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The Separate **Property Credit** in Divorce Actions

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Rules that grant discretionary authority to the court promote flexibility at the price of uncertainty and expense. The history of the separate property credit provides a vivid example of this dilemma, offering shifting and uncertain rules that make counseling a client difficult and costly.

Marital Residence

The Equitable Distribution Law is founded on the principle that "separate property"—property "acquired before marriage" or "by bequest, devise, or descent, or gift from a party other than the spouse"—"shall remain such." DRL §236(B)(1)(d) and (5)(b).

Since the dawn of the EDL, courts have interpreted this principle to warrant, upon divorce, reimbursement to a party who contributes separate property to acquire a residence irrespective of the form in which title is taken. *Duffy v. Duffy*, 94 A.D.2d 711 (2d Dept. 1983); *Parsons v. Parsons*, 101 A.D.2d 1017 (4th Dept. 1984); *Nalbandian v. Nalbandian*, 135 A.D.2d 621 (2d Dept. 1987); *Lisetza v. Lisetza*, 135 A.D.2d 20 (3d Dept. 1988); *Lolli-Ghetti v. Lolli-Ghetti*, 165 A.D.2d 426 (1st Dept. 1991); *Pauk v. Pauk*, 232 A.D.2d 386 (2d Dept. 1996); *Judson v. Judson*, 255 A.D.2d 656 (3d Dept. 1998); *Murphy v. Murphy*, 4 A.D.3d 460 (2d Dept. 2004); *Juhasz v. Juhasz*, 59 A.D.3d 1023 (4th Dept. 2009); *Wyser-Pratte v. Wyser-Pratt*, 68 A.D.3d 624 (1st Dept. 2009); *Fields v. Fields*, 15 N.Y.3d 158, 165-66 (2010).

This principle also applies to separate property that is rolled over into successive purchases. *Cunningham v. Cunningham*, 105 A.D.2d 997 (3d Dept. 1984); *Lolli-Ghetti*, supra.

Other Forms of Property

The credit is not restricted to marital residences. *Coffey v. Coffey*, 119 A.D.2d 620 (2d Dept. 1986) (certificates of deposit); *Lauricella v. Lauricella*, 143 A.D.2d 642 (2d Dept. 1988) (savings bonds); *Burns v. Burns*, 193 A.D.2d 1104 (4th Dept. 1993), modified on other

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grounds, 84 N.Y.2d 369 (1994) (payment of marital debts).

Standard of Proof

Uncertainty arises, however, because the standard of proof for a credit in a marital residence is unclear. In *Shkreli v. Shkreli*¸142 A.D.3d 546 (2d Dept. 2016), the husband was denied a separate property credit in a marital residence because his testimony alone did not "trace the source" of the separate property or prove its value. In *Iacomo*, the husband, failing to "offer clear and convincing evidence to substantiate the specific amount claimed" or intent to create "a marital beneficial interest," was denied the credit for separate property contributed to the jointly owned home. *Iacomo v. Iacomo*, 145 A.D.3d 972 (2d Dept. 2016), citing *Renck*, infra. Historically, the standard was less stringent. *Cleary v. Cleary*, 171 A.D.2d 1076 (3d Dept. 1991); *Zurner v. Zurner*, 213 A.D.2d 906 (3d Dept. 1995). The credit is available regardless of whether the separate property is used to acquire an asset or title to a separate property asset is transferred to marital names. *Myers v. Myers*, 119 A.D.3d 1114 (3d Dept. 2014).

The appellate courts' articulation of the standard of proof for a credit in a financial account is similarly inconsistent. In *DeGroat v. DeGroat*, 84 A.D.3d 1012 (2d Dept. 2011), the husband commingled in a joint account the proceeds from the redemption of pre- and post-marriage stock options. The court found he was not entitled to any credit for the value of the pre-marital options, having failed to trace the separate property with "sufficient particularly" (implying that had he produced documentation as to deposits and withdrawals, he would have been entitled to the credit). The court did not explain what "sufficient particularity" means under Banking Law §675. But in *Renck v. Renck*, 131 A.D.3d 1146 (2d Dept. 2015), the court held that to rebut the §675 presumption, the husband was required to produce "clear and convincing evidence" that the commingling in a joint account was done merely for convenience. The statute did not change between the two decisions, yet the standard apparently did.

The burden of proof for a separate property credit may be met by a party's uncorroborated testimony where the record contains no evidence of an alternative source for the funds. *Heine v. Heine*, 176 A.D.2d 77 (1st Dept. 1992); *Zanger v. Zanger*, 1 A.D.3d 865 (3d Dept. 2003); *Juhasz v. Juhasz*, 59 A.D.3d 1023, supra, (4th Dept. 2009). However, this rule will not be applied where a party offers even undocumented contradictory testimony of the source. *Cassara v. Cassara*, 1 A.D.3d 817 (3d Dept. 2004). Contrast *McLoughlin v. McLoughlin*, 63 A.D.3d 1017 (2d Dept. 2009) (credit overturned where the wife did not support her claim with "other evidentiary support").

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Entitlement or Discretion

While many cases use the word "entitled" to describe the credit, more recent cases have retreated from the entitlement language without discussion. For example, in *Fields*, 15 N.Y.3d at 167, the court noted that there is "no single template that directs how courts are to distribute a marital asset that was acquired, in part or in whole, with separate property funds … . [C]ourts have usually given the spouse who made [a] separate property contribution" to the acquisition of a marital asset "a credit for such payment." Unexplained changes like this create uncertainty, making settlement more difficult to achieve.

The Rules Change Again

In *Klauer v. Abeliovich*, 2017 NY Slip Op. 03110 (1st Dept. 2017), during the marriage, the parties purchased a cooperative apartment in their joint names, which they sold, and used part of the proceeds to purchase a condominium in joint names. The trial court granted the wife's application for a separate property credit of $350,000 toward the purchase price. The First Department reversed, noting that the wife used the money to purchase the coop in the parties' joint names, they lived in it "as an intact [family] unit," and then reinvested the net profits of the first sale into the condo acquisition. "The conveyance of separate funds under these circumstances resulted in the separate assets becoming presumptively marital (see *Fields*, 15 N.Y.3d at 167)" because there is a statutory presumption that commingled separate property is "committed to the marriage," citing *Fields*, 15 N.Y.3d at 165-167. The court also evidenced a disinclination to explore the "economic decisions made by parties in an intact marriage," citing

Mahoney-Buntzman v. Buntzman, 12 N.Y.3d 415, 421 (2009).

In *Lolli-Ghetti*, the court had no problem with the credit despite the fact that the separate funds were rolled over through three residences in two years, a pace of transfers that matches the facts in *Klauer*. The decision in *Klauer* does not refer to any complexity in the rollover to justify refusing to give the credit. The argument that the parties lived in the home as an intact family, which is the nature of a marital residence—that the commingled separate property was "committed to the marriage"—is true regardless of the presence of successive purchases and should therefore bar the credit in all cases.

The court found the "plaintiff also failed to rebut the statutory presumption that the separate property was not commingled or committed to the marriage (see *Fields*, 15 N.Y.3d at 165-66)." This language warrants analysis. Though the court referred to the statutory presumption that assets acquired during the marriage are marital, there is no presumption that separate property loses its separate character merely because it is commingled with marital property. For at least 34 years and as recently as 2010 in *Fields*, courts have recognized the credit even in jointly owned property. There is also no statutory presumption that relates to whether separate property was "committed to the marriage." In *Fields*, the parties lived in the marital residence for 30 years. In *Heine*, the parties lived together in the marital residence for 16 years. In both cases, the husband's down payments were surely "committed" to their respective residences, yet each was awarded a separate property credit. In *Klauer*, the parties lived together in the residence for two years and the wife was denied the credit. This kind of vague, subjective criterion invites litigation.

Citing *Heine*, supra, as an example of a properly awarded direct separate property credit, the court did not entirely foreclose direct separate property credits. But on this score, *Heine* offers no guidance. The parties had resided together in the marital residence for over 16 years and they extensively renovated it. There was no discussion about what facts warranted the credit, probably because at that time the credit was an entitlement. While *Heine* validates an inferential process for establishing a separate property credit, it does not rebut the fact that the down payment was unquestionably commingled. Read together, *Heine* and *Klauer* incongruously hold that inferentially based separate property credit arguments have a greater claim to recognition than claims based on unrebutted, direct, documentary evidence.

Rejecting a direct claim for a separate property credit, the *Klauer* court held that the same claim can and should be addressed indirectly. Rather than "using a scalpel to finely adjust for separate property contributions dollar-for-dollar over the course of the entire marriage, a court should effectuate an equitable distribution of marital assets, taking into account all relevant factors, including relative or disproportionate financial contributions (*Mahoney-Buntzman*, 12 N.Y.3d at 420, 421)." See, e.g., *Shkreli v. Shkreli*¸142 A.D.3d 546 (2d Dept. 2016). However, there is no assurance that these two approaches will produce similar outcomes. Counsel must spend the time presenting evidence for the claim without being able to conduct any meaningful cost-benefit analysis since the evidence in support of the credit is relevant irrespective of which approach the court takes. Furthermore, the assertion of equivalence is weakened by the necessarily indeterminate nature of an "equitable" distributive mechanism. Without published decisions that include an explicit comparison of outcomes, the assertion is untestable and uncertainty reigns.

What Are the Rules?

In *Todres v. Freifeld*, 2017 NY Slip Op. 04905 (1st Dept. 2017), the court held that the trial court "correctly credited each spouse for their separate property contributions to the purchase of the" marital residence without discussing *Klauer* or providing any guidance for distinguishing it from *Todres*. Read together, these cases, decided within six months of each other, underscore how difficult it is for lawyers to advise clients about the rules controlling separate property credits.