It pays to prove what's your separate property in a divorce

If you are facing divorce, a significant issue will be determining what is your *separate* property, what is your spouse's *separate* property, and what is *community* or *marital* property. This is because family courts in Texas only have jurisdiction to divide what is considered *marital* property between the parties according to state divorce law. The courts in this state also have jurisdiction to set aside separate property to its rightful owner in divorce cases.

Separate property would include anything you owned prior to the marriage -- real estate, investments, retirement accounts secured before your marriage, furniture, cash, personal belongings, jewelry, vehicles, antiques, collectables, etc. If any of these items has increased in value during the marriage, the increase in value remains your separate property. That is why keeping excellent financial records, receipts and documentation is very important to prove separate property and its value at the time of marriage.

Generally, marital property is property acquired during the marriage, even if this property is not specifically titled in both spouses' names. Yet, there are exceptions to this. It is important to consider how the property was acquired during the marriage when determining if it is marital.

Here are *some* assets that are considered *separate* property by Texas law even if acquired during a marriage: an inheritance in the form or cash or property, proceeds from a lawsuit involving you as an individual, and gifts or bequests to you during the marriage from your spouse, friend or family member.

Things get murky, however, if you mix or comingle separate property with marital property over the years. This is called "transmutation of property," meaning that non-marital property may be transformed into marital property. However, if a paper trail exists in the form of account statements, for example, a certified divorce financial analyst or a forensic accountant may be able to trace or track where the separate property begins and ends. These financial experts can calculate how much your separate property has appreciated.

My client, Mary, was blessed over the years by a generous mother, who made yearly gifts directly into mutual funds held jointly with Mary. Over the 34 years of marriage, Mary pulled funds out to support the family as needed to supplement rather meager earnings of her husband. Hundreds of times, dividends were reinvested along with capital gains distributions. Upon her mom's death in 2011, the accounts became entirely Mary's (and partially her husband's).

Mary and her husband assumed that the accounts were too mingled to ever separate. However, with 1,000s of pages of historical statements provided by Fidelity, Merrill

Lynch, Templeton funds and others, we pieced together a financial puzzle through tracing.

Starting in 1987 with the first gift by mom, I did “line-by-line” tracing, entering every transaction, every buy, sell, dividend, capital gain, withdrawals, etc. As the puzzle was assembled, the picture became clear, showing accurately the amount of community shares and separate property shares. We were able to show that over 95 percent of the funds were Mary’s separate property.

Why such a high percentage when so much was earned in dividends and interest that is community property? Because of a rule in Texas called “community out first.” Whenever there are community shares or cash held in the account and a distribution is made, that distribution comes first from the community portion, then is supplemented by separate if needed. Due to the 100s of thousands of dollars in distributions and liquidations, the remaining mutual funds were almost entirely hers.

For the IRAs funded by Mary’s mom, the results weren’t so one-sided. Since there were penalties and taxes for early withdrawal, the community portion wasn’t withdrawn. The continual reinvestment of community dividends into new shares and the continued capital gains divided between community and separate, resulted in 24 percent of the account being community property. Due to the excellent records kept, and our tracing efforts, Mary had a real accounting of the finances that could be proven.

For more information on getting help with your divorce finances, contact Patricia Barrett: pb@lifetimeplanning.cc, or call 832-858-0099.