer property to a non-spouse, or to a spouse by gift or by execution of a pre-or post-marital agreement. There is simply no reason to provide even greater protection than that provided by the UFTA to creditors of married debtors who transfer property in their divorce to former spouses.

Furthermore, it defies logic to extend community property rules, which were enacted to protect the rights of creditors during an intact marriage, to the period after divorce. These rules are directed at the rights of creditors to seize marital community property. Divorced parties no longer have community property because all community property has been partitioned by agreement or court order upon their divorce, and any community property not partitioned is held by the former spouses jointly as tenants in common.<sup>258</sup>

#### D. Proposal

The basic issue addressed by this Article is to what extent a creditor is allowed to obtain a judgment after divorce against a spouse who is not personally liable for a debt, which has been incurred solely by the other spouse, either before or during the marriage. Accordingly, it must be determined to what extent such a creditor is allowed to attach nonexempt property either received by the non-liable spouse in the divorce or subsequently acquired by such spouse. As discussed, community property jurisdictions should adopt rules to ensure that: (1) spouses who are not personally liable for debts owed at the time of divorce are

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to community property, to the period after divorce).

258. *See id.* at 830–31 (explaining that there is no community property that continues to exist after a divorce).

not unfairly deprived of community property that is transferred to them in the divorce; (2) rights of creditors are protected in a way that is consistent with the rights of creditors in any other situation; and (3) family law and debtor-creditor law are both applied consistently and fairly pursuant to the purposes for which such law was originally enacted. California embodies a community property jurisdiction that has adopted rules most closely accomplishing these objectives. As discussed in Part III(B) of this Article, a California statute provides that property received by a spouse in a divorce is exempt from debts incurred by the other spouse before or during marriage, and such spouse is not personally liable for those debts, unless such a debt is assigned for payment to such spouse in the divorce. In addition, as discussed in Part IV(B)(3) of this Article, case law in California makes it abundantly clear that the UFTA applies to a division of marital property in a divorce judgment. All community property jurisdictions should follow California's lead and adopt rules providing that property received in a divorce is exempt from debts incurred solely by the other spouse before or during marriage, with the only exception being to the extent that fraudulent transfer law applies to the division of the marital property in the divorce proceeding.

## V. Conclusion

The primary thrust of this Article is to address an issue that creditors face when seeking a judgment from a divorcee not personally liable for a debt. The rules developed by each of the community property jurisdictions with respect to this issue are quite distinct and were discussed separately for each jurisdiction in Part III. Some jurisdictions have adopted rules that are quite restrictive with regard to the rights of creditors; the rules in other jurisdictions are quite favorable to creditors, resulting in significant enhancement of the rights of creditors in some jurisdictions, and potential windfalls to creditors, simply because of the divorce.

The rules adopted in most of the community property jurisdictions with respect to this issue appear to be primarily focused on the perspective of marital property and family law without regard to general debtor-creditor law principles and

policies. For example, fraudulent transfer law has been ignored in those jurisdictions and not applied in the usual manner. As a result, the rules developed in those jurisdictions with regard to the post-divorce liability issue are not consistent with the basic principles and policies of debtor-creditor law. Part IV of this Article discussed basic debtor-creditor law as it relates to this issue. In particular, Part IV(B) described fraudulent transfer law under the UFTA and discussed its application to a division of marital property in a divorce proceeding, concluding that the UFTA does in fact apply.

Part IV(C) discussed policy considerations regarding the rights of creditors, and concluded that there is no conceivable purpose in extending the rules that were enacted to protect the rights of creditors during an intact marriage, with regard to community property, to the period after divorce. In fact, doing so creates a serious injustice with regard to a non-debtor former spouse. Furthermore, creditors do not need those rules to be extended to the period after divorce for their rights to be adequately protected because they are already protected by the UFTA. There simply is no reason to provide creditors of married debtors who obtain a divorce and transfer property in the divorce to their former spouses with any greater protection than any other creditor is afforded.

As a result, all community property jurisdictions should provide that property received in a divorce is exempt from debts incurred solely by the other spouse before or during marriage, except to the extent that fraudulent transfer law applies to the division of the marital property in the divorce proceeding. This will ensure that spouses who are not personally liable for debts owed at the time of divorce are treated fairly after the divorce is finalized, rights of creditors are protected in a way that is consistent with the rights of creditors in any other situation, and family law and debtor-creditor law are both applied consistently and fairly.