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FEDERAL INCOME TAX LIABILITY — EXCEPTION TO MARITAL BANKRUPTCY

Mrs. Draper had incurred unpaid federal income tax obligations prior to her marriage to Delmar Draper, and the Internal Revenue Service levied on one-half of Mrs. Draper's wages during marriage. The Drapers brought suit as a marital community to quiet title to the salary levied on to satisfy the wife's premarital obligation, contending that the wife's wages were community property and, therefore, not subject to satisfaction for the premarital debt. Defendant's motion to dismiss was sustained. *Held*: One-half of a spouse's wages, even though community property, can be levied on to satisfy a premarital federal income tax liability. *Draper v. United States*, 243 F. Supp. 563 (W.D. Wash. 1965).

The non-liability of community property for separate debts has long been the rule in Washington,¹ and is popularly designated as "marital bankruptcy." The question of a premarital income tax obligation had been previously considered by the same district court in *Stone v. United States*,² in which it was concluded that "marital bankruptcy" was an inherent characteristic of Washington community property law, and, consequently, the tax lien for the premarital obligation could not be satisfied from community property. The court in the principal case was presented with a conflict between the holding in *Stone* and considerations of public policy which support collectability of federal income taxes.

The court in the principal case accepted the ruling in *Stone* that federal courts should look to state law for determination of property rights.³ The court noted, however, that the Washington Supreme Court had created an exception to "marital bankruptcy," based on grounds of public policy, in allowing a former wife to collect alimony by garnishing the wages of her former husband, then remarried.⁴ Reasoning that collection of federal income taxes for the support of the nation was an equally strong public policy, the court in the principal case felt that the further exception to "marital bankruptcy"

¹ *E.g.*, *Katz v. Judd*, 108 Wash. 557, 185 Pac. 613 (1919); *Schramm v. Steele*, 97 Wash. 309, 166 Pac. 634 (1917); *Stockand v. Bartlett*, 4 Wash. 730, 31 Pac. 24 (1892); *Brotton v. Langert*, 1 Wash. 73, 23 Pac. 688 (1890).

² 225 F. Supp. 201 (W.D. Wash. 1963).

³ Compare *Yiatchos v. Yiatchos*, 376 U.S. 306 (1964), 40 WASH. L. REV. 358 (1965) (disposition of federal savings bonds, purchased with community funds, governed by federal law).

⁴ *Fisch v. Marler*, 1 Wn. 2d 698, 97 P.2d 147 (1939).

was justified. Although the court recognized that Washington may consider alimony an obligation created by judicial decree rather than a debt,⁵ it concluded that this distinction did not preclude holding the community property liable in the principal case. The court reasoned that a tax obligation was analogous to alimony, in that neither involved a voluntarily created debt but arose, rather, by operation of law. Consequently, the conclusion in *Stone* that the tax lien could not be levied on community property was rejected, and it was concluded that a federal tax obligation should be treated as an exception to "marital bankruptcy."

The court tried to fit the principal case into the exception to "marital bankruptcy," based upon public policy, which was created by the Washington court in *Fisch v. Marler*.⁶ In *Fisch*, the court had allowed a divorced wife to collect alimony from a former husband who had remarried. Thus, although *Fisch* was an exception to "marital bankruptcy," it was very narrow in scope. A policy reason for creating "marital bankruptcy" was to protect the family;⁷ however, there were *two* families involved in *Fisch*—the family of the dissolved marriage and the new family of the husband—and both required protection. The court in *Fisch* concluded that it was necessary to balance the prior claim of the first wife against the present claim of the second wife, in order to achieve an equitable result.⁸ While the court in the principal case recognized that the exception in *Fisch* was for support of the family, it argued that such policy was no more important than support of the nation. This argument may be valid in a general sense, but it goes beyond the narrow public policy exception necessitated by the compelling circumstances in *Fisch*.

Even the narrow exception granted in *Fisch* has been restricted by the Washington court. In *Stafford v. Stafford*⁹ the court had to decide

⁵ See *Stafford v. Stafford*, 18 Wn. 2d 775, 781, 140 P.2d 545, 548 (1943); *Haakenson v. Coldiron*, 190 Wash. 627, 629, 70 P.2d 294, 295 (1937).

⁶ 1 Wn. 2d 698, 97 P.2d 147 (1939).

⁷ BROCKELBANK, *COMMUNITY PROPERTY LAW OF IDAHO* 284 (1962); 1 DE FUNIAK, *PRINCIPLES OF COMMUNITY PROPERTY* 441 (1943).

⁸ 1 Wn. 2d 698, 716, 97 P.2d 147, 155 (1939):

Although the claim of the divorced wife upon the earnings of her former husband is a fixed and prior one, it is not in all cases to be enforced to the point of exhaustion of such earnings, for the present wife also has a claim thereon which is entitled to consideration. Upon a showing by the present wife of necessitous circumstances, particularly where there is a minor child or children of the husband's subsequent marriage, the court may make such adjustment and allocation of the husband's earnings as may appear to it to be just and equitable in the premises.

⁹ 10 Wn. 2d 649, 117 P.2d 753 (1941). (This case is to be distinguished from *Stafford v. Stafford*, 18 Wn. 2d 775, 140 P.2d 545 (1943), *supra* note 5.)

whether the award of a lump sum for alimony in a divorce decree created a lien upon real property subsequently purchased by a new marital community. The court in *Stafford* limited the holding in *Fisch* to community *personal* property, and did not allow the former wife to levy on the realty, even though the distinction between real and personal property had been generally abandoned in Washington.¹⁰ The use of this distinction in *Stafford* indicates a reluctance on the part of the Washington court to make additional exceptions to "marital bankruptcy."

In a footnote, the court in the principal case cited *Electrical Products Consolidated v. Clarke*¹¹—an unreported Washington superior court case—as additional authority for the existence of a "category" of exceptions based on public policy. In *Electrical Products*, the couple involved were divorced and then remarried. They contended that the "second" community was not liable for a community debt incurred during the "first" marriage. The court recognized that, if successful, this method could be used as a substitute for bankruptcy to free couples from their debts, and properly held the "second" community liable. The decision in *Electrical Products* does not provide authority for a "category" of exceptions based on public policy, as it is possible that the court had simply recognized that there was essentially only one marital community with a "dormant period" between the divorce and remarriage.¹² Thus, it cannot be said that there is a "category" of exceptions to "marital bankruptcy" based on public policy, but only a single limited exception that arose from special circumstances in an alimony case.

In a supplementary argument, the court in the principal case noted that Washington may consider alimony as an obligation created by judicial decree rather than as a debt. The court reasoned that, if this distinction was the basis of the alimony exception to "marital bankruptcy," then a federal tax obligation should be handled in a similar manner because it also was created by operation of law. The court concluded that obligations arising by operation of law are exceptions to "marital bankruptcy." There is some support for this position in Spanish community property law, which Washington has generally recognized and applied.¹³ Traditional Spanish law distinguished be-

¹⁰ See *Schramm v. Steele*, 97 Wash. 309, 166 Pac. 634 (1917); Cross, *Community Property Law in Washington*, 15 LA. L. REV. 640 (1955).

¹¹ 1 Seattle Bar Bulletin, No. 9, p. 4 (April 1958).

¹² *Ibid.*

¹³ 1 DE FUNIAK, *op. cit. supra* note 7, at 435 n.1.

tween separate contractual debts and separate obligations of law, and made an exception to the rule of "marital bankruptcy" for the latter. Professor De Funiak states that, under Spanish law, when the law imposed an obligation on only one spouse—as for taxes or criminal fines—that spouse's half share of the community property might be taken.¹⁴ However, with the exception of alimony, the Washington court has not made special exceptions to "marital bankruptcy" for obligations arising by operation of law. On the contrary, in *Bergman v. State*¹⁵ it was held that community property could not be levied on in satisfaction of a judgment for costs rendered in favor of the state in a criminal action against the husband. In so holding, the court in *Bergman* stated:

If costs be considered as a debt, or civil obligation, it was his debt, not that of the marital community. It arose out of a criminal prosecution in which the marital community was not legally concerned, and for the results of which it was not legally liable.¹⁶

In attaching one-half of the wife's wages, the court in the principal case apparently tried to reach the wife's share of the community property.¹⁷ However, community property is held indivisibly in Washington.¹⁸ The Washington court has held that, not only is the whole community property unavailable for satisfaction of a separate debt, but, in addition, the debtor's undivided half interest cannot be taken.¹⁹ Nor can the community property be involuntarily divided during the existence of the community.²⁰ Consequently, the one-half of the wife's wages awarded by the decision in the principal case to the government was not her "share," but rather that of the marital community. On dissolution of the community without a property settlement or award, the remaining community property would be held by the former spouses as tenants in common.²¹ But since half of the wife's "contribution" to the community had been taken by the government in satisfaction of her *separate* obligation, the result would be that the

¹⁴ *Id.* at 468-69.

¹⁵ 187 Wash. 622, 60 P.2d 699 (1936).

¹⁶ *Id.* at 628, 60 P.2d at 702.

¹⁷ This would be effective in jurisdictions in which the community property is liable for the antenuptial debts of the wife. See *Austin v. Crim*, 6 S.W.2d 348 (Tex. Comm. of App. 1928); CAL. CIVIL CODE § 167. *But see Forsythe v. Paschal*, 34 Ariz. 380, 271 Pac. 865 (1928). See generally 1 DE FUNIAK, *op. cit. supra* note 7, at 453-62.

¹⁸ *In re Coffey's Estate*, 195 Wash. 379, 382, 81 P.2d 283, 284 (1938); *Stockand v. Bartlett*, 4 Wash. 730, 31 Pac. 24 (1892). See 40 WASH. L. REV. 358, 360 (1965).

¹⁹ *Stockand v. Bartlett*, 4 Wash. 730, 31 Pac. 24 (1892). See also 1 DE FUNIAK, *op. cit. supra* note 7, at 448-49.

²⁰ See *Stockand v. Bartlett*, 4 Wash. 730, 731, 31 Pac. 24 (1892).

²¹ *Ambrose v. Moore*, 46 Wash. 463, 90 Pac. 588 (1907).

wife would end up receiving approximately three-quarters of her contribution to the community property. Although an adjustment might be made in the case of a divorce, there could be no adjustment if the community were terminated by death.²²

Implicit in the principal case is a questioning of the validity of "marital bankruptcy." There is considerable doubt whether "marital bankruptcy" is suited to modern society, and there have been informal proposals to eliminate the doctrine.²³ "Marital bankruptcy" originated in the Spanish community property law, in which it was considered that the well-being and interest of the family were superior to the rights of creditors.²⁴ Such a doctrine was appropriate for the social and economic environment in which the concepts of community property developed. The interest and well-being of the family are still significant, but the conditions that fostered "marital bankruptcy" may no longer be present. Government welfare machinery and private charities provide substantial protection against the consequences of failure to protect the family. In addition, doctrines that add instability and uncertainty to credit transactions in a credit-oriented economy are inconsistent with the nature of that economy. Although "marital bankruptcy" does not seem well-adapted to the contemporary society, the proper remedial device is not the creation of ill-defined, piecemeal exceptions, but rather correction through comprehensive statutory change.

TAXATION OF CORPORATE STOCK RECEIVED BY SOLE SHAREHOLDERS UPON CANCELLATION OF SALARY OBLIGATIONS

Randall and Fender, sole and equal shareholders of Fender Sales, Inc., twice cancelled equal salary debts owned to them by their corporation.¹ As part of these transactions, the corporation issued \$100 par value common stock for each \$100 of salary debt owed. Neither the

²² Compare WASH. REV. CODE § 26.08.110 (1958) (divorce), with WASH. REV. CODE § 11.04.050 (1956) (death).

²³ BROCKELBANK, *op. cit. supra* note 7, at 284-85; SPEER, *LAW OF MARITAL RIGHTS IN TEXAS* § 385 (3d ed. 1929); Cross, *supra* note 10, at 667; Cross, *Law Revision in Washington*, 27 WASH. L. REV. 193, 196 (1952).

²⁴ BROCKELBANK, *op. cit. supra* note 7, at 284; DE FUNIAK, *op. cit. supra* note 7, at 441.

¹ The transactions in question grew out of a suggestion by a bank-creditor of the corporation that its salary liabilities to Randall and Fender be capitalized in order to avoid potential priority over the bank's claim.