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The Community's Interest in Separate Corporate Stock: Jensen v. Jensen

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NOTE

THE COMMUNITY'S INTEREST IN SEPARATE CORPORATE STOCK: *JENSEN* *V. JENSEN*

IN the fall of 1974 Robert Jensen left his position at the *Dallas Times-Herald* to form his own printing company. In early 1975 Mr. Jensen purchased a subsidiary of the *Times-Herald*, renamed it RLJ Printing Company, and incorporated it soon thereafter.¹ Two months after incorporating the company Robert Jensen married Burlene Parks.² Five years later Mrs. Jensen sued for divorce. In dividing the property, the district court found the entire value of RLJ stock to be the separate property of Robert Jensen.³ Mrs. Jensen appealed,⁴ and the Tyler court of appeals

1. Mr. Jensen was the chairman of the board, president, and majority shareholder of the corporation, controlling approximately 51% of the shares of RLJ Printing Co., Inc.

2. Burlene Parks had been employed as an executive secretary at a maximum salary of \$14,400 per year.

3. *Jensen v. Jensen*, 629 S.W.2d 222, 224 (Tex. App.—Tyler 1983). The district court's findings of fact and conclusions of law were as follows:

FINDINGS OF FACT

1. The RLJ Printing Company, Inc. was created by Mr. Jensen before the marriage of the parties.
2. RLJ Printing Company, Inc. acquired the stock of Newspaper Enterprises, Inc., 64 days before the marriage of the parties in a unique business opportunity.
3. RLJ Printing Company, Inc. is not an alter ego of Mr. Jensen.
4. RLJ Printing Company, Inc. was not created in fraud of the rights of the community estate.
5. The salary paid Mr. Jensen has been adequate and reasonable.
6. The dividends paid Mr. Jensen have been adequate and reasonable.
7. The bonuses paid Mr. Jensen have been adequate and reasonable.
8. Mr. Jensen was the key man in the operation of RLJ Printing Company, Inc.
9. The successful operation of RLJ Printing Company, Inc. were primarily due to the time, toil, and effort of Mr. Jensen.

CONCLUSIONS OF LAW

1. The community was not the equitable owner of any shares of RLJ Printing Company, Inc.
2. The community was not entitled to receive the value of the appreciation in shares of RLJ Printing Company, Inc. that was due to the successful operations of the company.
3. The community was not entitled to receive the value of the appreciation in shares of RLJ Printing Company, Inc. that was due to the time, toil, and effort of Mr. Jensen.

Jensen v. Jensen, 27 Tex. Sup. Ct. J. 68, 69 (Nov. 9, 1983).

4. Mrs. Jensen appealed the findings and conclusions of law that the community was

reversed, holding that the increase in value of separate stock that occurs due to the time, toil, and effort of the members of the community is community property.⁵ Because of the mischaracterization by the district court, the court of appeals held that the district court had abused its discretion in dividing the property and remanded the case for proper division.⁶ The Texas Supreme Court granted Mr. Jensen's writ of error. *Held, reversed*: The increase in value of separately owned corporate stock is separate property, and the community is only entitled to reimbursement for the reasonable value of the time and effort of the spouse that contributed to the increase. *Jensen v. Jensen*, 27 Tex. Sup. Ct. J. 68 (Nov. 9, 1983).*

I. DEVELOPMENT OF THE LEGAL APPROACHES CONCERNING INCREASES IN VALUE OF SEPARATE PROPERTY

The Texas Constitution contains the basis of the Texas community property system.⁷ It provides that all property of a spouse either owned before marriage or received during marriage by gift or inheritance is the separate property of that spouse.⁸ The constitution also enables the legislature to pass laws further defining the property rights of spouses.⁹ Section 5.01 of the Texas Family Code reiterates the constitutional characterization of marital property¹⁰ and also characterizes as separate property damages recovered for personal injuries sustained by a spouse during marriage, except damages for loss of earning power.¹¹ Section 5.02 states that all property acquired by either spouse during marriage is presumed to be

not entitled to receive the value of the corporate stock's appreciation and that salaries and bonuses paid Mr. Jensen were adequate and reasonable.

5. 629 S.W.2d at 224. The case was transferred to the Tyler court from the Dallas court of appeals pursuant to docket equalization. Brief for Mr. Jensen at 15.

6. 629 S.W.2d at 226.

* Author's Note: On Feb. 29, 1984, after this issue went to press, the Texas Supreme Court granted Mrs. Jensen's motion for rehearing and withdrew its opinion of Nov. 9, 1983 (*Jensen II*); see *Jensen v. Jensen*, 27 Tex. Sup. Ct. J. 256 (Feb. 29, 1984). In this third opinion the court concluded, as in *Jensen II*, that reimbursement provides the only method of recovery for the increased value of separate corporate stock. The court found, contrary to its opinion in *Jensen II* (see *infra* text accompanying notes 90-94), that no evidence supported the trial court's finding that the community was adequately reimbursed. The court remanded the case to the trial court for that determination. Apparently, this holding shifted the dissenters in *Jensen II* to the majority, resulting in a 9-0 decision with Justice Robertson concurring. The fact that the supreme court has now decided *Jensen v. Jensen* three times illustrates the difficulty of determining how to treat the increase in value of separate corporate stock.

7. TEX. CONST. art. XVI, § 15. Texas community property law is based on and adheres strictly to the Spanish community property system. For a general discussion of the origin of the Texas community property system, see J. MCKNIGHT & W. REPPY, TEXAS MATRIMONIAL PROPERTY LAW 1-16 (1983); McKnight, *Texas Community Property Law—Its Course of Development and Reform*, 8 CAL. W.L. REV. 117 (1971), reprinted in ESSAYS IN THE LAW OF PROPERTY (Southern Methodist University School of Law 1975).

8. TEX. CONST. art. XVI, § 15.

9. *Id.* The constitution states "laws shall be passed more clearly defining the rights of the spouses . . ." *Id.*

10. TEX. FAM. CODE ANN. § 5.01(a)(1)-(2) (Vernon 1975).

11. *Id.* § 5.01(a)(3).

community property.¹²

When separate property increases in value during marriage, a difficult problem arises concerning treatment of the increase. Neither the Texas Family Code nor the Texas Constitution addresses this issue. Historically, Texas courts facing this problem have applied one of two theories of recovery, depending upon the source of the increase in value. When the value of separate property has increased due to the expenditure of community funds, Texas courts have typically applied an equitable theory of reimbursement for funds expended. If community labors have increased the separate property, then this increase belongs to the community under what is called an ownership theory. The application of the community ownership theory, however, has never been entirely consistent.

A. *The Community Ownership Approach*

In 1859 the Texas Supreme Court held in *De Blane v. Hugh Lynch & Co.*¹³ that the increase in value of separate property of one spouse that occurs due to the joint efforts of the husband and wife is community property.¹⁴ In that case the court ruled that crops grown on the wife's separate property were community property.¹⁵ Subsequent decisions firmly established the rule that profits derived from separate property due to time, toil, and efforts of the community is community property.¹⁶

The Texas Supreme Court modified this rule in 1953 in *Norris v. Vaughan*,¹⁷ holding that reasonable labor may be expended by a spouse in making his or her separate estate productive without impressing a community character upon the estate.¹⁸ *Norris* differed slightly from earlier community ownership cases in that it dealt not simply with profits earned from separate property, but with production from separate property.¹⁹ In *Norris* the property in dispute was the husband's one-fourth interest in several oil and gas leases. Producing gas wells were drilled on some of the leases

12. *Id.* § 5.02.

13. 23 Tex. 25 (1859).

14. *Id.* at 27.

15. *Id.* *But see* *Stringfellow v. Sorrells*, 82 Tex. 277, 18 S.W. 689 (1891). The *Stringfellow* court held that the increase in value of the wife's mules remained separate property. *Id.* at 279, 18 S.W. at 689. The court distinguished *De Blane*, stating that an increase in value under the *De Blane* rule would only occur if the mules produced offspring. *Id.* at 278, 18 S.W. at 689.

16. *Hardee v. Vincent*, 136 Tex. 99, 103, 147 S.W.2d 1072, 1073 (1941) (profits of separately owned dry goods store found to be community property); *Mitchell v. Mitchell*, 80 Tex. 101, 112, 15 S.W. 705, 708 (1891) (proper for trial court to instruct that profits of separately owned mercantile business were community property); *Epperson v. Jones*, 65 Tex. 425, 428 (1886) (storeowner's profits found to be community property); *Walker-Smith Co. v. Coker*, 176 S.W.2d 1002, 1007 (Tex. Civ. App.—Eastland 1943, writ ref'd w.o.m.) (profits of separately owned grocery store held to be community property); *Logan v. Logan*, 112 S.W.2d 515, 525 (Tex. Civ. App.—Amarillo 1937, writ dism'd) (profits from separately owned hotel business found to be community property).

17. 152 Tex. 491, 260 S.W.2d 676 (1953).

18. *Id.* at 499, 260 S.W.2d at 681.

19. The court in *Norris* stated: "Reasonable control and management is necessary to preserve the separate estate and put it to productive use." *Id.*

prior to the marriage. The husband achieved production from two of the leases during the marriage when he negotiated a farmout agreement.²⁰ The court held that profits from the wells drilled before marriage were separate property, but production from the wells drilled pursuant to the farmout agreement negotiated after marriage were community property.²¹ The court reasoned that the farmout agreement was community in nature because it was acquired through an unreasonable amount of community labors.²² Commentators have criticized this rule as illogical because it does not apportion enhancement in value according to what labor was reasonable or unreasonable but rather treats characterization as an all or nothing proposition.²³ The rule consequently is difficult to apply because it establishes no guidelines for determining how much labor is reasonable.²⁴

Early Texas decisions did not clearly establish whether the community ownership theory applied to situations where the property that increased in value was corporate stock.²⁵ In *Scofield v. Weiss*,²⁶ however, the Court of Appeals for the Fifth Circuit, applying Texas law, held that the increase in value of corporate stock did not belong to the community.²⁷ The issue before the court in *Scofield* was whether the issuance of stock dividends was separate or community for gift tax purposes.²⁸ The court concluded that because the increase in value of corporate stock retained its separate character, an issue of stock dividends also remained separate property even though the issue of dividends was due to efforts of the husband during the term of the marriage.²⁹ The precedential value of this decision is doubtful, for the court relied on *Beals v. Fontenot*,³⁰ a Fifth Circuit deci-

20. A farmout agreement occurs when a lessee assigns his interest in an oil and gas lease, retaining an overriding royalty interest in the oil and gas equivalent to a percentage of production or a specific number of barrels of oil in place. 43 TEX. JUR. 2D *Oil & Gas* § 418 (1963).

21. 152 Tex. at 501, 260 S.W.2d at 682.

22. *Id.*

23. W. REPPY & W. DEFUNIAK, COMMUNITY PROPERTY IN THE UNITED STATES 282 (1975); Weekley, *Appreciation of a Closely Held Business Interest Owned Prior to Marriage—Is It Separate or Community Property?*, 7 COMMUNITY PROP. J. 261, 282 (1980).

24. Professors Reppy and DeFuniak characterize the state of the law regarding separate and community property as "somewhat akin to that of obscenity and the first amendment in the 1960's, when Justice Stewart made the memorable comment that he could not define obscenity but 'I know it when I see it.'" W. REPPY & W. DEFUNIAK, *supra* note 23, at 284 (citing *Jacobellis v. Ohio*, 378 U.S. 184, 197 (1964)).

25. *See* *Brand v. Brand*, 102 S.W.2d 310, 312 (Tex. Civ. App.—Beaumont 1937, no writ) (holding, without rationale, that appreciation of separate stock belonged to community); *Fain v. Fain*, 93 S.W.2d 1226, 1229 (Tex. Civ. App.—Fort Worth 1936, writ dismissed) (finding enhanced value of corporate assets inure to stockholders, but no discussion of community ownership theory).

26. 131 F.2d 631 (5th Cir. 1942).

27. *Id.* at 632 ("[I]t is well settled that an original issue of corporate stock . . . retains its separate character, no matter how much it increases in value . . .").

28. *Id.* at 631.

29. *Id.* at 632.

30. 111 F.2d 956 (5th Cir. 1940).

sion that applied Louisiana law.³¹ Furthermore, the court in *Beads* held that the increase in value of separate stock remained separate property only because the evidence was insufficient to establish that the increase was due to the time, toil, and effort of the community.³² Nevertheless, subsequent Texas decisions adhered to the ruling in *Scofield*.³³

In 1968 the Fort Worth court of appeals mitigated the effects of *Scofield* in *Dillingham v. Dillingham*.³⁴ The court held that an increase in value of corporate stock that results from the efforts of the husband during marriage belongs to the community if the corporation is an alter ego of the husband.³⁵ The district court had found that the husband's wholly owned corporation was his alter ego and thus the increase in value of the corporation belonged to the community.³⁶ The court of appeals upheld this decision and, relying specifically on the opinion of the Texas attorney general, held that the enhancement in value of separate property consisting of corporate assets is community property when the corporation is an alter ego of one of the spouses.³⁷ This decision, although not directly disapproving the *Scofield* ruling, led to a gradual abandonment of the *Scofield* rule in the Texas courts of appeals.

The Texas courts' shift away from the *Scofield* rule became apparent in 1974 in *Bell v. Bell*.³⁸ The Beaumont court of appeals held in *Bell* that in dividing the marital estate the trial court should consider the increase in value of corporate assets resulting from business transmitted through the corporation during the term of marriage.³⁹ The Texas Supreme Court re-

31. The *Beads* court also stated that the community is not a partnership, which is contrary to Texas law. *Id.* at 959; see 30 TEX. JUR. 2D *Husband & Wife* § 52 (1962).

32. 111 F.2d at 959.

33. See *Johnson v. First Nat'l Bank*, 306 S.W.2d 927, 929 (Tex. Civ. App.—Fort Worth 1957, no writ); *Wells v. Hiskett*, 288 S.W.2d 257, 265 (Tex. Civ. App.—Texarkana 1956, writ ref'd n.r.e.). *Wells* did not cite *Scofield* but did state that an increase in value of separate stock cannot be recovered when the owning spouse has acted as an agent of the corporation and not as an individual. 288 S.W.2d at 265. In *Johnson* the increased value of separate stock was due to accumulated earnings of the corporation and not to the husband's time, toil, and effort, but the court nevertheless cited *Scofield* as authority. 306 S.W.2d at 929.

34. 434 S.W.2d 459 (Tex. Civ. App.—Forth Worth 1968, writ dism'd). Professor McKnight calls this decision a refinement of the rule in *Norris v. Vaughan*. McKnight, *Family Law: Husband and Wife, Annual Survey of Texas Law*, 24 Sw. L.J. 49, 52 (1970). From this characterization the labors expended in *Dillingham* can be viewed as an unreasonable preservation of separate property when the corporation has been set up as an alter ego of the spouse.

35. 434 S.W.2d at 461-62. A corporation may be deemed an alter ego if an individual manages the corporation in such a manner that its affairs are indistinguishable from the individual's personal affairs. *Torregrossa v. Szelc*, 603 S.W.2d 803, 804 (Tex. 1980); *Keith v. Woodul*, 616 S.W.2d 375, 377 (Tex. Civ. App.—Texarkana 1981, no writ).

36. 434 S.W.2d at 462.

37. *Id.* at 461-62 (citing Op. Tex. Att'y Gen. No. O-6595 (1945)). The attorney general's opinion involved an inheritance tax case in which the decedent's wife wanted the surplus of the decedent's separately owned corporate stock to be characterized as community property. This characterization would decrease the estate tax because only one-half of the surplus would be taxed. The attorney general stated that the increase in value of the decedent's corporate stock should belong to the community when the corporation was the alter ego of the decedent. 434 S.W.2d at 461; Op. Tex. Att'y Gen. No. O-6595 (1945).

38. 504 S.W.2d 610 (Tex. Civ. App.—Beaumont), *rev'd*, 513 S.W.2d 20 (Tex. 1974).

39. 504 S.W.2d at 611-12. *Scofield*, however, still carried weight. Both *Scofield* and

versed, but held only that regardless of whether the property was community or separate, an abuse of discretion in dividing the community property had not occurred, and the husband should receive the entire value of the stock.⁴⁰ The court thus sidestepped the characterization issue and increased the uncertainty regarding proper treatment of the increased value of corporate stock.⁴¹

In 1981 the Amarillo court of appeals held in *In re Marriage of York*⁴² that when separate corporate assets increase due to the efforts of the husband during marriage, this increase belongs to the community.⁴³ In *York* the husband incorporated his business in order to obtain a loan. Business profits that accumulated during the marriage up to the time of incorporation were determined by the court and included in the valuation of the stock. The court found a percentage of the stock value attributable to business profits to be community property due to the labors of the husband.⁴⁴ In the same year the Houston court of appeals, applying the reimbursement theory in *Wachendorfer v. Wachendorfer*,⁴⁵ denied recovery of the increase in value of corporate stock because the issue was not properly pled.⁴⁶ The court found that no pleading expressly asserted a right to reimbursement for labor expended.⁴⁷ The court held that a spouse claiming reimbursement for enhancement of the separate estate must affirmatively plead and prove both the amount of the community contribution and the enhanced value.⁴⁸ The court remanded the case to the trial court for an equitable distribution upon proper pleadings.⁴⁹ Examination of *York* and *Wachendorfer* reveals the two differing theories of recovery that Texas courts of appeals were applying to increases in value of corporate stock.

B. The Reimbursement Approach

In 1886 the Texas Supreme Court held in *Furrh v. Winston*⁵⁰ that the community must be reimbursed for funds spent in improving the separate property of one of the spouses.⁵¹ This case involved the use of community funds to place a dwelling upon separately owned real estate.⁵² The court held that the use of community funds gave the community no right, title,

Wells were cited by the dissent in *Bell* as solid authority for a contrary holding. *Id.* at 614 (Keith, J., dissenting).

40. *Bell v. Bell*, 513 S.W.2d 20, 22 (Tex. 1974).

41. Justice Keith's dissent in the court of appeals evidenced this uncertainty when he asked the supreme court to lay down definitive guidelines addressing this issue. 504 S.W.2d at 616.

42. 613 S.W.2d 764 (Tex. Civ. App.—Amarillo 1981, no writ).

43. *Id.* at 770.

44. *Id.*

45. 615 S.W.2d 852 (Tex. Civ. App.—Houston [1st Dist.] 1981, no writ). The reimbursement theory is discussed *infra* notes 50-76 and accompanying text.

46. 615 S.W.2d at 854.

47. *Id.*

48. *Id.*

49. *Id.* at 855.

50. 66 Tex. 521, 1 S.W. 527 (1886).

51. *Id.* at 524, 1 S.W. at 529.

52. *Id.*

or interest in the land, but did give the community a right to reimbursement for funds expended.⁵³

The claim for reimbursement has been held to be in the nature of a charge on the property so improved.⁵⁴ If benefits to the community from the improved separate property outweigh the amount spent in improving the property, the community has received adequate compensation and has no right to reimbursement.⁵⁵ Thus the rule is purely equitable.⁵⁶ This rule has been applied not only to situations involving community funds expended on separate property, but also to cases of separate funds expended on community property.⁵⁷

While use of the reimbursement theory to afford recovery when community funds have been spent on separate property seems well established,⁵⁸ Texas courts typically have not proceeded under a reimbursement theory when community labors, rather than community funds, have increased the value of separate property. One possible exception is *Wachendorfer v. Wachendorfer*,⁵⁹ which involved a wife's attempted recovery of the increased value of her husband's separately owned corporate stock. The court remanded the case because no pleading specifically asserted a right to reimbursement for the value of community labor expended.⁶⁰ Thus the court was proceeding under a reimbursement theory for community labors spent on enhancement of separate property.⁶¹ Another possible exception is *Faulkner v. Faulkner*.⁶² In that case the district court found that the increase in separate stock value was due to community efforts but did not award any portion of the stock to the wife.⁶³ Instead, the wife retained a judgment lien on the stock.⁶⁴ The court of appeals reversed, holding that answers to the questions of whether enhancement of the stock occurred as a result of the community's labor and whether the enhancement was above and beyond the salaries the spouses received from the corporation were

53. *Id.* The court also stated that this rule applied to community labors expended on separate property. *Id.*

54. *Welder v. Lambert*, 91 Tex. 510, 526, 44 S.W. 281, 286 (1898).

55. *Colden v. Alexander*, 141 Tex. 134, 147-48, 171 S.W.2d 328, 334 (1943).

56. *Id.*

57. *See Dakan v. Dakan*, 125 Tex. 305, 320, 83 S.W.2d 620, 628 (1935).

58. *See Burton v. Bell*, 380 S.W.2d 561, 564-65 (Tex. 1964) (reimbursement for improvements made on wife's separately owned real estate); *Lindsay v. Clayman*, 151 Tex. 593, 599, 254 S.W.2d 777, 781 (1952) (reimbursement for improvements placed on separately owned real estate); *Colden v. Alexander*, 141 Tex. 134, 147, 171 S.W.2d 328, 334 (1943) (use of community funds to pay interest on separate property's mortgage does not impress separate property with community character); *Dakan v. Dakan*, 125 Tex. 305, 320, 83 S.W.2d 620, 628 (1935) (reimbursement for separate funds spent in purchasing community property).

59. 615 S.W.2d 852 (Tex. Civ. App.—Houston [1st Dist.] 1981, no writ).

60. *Id.* at 854.

61. The court stated: "Although we are not aware of any recovery in Texas by a spouse for the contribution of community labor to the enhanced value of the other spouse's separate corporation, we cannot say that there can be no such recovery under Texas law." *Id.* at 855.

62. 582 S.W.2d 639 (Tex. Civ. App.—Dallas 1982, no writ).

63. *Id.* at 640-41.

64. *Id.* at 641.

purely speculative.⁶⁵ This analysis is equivalent to a reimbursement theory because a judgment lien approximates a charge on the property.⁶⁶ Moreover, the court of appeals reversed the district court's decision because the wife had not proved that the community expended labor in excess of the benefits it received from the separate property.⁶⁷

The Texas Supreme Court squarely addressed the issue of whether the reimbursement theory may afford recovery in situations where the increase in value of separately owned stock is due to community efforts in *Vallone v. Vallone*.⁶⁸ Tony Vallone had received from his father by gift a restaurant that he later incorporated. The initial capital of the restaurant was Tony's separate property.⁶⁹ The corporation's value increased dramatically over time and became the major asset of both the community and the husband's separate estate.⁷⁰

Mrs. Vallone sued for divorce, claiming that the corporation was Mr. Vallone's alter ego or, alternatively, that she should be reimbursed for the improvement of the separate estate at the expense of the community. The district court, however, awarded the entire value of the corporation to Mr. Vallone.⁷¹ The court of appeals reversed and remanded the case for a proper division of the property.⁷² Upon this decision, Mr. Vallone applied for and was granted a writ of error by the Texas Supreme Court.

The supreme court found that the corporation was not Mr. Vallone's alter ego.⁷³ The court did hold, however, that the community may recover an increase in the value of separate stock resulting from the efforts of one of the spouses under a theory of reimbursement.⁷⁴ The court denied recovery in *Vallone* because Mrs. Vallone had pled for reimbursement if community funds or property had been used to benefit the separate estate, but not if community labors had been expended.⁷⁵ The court concluded that the district court committed no error because Mrs. Vallone filed no specific pleadings seeking reimbursement for community labors.⁷⁶

The *Vallone* decision indicates that reimbursement is a method of recovery applicable to community labors spent increasing the value of corporate

65. *Id.*

66. See L. SIMPKINS, TEXAS FAMILY LAW § 22.38 (O. Speer 5th ed. 1977).

67. 582 S.W.2d at 641.

68. 644 S.W.2d 455 (Tex. 1982).

69. Property acquired by gift remains the separate property of the spouse. TEX. FAM. CODE ANN. § 5.01(a)(2) (Vernon 1975).

70. 644 S.W.2d at 457. The initial capital of the corporation consisted of approximately \$20,000 in assets, but grew to a valuation of over one million dollars in 10 years' time. *Id.*

71. *Id.*

72. *Vallone v. Vallone*, 618 S.W.2d 820, 824 (Tex. Civ. App.—Houston [1st Dist.] 1981), *rev'd*, 644 S.W.2d 455 (Tex. 1982). The court found that the trial court erred in not considering the increase in value of the corporation in division of the property. 618 S.W.2d at 824.

73. 644 S.W.2d at 458. The court held that Mrs. Vallone's appeal on the alter ego issue was based upon insufficiency of evidence, a question that the supreme court did not have jurisdiction to decide. *Id.*

74. *Id.* at 459.

75. *Id.*

76. *Id.* Justice Sondock vigorously dissented, stating that Mrs. Vallone's pleadings were adequate to recover under a community ownership theory. *Id.* at 468.

stock. The *Vallone* court did not make clear whether the community ownership theory was still a viable method of recovery of the increased value of corporate stock. In light of the inconsistency of prior courts of appeals decisions and the *Jensen* court of appeals decision, the Texas Supreme Court agreed to hear *Jensen v. Jensen*.

II. *JENSEN V. JENSEN*

The issue before the Texas Supreme Court in *Jensen v. Jensen* was whether the increase in value of separately owned corporate stock belongs to the community when the increase is due to the time, toil, and efforts of either or both spouses.⁷⁷ In a five-to-four decision the court initially held that the increased value did belong to the community.⁷⁸ In affirming the court of appeals, the supreme court avoided using the terms "characterization" and "reimbursement," holding simply that the community was entitled to be compensated for the increase in value of corporate stock.⁷⁹ Upon motion for rehearing, the court withdrew its judgment and opinion.⁸⁰ The new decision reversed the court of appeals and affirmed the decision of the trial court. The supreme court held that the reimbursement theory may provide relief in this situation, but under that theory Mrs. Jensen should not recover.⁸¹

The court began with a discussion of the community ownership and reimbursement theories.⁸² Based on its evaluation of Texas case law and other authorities,⁸³ the court concluded "that the reimbursement theory more nearly affords justice to both the community and separate estates" in cases involving the increased value of separately owned corporate stock.⁸⁴ The court stated that under the proper rule for recovery the community must be reimbursed for the value of time and effort expended, less the remuneration received for that time in the form of salary, bonus, dividends, and fringe benefits.⁸⁵ The majority gave three reasons for adopting

77. 27 Tex. Sup. Ct. J. 68, 69 (Nov. 9, 1983). No appeal was made as to whether the increase in value of the stock was actually due to Mr. Jensen's efforts. In the district court Mr. Jensen testified that he devoted 90% of his time to RLJ enterprises.

78. 26 Tex. Sup. Ct. J. 480, 482 (July 6, 1983) (*Jensen I*).

79. *Id.* The Tyler court of appeals referred to the district court's error as a "mis-characterization" of community property as separate property. *Jensen v. Jensen*, 629 S.W.2d 222, 225 (Tex. App.—Tyler), *rev'd*, 27 Tex. Sup. Ct. J. 68 (Nov. 9, 1983). The Supreme Court did not discuss this aspect of the appellate court's holding.

80. 27 Tex. Sup. Ct. J. 68 (Nov. 9, 1983) (*Jensen II*).

81. *Id.* at 70. The majority's opinion in *Jensen II* was Justice Wallace's dissenting opinion in *Jensen I* with minor changes. *See Jensen v. Jensen*, 26 Tex. Sup. Ct. J. 480 (July 6, 1983).

82. 27 Tex. Sup. Ct. J. at 69.

83. *Id.* The majority only makes note of a "consideration of the writings of various scholars in this field," not naming any specific authorities. *Id.*

84. *Id.*

85. *Id.* Fringe benefits are an unseen factor that the trial court could consider in finding that the community has been adequately compensated and thus has no right to reimbursement. Typically, closely held corporations provide material fringe benefits to their shareholders. Allowing the corporation to retain ownership of these benefits, such as cars or club memberships, provides substantial tax benefits because the corporation can deduct these

the reimbursement theory. First, it assures the community of reimbursement for the value of time expended while still protecting the separate estate.⁸⁶ Second, this theory relieves the district courts of the burden of determining what factors caused the increase in value of the stock and in what proportion.⁸⁷ Finally, the court found the reimbursement theory consistent with Texas case law, citing a line of cases that adhered to this theory.⁸⁸

The court applied the reimbursement theory to the facts at hand and held that Mrs. Jensen should not recover.⁸⁹ The court stated that for Mrs. Jensen to recover she must plead and prove that the community was entitled to a sum in addition to the salaries Mr. Jensen received.⁹⁰ Mrs. Jensen must first show that no evidence supported the finding of the trial court that the community was adequately compensated and then present evidence that would prove a contrary position as a matter of law.⁹¹ At trial, the only evidence offered concerning Mr. Jensen's compensation was that of an expert in the field of corporate valuation who stated that Mr. Jensen was adequately compensated.⁹² Mrs. Jensen offered no evidence to contradict the expert testimony and thus failed to sustain her point.⁹³

Justice Kilgarlin's dissent disagreed with the majority's holding that reimbursement was a sufficient method of recovery.⁹⁴ The dissent argued that in some circumstances the community may be entitled to greater compensation than that received by way of the spouse's salary.⁹⁵ Moreover, the dissent contended that the reimbursement theory was not even pled in this case; thus the court erred in reaching a decision under the reimbursement theory.⁹⁶ Justice Kilgarlin alternatively argued that even if reimbursement was the proper method of recovery and was properly pled, the trial court did not find that the community was adequately reimbursed.⁹⁷ According to the dissent, the evidence produced in the trial court did not support the majority's conclusion that the community was adequately reimbursed by Mr. Jensen's salaries and dividends, nor did the trial court find that the community was adequately reimbursed.⁹⁸

The dissent also noted that the majority ignored the Texas line of com-

costs as a business expense. The parties are unwilling to bring up the status of these benefits in court, however, for fear of inquiries from the I.R.S. Interview with Joseph W. McKnight, Professor of Law, Southern Methodist University, Dallas, Texas (Jan. 17, 1984).

86. 27 Tex. Sup. Ct. J. at 70.

87. *Id.*

88. *Id.* (citing *Welder v. Lambert*, 91 Tex. 510, 44 S.W. 281 (1898); *Daken v. Daken*, 125 Tex. 325, 83 S.W. 620 (1935)).

89. 27 Tex. Sup. Ct. J. at 70.

90. *Id.*

91. *Id.*

92. *Id.* The dissent disputed the majority's conclusion that the expert, Hickman, found the community to be adequately compensated. *Id.* at 71 (Kilgarlin, J., dissenting).

93. *Id.* at 70.

94. *Id.* at 71.

95. *Id.* The dissent did not, however, indicate what those circumstances were.

96. *Id.*

97. *Id.* at 71-72.

98. *Id.* The trial court's findings of fact only stated that the salaries and dividends paid

munity ownership cases, which hold that any property acquired by one of the spouses after marriage by toil or effort is community property.⁹⁹ The dissent concluded that the concept of reimbursement did not adequately protect the wife and that the proper remedy would be to follow a variation of the community ownership theory.¹⁰⁰ This approach would determine the amount of the enhanced value of stock that belongs to the community and compensate Mrs. Jensen for this value through a division of other community assets.¹⁰¹

In a separate dissent Justice Robertson also stated that the trial court's findings were in direct conflict with the majority's holding.¹⁰² Justice Robertson argued that the trial court did not consider the increase in value of the separately owned stock and therefore Mrs. Jensen could not have been adequately compensated for the stock's enhanced value.¹⁰³ Justice Robertson would have held that the reimbursement formula may offer insufficient relief in this case.¹⁰⁴ This dissent is confusing because it states that the traditional reimbursement formula may be inadequate in some cases, but also expressly agrees with the majority's statement of the law.¹⁰⁵

By holding that only the reimbursement method should be applied in situations involving the increase in value of separately owned corporate stock, the supreme court provided a workable solution for judges and attorneys faced with this problem. The decision avoids the problem of determining what is reasonable labor and exactly what factors caused the increase in value of corporate stock. Moreover, attorneys will not be faced with deciding what theory to plead. The reimbursement method provides a means of protecting the separate estate without causing loss to community interests.

The majority opinion, however, makes no attempt to explain the inconsistencies of this decision with prior community ownership cases. The court neither cites any cases from the community ownership line nor ex-

Mr. Jensen were adequate and reasonable and did not suggest that the community was adequately reimbursed for the enhanced value of the shares of stock. *Id.* at 71.

99. *Id.* at 72 (citing *Graham v. Franco*, 488 S.W.2d 390, 392 (Tex. 1972); *Norris v. Vaughan*, 152 Tex. 491, 501, 260 S.W.2d 676, 682 (1953)).

100. 27 Tex. Sup. Ct. J. at 72. The dissent failed to explain how this variation would fit with prior decisions that followed a community ownership theory. The language in those opinions explained the increase in value of separate property in terms of "characterization." *Norris v. Vaughan*, 152 Tex. 491, 500, 260 S.W.2d 676, 681 (1953); *In re Marriage of York*, 613 S.W.2d 764, 770 (Tex. Civ. App.—Amarillo 1981, no writ). In *Norris* the court stated that "[r]easonable control and management is necessary to preserve the separate estate" and would not impress community character upon the separate property. 152 Tex. at 500, 260 S.W.2d at 681. In *York* the court stated that "if the separate property of one spouse is increased due to the time, talent and industry of either spouse . . . then the entire increase acquires a community character." 613 S.W.2d at 770 (emphasis added).

101. 27 Tex. Sup. Ct. J. at 72. Justice Kilgarlin adhered to his conclusion in *Jensen I*, 26 Tex. Sup. Ct. J. at 482. In his dissent he clarified what he meant by compensation as stated in his initial opinion in *Jensen I*. 27 Tex. Sup. Ct. J. at 72.

102. *Id.* at 73.

103. *Id.*

104. *Id.*

105. *Id.*

pressly overrules them. The court might have distinguished earlier community ownership cases because they dealt with profits derived from separate property. No Texas case had clearly established that the increase in value of separate property belonged to the community, unless this increase was in the form of retained profits.¹⁰⁶ Although the court indicates that reimbursement is the only viable method of recovering the increase in value of corporate stock due to community labors, the court does not make clear whether reimbursement is now the only form of recovery in all situations involving the increase in value of separate property due to community labors. The broad language of the *Jensen II* decision may preclude recovery under the community ownership theory in all circumstances.¹⁰⁷

The court also does not reconcile the *Jensen II* decision with its holding in *Vallone* that reimbursement must be specifically pled and proved.¹⁰⁸ The court held that Mrs. Jensen should not recover under her plea of reimbursement, yet Mrs. Jensen did not specifically plead for reimbursement.¹⁰⁹ Mrs. Jensen's second counterpoint urged the court to hold that the "salary and bonuses [Mrs. Jensen received] were inadequate and unreasonable," but did not plead for reimbursement of the value of community labors expended upon separate property.¹¹⁰ The court held, however, that Mrs. Jensen failed upon her plea of reimbursement, rather than that she inadequately preserved error on that ground. To avoid inconsistency the court, as in the *Vallone* case, should have based its holding on Mrs. Jensen's failure to properly plead reimbursement.¹¹¹

The two *Jensen* decisions demonstrate the supreme court's difficulty in identifying a method of recovery that provides sufficient relief in all circumstances yet provides a practical means of distinguishing separate from

106. Arguably *Norris v. Vaughan*, 152 Tex. 491, 260 S.W.2d 676 (1953), dealt with the increase in value of separate property, but the property was in the form of a new acquisition of a farmout agreement that generated profits. The decision in *In re Marriage of York*, 613 S.W.2d 764 (Tex. Civ. App.—Amarillo 1981, no writ), could have resulted from the fact that the valuation of the increase of separate stock was tied to business profits. *Id.* at 770.

107. The court evaluated both theories and concluded "that the reimbursement theory more nearly affords justice to both the community and separate estates." *Id.* at 69. This language implies that the community ownership theory may no longer be applied in Texas.

108. *Vallone v. Vallone*, 644 S.W.2d 455, 462 (Tex. 1982).

109. Justice Ray asserts that "*Jensen* is remarkably similar to *Vallone* in its facts but is to be differentiated on procedural grounds. Whereas *Vallone* was a reimbursement case, *Jensen* is a characterization case." Ray, *Comments on Cameron and Vallone*, ST. B. SEC. REP., FAM. L., Winter 1982-83, at 6, 8 (emphasis in original). Moreover, when the court asked Mrs. Jensen's attorney at oral argument why he did not plead reimbursement, he replied that he specifically avoided that theory because he had little or no case under a reimbursement plea. Interview with James Blume, attorney for Mrs. Jensen, Dallas, Texas (Sept. 5, 1983).

110. Brief for Mrs. Jensen at 30.

111. The *Jensen* and *Vallone* pleadings are substantially similar. Mrs. Vallone's first cross point stated: "The trial court and the Court of Appeals both erred in their finding that 47% of the stock in Tony's Restaurant, Inc., as well as the total value thereof, is the separate property of TONY VALLONE." *Vallone v. Vallone*, 644 S.W.2d 455, 468 (Tex. 1982). Mrs. Jensen's first counterpoint stated: "The Court of Appeals correctly held that the community was entitled to the value of the appreciation of shares of RLJ Printing Company, Inc., due to time, toil and efforts of the community." Brief for Mrs. Jensen at 9. Both contain language resembling a characterization plea rather than one for reimbursement.

community property. *Jensen I* provided adequate protection of community interests by holding that the community must be compensated for increase in value of separate stock due to time, toil, and efforts of the community.¹¹² The decision was consistent with Texas case law under the community ownership theory,¹¹³ but provided a variation on that theory because it did not characterize the increase in value of community property.¹¹⁴ Thus the stock would not be split in two and viewed as part separate and part community property, as would occur under the basic community ownership concept.

Jensen I did not address the issue of when courts should afford this recovery,¹¹⁵ and provided no definition of reasonable labor. Neither did the opinion designate a method for determining the source of the increase in stock value, for only if the increase was due to the efforts of the community would the community receive compensation. Finally, *Jensen I* provided no means for valuation of the stock, leaving that problem to the trial courts.

Jensen II provided a more practicable means of recovery, but the court made no attempt to clarify the meaning or continuing viability of the community ownership cases after *Jensen*. Furthermore, the decision was inconsistent with the *Vallone* requirement that reimbursement be specifically pled. Finally, the court did not address the dissent's argument that the issue of adequate reimbursement was not considered at the trial level.

III. CONCLUSION

In *Jensen v. Jensen* the Texas Supreme Court held that only the reimbursement theory should be applied when the increase in value of separate corporate stock is due to the time, toil, and effort of the community. The court did not clearly indicate whether this decision extends to cases in which community labors have increased the value of separate property other than stock. The court held that the spouse asserting the community interest should not recover because she failed to prove as a matter of law that no evidence supported the finding of the trial court.

112. Under this theory even if the increase is found to be community property the case will only be remanded to the district court for division of the property if the error resulted in an abuse of discretion in the proportion of the division. *Smith v. Smith*, 620 S.W.2d 619, 625 (Tex. Civ. App.—Dallas 1981, no writ).

113. Commentators have long been of the opinion that the increase in value of separate property should belong to the community. See L. SIMPKINS, *supra* note 66, § 15.45; WEEKLEY, *supra* note 23, at 282; Comment, *The Effect of Community Time, Talent, and Industry upon Separate Property*, 22 BAYLOR L. REV. 527, 542 (1970); Comment, *Profits and Increases in the Value of Partnerships and Corporations as Governed by Community Property Law*, 36 TEX. L. REV. 187, 194-95 (1957). But see Comment, *Closely Held Corporations in the Wake of Vallone: Enhancement of Stock Value by Community Time, Talent and Labor*, 35 BAYLOR L. REV. 47, 87 (1983).

114. 26 Tex. Sup. Ct. J. at 482.

115. The dissent in *Vallone* referred to the reimbursement and community ownership theories as distinct. *Vallone v. Vallone*, 644 S.W.2d 455, 461 (Tex. 1982) (Sondock, J., dissenting). The first *Jensen* opinion failed to explain why two seemingly distinct theories could afford recovery in a situation including the increase in value of corporate stock.

The court's difficulty in finding a method of recovery that is both equitable and practical is evidenced by the reversal of *Jensen I* in *Jensen II*. *Jensen II* sets forth a more practicable method of recovery but does not reconcile its decision with prior Texas decisions under the community ownership theory or with the requirement in *Vallone* that reimbursement be specifically proved and pled. Trial courts will now be relieved of the practical problems that *Jensen I* left unresolved, but will be left with the problem of deciding the future relevance of Texas community ownership cases and determining the reach of *Jensen II*.

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