

Equitable Division of Property:
The Conversion of Separate Property Into Marital Property

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Equitable division of property is the allocation of assets acquired during the marriage of the parties based on their respective equitable interests in those assets.¹ This paper will discuss two areas of dispute when determining the equitable division of property: 1.) property owned by one party prior to the marriage but paid for with marital funds during the marriage and 2.) joint gifts. Where real property was in one party's name prior to the marriage but marital funds have been utilized to reduce the amount owed on the mortgage or other debt against the property, the proceeds from the sale of the property are distributed to the parties based on the "source of funds" rule, defined by the Georgia Supreme Court in Thomas v. Thomas.² Generally, property acquired during the marriage by either party by gift, inheritance, bequest, or devise remains the separate property of the party that acquired it and is not subject to equitable division.³ An important exception to this general rule is joint gifts to both spouses, a subject which has been recently addressed by the Georgia Supreme Court in the case of Lerch v. Lerch.⁴

The Evolution of the "Source of Funds" Rule in Georgia

¹ Boyd v. Boyd, 191 Ga.App. 718, 382 S.E.2d 730 (1989).

² Thomas v. Thomas, 259 Ga. 73, 377 S.E.2d 666 (1989).

³ Bailey v. Bailey, 250 Ga. 15, 295 S.E.2d 304 (1982).

⁴ Lerch v. Lerch, 278 Ga. 885, 608 S.E.2d 223 (2005).

Equitable division of property exists only in a divorce action. The court legally determines whether property is separate or marital in nature, and then as a matter of fact awards an equitable distribution of the marital property to each party, recognizing the joint enterprise of marriage.⁵ How to discern what property is separate and what property is marital, and the value of both, evolved in Georgia from common law assignment of all property to the husband by virtue of the marriage itself to the adoption of the source of funds rule by the Georgia Supreme Court in 1989.⁶

At Common Law, the joint enterprise of marriage merged all property of the parties, and all control of the property became the Husband's.⁷ Georgia varied common law to provide Wife as separate property all property of hers at the time of the marriage, and all property of Wife by gift, inheritance or acquisition by Wife during the marriage. Further, Georgia specifically exempted Wife from any responsibility of any liability of Husband.⁸

A long line of case law before Stokes v. Stokes offer that trial courts attempted to provide wives with the value of a factual finding of her separate property. Of course, the fact finder in attempting to provide a Wife with her separate property needed to assign a value to what she brought into the marriage or otherwise contributed from separate property; to determine whether the property remained separate in nature by practice and custom of the parties; and more often than not, to identify the portion enveloped into a marital property asset. For example, a Wife's down payment on the marital residence

⁵ Uniform Marriage and Divorce Act (UMDA) §307(a).

⁶ Note that this paper does not address the direct correlation of the evolution of alimony awards with that of equitable division of property, affected in large part by sociological changes and the affect on the definition of family.

⁷ Stokes v. Stokes, 246 Ga. 765, 768 (1980) (citations omitted).

⁸ Id.

was credited to her as well as a value representing an estimate of the amount she contributed to house payments.⁹ Practice and custom of the parties co-mingling their respective salaries provided evidence to support that monies in a savings account held solely in Wife's name to be marital funds for purposes of equitable division.¹⁰

The trier of fact attempted to credit for a portion of separate property in equitably dividing the property, but did not have a legal basis to provide a division of property based on non-financial contribution of a party until Stokes v. Stokes.¹¹ “Stokes simply recognized that a spouse's non-economic contributions to a marriage might be reflected in an ‘equitable division’ of property, notwithstanding the incidence of legal ownership, and that such an allocation might be appended to another allocation calculated, in theory, upon need and ability to pay.”¹² A trier of fact may award one spouse real property held in the name of the other spouse in the event the real property is found to be marital in character (arising out of the marital relationship).¹³

Stokes adopted that “the court has ancillary jurisdiction to determine the equitable division of either spouse in the real or personal property owned, either in whole or in part, by the other spouse”, but provided no formula by which the court could determine the value of the separate or marital interest, or the active or passive appreciation thereof.¹⁴ Resulting case law from the decision in Stokes to the ruling in Thomas evidence courts’ findings that any property brought into the marriage remained separate property, not divisible, and that courts struggled to discern division of a marital portion of property that

⁹ McLane v. McLane, 224 Ga. 748 (1968); Bragg v. Bragg, 224 Ga. 294 (1968). .

¹⁰ Holloway v. Holloway, 233 Ga. 631 (1975).

¹¹ Stokes v. Stokes, 246 Ga. 765 (1980).

¹² Rooks v. Rooks, 252 Ga. 11, 18 (1984) (concurring opinion).

¹³ Stokes v. Stokes, 246 Ga. 765, 770 (1980). 246 Ga. 765 (1980).

¹⁴ Id.

although separate at the time of the marriage, may have increase in value due to marital contribution.¹⁵ The Bailey Court found the marital residence, gifted to husband at the time of the marriage and titled solely in husband's name, was not subject to equitable division—it had no marital interest because no contribution was made by Wife or Husband toward the *acquisition* of the residence.¹⁶ The Court did not look at interest after acquisition, which may have provided a marital interest to be divided. But in Rooks the Court upheld a jury verdict providing Wife a portion of the marital residence because of facts indicating the marital residence may not have been a gift, but instead may have been purchased in part by a loan from Husband's Mother.¹⁷

The adoption of the theory of source of funds in 1989 provided courts in Georgia the opportunity, upon a party seeking an apportionment of separate property meeting his or her evidentiary burden, to assign value as to contribution of a separate estate and the marital estate to the value of an asset, and further to provide each entity the fair return of the separate and marital interest in the asset.

Thomas v. Thomas
259 Ga. 73, 377 S.E.2d 666 (1989)

In the Thomas case, the Husband appealed from the order of the Superior Court of Fulton County dividing the parties' property upon the dissolution of the marriage. At issue was the division of the proceeds from the sale of the marital home, which was in the Wife's name and had been purchased by her shortly before the marriage. Wife paid a down payment of \$75,000.00 and obtained a mortgage against the property in the amount of \$185,000.00 to meet the sales price of \$260,000.00 for the house. Wife made the

¹⁵ Bailey v. Bailey, 250 Ga. 15 (1982).

¹⁶ Id.; See Also Rooks v. Rooks, 252 Ga. 11 (1984).

¹⁷ Rooks v. Rooks, 252 Ga. 11 (1984).

mortgage payments between November of 1982, the date of the purchase, through the date of the marriage in July of 1983. Throughout the marriage, the mortgage was further reduced to \$177,000.00 with marital funds. A month after Husband and Wife separated in November of 1986, the house was sold for \$351,000.00. The trial judge awarded Wife almost all the proceeds from the sale of the house, and Husband appealed, arguing that all the appreciation and value of the house which occurred during the marriage should have been classified as marital property subject to equitable division.

The net appreciation in the house amounted to \$90,905.00. The trial court found that in addition to the down payment both parties had reduced the loan balance \$7,265.00, and that the total equity paid by both parties was \$82,623.00. Of the \$7,265.00 reduction in debt which had resulted from the monthly mortgage payments, the trial court determined that \$1,017.00 had been paid by Wife and \$6,393.00 had been paid out of marital assets. As a result, a ratio of the amount paid by marital assets (\$6,393.00) to total equity paid (\$82,623.00) works out to seven percent (7%) of the payments on the equity being marital. Therefore, seven percent of the appreciation of \$90,905.00 was subject to marital distribution as a marital asset, which amounted to \$12,756.00. The Supreme Court noted that the method of division used by the trial court is referred to as the “Source of Funds Rule,” which holds:

A spouse contributing non-marital property is entitled to an interest in the property in the ratio of the non-marital investment to the total non-marital and marital investment in the property. The remaining property is characterized as marital property and its value is subject to equitable distribution. Thus, the spouse who contributed non-marital funds, and the marital unit that contributed marital funds each receive a proportionate and fair return on their investment.¹⁸

¹⁸ Thomas v. Thomas, 259 Ga. 73, 76 377 S.E.2d 666, 669 (1989), citing Harper v. Harper, 294 Md. 54, 448 A.2d 916, 929 (1982).

The Thomas Court further noted that fundamental to the adoption of the source of funds theory is the recognition that property is not necessarily “acquired” on the date that legal obligation to purchase is created. Rather, the term “acquired” should be defined as the on-going process of making payment for property.

The Husband in Thomas argued that the entire appreciation in value of the parties’ interest in the house resulted from their joint efforts to maintain and pay for it. The Court, however, found this argument was not supported by the evidence, noting that the parties’ payments reduced the principal debt and were responsible for the resulting increase in equity caused by that reduction. The Court further noted that the only material cause for the remaining appreciation was outside market forces and that the source of funds method utilized assured that the property accumulated during the marriage was fairly distributed between the parties, while at the same time preserving the separate property for the benefit of the spouse to whom it belonged.

Lerch v. Lerch
278 Ga. 885, 608 S.E.2d 223 (2005)

In a matter of first impression, the Georgia Supreme Court considered the classification of joint gifts in the case of Lerch v. Lerch. During the marriage, Mr. and Mrs. Lerch lived on Skidaway Island in Savannah, Georgia in a house that the Husband had purchased prior to the marriage. In 1999, Husband executed and recorded a gift deed transferring ownership in the property to both he and Wife as “tenants in common” with right of survivorship. The trial court found that, as a result of the gift, half of the home qualified as marital property and the other half remained the Husband’s separate

property. Consequently, the court awarded the entire home to Husband, giving the portion of the home qualifying as marital property to Husband as his portion of the equitable division of marital property.

The Supreme Court reversed the trial court's decision, holding that the *entire home* should have been treated as marital property. The Court noted that, normally, a gift to *one* spouse becomes the *separate* property of the recipient spouse. However, when a gift is given to the *marital couple*, the property will become marital property absent evidence of a contrary intent by the donor. In this case, the Husband deeded the home to both his Wife and himself, to be held as "tenants in common" with right of survivorship, manifesting an intent to transform his own separate property into marital property. Therefore, both Husband and Wife owned an undivided one-half interest in the property.

In Lerch, there was also a prenuptial agreement in which the Wife promised not to make any claims against Husband's property in the event of a divorce. However, the property ceased to qualify as Husband's own separate property as soon as he deeded it to the marital couple, and so the Supreme Court held that the prenuptial agreement did not preclude Wife from making a claim for the marital home.

The Lerch opinion raises some questions in light of longstanding Georgia law which holds that a transfer into joint title raises only a rebuttable presumption of a gift:

Where a husband pays the purchase money of land from his own funds and has the land conveyed to his wife, the presumption which the law makes is that the husband intended to make a gift to his wife; but the presumption is a rebuttable one, and a resulting trust in favor of the husband may be shown.

Jackson v. Jackson, 150 Ga. 544, 104 S.E.236, 236 (1920).

The Lerch decision follows the general rule in other states, which holds that property given to *both* spouses is considered marital property. *E.g.*, Forsythe v. Forsythe, 558 S.W.2d 675, 678 (Mo.Ct. App. 1977); Burnett v. Burnett, 122 N.C. App. 712, 471 S.E.2d 649, 650 (1996). However, Courts in other states generally hold that a transfer into joint title does not automatically convert marital property into separate property, but rather that the donor's intent is the primary factor in determining whether a gift was made. Sexton v. Sexton, 125 S.W.3d 258 (Ky. 2004); Husband T.N.S. v. Wife A.M.S., 407 A.2d 1045 (Del. 1979); Stephenson v. Stephenson, 811 A.2d 1138 (R.I. 2002). As to the burden of proof, courts in other states are divided. A majority of other states apply the joint title gift presumption as stated in Jackson. *E.g.*, Conrad v. Bowers, 533 S.W.2d 614 (Mo. Ct. App. 1975); McLean v. McLean, 323 N.C. 543, 374 S.E.2d 376 (1988); Whiting v. Whiting, 183 W.Va. 451, 396 S.E.2d 413 (1990). A minority of other states require that a gift be proven by positive evidence. *E.g.*, Grant v. Zich, 300 Md. 256, 477 A.2d 1163 (1984); Pearson v. Pearson, 761 So.2d 157 (Miss. 2000); Schuman v. Schuman, 265 Neb. 459, 658 N.W.2d 30 (2003).

It has been suggested that the Supreme Court in Lerch had no intention of overruling over 80 years of Georgia case law holding that a conveyance into joint title creates only a *rebuttable presumption* of a gift.¹⁹ In a footnote following its categorical statement that a gift was present on the facts, the court cited a Florida decision, Goldstein v. Goldstein, 310 So. 2d 361 (Fla. Dist. Ct. App.1975), for the following proposition: “[G]ift from husband to husband and wife raised presumption that property qualified as

¹⁹ “Joint Interspousal Gifts and the Parol Evidence Rule,” Brett R. Turner, *Equitable Distribution Journal*, Vol. 22, No. 2, February 2005.

marital.”²⁰ It is noteworthy that the Court did not cite any Georgia cases, and specifically Jackson v. Jackson, which state the same proposition. However, the court’s direct reference to an out-of-state presumption case strongly indicates that the Court did not intend to overrule prior Georgia presumption cases.²¹

The Lerch court’s rationale seemingly lies in the fact that the conveyance into joint title was in a deed of gift.²² Case law from other states holds that when the deed states clearly and unambiguously that the conveyance is a gift, the deed cannot be impeached by parol evidence. Utsch v. Utsch, 266 Va. 124, 581 S.E.2d 507 (2003); see also Hall v. Hall, 734 P.2d 666 (Idaho Ct. App. 1987), aff’d on other grounds, 777 P.2d 255 (Idaho 1989)²³. However, the law in Georgia holds that parole evidence of the nature of the transaction, the circumstances, or the conduct of the parties, *is* admissible to rebut the presumption of a gift, although the proof must be clear and convincing. Jackson, 104 S.E. at 236.²⁴

It is not clear from the opinion in Lerch whether sufficient facts existed to rebut the presumption of a gift or whether the Husband even argued that the presumption of a gift was rebutted on the facts. The Lerch opinion has been criticized for not discussing this point directly so as to avoid misleading future courts and attorneys to believe that Lerch overrules Jackson and other cases holding that a transfer into joint title raises only a rebuttable presumption of a gift.²⁵ The opinion has been further criticized for having the possible effect of encouraging future Georgia courts to find donative intent based

²⁰ Id., citing Lerch, 278 n.3.

²¹ Id.

²² Id.

²³ Id.

²⁴ Id.

²⁵ Id.

upon joint title alone, which would result in a fundamental public policy problem of encouraging spouses to act selfishly by retaining sole use and control of their separate property.²⁶

In another recent case, Brock v. Brock, 279 Ga. 119, 610 S.E.2d 29 (2005), the Supreme Court similarly held that a party's actions can convert separate property into marital property. As in Lerch, the Brock marital home was the separate property of the Husband at the time of the marriage. In April of 2000, Husband executed and recorded a warranty deed transferring ownership in the home to Wife in consideration for her "love and affection." At the final hearing, Husband claimed, and the trial court agreed, that Wife held the property in an implied resulting trust for Husband because he conveyed the property to Wife for the purpose of protecting it from potential future creditors. Wife filed an application for discretionary appeal challenging the trial court's property division award.

The Georgia Supreme Court reversed the trial court, finding that Husband had not overcome the presumption under Georgia law that the conveyance was a gift. To rebut the presumption, Husband was required to prove by clear and convincing evidence that a resulting trust was contemplated by both parties by way of an understanding or agreement.²⁷ The Court found that the record was devoid of any evidence of mutual intent to create a trust and that Husband offered no evidence of a mutual understanding or agreement at the time the conveyance was made. Thus, the Court concluded that the trial

²⁶ Id.

²⁷ Brock, citing Ford v. Ford, 243 Ga. 763(1), 256 S.E.2d 446 (1979) (testimony that husband placed house in wife's name to protect property from prospective creditors but intended to maintain joint interest therein insufficient to overcome presumption in absence of understanding or agreement with wife); Scales v. Scales, 235 Ga. 509, 220 S.E.2d 267 (1975) (evidence husband conveyed property to wife to protect it from potential creditors insufficient to rebut presumption of gift).

court erred in finding that Wife held the property in trust for Husband and awarding the marital home to Husband. The Supreme Court unfortunately did not address whether Husband's gift of his separate property to Wife converted the property to Wife's separate property, or whether the gift converted the property into marital property.

Post Lerch²⁸

Lerch certainly imparts that changing title of real property may indeed create a marital interest in separate property. However, based on the Georgia Supreme Court's distinction of the holding in Lerch to that in Grissom v. Grissom, Lerch may be more narrowly construed than initially thought.²⁹ Both Lerch and Grissom deal specifically with cases determined pursuant to prenuptial agreements, where the prenuptial agreements both provided for specific acts which would manifest intent to transform separate property to marital. In Grissom, the husband refinanced his separate real property and conveyed the property as joint tenants with right of survivorship; however, since he claimed he had no knowledge of the change of ownership and that the change was not his intention, the Court reversed and remanded to determine Husband's intent and the circumstances surrounding the change.³⁰ "[I]t is not clear that the conveyances were legitimate."³¹ The Grissom holding seems to attempt to narrow the interpretation of Lerch, and to limit a blanket application regarding all changes in title from separate to joint.

²⁸ Georgia Appellate Courts have cited Lerch only once as of July 2008. See Grissom v. Grissom, 282 Ga. 267 (2007).

²⁹ Grissom v. Grissom, 282 Ga. 267, 269 (2007).

³⁰ 282 Ga 267.

³¹ Id. at 270