Methods of Tracing
by

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A. THE TRACING PROBLEM

Tracing is an integral part to the more complex practice of family law. It is the long a winding road to the truth of asset characterization. Under Texas law, property possessed by either spouse during or on dissolution of the marriage is presumed to be community property, absent clear and convincing evidence to the contrary. Tex.Fam.Code Ann. § 3.003 (Vernon _____). The initial characterization of property as either community or separate is determined by the inception of title to the property. Smith v. Smith, 22 S.W.3d 140, 145 (Tex.App.-Houston [14th Dist.] 2000, no pet.) (op. on reh'g). The major consideration in determining the characterization of property as community or separate is the intention of spouses shown by the circumstances surrounding the inception of title. Scott v. Estate of Scott, 973 S.W.2d 694, 695 (Tex.App.-El Paso 1998, no pet.). Section 3.003 of the family code provides that (a) Property possessed by either spouse during or on dissolution of marriage is presumed to be community property; and (b) The degree of proof necessary to establish that property is separate property is clear and convincing evidence.

Given the presumptive characterization of the property, and the burden of proof for an effective rebuttal is clear and convincing evidence, Courts will apply a higher standard of legal and factual sufficiency review. In re J.F.C., 96 S.W.3d 256, 265-66 (Tex.2002); In re C.H., 89 S.W.3d 17, 26 (Tex.2002). Clear and convincing evidence is defined as that "measure or degree of proof which will produce in the mind of the trier of fact a firm belief or conviction as to the truth of the allegations sought to be established." Tex. Fam.Code Ann. § 101.007 (Vernon XXXX); Transp. Ins. Co. v. Moriel, 879 S.W.2d 10, 31 (Tex.1994). There is no requirement that such evidence be unequivocal or undisputed. Addington, 588 S.W.2d at 570. In reviewing the evidence for legal sufficiency, the tier of fact must determine "whether the evidence is such that a fact finder could reasonably form a firm belief or conviction" that the separate property characterization was proven. J.F.C., Supra at 265-66.

Therefore, the tracing problem becomes the accumulation and presentation of evidence which overcomes the community property assumption.

B. THE BURDEN OF PROOF

The burden of overcoming the presumption rests squarely on the spouse claiming such property as separate. The complaining spouse must trace and clearly identify the property claimed to be separate otherwise the presumption remains and the proper shall be judicially divided. The burden of tracing is often difficult, but not impossible. Irvin v. Parker, 139 S.W.3d 703, 484 (Tex.Civ.App.- Fort Worth 1977, writ ref'd n.r.e.); Latham v. Allison, 560 S.W.2d 481, 484 (Tex.Civ.App.- Fort Worth 1977, writ ref'd n.r.e.). Tracing involves establishing the separate origin of the property through evidence showing the time and means by which the spouse originally obtained possession of the property. Nelson v. Nelson, ____ S.W. 3d, 2006 Wl 771378, (Tex.App.-Eastland 2006); Ganesan v. Vallabhaneni, 96 S.W.3d 345, 354 (Tex.App.-Austin 2002, pet. denied). Separate property will retain its character though a series of exchanges so long as the party asserting separate ownership can overcome the community presumption by tracing the assets on hand during the marriage back to property that, because of its time and manner of acquisition, is separate in character. Invin v. Parker, Supra; Cockerham v. Cockerham, 527 S.W.2d 162, 168 (Tex.1975). Yet when evidence shows that separate and community property have been so commingled as to defy re-segregation and identification, the community presumption prevails. Hanau, 730 S.W.2d at 667. It is also not enough to show that separate funds could have been the source of a subsequent deposit of funds. Latham v. Allison, supra.

C. METHODS OF TRACING

Although not universally adopted by all lawyers, Tracing can be loosely broken down into six subtypes: (1) community out first rule; (2) minimum sum balance; (3) the clearinghouse (a/k/a identical sum inferences); (4) pro rata; (5) item tracing; and (6) value tracing. Each subtype will have its own special approach and will be heavily depended on the facts of each case. Regardless, of the tracing approach taken
the practitioner must always be cognizant of the ultimate goal of tracing: to convince the trier of fact by that "measure or degree of proof which will produce in the mind of the trier of fact a firm belief or conviction as to the truth of the allegations sought to be established." Tex. Fam.Code Ann. § 101.007 (Vernon XXXX) Failing to do so, the character of property should be resolved in favor of the community estate. Akin v. Akin, 649 S.W.2d 700, 703 (Tex.App.-Fort Worth 1983, writ ref'd n.r.e.).

(1) Community-Out-First Tracing Theory of Tracing

The community-out-first theory was judicially developed over many years. It endures today as the primary method of tracing monies from commingled accounts back to their places of origin. When expenditures are made, community funds are exhausted before separate funds are reached. The following are the cases that have helped developed the community-out-first theory.

a. Sibley v. Sibley, 286 S.W.2d 657 (Tex. Civ. App.Dallas 1955, writ dism'd)

The Dallas Court of Appeals announced the community-out-first theory in the case of Sibley v. Sibley. In Sibley, a husband and wife shared a joint bank account comprised of $1,698.34 in community funds. The couple deposited $3,566.68 of the wife's separate funds into the joint account, thus commingling the wife's separate funds with the community funds. The parties made a number of deposits and withdrawals to the account; however, the account never dropped below the sum of $3,566.68, the total of the wife's separate property funds, until the couple made a down payment on a farm with funds from this account. The concern was whether the farm was community property in nature, or whether it was separate, either in whole or in part, because the purchase sums were derived from the account.

The court applied a trust rule developed for the establishment and enforcements of trusts which provides that “Where trustee draws checks on a fund in which trust funds are mingled with those of trustee, trustee is presumed to have checked out his own money first.” In keeping with that analogous presumption, the court presumed that the community funds in the joint bank account were withdrawn first, before the wife's separate funds were withdrawn. The court held: “The community moneys in joint bank accounts of the parties are therefore presumed to have been drawn out first, before the separate moneys are withdrawn; and since there were sufficient funds in the bank, at all times material here, to cover appellee's separate estate balance at the time of the divorce, such balance will be presumed to be her separate funds.”

It is important to not that Sibley has been distinguished most recently by an unreported case In re Marriage of Smith, Not Reported in S.W. 3d, WL 22715581 (Tex.App.-Amariool, 2003): “Although Matthew acknowledged that community funds had been deposited into the account, in his brief, he bases his support of the findings of the trial court on Sibley v. Sibley, 286 S.W.2d 657 (Tex.Civ.App.-Dallas 1955, writ dism'd) , which held that where an account contains community and separate funds, it is presumed the community funds are drawn first so that the balance in the account is presumed to be separate property. Although Sibley was a divorce case, it is not controlling here because it involved a "joint account," which is not presented here.”

b. Harris v. Ventura, 582 S.W.2d 853 (Tex. Civ. App.--Beaumont 1979, no writ)

In Harris, a surviving widow brought suit against the executrix of her deceased husband's estate to recover her community property share. The widow claimed certain bank accounts as her separate property, but the only evidence concerning the source of the funds was her testimony that "[s]ome was gifts and some may have been my social security checks, I don't remember." This evidence, which did not even purport to establish the separate character of all the funds on deposit, was obviously insufficient to overcome the presumption of community property.

An asset in question was a checking account containing $4,997.51. This accounts consisted of commingled funds of the husband's separate property, some community property, and funds of unknown origin. Upon final analysis, the trial court that he window did not overcome the community property presumption.

The appellate court commenced its review with the community property presumption and then held that the party claiming the property as separate property bears the burden to trace and clearly identify property claimed as separate property. The court stated that tracing showed that on April 12, 1974, the balance in the account was $460.15. This balance was presumptively community property. On April 16, the husband deposited the sum of $7,825.79 which constituted proceeds from the sale of his real estate acquired prior to marriage. These funds, therefore, were his separate property. On July 2, he deposited $1,174.62, of which, $878.63 was from the husband's inheritance. Between April 12, 1974 and TexasDivorceLaw.com

January 1, 1975, he made other deposits to the account, representing interest earned that was admittedly community property.

The aggregate of the community property deposits and the original balance was $1,339.63. Separate property deposits totaled $8,704.42, or $7,825.79 plus $878.63 in interest. Withdrawals during the period totaled $5,046.54. The court of appeals concluded that the husband's heirs had traced $3,657.88 of the bank balance as the husband's separate property.

The court of appeals then reasoned that if $3,657.88 of the ending balance was separate property, then the community balance must have been $1,339.63 ($4,997.51 minus $3,657.88). Applying the community-out-first rule, however, the initial community balance of $460.15 had been drawn out in the first withdrawal. Therefore, the trial court overstated the community balance by $460.15. Adding this amount to the previously determined separate property balance gave a new total ending balance of separate funds of $4,118.03. Subtracting $4,118.03 from the ending balance of $4,997.51 gave a community balance of $879.48. The wife owned half of this, or $439.74. Tracing failed as to the other accounts because the court of appears held that the community property presumption had not bee overcome. Without the evidence of traceability being adequately developed at trial, the burden could not be overcome. Venezia v. Venezia , 2000 WL 1273340, Tex App. – Beaumont 2000 Harris v. Ventura , supra.

In the instant case, the record reflects that on November 29, 1993, appellee withdrew $12,199.19 cash from the parties' joint bank account and tendered it at the closing of the purchase of the Nottinghill community residence. The record also indicates that at the time of the $12,199.19 cash withdrawal, the total balance in the parties' bank account was $15,255.47. Of this total balance, appellee properly traced his separate sale proceeds previously deposited in the amount of $11,096.78. That would leave $4,158.69 as representing the community's cash on hand in the bank account at the time of the Nottinghill purchase. Under the community-out-first rule, the $4,158.69 must be subtracted from the $12,199.19 closing payment. The amount remaining, $8,040.50, represents the proper reimbursement figure due appellee, not $10,473.98 as appears in the judgment.

The opinion does not contain enough information to determine exactly what process the court of appeals used in tracing the commingled bank account. However, it is apparent that the court accepted the proposition that by showing the character of each deposit, and presuming that community funds were drawn out first, a party can trace separate property funds that have been mixed with community funds in a bank account. The court traced the characterization of the husband's interest in the land owned through a conveyance and reconveyance of the note to and from a bank, back into the land, and finally into a new note and certificates of deposit. The court did not recognize any interest that may have accumulated on the original note prior to foreclosure or on the certificates of deposit.

c. Barrington v. Barrington , 290 S.W.2d 297, 298 (Tex. Civ. App.Texarkana 1956, no writ)

In Barrington v. Barrington, the divorce court adjudicated the parties' property rights and partitioned their community property. One issue in the case involved the character of the earnings from the Barrington Tire Shop from March 31, 1954 to March 1, 1955. These earnings totaled $3,620.92, and the withdrawals during that period totaled $4,637.22. The trial court found that the couple had made these withdrawals for their support, maintenance, and pleasure, thus, the court concluded that the withdrawals were of "community funds for community purposes." The trial court also found that the earnings of the Barrington Tire Shop never equaled nor exceeded regular withdrawals at any time during the marriage. In fact, the trial court found that withdrawals during the marriage exceeded the earnings of the business by $1,140.41. Thus, the evidence supported the finding that no community funds had been invested in the tire shop business and that all of the stock and machinery used in operation of the business were the separate property of the husband. The Texarkana Court of Appeals therefore affirmed the trial court's judgment.

The appellate court noted that the real estate, the original tools, appliances, office furniture and other original items in the Barrington Tire Shop that Mr. Barrington had owned prior to the marriage had not changed their form and remained his separate property upon the dissolution of his marriage. The remaining property of the Barrington Tire Shop purchased with the bank account of Barrington Tire Shop during the marriage and the stock of tires on hand at the dissolution of the marriage were the separate property of the husband.

d. DePuy v. DePuy , 483 S.W.2d 883, 887 (Tex. Civ. App.Corpus Christi 1972, no writ).

The parties in DePuy v. DePuy had one checking account. Forty-eight days after marriage, the husband deposited an inheritance check for $66,647.01 in the account. The husband used the money to invest in an Austin duplex and to purchase stocks and furniture. On January 7, 1969, the account had a balance of $2,215.12.

The Corpus Christi Court of Appeals noted that "(i)t is apparent that the parties had net earnings which approximated their living expenses with only small amounts, if any, left over." Accordingly, the court found that the investments and property purchased with the inheritance money from the account could not have been made from community income because their living expenses roughly equaled their income. Approving the trial court's determinations, the court of appeals held "(the) separate funds were not so commingled . . . as to defy segregation. . . ."

The unusual fact situation in this case allowed the court to deviate from the general rule. Here, the husband made a number of "honeymoon" (forty-eight days into the marriage) purchases with a $66,000 inheritance he had received from his grandfather. When the marriage terminated four years later, the courts allowed him to "trace" a large portion of the inherited funds into various investments that the courts deemed separate property.

(2) Minimum Sum Balance

Using the minimum balance sum theory, a party may trace funds on account by proving the balance never dropped below the amount of separate property proven to be in the account. This method, however, has a very narrow application, because rarely will a case involve very limited transactions.

a. Snider v. Snider, 613 S.W.2d 8, 11 (Tex. App.Dallas 1981, no writ).

Snider v. Snider is a probate case where the deceased husband's executor and widow was successful in tracing $29,642 of a total account balance of $35,809 as the husband's separate property. She alleged that a savings account held by the deceased husband prior to marriage was community property. The court, in deciding the characterization of the bank account, looked to the amount of money in the account prior to marriage as well as deposits and withdrawals during marriage. A determination was made by the court that the account was both community and separate in character by tracing the funds into and out of the account and recognizing that the account never dropped below a certain amount. The court used the minimum balance sum approach to tracing.

The balance on account as of the date of marriage, $27, 642, was established by entries in the savings passbook. The entries also indicated subsequent deposits and withdrawals which reduced the balance to $19, 642. An additional deposit of $10,000 of the husband's separate property was made, increasing the separate property portion of the account to $29,642. Thereafter, there were several credits and debits to the account, but the balance never fell below $29, 642. The court held these facts sufficient to establish that $29,642.45 of the $35,809.80 in the account at the time of the husband's death was his separate property. The remainder of the account was untraceable to the husband's separate estate and thus was considered community property.

Additionally, on the date of marriage, the husband was the principal shareholder in a corporation that owed the husband $3,228.87. The interest on this debt always accumulated faster than payments were made. Thus, the balance due on the date of the marriage was "a traceable and identifiable part of the balance on hand at the husband's death."

In tracing the bank account, the court charged all withdrawals against the community funds in the account. The remaining separate balance therefore was never reduced by any of the withdrawals. The tracing of the note was a variation on the same theme. All payments were attributed to accrued interest and not unpaid principal.

b. Coggin v. Coggin , 204 S.W.2d 47, 49 (Tex. Civ. App.Amarillo 1947, no writ).

In Coggin v. Coggin, the wife successfully employed the community-out-first theory to show the separate character of property. The wife owned several tracts of land before the marriage, as well as some producing oil wells from which she received royalties. During the marriage, the couple made several purchases: an automobile, a house, two tracts of land with associated mineral rights, and a $9,000 vendor's lien note. These purchases were made from the joint account of both spouses. Most of the money in the joint account was the wife's separate property, acquired from her oil wells. Virtually none of the money was earned by the husband and about $1,000 per year came from the wife's rental of some grasslands. The community living expenses ranged from $200 to $500 per month. During divorce proceedings, the husband tried unsuccessfully to have the house, mineral rights, and vendor's lien note classified as community property; the automobile was successfully classified as community property.

On appeal, the court considered whether the four items of property were community or separate property. There was evidence showing that the rentals from the grasslands, the only substantial community income, were spent in support of the community expenses. In fact, the expenses far exceeded the community income. The evidence showing that the tracts of land and their mineral rights, the house, and the vendor's lien note were all separate property was examined by the court of appeals, which affirmed the trial court's judgment. The court reasoned no community money was present in the bank account at the time of purchase, thus the three pieces of property were the separate property of the wife. Also, in affirming the trial court's classification of the automobile as community property, the court of appeals determined that there had been a bank loan of $26,800 which was placed in the joint account soon before the automobile was purchased. This meant that the funds used to purchase the car were community property, and the mutation of the funds into the automobile retained the status of community property.

In this case, the court used the community-out-first theory of tracing to determine the character of the funds in the bank account at the time of purchase of these four items of property. This case applies the community-out-first theory to a situation in which a spouse had considerable separate income and there was an excess of community expenses over the community income. The separate income will retain its character as separate property as long as adequate records are kept detailing the account activity.

c. Horlock v. Horlock, 533 S.W.2d 52, 55 (Tex. Civ. App.--Houston (14th Dist.) 1975, writ dism'd w.o.j.).

In Horlock, the husband owned properties having a net value of approximately $1,000,000. During the marriage, the husband sold separate real property for approximately $700,000 and received in excess of $200,000 under certain contracts that he had entered into and performed prior to the marriage. The total value of the husband's separate property collected during the marriage was $921,000. The proceeds from the sale of property became commingled with the community property of the parties. The husband used his separate estate as a foundation upon which he built the community's wealth. Utilizing this foundation, the husband established an estate worth between $3,000,000 and $4,000,000. Accordingly, the appellate court held that "the trial court was justified in awarding the husband a separate estate reimbursement."

Prior to the marriage, the husband owned 800 shares of stock in Student Housing, Inc. Student Housing, Inc. then merged with two corporations to form a new entity known as Collegiate Services Corporation. Because of the merger, the husband became the owner of 14,152 shares of Collegiate Services Corporation. The husband and wife later acquired 40 shares of Collegiate Services Corporation.

During trial and on appeal, the wife argued that the husband's shares of CSC stock, although presumed to be community property, were in fact the husband's separate property. Consequently, the wife further argued that if the CSC stock were the husband's separate property, then the community estate was entitled to $100,000 as reimbursement for funds spent to maintain the husband's interest in CSC. The trial court found that the husband had spent separate and community funds totaling approximately $100,000 for the maintenance of the CSC investment. However, the court made no specific findings regarding the separate or community nature of the CSC stock. The question presented on appeal was whether the wife had sustained her burden of overcoming the presumption that the CSC stock was community property. Because the shares were traceable, the stock was found to be the husband's separate property.

Once the characterization of the property had been determined, the burden then shifted to the wife to establish that the community had a right to reimbursement from the husband's separate property estate. "Based upon the presumptions favoring the position of the (wife), the community estate is entitled to a reimbursement from the separate estate of the (husband) in the sum of $100,000 expended during the period of the marriage."

d. Padon v. Padon, 670 S.W. 2d 354 (Tex.App. 4 Dist) 1984.

In Padon, the evidence elicited at trial showed the following: During the marriage of the parties, Mr. Padon's father died leaving Mr. Padon an amount in excess of $160,000.00. On February 25, 1977, $160,490.00 was deposited in Frost National Bank in San Antonio to open an account styled “R.H. Pat Padon or Carolyn Padon .” Mr. Padon inherited and deposited $160,000.00 into this joint account. In early July, a house was purchased for $89,900.00, which was paid for by check from that account. The March bank statement of the Padon's account shows no additional deposits from the time of the initial $160,490.00 deposit until March 4, 1977. On March 1, 1977, the statement shows a check cleared the account in the amount of $89,900.00.

Both parties testified that all monies received from all sources during the marriage were subsequently deposited into this account. The March 1977 statement is was the only statement in evidence. The court held that this evidence was sufficient to prove that the house was the husband’s separate property.

Tracing and reimbursement exist as two recognized methods of escaping the effect of the presumption of community property. Here, tracing was impossible, but reimbursement was not. Equity was well served by reimbursing the husband for his initial investment.

e. Kuehn v. Kuehn, 594 S.W.2d 158 (Tex. Civ. App.Houston (14th Dist.) 1980, no writ).

In Kuehn v. Kuehn, the husband failed in his attempt to use the community-out-first theory of tracing. After marriage, the husband placed some of his separate money into a joint bank account with his wife. Money from this joint account was later used to purchase a house and land during the marriage. During divorce proceedings, the husband claimed that both the house and land were his separate property under the community-out-first theory of tracing separate property.

This claim was fatally flawed, however, because the husband had not produced evidence to demonstrate how much of his separate funds he had deposited into the account, "whether funds from other sources were placed in the account, or what other expenditures were made therefrom." Because he failed to produce clear evidence that no community funds were in the account at the time the withdrawals were made, "the application of (the community-out-first theory) to the facts before (the court) buttress(ed) the presumption that the house and lots were paid for with community funds . . . ." The sole reason that this case was decided in the wife's favor was that the husband failed to establish an essential element of the community-out-first theory: The party wishing to use this theory must present clear and convincing evidence that there were no community funds in the joint account at the time of the purchase.

f. Welder v. Welder, 794 S.W.2d 420, 426 (Tex. App.Corpus Christi 1990, no writ).

In this case, the trial court awarded to the husband several tracts of land as his separate property, based upon the community-out-first theory of tracing ownership. The husband had inherited oil and gas interests that were indisputably his own separate property. During the marriage, all the money that came from the oil and gas interests was the husband's separate property; the courts consider such income to be compensation for waste. This separate income was placed in the couple's joint account, and records were kept detailing the additions and dispositions of the account. During the marriage, the husband purchased several tracts of land with the funds from the account. After the marriage ended in divorce, the wife attempted to lay partial claim to the recently acquired tracts of land by claiming that they were community property.

At trial, the judge admitted into evidence summaries of the couple's financial records made by the husband's accountant. The accountant, in drafting the summaries, used the community-out-first presumption to come to the result that the husband owned a majority of the disputed property separately. Almost all of the income that was community income was shown to have been used just as quickly as it was earned for the couple's community expenses. In these summaries, the amount of the bank account comprising separate property was accurately shown at the specific date of each purchase of the disputed property. Thus, the court of appeals agreed with the husband that the community-out-first theory applied, and that the husband had presented clear and convincing evidence showing that the funds in the joint account were his separate property. Consequently, the court had a basis on which it could make an accurate determination of the husband's separate interest in each of the tracts of land.

The importance of this case is that the community-out-first theory may be used either offensively or defensively, and can be an effective estate planning tool. Here, the husband showed the precise amount of separate property in the joint account when withdrawals were made both before and after the purchase of the disputed properties. This evidence allowed the husband to use the presumption that community funds are withdrawn before separate funds, and enabled the court to make an accurate determination of the amount of separate property without surmise or speculation.

(3) Clearinghouse Method of Tracing (a/k/a Identical Sum Inference)

One method of overcoming the community property presumption set out in Section 5.02 of the Texas Family Code is by tracing specific deposits and withdrawals through bank accounts under what has been termed by lawyers as the "clearinghouse" method or "identical sum inference.” The clearinghouse method holds that, in the event a deposit is made at approximately the same time as a withdrawal of a similar sum, the withdrawn funds will be of the same character as the funds deposited. The theory applies to tracing the deposit of an identifiable sum of money into an account through a subsequent withdrawal into a purchase or payment to prove the character of that purchase or payment. The identical sum inference method is a refinement of the clearinghouse theory focusing on an individual matching deposits and withdrawals.

Both theories have their greatest application when a clearly identifiable sum of money, the character of which can be clearly identified, is deposited into a bank account and, within a short period of time, withdrawn to purchase an asset. Upon the dissolution of marriage by divorce or death, the proponent of the characterization of property as separate property can show that an asset is separate property if he or she can trace the deposit of clearly identifiable separate property sums into an account, and thereafter trace the withdrawal of those same funds to the purchase of an asset.

These theories rebut the community-out-first presumption applied in tracing costs. Although case law supports the application of these theories to trace separate property through bank accounts, the theories become less applicable when the deposits and withdrawals are not in exact amounts, when the transactions are separated by greater periods of time, and when the separate property proponent fails to clearly show that the money withdrawn from the account is the actual sum used to purchase the asset whose characterization is in question.

a. Hanau v. Hanau, 730 S.W.2d 663 (Tex. 1987).

In Hanau v. Hanau, the husband owned 200 shares of Texaco stock at the time of marriage. Several years after the marriage, the husband sold the Texaco shares for $5,755, and on the same day he bought 200 shares of City Investment stock for $5,634. The husband and wife moved to Texas a few years later. Shortly thereafter, the husband sold the City Investment stock for $6,021, and on the same day he purchased 200 shares of TransWorld stock for $6,170.

Upon the husband's death, his will left his separate property to his children by a prior marriage and his community property to his wife. The issue in Hanau was whether the TransWorld stock could be traced to the husband's separate estate. If so, the TransWorld stock would pass to the husband's children from a previous marriage. The court of appeals held that the shares of TransWorld stock were community property. In addition, the court of appeals held that the parties' stipulations that they had kept their respective stock funds in their own names and in separate accounts throughout their marriage did not overcome the community presumption. Further, the court of appeals stated that merely showing "that the separate funds could have been the source of a subsequent deposit of funds" was not sufficient to overcome the community property presumption.

The Texas Supreme Court reversed the court of appeals by holding that the account had not been commingled. The court based its decision on the parties' stipulation that the husband had always kept the property in his own name and that the wife had no power over the account. The court noted that the husband's children "ha(d) shown the chain of events leading from the Texaco stock to the TransWorld purchase and (had)shown that no other transactions occurred on the days in question, which would have planted the seeds of doubt upon the possible source of the funds used to buy the stocks."

This case presents a good example of the application of the clearinghouse theory. The husband's stock account served as a clearinghouse for several sales and subsequent purchases of stock, all of which were traced to the husband's separate property. Significantly, in both of the stock transactions, the amount of the proceeds received from the sale of stock was within approximately two hundred dollars of the purchase price of the new stock. Although the sums were not identical, the court inferred that, because the transactions occurred on the same day, the proceeds received from the sale of stock were the same proceeds used to purchase the new shares of stock. Again, the short proximity of time in which the transactions occurred appeared to be a controlling factor in the court's application of the clearinghouse tracing theory. In Hanau, it appears that the property was sufficiently traced by showing that the husband deposited the separate funds into an account and immediately withdrew the funds to pay for the other stock from the same account.

b. Skinner v. Skinner, 202 S.W.2d 318 (Tex. App.San Antonio 1947, no writ).

Skinner v. Skinner was a divorce case in which the trial court had found that the wife owned certain property, including a bank account, note receivable, automobile, house and lot, and a Bandera County Ranch as her separate property. The husband appealed the award of these properties to the wife as her separate property. Both parties suggested at trial that an audit of their property be received into evidence. This audit covered the duration of the marriage. The audit revealed deposits and withdrawals from various bank accounts maintained by both the husband and wife. Additionally, the audit disclosed deposits into an account generally used for the deposit of community property funds, which were undoubtedly the separate property of the wife.

Using this information, the court noted that although the parties had deposited certain separate funds in a bank account that was generally used for community funds, the community funds could be traced into and out of the bank account. Similarly, the community funds could be traced into and out of the account generally used to deposit separate funds. Thus, the court concluded that the parties "were endeavoring to maintain a distinction between community and separate funds and prevent commingling of a nature (that) would prevent a successful tracing of funds." The court also held that the wife had successfully traced approximately $20,000 of separate property funds that she had deposited in the account to the purchase of a home, an automobile, a loan to her son, and various other expenditures, while retaining a balance in the account that was also her separate property.

Although the court did not discuss it in great detail in the opinion, the bank account at issue acted as a clearinghouse for the deposit of separate funds and the subsequent withdrawal of those funds for purchases. Apparently, the court relied heavily on the audit to trace the separate funds of the wife into and out of the bank account. The audit supported the parties' endeavor to maintain a distinction between the community and separate funds.

c. McKinley v. McKinley, 496 S.W.2d 540 (Tex. 1973).

Prior to the marriage in McKinley v. McKinley, the husband opened two savings accounts which were the source of funds used to purchase certificates of deposit at question in the trial. Between the date of marriage and the husband's death, numerous deposits and withdrawals were made in both accounts, including withdrawals from both accounts used to purchase the savings certificates at issue.

The husband's executor "filed an inventory and appraisement which listed the two savings certificates as the separate personal property (of the husband)." The wife initiated suit against the executor praying for a declaratory judgment that the two savings certificates were part of the couple's community estate. The trial court concluded that the certificates that totaled $26,400 were the couple's community property and not the separate property of the husband.

On appeal, the court of civil appeals discussed the evidence presented at the trial court. The two savings certificates were in the amounts of $10,400 and $16,000. Both certificates were purchased from savings and loan associations with funds from savings accounts in those institutions. The tracing of the $10,400 account began when the husband had $9,500 on deposit in the savings and loan savings account. The wife did not dispute that this $9,500 was the husband's separate property. The $9,500 originally deposited remained in the account and earned interest until December 31, 1967, when the account balance reached $10,453.81. During this time, neither party made withdrawals from the account, nor all deposits were shown to be interest income. The couple withdrew $10,400 from the savings account on January 2, 1968 and used it to purchase the $10,400 savings certificate. The Supreme Court easily traced the $10,400 savings certificate from the $9,500 originally on deposit with the savings and loan into the savings certificate of $10,400, thus clearly identifying $9,500 of the certificate as separate property.

The $16,000 certificate was actually a "consolidation of three smaller certificates in the amount of $10,000, $4,000 and $2,000." Although the court traced the funds used to purchase the $4,000 and $2,000 certificates to community property accounts, it could not easily trace the character of the $10,000 certificates. The court began the tracing by noting that the husband had an account with a balance of $9,570.27 at a savings and loan. This sum was indisputably the husband's separate property. The parties, however, made numerous deposits and withdrawals between the date of marriage and the date the husband withdrew the $10,000 in question to purchase the savings certificate. The couple deposited $7,740.34 during this period, $1,140.34 of which was interest earned on the account. The court could not identify the source of the remaining $6,600. Additionally, the couple made two withdrawals during this period, one for $437.99 and another for $4,985.91. When the husband finally withdrew the $10,000 used to purchase the certificate, a balance of $1,886.71 remained in the account.

The court determined that the husband did not attempt to trace any of the separate funds in the savings account to the certificate. Therefore, the evidence was "wholly inconclusive as to the nature of funds deposited or withdrawn. To come to any conclusion about the property status of the $16,000 certificate would require surmise and speculation." The court applied an identical sum inference, rather than a clearinghouse theory, to the facts of McKinley. The court was able to clearly determine that the original $9,500 was the separate property of the husband. Additionally, the court identified the increase in value of the account from $9,500 to $10,453.81 as community property interest income. Thus, the court segregated the original $9,500 as the husband's separate property, because the amount of withdrawal was identical to the amount originally in the account.

The identical sum theory was well suited to the tracing of this certificate because no withdrawals were made other than clearly identified community interest income. Also, there was a close proximity of time (the same day) between the withdrawal of the separate property funds from the savings account and the purchase of the savings certificate with the funds. Conversely, the clearinghouse or identical sum inference theory did not apply to the $16,000 savings certificate because the husband made no effort to trace the specific funds from savings and loan association account into the savings certificate. The holding of this case suggests that courts will apply these theories only in a narrow range of facts.

d. Peterson v. Peterson, 595 S.W.2d 889 (Tex. Civ. App.--Austin 1980, writ dism'd)

In Peterson v. Peterson, the husband entered into a sales contract with a construction company for the construction of a home for the couple. He issued a check for $2,000 as earnest money. The transaction closed approximately one month after the parties' marriage, at which time the husband wrote a check for $32,973.64, the balance of the purchase price. The deed named the husband and wife as co-grantees.

On appeal, the wife contended that the husband had failed to produce any evidence to overcome the community property presumption. However, the husband had "testified that he paid the balance of the purchase price from his personal account, and that the check was drawn against a deposit in excess of $35,000 representing the proceeds from the sale of property which he had inherited from his mother." Relying upon McKinley v. McKinley, the court held that the husband overcame the community presumption by tracing the entire purchase price to his separate funds. The court further stated that it had found the evidence presented during trial sufficient to support the trial court's judgment. Specifically, the Petersons had been married less than one month when Mr. Peterson made the payment from his personal account. Additionally, Mrs. Peterson admitted during trial that her only financial interest in the house was maintaining the home, such as landscaping and furniture.

Unlike the cases previously discussed, the Peterson court tied the purchase money withdrawal to the specific separate property funds in the account without knowledge of what deposits and withdrawals had been made between the date of the marriage and the purchase of the house. The wife contended that the husband's failure to fully document all transactions during this period defeated his attempt to rebut the community property presumption. However, the court apparently gave credence to the fact that the parties were married less than one month when the husband made the payment from his account.

In sum, the court apparently reached its decision on an equitable basis, rather than upon any clear and definite tracing principles. The identical sum inference theory does not apply to this case because there was no identical deposit and withdrawal. Instead, this case is perhaps the strongest example of a court's application of a clearinghouse theory. Here, the court held that husband adequately traced the separate property character of the deposit without exploring whether any intervening deposits and withdrawals changed the mixture of separate and community property in the account.

e. Beeler v. Beeler, 363 S.W.2d 305 (Tex. Civ. App.--Beaumont 1962, writ dism'd).

In Beeler v. Beeler, Mr. Beeler owned a 425-acre ranch prior to his marriage. During the first seventeen months of marriage, the husband and wife lived on the ranch. They then sold the ranch for $50,000. The purchase price included $16,275 in cash and a vendor's lien note of $33,725 payable in ten yearly installments. The couple executed a vendor's lien note on the day they sold the ranch. On the same day, the husband obtained a bank loan for $15,000. This loan required the husband to repay it in six annual installments of $2,500, plus interest. The husband then assigned to the bank the vendor's lien note as collateral security for the payment of the $15,000 note. The bank required that the wife sign the note as a condition to obtaining the loan. The couple then purchased a $24,000 home on eighteen acres using $9,000 of the $16,275 cash paid to the husband for the farm and the $15,000 borrowed from the bank. The husband and the bank agreed that the husband would collect the yearly installments from the sale of the ranch and, from those installments pay the bank the yearly installments on the note for the new home.

The court of appeals concluded that because $9,000 of the $24,000 paid for the home was the husband's separate property (the proceeds from the ranch), his separate estate owned a 9/24th interest in the home. The court went on to hold that, although the husband's vendor's lien note was sufficient to satisfy the remaining balance due on the home, the bank had not agreed to look solely to the husband for repayment of the loan. Hence, the remaining 15/24ths of the home was community property.

The court found that the husband had indeed been making payments on the bank loan out of his separate property. The wife, however, argued that because she and her husband went to the bank and deposited the installment collected on the ranch note in their joint account and at the same time gave a check on that account to the bank for the $2,500 due to the bank for the yearly installments on the $15,000 note, the account had become commingled with the husband's separate funds and the payments on the $15,000 note were therefore paid out of the community estate. The court held that "the fact that the sum of $2,500.00 plus interest on the (ranch) note was momentarily deposited in the joint bank account of the (husband and wife), and thereupon withdrawn to pay the bank, cannot convert such $2,500 plus interest to community funds." The court noted that "(s)uch sum, in each instance, was, in effect, earmarked a trust fund, in equity already belonging to the bank from the moment collected by (the husband)." The court of appeals held that the payments on the community note were made from the husband's separate funds. Therefore, the husband's separate estate was entitled to reimbursement for the payments.

The court applied the clearinghouse tracing approach in this case, because at the time the husband and wife deposited the installment payments from the ranch note into their joint account, they immediately gave a check on that account to the bank for the $2,500 due for the yearly installments on the $15,000 note. As seen from earlier cases, the simultaneous nature of these transactions appears to be the basis of the court's acceptance of the clearinghouse tracing approach. The tracing was successful in this case because the court was able to trace the payments on the bank note to the payments received from the ranch note. It stands as a good example of how to trace separate property from one source to another.

f. Lindsey v. Lindsey , 564 S.W.2d 143 (Tex. Civ. App.Austin 1978, no writ)

In Lindsey, the husband appealed the trial court's ordering the sale of certain property and payment of $60,000 from the proceeds of this sale to the wife. The trial court found that because the "'(wife) invested $60,000 of her separate property into the property,"' she was entitled to this award as reimbursement. The wife identified to the trial court the exact amount of her separate funds, all of which she had acquired from a prior divorce settlement. The court of appeals noted that "(a)ll such funds were deposited in a joint bank account, full records of which were before the trial court."

The court of appeals held that "(a)ll investments in real estate by (the parties) . . . came solely from the account (containing the wife's) separate funds. The investment sums were accounted for from records in the same manner the deposits were shown to the court." These records enabled the trial court to "determine accurately the interest of each estate." Therefore, the court of appeals held that the wife "met the burden of tracing her separate property as it was received and as it was invested in community realty."

The court of appeals did not discuss the proximity in time between the specific deposits and the specific withdrawals linked to those deposits. Although many of the underlying facts were not disclosed, the court arrived at its decision by reviewing records that clearly showed the nature of the deposits and the withdrawals. One can only infer that the wife must have done a good job at the trial level of proving the character of each deposit and linking those same deposits to subsequent withdrawals.

(4) Pro-Rata Approach

Although this method is only mentioned in a handful of Texas cases, an understanding of the methods of tracing would not be complete without addressing the pro-rata approach. For example, if separate funds of each spouse are mixed in an account containing no community funds, it would seem logical that acquisitions from the account would be owned pro-rata by each party in generally equal proportion to the entire account balance; therefore, there would be no “presumption” relating to the community and the pro-rata treatment of the asset would be only the means of determining the relative ownership of the parties.

a. Duncan v. U.S., 247 F.2d 845 (5th Cir. 1957).

In Duncan, the federal appeals court discussed a pro rata form of tracing. Over a brief marriage, the parties acquired only $16,000 of total community income. Despite such a low amount of income, substantial deposits were made to their accounts over the period of the marraige. As of the date of the purchase of stocks for $7,241, the account balance was $17,8113, of which $5,000 was community. Instead of applying the community out first theory (5,000/17,813) to total purchase of $7,241, the court stated that "All community funds might have been exhausted on the first purchase, or all might be ratably applied throughout the year. As this neither is nor can now be demonstrated, it does not overcome the presumption which the law affords to the community that to this full extent, all was proportionally community property".

(5) Item Tracing

Item tracing is no misnomer. It is, in fact, identifying the character of a specific item as separate, then tracing its transformations from its original form to its present form. As in all instances, the tracing must show clearly and convincingly that the original asset was separate, must show how, when, and in some instances why it changed forms each time that it transformed until the shift is complete within the current asset. Cockerham v. Cockerham; supra Tarver v. Tarver, 394 S.W.2d 780 (Tex. 1965); Love v. Robertson, 7 Tex 6 (1851).

To begin the tracing, the character of the original asset must be clearly established. This means an affirmative showing of how the asset was acquired in the first place in such a way as to make it a separate asset. Mortenson v. Trammell, 604 S.W.2d 269 (Tex. Civ. App. - Corpus Christi 1980, writ ref'd n.r.e.); Logan v. Barge, 568 S.W.2d 863 (Tex. Civ. App.-Beaumont 1978, writ ref'd n.r.e.); Bile v. Tupa, 549 S.W.2d 217 (Tex. Civ. App. - Corpus Christi 1977, writ ref'd n.r.e.). For instance, deeds to property acquired prior to marriage must be introduced, demonstrating that the inception of title was prior to marriage.

From the original characterization, the tracing begins and evidence must clearly establish the chain of character. It is not sufficient to show that the original asset, or some mutation of that original asset could have been the source of the ultimate asset in question. Latham v. Allison, supra; Barrington v. Barrington, supra; Sibley v. Sibley, supra; Farrow v. Farrow, 238 S.W.2d 255 (Tex. Civ. App. - Austin 1951, no writ); Coggin v. Coggin, supra; McKinley v. McKinley, supra.

This burden sounds stringent and, indeed it is. However, case law seems to suggest that stronger burdens are placed on creditors cases and estate disputes. In fact, referenced herein are Holloway v. Holloway and Coggin v. Coggin. The courts in those cases used a more liberal standard in allowing testimony by one party or the other regarding marital agreements, either expressed or implied. This is limited to a spouse of the marriage who would have that discreet knowledge and will generally not be extended to a third party. Furthermore, the fact finder is always able to disbelieve the spouse testifying to the agreement.

(6) Value Tracing

Value tracing is much the same as item tracing. However, in this case, instead of tracing the origin, transformation, and eventual nature of the asset, we are simply tracing cash assets in the same manner. In some ways, this form can be easier than asset tracing because the proponent of the tracing is aided by the theory that "(O)ne dollar has the same value as another; there can be no commingling of dollars where the number owned by each claimant is known." In Re Marriage of Tandy, 532 S.W.2d 714 (Tex. Civ. App. - Amarillo 1976, no writ).

Keeping in mind the other principals discussed in this paper, even commingled funds can potentially be traced, depending, of course, on how and to what extent the funds were commingled and what documentation and evidence is available to overcome the community property presumption.

(7) Before and After Accounting (Invalid Method of Tracing)

This section discusses the before and after accounting method of tracing. Though in many circumstances the method might intuitively appear logical to a client, it is nonetheless an invalid form of tracing and should indeed fail.

This method of accounting takes the value of property owned by a spouse at the time of marriage and the value of property at the time of the dissolution. For instance, a woman with an estate valued at 1 million dollars at the time of marriage might try to show that value and thereby endeavor to persuade the court that the 1 st 1 million dollars of the entire estate, both community and separate, should go to her as her separate property. Such an argument does not take into consideration market conditions, investment opportunities and losses, and the like. Such a before and after procedure does not relieve the party from her burden of tracing. Tarver v. Tarver, supra.

Therefore a decrease in net worth, the fact that one spouse, at the outset of the marriage, had a great deal of assets and the other had but few, or even a dramatic increase in net worth during the marriage are all of interest, but none will relieve a spouse of the necessity of tracing in the manners described herein above. See Meshwert . Meshwert, 543 S.W.2d 877 (Tex. Civ. App. - Beaumont 1976, writ ref'd n.r.e.); Stanley v. Stanley, 294 S.W.2d 132 (Tex. Civ. App. - Amarillo 1956, writ ref'd n.r.e.); Waheed v. Waheed, 423 S.W.2d 159 (Tex. Civ. App. - Eastland 1967, no writ); McKinley v. McKinley, supra; Logan v. Barge, supra; In Re Marriage of greer, 483 S.W.2d 490 (Tex. Civ. App. - Amarillo 1972, writ Dism'd).

A word about parole evidence: The status of property through tracing, as with any other fact that we tend to deal with, may be proven by any competent evidence, including parol evidence. Some of the more liberal cases have held that a spouse is competent to testify concerning the source of funds in a bank account without producing bank records on the deposits. Holloway v. Holloway, 671 S.W.2d 51 (Tex. Civ. App. - Dallas 1983, writ dism'd); Harris v. Ventura, Supra. See also King v. King, 661 S.W.2d 252 (Tex. App. - Houston [14 th Dist.] 1983, no writ); Carter v. Carter 736 S.W.2d 775 (Tex. Civ. App. - Houston [14 th Dist.] 1987, no writ); Newland v. Newland, 529 S.W.2nd 105 (Tex. Civ. App. - Fort Worth 1975, writ dism'd).

This comment on parol evidence is included here because it is relevant. The cases involving the sole use of parol evidence are helpful if you are in a tight spot on your discovery. However, it is certainly the better practice to have every record tracing the asset from inception to present existence.

D. Failure to Overcome the Presumption

Several cases exists which show what when and how litigants fail to overcome the community property presumption:

(1) A husband testified that accounts listed in a premarital agreement were his separate property and that they were separate property at divorce. This was the only evidence the accounts were his separate property. The court held there was insufficient evidence to support a separate property finding as without tracing the husband's testimony could not overcome the community property presumption. Osorno v. Osorno, 76 S.W.3d 509 (Tex. App.— Houston [14th Dist.] 2002, no pet.).

(2) A husband testified that money used to open a bank account came from the sale of stock, but he failed to explain what stocks were sold or the origin of the funds used to purchase the stocks. Robles v. Robles , 965 S.W.2d 605 (Tex. App.—Houston [1st Dist.] 1998, pet. denied).

(3) A husband testified that he had bought a parcel of real property with money he had received in an inheritance, but the deed for the property was not presented to the court and no documentary evidence was presented to trace the money used for the purchase. Robles v. Robles, 965 S.W.2d 605 (Tex. App.—Houston [1st Dist.] 1998, pet. denied).

(4) A wife testified that disputed bank accounts were created with income from her disability benefits provided by her employer and from the sale of timber from her separate real property; both of these sources were community property. McElwee v. McElwee, 911 S.W.2d 182 (Tex. App.—Houston [1st Dist.] 1995, writ denied).

(5) A wife testified that she and three siblings inherited $400,000.00 from their father, and that disputed bank accounts in the parties' names contained only the proceeds from such estate, but her evidence failed to trace the proceeds from her father's estate to the accounts and failed to account for the discrepancy between the amounts shown in the documents relating to the estate and the principal amounts appearing in the various accounts in the wife's evidence. Walton v. Johnson , 879 S.W.2d 942 (Tex. App.—Tyler 1994, writ denied).

(6) A couple's premarital agreement provided that income from the parties' separate property would be deemed community property and used to finance ordinary expenses during the marriage, but that excess income could be deposited to the corpus of separate property and would then become the separate property of the spouse whose separate property produced that income; the wife's proof that $69,000 of the $79,000 purchase price of the parties' residence had been saved excess income from her separate property

was not sufficient to overcome the community property presumption where she failed to prove that the excess income had been deposited to the corpus of her separate assets. Scott v. Scott , 805 S.W.2d 835 (Tex. App.—Waco 1991, writ denied).

E. Conclusion

Reimbursement and tracing are vital issues when a marriage terminates. Often, divorcing spouses pursuing a reimbursement claim must trace assets to determine their marital property character. T racing is one of the most important techniques a lawyer who deals with the question of the character of marital property can master. Successfully tracing an asset from separate property will remove it from the grasp of the trial court dividing the estate of the parties. Although tracing efforts are often impossible to complete, the courts have many times used the equitable remedy of reimbursement to overcome the strict requirements of tracing. Scott v. Estate of Scott, 973 S.W.2d 694, 695 (Tex.App.-El Paso 1998, no pet.)

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