

ORAL ARGUMENT — 10/7/97
96-1091
SCHLUETER V. SCHLUETER

FRIDAY: This is a tort claim expansion case. This was a divorce involving the transfer of funds by the husband to the husband's father. A jury verdict was rendered for constructive fraud upon that particular transaction; judgment jointly and severally against the husband and against his father in the amount of approximately \$13,000.00. There was a second verdict for exemplary damages. Actually one against each: \$30,000 against the husband, \$15,000 against the father.

When the money judgments were added into the property division along with the other property awarded to the wife and when they were backed out of the property that was awarded to the husband, the net result of the property division was that the wife got 100% of the assets on hand, and the husband got none.

The prevailing rule in this type of case is that fraud and other economic wrongs are not independent causes of action in a divorce case. This is a rule of *Belz, Moore* and the *Devine* cases all cited in my brief. But the Third CA below held that under this court's holdings in *Bounds v. Caudel, Price* and *Twyman* there is no impediment to an award of damages for an economic tort as part of a divorce.

I respectfully suggest to the court that this begs the real question, and the real question is whether the existing legal scheme for division of property incident to divorce adequately provides for economic wrongs?

OWEN: What if all of the community estate is exhausted by the fraud. What is the remedy for the spouse who has been defrauded?

FRIDAY: Well bear in mind that divorce courts have traditionally had a money judgment power. The issue is not the granting of a money judgment. The issue here is granting it in the context of an independent tort. Now what the courts have done is what the courts could do in the situation of your question. Let's assume a case where the community consisted of \$100,00 and the court found that all of that had been wasted. Under the existing scheme of law, the court would have the power in the fair and just division of property to grant the wronged spouse a judgment for that \$100,000, and in effect to deem that the wrongdoer spouse in effect had the benefit of that money wherever it is. So there is still a way to do it. The problem is that if you bring in the tort doctrine...

OWEN: Is that judgment enforceable against separate property just as if it were any other judgment?

FRIDAY: I think, and you pose a difficult question, the answer to that is perhaps not in the question. If you will allow me to answer it in this way. The assumption is that the wrongdoing

spouse had the benefit of that \$100,000 of the wasted or concealed assets. That money may be in existence, it may not be in existence. If it is in existence, then there is the fund to pay the judgment. If it is not, then the answer has to be that it would lie against whatever assets that the judgment creditor could collect that may turn out to be separate property after the divorce.

OWEN: You say there is existing law that holds that, that a family court judge can enter a personal judgment that's enforceable against separate property?

FRIDAY: Yes, cases to that effect cited in the brief. Mr. Campbell will not disagree with that proposition of law. The court has always had that power for the sake of achieving what it believes to be an overall fair and just result in the division of the estate.

HECHT: So what's the problem with the tort? Punitive damages, is that what it comes down to?

FRIDAY: That's certainly the biggest problem. But before we get to punitive damages, it is difficult for the TC's to integrate a tort judgment into the overall property settlement. In the *Twyman* case, Justice Cornyn pointed out that the award of personal injury tort damages does not relieve the court of the necessity of analyzing the overall division of property. And the gist of my argument to the court is that TC's can handle divisions of property much better, much more accurately, much more justly if they use the traditional approach of unequal division of property to account for an economic wrong that may have occurred. There is no question...I mean the law for decades has allowed TC to look at a fault generally and specifically to look at the wasting of assets in making an unequal division.

OWEN: Under my example, what's the legal basis for the money judgment? What do you call it?

FRIDAY: Restoring the wasted property.

OWEN: It's just awarding a money judgment flat out that's then enforceable against separate property of the other spouse?

FRIDAY: In the event in fact that the assets were just gone. However, that problem exist whether we're talking about a judgment of tort or a judgment to equalize property division. This court fell into several errors with respect to the accounting in the case. One must look at the impact of these judgments on the overall property division. What the court got correct, is the court did correctly treat the award of the almost \$13,000 as a community asset. It was indeed. The suit was for the loss of community assets and the court counted that in its balance sheet. On the other hand, the court completely ignored the liability side of the calculation and did not really weigh the impact of the \$13,000 judgment and the \$30,000 punitive damages on the husband's side. This is contrary to the established scheme, the Family Code §5.61(d), which is now 3.202. That provides that all

community property is subject to tortious liability. And even beyond that particular rule basic accounting says that if you are going to add money to one account, you're going to have to take it out of another account. Your fundamental double entry rule. The judge ignored the impact of the judgments on the husband's side.

OWEN: In my example would the judgment that the wife recover be community property so that he would get half of the judgment against him?

FRIDAY: No. Because the award in effect takes care of that.

OWEN: I thought your brief said that money judgments for property were community property as opposed to judgments for personal injury.

FRIDAY: The judgment is the means to the end. This was the point made in the *Belz* and the *Moore* cases. The fraud on the community doctrine is the means to raise the economic wrong and to get to the unequal division. The judgment then is the tool for transferring the money. The court in effect can do a couple of things. If there is still a lot of community property on hand, the court can do what it did in *Devine* - no money judgment in *Devine*. The TC simply pushed most of the assets over onto the wronged spouse's side, left a small portion on the wrongdoing spouse, observed that the wrongdoing spouse had had the benefit of the several hundred thousand dollars. Or, in the alternative, the court as it did in this case could decide that the assets weren't readily divisible in a way to give the wife some compensation, if you will. And so had the court done this one right, the court could have in its analysis have said, "Alright we are going to put a money judgment to equalize to accomplish a fair and just result leaving other assets on the other side, or leaving the wasted assets on the other side."

And this is a familiar way of doing it. Trial judges in divorce cases are used to thinking about this. But when you throw the tort analysis in, what the TC did here and it really was the exemplary damages issue more than anything else I think that threw the TC. The TC may have considered that they were somehow different than the actual damages. But this case was all about economic loss. There was no pleading ever of any emotional harm in this case.

ENOCH: I'm not connected with where you are going. You talked about the double entry accounting here. Are you saying that the problem with the tort analysis is that it forgets that when the community property, including the money judgment is pushed over to one spouse's side, it should be reflected as a negative on the other spouse's side, and the problem with the tort is you end up with a plus on one side without a corresponding negative on the other. Is that where you were going?

FRIDAY: That was the trap that the trial judge in this case fell into. And that is the trap, the traditional tort analysis...

ENOCH: And so what happens is there is not in fact an equitable division of the marital estate because the spouse who is giving up portions of the community property is not being given credit for that tort damage.

FRIDAY: Exactly that.

ENOCH: And so what resulted in 100% of the marital assets going to the wrong spouse would not have occurred if the \$15,000 and the \$30,000 figures had been considered a part of the marital estate to begin with. It would have shown that it was giving up \$30,000 when it was transferred to her, but in this case it's not shown. And so a second \$30,000 is shoved over there. Is that where you're going with this?

FRIDAY: I'm not suggesting a second \$30,000 was shoved over there. I am suggesting to you that the TC may not even have been aware of the ultimate impact of the judgment. There are at least 2 indications in the record. The hearing on the judgment was some months after both of the parts of the bifurcated trial, and she made the statement, and the record citation is page 11 of my brief, "I'm doing our usual 60/40." If you look in the judgment when the judgment deals with undivided property, any undivided property that may be out there, the judgment provides that that would be divided 60/40.

There's a strong indication she didn't even realize the impact. But the impact is clear. My brief contains an appendix, which is fully supported by the findings of fact and by the judgment itself, which demonstrates that this division was virtually 100 to zip. And ultimately my argument to the court is that that was an abuse of discretion, that that was not a fair and just division of the estate under these circumstances. But my suggestion for the jurisprudence is, that if you allow the tort judgments to be used, you are going to have a lot of these cases crying to be reviewed here, because it's not the way the traditional legal scheme handles them.

* * * * *

RESPONDENT

CAMPBELL: The real crux of this case does have to do with whether or not Texas recognizes the right of a spouse to sue for actual fraud in a divorce context. Generally speaking and in fact I think the way the statute defined fraud and defined punitive damages that constructive fraud will not support punitive damages.

HECHT: Do you agree that if one spouse in essences steals from the community, that the TC can restore that in the allocation of community property between the two spouses?

CAMPBELL: I think they can do that, and more.

HECHT: And render a judgment as counsel indicated?

CAMPBELL: Yes, I do.

HECHT: That would be enforceable against even the separate property?

CAMPBELL: Yes. And I think for years and years, the courts have granted money judgments not only to restore property, but also for _____. In other words, where there is not enough property in the estate and where you have a business for example to even out courts have granted a money judgment to even out the division. But we concede that we need to go further than that. And so in this case, you need to consider that this case is different from *Belz*. It's different from all of the other cases that *Belz* cites. What *Belz* says, and if it's correct, then we are out in the cold. Here's what *Belz* says, the way I read it: in a divorce context, you cannot have an independent action for actual fraud. Now just by its very nature, the relationship in a divorce is constructive fraud in the dissipation of assets.

HECHT: Why do you need it if the trial judge can do the same thing by dividing the community and rendering a judgment?

CAMPBELL: You need it for a couple of reasons. One, is punitive damages. The reason you need it for that, is this court in *Young* said, that you cannot use a division of property to punish. And when someone does something wrong in the divorce context, then the only way they can be punished, and we all know that punitive damage is a very salutary concept because it is how the courts control the actions of parties in divorce cases, and that's extremely important in this case. Because in this case the petitioner and his father conspired in the process of planning this divorce to move property from the community over to the father. And that's exactly what they did. When the husband was retiring, he turned his incentive money, which was about \$30,000 over to his father. His father put it in his account, and from there they used up this \$30,000, so that when the court came to divide up the property, the \$30,000 was gone.

In the process, the wife spent about \$25,000 in getting ready for the lawsuit. Someone might say, "well why in the world would you do that?" Well, I think one of the basic principles in family law and in any other case, is that everybody be honest, they be honest in their depositions, they be honest in dealing with the other side, they be honest in the court. And this case is replete with dishonesty. For example, in depositions, the Schlueter family all swore under oath: "Richard, the husband, owes the father money because of money that the father loaned to him over the years." And they had these little notes and they had little strips of paper, and this that and the other, and they said, "Each time we loaned Richard money, we made him sign a note." And then when we got to trial, the court had ordered them to turn those so-called notes over to us, so we had them examined. And we had a forensic expert who testified, "Those notes could not have been executed back when they said they were, they had to have been executed later." And so it turned up that at trial they came in with an estate tax planner who said, "Oh, yes, later on we advised them, we knew that they were keeping some kind of record in a notebook of these notes and all, but we advised them to reduce them to writing." And so they fabricated all of these notes, and we proved

that with a forensic examiner. So what we have here is a case of intentional outright fraud against not only the wife, but against the court.

HECHT: But you're saying the court can't take that into account in allocating the community?

CAMPBELL: I'm not saying they can't take it into account. In the *Twyman* case, I think this court was concerned about double recovery, and that is a problem. But the question is, Can a trial court separate that out? And if they can't then an appellate court can deal with it. Yes, they can take it into account, but they should not take it into account and at the same time grant a tort recovery.

HECHT: But could the TC say, "I think you lied to me the whole case, and therefore, I am going to give the other side 10% more of the community," just in so many words.

CAMPBELL: Yes, I think that might fly in the face of *Young*, because *Young* says we should not punish a person for wrongdoing. And that's why I think we need the punitive damages.

GONZALEZ: Was *Young* a no fault divorce?

CAMPBELL: No. As I recall it there was adultery, there was cruelty, and that's what the court said. In fact, I think the other side was arguing that fault should not have been considered at all. And in that case, the appellate court made the point of the fact that the jury had actually found adultery and cruelty in addition to other factors and that that justified the award in that case.

GONZALEZ: And this court said, you couldn't do that?

CAMPBELL: As a matter of fact in the *Young* case there was a disproportionate division. But in the same language they said, "You cannot use those actions to punish."

ENOCH: Why wouldn't it be an appropriate line to draw where the injury against the spouse is a separate injury and allow a tort claim for the separate injury of spouse as opposed to allowing an economic injury to the community be a basis for some sort of independent tort action? In other words, unless the wronged spouse has a claim for an action that would be a separate injury, either a personal injury or injury to the separate property of the spouse, why wouldn't it be a better rule to say, "All injuries that are claimed to the community by one spouse or the other simply be resolved by a redistribution of the community assets on a trial of the case," and just not get involved in the tort aspects of the injury?

CAMPBELL: I think that that limits the TC and the remedies that they can impose.

ENOCH: The only remedy they would be limited to would just simply be punitive damages?

CAMPBELL: Well it would be punitive and also I think it might be conspiracy. I'm not real sure about that. They have not raised that point in their appeals. But I think that on the issue of conspiracy, in other words, in this case the jury found that Hudson, the father, and the husband had conspired. And so the question is whether or not if you have only a constructed fraud will it also support the conspiracy? And we think here that there is certainly no reason why the wife cannot recover against the father for his wrongdoing in participating in the fraud.

ENOCH: I guess I wasn't talking about constructive fraud. Anything that would happen between the spouses on a claim for damage to community assets would not have any impact on a claim against a third party - someone who's a stranger to the marriage. If there was a fraud on the community, the wronged spouse has just as much right to sue the wrongdoer as the wrongful spouse.

CAMPBELL: But I think the problem with that is, and in our case we tried to distinguish that, we tried to distinguish Karen's part of the community as opposed to the community as a whole. The way this all came about, and I think where the court got confused when *Codel* was heard, that was the first time that you could theoretically have one spouse suing the other for intentional torts, and everybody concedes that actual fraud is an intentional tort. Well that was in 1977. In 1972, in the *Givens* case, the court there had held that in an insurance case, it was actually a probate case, but the court had to find there that the spouse who had been murdered or killed by the husband, that the deceased spouse had to have a cause of action for the survivors to sue the husband. And it was in that case where this doctrine of constructive fraud got started and the *Belz* case we think fell into the idea that every divorce case is constructive fraud because you have the fiduciary duty. In spite of the fact that the *Parker* case out of Ft. Worth said that you don't have a fiduciary relationship after you start a divorce where everybody is represented by attorneys there is no longer a fiduciary duty involved.

What I am trying to say is that a wrong by one spouse against another spouse in a marriage may deal only with that injured spouse's community property, because that may be all she has. But it's still an actual fraud, as it was in this case, and it still should support punitive damages, and it still should support a conspiracy.

HECHT: There's an argument that these kinds of actions cause additional strife in the divorce context. Why isn't that too expensive a price to pay?

CAMPBELL: I just think that that was taken care of when this court did away with the interspousal immunity. To me that was saying, "Look times have changed." And that's what the *Franco* case said, "Times have changed. Women now are not one in the same person as the man, the wife, the husband." And we've progressed beyond that and it is archaic for us to think that these wrongs that occur in marriage should somehow or another be treated differently than they would be if it was outside the marriage. Why should they be? Why should a wrong, an actual fraud, malicious mischief any kind of damage just to destroy.

I remember one old case where the husband flushed money down the toilet

and those kinds of things. Why can't we sue for those kinds of injuries just like you can against third parties? And that's what *Belz* would say. None of those cases can you sue the spouse because of the fiduciary relationship and that sort of insulates or isolates.

OWEN: Are we going to see a fraud in punitive damage claim in most divorces if we were to recognize this cause of action?

CAMPBELL: I don't really think so, because you don't have this kind of blatant action.

OWEN: What about when a couple knows that they are on the rocks and one couple cleans out the bank account and goes and hires a lawyer. Isn't that a fraud on the community? Wouldn't that fit within your definition of what happens?

CAMPBELL: I don't really think so, because in the first place even when you go to court and get a restraining order and restrain people from doing anything, using the property, one of the exceptions is clean it out for attorney's fees. Now the attorneys may have had something to do with getting that kind of a law passed, but that is one thing. But I do think again, the issue here is how much discretion do we leave with the TC's?

OWEN: If you allege fraud and you say, "here are my facts," don't you get a jury trial on fraud and punitive damages?

CAMPBELL: And you've still got to prove it.

OWEN: But you prove that one spouse cleaned out the bank account and went and rented an apartment and hired a lawyer, this is pre-filing, and then filed the lawsuit.

CAMPBELL: Now I'm not going to say that that couldn't happen. I can only say to you that in my experience in the law practice it hasn't happened. The same kind of scare thought came up when we opened the doors in *Bounds v. Caudel* and that has not created or generated any unusual increase in trials. And so I do think there is always going to be that issue and certainly it ought to be available. Why shouldn't it? Why shouldn't the wife not have a remedy if the husband goes and draws out \$25,000 out of the bank account and now she doesn't even have the money to...

OWEN: I thought you said the TC could take care of that in the division of property in several ways. But what I am talking about is fraud in a punitive damages issue on top of that.

CAMPBELL: Bear in mind that to prove actual fraud you've got to prove dishonesty. What's dishonest about a husband going to his bank account and taking the money out? You've got to prove deception.

OWEN: Well let's say it's a joint account and he needs her signature. He says, "Honey,

I'm going to go buy you a new car. Will you sign this so I can take the money out?" And she says, "Alright." And instead of doing that, he cleans out the bank account, moves out and hires a lawyer?

CAMPBELL: And why shouldn't it be? In the law people should be made to be honest. That's why we have punitive damages. People should not be allowed to tell the wife...In fact, that's what happened in the *Victory* case that you folks will probably be hearing. The husband told the wife a lot of things like that, and she believed him. Why shouldn't she? And if she's injured, why shouldn't she have a right to sue him for whatever if he in fact has damaged her? But you've still got if you believe in our system, that if that's wrong enough for a jury to find that it was dishonest, it was deceptive, then I think she ought to be entitled to it.

OWEN: Do you agree that under existing law the TC can enter a money judgment that's enforceable against the other spouse against their separate property?

CAMPBELL: Yes.

OWEN: Under what circumstances can a TC say: I don't think there's enough community property; therefore, I am awarding one spouse a money judgment that's enforceable against the other separate property?

CAMPBELL: No, I do not believe that you can do that. What these courts have said with regard to giving money judgments is either it's got to be to bring back property that's been removed wrongfully, or to even out the division of the property. So there's got to be something referable. No, I do not believe a court can go after the separate property of either spouse except you could enforce a judgment. If in fact this court allows an independent tort then, yes, I believe that that damage award could be used to levy. Unfortunately, in this case, and it's one of our findings of fact, the husband is judgment proof. He has no assets except his \$54,000 retirement that he got out of this case.

ENOCH: But that doesn't depend on a judgment for the independent tort. There could be a money judgment on the property division where there's a dollar judgment against the gentleman in this case and if she goes out and executes on that, she may be executing on some separate property. It's just that a divorce court has no authority to transfer title on that separate property?

CAMPBELL: That's correct. I agree with that.

HECHT: If *Belz* is the law are there jury issues in trying to determine proper allocation of the community?

CAMPBELL: I think it would be advisory questions.

HECHT: You wouldn't have to submit them to a jury?

CAMPBELL: Well you could submit them for an advisory.

HECHT: But on a fraud claim, you would be entitled to a jury?

CAMPBELL: Yes, that would be our position. And we think that that is the correct position.

* * * * *

REBUTTAL

FRIDAY: *Young* definitely does say that the court may consider fault. The opinion below explicitly says, "The court may consider the wasting of community assets in an unequal division." There's no question about that law.

Secondly, please be clear that this case is a constructive fraud case. Take time to go back and read the charge to the jury, the issues that were submitted. The definition of fraud that's given in the first issue is that fraud arises when a party transfers community property or expends community funds for the primary purpose of depriving the other spouse, etc. It is not a classic fraud case wherein a party makes its statement or fails to make a statement and the other party relies on that to their detriment.

I will go one beyond that. I will suggest to you that the distinction between the constructive fraud and the actual fraud is not really what's vital here. You are going to have to look at *Vickery* in this case, whether or not you've got it for review. The big difference in *Vickery*, and this goes to your question as to where do you draw the line? You draw the line where you've already drawn it, and that is on the one side personal injuries, injuries to the body, injuries to reputation, those injuries and harms that have always been defined as personal, and then on the other side economic torts. That's where it makes sense to draw the line.

In *Vickery*, the wife there pleaded and recovered a verdict for emotional harm. And on top of that recovered a verdict for exemplary damages. That's what really separates out *Vickery* from the case at bar. But to come back to the distinction I'm urging. This distinction lines up with all of our prior law. In the first place, it fits the statute. The family code, the old section 5.01 says, "That all property possessed during marriage is community property other than that which is separate property." And then you look to the separate property statute and it does create the special category of Recovery for Personal Injuries. This goes back to *Graham v. Franco*. Remember *Graham v. Franco* was wrestling with whether or not to bring recovery for personal injuries into the category of separate property. Up to that time it was considered that it was a chosen action, a cause of action, it was property that could be sold. And *Graham* decided that no, the better rule is to look at the personal injury damages as separate property. But in *Graham*, in quoting from the *Railway v. Freeman*, the court stated, "Mere personal torts dive at the party and are not assignable. Such are actions of slander, libel, assault and battery, false imprisonment, criminal conversations, seduction, etc. On the other hand, when the injury affects the estate rather than the person, when the action is

brought for damages to the estate and not for the injury to the person, personal feelings or character, the right of action could be bought or sold.”

Now clearly the court at the time of *Graham v. Franco* had in mind retaining this distinction between the economic harm on the other hand and the personal injury harm to the other side.

OWEN: If we were to agree with you and sent this case back to the TC...

FRIDAY: It has to be remanded. I suggest that perhaps there could be a rendition, but I have to back away from that. The court is entitled to consider the overall division of property in light of all of these factors.

OWEN: And the court can enter the same judgment that has been entered...

FRIDAY: I don't believe it could. My proposition to this court is that a 100% to 0% is an abuse of discretion in this case, and virtually in any case. Again, I will suggest to you that I'm not sure this trial judge intended to effect a 100% to 0%, judging from her comment on the record and judging from another provision of the judgment.

ABBOTT: If the trial judge were to do that, the standard of review would be abuse of discretion?

FRIDAY: Yes. To keep the traditional scheme frankly makes review easier and more appropriate. It's easier to look at the totality of the case rather than the kind of review you have in a tort scheme where you're on the softer legal sands of remittitur. I don't know whether there's going to be a flood of cases. But if you allow the economic tort to come in it's going to be more attractive for the trial lawyers to associates in these cases and to go for the big exemplary damage award, which may bear no relationship whatsoever to the overall size of the community estate, because once you've recognized this economic tort, you've let that once loose.

OWEN: Is it your position that the judgment against the husband's father in this case would be community or separate property?

FRIDAY: It's community.

OWEN: But the court could divide it subject to abuse of discretion on remand?

FRIDAY: There's no question. All of these damages were for replacement of the lost money. And the exemplaries as well have to be viewed as community, not only under the statutory scheme *Graham v. Franco*, and *Arnold v. Leonard*, but also you have the *Rosenbaum* opinion, commission appeals, Judge Hichman opinion adopted by this court which looked at this question of

the relationship of the exemplary damages to the actual damages and held that they take their character from the actual damages. All of these damages were for the economic loss. That's the appropriate way to do it.

BAKER: You are not saying that you are not entitled to get exemplary damages in an economic loss situation?

FRIDAY: I am saying that in a divorce case, that is not the existing legal scheme and that there is no reason for this court to depart from that legal scheme, that the existing legal scheme can take that into consideration in the overall division and in effect recognize it in some way.

BAKER: But you do agree that *Twyman* says that we do recognize tort with litigation by one spouse against another?

FRIDAY: No question. *Twyman* was a personal injury. *Twyman* was an intentional infliction of emotional harm.

OWEN: Let's assume there's a small law partnership. Two of the members are a husband and a wife, and the wife affirmatively defrauds her other partners. We've got actionable fraud and the individual partners sue the wife. In the meantime, the husband also sues the wife for divorce. Under your rationale, the other partners would have a cause of action against the wife for fraud but not the husband, is that correct? What do you do where you've got business relationships and others involved. Do we just say, Well because you are a husband and a wife there's no fraud here?

FRIDAY: The remedy would fit very neatly within the existing scheme. Suppose the other partners' suit resulted in a judgment which depleted the community estate. Clearly that's economic loss. Clearly that would be a factor to be considered in the overall.

OWEN: Do they get punitive damages? Does that husband who was a partner foreclose from getting punitive damages from his spouse?

FRIDAY: That's the way I would write the law. I would leave the court to its unequal division power and its money judgment power to arrive at a fair and just division, to take that into consideration and to compensate for it.