Collier Family Law and the Bankruptcy Code

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CHAPTER 9 Effects of Bankruptcy on Nonmarital Family Relationships

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P 9.05 Obligations of Unmarried Couples.

It is increasingly common for couples to live together without being married.n1 They may do so for economic reasons, such as the potential loss of social security, alimony or tax benefits upon marriage, or because they reject the state-imposed form and duties that arise from a marriage. They may do so because they are prohibited from marrying, due to another marriage which has not terminated, or because they are a gay or lesbian couple. Indeed, even if a same-sex couple has been validly married under the laws of a state or foreign country, there are serious questions whether they can be considered as married under the federal Bankruptcy Code, due to the strictures of the federal Defense of Marriage Act, which defines marriage, for purposes of federal law as "only a legal union between one man and one woman as husband and wife."n2

Although historically the law had little sympathy for economic claims arising from such relationships,n3 that picture has changed considerably in recent years. Following the lead of the Supreme Court of California in *Marvin v. Marvin*,n4 the courts of many states have recognized a right to enforce claims against a former cohabitant. They have done so using a variety of legal theories, including enforcement of express oral or written contracts, implied contracts and general equity powers and theories such as quasi-contract, quantum meruit, unjust enrichment and constructive trust.n5 Such cases have involved not only property division but also orders for support of the formerly dependent partner.

In addition, some states have granted the availability of official recognition of same sex relationships as domestic partnerships, giving the domestic partners all of economic benefits of marriage. Such benefits may include the right to won property as community propertyn5a or as tenants by the entireties.n5b These types of property receive special treatment in bankruptcy in various respects.n5c However, that treatment sometimes speaks of property owned by the debtor and the debtor's spouse and therefore may be prevented by the Defense of Marriage Act. Courts are only beginning to sort out how the state and federal statutory rights are to be sorted out.

To the extent that rights arise from such relationships to support, rather than to property settlements, an argument could perhaps be made that they should be considered the equivalent of marriage for federal bankruptcy law purposes. In the area of paternity, as discussed above, the courts have shown some willingness to ignore the literal language of the statute.n6 However, in view of the "plain language" approach which has been applied to the Bankruptcy Code generally,n7 and even in cases in which ceremonial marriages have been annulled,n8 it would be very dangerous to count upon such arguments having success. Especially since virtually all of the cases permitting awards against unmarried cohabitants have been based on contractual theories,n9 it is more likely that a court determining dischargeability under section 523(a)(5) would find the debt to be a contract claim not unlike all other contract claims in

bankruptcy.

Thus, in *In re Doyle*,n10 the Bankruptcy Appellate Panel for the Ninth Circuit rejected the claim of the debtor's former cohabitant that a state court judgment ordering the debtor to make monthly mortgage payments on her residence was nondischargeable under section 523(a)(5). The court held that, under California law, the order arose from contractual obligations and not from under the Family Law Act, and was, therefore, not akin to alimony.n11 The court also rejected the argument that, under federal law, the nondischargeability section should be interpreted broadly to include familial obligations not explicitly mentioned therein, as had been done in paternity cases, holding that the relationship between the parties could not be considered a family relationship.n12

A new argument for nondischargeability of such obligations could have been created by the enactment of section 523(a)(15).n13 As originally enacted, that section applied to separation agreements and court orders not encompassed by section 523(a)(5), and did not contain the requirement that the debts involved be owed to a spouse, former spouse, or child of the debtor.n14 However, section 523(a)(15) was amended in 2005n15 to add the words "to a spouse, former spouse, or child of the debtor." Therefore this argument is not available in cases filed on or after October 17, 2005. Section 523(a)(15), as amended, is discussed elsewhere in this volume.n16

If the claim of the party entitled to support was treated solely as one arising out of a contract, the only possible avenues to a nondischargeability finding would be through a determination that there had been fraud or false pretenses on the part of the debtor, or perhaps a willful or malicious conversion of property. These grounds for nondischargeability are discussed elsewhere in this text.n17 Since some theories upon which awards to unmarried cohabitants, like constructive trust, are grounded in fraud, a dischargeability complaint based upon such arguments could have success when the facts of a particular case warranted it.

However, the facts will not often support such theories. For example, in *In re Shear*,n18 the former unmarried cohabitant of the debtor had obtained a judgment in state court for unjust enrichment. The bankruptcy court held that the judgment could not provide a basis for a collateral estoppel finding that the debtor willfully or maliciously injured the nondebtor plaintiff because the facts necessary to prove unjust enrichment under state law did not require a showing of willful or malicious injury. Examining the facts independently, the bankruptcy court did not find sufficient evidence to support a finding of willful and malicious injury. It similarly rejected the plaintiff's argument that the debts were incurred through false pretenses, finding that even if the debtor had promised to repay the plaintiff, there was no showing that such a promise, made when the parties were intimately involved, was made without an intent to fulfill it.n19 Similarly, in *In re Meltzer*,n20 the court found that the debtor had not obtained funds advanced by his former cohabitant through false pretenses because the debtor had not made any promise to repay until months after the funds were advanced. And in *In re Kindrick,* n21 the court ruled against a debtor's former cohabitant who sought all of the proceeds of a mobile home for which she had provided the downpayment and most of the mortgage payments. The court held that the debtor had not breached any duty as a fiduciary under section 523(a)(4), because no express trust relationship had existed, and had not committed larceny or embezzlement because he had had no fraudulent intent but rather had honestly believed he was entitled to one half of the proceeds of the sale. In addition, if the debtor files a chapter 13 case, this exception to discharge is not applicable.n22

On the other hand, a transfer of property to a former unmarried cohabitant in a property settlement potentially might be attacked as a fraudulent conveyance in a bankruptcy case, with the trustee arguing that no obligation between the parties justified the settlement.n23 In such cases, it would be necessary to assert applicable principles of state law recognizing express or implied obligations between unmarried cohabitants to show fair consideration for the transfer. State domestic partnership laws may also impact parties' rights and obligations.n23a

However, such arguments may in some cases be inconsistent with steps taken due to tax planning. For tax purposes, it may be advantageous to characterize the transfer as a gift, motivated by feelings of "detached and disinterested generosity," such as "affection, respect, admiration, charity or like impulses," and not "the constraining force of any

moral or legal obligation."n24 In such cases, the property transferred is not taxable to the recipient, as it would be if transferred in payment for services or other contractual obligations.n25 If the transfer discharges a contractual obligation, it is also probably a taxable event upon which a gain or loss would be realized by the transferor.n26 Further, to the extent the transfer occurred within 90 days prior to the bankruptcy case and was founded upon an antecedent debt, it may be avoidable as a preference.n27 And, to the extent there was a close relationship with the transferee, the transferee may be considered an "insider" subject to a one year, rather than a 90 day, preference period.n28

In order to plan and protect against the possible adverse consequences of bankruptcy, the steps that should be taken are much like those that should be taken in the context of a dischargeable marital property settlement agreement. Written agreements between the parties should, from the outset, specify their obligations to each other,n29 and also their interests in property acquired during the relationship.n30 For example, an agreement could provide that all or some of such property would be jointly owned. The bankruptcy estate would then acquire only the debtor's one half interest in the property and the nondebtor would retain his or her interest.

Similarly, in the context of a separation of unmarried cohabitants, obligations for future support or property transfers could be secured by a mortgage or other nonavoidable security interest in the potential debtor's property.n31 If that were done, the obligation would be given preferred status in the bankruptcy casen32 and, if not paid in the bankruptcy case, would generally remain enforceable against the collateral thereafter.n33

FOOTNOTES:

(n1)Footnote 1. *See* Rutkin, Family Law and Practice § 65.01 (1991).

(n2)Footnote 2. *1 U.S.C. § 7. See In re Kandu, 315 B.R. 123 (Bankr. W.D. Wash. 2004)* (lesbian couple that had married in Canada could not file joint bankruptcy petition because they were not considered married under Defense of Marriage Act).

(n3)Footnote 3. *See* Rutkin, Family Law and Practice, § 65.01[2].

(n4)Footnote 4. *18 Cal. 3d 660, 134 Cal. Rptr. 815, 557 P.2d 106 (1976)* .

(n5)Footnote 5. *See* Rutkin, Family Law and Practice, § 65.01[3]; Roddy, *Rights and Remedies of Cohabiting Couples Upon Termination of the Relationship,* 4 Divorce Litigation 52 (1992). *See also Connell v. Francisco, 74 Wn. App. 306 (Wash. App. 1994)* (community property principles applied in division of property after long-term "meretricious" relationship).

(n6)Footnote 5a. Community property rights are discussed in chapter 4 *supra*.

(n7)Footnote 5b. Tenancy by the entireties is discussed in *P 2.02[2][c] supra*.

(n8)Footnote 5c. *See P 2.05[4]*, ch.4 *supra*.

(n9)Footnote 6. *See P 9.02[1] supra.*

(n10)Footnote 7. *See, e.g., United States v. Ron Pair Enters., Inc., 489 U.S. 235, 109 S. Ct. 1026, 103 L. Ed. 2d 290, 20 C.B.C.2d 267 (1989)* .

(n11)Footnote 8. *See P 9.04 supra.*

(n12)Footnote 9. *See* Rutkin, Family Law and Practice, § 65.01[3].

(n13)Footnote 10. *16 C.B.C.2d 761, 70 B.R. 106 (B.A.P. 9th Cir. 1986)* .

(n14)Footnote 11. *In re Doyle, 16 C.B.C.2d 761, 764, 70 B.R. 106, 108* .

(n15)Footnote 12. *In re Doyle, 16 C.B.C.2d 761, 765, 70 B.R. 106, 109* .

(n16)Footnote 13. *11 U.S.C. § 523(a)(15)*, enacted by the Bankruptcy Reform Act of 1994, Pub. L. No. 103-394 (effective with respect to cases commenced on or after October 22, 1994), *reprinted in* Vol. E Collier on Bankruptcy, App. Pt. 9(a) (Matthew Bender 15th Ed. Revised).

(n17)Footnote 14. The 2005 Act, applicable to cases filed on or after October 17, 2005, amended this section to provide that this exception to discharge applies only to obligations to a "spouse, former spouse, or child of the debtor." *11 U.S.C. § 523(a)(15)*, as amended by Pub. L. No. 109-8 (2005), effective in cases commenced on or after October 17, 2005.

(n18)Footnote 15. Pub. L. No. 109-8 (2005), effective with respect to cases filed on or after October 17, 2005.

(n19)Footnote 16. *See P 6.07A supra.*

(n20)Footnote 17. *See P 6.08[3], [6] supra. See also In re Marcus, 45 B.R. 338 (S.D.N.Y. 1984)* (discharge denied because of debtor's transfer to hinder, delay or defraud "palimony" judgment creditor).

(n21)Footnote 18. *123 B.R. 247 (Bankr. N.D. Ohio 1991)* .

(n22)Footnote 19. *See also Kenna v. Lee (In re Lee), 304 B.R. 344 (Bankr. N.D. Ill. 2004)* (also rejecting nondischargeability claims under § 523(a)(2) and (a)(6) when debtor used former relationship partner's credit card with partner's express or implied consent).

(n23)Footnote 20. *171 B.R. 166 (Bankr. S.D. Fla. 1994)* .

(n24)Footnote 21. *In re Kindrick, 213 B.R. 504 (Bankr. N.D. Ohio 1997)* .

(n25)Footnote 22. *In re Lincoln, 264 B.R. 370 (Bankr. E.D. Pa. 2001)* (wrongful conversion of former cohabitant's property, leading to contempt order when debtor failed to return it or pay its value, simply created an unsecured claim in chapter 13 case).

(n26)Footnote 23. *See PP 7.06[3]* and *7.09 supra* .

(N27)Footnote 23a. *See Rabin v. Schoenmann (In re Rabin), 359 B.R. 242 (B.A.P 9th Cir. 2007)* (because California domestic partners had same economic rights as a married couple, they were limited to the single homestead exemption to which a married couple would be entitled).

(n28)Footnote 24. *Comm'r v. Duberstein, 363 U.S. 278, 80 S. Ct. 1190, 4 L. Ed. 2d 1218 (1960)* .

(n29)Footnote 25. *See* Rutkin, Family Law and Practice, § 41.06[1], [4].

(n30)Footnote 26. *See* Rutkin, Family Law and Practice, § 41.06[2].

(n31)Footnote 27. *See P 7.08 supra.*

(n32)Footnote 28. *In re Tanner, 145 B.R. 672 (Bankr. W.D. Wash. 1992)* (debtor's former lesbian companion was an insider). *See also P 7.08 supra.*

(n33)Footnote 29. *See* Rutkin, Family Law and Practice, § 65.02.

(n34)Footnote 30. For an example of such an agreement, *See* Rutkin, Family Law and Practice, § 65.04.

(n35)Footnote 31. *See* Chapter 7 *supra* for a discussion of avoidable liens. *See also In re Lincoln, 264 B.R. 370 (Bankr. E.D. Pa. 2001)* (wrongful conversion of former cohabitant's property, leading to contempt order when debtor failed to return it or pay its value, simply created an unsecured claim in chapter 13 case).

(n36)Footnote 32. *See, e.g., P 8.06 supra.*

(n37)Footnote 33. *See P 6.02[3] supra.*