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**TRAFFIC JAM:
At the Intersection of Community Property,
Probate, and Bankruptcy**

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Traffic Jam: at the Intersection of Community Property, Probate, and Bankruptcy

The laws of community property, probate, and bankruptcy frequently intersect in ways that can impact the administration of bankruptcy cases. Often involving complex analyses of fact and law, those intersections can be a mare's nest to have to navigate, particularly where the stakes are high (e.g. high-value assets are in question, substantial creditor claims are at issue). The difficulty of handling these situations can be compounded by the substantial likelihood that emotional attachment will be involved (as it often is when familial disputes occur). Because of the frequency with which these three aspects of the legal system intersect, few and far between are the consumer bankruptcy practitioners who do not have to endure from time to time the legal traffic jam that occurs when two or more of them come to a crossroad.

This paper attempts to succinctly outline the interplay between community property, probate, and bankruptcy in the context of the laws of the Texas,¹ focusing on some of the basic principles underpinning each field of law and some of the more prominent ways in which they will intersect with each other. At the end of the paper are several recent opinions arising out of matters arising in bankruptcy courts in the Fifth Circuit which consumer bankruptcy practitioners may find useful to have in their repertoire.

¹ Because not all community property states are the same, and because not all state's probate laws are the same, it would not be advisable to extrapolate many of the statements made herein to other jurisdictions, a fact which further underscores the complexity of the community property, probate, bankruptcy intersection.

Basic Backdrop

In community property states like Texas that have a dual-regime of community and separate property, the administration of both probate and bankruptcy estates can sometimes be made more complex where questions exist with respect to whether certain assets actually entered the estate in question. For instance, the spouse of a decedent or a debtor may claim that a particular asset is his/her separate property but other parties-in-interest may claim that that same asset is actually community property. This equation can be similarly compounded where divorce is involved.

The probate process and the bankruptcy process are niche legal proceedings that have many similarities to them.² At their core, both are aimed at utilizing a statute-driven process to determine who will be entitled to share in assets belonging to the estate of the decedent/debtor. Furthermore, both rely upon specialized courts exercising in rem jurisdiction over property that is to be administered by a fiduciary.

While the probate system and the bankruptcy system function on separate planes, there is often overlap and interaction between them. It is not uncommon, for instance, for probate estates to have claims against bankruptcy estates, and vice versa. Because the jurisdictional authority exercised by probate courts and bankruptcy courts will appear to intersect regularly, a substantial amount of case-law has developed addressing the issue of which

² For a basic primer on probate law, we recommend reading "A Texas Probate Passport: A guide to probate and estate planning in Texas", prepared and made available to the public by the Texas Young Lawyers' Association, <http://www.tyla.org/tyla/assets/File/38668TexasProbatePassportWebReady.pdf>.

court should adjudicate specific types of disputes.

Each of the three topics (community property, probate, and bankruptcy) are specialized enough that the casual practitioner should be wary of merely dabbling in them, yet that is what many of us as consumer bankruptcy practitioners must do. In a legal economy that increasingly values specialization, consumer bankruptcy attorneys nevertheless must be at a minimum moderately well-versed in community property law and will likely have multiple occasions over the course of a career to learn how to interpret the relationship between probate law and bankruptcy law.

Community Property: Yours, Mine, Ours

Community Property Regimes

There are nine states that have community property laws: Arizona, California, Idaho, Louisiana, Nevada, New Mexico, Texas, Washington, and Wisconsin.³ In community property states, a married person may own property either as community property or as separate property. Under Texas law, community property consists of all property, other than separate property, acquired by either spouse during a marriage.⁴ Property possessed by either spouse during a marriage is presumed to be community property and the burden of proof to show otherwise is clear and convincing evidence.⁵ The presumption is strong enough, for instance, that the mere fact that a vehicle is titled in the name of only one spouse is

³<https://family.findlaw.com/divorce/community-property-overview.html>. The Territory of Puerto Rico also has community property laws, as do some Native American tribes, and Alaska and Tennessee have opt-in community property system (Alaska Stat. § 34.77.090 and Tennessee Code Title 35 Chapter 17 et seq.)

⁴ Tex. Fam. Code § 3.002.

⁵ Tex. Fam. Code § 3.003.

insufficient to rebut the community property presumption.⁶ The presumption is strong enough that rebutting it requires evidence sufficient to meet the clear and convincing standard.⁷

When a bankruptcy is filed, a bankruptcy estate is automatically created that, with limited exceptions, includes all property in which the debtor had a legal or equitable interest.⁸ State law will determine whether property is to be classified as separate or community for bankruptcy purposes.⁹ Community property is specifically included in the bankruptcy estate regardless of whether both spouses file the bankruptcy petition.¹⁰

Joint Management v. Sole Management

A potentially critical distinction that arises when only one spouse files for bankruptcy is that between joint management community property and sole management community property. Under the Bankruptcy Code, community property that is under the sole management of the non-debtor may be excluded from the bankruptcy estate, depending on whether it is subject to recovery for a claim against the debtor or a claim against the debtor and the debtor's spouse.¹¹ Sole management community property is roughly defined as that property which, although it had been acquired during the marriage, would have belonged to the one spouse if he/she had been single.¹² Or, as the statute more densely phrases it:

⁶ *Lusk v. General Motors Acceptance Corp.*, 395 S.W.2d 847, 850 (Tex. App.—Tyler 1965, no writ).

⁷ Tex. Fam. Code § 3.003.

⁸ 11 U.S.C. 541(a)(1).

⁹ *In re McCloy*, 296 F.3d 370, 373 (5th Cir. 2002).

¹⁰ 11 U.S.C. 541(a)(2).

¹¹ 11 U.S.C. 541(a)(2)(A) and (B).

¹² *Montemayor v. Ortiz*, 208 S.W.3d 627 (Tex. App.—Corpus Christi 2006, pet. denied).

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