CREDITOR AND DEBTOR WINDFALLS FROM DIVORCE

by James R. Ratner[*]

Question: What is worse than assuming financial responsibility for your spouse's debts while you are married?

Answer: Being forced to assume even greater financial responsibility for those debts after you divorce.

This brief article addresses the question and proposes a solution to at least minimize the answer.

I. INTRODUCTION

Debt is hard, and marital debt can be even harder, as assets generated by one spouse during a marriage are often available to satisfy obligations incurred by the other spouse.[1] One relatively ancient form of protection offered to the non-debtor spouse, however, is the concept of separate property.[2] Separate property of a non-debtor spouse is, during a marriage,

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1. In Community Property jurisdictions, including Washington, Idaho, Nevada, California, Arizona, New Mexico, Texas, and Louisiana, assets generated by the productive efforts of each spouse during the marriage are generally community property, and community assets are generally available to satisfy community obligations incurred by either spouse. WILLIAM A. REPPY JR. & CYNTHIA A. SAMUEL, COMMUNITY PROPERTY IN THE UNITED STATES, 313–14, 327 (7th ed. Aspen Publishers 2009).

2. The concept of separate property is entrenched in all community property jurisdictions. *See* Grace Blumberg, COMMUNITY PROPERTY IN CALIFORNIA 6 (5th ed., Aspen Publisher 2007); James Ratner, *But From Where Will the Money Come? Community Property Liability for Child Support and Other Premarital Obligations*, 9 WHIT. J. CHILD AND FAM. AD. 17, 23–24 (2009) [hereinafter Ratner, *But From Where Will the Money Come?*]. The concept of separate property is also generally applicable in common law jurisdictions, including those jurisdictions that give divorce judges the ability to allocate

ordinarily isolated from creditors seeking satisfaction of debts incurred by the debtor spouse.[3]

Divorce is hard, too, and may end up making marital debt even more difficult in community property jurisdictions. In almost all community property jurisdictions, creditors, for reasons that turn out to be sensible, are permitted to obtain satisfaction of community debt from the non-debtor spouse regardless of whether the debtor spouse is assigned the debt by a divorce court.[4] As a consequence, however, the separate property of the non-debtor spouse, unavailable to the creditor during the marriage, can quietly become available to the creditor in the event of divorce.[5] Thus, creditors can receive a windfall from divorce, as the divorce increases the pool of assets available to satisfy the obligation. Nor is the matter of this creditor windfall restricted to community property jurisdictions: the same windfall may occur in common law jurisdictions that follow a "kitchen sink" or "hotchpot" approach to asset division at divorce, to the extent that a debtor spouse's creditor is allowed access to that spouse's share of all of the assets available at divorce, including the non-debtor spouse's separate property.[6]

A few community property jurisdictions, including California, Idaho, and to a lesser extent Wisconsin, have apparently responded to the problem of what to do with marital debt at divorce by offering the non-debtor spouse greater protection from divorce than exists during the marriage.[7] This solution, at least in theory, encourages divorce.[8] As a practical matter, the solution is undesirable, as it generates considerable uncertainty in the result and forces unrealistic, unattainable emphasis on a judicially-determined rather than a divorcing-couple-determined debt allocation at divorce. By hinging the answer to the question of whether the creditor or the non-debtor

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all marital assets between the couples. *See* Shari Motro, *Labor, Luck, and Love: Reconsidering the Sanctity of Separate Property*, 102 NW. U. L. REV. 1623, 1630 (2008).

3. REPPY & SAMUEL, *supra* note 1, at 314, 316, 328–30; Ratner, *But From Where Will the Money Come*, *supra* note 2 at 23–24. *See, e.g.*, ARIZ. REV. STAT. ANN. § 25-215 (West 2010) (indicating that in the absence of a contrary agreement the separate property of a spouse is liable for neither the separate debts of the other spouse nor community obligations incurred by the other spouse).

4. *See, e.g.*, ARIZ. REV. STAT. ANN. § 25-318(H) (2010); Marine Midland Bank v. Monroe, 756 P. 2d 1193 (1988) (both indicating that the allocation of debts at divorce is not binding on creditors).

5. *See* discussion *infra* Part II.

6. Kitchen sink or hotchpot common law jurisdictions do not distinguish for purposes of distribution at divorce between those assets generated by one of the spouses during the marriage due to productive activity (generally thought of as community property) and those assets acquired by one of the spouses prior to the marriage or during the marriage via gift, descent, or devise (generally thought of as separate property). J. Thomas Oldham, *Divorce, Separation and the Distribution of Property* § 3.03 [2] (1991).

7. *See* CAL. FAM. CODE ANN. § 916 (West 2009); Twin Falls Bank and Trust v. Holley, 723 P.2d 893 (Idaho 1986); WIS. STAT. ANN. § 766.55 (2m) (precluding marital creditors from seeking income of a non-debt incurring spouse generated after a divorce).

8. Andrea B. Carroll, *Incentivizing Divorce*, 30 CARDOZO L. REV. 1925, 1929–44 (2009) [hereinafter Carroll, *Incentivizing Divorce*].

spouse receives a windfall at divorce on the decision concerning which spouse is allocated the debt at divorce, this solution creates incentives for spouses to strategically divorce, or at least strategically allocate debts at divorce, and for creditors to seek to participate in the debt allocation decision in every divorce in which there is an unpaid marital debt.[9] In the extreme, it has the potential to turn every divorce involving debt into a de facto bankruptcy proceeding in which creditor concerns may well swamp the focus on the divorcing couple.

There is little need to offer windfalls to either the debtor or the creditor in these staggeringly common situations.[10] A simple solution, fully compatible with existing marital debt techniques, is to adopt a mirror image of the solution already adopted in several community property jurisdictions for the analogous problem of pre-marital debt.[11] For the "post-marital liability for marital debts" problem, marital creditors should be limited to assets that would have been available had there been no divorce. This will leave available to community creditors all marital assets received by each spouse at the divorce, and all assets traceable to those assets. Any asset generated by either spouse subsequent to the marriage that would have been the community property of the spouses if they were still married will also be available. Assets unavailable to a community debt creditor include any asset that (1) was the separate property of the non-debtor spouse at divorce, (2) is traceable to such separate property, or (3) was obtained by the non-debtor spouse subsequent to the divorce but would have been separate property if there had been no divorce.[12] This solution necessitates a sometimes complex tracing of assets, but such a tracing process is often an uneventful, familiar one. It is currently undertaken in several contexts, including debt liability issues in all community property jurisdictions.[13]

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9. *Id.*

10. Given the low level of saving generally in the United States combined with home loans and enormous consumer debt, it seems safe to predict that the number of divorces in which debt is the major issue is large. *See generally* Jeffrey Dew, *Two Sides of the Same Coin? The Differing Roles of Assets and Consumer Debt in Marriage*, 28 J. FAM. & ECON. ISSUES 89 (2007) (discussing generally marital assets and debt and the effect of debt on the quality of marriage and likelihood of divorce).

11. Premarital debt creates an interesting problem. If community assets, generally unavailable to satisfy separate property obligations, are not available for a pre-marital debt (which by definition is a separate debt), debtors could engage in "marital bankruptcy" for premarital debts by marrying and then asserting that all community assets, including the debtor's salary, are unavailable to satisfy the obligation. Most community property jurisdictions have responded to this potential windfall for pre-marital debtors with laws permitting premarital creditors to obtain community assets to satisfy the separate property premarital debts to the extent that the assets sought were generated by the debt incurring spouse and thus would have been available to the creditor had there been no marriage. *See, e.g.*, ARIZ. REV. STAT. ANN. § 25-215(B) (2010); WIS. STAT. § 766.55(2)(c)(1) (2009); WASH. REV. CODE ANN. § 26.16.200 (West 2009); NEV. REV. STAT. § 123.050 (2009); *see* Ratner, *But From Where Will the Money Come*, *supra* note 2, at 38–49 (discussing the problems of premarital debt generally and the advantages and disadvantages of various approaches).

12. *See* discussion Part II, *infra.*

13. *See* Blumberg, *supra* note 2, at 170–71; REPPY & SAMUEL, *supra* note 1, at 159–60.

The solution eliminates windfalls in either direction and the incentives they create, without causing disruptions, and removes any necessity to consider creditor needs in the face of a divorce.

II. CREDITOR WINDFALLS FROM DIVORCE

When either spouse incurs debt during a marriage, an issue may arise concerning the various assets potentially available to the creditor for satisfaction of the debt. Different community property regimes have developed alternative approaches to this issue.[14] Managerial systems give creditors access to all assets managed by the debtor spouse regardless of the community or separate characterization of the debt.[15] Community debt/separate debt systems allow creditors access to all community assets for community debts but deny access to community assets for separate debts.[16] Partition systems grant creditors access to all community assets for a community debt and to half the community assets for a separate debt.[17] Regardless of whether the jurisdiction maintains a managerial, community debt/separate debt, or partition creditor satisfaction system, community debts are generally satisfied first out of the community property and second from the separate property of the debt incurring spouse, rendering the separate property of the non-debtor spouse unavailable to creditors.[18] This structure isolates and protects the separate property of the non-debt-incurring spouse from being used to satisfy community obligations.[19] At

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14. Ratner, *But From Where Will the Money Come*, *supra* note 2, at 27–31, 31–36, 36–38.

15. California is a typical managerial regime. *See* CAL. FAM. CODE § 910 (West 2009). Texas and Louisiana also maintain managerial systems. *See* TEX. FAM. CODE ANN. §§ 3.201–3.202 (West 2009); LA. CIV. CODE ANN. art. 2340 (2009); Ratner, *But From Where Will the Money Come*, *supra* note 2, at 31–36.

16. Arizona, Washington, New Mexico, and Wisconsin maintain at least partial attributes of a community debt/separate debt system. *See* ARIZ. REV. STAT. ANN § 25-215 (2010); N.M. STAT. ANN. § 40-3-10(A) (West 2009); WIS. STAT. ANN. § 766.55(1) (West 2009); deElche v. Jacobsen, 622 P.2d 835, 840 (Wash. 1980).

17. New Mexico, Washington, and Wisconsin also maintain partition attributes. N.M. STAT. ANN. § 40-3-10(A); WIS. STAT. ANN. § 766.55(2)(b), (d); *deElche*, 622 P.2d at 840.

18. *E.g.*, ARIZ. REV. STAT. ANN. § 25-215(D) (explaining that a community "debt or obligation shall be satisfied: first, from the community property, and second, from the separate property of the spouse contracting the debt or obligation"). *See also* CAL. FAM. CODE § 913(b)(1); IDAHO CODE ANN. § 32-911 (2009); N.M. STAT. ANN. § 40-3-11(A). There are exceptions in some community property jurisdictions for situations in which creditors have supplied "necessaries" such as medical treatment, food, or shelter to a debt-incurring spouse. *See* Ratner, *But From Where Will the Money Come*, *supra* note 2, at 25 n.34; 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, 21–26 (2007) [hereinafter Carroll, *The Superior Position of the Creditor*]. *See, e.g.*, CAL. FAM. CODE § 914; NEV. REV. STAT. ANN. § 123.090 (West 2009); TEX. FAM. CODE. ANN. § 3.201(a)(2); WASH. REV. CODE ANN. § 26.16.205 (West 2005).

19. This structure is necessary to maintain the concept of separate property, which includes total management and control by the separate property owner and none by the separate property owner's spouse. If the separate property of a non-debt-incurring spouse were not insulated from community creditors and separate creditors of a debt incurring spouse, a debt-incurring spouse could in effect

divorce, however, that protection for the non-debtor spouse may prove evanescent.

Divorces frequently feature community debts.[20] As has always been true—and is reiterated in statutes such as the relatively new Arizona statutory "creditors bill of rights"—debt allocation by a divorce court generally allocates the debt only between the spouses and is not binding on creditors.[21] If the spouse not allocated the debt is forced to pay, the allocation enables the spouse who pays to obtain reimbursement and thus serves as a judgment on behalf of the paying spouse against the spouse who did not pay.[22] In other words, the spouse that actually pays becomes the creditor. As a practical matter, reimbursement may be hard to come by—one reason why the original creditor goes after the spouse who ends up paying the debt is because the other spouse has only a few assets easily available to creditors.[23]

This structure poses a potential nightmare for a non-debtor spouse. As a practical matter, neither spouse has much control over the spending habits of the other spouse. This practical oddity stems from the rules entitling each spouse to equal management and control, combined with little authoritative strength to any rules concerning the standard of care one spouse owes to the other during marriage.[24] The only protections community property jurisdictions offer are fairly minimal requirements of a joint management and control decision in order to make certain transactions enforceable and perhaps an opportunity to seek redress for breach of the

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alienate his spouse's separate property by incurring debt that would end up paid by the separate property of his spouse.

20. *See supra* note 15.

21. ARIZ. REV. STAT. ANN. § 25-318 (H). *See also* Marine Midland Bank v. Monroe, 756 P.2d 1193, 1194 (Nev. 1988); Black v. Amoco Fed. Credit Union, 900 S.W.2d 108, 111–12 (Tex. App.—Houston [14th Dist.], 1995, no writ). Some community property jurisdictions have restricted or precluded creditor access to assets the non-debtor spouse received pursuant to or subsequent to divorce if the non-debtor spouse is not allocated the debt at divorce; this forces the creditor to care about the allocation of debt between the spouses at divorce. *See infra* Part III.

22. *See* ARIZ. REV. STAT. ANN. § 25-318(N), (P) (2010) (authorizing a spouse who paid a debt allocated at divorce to the other spouse to obtain a limited reopening of the divorce decree for purposes of transferring property to the debt-paying spouse, and authorizing a court to transfer property of a spouse who fails to pay a debt to the other spouse to compensate for the payment of a non-allocated debt); Srock v. Srock, 466 P.2d 34, 36 (Ariz. Ct. App. 1970) (describing the divorce allocation as having "the character of a declaratory judgment," ordering the husband to reimburse his wife, who subsequent to divorce paid a debt allocated to the husband in the divorce decree, and refuting the notion that in order to collect the wife must file a separate action).

23. *See, e.g.*, Birt v. Birt, 96 P.3d 544, 552 (Ariz. Ct. App. 2004) (husband refused to pay debts allocated to him at divorce and declared bankruptcy, leaving the wife unable to obtain reimbursement).

24. After an extensive period in which the husband had sole power to manage and control the community property, all community property jurisdictions abandoned the Spanish civil-law-derived, sex-based rule in favor of sex-neutral equal management and control rules. *See* REPPY & SAMUEL, *supra* note 1, at 257–58; Blumberg, *supra* note 2, at 415.

duty of care each spouse owes to one another.[25] Otherwise one spouse cannot generally avoid unwise marital debt incurred during marriage.[26] Nor can the non-debtor spouse avoid responsibility for that debt simply by

25. A joint management and control decision, meaning that both spouses need not be parties to a transaction but must consent to the transaction, is typically required for transactions such as buying, selling, or encumbering real community property. *See* REPPY & SAMUEL, *supra* note 1, at 267–68; Carroll, *Incentivizing Divorce*, *supra* note 8, at 1945 & n.120. Other transactions for which a joint management and control decision may be required include guarantee, indemnity, and surety commitments of the community. *See, e.g.*, ARIZ. REV. STAT. ANN. § 25-214(C)(2). Most community property jurisdictions, by statute or case law, require a spouse at a minimum to "act in good faith" toward the other spouse concerning community property management and control decisions. *See* WIS. STAT. ANN. § 766.15(1) (West 2010). California requires that "[e]ach spouse shall act with respect to the other spouse in the management and control of the assets and liabilities property in accordance with the general rules governing fiduciary relationships . . . ," CAL. FAM. CODE. ANN. § 1100(e) (West 2010), and establishes that a fiduciary relationship "imposes a duty of the highest good faith and fair dealing on each spouse . . . ," CAL. FAM. CODE. ANN. § 721(b)(West 2010). But in all jurisdictions, in the absence of bad faith or out-and-out fraud, relief is seldom granted. REPPY & SAMUEL, *supra* note 1, at 302–03 ("Most contemporary cases . . . [refuse] to second-guess *H's* or *W's* management decisions. Liability for mismanagement is seldom imposed absent conduct that [amounts to fraud or bad faith] . . . . Louisiana has said that the manager spouse may 'squander the community funds or property on unworthy objects or in the gratification of extravagant tastes or luxurious indulgences.' *Succession of Boyer*, 36 La. Ann. 506, 512 (1884)."). Even where relief might be available to an aggrieved spouse, however, in the absence of power to block the transaction leading to indebtedness, the creditor will have access to community assets to satisfy the obligation, with the aggrieved spouse left to seek relief from remaining assets.

26. Carroll, *Incentivizing Divorce*, *supra* note 8, at 1945. A particularly unfortunate example occurs in Arizona concerning partnership obligations. Despite the fact that ARIZ. REV. STAT. ANN. § 25-214(C)(1) and (2) require a joint management and control decision for the purchase, sale, or encumbering of real property, and for "[a]ny transaction of guaranty, indemnity or suretyship," when one spouse becomes a general partner in a partnership designed to buy and sell real property, the community will be liable for all debts of the partnership without joinder. *See* Chase Bank v. Acosta, 880 P.2d 1109, 1119 (Ariz. 1994) (concluding that general partnership law renders each general partner jointly and severally liable for all obligations of the entire partnership, but because the community ownership interest in the partnership is personal and not real property, there is no joinder requirement for partnership transactions in real property). In *Acosta*, the husband signed on as a general partner for a partnership that bought and sold real property. *Id.* at 1111. His wife did not consent to the joining of the partnership. *Id.* at 1112. The partnership incurred substantial debt as part of purchasing real property, with each partner, including Mr. Acosta, signing a personal guarantee to the lender. *Id.* at 1111. Mr. Acosta's wife did not join on the guarantee or on the underlying transaction for real property. *Id.* at 1112. The partnership subsequently was unable to pay the debt, and the lender sued the Acosta marital community. *Id.* at 1114. The marital community defended on the ground that there was no joinder. *Id*. at 1117. While the lender was unable to obtain access to community assets on the basis of the guarantee, as there was no joinder, the lender was permitted to obtain access to community assets on the basis that a general partner is jointly and severally liable for all partnership obligations, and the husband's activity as a general partner was management and control of community personal property interest for which there was no joinder requirement. *Id.* at 1118. Thus, Mr. Acosta managed to subject the community to a staggering amount of debt concerning a real estate transaction without Mrs. Acosta having any ability to object or otherwise protect her undivided ownership of the community property. *See id*. at 1119. Who would have suspected when learning the difference between personal and real property in a first year property course that the distinction could devastate a marriage? A sensible solution that offers real meaning to the joinder requirement is to either (1) interpret "any transaction of guarantee, indemnity or suretyship" to apply to joining a partnership because of the joint and several liability aspect, or (2) enact a joinder requirement for joining partnerships.

divorcing.[27] A divorce can preclude responsibility only for *further* debt incurred by an excessively spending spouse.[28] Thus, the spouse who never approved of the debts during the marriage when the debt was incurred may end up paying the debts and become a creditor of the debt-incurring spouse. Even worse, the spouse who never approved of the debts may also become an unsatisfied creditor if the debt-incurring spouse has no assets available for collection. The only assets the non-debtor spouse can safely unilaterally protect are her separate property assets.[29]

As appalling as this rule may sound to the more fiscally responsible spouse, it makes some sense. Divorce is not bankruptcy. Creditors are not parties to a divorce, and the focus in a divorce is on the proper allocation of the marital assets between the two spouses, not on the allocation that maximizes easy collection for the creditors. If a creditor were restricted to collect from only the spouse allocated the debt at divorce, that creditor's ability to collect could be jeopardized by a particular allocation, in effect undermining the value of the creditor's asset (i.e., the ability to collect) without the creditor being a party to the revaluation. In addition, couples could attempt to avoid obligations by agreeing in their divorce settlement to allocate all of the assets to one spouse and a particularly nagging debt to the other relatively judgment-proof spouse.[30] While some of these problems can be minimized by making creditors parties to a divorce, that is not the solution. Doing so turns a routine divorce into an odd sort of bankruptcy proceeding and escalates the expense of divorcing. One particularly troublesome problem is that allocations will likely offer priority to some creditors unless all are made parties, something not likely to happen under current divorce structures, and steer the focus of the divorce away from the appropriate allocation of marital assets and liabilities and toward the needs of creditors.[31] Consequently, to avoid turning every divorce with debt into

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27. *See* REPPY & SAMUEL, *supra* note 1, at 334–35 ("As a general rule in most states a divorce decree dividing community property, or a property settlement agreement making such division, 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 . . . . A divorce decree assigning debts to one spouse or the other is binding on the spouses but not on the creditors."). *See, e.g.*, ARIZ. REV. STAT ANN. § 25-318(H) (2010) ("Since your creditors are not parties to this court case, they are not bound by court orders or any agreements you and your spouse reach in this case.").

28. *See* sources cited *supra* note 27.

29. Most community property jurisdictions do not allow a spouse to unilaterally sever community property except by marriage. *See* Carroll, *Incentivizing Divorce*, *supra* note 8, at 1944–45, 1954–56 (pointing out the lack of availability of unilateral severing except in Louisiana and Wisconsin, and advocating simplified and expanded use of the idea).

30. *See* Carroll, *Incentivizing Divorce*, *supra* note 8, at 1930, 1934, 1939–44.

31. Divorce allocations currently depend on the parties to identifying all outstanding debts. *See, e.g.*, § 25-318(H) (suggesting, but not requiring, that parties to a divorce contact creditors and discuss the effect of the divorce on the debts). Parties have incentives to not disclose all outstanding debts and creditors, and in any event, it is well known that parties do not always identify all creditors. Interview with Hon. Lori B. Jones, Superior Court J., in Pima County, Ariz., (Feb. 10, 2009) (Judge Jones handles default and settled divorces in Pima County Superior Court.). In recognition of this inevitability, cases

a prolonged yet incomplete evaluation concerning how community creditors can most effectively be paid, community property jurisdictions have gravitated toward the above-described approach of enabling creditors to seek satisfaction of the full amount of the obligation from either spouse, and offering reimbursement to the spouse not allocated the debt.[32]

This structure, however, enables community creditors to receive a windfall from the divorce in the absence of post-divorce restrictions concerning the source of the assets available to the creditor. In Arizona, for example, no statute contains instructions concerning asset availability post-divorce. Instead, pursuant to (meager) case law, each spouse is jointly and severally liable for all community debts after divorce.[33] As a consequence, regardless of the allocation of a debt at divorce, after divorce a community creditor may seek satisfaction from the non-debt-incurring spouse's assets, and no statute or case law prevents the creditor from seeking the non-debt-incurring spouse's *separate property*.[34] The divorce thus enables a community creditor to obtain windfall access to assets that were separate property of the non-debtor spouse during marriage, assets traced to those assets, or assets that would have been the separate property of the non-debtor spouse even if there had been no divorce, all of which are assets that would have been unavailable during the marriage.

The following example illustrates the structure and the windfall using Arizona's community property structure:

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have clarified that for outstanding community debts not identified by the parties to the divorce in the divorce proceedings, each spouse is allocated half the debt. *E.g.*, Ellsworth v. Ellsworth, 423 P.2d 364 (Ariz. Ct. App. 1967). If the creditor obtains payment in full from one spouse, that spouse can seek reimbursement for half from the other spouse. *Id.* at 367–68 (holding that spouses are liable for up to half of all community obligations not dealt with in a divorce proceeding).

32. Given this approach, it will frequently be in the interest of a more fiscally responsible spouse to use community assets to pay off as many community obligations at divorce as possible rather than seek to have them allocated to the other spouse, even if the other spouse was the debt-incurrer, and even if that means there will be few or no community assets remaining at divorce. The problem with leaving the community assets intact and arguing that the debt-incurrer be allocated the debt is that it is predictable that the less responsible debt-allocated spouse will not pay off the debts with any assets he obtains from the divorce. In that event, the creditors can obtain payment from the more responsible spouse, leaving that spouse with a distinct possibility of being unable to obtain reimbursement from the less responsible spouse. It is often better to in effect force the less responsible spouse to spend his share of the community assets paying down the debts, even though it will mean little or no community assets will remain for the more responsible spouse.

33. *See, e.g.*, Cmty. Guardian Bank v. Hamlin, 989 P.2d 1005, 1009 (Ariz. Ct. App. 1995) (permitting a creditor to garnish a non-debtor spouse's wages to obtain satisfaction of a community obligation incurred by the debtor spouse during the divorce regardless of whether the debt was allocated to debtor, non-debtor, or neither at divorce).

34. *Id.* (concluding that a creditor can satisfy a community obligation with the separate property of the non-debtor spouse who was not allocated the debt at divorce). It is understandable to not exclude *all* separate property of the non-debt-incurring spouse, because once the divorce is final, all of her property is, by definition, separate. No statute or case attempts to identify separate property assets that were the separate property of the non-debtor-spouse during the marriage.

A husband incurs considerable outstanding credit card debt during the marriage. The purchases were all in furtherance of the community, making the debt a community debt.[35] The credit card company sues the married couple, but has trouble collecting on the debt because there are few wages to garnish, community assets are scarce, and the debt-incurring husband has no separate property.[36] During the marriage, the wife's family, concerned about the free spending ways of the husband, began gifting amounts to the wife, placing them in an account the wife kept entirely separate and did not make available to the husband and did not use for community expenses. The creditor tries to attach the accounts to use the money to satisfy the judgment but fails because the separate property of a non-debt-incurring spouse is not available to satisfy a community property judgment.[37] The Arizona community debt/separate debt statutory structure, for example, makes community property and the separate property of the debt-incurring spouse available (in that order), leaving the separate property of the non-debt-incurring spouse fully protected.[38]

If the wife, fed up with her husband's behavior, seeks and obtains a divorce, the meager community property will be divided between the spouses.[39] In contrast, all of the wife's separate property is simply hers and must go to her—it is not subject to

35. Community debts are defined as debts incurred during the marriage for the benefit of the community. *See* Ratner, *But From Where Will the Money Come*, *supra* note 2, at 31–35. All during-the-marriage debts are presumed community debts, and the community generally has the burden to show that it was a separate property obligation—a burden that is hard to overcome, especially if the debts were incurred for what appear to be usual family expenses. *Id.*; REPPY & SAMUEL, *supra* note 1, at 133–35.

36. The spouses are considerably less able to avoid the debt via bankruptcy than they were when they originally signed up for the credit card, raising the question of why the bankruptcy changes were allowed to apply retroactively to credit arrangements originally negotiated under a different regime. *See* Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, Pub. L. No. 109-8, 119 Stat. 23 (2005). But that is another story for another time.

37. The money is the separate property of the wife because money acquired by gift, descent, or devise is by statute made separate property. *See, e.g.*, ARIZ. REV. STAT. ANN. § 25-213(A) (2010); CAL. FAM. CODE ANN. § 770 (West 2009); Ratner, *But From Where Will the Money Come*, *supra* note 2, at 23.

38. *See* ARIZ. REV. STAT. ANN. § 25-215(A), (D). Community property regimes generally do not offer separate property of the non-debtor spouse to creditors. Ratner, *But From Where Will the Money Come*, *supra* note 2, at 25 n.34. There is an exception in some jurisdictions for the "necessaries" doctrine, not applicable to the example, enabling creditors some access if the creditor supplied medical treatment, food, or shelter to a debt-incurring spouse. California, Louisiana, Nevada, Texas, Washington, and Wisconsin all have some version of a necessaries doctrine. *Id.* The necessaries doctrine is grounded more in quasi-contractual "unjust enrichment" than in marital property or creditor-debtor concepts. *Id. See also* Carroll, *The Superior Position of the Creditor*, *supra* note 18, at 22–26 (describing use of agency theories, ratification, and unjust enrichment to justify a creditor obtaining the separate property of a non-debtor spouse).

39. *See, e.g.*, ARIZ. REV. STAT. ANN. § 25-318(A).

division at divorce.[40] But the credit card debt, a community debt, must be allocated at the divorce.[41] It could end up allocated to either spouse, or split in some way between them, but even if it ends up allocated solely to the husband via the divorce decree, the credit card company is not bound to seek satisfaction from the husband only, as creditors are not bound by the allocation, and can seek satisfaction for community debts against either spouse.[42] The creditor, gravitating toward the most reliable way to get paid, will once again seek satisfaction of the debt from the separate property money in the wife's account, but this time the creditor will succeed. Each former spouse is jointly and severally liable on all community obligations.[43] When the community assets are divided at divorce, all assets, regardless of their original characterization, by definition become the separate property of the respective ex-spouses.[44] Unless there is case law or a statute that explicitly shields an ex-spouse's assets that were separate property during the marriage from being used to satisfy what was

40. *See id.* (stating that a divorce court "shall assign each spouse's sole and separate property to such spouse"). Wisconsin has departed from this concept for separate property not obtained via gift, descent, or devise. WIS. STAT. ANN. § 767.61 (West 2009). The rule that separate property must go to the owning spouse at divorce was one that distinguished community property jurisdictions from hotchpot or kitchen sink common law jurisdictions, which subjected all property of either spouse to division at divorce. *See* Blumberg, *supra* note 2, at 5. A recent practice in those jurisdictions is to award "most or all preexisting, gifted, and inherited property to the owner spouse." Motro, *supra* note 2, at 1630 & n.16.

41. In Arizona, the "must be" is a bit controversial. The Arizona divorce distribution statute does not explicitly require all division and allocation of community liabilities at divorce, only the assets. ARIZ. REV. STAT. ANN. § 25–318(A) (2009). *See also* Jankowski v. Jankowski, 561 P.2d 327, 328 (Ariz. Ct. App.1977) (explaining that the trial court is not required to allocate community debts, and in the absence of an allocation the husband and wife remain jointly and severally liable for each debt). Recent amendments to that statute, designed to clarify and protect creditors and thus dubbed the "creditor's bill of rights," focused on the nonbinding nature of such allocations on third party creditors and did not clarify that the divorce court is required to allocate debts between the parties. *See, e.g.*, ARIZ. REV. STAT. ANN. § 25-318(H) (2009). The closest the amended structure comes to requiring distribution of debt is in section 25-318(J) and (L), which indicate that on request of either party the divorce court "shall" require the parties to submit a debt distribution plan and in its order pertaining to division of the property "shall reflect the debt distribution plan . . . ." ARIZ. REV. STAT. ANN. § 25–318(L) (2009). By implication, but only by implication, these portions of the statute suggest a divorce court has no discretion and must allocate marital debts.

42. *See* REPPY & SAMUEL, *supra* note 1, at 334–35; *see, e.g.*, ARIZ. REV. STAT. ANN. § 25-318(H) ("Since your creditors are not parties to this court case, they are not bound by court orders or any agreements you and your spouse reach in this case."); Marine Midland Bank v. Monroe, 756 P.2d 1193, 1194 (Nev. 1988) (holding that the allocation of credit card debt to the husband at divorce was not binding on the creditor, who was permitted to collect from the wife).

43. *See Jankowski*, 561 P.2d at 328; REPPY & SAMUEL, *supra* note 1, at 334–35.

44. *See, e.g.*, Koelsch v. Koelsch, 713 P.2d 1234, 1239 (Ariz. 1986) ("[Pursuant to] clearly established community property principles . . . [w]hen the community property is divided at dissolution . . . each spouse receives an immediate, present, and vested separate property interest in the property awarded to him or her by the trial court."). There are some exceptions for community property left unallocated at divorce, which is usually treated as tenancy in common. *See* REPPY & SAMUEL, *supra* note 1, at 360–62.

a community obligation, the wife has no basis for protecting what was always her separate property in her separate property bank account.[45]

So the wife must pay, forced by the creditor to do so, from that separate property account.[46] She is entitled, due to the divorce court allocation of the debt, to seek immediate reimbursement for the full amount from her ex-husband.[47] But collection against him will be problematic, as the creditor already knew when deciding to go after the wife's assets instead. In any event, what was the non-debtor-spouse's separate property during the marriage has already gone to the community creditor, replaced by a chance to sue an ex-spouse to try to collect that amount. The same result occurs if the separate property assets are cash, heirlooms, real property (unless homestead protection prevents it), or other investments, and regardless of whether the assets were acquired before, during, or after marriage. If the wife's family had continued to give her money after the divorce, the creditor would be able to obtain that money to satisfy the community debt.

The example demonstrates that a divorce quietly, almost magically, provides a community creditor with access to separate property of the non-debt-incurring spouse, access unavailable as long as she remained married.[48] It is true that the windfall will only materialize when the non-debtor spouse actually has separate property, but there is no reason to offer it to marital creditors. They do not need it. Marital creditors are already entitled to what could be viewed as a fortuity of access both to the community assets generated by the non-debtor spouse during marriage[49] and to the community assets generated by the debtor spouse for separate property debts incurred prior to the marriage.[50] No regime, be it

45. *See* Cmty. Guardian Bank v. Hamlin, 898 P.2d 1005, 1009 (Ariz. Ct. App. 1995).

46. *See id.* at 1009.

47. *See id.*

48. In California it is not so quiet. CAL. FAM. CODE § 916 (West 2010) specifically authorizes this result whenever the non-debtor spouse is allocated all or a portion of that debt at divorce. *See infra* Part III.

49. *See* Carroll, *The Superior Position of the Creditor*, *supra* note 18, at 17, 20. Professor Carroll views both the managerial and the community debt/separate debt systems to be overly favorable to creditors because of the presumption of availability of community assets to satisfy one spouse's debt. *Id*. I am less convinced than Professor Carroll that there is a fortuity involved. Creditors should offer credit on better terms to married couples because of the availability of community assets, although it is safe to point out that credit markets do not always function smoothly. In any event, if either spouse is to have genuine ability to transact on behalf of the community, the creditor needs to have access to all community assets, including the assets generated by the non-debtor spouse. Otherwise, rational creditors will either insist on transacting with the more financially secure spouse or insist that both spouses participate as parties to the transaction.

50. *See generally* Ratner, *But From Where Will the Money Come*, *supra* note 2, at 38–49. In most of the community property jurisdictions, premarital creditors can obtain access to community property

managerial, partition, or community debt/separate debt oriented, grants community creditors access to the separate property of the non-debtor spouse during a marriage.[51] It is the divorce, which turns all of the assets of each spouse into his and her own separate property, that opens up the availability to the creditor. Under this structure, community creditors of debtors who lack community property but have spouses with ample separate property should be hoping desperately for a divorce.[52]

There is no good reason to allow a divorce windfall for community creditors. This windfall, inconsistent with all debt classification regimes, interferes with the protections granted to a non-debtor spouse and compounds the difficult problem of a marriage in which one spouse racks up community debt and leaves the fiscally responsible spouse with divorce as the only way to effectively avoid ever increasing debts.

Leaving the creditor windfall intact in order to discourage divorce should not be seriously considered.[53] In the example above, the non-debtor wife is in an impossible position. Under the current regime, to protect her separate property assets, she has to stay married, but if she stays married she becomes financially responsible for the increasingly vast debt incurred by the husband on behalf of the marital community.[54] As an intermediate step, the responsible spouse might obtain the debt-inclined spouse's agreement to a transmutation agreement.[55] Such an agreement is effective against subsequent debt although not generally effective concerning debts already incurred.[56] A transmutation strategy only works, however, if both spouses can agree concerning how to restructure the financial situation, and even then the agreement may be challenged by creditors.[57] In addition,

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generated by a premarital debtor. *See generally id.* The problem of a creditor windfall created from a divorce is also the mirror image of the problem of how to treat premarital debts. *See id.* at 20–21.

51. Carroll, *The Superior Position of the Creditor*, *supra* note 18, at 21.

52. An additional type of creditor may also be hoping for a divorce: separate creditors. During marriage, in community debt/separate debt jurisdictions, separate creditors cannot obtain access to community assets, such as salary generated by the debt-incurrer. *See* REPPY & SAMUEL, *supra* note 1, at 336. At divorce, that salary and any other assets that would have been community assets become available. *Id*.

53. *See generally* Carroll, *Incentivizing Divorce*, *supra* note 8, at 1928–31, 1938–44 (discussing the incentives for divorce created by the California and Idaho regimes that correct the windfall by making community assets unavailable to the creditor).

54. *See* Ratner, *But From Where Will the Money Come*, *supra* note 2, at 23–26.

55. Carroll, *Incentivizing Divorce*, *supra* note 8, at 1945–46.

56. *See* Ratner, *But From Where Will the Money Come*, *supra* note 2, at 46; Richard Bartke, *Marital Sharing - Why Not Do it By Contract?* 67 GEO. L.J. 1131, 1151–55 (1979); REPPY & SAMUEL, *supra* note 1, at 459–60. Transmutation agreements, often effective concerning obligations incurred subsequent to the agreement, are seldom retroactively effective. REPPY & SAMUEL, *supra* note 1, at 338–39.

57. *See, e.g.*, State *ex rel.* Indus. Comm'n v. Wright, 43 P.3d 203, 206 (Ariz. Ct. App. 2002) (holding that a creditor may successfully challenge a transmutation agreement as a fraudulent conveyance); Elia v. Pifer, 977 P.2d 796, 805 (Ariz. Ct. App.1998) (enforcing transmutation agreement against a subsequent creditor, but only after assessing whether the agreement was involuntary or unconscionable). *See also* Hrudka v. Hrudka, 919 P.2d 179 (Ariz. Ct. App. 1995) (initially wife, and

more availability of a "unilateral severing" approach might be helpful.[58] Nevertheless, for many spouses the only secure, practical way to prevent the other spouse from continuing to incur community credit card and other significant debt may be to get a divorce. In addition, a non-debtor spouse cannot choose to protect her separate assets by continuing in the marriage if the debtor spouse chooses to seek a divorce. Perpetuating a disguised form of punishment for divorce—forcing spouses with separate property to use it to pay debts incurred by their spouses during marriage—is not a healthy approach for insisting that a marriage hampered by major debt continue rather than discontinue via divorce.

III. A SIMPLE SOLUTION: USE TRACING RULES TO RENDER DIVORCE A NON-EVENT FOR CREDITORS

There is neither a need to give creditors a windfall from divorce nor a need to overcorrect.[59] States can eliminate divorce-imposed windfalls, in either direction, with a rule that mirrors the typical premarital debt solution. Virtually all community property jurisdictions give a premarital creditor access to the community property generated by the debtor spouse during the marriage, in effect giving creditors access to any asset the creditor can trace to a source that would have been available had there been no marriage.[60]

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subsequently husband, challenged a prenuptial transmutation agreement as unconscionable and involuntary).

58. Carroll, *Incentivizing Divorce*, *supra* note 8, at 1944–56. Unilateral severing is a possible method short of divorce of addressing problems of differing financial perspectives within a marriage. The solution is not available in most community property jurisdictions, however, and is overly cumbersome in those in which it is available. *Id.* at 1946.

59. California, Idaho, and to a lesser extent Wisconsin overcorrect the problem by offering a windfall to the non-debtor spouse from divorce. *See infra* Part IV.

60. *See* Ratner, *But From Where Will the Money Come*, *supra* note 2, at 38–49. Premarital debts are by definition separate debts, but if the creditor were unable to obtain access to assets generated by the debtor spouse, including community assets, the debtor spouse could commit "marital bankruptcy." *Id.* To address that problem, most community property jurisdictions have enacted statutes permitting a partition system that allows a premarital creditor access to all assets that would have been available to the creditor had there been no marriage. *Id.* *See, e.g.*, ARIZ. REV. STAT. ANN. § 25–215(B) (2011) ("[C]ommunity property is liable for the premarital separate debts or other liabilities of a spouse . . . but 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."); CAL. FAM. CODE § 911(a) (West 2011) (departing from its managerial system to make available to premarital creditors only those community assets not generated by the non-debtor spouse); NEV. REV. STAT. ANN § 123.050 (West 2010) (implementing a partition system that protects the non-debtor spouse's separate property and "share of the community property" from premarital creditors); TEX. FAM. CODE ANN. § 3.202(b)(1) (West 2009) (precluding community property managed solely by the non-debtor spouse from liability to a premarital creditor); WIS. STAT. ANN. § 766.55(2)(c)(1) (West 2011) ("An obligation incurred by a spouse before or during marriage that is attributable to an obligation arising before marriage or to an act or omission occurring before marriage may be satisfied only from property of that spouse that is not marital property and from that part of marital property which would have been the property of that spouse but for the marriage."); WASH. REV. CODE § 26.16.200 (West 2011) (limiting premarital creditors' access to community property to the "earnings and accumulations" of the debtor spouse, and requiring that

The access is given to prevent bankruptcy by marriage for premarital separate property debts. The same idea needs to be implemented after a marriage is over. Marital creditors should be able to satisfy marital obligations only from assets of the non-debtor spouse that are community assets received in a divorce distribution or are assets that would have been available as community assets if there had been no divorce.

A tracing approach resolves the windfall problem without rendering the creditor impotent, as the creditor will still have generous access.[61] For community obligations, creditors will still be able to obtain access to any asset controlled by either spouse that (1) was community property during the marriage, (2) is traceable to that community property, or (3) would have been community property except for the divorce. Most notably, this will include the earnings of either spouse after the divorce, which would have been community property if there had not been a divorce.

One concern about using a tracing system to identify the assets available to community creditors after a divorce has ended the community is that tracing is messy.[62] Although this concern may be overblown, tracing is not always going to be easy.[63] Commingling of assets will inevitably

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creditors seek premarital claims against community assets within three years of the day the marriage begins). Louisiana eschews any tracing system that would protect some of the non-debtor spouse's interest in the community property, and instead allows premarital creditors access to all community assets, including those generated by the non-debtor spouse. Carroll, *The Superior Position of the Creditor*, *supra* note 18, at 5–9.

61. *See* Ratner, *But From Where Will the Money Come*, *supra* note 2, at 38–49. Different states make different amounts available to creditors depending on whether the debt is a community debt or a separate debt and depending on whether the state adopts a managerial, partition, or CP debt/SP debt structure. *Id*.

62. *See Liability of Marital Property for Debts*, 17 CAL. L. REVISION COMM'N REP. (1984) *available at* http://elrc.ca.gov.pub/Printed-Reports/Pub143.pdf (stating that a system requiring tracing assets after divorce "creates procedural burdens of tracing former community property in the hands of the nondebtor spouse and raises problems whether any increase in value of the property, due to improvements, inflation, or otherwise, is also liable and whether the property should be traceable through changes in form after it has lost its community identity").

63. *See id.* The California Law Commission Report also describes the California managerial regime of making all community property available to creditors as based on a need to avoid "the serious administrative problems of characterizing the type of property and debt and partitioning the community property, and gives greatest assurance that creditors will be satisfied." *Id.* Inexplicably, the Commission then suggests that "[t]he administrative and policy reasons for undifferentiated liability of community property are thus eliminated upon dissolution and division of the property and debts." *Id.* This is an odd comment. Creditors that incurred obligations during the marriage, when they could count on the entirety of assets generated by the debt incurring spouse, are not given greatest assurance that they will be satisfied by a regime that has the potential to eliminate access to any of those assets that are given to the non-debtor spouse at divorce. The explanation of the managerial regime is sensible when applied to making *community* assets available to satisfy *separate* obligations of one of the spouses. The main feature of a managerial regime, in contrast to a community debt/separate debt system, is that a managerial regime allows creditors access to the community assets for separate debts. See Ratner, *But From Where Will the Money Come*, *supra* note 2, at 27–35 (assessing and contrasting managerial regimes and community debt/separate debt regimes). For *community* debts, the availability of all community property to creditors is routine—all community property jurisdictions make it available, and

take place after a divorce, and untangling will be required in order to identify the portions of the commingled assets that will be available to creditors seeking satisfaction of a community debt after the divorce. There may be a need to apportion between what would have been separate property during the marriage and what would have been community property during the marriage. Increases in the values of assets may be due to post-marriage improvements with separate money or due to post-marriage increases in market value, and decisions will have to be made.

In general, although tracing matters can be complex, and sometimes the tracing evidence will be skimpy and yield unsatisfactory results, this is not a sufficient reason to offer a creditor a windfall from a divorce.[64] It is important to consider that tracing often involves routine rather than complex accounting, and that each community property jurisdiction already has a well-developed process with well-established marital property structures for undertaking the tracing.[65] Every divorce currently creates the potential for tracing difficulties, as does any debt that a creditor seeks to satisfy out of marital assets during a marriage. Thus, a rule that permits a non-debtor spouse to use the same tracing process concerning assets a community creditor seeks after a divorce is not particularly undermined by the idea that sometimes it may be difficult. A tracing-based, divorce-neutral system is preferable to one that enables creditors by virtue of divorce to obtain access to assets unavailable during marriage. It is also preferable to the alternative of precluding creditors from access to assets for which they would have had access, during the marriage, in a process that places enormous pressure on debt allocation at divorce.

Some aspects of tracing complexity can be ameliorated via the assignment of burdens for tracing.[66] Whenever asset characterization hinges on tracing, an initial default must be set and a burden assigned, so the question of the proper place and level of burden can be expected to arise whenever a creditor seeks the non-debtor spouse's assets post-divorce. The burden for tracing should be placed carefully to facilitate ease on the

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that process involves occasionally tricky, but hardly insurmountable, characterization problems or partitioning of the community property.

64. *See, e.g.*, REPPY & SAMUEL, *supra* note 1, at 159–74.

65. Every community property jurisdiction undertakes tracing for purposes of deciding what is separate property and what is community property. Typical problems include commingling and intertwining of community and separate property. *See id.* at 159–74; Blumberg, *supra* note 2 at 170–71.

66. In divorce situations, there is neither a plaintiff nor a defendant to assume particular burdens, so a burden and a level of proof must be assigned. *See* DE FUNIAK & VAUGHN, PRINCIPLES OF COMMUNITY PROPERTY, 177 (University of Arizona Press: Tucson, 2nd Ed 1971). A longstanding standard community property presumption is that all assets acquired during the marriage are presumed community property, therefore the party arguing something different is held to an elevated evidentiary level, often described as "clear and convincing" to prove otherwise. *See id.* at 117; Porter v. Porter, 195 P.2d 132, 136 (Ariz. 1948). This presumption is applicable to creditors seeking satisfaction against the community as well as to spouses in a divorce. *See* Ratner, *But From Where Will the Money Come*, *supra* note 2, at 31 n.52.

creditor and on the non-debtor ex-spouse. One approach is to follow the current community property approach of presuming that assets acquired during a marriage are community assets.[67] That approach would place the burden on the ex-spouse, rather than the creditor, to show that the disputed asset is not available to the creditor. Creditors who seek satisfaction during the marriage often benefit from this default because it enables them to go after all marital assets and make the non-debtor spouse prove either that the debt was not a community debt, or the assets the creditor seeks are the separate property of the non-debtor spouse and unavailable to the creditor.[68] Since the non-debtor spouse has original access to all tracing data, placing an *a priori* obligation on creditors to determine the status of the asset may be costly.

On the other hand, in post-divorce situations, the creditor is seeking assets from a non-debtor to whom the debt may not have been allocated at divorce. In this context, it seems overly intrusive to enable the creditor to take all the non-debtor spouse's assets and force her to prove the separate nature of the assets. In the face of that burden, the ex-spouse might pay the debt rather than incur the expense of proving the unavailability of the asset.

Given the ex-spouse's non-debtor status, a sensible approach is to place the initial burden on the creditor to demonstrate a basis for obtaining the asset the creditor seeks. If the creditor shows that the asset in question was generated during the marriage, the burden should shift to the non-debtor ex-spouse to show that she is the non-debtor spouse and that the asset in question would not have been available to this creditor during the marriage. The burden of proof should be a straight preponderance-of-the-evidence standard rather than the typical heightened evidentiary burden placed on a spouse who attempts to prove the separate nature of a presumed community asset. If a creditor is unable to demonstrate that the asset it seeks was generated during the marriage, the creditor has failed to demonstrate a reason why it should get the benefit of a presumption, and

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67. *See* DE FUNIAK & VAUGHN, *supra* note 66, at 117.

68. *Id*. Why the creditor should get the benefit of a presumption originally designed for disputes between spouses is something of a mystery. Between spouses, the presumption and heighted evidentiary burden is justified by the need to provide a burden in situations where there is neither a plaintiff nor a defendant, by the idea that a community property presumption is empirically supportable as a default, and by the presumption that the burden is community maximizing and a compromise, since the community characterization means each spouse receives half. *See* James Ratner, *Community Property, Right of Survivorship, and Separate Property Contributions To Marital Assets: An Interplay*, 41 ARIZ. L. REV. 993, 1010 (1999) [hereinafter Ratner, *Community Property*]; Johnson v. Johnson, 131 Ariz. 38 (Ariz. 1981). These bases, however, are not particularly applicable when the issue is a creditor against a non-debtor spouse, and the application to those situations appears to have been fairly carelessly applied, leaving the creditor with the benefit of what was originally a community maximizing presumption. *See* Ratner, *But from Where Will the Money Come?*, *supra* note 2, at 31–32 n.52; Carroll, *The Superior Position of the Creditor*, *supra* note 18, at 17–18. One decent basis for the pro-creditor presumption is that the spouse objecting to the creditor's attempt to reach assets virtually always has better access to characterization tracing evidence than does the creditor. Ratner, *But from Where Will the Money Come?*, *supra* note 2, at 31–32 n.52.

the presumption should be that the asset is unavailable to the creditor. The creditor could overcome this presumption with proof that the asset would have been available to the creditor if there had been no divorce. The creditor should be held to a heightened evidentiary standard in order to discourage creditors from simply grabbing assets when there is doubt as to whether it is justified. This combination of burdens and presumptions minimizes the discovery and tracing expenses facing creditors, because those expenses will not be imposed on a creditor simply by virtue of the creditors' suit for satisfaction from the non-debtor spouse. At the same time, the combination precludes the creditor from any particular benefit if tracing evidence is somewhat hard to come by.

One challenging problem surrounds income earned post-divorce by a non-debtor spouse who was not working during the marriage (and assets traced to that income). While the creditor can persuasively argue that any income generated by the non-debtor spouse would have been community income available to the creditor had there been no divorce, the non-debtor spouse can also persuasively argue that there was no reliance by the creditor on that source of income during the marriage when the creditor extended the credit. The divorce may have been a major impetus leading to the non-debtor spouse's decision to generate assets. Perhaps for this reason, Wisconsin precludes community creditors from obtaining a non-debtor spouse's post-divorce income to satisfy a community obligation if the debt is not allocated to the non-debtor at divorce.[69] Wisconsin's approach, however, broadly offers the non-debtor spouse a windfall from divorce as long as the non-debtor avoids allocation of the debt at divorce.[70] A better approach is to place a burden on a creditor to demonstrate its time-of-the-debt reliance on the income-generating capabilities of the non-debtor spouse. This will address the issue without precluding creditor access in situations in which the creditor originally extended credit to the marital community in part on the basis of the earning capability of the non-debtor spouse.

A non-debtor spouse will naturally intertwine all of her assets, regardless of the source, once a divorce is final. This may create difficulties if the non-debtor spouse needs to trace in order to prevent a community creditor from obtaining a particular asset. For example, the non-debtor ex-spouse may make payments on or improve a separate property asset using what would have been community property resources. The creditor may

69. WIS. STAT. ANN. § 766.55(2)(2m) (West 2009).

70. The Wisconsin approach provides some insulation to the non-debtor ex-spouse, but it is at the cost of a debtor windfall from divorce, thus creating incentives for couples to divorce as well as incentives for creditors to attempt participation in the allocation of debts upon divorce. See *infra* part IV. The approach also hinges the collectability of a particular debt on the divorce court decision concerning allocation of the debt, undesirably creating incentives for creditors to participate in and influence divorce court allocations of assets and liabilities. *Id.*

argue that because an increase in value attributable to what would have been community assets resides in the separate property, the creditor is entitled to some portion of the value of the asset for which payments or improvements were made. This approach is applied at divorce to protect a community when separate property is paid for or improved with community resources during the marriage.[71] Another example is that an ex-spouse can be expected to combine what would have been community money with separate property money after a divorce. Such "commingling" activity seems fully understandable, as there is no longer a marriage. Nevertheless, a creditor might argue, consistent with the presumption applied between spouses at divorce, that all the funds in a commingled account and all the assets traced to that account are presumed community.[72] This would force the non-debtor spouse to trace to preserve her separate property.[73] Presumptions for commingled accounts, similar to general presumptions that all assets acquired during the marriage are community property, were developed to protect one spouse from the other spouse and have a community maximizing bias.[74] The presumptions are not particularly appropriate for situations pertaining to a creditor going against a non-debtor spouse. To the contrary, it is unwise to entitle a creditor the benefit of a commingling presumption, as it would enable a creditor to grab all assets belonging to the non-debtor spouse and force a non-debtor to prove otherwise. Instead, the burden should be on the creditor to trace any asset it seeks to an asset that would have been available had there been no divorce. This burden placement protects the non-debtor spouse while minimizing the possibility that a debt allocation at divorce will compromise a creditor's ability to obtain satisfaction.

The tracing approach for post-divorce satisfaction of community debt does not impose a radical change. It leaves intact the standard community property result that the non-debtor spouse suffers for the foolhardy spending of the debtor spouse.[75] Under this approach, creditors are able to seek a non-debtor spouse's earnings during the marriage. In the event of a divorce, creditors will continue to be able to force the non-debtor spouse to

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71. *See* REPPY & SAMUEL, *supra* note 1, at 139–58. Each community property jurisdiction has a method for "reimbursing" the community in such instances to protect the community and prevent a spouse from appropriating community property by spending it for the benefit of his separate property. *See* Ratner, *Community Property*, *supra* note 68, at 1010–11, 1053–54. These rules could be, but need not be, imported into the post-divorce tracing issues, offering protection for a non-debtor spouse yet preserving assets for a community creditor after divorce.

72. REPPY & SAMUEL, *supra* note 1, at 160, 162; Cooper v. Cooper, 635 P.2d 850, 852–53 (Ariz. 1981) ("[T]he burden is upon the person claiming that the commingled funds, or any portion of them, are separate to prove that fact and the amount by clear and satisfactory evidence.").

73. *See* REPPY & SAMUEL, *supra* note 1, at 159–68 (tracing can be accomplished by directly tracing the separate property money or indirectly, by demonstrating that the community money has been used up).

74. *See id.*

75. *See supra* Part II.

pay and seek reimbursement from the spend-happy spouse.[76] Thus, a creditor who transacts with the community can rely on continued access to those assets. In addition, consistent with typical treatment concerning community debts and other obligations, the creditors will be able to obtain access to the assets that would have been characterized as the debtor ex-spouse's separate property during the marriage, if there are not enough assets traceable to community property or assets that would have been community property but for the divorce to satisfy the obligation. In contrast, assets that were (1) the separate property of the non-debtor spouse at the time of divorce, (2) assets that are traceable to that separate property, and (3) assets that are acquired by the debtor spouse after the divorce that would have been separate property even if obtained during the marriage, however, will not be available to the creditor.[77] Those assets are not separate property solely by virtue of the divorce and would not have been available to the creditor during the marriage.

This proposed tracing regime for post-divorce collection of community debts could be implemented through an expansive, although not appallingly unrealistic, interpretation of statutes that supply a hierarchy of the assets for community debts.[78] One point of such statutes is that they identify for creditors the assets on which they can and cannot rely when dealing with one spouse and the marital community.[79] The statutes also affirmatively protect a non-debtor spouse's interest in her separate property.[80] A tracing regime for post-divorce collection is entirely consistent with both of those statutory goals. Where such an interpretation would be too big a leap, or in jurisdictions that explicitly maintain alternative structures, legislatures should enact a post-marital debt statute that mirrors the premarital debt statute to clarify that there should be no windfall.

IV. DUELING WINDFALLS: SOLUTIONS TO AVOID

To protect the non-debtor spouse, and presumably to address the problem of a creditor windfall at divorce, some community property jurisdictions have overcorrected and offered a divorce windfall to the non-debtor spouse. The best example is California, which statutorily adjusts its managerial structure concerning application to post-divorce debt

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76. *See id*.

77. *See id*.

78. *See, e.g.*, ARIZ. REV. STAT. ANN. § 25–215(D) (2011) (providing that marital debts will be satisfied "first, from the community property, and second, from the separate property of the spouse contracting the debt or obligation"). Interpreting this language to require the same tracing post-divorce that is required during the marriage does not require a tortured reading of the language and overall statutory scheme.

79. *See* Ratner, *But from Where Will the Money Come?*, *supra* note 2, at 23–38.

80. *Id*.

collection.[81] In California, a creditor seeking satisfaction during the marriage has access to all assets managed by the debtor spouse, including all of the community assets and the debtor spouse's separate property assets.[82] Consistent with that managerial regime, after a divorce-initiated property division all of the assets belonging to the debt-incurring spouse are available to creditors.[83] This result applies regardless of whether the assets are traced to what was community property divided at divorce or to separate property, and regardless of the debt allocation at divorce.[84] In addition, in a departure from the managerial regime, a marital creditor has access to all of the *non-debtor* spouse's assets if (and only if) the non-debtor spouse is assigned a portion of the community obligation in a divorce proceeding.[85] If the non-debtor spouse is not assigned a portion of a community obligation, however, neither the separate property nor "the property received by the person in the division" of the non-debtor spouse is available to the creditor unless that spouse was assigned the debt by the divorce court as part of the debt distribution at divorce.[86] Based on case law, it appears that Idaho maintains a similar approach.[87] Wisconsin adopted a similar but tweaked structure: although marital property assigned to each spouse at divorce is available to the extent of the value of those assets at divorce, "income" of

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81. CAL. FAM. CODE § 916(a) (West 2009). *See also* Carroll, *Incentivizing Divorce*, *supra* note 8, at 1931–34. Professor Carroll also points out that there is a surprising lack of legislative history given that the statute at least on the surface encourages divorce. *Id.* at 1933–34.

82. CAL. FAM. CODE § 910(a) (West 2009). *See also* Carroll, *Incentivizing Divorce*, *supra* note 8, at 1931 (providing that "creditors seeking satisfaction of debts incurred 'before or during marriage' may freely seize the California spouses' community property, regardless of which spouse incurred the debt and regardless of the rights of the spouses to manage the property subject to seizure").

83. CAL. FAM. CODE § 916 (a)(1) (West 2009).

84. *Id*.

85. CAL. FAM. CODE § 916 (a)(3).

86. CAL. FAM. CODE § 916 (a)(2).

87. *See* Twin Falls Bank and Trust v. Holley, 723 P.2d 893, 896 (Idaho 1986); Spokane Merchants Ass'n v. Olmstead, 327 P.2d 385, 387–88 (Idaho 1958); Carroll, *Incentivizing Divorce*, *supra* note 8, at 1934–39. *See also* Lamont C. Loo, *Casenote & Comments: Contractual Creditor Rights Upon Dissolution of Marriage: Revisiting Twin Falls Bank & Trust v. Holley, Proposal: A Tripartite Analysis*, 30 IDAHO L. REV. 777 (1994). In *Twin Falls*, the Idaho Supreme Court concluded, albeit under highly stylized circumstances, that a creditor of a community debt is restricted to the assets of the debtor spouse in the event of a divorce. *See Twin Falls*, 723 P.2d at 896–97. The decision suggests that although a debt may be characterized as a community debt, the characterization does not render the community a "community debtor." *Id.* Creditors for debts incurred during the marriage are thus apparently precluded from seeking assets from the non-debtor spouse after divorce. If a debt was allocated to a spouse at divorce and the spouse failed to obtain sufficient community assets to cover the debt, however, the creditor may seek to be paid from the community assets distributed to the non-debtor spouse at divorce to prevent fraud. *Id.* Neither *Twin Falls Bank* nor *Spokane Merchants* addresses whether creditors have access to what would have been the separate property of the non-debtor spouse when the non-debtor spouse is allocated all or a portion of the debt by a divorce decree. *See id.*; *Spokane Merchants,* 327 P.2d at 387–88.

the non-debt incurring spouse is not available to a creditor after divorce unless specifically made available by a divorce decree.[88]

The California approach is a flip-flop. It has the desirable attribute of preventing, in some situations, a creditor from obtaining the separate property of a non-debtor spouse, thus avoiding creditor windfalls from the divorce in those situations. But the approach also precludes the creditor from access to *any* of a non-debtor ex-spouse's assets unless that ex-spouse is assigned the community debt at divorce.[89] This offers the non-debtor spouse a windfall from the divorce. The assets received by the non-debtor spouse at divorce that are traceable to community property would have been available to the creditor if there had not been a divorce but are no longer available to the creditor because of the divorce. At the same time, if the non-debtor spouse *is* assigned a portion of a debt, all of that spouse's assets are available, including *separate property* of the non-debtor spouse that would be unavailable to the creditor had there been no divorce.[90]

Under the California approach, in a standard spouse-negotiated divorce settlement that assigns half the debts to each spouse, the creditors for debts assigned to the non-debtor spouse will get a windfall, and the creditors for debts assigned to the debtor spouse will lose access to the community assets assigned to the non-debtor spouse that would have been available during the marriage. If the debts are assigned so that each spouse has 50% responsibility for each debt, each creditor gets a windfall.[91] If the non-debtor spouse is assigned no debt, all creditors are undermined. If the spouses agree that all community assets and none of the debt should go to the non-debtor spouse, the effect would be to render the debt unenforceable. At this point, however, a creditor might argue that the marital settlement agreement should be considered a fraudulent transfer, an argument available under California law.[92] Thus either the creditor or a debtor will receive a windfall under the California solution. The recipient of the windfall hinges on the final decision concerning debt allocation at divorce. Not surprisingly, this approach is less than optimal for several reasons.[93]

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88. WISC. STAT. ANN. § 766.55(2)(2m) (West 2009). The statute doesn't specify whether post-divorce creditors can obtain what would have been the separate property of the non-debtor spouse.

89. *See* CAL. FAM. CODE § 916 (a)(3). See also Lamont C. Loo, *supra* note 87, at 796–97.

90. *See Liability of Marital Property for Debts*, 17 CAL L. REVISION COMM'N REPORTS 1, 22–23 (1984) *available at* http://clrc.ca.gov/pub/Printed-Reports/Pub143.pdf (proposing this result and defending it by suggesting that tracing may be too difficult for the creditor).

91. CAL. FAM. CODE § 916(a)(2) (West 2010). The statute is vague about whether the creditor is precluded from access to the non-debtor's assets for an amount greater than 50% of the debt. The statutory language appears to assume that a debt is allocated in its entirety to one spouse or the other "unless the debt was assigned for payment by the person in the division of the property." *Id.*

92. *See generally* Mejia v. Reed, 74 P.3d 166 (2003).

93. While the California approach has drawbacks concerning satisfaction of *community* debts, it is entirely sensible when applied to *separate* debts incurred by a spouse during the marriage. Pursuant to California's managerial regime, creditors of either spouse are entitled to seek all assets managed and controlled by the debtor spouse. *See* CAL FAM. CODE § 910 (West 2009); *See* Ratner, *But from Where*

A. Increased Incentives to Divorce

The California approach may have been adopted with hopes of streamlining procedural burdens and avoiding practical difficulties,[94] but the offer of a potential windfall to the non-debtor spouse undermines rather than assists those objectives by creating incentives for two needless and expensive legal matters: (1) divorce, and (2) a fraud claim accompanying what would otherwise be a routine collection action. Offering a windfall to the non-debtor spouse creates incentives for couples to divorce in order to escape creditors and for creditors to respond by challenging the technique.[95] The incentive to divorce is straightforward: a couple could divorce and allocate as many community assets as possible to the non-debtor spouse, while not allocating to that spouse any marital debts the couple wishes to avoid.[96] The divorce insulates the entire community share received by the non-debtor spouse from creditors. The same assets would be available to the creditors if the couple stays married. A couple could continue to live together and manage their financial affairs exactly as they had while married, although in theory the debtor spouse would no longer have management and control over the assets insulated by this technique. A creditor, frustrated by the divorce strategy, might then challenge the divorce itself as sufficiently analogous to a "fraudulent conveyance" to justify ignoring it for purposes of obtaining access to both sides of the community assets.[97]

A law that encourages divorce is not automatically a bad idea. While it is important to explicitly identify and evaluate incentives for divorce created by any law, concern over laws that provide incentives to divorce, like concern over laws that discourage marriage in the first place, should be

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Will the Money Come?, *supra* note 2, at 29 n.46. This means that a separate creditor is entitled to all of the community property, including any salary and other community assets generated by the non-debt-incurring spouse, in addition to the debtor spouse's separate assets. This result is quite favorable to separate creditors, who receive windfall access to community assets generated by a non-debtor spouse. *Id.* at 30. At divorce, however, there is no need to continue to perpetuate the managerial windfall for separate creditors. As a result the community assets the non-debtor spouse receives from the divorce, including salary generated after the divorce, are no longer available to the separate creditor unless the debt was allocated at divorce to the non-debtor spouse, an unlikely event for any genuinely separate obligation.

94. CAL. L. REVISION REPORT, *supra* note 62, at 23.

95. Carroll, *Incentivizing Divorce*, *supra* note 8, 1928–44. Professor Carroll expresses a dual-sided attitude concerning California's and Idaho's approach. Her main point is that the approach creates incentives to divorce and all such incentives should be explicitly identified, evaluated, and minimized if possible. *Id.* at 1941. For this reason, Professor Carroll is wary of the approach of protecting assets given to a non-debtor spouse who is not allocated a debt at divorce, especially considering the potential effect on people who might otherwise not divorce. *Id.* at 1939–40. At the same time, Professor Carroll's desire to offer general protections to non-debtor spouses leads her away from a condemnation of the approach and toward tentative approval. *Id.* at 1941.

96. *Id.* at 1941–42.

97. *Id.*

tempered with skepticism.[98] Some laws that may facilitate divorce, such as the no-fault regimes enacted throughout the United States in the 1970s that preclude fault as a factor in property distribution, may prove quite useful.[99] If at least one spouse concludes that the negative financial implications of marriage swamp the benefits, an end to the marriage may be the optimal result. A debt allocation regime encouraging that result is not automatically undesirable.

In any event, it is not clear that the California system concerning post-divorce-asset-availability has led to enormous increases in the divorce rate.[100] The incentive to divorce is in fact created not by the debt-allocation-at-divorce statute, but instead by California's managerial system, which offers a creditor access to the assets in question only by virtue of the marriage.[101] From the perspective of a concern with avoiding laws that encourage divorce, the real question is whether California's managerial system contains undesirable disincentives to marry in the first place. A system that precludes a creditor from access to the entirety of community

98. No-fault divorce laws did not necessarily increase divorce rate, and many scholars have extensively debated why this is the case. *See* Justin Wolfers, *Did Unilateral Divorce Raise Divorce Rates? A Reconciliation and New Results*, 96 AM. ECON. REV. 1802 (2006). Professor Wolfers concludes that state "unilateral divorce" laws caused only a temporary increase in divorce rates rather than effectuating permanent incentives to divorce. *Id*. Increased divorce rates may have prompted the changes rather than been prompted by the changes. See Ira Mark Ellman & Sharon L. Lohr, *Dissolving the Relationship Between Divorce Rates and Divorce Laws*, 18 INT'L REV. L. & ECON. 341 (1998) (giving a state by state analysis of divorce changes and divorce rates); Ira Mark Ellman, *Divorce Rates, Marriage Rates, and the Problematic Persistence of Traditional Marital Roles*, 34 FAM. L.Q. 1 (2000). For an example of skepticism concerning laws promoting marriage see e.g. Ratner, *But from Where Will the Money Come?*, *supra* note 2, at 66–72 (arguing that if a main reason to marry is to frustrate a creditor, particularly a creditor who is a parent seeking to enforce a child support order, such a marriage need not be encouraged). In general, many arguments that offered by those that argue for a majoritarian societal preference for marriage are unconvincing. *See, e.g.*, Anita Bernstein, *For and Against Marriage: A Revision*, 102 MICH. L. REV. 129 (2003) (reviewing many different arguments for and against state-sponsored marriage); MARTHA ALBERTSON FINEMAN, THE NEUTERED MOTHER, THE SEXUAL FAMILY AND OTHER TWENTIETH CENTURY TRAGEDIES, 228 (1995); Nancy Polikoff, *Why Lesbians and Gay Men Should Read Martha Fineman*, 8 AM. U.J. GENDER SOC. POLICY 167, 176 (2000); Dianne Post, *Why Marriage Should Be Abolished*, 18 WOMEN'S RIGHTS L. REP. 283 (1997).

99. *See* BLUMBERG, *supra* note 2, at 14–15, 79 (discussing the no fault regimes enacted in the 1970's); *see, e.g.*, ARIZ. REV. STAT. ANN. § 25-318(A) (2011) (stating that a divorce court shall divide all marital property "without regard to marital misconduct").

100. Carroll, *Incentivizing Divorce*, *supra* note 8, at 1941 ("Policy-makers certainly should not overindulge in the worry that mass divorces will result from post-termination collection rules like those in California . . . .").

101. Ratner, *But from Where Will the Money Come?*, *supra* note 2, at 27–31. The debt allocation statute gives relief from the managerial system to the non-debtor spouse who is not allocated all or part of a marital debt. CAL. FAM. CODE § 916(a)(2) (West 2004). In effect, the statute pretends that all the community assets the non-debtor spouse receives in the divorce, and any of her separate property, are assets she generated in the absence of the marriage, and because she is not the debtor, creditors have no claim against any of her assets. *Id*. Thus the question of whether to give the non-debtor spouse a windfall from the divorce arises only because of the rule that all community property is available to satisfy a marital debt. At the same time, however, the community property regime itself, which offers a spouse undivided half interest in assets generated by the other spouse, provides strong incentives for some spouses to marry. *See* Ratner, *But from Where Will the Money Come?*, *supra* note 2, at 32–33.

property during marriage features less of a disincentive to marry compared to the managerial regime. It is unclear the extent to which the managerial regime maintained in California creates a disincentive to marry and whether that is undesirable.[102] The immediacy of avoiding debt and the unavailability of other forms of transmutation as an alternative, however, suggests that the incentive to divorce created by California's post-divorce asset-availability rule may be greater than the extent to which the managerial system creates incentives to not marry in the first place.

The understandable justification for a debt allocation approach that offers a divorce windfall to the non-debtor spouse is a desire to protect the non-debtor spouse.[103] What California offers to the non-debtor spouse, however, is far short of complete protection. To the contrary, the statute specifically authorizes a windfall for creditors for every community debt allocated in whole or in part to the non-debtor spouse at divorce.[104] The California approach thus offers a set of incentives for the non-debtor spouse to consider concerning the financial advisability of divorce. A divorce may enable protection of assets depending on how successful the ex-spouses are at beating a creditor's claim that the divorce itself was a fraudulent transaction. Divorce may also render the non-debtor spouse worse off as it can enable creditor access to assets unavailable if the marriage is kept intact. Assessing the gamble requires assessing a debt allocation decision seemingly made on a standardless basis.[105]

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102. *Id.* at 28, 67. Couples have always faced the question of whether to refrain from marrying in order to protect assets from creditors, yet many people continue to marry.

103. *See* Mont E. Tanner, *Twin Falls Bank & Trust v. Holley: Restricting Creditors' Rights Under A Property Settlement Agreement—A Departure That Sets Idaho Apart*, 26 IDAHO L. REV. 595 (1989); Carroll, *Incentivizing Divorce*, *supra* note 8, at 1940–41.

104. CAL. FAM. CODE § 916(a)(2). *See supra* text accompanying Part II for discussion of the windfall for creditors and why it is undesirable.

105. There are few or no standards for allocating marital debt to one or the other spouse at divorce. California, New Mexico, and Louisiana require an equal division of community property. *See* CAL. FAM. CODE § 2550 (West 2009); LOUISIANA CIV. CODE ANN. art. 2336 (2009); Ruggles v. Ruggles, 860 P.2d 182, 188 (N.M. 1993); REPPY & SAMUEL, *supra* note 1, at 351. Generally, this requires division of both the assets and the liabilities. In California, liabilities are divided equally by assigning each of the debts to one spouse or the other, with exceptions for educational loans, tort liability not incurred in furtherance of the marital community, and for divorces in which total liabilities exceed total community assets. BLUMBERG, *supra* note 2, at 566. In the latter situation, "the excess of debt shall be assigned as the court deems just and equitable, taking into account factors such as the parties' relative ability to pay." CAL. FAM. CODE § 2622(b) (West 2010). Wisconsin provides for presumptive equal division of property, but permits departure from an equal distribution based on numerous factors, including length of marriage, property brought into the marriage, separate property, contributions to the marriage or the education or earning ability of one of the spouses, the age and health of the spouses, and the earning abilities of each spouse. WISC. STAT. ANN. § 767.61 (West 2010). The presumption of equal division, but ability to depart from it, is apparently applicable to debts as well as assets. *See* Hauge v. Hauge, 427 N.W.2d 154, 156 (Wis. Ct. App. 1988). In Arizona, division of assets and debts is made "equitably although not necessarily in kind." ARIZ. REV. STAT. ANN. § 25-318(A) (2010). The statute requires equal division unless there are "sound reason[s]" to depart. *See* Toth v. Toth, 946 P.2d 900, 903 (Ariz. 1997). Idaho and Nevada have structures similar to Arizona, while Texas and Washington permit unequal divisions of property. *See* TEX. FAM. CODE ANN. § 7.001 (Vernon 2010); REPPY & SAMUEL,

While it is not entirely clear the extent to which a divorce debt allocation regime destructively tempts happily married couples to consider divorce purely to preserve assets, the temptation can easily be removed by instituting the divorce-neutral tracing system I propose.[106] Regardless of whether a community property jurisdiction uses a managerial regime, community debt/separate debt regime, or partition regime, forcing a creditor to trace in order to show that an asset would have been available if there had been no divorce eliminates both the incentive to divorce created by protecting assets for debts not allocated to the non-debtor spouse and the incentive to stay married created by giving creditors access to the non-debtor spouse's separate property.[107] If a particular debt allocation scheme genuinely discourages marriage (a dubious proposition) and the discouragement is thought to be unfortunate (also a dubious proposition), the way to address the unfortunate incentive is by adjusting the general level of protection offered to non-debtor spouses at the outset, rather than addressing it in an inconsistent, haphazard, and standardless way at divorce.[108]

B. Overemphasis on Debt Allocation at Divorce

Perhaps the most undesirable attribute of the California approach is that it places far too much pressure on divorce court decisions concerning allocation of debt at divorce. The vast bulk of allocations will take place without genuine judicial deliberation concerning the allocation of debts and assets. The premise of the California system, however, is that allocation of debts and assets should be made after careful consideration of whether creditors will be frustrated by the allocation and whether the allocation properly leaves both spouses with equal debt burden and assets.[109]

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supra note 1, at 351. In all jurisdictions, decisions concerning which community debts are allocated to which spouse are left to the discretion of the divorce court.

106. *See supra* Part III.

107. *See supra* Part III.

108. Texas, by way of example, has a more "nuanced" system that protects some of the community assets generated by one spouse from the debt incurring activity of the other spouse during the marriage. *See* Musselman, *Once Upon a Time in Bankruptcy Court*, 41 FAM. L.Q. 249 (2007). For debts (other than torts) incurred during marriage, neither the separate property of a non-debtor spouse nor the community property over which the non-debtor spouse has "sole management and control" are available to creditors, even if the debt was in furtherance of the community. *Id.* at 256. A spouse has "sole management and control" over a community asset if that spouse generated the asset as income, received it via a personal injury award, or the asset in question is traced to one of those sources. *See id.* at 257–58.

109. One purpose of California's divorce debt-allocation statutory structure is to accommodate creditors "so there will be available sufficient property to satisfy the debt by the person to whom the debt is assigned." Lezine v. Sec. Pac. Fin. Serv., Inc., 14 Cal. 4th 56, 75 (Cal. 1996). *See also* Mejia v. Reed, 74 P.3d 166 (Cal. 2003); *In re* Beverly, 374 B.R. 221 (B.A.P. 9th Cir. 2007). The general California distributional structure is to divide each asset equally except "when economic circumstances warrant." CAL. FAM. CODE § 2601 (West 2010); BLUMBERG, *supra* note 2, at 546–47. Liabilities can

There is no decent way to take account of creditors in the middle of a standardless process that most often will feature a settlement agreement between the spouses. Community creditors seeking windfalls have incentives to participate and to have as much debt as possible allocated to the non-debtor spouse. The non-debtor spouse has incentives to avoid allocations of as much community debt as possible and claim the windfall for herself. Debtor spouses, especially those headed for bankruptcy regardless of the debt allocation, may be willing to accommodate.[110]

There are other unfortunate attributes of the California approach of considering creditor needs when allocating debts at divorce. The structure subtly encourages divorce courts to consider whether a spouse has separate property that could pay off a debt.[111] This may tempt a divorce court to force a "division" of separate property assets through an allocation of marital debt in whole or in part to the non-debtor spouse, seemingly inconsistent with the statutory mandates to protect separate property.[112] The potential use of the debt allocation structure to implement a departure from a 50-50 split of the community assets and liabilities based on the fact that one spouse has separate property seems great. In addition, the California structure also has the potential to penalize a creditor who does not insist on moving to judgment quickly and instead gives debtors time to work it out. If a creditor waits too long, the couple may divorce, and the divorce might result in an unfavorable (for the creditor) debt allocation that significantly reduces the creditor's ability to collect.[113] For significant debt, these effects may be pushed back to the time of the transaction—imposing costs on lenders who try to predict the possibility of divorce and the effect a

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apparently be divided on a liability-by-liability basis, although nothing statutorily appears to prohibit a trial judge from dividing each liability in-kind as well. *See* BLUMBERG, *supra* note 2, at 566.

110. *See generally* Mechele Dickerson, *To Love, Honor, and (Oh!) Pay: Should Spouses Be Forced to Pay Each Other's Debts?*, 78 B.U. L. REV. 961 (1988). The credit rating of the debtor spouse may be at stake here, discouraging the couple from adopting this approach, but the concern may have only marginal influence, as the debtor spouse cannot avoid liability even if the debt is allocated to the non-debtor spouse. CAL. FAM. CODE § 916(a)(1) (West 2010).

111. Wisconsin's statutory structure does the same thing by providing for departures from a 50-50 split of community assets and liabilities based in part on the assets that one or the other spouses may own that are not subject to division at divorce. WIS. STAT. ANN. § 767.61(3)(c) (2010).

112. A feature of community property jurisdictions is that they do not permit hotch pot distributions—separate property is directed by statute to go to the separate property owner at divorce. *See, e.g.*, ARIZ. REV. STAT. ANN. § 25-318(A) (2010).

113. For example, in *Twin Falls Bank & Trust* the creditor twice renegotiated rather than seeking judgment and payment after an original default on a debt incurred during the marriage. Twin Falls Bank & Trust v. Holley, 723 P.2d 893, 895 (Idaho 1986). The couple divorced prior to the second renegotiation and the debt-incurring spouse was allocated the debt. *Id.* When the debt-incurring spouse defaulted on the second renegotiated loan and filed for bankruptcy, the creditor sought satisfaction against the non-debt-incurring spouse but was unsuccessful. *Id.* The creditor could have obtained the spouse's community property if it had sought judgment and execution during the marriage. *Id.* at 896. Because the creditor had renegotiated after the divorce without any suggestion that the non-debtor spouse was also liable, the creditor waived its ability to seek the former community assets given to the non-debtor ex-spouse at divorce. *Id.*

particular allocation of debts and assets may have on the lender's ability to collect. Such cost may be ultimately borne by borrowers, and may push back the ease with which married people can obtain credit.[114]

An additional, substantial drawback of the California approach of issuing divorce debt allocations that influence the possibility of debt collection is that it can turn run-of-the mill default divorces into an odd, haphazard bankruptcy proceeding that could pit various creditors against one another. The approach of (1) fully protecting the non-debtor spouse's assets from community creditors for all debts not allocated to the non-debtor spouse, and (2) leaving the entirely unprotected all of the non-debtor spouse's assets in the even she is allocated a portion of the community debt, forces creditors and non-debtor spouses to care about the debt distribution at divorce.[115] Each creditor cares because its ability to collect will vary depending on which spouse is assigned the bulk of the debt owed to the particular creditor and whether enough community assets are going in the same direction as the debt. Non-debtor spouses with separate property care because if they are allocated any portion of any community debt, their separate property available to community creditors during the marriage is made available because of the divorce.

The idea behind the California approach, which is to eliminate "messy" tracing and hinge asset access to characterization and assignment of debt at divorce, has the potential to increase litigation and raise costs for divorcing couples.[116] Currently, the vast bulk of divorces are uncontested.[117] In all uncontested divorces, the parties eventually come to an agreement concerning the allocation of assets and debts. By hinging the availability of assets to the debt allocation, however, California has offered the potential for couples to create a debt allocation that will reduce the total assets available. That potential may render creditors wary of agreed-upon allocations of debt regardless of whether the couple contemplated defeating creditor access by the agreed-upon allocation. Creditors may object to what in fact are routine allocations of debts and assets, because the allocations may have a significant effect on a creditor even if the couples had no idea about this issue. Even when the creditor does not object, the statutory

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114. Ratner, *But from Where Will the Money Come?*, *supra* note 2, at 30–31, 33–34.

115. *See Recommendations Relating to Family Law*, 17 Cal. L. Revision Comm'n Reports 201 at 24 (1984) (advising a divorce court to "take into account the rights of creditors so there will be available property to satisfy the debt by the person to whom the debt is assigned").

116. *Id.* at 23. The use of tracing for purposes of allocating debts cannot be fully avoided in divorce court, however, as characterizations of debts as community or separate may require tracing. California resisted the concept of debt characterization, but ultimately found the need to statutorily mandate that a divorce court characterize unpaid obligations as community or separate in nature for purposes of allocation at divorce. *See* Cal. Fam. Code § 2551 (West 2010); BLUMBERG, *supra* note 2, at 566.

117. ABA Family Legal Guide, Family Law, 3.4 *Separation, Annulment, and Divorce*, http://public.findlaw.com/abaflg/flg-3-4c-2.html (last visited Jan. 2, 2011) (estimating that "close to 95 percent of divorces do not end up in a contested trial").

structure seems to require a divorce court to carefully scrutinize every entire agreed-upon asset and debt allocation to ensure it does not disadvantage a creditor. In the extreme, some divorce court judges might feel the need to require a hearing to assess the allocation of community debt in every ex parte or settled divorce to make sure that the agreed upon debt allocation does not prejudice the creditor. Divorce court judges, however, are not bankruptcy judges, and are likely to lack the expertise to make capable decisions concerning the well being of creditors. The structure thus has the potential to raise the chances of a hearing and extensive litigation for even the most routine uncontested divorces, thus thrusting increased time and expense on unsuspecting divorcing couples.

This is not to say that tracing is costless. If a creditor seeks access to assets that are traceable to the ex-spouse's separate property, a non-debtor ex-spouse may need to hire a lawyer and litigate. The need to hire a lawyer will not arise every time a couple divorces with debt, however, because the need only arises when creditors seek payment from a non-debtor spouse. If the debtor spouse pays the debts, the non-debtor spouse will have no tracing issue to contend with and no need for a lawyer. The advantage of adopting the tracing approach, compared to the approach of having the divorce debt allocation dictate the assets available to creditors, is that the role of the creditor at divorce can be fully eliminated, leaving the vast bulk of divorces free from the need for extensive review (which appears not to be happening in any event). Tracing for debt payment purposes will only arise in a small percentage of divorces and can be addressed in a creditor-debtor context that is more equipped to assess the entire situation. A creditor's presence in a creditor-debtor context is familiar and appropriate, unlike a divorce proceeding, because the issues of tracing and access are already undertaken frequently in a creditor-debtor context.

V. CONCLUSION

At the end of a marriage, marital debt must be allocated. In most community property regimes a divorce allocation does not preclude a creditor of the marital community from seeking satisfaction from either spouse.[118] As a consequence, the divorce enables a community creditor to obtain satisfaction of the debt from assets that are separate property of a non-debtor spouse although these assets are unavailable to the creditor during marriage.[119] Arizona offers this divorce windfall to creditors regardless of the debt allocation at divorce, and California explicitly offers the windfall whenever the non-debtor spouse is allocated all or a portion of

118. *See* discussion *supra* Part II.
119. *See* discussion *supra* Part II.

a community debt at divorce.[120] At the same time, California offers a divorce windfall to the non-debtor spouse at a creditor's expense whenever a community obligation is not allocated to the non-debtor spouse at divorce.[121]

Both approaches are undesirable. Arizona's approach is a trap for a non-debtor spouse—consistent with the purposes of preserving some assets as separate property, creditors should not be able to obtain post-divorce what they would not be able to obtain during a marriage.[122] The potential windfall California offers to the non-debtor spouse, while understandable as an attempt to protect non-debtor spouses from community creditors after the marriage is over, is particularly unfortunate. It creates incentives for couples to divorce to minimize the assets available to creditors, places pressure on allocation of debt between the spouses at divorce, and in the extreme could turn every divorce in which there is community debt outstanding into a bankruptcy-style procedure in which the needs of the creditors influence the divorce allocation of community assets and debts.

A simple solution will eliminate windfalls from divorces and avoid the incentives created by these windfalls.[123] A post-marital debt structure that is the mirror image of the premarital debt structure should be either read into current statutes or enacted to remove the windfalls. The result would entitle creditors to only those assets that would have been available had there been no divorce. While this will necessitate tracing each asset that a creditor seeks to obtain from a non-debtor ex-spouse, such tracing is a familiar activity already undertaken in creditor-debtor contexts whenever a creditor seeks contested assets against a married creditor. A tracing regime, while not perfect, will eliminate windfalls in either direction, thus rendering divorce a neutral event for spouses and creditors alike from a debt collection perspective. A tracing solution thus eliminates harm to non-debtor ex-spouses and avoids the encompassing problem of involving creditors in every divorce in which there is unpaid marital debt.

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120. *See* discussion *supra* Part II for Arizona, *supra* Part IV for California.

121. This result also occurs to some extent in Wisconsin and Idaho. *See* discussion *infra* Part IV.

122. *See* discussion *supra* Part II. California's approach preserves this windfall for creditors if the non-debtor spouse is assigned the debt at divorce, as do the Wisconsin and Idaho approaches. *See* discussion *supra* Part IV.

123. *See* discussion *supra* Part III.