APPORTIONMENT OF INCOME FROM A SPOUSE'S SEPARATELY OWNED PROPERTY

California, in accordance with the majority of community property states, provides that the rents and profits from a spouse's separate property are also separate property.¹ The earnings of either spouse, however, form the essence of the community property system,² and are clearly allocable to the community.³ If either spouse devotes time, labor, and skill during marriage to the production of income from separate property, these two concepts come into direct conflict.⁴ In such cases problems arise whether the income should be divided between the community and separate interests,⁵ and if so, what method of apportionment should be used.⁶ In California, the proceeds of such separately owned property are theoretically com-

¹ CAL. CIV. CODE § 162: "All property of the wife, owned by her before marriage, and that acquired afterwards by gift, bequest, devise, or descent, with the rents, issues, and profits thereof, is her separate property." CAL. CIV. CODE § 163: "All property owned by the husband before marriage, and that acquired afterwards by gift, bequest, devise, or descent, with the rents, issues, and profits thereof, is his separate property."

In Arizona, Nevada, New Mexico, and Washington the rents and profits of separate property remain separate. ARIZ. REV. STAT. ANN. § 25-213 (1956); NEV. REV. STAT. § 123.130 (1957); N.M. STAT. ANN. §§ 57-3-4, -5 (1953); WASH. REV. CODE §§ 26.16.010, .020 (1961). In Idaho, Louisiana, and Texas they are community property. IDAHO CODE ANN. § 32-903 (1948); LA. REV. STAT. arts. 2334-35, 2386, 2402 (1952); TEX. REV. CIV. STAT. ANN. arts. 4613-14 (1960). See generally 2 AMERICAN LAW OF PROPERTY § 7.12 (Casper ed. 1952); BURBY, CASES ON COMMUNITY PROPERTY 142 (1933); 4 POWELL, REAL PROPERTY 684 n.41 (1954); 2 TIFFANY, REAL PROPERTY § 439 (3d ed. 1939); 3 VERNIER, AMERICAN FAMILY LAWS 210-12 (1935).

² BALLINGER, COMMUNITY PROPERTY § 11 (1895) [hereinafter cited as BALLINGER]; BURBY, REAL PROPERTY § 204 (2d ed. 1954); DE FUNIAK, PRINCIPLES OF COMMUNITY PROPERTY § 66 (1943) [hereinafter cited as DE FUNIAK]; MCKAY, COMMUNITY PROPERTY § 296 (2d ed. 1925); EVANS, *Primary Sources of Acquisition of Community Property*, 10 CALIF. L. REV. 271 (1922); POMEROY, *Community Property*, 4 WEST COAST RPTR. 305 (1884); see *Yesler v. Hochstetler*, 4 Wash. 349, 30 Pac. 398 (1892).

³ *Washburn v. Washburn*, 9 Cal. 475, 476 (1858); 4 WITKIN, SUMMARY OF CALIFORNIA LAW 2720 (7th ed. 1960); see *Martin v. Southern Pac. Co.*, 130 Cal. 285, 62 Pac. 515 (1900); *Bekins v. Dieterle*, 5 Cal. App. 690, 91 Pac. 173 (1907).

⁴ See HUIE, TEXAS CASES ON MARITAL PROPERTY 214 (1955); MCKAY, *op. cit. supra* note 2, at § 289; WOOD, THE COMMUNITY PROPERTY LAW OF NEW MEXICO §§ 39-40 (1954); EVANS, *supra* note 2, at 279.

⁵ Neither Arizona nor Nevada seem to make any apportionment. See *Rundle v. Winters*, 38 Ariz. 239, 298 Pac. 929 (1931); *Ormachea v. Ormachea*, 67 Nev. 273, 217 P.2d 355 (1950). See also *Guthrie v. Guthrie*, 73 Ariz. 423, 242 P.2d 549 (1952); *Lawson v. Ridgeway*, 72 Ariz. 253, 233 P.2d 459 (1951); *Porter v. Porter*, 67 Ariz. 273, 195 P.2d 132 (1948); *Anderson v. Anderson*, 65 Ariz. 184, 177 P.2d 227 (1947); *Estate of Torrey*, 54 Ariz. 369, 95 P.2d 990 (1939); *Youngworth v. Jewell*, 15 Nev. 45 (1880); *Grimes v. Grimes*, 52 F.2d 171 (D. Nev. 1931). Washington makes an apportionment in certain cases. See *Hamlin v. Merlino*, 44 Wash. 2d 851, 272 P.2d 125 (1954); *Estate of Dewey*, 13 Wash. 2d 220, 124 P.2d 805 (1942). See also *Jacobs v. Hoitt*, 119 Wash. 283, 205 Pac. 414 (1922); *Yesler v. Hochstetler*, 4 Wash. 349, 30 Pac. 398 (1892). New Mexico seems to treat the problem in the same manner as California. See *Laughlin v. Laughlin*, 49 N.M. 20, 155 P.2d 1010 (1944); *Katson v. Katson*, 43 N.M. 214, 89 P.2d 524 (1939). See generally Annot., 29 A.L.R.2d 530 (1953).

⁶ See King, *The Challenge of Apportionment*, 37 WASH. L. REV. 483 (1962). In New Mexico and Washington the community seems to be limited to the salary that the husband draws from the business. See *Katson v. Katson*, 43 N.M. 214, 89 P.2d 524 (1939); *Hamlin v. Merlino*, 44 Wash. 2d 851, 272 P.2d 125 (1954); *Estate of Dewey*, 13 Wash. 2d 220, 124 P.2d 805 (1942). In New Mexico the income from a farm is apportioned in accord with the rule established in *Pereira v. Pereira*, 156 Cal. 1, 103 Pac. 488 (1909). *Laughlin v. Laughlin*, 49 N.M. 20, 155 P.2d 1010 (1944); see text accompanying notes 9-10 *infra*.

munity property to the extent they reflect the effort of the spouses, and separate to the extent they reflect the earning power of the separate property itself.⁷ In practice, however, it is not clear how this theoretical apportionment is to be made.⁸ An analysis of this problem, including a proposed solution, is the main objective of this comment.

The early cases of *Pereira v. Pereira*⁹ and *Estate of Pepper*¹⁰ are at the root of the existing confusion in California. The *Pereira* case held that when a husband continues to work after marriage in his separately owned business, the revenue from the business must be apportioned between the community and his separate estate. In making this apportionment, the California Supreme Court decided that the husband's separately owned capital, invested in what was a profitable business, should be credited with at least the legal interest rate,¹¹ with the remainder of the business profits going to the community. But, one year later in *Estate of Pepper*,¹² the same court refused to apportion the proceeds of the husband's separately owned nursery business because such proceeds were products of the land. The entire business profit was held to be the husband's separate property, notwithstanding the fact that during the marriage the husband devoted his time and labor exclusively to running the nursery.¹³

In *Estate of Neilson*,¹⁴ decided in May of 1962, the California Supreme Court overruled the *Pepper* case, holding that profit resulting from the sale of products of land could be apportioned in the same manner as profits from other commercial ventures.¹⁵ In *Neilson* Justice Traynor set forth a method of apportionment based on several relevant California cases.¹⁶ These cases, however, do not appear to be reconcilable, since they rely to some extent on the basically conflicting doctrines of *Pepper* and *Pereira*.¹⁷ Consequently, the extent to which *Neilson* expunges the influence of *Pepper* and resolves the problems of apportionment is not

⁷ *Estate of Neilson*, 57 Cal. 2d 733, 740, 371 P.2d 745, 749, 22 Cal. Rptr. 1, 4-5 (1962); *Huber v. Huber*, 27 Cal. 2d 784, 792, 167 P.2d 708, 713 (1946); *Estate of Gold*, 170 Cal. 621, 623, 151 Pac. 12, 13 (1915); *Pereira v. Pereira*, 156 Cal. 1, 7, 103 Pac. 488, 491 (1909); see Annot., 55 A.L.R.2d 960, 965 (1957).

⁸ See *Strohm v. Strohm*, 182 Cal. App. 2d 53, 62, 5 Cal. Rptr. 884, 889 (1960); *Tassi v. Tassi*, 160 Cal. App. 2d 680, 690, 325 P.2d 872, 878 (1958); 4 WITKIN, SUMMARY OF CALIFORNIA LAW 2725 (7th ed. 1960).

⁹ 156 Cal. 1, 103 Pac. 488 (1909).

¹⁰ 158 Cal. 619, 112 Pac. 62 (1910).

¹¹ 156 Cal. at 7, 103 Pac. at 491.

¹² 158 Cal. 619, 112 Pac. 62 (1910).

¹³ *Id.* at 624, 112 Pac. at 64. See VERRALL, CASES ON CALIFORNIA COMMUNITY PROPERTY 117-18 (1960).

¹⁴ 57 Cal. 2d 733, 371 P.2d 745, 22 Cal. Rptr. 1 (1962).

¹⁵ *Id.* at 740, 371 P.2d at 749, 22 Cal. Rptr. at 4-5. The holding in *Neilson* overruling *Pepper* was reaffirmed by the California Supreme Court in *Mayhood v. La Rosa*, 58 A.C. 510, 374 P.2d 805, 24 Cal. Rptr. 837 (1962), and in *Machado v. Machado*, 58 A.C. 513, 375 P.2d 55, 25 Cal. Rptr. 87 (1962).

¹⁶ *Estate of Arstein*, 56 Cal. 2d 239, 364 P.2d 33, 14 Cal. Rptr. 809 (1961); *Gilmore v. Gilmore*, 45 Cal. 2d 142, 287 P.2d 769 (1955); *Harrold v. Harrold*, 43 Cal. 2d 77, 271 P.2d 489 (1954); *Huber v. Huber*, 27 Cal. 2d 784, 167 P.2d 708 (1946); *Pereira v. Pereira*, 156 Cal. 1, 103 Pac. 488 (1909); *Estate of Cudworth*, 133 Cal. 462, 65 Pac. 1041 (1901); *Tassi v. Tassi*, 160 Cal. App. 2d 680, 325 P.2d 872 (1958); *Randolph v. Randolph*, 118 Cal. App. 2d 584, 258 P.2d 547 (1953); *Logan v. Forster*, 114 Cal. App. 2d 587, 250 P.2d 730 (1952); *Jenkins v. Jenkins*, 110 Cal. App. 2d 663, 243 P.2d 79 (1952); *Stice v. Stice*, 81 Cal. App. 2d 792, 185 P.2d 402 (1947); *Cozzi v. Cozzi*, 81 Cal. App. 2d 229, 183 P.2d 739 (1947); *Witaschek v. Witaschek*, 56 Cal. App. 2d 277, 132 P.2d 600 (1942); *Estate of Barnes*, 128 Cal. App. 489, 17 P.2d 1046 (1932); *McDuff v. McDuff*, 48 Cal. App. 175, 191 Pac. 957 (1920).

¹⁷ See text following note 164 *infra*.

clear. The holdings of *Pepper* and *Pereira*, and the inconsistent manner in which subsequent cases have applied the two decisions, may still leave some uncertainty concerning the proper method for apportioning profits.¹⁸

While otherwise adopting the common law,¹⁹ the framers of the first California constitution chose to retain²⁰ the civil law community property system.²¹ Common law principles, however, infiltrated that system in *Pereira*²² and *Pepper*,²³ thus initially contributing to the confusion.²⁴ A complete analysis of *Neilson*, therefore, must begin with the cases leading up to *Pereira* and *Pepper*. Such an historical treatment is undertaken in part I of this comment.²⁵ Part II develops the law from *Pereira* and *Pepper* to *Neilson*,²⁶ and part III discusses the present impact of *Neilson*.²⁷ Finally, part IV proposes a method of apportionment for successful²⁸ and losing²⁹ businesses.

I

EARLY DEVELOPMENT OF THE PROBLEM

A. Rents and Profits of Separate Property Are Not Solely Community Property

The community property system was in force when California was under Mexican rule,³⁰ and it was from the Spanish-Mexican civil law that the present community property system was derived.³¹ Under the Spanish-Mexican system the

¹⁸ See note 8 *supra*. See also 1 DEFUNIAK § 72, at 14 (Supp. 1948).

¹⁹ CONMY, THE HISTORIC SPANISH ORIGIN OF CALIFORNIA'S COMMUNITY PROPERTY LAW 9 (1957) [hereinafter cited as CONMY]; McMurray, *The Beginnings of the Community Property System in California and the Adoption of the Common Law*, 3 CALIF. L. REV. 359, 373-76 (1915).

²⁰ See Huie, *The Texas Constitutional Definition of the Wife's Separate Property*, 35 TEXAS L. REV. 1054 (1957).

²¹ See note 31 and text accompanying note 46 *infra*.

²² See text following note 111 *infra*.

²³ See text following note 183 *infra*.

²⁴ The earlier decision in *George v. Ransom*, 15 Cal. 322 (1860), relied on common law notions to create the problem of apportionment in the first place, and without this decision the rents and profits of separate property would have been classified as wholly community property. See text following note 37 *infra*.

²⁵ See text following note 29 *infra*.

²⁶ See text following note 101 *infra*.

²⁷ See text following note 244 *infra*.

²⁸ See text following note 302 *infra*.

²⁹ See text following note 330 *infra*.

³⁰ 1 ARMSTRONG, CALIFORNIA FAMILY LAW 431 (1953) [hereinafter cited as ARMSTRONG]; CONMY 4.

³¹ *Stewart v. Stewart*, 199 Cal. 318, 249 Pac. 197 (1926); *Roberts v. Wehmeyer*, 191 Cal. 601, 218 Pac. 22 (1923); *Spreckels v. Spreckels*, 116 Cal. 339, 48 Pac. 228 (1897); *Packard v. Arellanes*, 17 Cal. 525 (1861); 2 AMERICAN LAW OF PROPERTY §§ 7.2, .3 (Casner ed. 1952); CONMY 2-9; MCKAY, COMMUNITY PROPERTY § iii (1st ed. 1910); OGDEN, CALIFORNIA COMMUNITY PROPERTY LAW § 4.2 (1956); Powell, *Community Property—A Critique of Its Regulation of Intra-Family Relations*, 11 WASH. L. REV. 12, 26-27 (1936).

In accordance with ordinary principles of international law, this legal system remained in force after California was ceded to the United States in the Treaty of Guadalupe Hidalgo. *Estate of Buchanan*, 8 Cal. 507 (1857); *Fowler v. Smith*, 2 Cal. 568, 569 (1852); *Kirkwood, Historical Background and Objectives of the Law of Community Property in the Pacific Coast States*, 11 WASH. L. REV. 1, 3 (1936). The Treaty of Guadalupe Hidalgo guaranteed that the property rights of Mexicans residing in California would not be affected by the ceding of California to the United States. 1 ARMSTRONG 432; see CONMY 5. See also 2 WITKIN, SUMMARY OF CALIFORNIA LAW *Real Property* § 2 (7th ed. 1960).

revenue from a spouse's separate property went into the community.³² This principle was based on the realization that "most things till touched by the hand of man are wholly unproductive,"³³ and the concept that each spouse is primarily interested in the welfare of the community.³⁴ The original California constitution, adopted in 1849, included the following clause:

All property, both real and personal of the wife, owned or claimed by her before marriage, and that acquired afterward by gift, devise or descent shall be her separate property; and the laws shall be passed more clearly defining the rights of the wife, in relation as well to her separate property, as to that held in common with her husband.³⁵

The first California legislation dealing with community property followed the Spanish law, and provided that the rents and profits of either spouse's separate property belonged to the community.³⁶

In *George v. Ransom*,³⁷ the California Supreme Court, relying on the aforesaid constitutional definition of the wife's separate property, held the legislation invalid with regard to income from the wife's separate estate.³⁸ Such income was held to be her separate property. The reasoning of *George* was that the common law background of the framers of the constitution, coupled with the tendency in common law jurisdictions to recognize the rights of a wife to hold and administer property in her own name,³⁹ was responsible for the adoption of the constitutional section⁴⁰ in question. Thus, the court held that:

This term "separate property" has a fixed meaning in the common law, and had in the minds of those who framed the Constitution, the large majority of whom were familiar with, and had lived under that system. . . . It is not perceived that property can be in one, in fixed and separate ownership, with a right in another to control and enjoy all its benefits.⁴¹

The facts of *George* presented the court with a situation in which a creditor of the husband was attempting to attach the dividends of stock owned separately by the

³² Estate of Hale, 2 Cal. Prob. Dec. 191, 200 (1906); Fuller v. Ferguson, 26 Cal. 546 (1864); Scott v. Ward, 13 Cal. 458, 471 (1859); LOEB, THE LEGAL PROPERTY RELATIONS OF MARRIED PARTIES 68 (1900); SCHMIDT, THE CIVIL LAW OF SPAIN AND MEXICO pt. 2, at 13 (1851) (art. 44(2)); 1 WHITE, A NEW COLLECTION OF LAWS OF GREAT BRITAIN, FRANCE AND SPAIN 61-62 (1839); Loewy, *The Spanish Community of Acquests and Gains and Its Adoption and Modification by the State of California*, 1 CALIF. L. REV. 32, 40 (1912).

Under Mexican law this principle was defined in the following manner: "Maguer que el marido haya mas que la mujer, ó la mujer mas que el marido, quier en . . . mueble, . . . los frutos sean comunes de ambos á dos. . . ." ESCRICHE, DICCIONARIO RAZONADO DE LEGISLACION Y JURISPRUDENCIA 366 (1925).

³³ MCKAY, COMMUNITY PROPERTY § 176 (1st ed. 1910).

³⁴ DEFUNIAK § 71 n.43.

³⁵ Cal. Stats. 1949-1950, at 33 (art. 11, § 14).

³⁶ Cal. Stats. 1850, ch. 103, § 9.

³⁷ 15 Cal. 322 (1860).

³⁸ Prior to the decision in *George*, the statute had been recognized by the court as valid. Snyder v. Webb, 3 Cal. 83, 87 (1853).

³⁹ See 1 ARMSTRONG 432; VERRALL, CASES ON CALIFORNIA COMMUNITY PROPERTY 20 n.47 (1960); Schreter, "Quasi-Community Property" in the Conflict of Laws, 50 CALIF. L. REV. 206 (1962).

⁴⁰ See note 35 *supra* and accompanying text.

⁴¹ 15 Cal. at 324.

wife.⁴² The court's use of the common law⁴³ was apparently influenced by a desire to protect the wife.⁴⁴

The proceedings in the Constitutional Convention do not appear to support the conclusion reached by *George*.⁴⁵ Although it is not clear what motivated the delegates to adopt the community property system,⁴⁶ by passing the section as it

⁴² In the Spanish-Mexican system the wife's share of the community property was not liable for the separate debts of the husband. 1 DEFUNIAK § 160; MARSH, *MARITAL PROPERTY IN CONFLICT OF LAWS* 21 n.27 (1952); 2 TIFFANY, *REAL PROPERTY* § 441 (3d ed. 1939). However, in an early case the California Supreme Court used common law principles to determine that the community property was liable for the separate debts of the husband. *Van Maren v. Johnson*, 15 Cal. 308 (1860). Not grasping the true community property principles involved, 1 DEFUNIAK § 162, at 455-57 (see also Evans, *Community Obligations*, 10 CALIF. L. REV. 120, 123 (1921)), the court in *George* turned to the more familiar common law, see 1 ARMSTRONG 432, in order to protect the wife in this situation. See MARSH, *MARITAL PROPERTY IN CONFLICT OF LAWS* 20-21 (1952).

In Idaho, the original community property provision that the wife's share of the community property is not liable for the husband's debts is still retained by construing the statute exempting the wife's property from the husband's debts to apply to her half of the community property. IDAHO CODE ANN. §§ 32-906, 11-204 (1948); see JACOB, *COMMUNITY PROPERTY IN IDAHO* 37 (1943). In the Scandinavian countries the rents and profits of the wife's separate property belong to the community, but this particular class of community property is not liable for debts of the husband. LOEB, *LEGAL PROPERTY RELATIONS OF MARRIED PARTIES* 72 (1900).

⁴³ The use of common law principles to interpret the constitution in *George* clearly caused a departure from the Spanish-Mexican community property system. 1 DEFUNIAK § 160; McKAY, *COMMUNITY PROPERTY* § 795 (2d ed. 1925); 2 TIFFANY, *REAL PROPERTY* § 441 (2d ed. 1939); Clark, *New Mexico Community Property Law*, in CHARMATZ & DAGGETT, *COMPARATIVE STUDIES IN COMMUNITY PROPERTY* 81, 96 (1955); Lobingier, *The Marital Community: Its Origin and Diffusion*, 14 A.B.A.J. 211, 216 (1928).

Ironically, however, it has been pointed out that the use of the common law in *George* was not in itself entirely correct. CAL. JUR. *Community Property* § 39 n.14 (McMurray Supp. 1930). The courts of equity had recognized the rights of married women at an early date, POMEROY, *EQUITY JURISPRUDENCE* 15 (1883); STEWART, *HUSBAND AND WIFE* § 464 (1885); 2 STORY, *EQUITY JURISPRUDENCE* § 1367 (9th ed. 1866), but "at common law, without the intervention of equitable interests and principles, the rents of the wife were absolutely the husband's property, though her real property was her own," CAL. JUR. *Community Property* § 39 n.14 (McMurray Supp. 1930); and at common law the husband had the right to the present enjoyment of the wife's property, STEWART, *op. cit. supra* § 464. Thus, the common law could actually have been used to bolster a result more properly reached under the Spanish system, that rents and profits are community property. See 3 POMEROY, *EQUITY JURISPRUDENCE* 29 (1883); STEWART, *op. cit. supra* § 470; VERNIER, *AMERICAN FAMILY LAW* § 159 (1935); WELLS, *SEPARATE PROPERTY OF MARRIED WOMEN* 165 (1878); Horne, *Community Property—A Functional Approach*, 24 So. CAL. L. REV. 42, 45 (1950).

⁴⁴ Although the court was worried about protecting the wife, it is interesting to note that in the California Constitutional Convention, Mr. Lippitt, arguing for the adoption of the common law, was worried that creditors of the husband would not receive the protection under a community property system that they would under principles of common law. BROWNE, *THE DEBATES IN THE CONVENTION OF CALIFORNIA* 262 (1850) [hereinafter cited as BROWNE].

⁴⁵ CAL. JUR. *Community Property* § 39 n.14 (McMurray Supp. 1930); see BROWNE 257-69; Kirkwood, *Historical Background and Objectives of the Laws of Community Property in the Pacific Coast States*, 11 WASH. L. REV. 1, 4 (1936).

⁴⁶ During the debates, Secretary of State Halleck of Monterey stated:

I am not wedded either to the Common Law or the Civil Law, nor as yet to a women . . . I shall advocate this section in the Constitution, and I would call upon all the bachelors in this convention to vote for it. I do not think we can offer a greater inducement for women of fortune to come to California. It is the very best provision to get us wives that we can introduce into the Constitution.

was originally proposed the delegates manifested their intention that the community property system should be adopted.⁴⁷ Later cases seemed to accept this as the intention of the framers.⁴⁸ Furthermore, even though most of the justices of the California courts were schooled in the common law,⁴⁹ it was early realized that "our system . . . is borrowed from the civil and Spanish law, and we must look to these sources for . . . the rules and principles which govern its operation and effect."⁵⁰ Thus, it seems clear that the words "separate property" in the California constitution were not intended in their common law sense.⁵¹

A comparison between the history of the community property system in Texas with that of California may help to clarify the intent of the framers of the California constitution. In 1840 the Texas Congress decided to retain the Spanish community property system which had been in force before they gained their in-

⁴⁷ *Stewart v. Stewart*, 199 Cal. 318, 249 Pac. 197 (1926); *Dow v. Gould & Curry Silver Mining Co.*, 31 Cal. 629 (1867); *Robbins v. United States*, 5 F.2d 690 (1925); 1 *DEFUNIACK* 51; *CAL. JUR. Community Property* § 39 n.14 (McMurray Supp. 1930); *Kirkwood*, *supra* note 45, at 4; *Lobingier, The Marital Community: Its Origin and Diffusion*, 14 A.B.A.J. 211, 216 (1928); *Loewy, The Spanish Community of Acquests and Gains and Its Adoption and Modification by the State of California*, 1 CALIF. L. REV. 32, 33 (1912); *McMurray, The Beginnings of the Community Property System in California and the Adoption of the Common Law*, 3 CALIF. L. REV. 359, 369-73 (1915); see 1 *SCHOULER, MARRIAGE, DIVORCE AND SEPARATION* § 298 (6th ed. 1921).

In the convention, Mr. Lippitt, a delegate from San Francisco, proposed an alternative provision to the one adopted. *BROWNE* 257. This provision would have made it possible to later adopt the common law pertaining to the rights of married persons. *Ibid.* Mr. Lippitt admitted that he was "wedded to the common law," and argued that it was "the law under which nine-tenths of the people now in California were born and educated." *Id.* at 260. The debate in the convention revolved around the question whether the common or civil law should be adopted as the method for determining the property rights of married persons in California. *Racouillat v. Sansevan*, 32 Cal. 376, 385 (1867); *BROWNE* 257-69; 1 *DEFUNIACK* § 51, at 108; *Kirkwood*, *supra* at 3; see *Hitchcock, Modern Legislation Touching Marital Property Rights*, 6 So. L. Rev. N.S. 633, 656 (1880).

The California constitution provision was copied from the constitution of Texas, see note 53 *infra*; when this provision was written into the Texas constitution the intent of the Texas framers was to adopt the community property system. *Huie, The Texas Constitutional Definition of the Wife's Separate Property*, 35 TEXAS L. REV. 1054, 1055 (1957).

⁴⁸ In *Estate of Moffitt*, 153 Cal. 359, 363, 95 Pac. 653, 654 (1908), the court said, "it was the design of the constitution of 1849 to preserve . . . to the wives of the inhabitants of the new state . . . the rights to the community property which they had enjoyed under the Mexican rule." See *Stewart v. Stewart*, 199 Cal. 318, 249 Pac. 197 (1926); *Roberts v. Wehmeyer*, 191 Cal. 601, 218 Pac. 22 (1923); *In re Spencer*, 82 Cal. 110, 23 Pac. 37 (1889) ("separate property is a relative term; it implies the existence of the community").

⁴⁹ 1 *ARMSTRONG* 432.

⁵⁰ *Packard v. Arellanes*, 17 Cal. 525, 537 (1861). See also *Schuyler v. Broughton*, 70 Cal. 282, 11 Pac. 719 (1866). *But see Dow v. Gould & Curry Silver Mining Co.*, 31 Cal. 629 (1867); *cf. Van Maren v. Johnson*, 15 Cal. 308, 311-12 (1860); Preface, 1 Cal. v, vi (1851).

⁵¹ The decision in *George v. Ransom* has been widely criticized. *BALLINGER* §§ 22, 24; 1 *DEFUNIACK* §§ 71 at 183, 51 at 111; *McKAY, COMMUNITY PROPERTY* § 288 (2d ed. 1925); *Huie*, *supra* note 47, at 1059; *Lobingier, The Marital Community: Its Origin and Diffusion*, 14 A.B.A.J. 211, 216 (1928). Making the rents and profits of separate property the separate property of either spouse tends "to enasculate the community property system and further a trend toward a system of separate property in each spouse which may ultimately leave the community property system one in name only." 1 *DEFUNIACK* § 72, at 187. Such deviations from the Spanish-Mexican system should be made only after full consideration has been given to the problems which are likely to result. See *Huie*, *supra* at 1059-60. See also *BALLINGER* § 24; *McKAY, COMMUNITY PROPERTY* § 76, at 161 (1st ed. 1910).

dependence,⁵² and in 1845 that system was written into the Texas constitution.⁵³ The California constitutional provision involved in *George v. Ransom*⁵⁴ was copied verbatim from this Texas provision.⁵⁵ The California statute⁵⁶ providing that revenue from separate property should inure to the community was also modeled on a Texas provision.⁵⁷ In 1917 the Texas legislature, following California's lead in *George*,⁵⁸ changed their law to provide that the rents and profits of separate property should remain separate.⁵⁹ However, the Supreme Court of Texas, in *Arnold v. Leonard*,⁶⁰ held this statute to be unconstitutional. The court said that the constitution was exclusive; the only property acquired after marriage that could become the separate property of the wife was property acquired by "gift, devise or descent."⁶¹ Thus, the rents and profits of separate property were held to belong to the community.⁶²

The decision in *George v. Ransom* had no effect on the profits of the husband's property because his rights to hold property separately were not guaranteed in the constitution until 1879.⁶³ The court in *Lewis v. Lewis*⁶⁴ held that the rents and profits of the husband's separate property belonged to the community in accordance with the Act of 1850.⁶⁵ In 1872, however, the legislature, influenced by *George*,⁶⁶ made the rents and profits of either spouse the separate property of that spouse.⁶⁷ Inasmuch as the statutes of most of the other community property

⁵² EARLY LAWS OF TEXAS 334 (1888); see BURNETT, COMMUNITY PROPERTY LAW 40 (1926); Huie, *The Community Property Law of Texas*, 13 TEX. REV. CIV. STAT. ANN. 1 (1960).

⁵³ BURNETT, COMMUNITY PROPERTY LAW 40 (1926); Huie, *supra* note 47, at 1055.

⁵⁴ See note 37 *supra* and accompanying text.

⁵⁵ *Selover v. American Russian Commercial Co.*, 7 Cal. 266, 270 (1857); BALLINGER § 22; McMurray, *The Beginnings of the Community Property System in California and the Adoption of the Common Law*, 3 CALIF. L. REV. 359, 373 (1915). But see McMurray, *Seventy-Five Years of California Jurisprudence*, 13 CALIF. L. REV. 445, 453 (1925).

⁵⁶ Cal. Stats. 1850, ch. 103, § 9.

⁵⁷ Kirkwood, *Historical Background and Objectives of the Law of Community Property in the Pacific Coast States*, 11 WASH. L. REV. 1, 4 (1936).

⁵⁸ MCKAY, COMMUNITY PROPERTY § 287 (2d ed. 1925).

⁵⁹ Tex. Gen. Laws 1917, ch. 194, at 460.

⁶⁰ 114 Tex. 535, 273 S.W. 799 (1925).

⁶¹ *Id.* at 539-40, 273 S.W. at 801; see GOODRICH, CONFLICT OF LAWS § 122 n.8 (3d ed. 1949). In Washington such legislation was upheld. See cases cited in Evans, *Primary Sources of Acquisition of Community Property*, 10 CALIF. L. REV. 271, 277 (1922).

⁶² It has been suggested that the framers of the California constitution similarly intended to place the Spanish system beyond the reach of the legislature. BURNETT, COMMUNITY PROPERTY LAW 41 (1926); 1 DEFUNIAK § 51. Mr. Burnett takes the position that the constitution recognized rather than adopted the system as existing in California, and the direction to the legislature in the last part of the section was intended to mean that the legislature should define the rights of the wife in the community property in accordance with Mexican Law. There was no authority, however, to change the existing community property system in any way. BURNETT, *op. cit. supra* at 40-43. But cf. McMurray, *Seventy-Five Years of California Jurisprudence*, 13 CALIF. L. REV. 445 (1925).

⁶³ Cal. Stats. 1880, at *liv* (art. XX, § 8).

⁶⁴ 18 Cal. 654 (1861).

⁶⁵ See BALLINGER § 22; Evans, *Primary Sources of Acquisition of Community Property*, 10 CALIF. L. REV. 271, 277 (1922); McMurray, *Community Property*, 5 CAL. JUR. 268 (1922).

⁶⁶ 1 THE CALIFORNIA FAMILY LAWYER 114 (Cont. Ed. Bar 1962); Huie, *supra* note 47, at 1058 n.25; see CONMY 12; MCKAY, COMMUNITY PROPERTY § 287 (2d ed. 1925).

⁶⁷ CAL. CIV. CODE §§ 162, 163.

states⁶⁸ are modeled on the California code,⁶⁹ the decision in *George* was thus directly responsible for introducing this novel treatment of the rents and profits of separate property to the American law of community property.⁷⁰

B. Initial Problem of Whether To Apportion

If having been decided that rents and profits of separate property are not community property, there arose the problem of determining the character of income from a separate property business where one of the spouses actively participated in the business during the marriage period. This problem was not considered in *George v. Ransom*, since in that case the income produced did not involve the efforts of either spouse.

Just as the court's desire in *George* to protect the wife's property was responsible for the creation of the problem,⁷¹ the same motivation influenced the early attempts to solve it.⁷² The first cases arising after *George* concerned the attempts of an assignee⁷³ or creditor of the husband⁷⁴ to reach the profits of the wife's separate property.⁷⁵ The courts, influenced by the desire to protect the rights of women,⁷⁶ took the view that "one object of the [constitutional] provision⁷⁷ was to protect the wife against the improvidence of the husband."⁷⁸ Accordingly, all the income was held to be the separate property of the wife,⁷⁹ thereby protecting what were felt to be her property rights.⁸⁰ In order to reach this result, the courts had to disregard the effort and labor of the husband as factors in the production

⁶⁸ ARIZ. REV. STAT. ANN. §§ 25-211, -213 to -214 (1956); NEV. REV. STAT. §§ 123.130, .220 (1957); N.M. STAT. ANN. §§ 57-3-4, -6, -4-1 (1953); WASH. REV. CODE §§ 26.16.010, .020, .030 (1961).

⁶⁹ 2 AMERICAN LAW OF PROPERTY § 7.3 (Casner ed. 1952); BALLINOER § 24; HUIE, TEXAS CASES ON MARITAL RIGHTS 212 (1955); MCKAY, COMMUNITY PROPERTY § 6 (2d ed. 1925); VERNIER, AMERICAN FAMILY LAWS 207-08 (1935); Kirkwood, *Historical Background and Objectives of the Law of Community Property in the Pacific Coast States*, 11 WASH. L. REV. 1, 8 (1936); LeSourd, *Community Property Status of Income from Business Involving Personal Services and Separate Capital*, 22 WASH. L. REV. & ST. B.J. 19, 21 (1947); Lyons, *Development of Community Property Law in Arizona*, in CHARMATZ & DAGGETT, COMPARATIVE STUDIES IN COMMUNITY PROPERTY 3, 5 (1955).

⁷⁰ MCKAY, COMMUNITY PROPERTY § 287 (2d ed. 1925); see *id.* § v (1st ed. 1910).

⁷¹ See note 44 *supra* and accompanying text.

⁷² LeSourd, *supra* note 69, at 22.

⁷³ See, e.g., *Diefendorff v. Hopkins*, 95 Cal. 343, 28 Pac. 265 (1891).

⁷⁴ See, e.g., *Lewis v. Johns*, 24 Cal. 98 (1864).

⁷⁵ *Walsh v. Walsh*, 84 Cal. 101, 23 Pac. 1099 (1890); *Diefendorff v. Hopkins*, 95 Cal. 343, 28 Pac. 265 (1892); *Peck v. Brummagim*, 31 Cal. 440 (1866); cf. *Davis v. Green*, 122 Cal. 364, 55 Pac. 9 (1898).

⁷⁶ See *Hitchcock, Modern Legislation Touching Marital Property Rights*, 6 So. L. REV. N.S. 633, 634 (1880); LeSourd, *supra* note 69, at 22.

⁷⁷ See text accompanying note 35 *supra*.

⁷⁸ *Lewis v. Johns*, 24 Cal. 98, 101-02 (1864), quoting from *George v. Ransom*, 15 Cal. 322 (1860).

⁷⁹ To the same effect were the decisions of the Washington Supreme Court holding that the community derived no interest in the income from a separate property business by reason of the effort and skill of the spouses. See *Hester v. Stine*, 46 Wash. 469, 90 Pac. 594 (1907); *Brookman v. State Ins. Co.*, 18 Wash. 308, 51 Pac. 395 (1897); *Leake v. Hayes*, 13 Wash. 213, 43 Pac. 48 (1895); LeSourd, *supra* note 69, at 22 n.19.

⁸⁰ In *Spear v. Ward*, 20 Cal. 659 (1862), the creditors of the husband were held not entitled to the products of the wife's separate property farm, even though the wife had executed a crop mortgage in their favor. The court held that the wife was merely a surety for the husband's debt.

of the profits.⁸¹ When cases involving the rents and profits of the husband's property later arose, the courts, to remain consistent, held the entire proceeds to be his separate property.⁸²

The first consideration given to the factor of a spouse's skill or effort in operating a separately owned business was in the Nevada decision in *Lake v. Bender*.⁸³ This case, rather than considering an apportionment, looked at the various factors only to determine whether or not the sum in dispute came within the definition of rents and profits. The court held that where the separate property itself was a more important factor than the skill of the husband in the production of the income from a hotel and ranch,⁸⁴ the entire income from the business constituted rents and profits of the separate property. The community was not permitted a share in the profits. *Lake* differed from previous cases, however, in that it recognized that the skill of the spouses had been instrumental in the production of the income.⁸⁵ Furthermore, the court stated in a dictum that "if profits come mainly from the efforts or skill of one or both, they belong to the community."⁸⁶

In an article criticizing the *Lake* case, Professor Pomeroy expressed doubt that the income from a commercial enterprise was intended by the legislature to constitute rents and profits.⁸⁷ He also pointed out that the decision in *Lake* furnished no real test to determine which interest in the property should predominate. This inadequacy was recognized in *Lake* itself, the court stating that "it may be difficult in a given case to determine the controlling question, owing to the equality of the two elements mentioned, but we know of no other method of determining to whom the profits belong."⁸⁸ Apportionment simply was not considered.

In finding the entire amount to be separate property, the court in *Lake* found support in cases from common law jurisdictions holding that the profits from a business or farm that were the separate property of the wife could not be reached by the creditors of the husband, even though he had participated in operating the business.⁸⁹ Since the common law courts would not allow the creditors to reach the profits on the basis of the husband's participation, it was analogized that no part of the profits could be allocated to the community on the basis of the husband's skill and effort.

⁸¹ The language used in *Lewis v. Johns*, 24 Cal. 98, 102 (1864), is typical of the court's attitude: "the husband cannot, by any independent act of his, acquire an interest in the separate estate of the wife."

⁸² *Estate of Granniss*, 142 Cal. 1, 75 Pac. 324 (1904); *Estate of Cudworth*, 133 Cal. 462, 65 Pac. 1041 (1901); *Estate of Higgins*, 65 Cal. 407, 4 Pac. 389 (1884). *But cf.* *Estate of Bauer*, 79 Cal. 304, 21 Pac. 759 (1889).

It is ironical that this desire to protect the wife's property rights should result in a situation where "her only chance to acquire by marriage any interest in property is to marry a man who has nothing, with the hope that he may afterwards earn something in which she will have a community right." *Estate of Cudworth*, *supra* at 469, 65 Pac. at 1044 (concurring opinion). See Pomeroy, *Husband's Separate Estate*, 4 WEST COAST REPR. 193, 195 (1884).

⁸³ 18 Nev. 361 (1884).

⁸⁴ In *Lake*, the wife had also worked in the hotel during the entire period of marriage.

⁸⁵ In earlier California cases it was contended that the effort and skill of the spouses should have the effect of making the profits community property. See, e.g., *Lewis v. Johns*, 24 Cal. 98, 100 (1864). But the doctrine of *George v. Ransom* was felt to preclude such a holding. *Id.* at 102.

⁸⁶ *Lake v. Bender*, 18 Nev. 361, 392 (1884). See LeSourd, *supra* note 69, at 23.

⁸⁷ Pomeroy, *supra* note 82, at 196, suggesting that the husband's estate be credited with the average rate of interest or the fair rental value in these circumstances.

⁸⁸ 18 Nev. at 392.

⁸⁹ *Id.* at 387.

The *Lake* case was important in three ways in shaping the early law concerning the disposition of the income from separate property businesses.⁹⁰ First, the case became the accepted authority for the black letter rule⁹¹ that the profits would be separate property if the predominant factor in their production was the capital, but would be community if the effort of one of the spouses had been more instrumental.⁹² Second, the *Lake* case pointed up the injustice of allocating the entire profits to either the community or the separate estate.⁹³ Perhaps the greatest influence of *Lake*, however, was in the example the court set by analogizing this community property problem to the common law problem involving creditors of the husband seeking to seize the revenue of the wife's business or farm.⁹⁴ It was the use of similar unsound analogies that led to the creation of the apparent inconsistency between *Pereira v. Pereira*⁹⁵ and *Estate of Pepper*.⁹⁶

Another way in which the courts approached the problem before the idea of apportionment was first crystalized was to consider the income as a commingled fund. The decision of the Supreme Court of Washington in *In re Buchanan's Estate*⁹⁷ typifies this approach.⁹⁸ The court held the profits of the separate investment to be so commingled with community earnings as to make the income from the business during ten years of marriage entirely community property.⁹⁹

Although the results differed, the *Lake* and *Buchanan* cases were both decided on the principle that the character of the property is determined by deciding which

⁹⁰ Even today remnants of the *Lake* rule are found in California apportionment cases, in that the relative importance of the capital or the personal services as factors in the production of income may bear on what apportionment is made or whether the entire amount of the profits are allocated to the separate estate. See *Estate of Neilson*, 57 Cal. 780, 787, 371 P.2d 733, 736, 22 Cal. Rptr. 1, 5 (1962).

⁹¹ McKay's statement in 6 AM. & ENG. ENCY. LAW 324 (1898), was particularly influential, as it was frequently cited by counsel as the "rule" of the *Lake* case. See Respondents Brief, pp. 106-07, *Pereira v. Pereira*, 156 Cal. 1, 103 Pac. 488 (1909); Appellant's Points and Authorities, pp. 1, 22-23, *Estate of Pepper*, 158 Cal. 619, 112 Pac. 62 (1910). Despite the fact that the statutes of all the community property states were different, the treatises were all written in generalizations. See, e.g., 21 Cyc. 1648 n.56 (1906).

⁹² McKay also stated the *Lake* case as a rule in his treatise, MCKAY, COMMUNITY PROPERTY § 76 (1st ed. 1910), as did Judge Ballinger, BALLINGER § 24, and Professor Pomeroy, *Digest of Cases*, 4 WEST COAST RPT. 765, 858 (1884).

⁹³ McKay realized that the rule of the *Lake* case, on its face, confessed an injustice to either the separate estate or the community. MCKAY, COMMUNITY PROPERTY § 313 (2d ed. 1925).

⁹⁴ In *Lake* the court said, "most of the cases to which we shall refer upon this question involve [*sic*] the right of a wife to claim profits arising from the use of her separate estate, as against the creditors of the husband, when they have been increased by his labor and skill." 18 Nev. at 387.

⁹⁵ 156 Cal. 1, 103 Pac. 488 (1909).

⁹⁶ 158 Cal. 619, 112 Pac. 62 (1910). See text following notes 111 and 183 *infra*.

⁹⁷ 89 Wash. 172, 154 Pac. 129 (1916).

⁹⁸ Apportionment had been made earlier in *Pereira*, see text accompanying notes 9-10 *supra*, but the Washington courts refused to apply this rule, LeSourd, *supra* note 69, at 25-26. In California, the commingling approach had been used both before *Pereira*, *Estate of Bauer*, 79 Cal. 304, 21 Pac. 759 (1889), and after, *Estate of Fellows*, 106 Cal. App. 681, 289 Pac. 887 (1930).

⁹⁹ 89 Wash. 172, 179-80, 154 Pac. 129, 132 (1916). In finding the income to be community property, the court relied on *Lake v. Bender* as well as on the line of common law cases, rejected in *Lake*, that had allowed the creditors to reach the income from the wife's separate property on the basis of the personal service he had devoted to that property. See text accompanying note 89 *supra*. Compare the use of *Glidden v. Taylor*, 16 Ohio St. 510 (1866), in *Lake v. Bender*, 18 Nev. 361, 393 (1884), with its use in *In re Buchanan's Estate*, 89 Wash. 172, 181, 154 Pac. 129, 132 (1916).

of two factors, the capital or the skill of one of the spouses, was more important in the production of the income.¹⁰⁰ The Nevada court in *Lake* found that the capital was the primary factor in the production of the profits, whereas the Washington court in *Buchanan* found the skill of the spouses a more important factor. The importance of the *Buchanan* case lies in the additional step to the *Lake* approach, in that once it was found that the profits were primarily community, the concept of commingling was further used to justify holding the entire sum allocable to the community.¹⁰¹

II

BEFORE *Neilson*

A. Pereira v. Pereira

The first decision apportioning profits in a community property state was *Pereira v. Pereira*.¹⁰² The trial court found that the proceeds from the husband's separately owned cigar store-saloon were all community property. Mr. Pereira appealed, claiming that the entire proceeds should be his separate property because they were the rents and profits of his separate property.¹⁰³ This contention was supported by the early California cases¹⁰⁴ that had not considered the skill of either spouse as a factor in the production of income.¹⁰⁵ Mrs. Pereira, relying mainly on the dictum in *Lake v. Bender*,¹⁰⁶ argued that the entire proceeds should be community property,¹⁰⁷ since the evidence had shown the husband's skill to be the main factor in producing the income.¹⁰⁸ To further support this contention

¹⁰⁰ Although the Washington court treated the fund as commingled, the implication was that if the capital invested was more important than the services of the spouse the entire fund would be separate. 89 Wash. at 179-81, 154 Pac. at 132. The cases relied on in *Lake* did not allow creditors of the husband to seize the income of the wife's separate property, but the cases relied on in *Buchanan* allowed the proceeds to be reached in certain circumstances. See notes 118-21 *infra*.

¹⁰¹ The problem is often still treated in terms of a commingled fund. *Ormachea v. Ormachea*, 67 Nev. 273, 217 P.2d 355 (1950); *BURBY & PATTY, SELECTED PROBLEMS IN COMMUNITY PROPERTY AND DOMESTIC RELATIONS* 12 (1958); *KEDDIE, COMMUNITY PROPERTY LAW IN ARIZONA* 15 (1958); *McKAY, COMMUNITY PROPERTY* § 317 (2d ed. 1925); *Cross, The Community Property Law in Washington*, in *CHARMATZ & DAGGETT, COMPARATIVE STUDIES IN COMMUNITY PROPERTY* 150, 162-66 (1955); see *Porter v. Porter*, 67 Ariz. 273, 195 P.2d 132 (1948); *Jacobs v. Hoitt*, 119 Wash. 283, 205 Pac. 414 (1922). See also *In the Matter of Estate of Torrey*, 54 Ariz. 369, 95 P.2d 990 (1939).

The problem is also analogous to situations where separate and community funds are used to buy land or when community property is used to improve separate property, and vice versa. 4 *POWELL, REAL PROPERTY* 685 (1954); *Comment*, 50 CALIF. L. REV. 844 (1962).

¹⁰² 156 Cal. 1, 103 Pac. 488 (1909).

¹⁰³ Opening Brief of Appellant, pp. 30-31.

¹⁰⁴ See cases cited note 82 *supra*.

¹⁰⁵ Opening Brief of Appellant, pp. 26-31.

¹⁰⁶ See text accompanying note 86 *supra*.

¹⁰⁷ Brief for Respondent, pp. 102-07.

¹⁰⁸ The record includes the following:

Q. Of course that is an enormous profit Mr. Pereira on that amount of money.

I suppose it is due to your individual efforts?

A. I judge it is

The Court. Mr. Pereira, it is due to your own efforts you made this money?

A. Yes, sir, hard labor day and night.

Transcript on Appeal, pp. 102-04.

she cited common law decisions involving attempts of the husband's creditors to reach the profits of a business operated by the husband with capital belonging to his wife.¹⁰⁹

Pereira was argued by both sides on the assumption that the profits were either entirely community property or entirely separate.¹¹⁰ Nevertheless, it was held that unless the contrary could be shown, it must be assumed that the separate property investment was responsible for part of the profits, and that this share would at least amount to the interest rate on a long-term investment, with the remainder being held community property.¹¹¹

1. The Rationale Behind *Pereira*

To support the holding that an apportionment should be made, measured by the interest rate on a well secured investment, *Pereira*, like *Lake*,¹¹² drew analogies from common law creditor cases.¹¹³ Each of the cases cited had been decided during a period when the recognition of a married woman's right to hold property and transact business in her own name¹¹⁴ was new to the common law,¹¹⁵ and when there was much confusion in handling the problems created by these new rights.¹¹⁶ As a result of such recognition, a debt-ridden husband was afforded an opportunity to run his wife's business while denying his creditors recourse to the business income. The courts thus were confronted with the problem of protecting the wife in accord with the statutes, yet preventing the husband from defrauding his creditors.¹¹⁷

In most instances the income from the wife's business was held to belong to

¹⁰⁹ Brief for Respondent, pp. 107-13.

¹¹⁰ Oral Argument of J. F. Bowie on Behalf of Respondent, pp. 9-14; Oral Argument of Myer Jacob on Behalf of Appellant, pp. 19-21.

It appears as though counsel for Mrs. *Pereira* thought that opposing counsel was arguing for at least some of the earnings to be separate property. Brief for Respondent, p. 117. It would seem, however, that counsel for Mr. *Pereira* was only claiming that part of the piece of property in question was bought with separate funds other than those earned in the business, and was not seeking a division of the earnings. Opening Brief of Appellant, pp. 31-32.

¹¹¹ The court stated that "in the absence of circumstances showing a different result, it is to be presumed that some of the profits were justly due to the capital invested. There is nothing to show that all of it was due to defendant's efforts alone. The probable contribution of the capital to the income should have been determined from all the circumstances of the case, and, as the business was profitable, it would amount at least to the usual interest on a long investment well secured." 156 Cal. at 7, 103 Pac. at 491.

¹¹² See text accompanying notes 89 and 94 *supra*.

¹¹³ *Bogges v. Richards*, 39 W. Va. 567, 20 S.E. 599 (1894); *Trapnell v. Conklyn*, 37 W. Va. 242, 16 S.E. 570 (1892); *Penn v. Whitehead*, 17 Gratt. 503, 94 Am. Dec. 478 (1867); *Glidden v. Taylor*, 16 Ohio St. 509 (1866). Neither *Penn* nor *Trapnell* appear in the briefs of either party discussing the community property issue. See Opening Brief of Appellant, pp. 25-32, Brief for Respondent, pp. 103-20, Reply Brief for Appellant, pp. 60-79.

¹¹⁴ See STEWART, HUSBAND AND WIFE § 184 (1885). Although a married woman's ability to administer her property was especially restricted by the fact that she could not, at common law, contract in her own name, this restriction was also lifted by statute. See ANSON, CONTRACTS 234-36 (1939); WHITNEY, CONTRACTS § 11, at 10 (1953).

¹¹⁵ SCHOULER, DOMESTIC RELATIONS § 164 (5th ed. 1895); Hitchcock, *Modern Legislation Touching Marital Property Rights*, 6 SO. L. REV. N.S. 633 (1880).

¹¹⁶ PARSONS, LAW OF PARTNERSHIP 24 (1867); SCHOULER, DOMESTIC RELATIONS 9-10 (2d ed. 1874).

¹¹⁷ See SCHOULER, DOMESTIC RELATIONS § 168 (5th ed. 1895); *id.* at 19-20 (2d ed. 1874).

her, notwithstanding the husband's skill and effort involved.¹¹⁸ Nevertheless, where the husband had acted with an obvious intent to defraud his creditors, the courts would look behind the form of the transaction and protect the creditors where the equities warranted it.¹¹⁹ In such instances the courts generally held that the business really belonged to the husband, and that his creditors could reach its entire income.¹²⁰ Where the fraudulent nature of the transaction was less evident, the courts would find that part of the proceeds constituted rents of the wife. But the courts then reasoned that since she had allowed the rents to become commingled with the earnings of the husband, the creditors should not be prejudiced and could satisfy their debts from the entire income.¹²¹ The rationale was that the wife could have prevented the commingling, whereas the creditors were powerless to do anything and should not be made to suffer a loss.¹²²

In cases where the wife did not partake in the fraud, some of the equity courts

¹¹⁸ In *Bogges v. Richards*, 39 W. Va. 567, 574, 20 S.E. 599, 602 (1894), the court said:

It has been settled by numerous and repeated decisions that it matters not how much of his labor and skill a man may devote to his wife's property; and, although it may be changed from a rude to a manufactured state, it remains her property still, and can not be levied on by execution or attached for his debts.

Citing *Atwood v. Dolan*, 34 W. Va. 563, 12 S.E. 688 (1890); *Miller v. Peck*, 18 W. Va. 75 (1881). See *Scott v. Hudson*, 86 Ind. 286 (1882); *Hearts v. Klinkhammar*, 39 Minn. 488 (1888); *Coddington v. Bowen*, 53 N.Y. (Hun.) 631 (1889); *Atwood v. Dolan*, 34 W. Va. 563, 12 S.E. 688 (1890); 1 FREEMAN, EXECUTIONS 566 (3d ed. 1900); STEWART, HUSBAND AND WIFE § 477 (1885). See also 3 POMEROY, EQUITY JURISPRUDENCE 24 (1881).

¹¹⁹ See, e.g., *Wortman v. Price*, 47 Ill. 22 (1868); 1 SCHOULER, MARRIAGE, DIVORCE AND SEPARATION § 313 (6th ed. 1921); STEWART, HUSBAND AND WIFE § 469 (1885); WELLS, SEPARATE PROPERTY RIGHTS OF WOMEN 195-96 (1878). The theory of the courts in those instances where the creditors were allowed to seize the profits was either that the husband had attempted to make a fraudulent conveyance of his services to the wife, BUMP, FRAUDULENT CONVEYANCES 263 (4th ed. 1896), that the wife had merely put her money in the husband's business, *Annot.*, 77 Am. St. Rep. 92 (1899), or that the husband had carried on the business in his own name without revealing he was the agent of the wife, SCHOULER, DOMESTIC RELATIONS § 168 (5th ed. 1895).

¹²⁰ BUMP, FRAUDULENT CONVEYANCES 262-63 (4th ed. 1896); SCHOULER, DOMESTIC RELATIONS § 168 (5th ed. 1895); SCHOULER, MARRIAGE, DIVORCE AND SEPARATION § 313 (6th ed. 1921); *Annot.*, 77 Am. St. Rep. 92, 101 (1899); *cf.* *Glidden v. Taylor*, 16 Ohio St. 509 (1866). There was more of a reluctance to find that the product of a wife's farm could be reached by the husband's creditors because of the notion that crops arising naturally from the soil remain separate property. See *Lake v. Bender*, 18 Nev. 361, 395-400 (1884) (dissenting opinion); BUMP, *op. cit. supra* at §§ 224-25; 1 FREEMAN, EXECUTIONS 566 (1900); *Annot.*, 77 Am. St. Rep. 92, 97-100, 100-09 (1899). Some cases distinguished between the situations where the husband rents the farm and where he is the wife's agent. In the latter case the rents and profits cannot be seized. WELLS, SEPARATE PROPERTY RIGHTS OF MARRIED WOMAN 172 (1878).

¹²¹ BUMP, FRAUDULENT CONVEYANCES 262 (4th ed. 1896); 1 SCHOULER, MARRIAGE, DIVORCE AND SEPARATION § 326 (6th ed. 1921); STEWART, HUSBAND AND WIFE §§ 129, 311 (1885).

¹²² *Quidort v. Pergeax*, 18 N.J. Eq. 472 (1867); see *Glidden v. Taylor*, 16 Ohio St. 509, 521 (1866). The party responsible for commingling a fund is treated similarly in other branches of the law. See *BOGERT, TRUSTS* § 100 (3d ed. 1952); *BROWN, PERSONAL PROPERTY* §§ 30-36 (1936). In community property states a fund consisting of an uncertain amount of community property and separate property is treated as belonging entirely to the community. See *Falk v. Falk*, 48 Cal. App. 2d 762, 120 P.2d 720 (1941); note 314 *infra*. Part of the rationale for this treatment is that the husband has control of community property and where he allows it to become so mixed with his own funds that the amount belonging to the community cannot be determined he must suffer the loss. *Pope v. Pope*, 102 Cal. App. 2d 353, 227 P.2d 867 (1951); 1 DEFUNIAK § 61.

tried to help her¹²³ even though they found the transaction to be fraudulent.¹²⁴ *Bogges v. Richards' Adm'r*¹²⁵ and *Glidden v. Taylor*,¹²⁶ two of the cases relied upon in *Pereira*, were of this nature. In *Bogges*, the money that constituted the wife's investment had originally been given to her by the husband before marriage. After the husband became insolvent he used the money to establish a profitable business. In allowing the creditors of the husband to reach these assets the court was strongly motivated by the fraudulent nature of the entire transaction,¹²⁷ but since the wife had not taken an active part in the fraud,¹²⁸ she was allowed her original investment plus the legal interest rate.¹²⁹ The facts in *Glidden* were very similar, and the court, in effect, found the transaction to be a loan of money from the wife to the husband.¹³⁰ By analogy it was held that the wife was a creditor of the husband, and as such, entitled to her original investment plus interest.¹³¹ It was from the suggestions in *Glidden* and *Bogges* that the California court probably obtained the method of apportionment used in *Pereira*.¹³² Since the common law courts allowed the creditors to reach the profits of the business as a result of the husband's skill and talent, the California court reasoned that the community was entitled to the profits for the same reason.¹³³ Although this was the same type of analogy used in *Buchanan*,¹³⁴ the California court went even further and

¹²³ SCHOULER, DOMESTIC RELATIONS § 165 (5th ed. 1895); WELLS, SEPARATE PROPERTY RIGHTS OF MARRIED WOMAN 195-96 (1876); see 2 STORY, EQUITY JURISPRUDENCE §§ 1372a-b (9th ed. 1866).

¹²⁴ This was the result reached in *Glidden v. Taylor*, 16 Ohio St. 509 (1886). See text accompanying note 130 *infra*.

¹²⁵ 39 W. Va. 567, 20 S.E. 599 (1894).

¹²⁶ 16 Ohio St. 510 (1866).

¹²⁷ One writer warned against relying on *Bogges* as authority for the proposition that the application of the husband's services subjected the profits of the wife's separate property to the creditors of the husband because of the extremely fraudulent nature of the transaction. 1 FREEMAN, EXECUTIONS 568-69 (1900). In *Deere v. Bonne*, 108 Iowa 281, 79 N.W. 59 (1899), the court distinguished *Glidden* on the grounds that the husband had controlled the wife's property absolutely.

¹²⁸ Although the wife was not guilty of any actual fraud, the court found that "her hand be it ever so chaste is polluted by receiving as a gift from her husband the funds which he is endeavoring to fraudulently conceal . . . from the searching eyes of his creditors." *Bogges v. Richards*, 39 W. Va. 567, 576, 20 S.E. 599, 602 (1894).

¹²⁹ "The only way that the law furnishes for the ascertainment of how much of this handsome profit is due to the skill and labor of the husband is to deduct therefrom the legal interest on the amount of capital invested." *Ibid*.

¹³⁰ The court recognized that a wife could not be a creditor of the husband at common law, but concluded that, since this was an action in equity to divest her of title, she was entitled to protection. *Glidden v. Taylor*, 16 Ohio St. 509, 522 (1866). See also 2 STOREY, EQUITY JURISPRUDENCE § 1373 (9th ed. 1866).

¹³¹ In *Trapnell v. Conklyn*, 37 W. Va. 242, 16 S.E. 570 (1892), and *Penn v. Whitehead*, 58 Va. (17 Gratt.) 503, 94 Am. Dec. 478 (1867), it was mentioned that equity would make an apportionment in a proper case, but none was made.

¹³² The language used by the court in *Pereira* was the same language that was used in *Glidden*. It has also been suggested that the *Pereira* apportionment rule was abstracted from the *Bogges* case. Evans, *Primary Sources of Acquisition of Community Property*, 10 CALIF. L. REV. 271, 281 n.78 (1922).

¹³³ In an earlier case the California Supreme Court, recognizing the skill and talent of the husband as a factor in the production of income, found the entire amount to be community property under the rationale that the profits constituted a commingled fund. *Estate of Bauer*, 79 Cal. 304, 21 Pac. 759 (1889).

¹³⁴ See notes 99 and 100 *supra* and accompanying text.

allowed the husband's separate estate the interest on his investment just as the common law court had allowed this to the wife.¹³⁵

Apart from the lack of any rational basis for interpreting a community property problem by common law principles,¹³⁶ sound reasons appear why the *Boggess* and *Glidden* cases should not have been relied on by the *Pereira* court. The married women's property acts were a new innovation in the common law,¹³⁷ and the statutes of various states differed.¹³⁸ Cases from one common law state were not sound precedent for another such jurisdiction,¹³⁹ much less for a community property state.¹⁴⁰ Furthermore, the legal relationships involved were not analogous. In community property states a wife cannot force her spouse to labor,¹⁴¹ as neither can creditors in common law states.¹⁴² If, however, the husband chooses to work, the implications are different. The husband's skill is an asset of the community,¹⁴³ and when he exercises it the resulting product automatically must be considered community property.¹⁴⁴ In comparison, the common law creditors have no such

¹³⁵ Since the common law courts held that the wife's capital could only be credited with some type of interest rate, and that the creditors could reach the remaining income on the theory that the husband's efforts had produced it, the California court held by analogy that the husband's capital was only entitled to interest, and that the community was entitled to the rest of the profits because they must be similarly treated as the product of his skill.

¹³⁶ 1 DEFUNIACK § 51, at 110; see DAGGETT, *THE COMMUNITY PROPERTY SYSTEM OF LOUISIANA* 3 (1931).

¹³⁷ See note 115 *supra* and accompanying text.

¹³⁸ STEWART, *HUSBAND AND WIFE* § 464 (1885); Hitchcock, *Modern Legislation Touching Marital Property Rights*, 6 SO. L. REV. N.S. 633, 634 (1880). In some states the only provision was one entitling the wife to hold property; since these statutes were not construed as giving the authority to trade in her own name, the rents and profits belonged to the husband in the same manner as they had at common law. STEWART, *op. cit. supra* §§ 464, 470, 473; Annot., 77 AM. ST. REP. 92, 100 (1899). In some states the wife was allowed to trade in her own name with permission of her husband, but, if the arrangement appeared fraudulent, the husband's creditors could reach the profits. STEWART, *op. cit. supra* § 469.

¹³⁹ STEWART, *HUSBAND AND WIFE* § 464 (1885); Annot., 77 AM. ST. REP. 92 (1899). As was the case with community property states, one of the reasons for the confusion in common law jurisdictions was the reliance on treatises and encyclopedias which treated the laws of all jurisdictions without differentiating them. See note 91 *supra*.

¹⁴⁰ Inasmuch as the holdings of the four common law cases cited by *Pereira* were that the creditors of the husband could reach the profits of a business owned by the wife, their use by California courts seems particularly strange; it was the desire to protect the wife against just such creditors that was responsible for the original departure from the Spanish-Mexican system in *George Evans, Primary Sources of Acquisition of Community Property*, 10 CALIF. L. REV. 271, 281-82 (1922); see notes 42 and 44 *supra*. California has expressly rejected the holdings of these common law cases, both before *Pereira*, see *Lewis v. Johns*, 24 Cal. 98 (1864), and after, see *Gray v. Perlis*, 76 Cal. App. 511, 245 Pac. 221 (1926).

¹⁴¹ *Spreckles v. Spreckles*, 172 Cal. 775, 158 Pac. 537 (1916). See also CAL. CIV. CODE § 156 (the husband chooses the mode of living).

¹⁴² In *Penn v. Whitehead*, 58 Va. (17 Gratt.) 503, 528, 94 Am. Dec. 478, 494 (1867), the court stated: "[T]he law cannot, or does not, compel a man in advance to labor for his creditors." See BUMP, *FRAUDULENT CONVEYANCES* § 225 (4th ed. 1896); 1 FREEMAN, *EXECUTIONS* 567 (1900).

¹⁴³ *Strohm v. Strohm*, 182 Cal. App. 2d 53, 62, 5 Cal. Rptr. 884, 889 (1950); Cross, *The Community Property Law in Washington*, in CHARMATZ & DAGGETT, *COMPARATIVE STUDIES IN COMMUNITY PROPERTY LAW* 150, 164 (1955); MCKAY, *COMMUNITY PROPERTY* § 76, at 161 (1910); WOOD, *THE COMMUNITY PROPERTY LAW OF NEW MEXICO* § 39 (1954); Comment, 36 TEXAS L. REV. 187, 192 (1957).

¹⁴⁴ 3 VERNIER, *AMERICAN FAMILY LAWS* 214 (1931). But see *Gray v. Perlis*, 76 Cal. App. 511, 245 Pac. 221 (1926), where the value of the husband's labors in the wife's separate property business were held not reachable by creditors of the community.

lien on the husband's services,¹⁴⁵ and the husband's earnings are not necessarily subject to their claims.¹⁴⁶ Thus, the reasons for granting or denying recovery to a creditor in a common law case were not founded upon the same rationale that entitles the community to an interest in the profits under California law.¹⁴⁷ Still further, the word "apportionment" was not used by the common law courts in the same sense of an attempt to determine the respective shares of the community and the separate estate. As the *Glidden* case shows, no attempt was made to determine the true relationship between the wife's capital and the husband's services in the production of the income.¹⁴⁸ The idea of "apportioning" served only to protect the wife from the husband's creditors to whatever extent possible.¹⁴⁹

2. The "Rule" of *Pereira*

Despite its unsound origin¹⁵⁰ and the vagueness of its terms,¹⁵¹ the use in *Pereira* of "the usual interest on a long investment well secured"¹⁵² has been taken by many writers to be a rule of law,¹⁵³ and is frequently applied by the courts as a mathematical formula to apportion profits from a separately owned business.¹⁵⁴ The language used in *McDuff v. McDuff*¹⁵⁵ illustrates how the courts have come to regard the *Pereira* holding:

It has been held that the proper method of determining the value of a husband's interest in a business in which he was engaged at the time of his marriage is to allow the usual interest to the husband on the amount invested on the basis of a long investment, well secured.¹⁵⁶

¹⁴⁵ *Abbey v. Deyo*, 44 N.Y. 343 (1871); *Heckinger v. Swank*, 78 Ore. 526, 153 Pac. 784 (1915); 1 FREEMAN, EXECUTIONS 565-66 (1900); Annot., 77 Am. St. Rep. 92 (1899); see Annot., 28 A.L.R. 1046, 1048 (1924). See also *Gray v. Perlis*, 76 Cal. App. 511, 245 Pac. 221 (1926).

¹⁴⁶ "A debtor may therefore bestow his skill and labor upon his wife's estate so far as may be reasonably necessary, without rendering the products liable to his creditors." BUMP, FRAUDULENT CONVEYANCES § 225, at 264 (4th ed. 1896). In *Trapnell v. Conklyn*, 37 W. Va. 242, 16 S.E. 570 (1892), the court stated that the fact that an insolvent husband voluntarily bestows his labor and skill in the business of farming carried on by his wife upon land which is her separate property, and operated with her separate property, will not, in the absence of fraud, render the products the property of the husband and liable for his debts.

¹⁴⁷ Another difference is that in common law states where the husband's creditors attempt to seize the income from his wife's separate property, they have the burden of proving that any of the proceeds were earned as a result of the husband's skill, see *Commonwealth v. Fletcher*, 69 Ky. 171, 172-73 (1869), whereas in community property states the party claiming that the profit was produced by the capital (the separate property) would have the burden of proof, see text following note 279 *infra*.

¹⁴⁸ In *Glidden*, the court admitted that "the property in controversy can, in no just sense, be said to be either the income, increase, or profits of the money given to Mrs. Taylor," but allowed her to share in the profits as a creditor. 16 Ohio St. at 521.

¹⁴⁹ See SCHOULER, DOMESTIC RELATIONS § 165 (5th ed. 1895).

¹⁵⁰ See text following note 136 *supra*.

¹⁵¹ "The terms of this rule, if we may call it such, are so ample, not to say vague, that it scarcely helps us in a case that varies from these facts." Evans, *supra* note 140, at 282.

¹⁵² See note 111 *supra* and accompanying text.

¹⁵³ 2 AMERICAN LAW OF PROPERTY 146 (Casner ed. 1952); 1 DEFUNIAK 186; Note, 4 CALIF. L. REV. 329-31 (1916); 5 R.C.L. 841-42 (1914).

¹⁵⁴ *Randolph v. Randolph*, 118 Cal. App. 2d 584, 258 P.2d 547 (1953); *Margolis v. Margolis*, 115 Cal. App. 2d 131, 251 P.2d 396 (1952); *Estate of McCarthy*, 127 Cal. App. 80, 15 P.2d 223 (1932); *McDuff v. McDuff*, 48 Cal. App. 175, 191 Pac. 957 (1920); *Lawrence Oliver*, 4 T.C. 684 (1945); see *Estate of Arstein*, 56 Cal. 2d 239, 364 P.2d 33, 14 Cal. Rptr. 809 (1961); *Tassi v. Tassi*, 160 Cal. App. 2d 680, 325 P.2d 872 (1958).

¹⁵⁵ 48 Cal. App. 175, 191 Pac. 957 (1920).

¹⁵⁶ *Id.* at 178, 191 Pac. at 957.

Some lawyers have even argued that *Pereira* limited the husband to a seven per cent return on his investment,¹⁵⁷ but this contention has been rejected.¹⁵⁸

The interpretation of the *Pereira* case as having established a "rule" by which the income of every separate property business can be apportioned seems unfounded. The method in *Pereira* was used only as a means to ascertain the *least* amount to be credited to the husband's separate estate in the *absence* of other circumstances.¹⁵⁹

The only "rule" that the court intended to state in *Pereira* was that some apportionment should be made, not that there should be any universally applicable proportion or method of division.¹⁶⁰ In *Estate of Gold*,¹⁶¹ Justice Shaw, the author of the *Pereira* opinion, stated:

The rules regarding the character of such property were considered in *Pereira v. Pereira* The principle there stated is that the question what part of the subsequent profits arises from the use of this capital and what part from the personal activity, ability, and capacity of the husband is to be determined by the court from the circumstances appearing in the case, that whatever accrues from the latter sources is community property, and that the remaining profits must be classed as separate estate.¹⁶²

The fact that *Gold* held the entire profit to be community property shows even more clearly that the court did not intend that the particular method used in *Pereira* should be adopted as a formula for the solution of all cases. Moreover, *Gold* indicates that *Pereira* was not meant to require an apportionment in every case.¹⁶³

B. *Estate of Pepper*

The decision in *Estate of Pepper*¹⁶⁴ initiated a line of reasoning that has led to what is generally considered a different rule¹⁶⁵ from that of the *Pereira* case. The supreme court in *Pepper* held the entire proceeds from a nursery business to be separate property, stating:

It is, in the nature of things, impossible to apportion the crop so as to determine what share of it has come from the soil and what share from the exertion of man. The product must be treated as a whole, and, if it is the growth of land separately owned it is separate property of the owner of the land.¹⁶⁶

¹⁵⁷ The rate of 7% was not even set by the court in *Pereira*; it was agreed upon by the parties and recognized on rehearing. 156 Cal. at 11, 103 Pac. at 492-93.

¹⁵⁸ The taxpayer's argument in *Todd v. McColgan*, 89 Cal. App. 2d 509, 201 P.2d 414 (1949), that the 7% rate of return was a rule of property law, was rejected. See 4 WIKKIN, SUMMARY OF CALIFORNIA LAW 2726 (7th ed. 1960). A similar contention by this same taxpayer had been previously rejected by a federal court. *Todd v. Commissioner*, 153 F.2d 553, 555 (9th Cir. 1945).

¹⁵⁹ See text accompanying note 111 *supra*.

¹⁶⁰ The holding of the *Pereira* case was only that whatever portion of the income is attributable to the capital invested must be considered separate property and whatever portion is attributable to the skill and effort of the husband must be community property. See *Huber v. Huber*, 27 Cal. 2d 784, 167 P.2d 708 (1946).

¹⁶¹ 170 Cal. 621, 151 Pac. 12 (1915).

¹⁶² *Id.* at 623, 151 Pac. at 13.

¹⁶³ The fact that no apportionment was made in *Gold*, and that the decision was based on *Pereira*, indicates that the *Gold* court did not view *Pereira* as requiring an apportionment in all cases, let alone that it should be made in a certain way.

¹⁶⁴ 158 Cal. 619, 112 Pac. 62 (1910).

¹⁶⁵ See text following note 190 *infra*.

¹⁶⁶ 158 Cal. at 624, 112 Pac. at 64.

It is unfortunate that the court phrased its decision in terms of an inability to apportion. Although it has been this language that has greatly influenced the apportionment cases,¹⁶⁷ it does not appear that the possibility of apportionment was even considered.¹⁶⁸ The case was briefed in much the same manner as *Pereira* and other early cases,¹⁶⁹ with the husband arguing that the income was all his separate property, and the wife arguing that it belonged exclusively to the community.¹⁷⁰ The basic issue was whether the husband's nursery was a business or a farm,¹⁷¹ with Mrs. Pepper conceding that if it were a farm the proceeds would be entirely separate.¹⁷² The district court of appeal had decided that the nursery was a business,¹⁷³ and, relying on Professor Pomeroy's suggestion,¹⁷⁴ held that the income from a business was not within the meaning of "rents and profits" as used by the legislature in the statute.¹⁷⁵ In reversing, the supreme court took the view that the nursery was more like a farm than a business,¹⁷⁶ and the income was held to be within the statutory definition of rents and profits, thus belonging to the husband's separate estate.

1. Rationale of *Pepper*

In retrospect, it may appear strange that the court in *Pepper* did not decide the case in the same manner as *Pereira* and hold that some apportionment should be made. However, there were several factors existing in 1910 that make it under-

¹⁶⁷ See text accompanying notes 192 and 202 *infra*.

¹⁶⁸ But see VERRALL, CASES ON CALIFORNIA COMMUNITY PROPERTY 117-18 (1960). See also 4 WITKIN, SUMMARY OF CALIFORNIA LAW 2725 (7th ed. 1960).

¹⁶⁹ See text following note 103 *supra*.

¹⁷⁰ See Appellant's Points and Authorities, pp. 23-51, Respondent's Points and Authorities, pp. 29-41, Reply Brief for Appellant, pp. 10-23, Applications for Hearing, pp. 27-34, Application for Rehearing, pp. 1-23, Appellant's Answer to Petition for Rehearing, pp. 1-6, Estate of Pepper, 158 Cal. 619, 112 Pac. 62 (1910). The wife's contention, based on *Lake v. Bender*, was that the husband's skill had been the main factor in producing the income. Reply Brief for Appellant, p. 25.

¹⁷¹ "The question here is whether the proceeds of the nursery conducted on the land can be considered as 'issues' or 'profits' of the land." 158 Cal. at 623, 112 Pac. at 64.

¹⁷² Reply Brief for Appellant, pp. 13-15. Before the *Pepper* case was overruled, it was pointed out that it lacked precedent because Mrs. Pepper had conceded that the crops from a farm would all be separate property. 1 ARMSTRONG 480. This was also mentioned in *Estate of Neilson* as one of the reasons that *Pepper* was overruled. 57 A.C. at 739, 22 Cal. Rptr. at 4, 371 P.2d at 748.

¹⁷³ Estate of Pepper, 8 Cal. App. Dec. 720 (1909).

¹⁷⁴ See note 87 *supra*. The court quoted from Professor Pomeroy's article, adopting the rationale that the income of a commercial enterprise was not meant to be within the term "rents and profits" as used in the California Civil Code. 8 Cal. App. Dec. at 726, 727.

¹⁷⁵ "[I]t is, it seems to us, absolutely clear that it is a business as independent of that of farming or horticulture as the business of selling fruits or vegetables or commodities of any character . . ." 8 Cal. App. Dec. at 725.

¹⁷⁶ The court stated that:

If the crop of grain sown and harvested by the owner of the land constitutes "issues and profits" of the land, we are unable to see why the same may not be said of young trees and plants raised on the land until they are ready for transplanting. There may be cases in which the business is virtually one of purchase and sale of plants, the ground being used merely to preserve the plants until sales can be effected. In such cases it might well be said that the enterprise is so predominantly commercial that the profits are not to be treated as issuing from the land. But on the facts before us, the court below was not bound to [regard the case as coming within this class].

158 Cal. at 624, 112 Pac. at 64-65.

standable why the court did not construe *Pereira* to require consideration of an apportionment.¹⁷⁷

The first of these was the notion that since the legislature had provided for rents and profits to remain separate, the owner of the separate property was entitled to devote at least enough time to his property as it would take to make it valuable.¹⁷⁸ This was considered "ordinary use" of the property.¹⁷⁹ In *Estate of Cudworth*,¹⁸⁰ one of the early California cases preceding *Pereira*,¹⁸¹ the money that

¹⁷⁷ Although it is important to understand the *Pepper* decision in light of the prevailing attitude of the period in which it was decided, see text following note 178 *infra*, the decision was incorrect in several respects, apart from the concession of counsel, see note 172 *supra*. In the first place, the *Pepper* decision has no basis in its supporting authorities. The only case relied on for the proposition that the proceeds of a farm are separate property was *Diefendorff v. Hopkins*, 95 Cal. 343, 28 Pac. 265, *aff'd per curiam*, 30 Pac. 549 (1892), a case that is easily distinguished. In *Diefendorff* the plaintiff, claiming to be a purchaser from the husband, sued a sheriff of the City and County of San Francisco for conversion of the furniture of a boarding house. The sheriff had attached the furniture at the request of the wife's creditors. Plaintiff's case was based on the theory that the attachment was improper because the property belonged to the husband. The court held on two alternate theories that the furniture was the separate property of the wife. The furniture was purchased either with money which Mr. Rix gave to his wife, or with the proceeds from the boarding house which was the separate property of the wife. In the first instance the furniture would constitute an outright gift to the wife and thus be her separate property; in the second, the furniture would be the wife's separate property on the grounds that the husband had made an implied gift to Mrs. Rix by allowing her to keep and manage these earnings. At best, the case is authority only for the proposition that a husband who allows his wife to manage her own earnings will be held to have made a gift of them to her.

Even more fault can be found with the *Pepper* decision on the ground that the court seemingly failed to follow the very principles expressed within its opinion. It was recognized that:

There may be cases in which the business is virtually one of purchase and sale of plants, the ground being used merely to preserve the plants until sale can be effected. In such cases, it might well be said that the enterprise is so predominantly commercial that the profits are not to be treated as issuing from the land.

158 Cal. at 624, 112 Pac. at 64-65. The uncontradicted testimony elicited at the trial, however, shows that Mr. Pepper's practice was to import trees from foreign countries and eastern states in the winter, have them grafted, budded, and tended by his employees for a little over a year and place them for sale the following spring. Each year he issued price lists. For quite some time he sold the trees from a store in Petaluma, California. See *Estate of Pepper*, 8 Cal. App. Dec. 720, 725 (1909).

Although the *Pepper* court seemed unwilling to distinguish a nursery and a farm because of the differing degrees of individual skill connected with the management of each, it was willing to distinguish the nursery from a business "virtually one of purchase and sale of plants" apparently because of the length of time the plants were held before being offered for sale. This distinction appears to be based even more on a matter of degree than the one the court refused to make.

It would seem that there was ample evidence to find that the business prospered primarily from Mr. Pepper's efforts during marriage since the nursery was run for fifteen or sixteen years before marriage at a very small return. *Estate of Pepper*, 8 Cal. App. Dec. 720, 722 (1909).

¹⁷⁸ *McKAY, COMMUNITY PROPERTY* 161 (1st ed. 1910).

¹⁷⁹ In *Diefendorff v. Hopkins*, 95 Cal. 343, 28 Pac. 265, *aff'd per curiam*, 30 Pac. 549 (1892), the court held that the profits of the wife's separate property boarding house were her separate property notwithstanding the fact that some part of this income was attributable to her efforts. The court reasoned that personal labor would be involved in the production of all rents, issues, and profits in some degree but this was no reason to alter the holding that the profits were separate. See *LeSourd, Community Property Status of Income from Business Involving Personal Services and Separate Capital*, 22 WASH. L. REV. & ST. B.J. 19, 22 (1948); note 177 *supra*.

¹⁸⁰ 133 Cal. 462, 65 Pac. 1041 (1901).

¹⁸¹ See also cases cited note 82 *supra*.

the husband had earned from making investments with his separate capital was held not to belong to the community.¹⁸² The court reasoned that "those profits . . . which have arisen naturally and without the active engagement by the husband of his capital in some business or employment" were separate property.¹⁸³

The second factor that caused the *Pepper* court to feel that *Pereira* was not binding was the notion that crops grown on land are the natural product of the soil and necessarily arise from the ordinary use of the property. This notion seems to have been borrowed from the common law cases dealing with the attempts of a husband's creditors to reach the profits of the wife's separate property where the husband had devoted his time and skill to producing these profits. In *Lake v. Bender*,¹⁸⁴ which first used these cases,¹⁸⁵ the dissent pointed out that the principle of not allotting any part of the income to the ability of the husband was applicable

to cases where the accumulations of property were derived from conducting and carrying on the farming business, and other business of like character . . . [because] the ownership of a farm necessarily carries with it the right to the products grown thereon.¹⁸⁶

The influence of the cases discussed by the dissent in *Lake* seems to have caused the *Pepper* court to draw a distinction between a farm and a business. The products of a farm were viewed as necessarily following from the ordinary use of land, whereas the profit from a business may or may not result from ordinary use, depending on the circumstances of the individual case.

It was a combination of these factors that was responsible for the *Pepper* decision. The court in *Pepper* undoubtedly felt that all the income from a farm issued "naturally" from the soil, notwithstanding the fact that a certain amount of labor was necessary in its production, and that all income arising naturally constituted rents and profits, thus belonging to the owner of the separate property under Civil Code sections 162 and 163.¹⁸⁷

2. *Pepper* and *Pereira* Reconciled

In light of the fact that the "apportionment rule" of *Pereira v. Pereira* was formulated by a resort to the same line of common law creditor cases considered in the dissent in *Lake*,¹⁸⁸ *Pereira* may be viewed as being consistent with *Pepper*. Arguably, the court in *Pereira* decided that the income from the husband's business did not constitute rents and profits since it did not issue from the ordinary use of his property.¹⁸⁹ Because the income from Mr. Pereira's business in no way involved a product of the soil, the court could have decided whether such profits arose from the ordinary use of the property under the facts of the case. There not

¹⁸² The notion that the owner of property must be given its beneficial use was one of the reasons for holding that the rents and profits of the wife's separate property must be considered separate property in *George v. Ransom*, 15 Cal. 322 (1860). See *Boyd v. Oser*, 23 Cal. 2d 613, 145 P.2d 312 (1944).

¹⁸³ 133 Cal. at 468, 65 Pac. at 1044.

¹⁸⁴ 18 Nev. 361, 4 Pac. 711 (1884), discussed in text following note 83 *supra*.

¹⁸⁵ See note 94 *supra* and accompanying text.

¹⁸⁶ 18 Nev. at 396, 4 Pac. at 731-32; see *Lake v. Bender*, 18 Nev. 361, 395-400, 4 Pac. 711, 731-36 (1884) (dissenting opinion).

¹⁸⁷ See note 1 *supra*.

¹⁸⁸ Note 186 *supra*; see text following note 124 *supra*.

¹⁸⁹ It appears that a large part of the profits may have been attributable to the gambling done by Mr. Pereira in his saloon. See Transcript on Appeal, pp. 81-85, *Pereira v. Pereira*, 156 Cal. 1, 103 Pac. 488 (1909).

being "ordinary use," the husband would then have been entitled only to the interest rate on the capital he had invested as if he had loaned it to the community to operate the business. Had the court desired to apportion in *Pepper*, they could have easily relied on *Pereira*, and found that the profits belonged to the community, except for the separate property's fair rental value.¹⁹⁰

C. Van Camp v. Van Camp

The *Pepper* case had its greatest impact through its use in *Van Camp v. Van Camp*.¹⁹¹ In this case, the husband was the controlling shareholder of a large incorporated business, and devoted his efforts exclusively to the management of the business. During the marriage he received a total of \$141,000 as dividends on his stock in the corporation, and a total of \$90,000 as salary which the evidence established as reasonable for the services he performed. The court found that although the salary belonged to the community, all the dividends were the husband's separate property. The court relied on *Pepper* for the proposition that where no apportionment of business income can be made the entire amount should be considered separate property.¹⁹² Thus, since the court felt that it was impossible to determine what part of the dividends accrued from the skill of the husband, and what part from factors attributable only to the business,¹⁹³ the whole amount was held to be separate property.¹⁹⁴

The reliance on *Pepper* would seem unjustified. *Pepper* clearly indicated that its holding was restricted to situations involving products of the soil, and distinguished the situation where the profits take the form of business profits.¹⁹⁵ Con-

¹⁹⁰ This was the result reached by the court in *Laughlin v. Laughlin*, 49 N.M. 20, 155 P.2d 1010 (1944), where the court rejected the *Pepper* case and applied the *Pereira* "rule" to a farm.

¹⁹¹ 53 Cal. App. 17, 199 Pac. 885 (1921).

¹⁹² The court stated that "the case presented is not unlike that involved in *Estate of Pepper* . . . wherein it was held that the profits and earnings [were] his separate property, notwithstanding the success of the venture required industry, skill, and attention." 53 Cal. App. at 28, 199 Pac. at 889.

¹⁹³ After citing *Pepper*, the court in *Van Camp* said:

So, in the instant case, it is impossible to say what part of the enormous dividends paid by the Van Camp Sea Food Company should be apportioned to the skill and management thereof and what part should be apportioned to the investment of the capital and the favorable conditions under which the business was conducted.

53 Cal. App. at 28, 199 Pac. at 889.

¹⁹⁴ The confusion that would result from an application of the *Pepper* reasoning to a commercial enterprise was recognized by the counsel for Mrs. Van Camp, who argued before the Supreme Court that

whatever may be determined of the corporate character of the appellant's business, the *Estate of Pepper* cannot be applied in this action as an authority, without confusing the law relating to the question of community property rights in the state of California, and if the principles which have heretofore been marked out by these two decisions are to be adhered to, the case of *Pereira v. Pereira* must be given controlling force.

Petition for Hearing by the Supreme Court, pp. 27-28, *Van Camp v. Van Camp*, 53 Cal. App. 17, 199 Pac. 885 (1921).

¹⁹⁵ It was recognized in *Pepper* that

there may be cases in which the business is virtually one of purchase and sale of plants, the ground being used merely to preserve the plants until sales can be effected [and] in such cases it might well be said that the enterprise is so predominantly commercial that the profits are not to be treated as issuing from the land.

158 Cal. at 624, 112 Pac. at 64-65. See BURBY & PATTY, SELECTED PROBLEMS IN COMMUNITY PROPERTY AND DOMESTIC RELATIONS 13 (1948); 3 MERTENS, INCOME TAX § 19.38 n.49 (1957).

cerning the latter situation, *Pepper* acknowledged that such profits would not necessarily be considered as arising from the "ordinary use of the separately held property," indicating that they should be subjected to apportionment insofar as it was required by *Pereira*.

1. *The Van Camp "Method"*

As happened with *Pereira*, the decision in *Van Camp* has been extended beyond the context in which it was decided.¹⁹⁶ In *Huber v. Huber*,¹⁹⁷ the California Supreme Court first approved the "method" used in *Van Camp*,¹⁹⁸ stating that a proper apportionment is to take what the evidence establishes as being the reasonable value of the spouse's services as the full amount of the community interest, with the remainder all being separate property.¹⁹⁹ The community interest in *Huber* was found to be \$7,200, which the husband's accountant testified was the reasonable value of the husband's services, although the husband had taken a total of \$14,400 in salary or drawing.²⁰⁰

The rule in *Huber* was not required by the *Van Camp* decision. *Van Camp* did not hold that the community interest was limited to the amount established by the evidence as the reasonable value of the spouse's services. It indicated only that business profits not capable of being apportioned must belong to the spouse owning the business.²⁰¹ *Van Camp* did not hold that all business profits are necessarily not apportionable.²⁰²

¹⁹⁶ As with *Pereira*, see text following note 150 *supra*, the *Van Camp* case has been taken as establishing a method of apportionment. In *Gilmore v. Gilmore*, 45 Cal. 2d 142, 149-50, 287 P.2d 769, 773 (1955), the court said: "It has frequently been held that a proper method of making such allocation is to deduct from the total earnings of the business the value of the husband's services to it. The remainder, if any, represents the earnings attributable to the separate property invested in the business." See *Harold v. Harold*, 43 Cal. 2d 77, 271 P.2d 489 (1954); *Huber v. Huber*, 27 Cal. 2d 784, 167 P.2d 708 (1946); *Belmont v. Belmont*, 188 Cal. App. 2d 33, 10 Cal. Rptr. 227 (1961); *Mears v. Mears*, 180 Cal. App. 2d 484, 4 Cal. Rptr. 618 (1960); *Tassi v. Tassi*, 160 Cal. App. 2d 680, 325 P.2d 872 (1958); *Logan v. Forster*, 114 Cal. App. 2d 587, 250 P.2d 730 (1952); *Cozzi v. Cozzi*, 81 Cal. App. 2d 229, 183 P.2d 739 (1947); *Gump v. Commissioner*, 124 F.2d 540 (1941).

¹⁹⁷ 27 Cal. 2d 784, 167 P.2d 708 (1946).

¹⁹⁸ See 1 ARMSTRONG 478.

¹⁹⁹ Some courts have even taken the view that the *Van Camp* "method" limits the community to the actual salary that the husband draws. In *Seligman v. Seligman*, 85 Cal. App. 683, 687, 259 Pac. 984, 986 (1927), the court stated: "Not the profits of the business, but only the earnings of the plaintiff from his individual efforts, or what might be called his salary or wages, would be community property." See *Shea v. Commissioner*, 81 F.2d 937, 939 (1936); *Horne, Community Property—A Functional Approach*, 24 So. CAL. L. REV. 42, 53 (1950); Comment, 1 So. CAL. L. REV. 161, 162-63 (1927).

The New Mexico courts rejected the *Pepper* decision in *Laughlin v. Laughlin*, 49 N.M. 20, 155 P.2d 1010 (1944), but adopted the *Van Camp* "method" in *Katson v. Katson*, 43 N.M. 214, 89 P.2d 524 (1939), and found that the community was limited to the salary. See Comment, 36 TEXAS L. REV. 187, 193-94 (1957).

²⁰⁰ Thus, the *Huber* case put to rest the contention that the *Van Camp* "method" limited the community to the actual salary of the husband. See *Tassi v. Tassi*, 160 Cal. App. 2d 680, 325 P.2d 872 (1958); note 199 *supra*.

²⁰¹ See notes 192-93 *supra* and accompanying text.

²⁰² In the sense that the *Van Camp* case held that the salary was community but that all the dividends were separate, the case can be taken as a combination of *Pepper* and *Pereira*. See VERRALL, CASES ON CALIFORNIA COMMUNITY PROPERTY 118 (1960); Evans, *Primary Sources of Acquisition of Community Property*, 10 CALIF. L. REV. 271, 282 (1922); Note, 14 CALIF. L. REV. 402, 404 n.15 (1926).

Whether there still exists a sound basis for using the *Van Camp* "method" depends on the effect of *Estate of Neilson* in overruling *Pepper*,²⁰³ since the latter case was relied on in the *Van Camp* decision.²⁰⁴

2. The Problem of Increase

In *Gilmore v. Gilmore*,²⁰⁵ the *Van Camp* "method" was used to apportion the increased value or appreciation of the husband's separately owned business.²⁰⁶ Professor Burby suggests that it was unwise to consider the increase in a business in the same manner as its profits,²⁰⁷ apparently arguing that the appreciated value of separate property should belong to the community. This contention could be supported on the basis that Civil Code sections 162 and 163,²⁰⁸ the provisions defining separate property, do not include the increased value of separate property, and that the residual definition of community property would thus apply to the increase, making it community property.²⁰⁹ Furthermore, since the statutes of other states include increase in their definitions of separate property,²¹⁰ it could be argued that the Legislature of California, by omitting the mention of increase from their definition, intended increases to belong to the community.

These arguments, however, overlook the fact that the increase of separate property remained separate under the original Spanish-Mexican laws.²¹¹ Even states like Texas, which continue to classify the rents and profits of separate property as belonging to the community, classify the increase as separate.²¹² As stated by the Washington court in *Guye v. Guye*,²¹³ "since by the statute the spouse owning separate property is entitled to the rents, issues and profits thereof, so such owner must be entitled to the natural increase in value, as such increase is as much the issue of such property as would be the rents derived therefrom."²¹⁴

²⁰³ See note 272 and text accompanying note 273 *infra*.

²⁰⁴ See text accompanying note 192 *supra*.

²⁰⁵ 45 Cal. 2d 142, 287 P.2d 769 (1955).

²⁰⁶ In *Gilmore* the wife contended that the increase in value of the husband's three incorporated auto dealerships from \$182,010.46 to \$786,045.52 should be partially allocated to the community. The court, however, applied the *Van Camp* "method" and held that the salary or drawings of the husband had been adequate compensation for his services; thus, the entire amount of increase was apportioned as his separate estate.

²⁰⁷ FAMILY LAW FOR CALIFORNIA LAWYERS 369 (Cont. Ed. Bar 1956).

²⁰⁸ CAL. CIV. CODE §§ 162, 163. See note 1 *supra*.

²⁰⁹ CAL. CIV. CODE § 687: "Community property is property acquired by husband and wife, or either, during marriage, when not acquired as the separate property of either." See *Dow v. Gould & Curry Silver Mining Co.*, 31 Cal. 629 (1867); CAL. CIV. CODE § 164. See also *Estate of Gold*, 170 Cal. 621, 151 Pac. 12 (1915); 2 TIFFANY, REAL PROPERTY § 439 (3d ed. 1939); Evans, *Ownership of Community Property*, 35 HARV. L. REV. 47 (1921). But see DEFUNIAK, CASES ON COMMUNITY PROPERTY 58 (1947).

²¹⁰ See, e.g., ARIZ. REV. STATS. ANN. § 25-213 (1956).

²¹¹ SCHMIDT, THE CIVIL LAW OF SPAIN AND MEXICO pt. 2, at 13 (1851) (art. 47); 1 WHITE, A NEW COLLECTION OF THE LAWS OF THE GOVERNMENTS OF GREAT BRITAIN, FRANCE AND SPAIN 61-63 (1839); see ESCRICHE, DICCIONARIO RAZONADO DE LEGISLACION Y JURISPRUDENCIA 367 (1925); Huie, *Some Principles of Texas Community Law*, in CHARMATZ & DAGGETT, COMPARATIVE STUDIES IN COMMUNITY PROPERTY 115, 116-17 (1955).

²¹² TEX. REV. CIV. STAT. ANN. art. 4613 (1960).

²¹³ 63 Wash. 340, 115 Pac. 731 (1911).

²¹⁴ *Id.* at 348, 115 Pac. at 734. Recently the California Supreme Court recognized that "any increase in the value of the land attributable to plaintiff's [husband's] efforts was also community property." *Mayhood v. LaRosa*, 58 A.C. 510, 512, 374 P.2d 805, 806, 24 Cal. Rptr. 837 (1962).

Since the increased value of a business may in part be attributed to what is in effect a reinvestment of the profits, it is difficult to distinguish rationally the profits of a business from its increase. Thus, if the skill and efforts of a spouse are at least in part responsible for the increase, the increase resulting from such efforts would seem allocable to the community in the same manner as business profits.²¹⁵

D. The Tax Formula

Because of the divergence in approach, the results reached under the *Pereira* "rule" and *Van Camp* "method" are at opposite extremes. In any given case, if the apportionment were first to be made in accordance with the *Pereira* interest rate formula, and then separately computed in the manner indicated by *Van Camp*, part of the total income may remain unallocated to either.²¹⁶

Recognizing this hiatus in the results of the *Pereira* "rule" and *Van Camp* "method," Professor Burby²¹⁷ and Professor Moynihan²¹⁸ have suggested that the formula applied in tax cases be used as a compromise.²¹⁹ This "tax formula" involves first computing both the fair rate of return of the separate capital invested in the business, and the value of the services rendered.²²⁰ The ratio of the value of the services is then taken to the total of the fair rate of return and such value of services, with the ratio being multiplied times the total profits in dispute to establish the share of the community. The share of the separate estate is determined by taking the ratio of the fair rate of return to the same denominator as above, and again multiplying times the total profits.²²¹ This tax formula is actually a means of dividing the difference between the value the courts place on the services and the rate of return given the capital.²²² The fact that a difference exists

²¹⁵ See Oppenheim, *A Comparative Study of Community Property Systems*, 21 TEMP. L.Q. 235 (1948). See also Emery, *Mutations*, 4 SW. L.J. 123, 126-27 (1950).

²¹⁶ If, in a hypothetical case, the husband had \$100,000 invested in his separate property business which earned \$38,000 a year, and from which he drew a salary of \$12,000, the amount given the separate estate will vary greatly depending on which method of apportionment is used. If the *Pereira* method is used, the court would apply a rate of about 7% and find that \$7,000 was separate property and \$31,000 was community property. If the court were to apply the *Van Camp* rule, they would probably find that his salary was the reasonable value of his services, and \$12,000 would be held to be community property with the remaining \$24,000 going to his separate estate. Thus if the husband was given \$7,000 by applying *Pereira*, and the community given \$12,000 under *Van Camp*, there would remain \$19,000 unallocated to either.

²¹⁷ BURBY, CASES ON COMMUNITY PROPERTY 91 (2d ed. 1955).

²¹⁸ 2 AMERICAN LAW OF PROPERTY § 7.12, at 147-48 (Casner ed. 1952).

²¹⁹ This formula was first promulgated in G.C.M. 9825; X-2 CUM. BULL. 146 (1931), and first used in Clara B. Parker, 31 B.T.A. 644 (1934). See generally SURREY & WARREN, CASES ON FEDERAL INCOME TAXATION 1048-49 (1962).

²²⁰ In this sense the "tax formula" appears to be based on the idea that there are two different methods for making the apportionment. See Comment, 21 SO. CAL. L. REV. 447, 450 n.9 (1948).

²²¹ Thus, if the husband has \$100,000 invested in his restaurant business which he owned at the time of marriage, assume that 7% would be a fair rate of return on capital, that \$12,000 would be a reasonable salary, and that the net income was \$38,000. The separate property portion would be \$7,000 (7% of \$100,000) divided by \$19,000 (total of fair return and reasonable salary), multiplied by \$38,000 (the earnings for the year), or \$14,000. The community share would be \$12,000 divided by \$19,000 times \$38,000, or \$24,000.

²²² If the fair return on capital plus the reasonable value of services rendered equaled the income, there would be no need to apply the ratio. In the illustration in note 221 *supra*, if the net income was \$19,000 instead of \$38,000 an application of the ratio would result in a finding that \$7,000 was separate property and \$12,000 was community property.

cannot logically be the basis of a solution to the problem, but rather points out that the two methods upon which the tax formula is based²²³ are arbitrary.²²⁴ Consequently, the tax formula itself cannot help but yield an arbitrary result.²²⁵

In addition to being arbitrary, the use of the "tax formula" in federal tax cases would also seem unjustified. The tax laws specify that property is to be classified according to the law of the state in which it is located.²²⁶ Inasmuch as the formula had never been used by a California court prior to its appearance in the tax case,²²⁷ its use in the federal courts appears improper;²²⁸ these courts should have determined whether income was community or separate in accordance with the apportionment methods previously used in California civil cases.²²⁹ Moreover, the courts of the Ninth Circuit, in applying this "formula," do not take into account the basic presumption of the community property system²³⁰ that all property acquired after marriage belongs to the community.²³¹ Rather, they presume that the Commissioner has correctly determined the tax, thereby placing upon the taxpayer, who is normally trying to show that more community property exists,²³² the burden of showing the character of the property.²³³

²²³ The first tax method, proposed in 1925, recognized the *Pereira* case as the rule in California. After the *Van Camp* "method" gained acceptance, G.M.C. 9825 was proposed. See IV-2 CUM. BULL. 125 (1925); VI-1 CUM. BULL. 26 (1927); X-2 CUM. BULL. 146 (1931). See also LeSourd, *Community Property Status of Income From Business Involving Personal Services and Separate Capital*, 22 WASH. L. REV. & ST. B.J. 19, 27-33 (1947); Kizer, *Community Interest in Commingled Income, Derived from Personal Service and Separate Capital—Another View*, 23 WASH. L. REV. & ST. B.J. 8 (1948); Note, 20 So. CAL. L. REV. 108, 110 (1946); Comment, 21 So. CAL. L. REV. 447, 450 n.9 (1948).

²²⁴ If either the *Pereira* "rule" or the *Van Camp* "method" were accurate ways to assess the value of the separate estate, the amounts yielded by their application should equal the profits of the business. That is, if *Pereira* had furnished a method to determine accurately the separate property interest, and if *Van Camp* had set down a rule by which the community's contribution could be properly determined, their application in any given case would yield consistent results. But see note 216 *supra*.

²²⁵ See Kizer, *supra* note 223, at 10-12.

²²⁶ 3 MERTENS, FEDERAL INCOME TAXATION § 19.10 (1957).

²²⁷ Although the tax formula has been used in a California tax case, *Todd v. McColgan*, 89 Cal. App. 2d 509, 201 P.2d 414 (1949), it had been used many times by the federal courts before it had been adopted in California. *E.g.*, *Todd v. Commissioner*, 153 F.2d 553 (9th Cir. 1945).

²²⁸ It has been suggested that the application of the "tax formula" violates the policy of *Erie v. Tompkins*, 304 U.S. 64 (1938). See Kizer, *Community Interest in Commingled Income, Derived from Personal Service and Separate Capital—Another View*, 23 WASH. L. REV. & ST. B.J. 8, 15-16 (1948). It would not seem, however, that the *Erie* doctrine is applicable. See generally HART & WECHSLER, *THE FEDERAL COURTS AND THE FEDERAL SYSTEM* 633-36 (1953); LOUISELL & HAZARD, *CASES ON PLEADING AND PROCEDURE* 1271-76 (1962).

²²⁹ This apparently was realized in the first bulletin covering the income from a separate property business. See IV-2 CUM. BULL. 125 (1925), Lawrence Oliver, 4 T.C. 684 (1945). Liability under the federal estate tax is determined in accordance with local law. See LOWNDES & KRAMER, *FEDERAL ESTATE AND GIFT TAXES* 250 (2d ed. 1962).

²³⁰ The presumption is recognized by the Fifth Circuit in tax cases. See *McFadden v. Commissioner*, 148 F.2d 570 (5th Cir. 1945); *Howard v. United States*, 125 F.2d 986 (5th Cir. 1942). The presumptions are also followed in determining liability for the federal estate tax. See *J. G. Sweeney*, 15 B.T.A. 1287, 1292 (1929); LOWNDES & KRAMER, *FEDERAL ESTATE AND GIFT TAXES* 240-42 (1st ed. 1956).

²³¹ See, *e.g.*, *Shea v. Commissioner*, 81 F.2d 937 (9th Cir. 1936).

²³² See LeSourd, *Community Property Status of Income from Business Involving Personal Services and Separate Capital*, 22 WASH. L. REV. & ST. B.J. 19, 30-31 (1947). See also Kizer, *Community Interest in Commingled Income, Derived from Personal Service and Separate Capital—Another View*, 23 WASH. L. REV. & ST. B.J. 8, 10-11 (1948).

²³³ See Kizer, *supra* note 232, at 14-16.

E. Each Case Decided on its Facts

The proposed use of the tax formula could be supported by language in several cases that the apportionment question is a factual one to be decided in each case by the trier of fact in any manner deemed equitable.²³⁴ Treating the apportionment of income solely as a question of fact seems to be regarded by deFuniak as the only solution to the problem of apportionment.²³⁵ Indeed, the language used in *Estate of Gold*²³⁶ could be taken to indicate that the "rule" intended by *Pereira* was only that each case must be decided in light of all the circumstances.²³⁷ Nevertheless, the construction given to *Pereira* by the later cases, including *Estate of Neilson*,²³⁸ suggests that the California Supreme Court would not presently support an unrestrained rule of apportionment.²³⁹

Several difficulties confront deFuniak's suggestion to allow the trier of fact to make the apportionment as a purely factual matter. With no guides for handling the problem, none of the confusion in selecting from the various rules would be cleared up, and the inconsistent *Pereira* and *Van Camp* approaches would continue to be applied at random. Furthermore, deFuniak's approach would give practically unlimited discretion to the trial judge in deciding the character of the property. Admittedly, discretion in a trial court is desirable in many instances, but in apportionment cases the trial judge may be prone to view the fault of the parties in determining which property belongs to the community. In the past, the fault of the parties seems to have had a great deal of effect on the results reached in a given case. It is possible, for example, that the favorable apportionment given the wife in *Pereira v. Pereira* was made because of the extremely cruel conduct of the husband;²⁴⁰ the failure in *Estate of Pepper* to find any community property for the wife to share could be explained by the fact that the wife had destroyed all the records kept by Mr. Pepper and offered no explanation for her actions.²⁴¹ Similarly, it has been suggested that the apportionment made in *Van Camp v. Van Camp*

²³⁴ The tax method was used by the California courts in *Todd v. McColgan*, 89 Cal. App. 2d 509, 201 P.2d 414 (1949), to determine the state income tax liability. The court, however, used language from federal cases to the effect that each case should be decided on its facts by any method the court chooses to apply. While the tax method has never been used in a California civil case, the courts have cited this language from *Todd*, and thus this notion has entered the California law. See, e.g., *Logan v. Forster*, 114 Cal. App. 2d 587, 250 P.2d 730 (1952).

²³⁵ See 1 DEFUNIAK § 71, at 185; DEFUNIAK, *Community Property*, 5 SURVEY OF CALIFORNIA LAW 154 (1952-1953). See also 3 MERTENS, FEDERAL INCOME TAXATION § 19.38 n.50 (1957).

²³⁶ 170 Cal. 621, 151 Pac. 12 (1915).

²³⁷ This is well illustrated by Justice Shaw's statement in *Gold*:

The principle there stated [in *Pereira*] is that the question what part of the subsequent profits arises from the use of this capital, and what part from the personal activity, ability, and capacity of the husband, is to be determined by the court from the circumstances appearing in the case . . .

170 Cal. at 623, 151 Pac. at 13.

²³⁸ 57 Cal. 2d 733, 740, 22 Cal. Rptr. 1, 4-5 (1962).

²³⁹ This is indicated by the construction given *Pereira* in *McDuff v. McDuff*. See text accompanying note 156 *supra*. The language used in *Neilson* suggests a similar conclusion, where *Pereira* is taken as the usual rule, and explicit situations calling for departures are listed. See text following note 255 *infra*.

²⁴⁰ In *Pereira*, the cruelty of the husband was of an extreme nature. Findings of Fact, Transcript on Appeal, pp. 46-50, *Pereira v. Pereira*, 156 Cal. 1, 103 Pac. 488 (1909); see THOMAS, APPORTIONMENT IN COMMUNITY PROPERTY STATES 38 (1927).

²⁴¹ Application That Cause be Heard and Determined by Supreme Court After Decision by the District Court of Appeal, p. 6, *Estate of Pepper*, 158 Cal. 619, 112 Pac. 62 (1910).

was influenced by the court's attitude toward the wife, whom it viewed as a gold digger.²⁴² It thus appears that the courts are susceptible to confusing their discretion in *dividing* the community property²⁴³ with the decision of what property is community property.²⁴⁴

III

APPORTIONMENT AFTER *Neilson*

Although neither *Van Camp v. Van Camp* nor *Pereira v. Pereira* were intended to promulgate methods of apportionment,²⁴⁵ the subsequent cases proceeded along diverging lines of approach based on these two decisions.²⁴⁶ While there was authority that an apportionment could be made in either manner,²⁴⁷ most commentators considered the *Van Camp* and *Pereira* methods to be inconsistent.²⁴⁸ In any event, it was impossible to predict which approach would be used by the courts in any given situation.²⁴⁹

In *Estate of Neilson*,²⁵⁰ the wife, having been disinherited by her husband, exercised her election to take half of the community property against the will.²⁵¹ The trial court refused to give an instruction proposed by the heirs of the husband's estate to the effect that the income from the husband's farm was all his separate property even though the husband devoted his efforts to running the farm during marriage. The trial court stated "that the rule of *Estate of Pepper* has been 'practically wrecked' by subsequent cases."²⁵² In affirming, the Supreme Court of California expressly overruled *Pepper*, stating that an apportionment must be made whenever one of the spouses has earned money by combining his skill with the use of a separate asset, regardless of whether the revenue has been earned through a business, farm,²⁵³ or constant reinvestment²⁵⁴ of separate capital.

²⁴² 1 ARMSTRONG 478.

²⁴³ In certain divorce situations the trier of fact must award more than one-half of the community property to the innocent party, but has discretion as to what portion over one-half should be awarded. 1 ARMSTRONG 791-96.

²⁴⁴ While the discretion of the judge to view the fault of the parties in deciding *how* the community property should be divided is desirable, this type of discretion should have no bearing on the issue of *whether* property is community or separate.

²⁴⁵ See text following notes 150 and 196 *supra*.

²⁴⁶ Compare cases cited note 196 *supra* with cases cited note 154 *supra*.

²⁴⁷ In *Tassi v. Tassi*, 160 Cal. App. 2d 680, 690, 325 P.2d 872, 878 (1958), the court said, "Two approaches have ordinarily been made to the allocation of earnings in such cases," citing *Pereira* for one rule and *Huber v. Huber* for another.

²⁴⁸ Comment, 21 So. CAL. L. REV. 447, 450 n.9 (1948); see *Logan v. Forster*, 114 Cal. App. 2d 587, 250 P.2d 730 (1952); *Shea v. Commissioner*, 81 F.2d 937, 938-39 (1936); 4 WILKIN, SUMMARY OF CALIFORNIA LAW *Community Property* §§ 17-18 (7th ed. 1960); cf. Comment, 1 So. CAL. L. REV. 161, 163 (1927).

²⁴⁹ The disparity in result between an application of the *Pereira* "rule" and the *Van Camp* "method," coupled with the impossibility of foreseeing which will be applied, perhaps has some merit in that parties are more likely to settle their dispute out of court.

²⁵⁰ 57 Cal. 2d 733, 22 Cal. Rptr. 1 (1962).

²⁵¹ See *Estate of King*, 19 Cal. 2d 354, 121 P.2d 716 (1942); cf. CAL. PROB. CODE § 201.7. The nature of the wife's claim is not the same as the husband's claim. See CALIFORNIA ESTATE ADMINISTRATION §§ 26.46, 26.48 (Cont. Ed. Bar 1959).

²⁵² 57 Cal. 2d at 738, 22 Cal. Rptr. at 4.

²⁵³ The court stated that "there is no reason why a grain farmer or nursery operator who conducts his enterprise on separate property should be exempted from the normal apportionment rule and not required to account to the community for a portion of the profits." *Id.* at 741, 22 Cal. Rptr. at 5.

²⁵⁴ Justice Traynor stated that, "An apportionment of profits is required not only when

Having decided that an apportionment must be made, Justice Traynor stated that the usual method of making such an apportionment is in accordance with the rule of *Pereira*.²⁵⁵ A departure from *Pereira*, according to Justice Traynor, should be made only when the husband can show that his capital is entitled to a greater return.²⁵⁶ This showing can be established by proof that there were unusually large profits and increases in other businesses of the same type;²⁵⁷ that the spouse did not take an active part in the control of the business;²⁵⁸ that there has been a general increase in population and economic growth in the community;²⁵⁹ or that the business requires a large sum of capital.²⁶⁰

the husband conducts a commercial enterprise but also when he invests separate funds in real estate or securities." *Id.* at 740, 22 Cal. Rptr. at 5. Although the language used might indicate that this was settled law, there had been much confusion whether investing in securities and real estate was a business and came within the rules relating to apportionment. 1 CALIFORNIA FAMILY LAWYER § 4.23 (Cont. Ed. Bar 1961); LeSourd, *Community Property Status of Income From Business Involving Personal Services and Separate Capital*, 22 WASH. L. REV. & ST. B.J. 19, 24-25 (1947).

²⁵⁵ The language that *Pereira* is the "usual method" was first used in *Randolph v. Randolph*, 118 Cal. App. 2d 584, 258 P.2d 547 (1953), although similar language was used earlier in *Stice v. Stice*, 81 Cal. App. 2d 792, 185 P.2d 402 (1947). While no citation was given for the language in *Randolph*, it is interesting to note that the language appears to have originated in 3 CAL. JUR. 534 (Ten Yr. Supp. 1936). See Brief for Respondent, pp. 6-7, *Randolph v. Randolph*, 118 Cal. App. 2d 584, 258 P.2d 547 (1953).

²⁵⁶ In *Neilson*, the court quoted from *Randolph* to the effect that: "Only when the profits and accruals actually attributable to the separate property are proved to differ from [the usual interest rate for a well secured investment] . . . is there reason to depart from this system." 57 Cal. 2d at 740, 22 Cal. Rptr. at 5.

²⁵⁷ *Ibid.*, citing *Gilmore v. Gilmore*, 45 Cal. 2d 142, 287 P.2d 769 (1955); *Harrold v. Harrold*, 43 Cal. 2d 77, 271 P.2d 489 (1954); *Tassi v. Tassi*, 160 Cal. App. 2d 680, 325 P.2d 872 (1958).

²⁵⁸ 57 Cal. 2d at 740, 22 Cal. Rptr. at 5, citing *Gilmore v. Gilmore*, 45 Cal. 2d 142, 287 P.2d 769 (1955); *Logan v. Forster*, 114 Cal. App. 2d 587, 250 P.2d 730 (1952); *Cozzi v. Cozzi*, 81 Cal. App. 2d 229, 183 P.2d 739 (1947). See also *Estate of Graniss*, 142 Cal. 1, 75 Pac. 324 (1904); *Estate of Cudworth*, 133 Cal. 462, 65 Pac. 1041 (1901); *Estate of Higgins*, 65 Cal. 407, 4 Pac. 389 (1884); *Kenney v. Kenney*, 128 Cal. App. 2d 128, 274 P.2d 951 (1954); *Estate of Barnes*, 128 Cal. App. 489, 17 P.2d 1046 (1932); *Gump v. Commissioner*, 124 F.2d 540 (9th Cir. 1941).

²⁵⁹ 57 Cal. 2d at 740, 22 Cal. Rptr. at 5, citing *Gilmore v. Gilmore*, 45 Cal. 2d 142, 287 P.2d 769 (1955); *Logan v. Forster*, 114 Cal. App. 2d 587, 250 P.2d 730 (1952). See also *Berry v. Berry*, 117 Cal. App. 2d 624, 256 P.2d 646 (1953); *Gump v. Commissioner*, 124 F.2d 540 (9th Cir. 1941).

²⁶⁰ 57 Cal. 2d at 740, 22 Cal. Rptr. at 5, citing *Huber v. Huber*, 27 Cal. 2d 784, 167 P.2d 708 (1946). Other cases have shown that if the inactive spouse can prove that the capital was not an important factor, and that the profits are due almost entirely to the skill and ability of the active spouse, the entire profit would be community. *Austin v. Austin*, 190 Cal. App. 2d 45, 11 Cal. Rptr. 593 (1961); *Estate of Fellows*, 106 Cal. App. 681, 289 Pac. 887 (1930); *cf. Estate of Gold*, 170 Cal. 621, 151 Pac. 12 (1915).

Under the *Neilson* decision, there can be an allocation of the entire proceeds and increment only when they are attributable solely to the natural enhancement of the property, 57 Cal. 2d at 740, 22 Cal. Rptr. at 5, citing *Estate of Cudworth*, 133 Cal. 462, 65 Pac. 1041 (1901); *McDuff v. McDuff*, 48 Cal. App. 175, 191 Pac. 957 (1920), or when the husband expended only minimal effort and the wife introduced no evidence attributing a value to his services, 57 Cal. 2d at 740, 22 Cal. Rptr. at 5, citing *Cozzi v. Cozzi*, 81 Cal. App. 2d 229, 183 P.2d 739 (1947); *Estate of Barnes*, 128 Cal. App. 489, 17 P.2d 1046 (1932). See discussion in text following note 282 *infra*. See also *Estate of Heltsel*, 200 Cal. App. 2d 398, 19 Cal. Rptr. 352 (1962). In New Mexico there is no apportionment made if the increase is due to the natural enhancement of the property. CLARK, COMMUNITY OF PROPERTY AND THE FAMILY IN NEW MEXICO 19 (1956).

From the unhesitating manner in which the *Pereira* method was applied, it would appear that little confusion had ever existed. However, Justice Traynor's straightforward application of the *Pereira* rule as the usual method is surprising in view of his prior opinion in *Gilmore v. Gilmore*.²⁶¹ In the latter opinion, he stated that the *Pereira* rule was applicable "only in the absence of other circumstances";²⁶² the trial court's use of the *Van Camp* method²⁶³ was held sustained by the evidence. Although the language of *Gilmore* taken literally might appear consistent with *Neilson*,²⁶⁴ the differing emphasis in the two cases would seem to suggest that a change has occurred in the supreme court's attitude towards apportionment. The language in *Gilmore* indicated that the *Van Camp* method was preferred, and that *Pereira* was more of an exception. In fact, the *Gilmore* decision prompted Professor Marsh to write that "the Supreme Court in *Gilmore* in effect overruled *Pereira*. . . ."²⁶⁵ Thus, although *Neilson* has dispelled any thought that *Pereira* is overruled, the extent to which it is now to be applied is still uncertain.

The decision in *Neilson* purports only to reiterate what the proper method of apportionment is; it does this by citing previous apportionment cases with approval. Justice Traynor's opinion, however, is the first decision by any California court to consider all the relevant cases in stating the manner for making an apportionment,²⁶⁶ and he has in effect woven the old cases into a new pattern. In the past, the courts generally have either relied on the *Van Camp* line of cases without considering the *Pereira* method,²⁶⁷ or conversely have used *Pereira* without mention of *Van Camp*.²⁶⁸ *Neilson* makes no comment on the apparent inconsistency of the two approaches, but rather makes *Pereira* the starting point of an apportionment problem, with the criteria used in cases applying *Van Camp* serving in some manner to modify the result reached with *Pereira*.

Justice Traynor lists several criteria for determining when *Pereira* may be departed from,²⁶⁹ but he fails to state what is to be done once the departure is made. Since the cases cited as illustrative of the criteria for departure all use the *Van Camp* approach²⁷⁰ it is possible that Justice Traynor intended a complete departure from *Pereira* to the *Van Camp* method once the relevant criteria are established.²⁷¹ However, a departure from *Pereira* need not entail a complete switch to *Van Camp*. In keeping with the use of *Pereira* as the usual method under

²⁶¹ 45 Cal. 2d 142, 287 P.2d 769 (1955).

²⁶² *Id.* at 150, 287 P.2d at 774.

²⁶³ See text following note 196 *supra*.

²⁶⁴ Application of *Pereira* only "in the absence of other circumstances," as suggested by *Gilmore*, is not necessarily inconsistent with the use of *Pereira* as the "usual method" under *Neilson*, particularly in view of the "other circumstances" mentioned by *Neilson* as reasons for departing from *Pereira*. See text following note 256 *supra*. But whether a departure from *Pereira* under the *Neilson* framework calls for application of *Van Camp* is unclear. See text following note 269 *infra*. If *Van Camp* may still be applied, then *Gilmore* and *Neilson* are at least to some extent consistent. See note 272 *infra*.

²⁶⁵ 1 CALIFORNIA FAMILY LAWYER § 4.23, at 115 (Cont. Ed. Bar 1961).

²⁶⁶ See cases cited in notes 256-60 *supra*. In *Gilmore v. Gilmore*, 45 Cal. 2d 142, 150, 287 P.2d 769, 774 (1955), Justice Traynor attempted to reconcile the *Pereira* and *Van Camp* rules, but he did not list the factors that called for a departure from *Pereira*.

²⁶⁷ See, e.g., *Belmont v. Belmont*, 188 Cal. App. 2d 33, 10 Cal. Rptr. 227 (1961).

²⁶⁸ See, e.g., *Estate of Arstein*, 56 Cal. 2d 239, 14 Cal. Rptr. 809 (1961).

²⁶⁹ See text at notes 257-60 *supra*.

²⁷⁰ See notes 257-60 *supra*.

²⁷¹ This would make the *Gilmore* and *Neilson* decisions more readily reconcilable. See note 264 *supra*.

the renewed emphasis of *Neilson*, the various factors, if established, could be used only to modify the rate of return on the separate investment. The *Pereira* approach of first establishing a reasonable return for the separate estate could be basically adhered to, with the relevant factors then bearing only on what is the return.²⁷²

Since it still is not clear when the *Pereira* or *Van Camp* methods are to be applied, even though *Pereira* is now preferred as the "usual method,"²⁷³ it is important to analyze in what respects these methods differ. This will assist in deciding if and when it would be desirable to switch from *Pereira* to *Van Camp* under the framework set forth in *Neilson*. In theory, the two methods can be reconciled as differing only in approach, with the *Van Camp* method inquiring what the probable contribution of the spouse's efforts were in earning the income, while *Pereira* inquires what was the probable contribution of the capital.²⁷⁴ If both approaches achieved their intended goals, it would not be particularly important which method was used.

In practice, however, an application of *Van Camp* can yield a result different

²⁷² Since *Neilson* stated that "the long line of cases starting with *Pereira* dispels any notion that such impossibility [of apportionment] justifies a finding that none of the proceeds belongs to the community," 57 Cal. 2d at 741, 22 Cal. Rptr. at 5, a question remains whether the *Van Camp* "method" can still properly be used in California. As noted heretofore, see text following note 191 *supra*, the decision in *Van Camp* was based on the language in the *Pepper* case that where profits cannot be apportioned they must be considered as rents and profits of separate property, and, as such, allocated to the separate estate. Now that *Pepper* has been overruled, it would appear that the foundation of the *Van Camp* decision has been destroyed and that the holding of that case is itself no longer valid. However, the *Van Camp* case has been misconstrued and has been understood to stand for an apportionment method not actually put forth by the opinion. See text following note 196 *supra*. Inasmuch as this method has become an accepted part of California jurisprudence through its use in cases not relying on the *Van Camp* decision, see, e.g., *Huber v. Huber*, 27 Cal. 2d 784, 167 P.2d 708 (1946), it is doubtful that *Neilson* has rejected the *Van Camp* "method," although the case itself may no longer be good law. By failing to explain how an apportionment should be made when a departure from *Pereira* is indicated, see text following note 269 *supra*, *Neilson* has left room for dispute concerning the propriety of using *Van Camp*.

²⁷³ *Neilson* reversed the decision of the lower court on the ground that the jury had misinterpreted the trial court's instruction relating to the transmutation of the husband's separate property into community property. 57 Cal. 2d at 743, 22 Cal. Rptr. at 7. Although the Supreme Court considered the evidence in order to aid the trial court on remand on the issue of transmutation, *id.* at 743-46, 22 Cal. Rptr. at 7-9, it failed to make any comment on the evidence with regard to the issue of apportionment. The husband's heirs had argued that the income during the marriage was attributable primarily to the natural enhancement of the husband's separately owned property, apart from any reliance on *Pepper*. Appellant's Reply Brief, p. 11, *Estate of Neilson*, 181 Cal. App. 2d 769, 4 Cal. Rptr. 542 (1961). They further urged the *Gilmore* case as precluding the application of *Pereira*. Appellant's Reply Brief, pp. 11-14. The wife on the other hand urged the *Pereira* rule, arguing that gifts by the husband more than accounted for the value of the separate estate as determined under *Pereira*, relying on *White v. White*, 26 Cal. App. 2d 524, 79 P.2d 759 (1933), for the proposition that any gifts made by the husband would be presumed to have been made out of his own separate property. Respondent's Brief, p. 23, Respondent's Answer to Appellants' Petition for a Hearing by the Supreme Court, pp. 20-23. *Neilson* thus clearly presented the clash between *Van Camp* and *Pereira*, and it is unfortunate that the situation was not used to elaborate further on the application of these diverse approaches.

²⁷⁴ The holding in *Pereira* was restricted to what the minimum amount of separate property would be. See note 160 *supra* and accompanying text. This was apparently realized in *Estate of McCarthy*, 127 Cal. App. 80, 15 P.2d 223 (1932), where the court stated:

In determining what portion of such profits is community property, while it must be presumed in the absence of evidence that some thereof were due to the capital

from one reached upon application of *Pereira*.²⁷⁵ As the *Gilmore*²⁷⁶ case shows, courts applying the *Van Camp* method are prone to accept the testimony of the husband or his accountant that his salary accurately reflects his value to the business. Similarly, the *Huber*²⁷⁷ court limited the community to the amount testified to by the husband's accountant as being reasonable compensation for his services, even though the husband had drawn twice that amount from the business.²⁷⁸ Perhaps the courts give controlling weight to this testimony of the husband because the *Van Camp* approach does not produce other evidence for the courts to consider. As a practical matter, an application of *Van Camp* cannot give effect to the basic presumption that all property acquired during marriage is community²⁷⁹ and still produce enough evidence for the trier of fact to make an accurate determination. The basic presumption places the risk of nonpersuasion as well as the burden of going forward upon the party who is asserting that the property is separate.²⁸⁰

invested, and would equal at least the usual interest on a long term investment well secured, yet if the husband claims that his capital was entitled to a greater return than legal interest the burden of showing the fact rests upon him.

Id. at 86, 15 P.2d at 225. However, *Pereira* was soon interpreted as holding that the entire separate property interest was to be determined by affixing the rate of return indicated above. See text following note 149 *supra*; *Randolph v. Randolph*, 118 Cal. App. 2d 584, 587, 258 P.2d 547, 549 (1953), where the court states:

The usual method of determining the value of a husband's interest in a business in which he works and in which he also uses his separate property is to allow the husband the amount so invested by him with interest at the usual rate for well secured investments; profits or accruals in excess of that amount are then considered community property as attributable to the husband's personal labor, ability, energy and character [citing *Pereira*].

Pereira v. Pereira may thus be viewed in more than one aspect. Aside from the actual holding of the case, the courts have come to take *Pereira* as a method for solving apportionment problems. Furthermore, the method itself may be taken as setting forth an approach that requires the initial allocation to be made to the separate estate, and a subsequent allocation of any remainder to the community. See text following note 292 *infra*.

As regards the use of *Pereira* as a method, in conjunction with the *Van Camp* approach, see *Margolis v. Margolis*, 115 Cal. App. 2d 131, 251 P.2d 396 (1952), where the court awarded Mr. Margolis a 6% return on his capital as the sole separate property investment, stating that "the court did not arbitrarily or unfairly determine that his assets held in 1950, less that part attributable to his managerial skills, were then his separate estate." *Id.* at 137, 251 P.2d at 400.

²⁷⁵ See note 216 *supra*, for a typical example.

²⁷⁶ *Gilmore v. Gilmore*, 45 Cal. 2d 142, 287 P.2d 769 (1955).

²⁷⁷ *Huber v. Huber*, 27 Cal. 2d 784, 167 P.2d 708 (1946).

²⁷⁸ See text accompanying note 197 *supra*.

²⁷⁹ CAL. CIV. CODE § 687. Although the statute was not enacted until 1872, this presumption was recognized early in California. *Smith v. Smith*, 12 Cal. 216, 224 (1859); *Meyer v. Kinzer*, 12 Cal. 247, 252-54 (1859); LEVITT, *THE LAW OF COMMUNITY PROPERTY* 59 (1950). The presumption was recognized earlier by implication in *Alverson v. Jones*, 10 Cal. 9 (1858); *Bessie v. Earle*, 4 Cal. 200 (1854); 1 ARMSTRONG 441; see CONMY, *THE HISTORIC SPANISH ORIGIN OF CALIFORNIA'S COMMUNITY PROPERTY LAW* 14 (1957).

²⁸⁰ Because the courts have used the term to describe two separate and distinct burdens, the words "burden of proof" have been eliminated by the *Model Code of Evidence*, and two new terms, "burden of persuasion of a fact" and "burden of producing evidence of a fact," have been adopted. MODEL CODE OF EVIDENCE rule 1(2)-(3), comment at 73-74 (1942); see 9 WIGMORE, EVIDENCE §§ 2485, 2487 (3d ed. 1940). See also Morgan, *Some Observations Concerning Presumptions*, 44 HARV. L. REV. 906, 927-28 (1931). In the text herein the term "burden of going forward" is used to describe "burden of producing evidence of a fact" and the term "risk of nonpersuasion," see 9 WIGMORE, EVIDENCE § 2485 (3d ed. 1940), is used to describe the "burden of persuasion of a fact."

If, however, this risk is to be placed on the husband under the *Van Camp* method, he could meet his burden of going forward by having his accountant testify as to the reasonable value of his services. Because *Van Camp* defines the issue in terms of valuing the husband's skill, this would be direct evidence on the issue, and may strongly influence a decision in the husband's favor, particularly in the absence of any further evidence. The husband's evidence should not, however, negate the basic presumption favoring the community, and the wife should be able to win without introducing any evidence. Nevertheless, the courts usually give controlling weight to the husband's evidence under the *Van Camp* method.²⁸¹ The wife is, in effect, forced either to come forth with additional evidence tending to limit the return on the separate investment, or to gamble that the husband's evidence will not be conclusive.

The foregoing analysis may not be consistent with a part of the *Neilson* opinion wherein Justice Traynor states:

The proceeds and increment in value are apportioned entirely to the husband's estate only when they are attributable solely to the natural enhancement of the property . . . or when the husband expended only minimal effort and the wife introduced no evidence attributing a value to his services.²⁸²

But, the last twelve words of this passage are inconsistent with another part of the opinion in which it is said to be incumbent upon the owner of a business to prove that it is making a higher rate of return than the usual interest rate.²⁸³ Justice Traynor thus seems to acknowledge that some burden rests on the party who is asserting that the property is separate.²⁸⁴ While the husband may introduce evidence that a higher return is justified, this should not place a burden of persuasion on the wife to establish what portion of the profits are community property. The quoted language should be taken to mean only that the establishment of certain facts by the husband shifts the burden of going forward to the wife, and not the burden of persuasion. However, *Cozzi v. Cozzi*²⁸⁵ and *Estate of Barnes*,²⁸⁶ the two cases *Neilson* relies on for this language, held that the wife must bear the risk of proving that some part of the profits were community. Neither *Cozzi* nor *Barnes* considered the presumption that all property acquired after marriage is community.

Because *Pereira* as the usual method requires the husband to prove any greater than normal value of his capital, the basic presumption of community property can be more readily adhered to. Evidence as to the value of the husband's services does not now go directly to the issue, and is less likely to be taken by the courts as conclusive. Thus, under *Pereira*, the husband is induced to come forth with more evidence, and is required to prove with greater particularity the value of his

²⁸¹ See text following note 276 *supra*.

²⁸² 57 Cal. 2d at 740, 22 Cal. Rptr. at 5. (Emphasis added.)

²⁸³ In *Neilson*, Justice Traynor stated that, "Departures from the *Pereira* formula have been made when the husband introduced evidence that 'a larger return on his capital had in fact been realized.'" 57 Cal. 2d at 740, 22 Cal. Rptr. at 5, citing *Gilmore v. Gilmore*, 45 Cal. 2d 142, 150, 287 P.2d 769, 774 (1955).

²⁸⁴ With *Pereira* being the usual method under *Neilson*, the husband, notwithstanding any evidentiary burden, may get some return on his separate investment even without introducing any evidence. But see text following note 292 *infra*. The burden possibly placed on the husband by *Neilson* relates only to his receiving a larger than usual return. See note 283 *supra*.

²⁸⁵ 81 Cal. App. 2d 229, 183 P.2d 739 (1947).

²⁸⁶ 128 Cal. App. 489, 17 P.2d 1046 (1932).

separate estate in the production of the income.²⁸⁷

Difficulties may arise from the use of *Pereira* as the usual method unless previous limitations in its application are eliminated. Some cases have used the original language of *Pereira* and determined that the "usual interest on a long investment well secured" should be allocated to the separate property.²⁸⁸ Other decisions have determined that the *Pereira* method consists of allowing the legal interest rate.²⁸⁹ Neither of these two rates is very closely related to practical reality. The use of the rate on a well secured investment does not give consideration to the risk factor, which is of primary importance in determining the return on any investment.²⁹⁰ The separate capital in the husband's business is an equity investment rather than a loan, and is unsecured rather than "well secured."²⁹¹ Similarly, the use of the legal interest rate ignores the possibility that the husband may have made a better or worse than average investment. It would seem that the amount to be attributed to the separate investment should be the usual rate of return on investments in similar enterprises operating in generally the same environment.

The relatively narrow and limited interpretation given to the *Pereira* approach in the past has worked injustice in two respects. Where a large sum of money is in dispute, allocation to the separate estate of a conservative rate of return does not adequately reward the investment, and the community gets more than a reasonable value for the spouse's efforts. On the other hand, where the business has been only a marginally successful or losing investment, the community suffers. These problems arise because the difference between *Pereira* and *Van Camp* has been taken as bearing upon which interest, the separate estate or the community, is to be credited or paid first. It was thought that the *Van Camp* method called for subtracting the community interest first, with the remainder being considered separate property.²⁹² *Pereira* was taken to require the separate estate to be credited first, with anything remaining being allocated to the community.²⁹³ Under this

²⁸⁷ The *Neilson* decision does not, however, make clear how such evidence is to be used. See note 273 and text following note 269 *supra*. The evidence produced may require a switch to the *Van Camp* approach, see text at note 270 *supra*, or may be used only to modify the return to be given the separate investment while staying within the framework of *Pereira*, see text following notes 271 *supra* and 301 *infra*.

Further reasons may also suggest preference for the *Pereira* approach. An apportionment in terms of the fair rate of return on the separate capital may be more suitable for an accurate determination, since there are usually businesses similarly situated that can be used as guides in establishing the share attributable to the capital. Also, evidence is available as to the earning value of various types of invested funds. See DUN & BRADSTREET, INC., HOW DOES YOUR BUSINESS COMPARE WITH OTHERS IN YOUR LINE? (1960); 13 MAIL-ME-MONDAY BAROMETER OF SMALL BUSINESS, YEARBOOK (1961). In comparison, figures on which to value the husband's efforts would not seem as accurate. The skill and abilities required to operate a business are numerous and varied, and aside from the case of ministerial positions different people can rarely be said to possess the same degree of capability. See note 323 *infra*. Even the value of the husband's ability as measured by job offers or previous employment may have little bearing on his value to the particular business in question. See note 324 *infra*.

²⁸⁸ See, e.g., *Stice v. Stice*, 81 Cal. App. 2d 792, 185 P.2d 402 (1947).

²⁸⁹ See, e.g., *Tassi v. Tassi*, 160 Cal. App. 2d 680, 325 P.2d 872 (1958).

²⁹⁰ See 1 CALIFORNIA FAMILY LAWYER § 4.23, at 115 (Cont. Ed. Bar 1961).

²⁹¹ *Ibid*.

²⁹² See 4 WITKIN, SUMMARY OF CALIFORNIA LAW *Community Property* § 19, at 2726-27 (7th ed. 1960).

²⁹³ See Evans, *Primary Sources of Acquisition of Community Property*, 10 CALIF. L. REV. 271, 282 (1922).

latter interpretation of *Pereira*, in a marginally successful or losing business where the entire profit is about the same or less than the arbitrary return given on the investment, there would be little or nothing left for the community after payment to the separate estate.²⁹⁴ The *Pereira* case clearly did not intend such a result. This was shown in *Estate of Gold*,²⁹⁵ where Justice Shaw, who also wrote the *Pereira* opinion, interpreted it as holding that "whatever accrues from the personal activity, ability, and capacity of the husband is community property and the remaining profits must be classed as separate estate."²⁹⁶ Fundamental accounting and good business practice would seem to uphold this language in *Gold*, since labor expenses must be first satisfied before any profit or return on capital can be declared.²⁹⁷ If the husband had chosen not to run the business himself, he would have had to pay wages to a manager before any profit was realized on his separate investment.²⁹⁸ Therefore, in view of *Gold*, the *Pereira* method should not be used to give an arbitrary return to the separate estate to the detriment of the community interest.²⁹⁹ Similarly, there appears to be no reason why it should act arbitrarily to the detriment of the separate investment when a large rather than small sum is in dispute.

In *Neilson*, Justice Traynor seemed to recognize the inadequacy of using either the legal interest rate or the rate on a long-term investment, as he stated the *Pereira* rule as calling for a "fair rate of return."³⁰⁰ If this language is taken literally, rather than being understood as calling for one of the rates used in past cases, a proper result could be reached. Evidence relating to the value of the husband's services, the returns on similar business investments, as well as the several factors set forth in *Neilson*, could be used to determine what rate of return would be the "fair" value of the capital. If this were done, and the husband was actually given

A logical basis for the framework would seem to be the basic presumption that

²⁹⁴ See *McDuff v. McDuff*, 48 Cal. App. 175, 191 Pac. 957 (1920). See also Note, 14 CALIF. L. REV. 402, 404 nn.16-17 (1926); Evans, *Primary Sources of Acquisition of Community Property*, 10 CALIF. L. REV. 271, 282 (1922).

Courts using the *Van Camp* method often conclude that no community property exists by holding that where the expenses are greater than the income, the community has earned nothing. See, e.g., *Huber v. Huber*, 27 Cal. 2d 784, 167 P.2d 708 (1946). The rationale for this holding is a presumption that all expenses were paid out of community property. *Kenney v. Kenney*, 128 Cal. App. 2d 128, 274 P.2d 951 (1954); see *Estate of Ades*, 81 Cal. App. 2d 334, 184 P.2d 1 (1947). This presumption has arisen out of the statement in *Estate of Cudworth*, 133 Cal. 462, 65 Pac. 1041 (1901), that there is no presumption that the husband paid the expenses out of his own separate property. It would seem that saying there is no presumption debts are paid out of separate property is not support for a finding that there is a presumption that such debts were paid from community funds. See Respondant's Brief, p. 290, *Van Camp v. Van Camp*, 53 Cal. App. 17, 199 Pac. 885 (1921).

²⁹⁵ 170 Cal. 621, 151 Pac. 12 (1915).

²⁹⁶ *Id.* at 623, 151 Pac. at 13. (Emphasis added.)

²⁹⁷ See *BALLETINE, CORPORATIONS* §§ 245-50 (1946); *LATTIN, CORPORATIONS* 467-72 (1959); cf. *MCLAUGHLIN, BANKRUPTCY* § 152 (1956). See also *MECHEM, AGENCY* §§ 543-51 (4th ed. 1952).

²⁹⁸ Comment, 14 CALIF. L. REV. 402, 404 n.17 (1926).

²⁹⁹ Moreover, since the community must bear the loss of any debts contracted by the husband if his business is losing money, see *Schuyler v. Broughton*, 70 Cal. 282, 11 Pac. 719 (1886), it would appear just that the separate property bear the expense of paying for the services of the husband. See Evans, *Primary Sources of Acquisition of Community Property*, 10 CALIF. L. REV. 271, 282-83 (1922); Comment, 14 CALIF. L. REV. 402 (1926).

³⁰⁰ "The usual method of apportionment is to allocate a fair return on the investment to the separate property. . . ." *Estate of Neilson*, 57 Cal. 2d 733, 740, 22 Cal. Rptr. 1, 5 (1962).

a fair return, it would then not matter which interest was subtracted first. It would appear that this is the only way an apportionment can be made under the *Pereira* approach while adhering to its correct interpretation as stated in *Gold*.³⁰¹

Any problems remaining after the *Neilson* decision will exist because two basically conflicting methods of apportionment continue to be used. By setting up *Pereira* as the usual method, *Neilson* may have provided the groundwork for resolving this conflict. Nevertheless, the failure to indicate when and if *Pereira* must yield to *Van Camp* leaves room for the confusion of the past to project itself into the future. If a satisfactory method of apportionment is to be established, it must at least be recognized that past cases have been decided along two separate lines of analysis. A choice can then be made as to which is more suitable, or perhaps a decision can be made to establish another approach not bound up with any of the previous approaches.

IV

A SUGGESTED SOLUTION

A. Evidentiary and Procedural Framework

The problems of apportionment cases may vary with the size and nature of the business, the extent of the spouses' participation, the business climate, and other factors. Since no rigid formula could do justice in every fact situation, a more reasonable approach would seem to consist of a broad framework within which the various facts all may be considered. This framework should determine the issue presented, the party having the burden of proof, and the type of evidence to be considered.³⁰²

³⁰¹ See text at note 296 *supra*.

³⁰² Although the *Neilson* decision and much of the discussion following hereinafter are written in terms of a business belonging to and operated by the husband, it should be clear that the principles discussed are equally applicable to cases involving a separate property business owned and operated by the wife. While there are cases holding that a husband allowing his wife to run her own business makes an implied gift of her earnings by allowing her to control them, *Diefendorff v. Hopkins*, 95 Cal. 343, 30 Pac. 549 (1892); *Smith v. Smith*, 47 Cal. App. 650, 191 Pac. 60 (1920), this result probably would not apply after 1951 as the wife now is given the right to control and manage the "community property money earned by her," in CAL. CRV. CODE § 171c. Two other situations to be treated similarly to the two already mentioned are where the husband operates the wife's separate business, and where the wife operates the husband's business. In *Lewis v. Johns*, 24 Cal. 98 (1864), an early case involving a business owned by the wife but run by the husband, the principle was established that a husband could obtain no interest in the property of the wife by any act of his own. See *Lencioni v. Fidelity Trust & Sav. Bank*, 95 Cal. App. 490, 273 Pac. 103 (1928); *Gray v. Perlis*, 76 Cal. App. 511, 245 Pac. 221 (1926). But see *Pacific-Southwest Trust & Sav. Bank v. Ross*, 81 Cal. App. 204, 253 Pac. 351 (1927). This principle was probably founded on the same reasoning that motivated the court in *George v. Ransom*. See notes 42 and 44 *supra*. It would seem clear at present, however, that the earnings attributable to the husband's skill are community property, regardless of whether they are earned by operating his separate property business or that of his wife. But, where it appears that the husband worked in the wife's business without expecting any compensation, it would be proper to hold that the husband had made a gift of his services to the wife. *Gray v. Perlis*, 76 Cal. App. 511, 245 Pac. 221 (1926). This conclusion is supported by the fact that the husband has control of the community assets, CAL. CRV. CODE §§ 172, 172a, which include the value of his own skill and labor. Under the provisions of CAL. CRV. CODE § 171c, it would seem that the wife similarly could make a gift of her services to her husband's separate business.

all property obtained during marriage is community property.³⁰³ This presumption is fundamental to the community property system, and was a part of the system as it existed under early Spanish law.³⁰⁴ When applied to apportionment, the presumption should place on the owner of the separate property both the burden of persuasion³⁰⁵ and of going forward³⁰⁶ to show what portion of the profits are not to be allocated to the community.

The use of the basic presumption in cases involving the classification of profits from a separate property business has been considered previously.³⁰⁷ But the courts have not followed through with a sound application of the presumption, and often have confused it.³⁰⁸ In *Estate of Pepper*, although the court's analysis began with

³⁰³ See note 279 *supra*.

³⁰⁴ *Wilson v. Wilson*, 76 Cal. App.2d 119, 172 P.2d 568 (1946). The presumption is said to be founded upon the likelihood that any property acquired by a spouse during marriage would be community property. 1 *DEFUNIAK* § 60, at 140. The presumption is also based on the greater precision with which separate property is defined. *Horne, Community Property—A Functional Approach*, 24 So. CAL. L. REV. 42, 52 (1950). See also *Evans, The Ownership of Community Property*, 35 HARV. L. REV. 47 (1921). One purpose of the presumption is that it resolves doubts in favor of the community as against questionable claims of separate ownership by third parties and individual spouses. *ROBBINS, COMMUNITY PROPERTY LAWS* 16 (1940); see *CLARK, COMMUNITY OF PROPERTY AND THE FAMILY IN NEW MEXICO* 20 (1956).

³⁰⁵ *Myer v. Kinzer*, 12 Cal. 247, 252-54 (1859); *Falk v. Falk*, 48 Cal. App.2d 762, 120 P.2d 714 (1941); *BALLINGER* § 43; *Mechem, Progress of the Law in Washington Community Property*, 7 WASH. L. REV. 367, 370 (1933); *Pomeroy, Community Property*, 4 WEST COAST RPTR. 357, 358 (1884); Note, 4 TEXAS L. REV. 362 (1926); see *Fennell v. Drinkhouse*, 131 Cal. 447, 63 Pac. 734 (1901); *Estate of Boody*, 113 Cal. 682, 45 Pac. 858 (1896); *Wynn v. Wynn*, 170 Cal. App.2d 484, 338 P.2d 930 (1959); *Kenney v. Kenney*, 128 Cal. App.2d 128, 274 P.2d 951 (1954); 1 *DEFUNIAK* § 60, at 140-41. But see *Lenninger v. Lenninger*, 167 Cal. 297, 139 Pac. 679 (1914).

Insofar as the presumption fixes the burden of persuasion it is more accurately stated as a law determining the character of property than as a rule of evidence. *Nilson v. Sarment*, 153 Cal. 524, 96 Pac. 315 (1908); *Jordan v. Fay*, 98 Cal. 264, 33 Pac. 95 (1893); *McFadden v. Commissioner*, 148 F.2d 570 (5th Cir. 1945); *McKAY, COMMUNITY PROPERTY* § 256 (1st ed. 1910); see *Clark, Presumptions in New Mexico Community Property Law: The California Influence*, 25 So. CAL. L. REV. 149, 163 (1952). See generally 1 *DEFUNIAK* § 60. The basic presumption should be given added force by the California doctrine that presumptions themselves are to be treated as evidence. 1 *JONES, EVIDENCE* § 117 (5th ed. 1958); 2 *STANBURY, CALIFORNIA TRIAL AND APPELLATE PRACTICE* § 1024 (1958); see *Jolly v. Rea*, 196 Cal. 547, 238 Pac. 353 (1925); cf. *Thompson v. Davis*, 172 Cal. 491, 157 Pac. 595 (1916). See generally 9 *WIGMORE, EVIDENCE* § 2490 (3d ed. 1940).

³⁰⁶ See *Ganong, Community Property and Presumptions*, 28 ORE. L. REV. 157, 170 (1949). See also *THAYER, EVIDENCE AT THE COMMON LAW* 339 (1898); 9 *WIGMORE, EVIDENCE* § 2490 (3d ed. 1940); *MODEL CODE OF EVIDENCE* 309-11 (1942). See generally *Morgan, Presumptions*, 12 WASH. L. REV. 255, 259-66 (1937).

³⁰⁷ In *Lake v. Bender*, 18 Nev. 361, 384 (1884), where the entire profit was found to belong to the husband's separate estate, the court stated: "It is conceded that property acquired during coverture presumably belongs to the community. The burden is on the defendant [husband] in this case to overthrow this presumption, by proof sufficiently clear and satisfactory, to convince the court and jury of the correctness of his claim, as in other cases."

³⁰⁸ It has been held that the presumption could be overcome only by "clear and convincing" evidence. *Bauer v. Garrett*, 79 Cal. 304, 21 Pac. 759 (1889); *Thomasset v. Thomasset*, 122 Cal. App.2d 116, 264 P.2d 626 (1953); *McBAIN, CALIFORNIA EVIDENCE MANUAL* § 1294 (2d ed. 1960); *PLATT, PROPERTY RIGHTS OF MARRIED WOMEN* § 14, at 19 (1885), but that "absolute certainty" was not required, *Estate of Pepper*, 153 Cal. 619, 112 Pac. 62 (1910); *Wirz v. Wirz*, 96 Cal. App.2d 171, 214 P.2d 839 (1950). Such language should be taken to mean only that the presumption must be overcome by a preponderance of the evidence. *Simonton v. Los Angeles Trust & Sav. Bank*, 205 Cal. 252, 270 Pac. 672 (1928); *Freeze v. Hibernia Sav. & Loan Soc'y*, 139 Cal. 392, 73 Pac. 172 (1903); *Wirz v. Wirz*, 96 Cal. App.2d 171,

the presumption, once the husband traced the property to his separately owned business, the court held that the presumption was rebutted completely.³⁰⁹ The soundness of such analysis is questionable. The fact that the husband traces the property to income from his separate investment should not, by itself, overcome the presumption and thereby place the burden of persuasion on the wife who is asserting the property to be separate.

To illustrate a more logical application of the basic presumption, it is useful to view the various steps of proof that are considered in a trial. Initially, the party asserting that the property belongs to the community must establish that the property was acquired after marriage,³¹⁰ since there is no presumption to this effect regarding property held by a married person.³¹¹ With this much shown, however, the entire value of the property should be presumed to belong to the community.³¹² If it is further established that the property was derived from a separate investment, the property, in the absence of a showing of labor contributions of a spouse, all should be considered separate under the rule of *George v. Ransom*.³¹³ However, if it also is shown that one of the spouses has contributed his efforts to operating the business, the basic presumption should subsist, thereby leaving the burden of persuasion on the party asserting the property to be separate. The use of the presumption in this manner is supported by the community property doctrine relating to commingled funds,³¹⁴ since the property in dispute derives from a commingling of the profits of the separate capital with the value of the community owned

214 P.2d 839 (1950); *Estate of Moramarco*, 86 Cal. App. 2d 326, 194 P.2d 740 (1948) (degree of proof which produces conviction in an unprejudiced mind); *Wilson v. Wilson*, 76 Cal. App. 2d 119, 172 P.2d 568 (1946); cf. *Gibson v. Gibson*, 126 Cal. App. 2d 534, 272 P.2d 807 (1954). See generally 1 DEFUNIAK § 60.

³⁰⁹ *Estate of Pepper*, 158 Cal. 619, 622-23, 112 Pac. 62, 63-64 (1910).

³¹⁰ In a divorce case the community property becomes an issue if the plaintiff lists in the complaint the property that is contended to belong to the community. 2 WITKIN, CALIFORNIA PROCEDURE § 457 (1954); see 2 CHADBOURN, GROSSMAN, & VAN ALSTYNE, CALIFORNIA PLEADING § 1042 (1961).

³¹¹ *Fidelity & Cas. Co. v. Mahoney*, 71 Cal. App. 2d 65, 161 P.2d 944 (1945). But cf. *Jolly v. Rea*, 196 Cal. 547, 555, 238 Pac. 353, 356 (1925), where the court stated that any property existing "at the close of a long marital relation" is presumed to be community property. There were, however, inferences to support a finding that the property was acquired after marriage.

³¹² See VERRALL, CASES AND MATERIALS ON CALIFORNIA COMMUNITY PROPERTY 118-19 (1960); see *Austin v. Austin*, 190 Cal. App. 2d 45, 11 Cal. Rptr. 593 (1961). See also *Kenney v. Kenney*, 128 Cal. App. 2d 128, 274 P.2d 951 (1954).

³¹³ 15 Cal. 322 (1860); VERRALL, CASES AND MATERIALS ON CALIFORNIA COMMUNITY PROPERTY 118 (1960); see *Gudelj v. Gudelj*, 41 Cal. 2d 202, 210, 259 P.2d 656, 661 (1953). See *Estate of Boody*, 119 Cal. 402, 51 Pac. 634 (1897), where the court stated that the presumption of community property is rebutted and overcome by proof that the property was acquired by the ordinary use of his separate property.

³¹⁴ In community property states, a presumption exists that a commingled fund belongs entirely to the community. 1 DEFUNIAK § 61. If a portion of the fund can be traced to separate property, it will be characterized as separate property. *Belmont v. Belmont*, 188 Cal. App. 2d 33, 10 Cal. Rptr. 227 (1961); *Garten v. Garten*, 140 Cal. App. 2d 489, 295 P.2d 23 (1956); *Kenney v. Kenney*, 128 Cal. App. 2d 128, 274 P.2d 951 (1954); see *Wynn v. Wynn*, 170 Cal. App. 2d 484, 338 P.2d 930 (1959). But where the fund cannot be traced it is all conclusively presumed to be community property. *Falk v. Falk*, 48 Cal. App. 2d 762, 120 P.2d 714 (1941). This presumption can also only be overcome by a preponderance of the evidence. See *Gibson v. Gibson*, 126 Cal. App. 2d 534, 272 P.2d 807 (1954).

labor.³¹⁵ Also, it has been held that profits from a separately owned business are all community property unless the separate investment was shown to be a factor in producing the income.³¹⁶

Under the foregoing framework the issue is clearly defined to be the determination of the portion of the profits attributable to the separate investment. The burden of persuasion rests on the party asserting some portion to be separate, and failure to carry this burden results in the whole amount being allocated to the community. This approach is not particularly harsh on the spouse owning the separate business, however, since he still is entitled to whatever portion of the profits the evidence supports as being attributable to the separate investment. Moreover, the burden of producing evidence³¹⁷ is placed on the party most able to do so,³¹⁸ since the owner of the business should be in the best position to establish those factors important in evaluating his investment.

Unlike the *Van Camp* approach, consideration of the evidence would not be limited to a narrow factual determination.³¹⁹ Various types of evidence could be considered, with each bearing on the issue for whatever weight it might carry. For example, evidence of profits in similar industries could be shown.³²⁰ Goodwill shown to have been established by the owner of the separate business before marriage could be considered as a part of the capital investment.³²¹ Direct evidence may be introduced regarding the value of the spouse's services to the business,³²²

³¹⁵ The California Supreme Court considered the profit from a separate property business as a commingled fund before the turn of the century. *Estate of Bauer*, 79 Cal. 304, 21 Pac. 759 (1889); see *Estate of Fellows*, 106 Cal. App. 681, 289 Pac. 887 (1930).

³¹⁶ *Austin v. Austin*, 190 Cal. App. 2d 45, 11 Cal. Rptr. 593 (1961); accord, *Estate of Fellows*, 106 Cal. App. 681, 289 Pac. 887 (1930); cf. *Estate of Gold*, 170 Cal. 622, 151 Pac. 12 (1915).

³¹⁷ See note 306 *supra*.

³¹⁸ See *Wilson v. Wilson*, 76 Cal. App. 2d 119, 172 P.2d 568 (1946); McKAY, *COMMUNITY PROPERTY* § 210 (2d ed. 1925); Ganong, *Community Property and Presumptions*, 28 ORE. L. REV. 157, 167 (1949). This is one of the recognized reasons for the existence of presumptions, MORGAN & MAGUIRE, *CASES AND MATERIALS ON EVIDENCE* 88-90 (2d ed. 1942); see MCCORMICK, *EVIDENCE* § 309, at 643 (1954); cf. MAGUIRE, *EVIDENCE OF GUILT* 100 n.9 (1959); PROSSER, *TORTS* § 42, at 209-10 (2d ed. 1955). See also *Ramsdell v. Fuller*, 28 Cal. 37 (1865). See generally Morgan, *Techniques in the Use of Presumptions*, 24 IOWA L. REV. 413, 416 (1939); Morgan, *Presumption*, 12 WASH. L. REV. 255, 257-59 (1937); Morgan, *Some Observations Concerning Presumptions*, 44 HARV. L. REV. 906, 924-31 (1931).

³¹⁹ See text following note 276 *supra*.

³²⁰ See note 287 *supra*.

³²¹ Where a spouse has operated his separate business prior to marriage, he owns not only the tangible capital assets of the business, but also the goodwill or earning potential he has established. But when a man enters marriage and brings with him a certain amount of previously acquired skill, the monetary returns obtained through the use of this skill belong to the community. In *Thomasset v. Thomasset*, 122 Cal. App. 2d 116, 264 P.2d 626 (1953), the husband, a lawyer, tried to establish that the earnings from his practice were due in part to the goodwill he had built up during the years prior to marriage. The husband argued for an apportionment of the income, even though he had to work to account for all of it. Apparently, the only evidence introduced by the husband to substantiate his theory consisted of salaries paid to attorneys employed by the county and city. The court ruled such evidence irrelevant, thus leaving nothing of the apportionment theory based on the husband's goodwill investment. It would seem, however, that relevant evidence could have been introduced concerning goodwill by showing, for example, how many of the husband's clients during marriage were established prior to marriage. Some reasonable percentage of the fees received from such clients could then be attributed to the goodwill, with this percentage being apportioned to the husband's separate estate.

³²² This would be the only type of evidence to be considered under the *Van Camp* approach. See text following note 276 *supra*.

which might include job offers made to the spouse during marriage or salaries earned in employment other than with the separate business. Testimony regarding the salary of other persons in similar job positions, or of the cost to hire another person to run the separate business, could also be considered.³²³ The size and nature of the business may also bear on the value of the spouse's efforts to the business.³²⁴ Evidence could be shown relating to the general business climate.³²⁵ Similarly, general rises in land values are relevant where there has been appreciation with little or no improvement to the land in question.³²⁶

As countering evidence in behalf of the community, it might be shown that the business was not capable of being run successfully without the owner-spouse's efforts.³²⁷ Also, evidence of the type described above could tend to minimize or eliminate any return on the investment, as for example a showing that the particular industry has not been profitable.

This suggested framework does not differ greatly from the apportionment method established by *Neilson*. Most significantly, if *Pereira* is the usual method it still is possible for the holder of the separate investment to gain some portion of the profits without introducing any evidence bearing on the issue of apportionment. He may be entitled to a fair return so long as the property in dispute is traced to the separate investment.³²⁸ In comparison, under the above analysis an apportionment to the separate property interest would be made only upon evidence supporting a finding that the separate investment was partially responsible for the profits. Without such evidence everything would be community property under the basic presumption. Nevertheless, depending on how the various factors set forth in *Neilson* are to be used in modifying *Pereira*,³²⁹ the *Neilson* approach may closely approximate results under the suggested framework. If such factors are used only to modify the "fair return" under *Pereira*, rather than switching to a *Van Camp* inquiry,³³⁰ the burden in effect is placed on the holder of the separate

³²³ This might be less reliable evidence because it would establish directly only the worth of the person whose salary is shown.

³²⁴ For example, while the spouse may have a yearly earning capacity of \$25,000 in relation to possible employment as a corporate executive, the value of his productive capacity to the separate business is likely to be a lesser figure where such business is a neighborhood grocery store which is not able to fully utilize the spouse's ability. This raises the issue of whether the community is entitled to the value of the husband's services determined apart from their value to the business in which the husband is working. Since the husband can choose the mode of living for the community, CAL. CIV. CODE § 103, he is able to choose to work in a position where he is less valuable to his employer than in another position, and this should hold true even if he chooses to work in his own separately owned business. This situation should be distinguished from that of a losing business, where the husband may be valuable to the business even though it is not realizing any overall profit. See text following note 330 *infra*.

³²⁵ See *Gilmore v. Gilmore*, 45 Cal. 2d 142, 287 P.2d 769 (1955).

³²⁶ See *Mayhood v. La Rosa*, 58 A.C. 510, 374 P.2d 805, 24 Cal. Rptr. 837 (1962); *Estate of Heltcel*, 200 Cal. App. 2d 398, 19 Cal. Rptr. 352 (1962).

³²⁷ If, for example, the husband's personal contact with consumers was necessary, this would indicate that the profits were dependent on his efforts. On the other hand, if the husband's duties were primarily ministerial, it would indicate that his duties could have been readily assumed by someone else.

³²⁸ This does not mean that the separate investinent always will be entitled to some return under the *Pereira* rule. In the case of the losing or marginally successful business, an apportionment to the separate estate might not be made if it would be to the detriment of the community. See text following note 292 *supra*.

³²⁹ See text following note 269 *supra*.

³³⁰ See text accompanying note 271 *supra*.

investment to show what portion of the profits are attributable to his investment. If *Pereira* is completely abandoned under *Neilson*, then the results are likely to differ more drastically from those of the suggested framework, much in the same manner as they would from a strictly *Pereira* analysis.

B. The Losing Business

A decrease in the value of a separate property business should be treated in generally the same way as an increase. The first impression in such cases, however, might be that the entire value of an investment that has declined is all separate property.³³¹ This notion is perhaps based on the misconception that the *Pereira* rule always entitles the capital to some rate of return. It has already been shown, however, that *Pereira* should not require allocation to the capital to the detriment of the community.³³² The community is entitled to the value of the spouse's efforts, and this is not altered when the service is rendered to a losing cause.

Suppose that *H* and *W*, after five years of marriage, are obtaining a divorce, and the only property in question is a business that *H* owned before marriage and continued to operate during the five year period. *W* has been employed elsewhere, and her earnings have been used for the general expenses of the family. At the time of marriage *H*'s business was valued at \$125,000, but at the end of the five years it is worth only \$100,000. *H* has taken no money out of the business in the five years. During the same period of time other similar businesses of about the same size and character have declined about forty per cent in value, so that a business valued at \$125,000 five years ago would now be worth \$75,000. During the marriage *H* had the opportunity to give up his position with the business and take another job at a salary of \$10,000 a year. Under these facts, *W* initially could argue that the business would be worth less than \$100,000 had it not been for *H* contributing his efforts, and that the community is therefore entitled to some portion of its value. This contention is supported by the showing of decrease in value of other businesses. Moreover, had *H* hired someone else in his place, the \$100,000 would be diminished at least by the salary paid to such other person.³³³

The foregoing might be said to force *H* to choose between taking another job or having his business lose its separate character. However, while it is true that *H* has the power to choose the mode of living during marriage,³³⁴ and to manage the community assets,³³⁵ his skill is an asset that belongs to the community,³³⁶ and the community is entitled to whatever value it reaps.³³⁷ *H* should not be able to deprive the community of the value of his skill used to keep his separate estate intact any more than he could otherwise improve his separate property with com-

³³¹ Since the impression was that the separate property was entitled to a reasonable interest return even if that consumed all the profits, see text following note 292 *supra*, where there was no profit at all it would follow from such reasoning that the community likewise gained no interest.

³³² See text following note 292 *supra*.

³³³ Note, 14 CALIF. L. REV. 402, 404 n.17 (1926). Estate of Cudworth, 133 Cal. 462, 65 Pac. 1041 (1901) (concurring opinion); see Pomeroy, *Husband's Separate Estate*, 4 WEST COAST RPTR. 193, 195 (1884).

³³⁴ CAL. CIV. CODE § 103; see *Vosburg v. Vosburg*, 136 Cal. 195, 68 Pac. 694 (1902); 1 ARMSTRONG 159.

³³⁵ CAL. CIV. CODE §§ 172, 172a; see 1 DEFUNIACK § 113, at 322; 3 VERNIER, AMERICAN FAMILY LAWS 218-19 (1935).

³³⁶ See note 143 *supra*.

³³⁷ 3 VERNIER, AMERICAN FAMILY LAWS 214 (1935).

munity funds.³³⁸ Similarly, just as *H* is not entitled to give away community property without receiving consideration,³³⁹ he should not be allowed to give his services to the business without having the community receive some compensation. No matter what apportionment theory is applied it is clear that the community should be entitled to some amount.

A variation of the foregoing hypothetical illustrates a situation wherein the community's interest in a losing business is even more apparent. Suppose that during the first two years of marriage the business grew to a value of \$200,000, while other similar businesses grew at some rate less than this. If the marriage were to be terminated at this point, the community would clearly have some interest in the successful business, which could be apportioned as suggested above. If, however, the divorce occurs three years later, at a time when *H*'s business has dropped to a value of \$100,000, while most other similar businesses have become bankrupt, how is the property to be apportioned? Does the community lose the interest it had in the business because the divorce, or perhaps the death of *H*, occurs at a time when the value of the business has dipped below the value at the time of marriage? It would seem clear that whatever community interest was created while the business was successful should in some manner continue until the time of the dissolution of the marriage.³⁴⁰ In deciding what the value of the community interest is, no single factor should be controlling. The cost of hiring someone in *H*'s place, the amount of job offers to *H*, and the general extent of decline in the industry should all be weighed.

The major change in applying the suggested framework to a losing business would have to be with regard to the initial burden of proof. Inasmuch as the business would not appear initially to be property acquired during marriage, it would not be readily subjected to the basic presumption of community property. Therefore, *W* would have to bear the burden of showing that *H*'s services had some value to the business. Once *W* has carried this burden, *H* should have to show what part of the business would have remained intact even had he not worked in it. He would clearly be in the best position to produce this type of evidence, and preserving the basic presumption to this extent would not seem unjustified once the wife has connected the husband's efforts to the business.

W could establish the significance of the husband's efforts by showing the much larger decline in other similar businesses. Evidence regarding the type of business, nature of *H*'s duties, and importance of capital could also be used in this respect.

³³⁸ *Dunn v. Mullan*, 211 Cal. 583, 296 Pac. 604 (1931); *Provost v. Provost*, 102 Cal. App. 775, 283 Pac. 842 (1929). See Comment, 50 CALIF. L. REV. 844 (1962).

³³⁹ CAL. CIV. CODE §§ 172, 172a; see *Union Mut. Life Ins. Co. v. Broderick*, 196 Cal. 497, 238 Pac. 1034 (1925).

³⁴⁰ As to valuation of the community's interest, it would seem too harsh to conclude that the community should not in some way bear part of the decline in the value of the business. If it is found that the community interest after the first two years was \$100,000, there would be nothing left for the separate estate at the end of the five year period if the community is not affected by the decline. Perhaps a better way to express the community's interest in the business would be to determine at the end of each year the proportion of the value of the husband's services in relation to the total value of the business. Such percentage could be established for each year that the husband does not withdraw a salary corresponding to the value of his services, with the community's percentage interest then being traced through the ensuing years in effect as an investment in the separate business. Thus, for example, if after the first two years the community has acquired a 50% interest in the business, the decline during the next three years would be shared half by the community. This is without considering any further interest acquired by the community for the value of *H*'s services during these three years.

Once *H*'s connection is shown, it could be presumed that the business would have declined in value at about the same rate as the other businesses, with the burden resting on *H* to prove that his separate estate is entitled to a greater valuation. He could show this, for example, by evidence of the comparative situation of his business in the industry before marriage. If he had built up goodwill prior to marriage, and his business was generally superior in the industry, it could be established that his business would not have dropped in accordance with others. To the extent that *H* proves his business to have a higher earning power than the general industry, the value of the business would be apportioned as separate property.

CONCLUSION

The problem of apportioning profits between the community and separate estates could be completely avoided by a constitutional amendment conforming to the original Act of 1850,³⁴¹ thereby overruling *George v. Ransom* and making the rents and profits of separate property all community property.³⁴² However, such reform does not appear forthcoming; therefore, a method for apportionment must be formulated by which the trial courts can proceed rationally to determine the conflicting interests.

It must be realized that the underlying presumption of the community property system is that whatever is earned or acquired by the spouses during marriage belongs to the community.³⁴³ The introduction of the common law influence in *George v. Ransom* admittedly has made a basic change in this system. If, however, this change is to result in situations where long years of marriage can terminate with no community property having been acquired,³⁴⁴ then the purpose of the community system will have been defeated.³⁴⁵ While it is perhaps easy to understand the deviations from community property law in the early years, the courts in recent times have shown a better understanding of the community property system. Nevertheless, the principles used today in attempting to deal with the complex problem of apportionment are the same ones that developed from the early misunderstanding of the community property system which gave rise to the problem. If a solution is to be found, it must result from a full understanding of the past and a realization that the early cases can no more furnish an answer to the problem than did the *George* decision in creating it.

While it might be best to depart from existing case law where necessary to design a new approach to apportionment based on fundamental principles of community property law, such development may not be readily expected. Nevertheless, if the present system is to be retained, it is hoped that rational guidelines will be established to prevent random application of the two arbitrary and divergent approaches to apportionment which still confront us.

Edwin S. Saul*

³⁴¹ The Act of April 17, 1850, Cal. Stats. 1850, ch. 103, § 9. See also Clark, *New Mexico Community Property Law; The Senate Interim Committee Report*, in CHARMATZ & DAGGETT, *COMPARATIVE STUDIES IN COMMUNITY PROPERTY* 81, 96-98 (1955).

³⁴² See text following note 37 *supra*.

³⁴³ See notes 279 and 304 *supra*.

³⁴⁴ See *Estate of Cudworth*, 133 Cal. 462, 469, 65 Pac. 1041, 1044 (1901) (concurring opinion).

³⁴⁵ See 1 DEFUNIAK § 72; Pomeroy, *Husband's Separate Estate*, 4 WEST COAST RPTR. 193, 195 (1884).

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