

Fraud and Waste Claims in Texas Divorces - 2024

by Greg Enos

The division of community property in a Texas divorce can be effected by claims of fraud made by one spouse against the other. “Actual fraud” involves intentional misrepresentation and “constructive fraud” involves secret or unauthorized transfers or expenditures of community funds. Sec. 7.009(c) of the Texas Family Code now provides a list of remedies for fraud.

1. Actual Fraud

Actual fraud is not often asserted in divorce cases because it is harder to prove than constructive fraud. The spouse alleging actual fraud has the burden of proof. On the other hand, an allegation of constructive fraud changes the burden of proof to the spouse who made the transfers to show those transfers were fair. Bad behavior that would constitute actual fraud will almost always also be constructive fraud and it is far easier to win a constructive fraud case.

Actual fraud involves dishonesty of purpose or intent to deceive and requires proof that a transfer of community property was made with the primary purpose of depriving the other spouse from having the use and enjoyment of the assets. *Horlock v. Horlock*, 533 S.W.2d 52, 55 (Tex. App. - Houston [14th Dist.] 1975, writ dismissed). Proving actual fraud requires evidence of the spouse's "subjective intent," but "[n]o 'dishonesty of purpose of intent to deceive' must be established" for constructive fraud. *Puntarelli v. Peterson*, 405 S.W.3d 131, 138 (Tex. App. - Houston [1st Dist.] 2013, no pet.).

Clarke v. Clarke, No. 08-23-0016-CV (Tex. App. – El Paso, Jan. 30, 2024)(mem. op.) is an example of fraudulent inducement, “a species of common law fraud,” being used in a divorce case. To recover for fraudulent inducement, a plaintiff must show that the defendant made a promise of future performance with no intention of performing, and that the promise induced her to enter a contract to her detriment. *Anderson v. Durant*, 550 S.W.3d 605, 614 (Tex. 2018). In *Clarke*, the wife claimed that her husband fraudulently induced her to withdraw \$22,000 from her retirement account by promising to give her a half interest in his separate property house. The money was used to pay a tax debt on the house. The husband did sign a deed to the wife but when the divorce was filed, the husband convinced the trial court to set aside the deed because it did not contain the language needed to convert separate property to community property. The opinion quoted *Spoljaric v. Percival Tours, Inc.*, 708 S.W.2d 432, 434 (Tex. 1986), "While a party's intent is determined at the time the party made the representation, it may be inferred from the party's subsequent acts after the representation is made." The husband's actions once the divorce case was filed supported the claim that he never intended to actually transfer half ownership of his separate property house to his wife.

Actual fraud is more likely to be asserted in a divorce case against a third party, such as a girlfriend or relative, who has helped a spouse transfer or hide community funds (see discussion below of third-party claims).

2. Constructive Fraud

Constructive fraud, waste, and breach of fiduciary duty all mean basically the same thing in the context of a divorce. *Ricks v. Ricks*, 169 S.W.3d 523, 526 (Tex. App. - Dallas 2005, no pet.). The court in *Puntarelli v. Peterson*, 405 S.W.3d 131, 138 (Tex. App. - Houston [1st Dist.] 2013, no pet.) said, “[a] fiduciary duty exists between a husband and a wife as to the community property controlled by each spouse. A presumption of constructive fraud, i.e., waste, arises when one spouse disposes of the other spouse’s interest in community property without the other’s knowledge or consent.”

Constructive fraud is presumed when one spouse during the marriage transfers community property outside of the community without the other spouse’s knowledge or consent. *Knight v. Knight*, 301 S.W.3d 723, 731 (Tex. App. - Houston [14th Dist.] 2009, no pet.).

“Transfer” can include transfer to a third party, excessive gifts to third parties, and use of community property to benefit a spouse’s separate estate. *In re Marriage of Notash*, 118 S.W.3d 868, 873 (Tex. App. - Texarkana 2003, no pet.).

A recent case summed up the breach of fiduciary duty, constructive fraud, and waste claims a spouse can make in a divorce:

“In the divorce context, a claim for a breach of fiduciary duty is the same as a claim for fraud on the community,” which is “a judicially created concept based on the theory of constructive fraud,” No dishonesty of purpose or intent to deceive must be established to prove constructive fraud. “A presumption of constructive fraud arises where one spouse breaches the fiduciary duty owed to the other spouse and disposes of the other spouse's one-half interest in community property without the other's knowledge or consent.”

A related concept is waste of community assets, which occurs when one spouse, dishonestly or purposefully with the intent to deceive, deprives the community estate of assets to the detriment of the other spouse. “Evidence of a spouse using excessive funds without the other spouse's consent supports a waste finding.” “Expenditures for the benefit of a paramour also establish waste,” as do disbursements of community funds to relatives and friends, “Further, while waste claims are often premised on specific transfers or gifts of community property to a third party, a waste judgment can also be sustained by evidence of community funds unaccounted for by the spouse in control of those funds.”

Banister v. Banister, No. 03-21-00517-CV (Tex. App. – Austin, June 13, 2023)(mem. op.).

Once alleged by the complaining spouse, the responding spouse carries the burden of rebutting the presumption of constructive fraud by proving the fairness of the transaction. *See Mazique v. Mazique*, 742 S.W.2d 805, 807 (Tex. App.—Houston [1st Dist.] 1987, no writ).

The factors that the court can consider in determining whether or not a spouse's actions constitute constructive fraud are:

1. the relationship between the spouse and the recipient;
2. the size of the gift or transfer in relation to the total size of the community estate;
3. the adequacy of the estate remaining to support the other spouse in spite of the gift or the transfer; and
4. any special justifying factors for the gift or transfer.

Massey v. Massey, 807 S.W.2d 391, 402 (Tex. App. - Houston [1st Dist.] 1991), *writ denied*, 867 S.W.2d 766 (Tex. 1993) (per curiam).

No dishonesty of purpose or intent to deceive need be established for the Court to find constructive fraud. *Puntarelli v. Peterson*, 405 S.W.3d 131, 138 (Tex. App. - Houston [1st Dist.] 2013, no pet.).

3. The Presumption of Constructive Fraud

A presumption of constructive fraud arises when a spouse provides evidence of:

- a. Transfers, withdrawals, or unexplained decreased in account balances; and
- b. The spouse alleging fraud testifies he or she did not consent or know about the transactions. It helps if the spouse testifies that he or she did not have access to the account or see the statements and that the other spouse controlled the finances.

There is no requirement that the transfer, gift, or disposition was secret. The presumption may arise even when the other spouse has knowledge of the disposition, so long as he or she did not consent. *Everitt v. Everitt*, No. 01-11-00031-CV (Tex. App. - Houston [1st Dist.] 8/31/2012, no pet.)(mem. op.)(citing *Zieba v. Martin*, 928 S.W.2d 782, 790 (Tex. App. - Houston [14th Dist.] 1996, no writ).

In *Stallworth v. Stallworth*, No. 13-21-00251-CV, (Tex. App.—Corpus Christi—Edinburg, 2/2/2023, no pet. h.)(mem. op.), the husband introduced bank statements showing \$33,951 of transfers to an account solely in wife's name which at the time of trial had a balance of \$1,605.24. The husband testified that he knew nothing of the transfers or their purpose and that he put money in the joint account for his wife to pay bills. These facts were enough to shift the burden to the wife to prove the fairness in her disposing of community assets.

Vedullapalli v. Velagandula, 05-22-01248-CV (Tex. App. – Dallas, June 28, 2024)(mem. op.) involved a husband who had control of a Merrill Lynch IRA which decreased about \$71,483.33 in value in seven months right before trial. Once the wife testified that she had no access to the account and she proved the sudden decrease in value right before trial (using the husband's various sworn inventories), the burden shifted to the husband to rebut the presumption of fraud.

In *Kazmi v Kazmi*, No. 03-22-00330-Cv (Tex. App. – Austin, Nov. 17, 2023)(mem. Op.), bank records were admitted showing large transfers and withdrawals by the husband in the years before the divorce. The wife testified that she had no access to the account, never saw the bank statements and never went to the bank to withdraw or transfer money. This was enough to support the presumption of fraud.

For example, in *Cantu*, when there was a discrepancy between income recorded in the books of Husband’s pharmacy verses what actually flowed through the bank, the \$2,322,955 shortage created a presumption of fraud on the community because the accounts had been under the husband’s control. He was required to provide an explanation of the difference to rebut the presumption of the fraud, which he could not fully do. *Cantu v. Cantu*, 556 S.W.3d 420, 427 (Tex. App. - Houston [14th Dist.] 2018, no pet.).

4. Disproving the Presumption of Community Fraud

Once the presumption of constructive fraud arises, the spouse accused of constructive fraud has the burden to prove that the transfer was “fair.” *Wright v. Wright*, 280 S.W.3d 901, 911-12 (Tex. App. - Eastland 2009, no pet.).

Vedullapalli v. Velagandula, 05-22-01248-CV (Tex. App. – Dallas, June 28, 2024)(mem. op.) is an example of how the spouse accused of constructive fraud must be prepared at trial to disprove the allegation. In this divorce, the husband had control of a Merrill Lynch IRA which decreased about \$71,483.33 in value over seven months. Once the wife testified that she had no access to the account and then proved the sudden decrease in account’s value, the burden shifted to the husband to rebut the presumption of fraud. The husband’s testimony that he had not made any withdrawals from the IRA and that the drop in value was due to market conditions was not enough for the trial court or the court of appeals. It was noted that the husband never admitted statements explaining the decrease in value in the IRA. The trial court’s finding of constructive fraud was upheld and the reconstitution of the community estate in the amount of \$71,483.33 was approved. In retrospect, the husband should have come to trial with his monthly IRA statements and evidence of the general decline in most U.S. stocks from September 2021 to March 2022.

The husband in *Clarke v. Clarke*, No. 08-23-0016-CV (Tex. App. – El Paso, Jan. 30, 2024)(mem. op.) wrote two checks totaling \$11,300 to his niece and he said those checks paid off a cash loan given to him by his niece for attorney’s fees. The husband did not produce evidence of the loan or payment to his attorney or explain why he needed the loan to begin with. The Court of Appeals held that the trial court was within its discretion to disbelieve the husband’s testimony and so he was unable to rebut the presumption of fraud. Presumably, the husband should have called his niece as a witness, proven the transfer of funds from the niece to him and the payment to the attorney, and explained why he needed the loan.

Rue v. Rue, No. 03-22-00758-CV (Tex. App. – Austin, Octo. 6, 2023)(mem. op.) involved different financial transgressions by the husband, all of which were held to be constructive fraud:

- \$100,000 from the sale of a residence went to settle an IRS tax debt which the husband had

incurred without the wife's knowledge (she signed tax returns each year and he falsely told her he filed the returns when he did not).

- \$95,000 from the sale of real estate was used to pay off the above IRS debt and a second mortgage that husband had taken without wife's consent (even if she signed the second mortgage papers, she was unaware of the terrible financial situation the husband had put the family in).
- \$257,000 taken from retirement and brokerage accounts without explanation.
- \$20,000 in community funds used to pay off a line of credit that husband took out without the wife's knowledge.
- \$45,000 in credit card debt paid off with community funds because the wife did not know the husband had incurred the debt.
- Took \$6,000 from children's savings accounts.

In *Kazmi v Kazmi*, No. 03-22-00330-Cv (Tex. App. – Austin, Nov. 17, 2023)(mem. op.) the trial court found that the husband depleted the community estate of \$163,377 through constructive fraud and awarded the wife a \$99,125 judgment to compensate her. Bank records were admitted showing large transfers and withdrawals by the husband in the years before the divorce. The wife testified that she had no access to the account, never saw the bank statements, and never went to the bank to withdraw or transfer money. This was enough to support the presumption of fraud. The husband and his mother testified that the transfers were made repay the husband's parents for debts that the couple or the husband individually owed. This testimony without documentation was found to be insufficient to rebut the presumption of fraud. The Court of Appeals stated:

[Wife] responds that the record supports the district court's finding that he failed to rebut the presumption. We agree with [Wife]. The district court concluded that [Husband] failed to rebut the presumption of fraud, referencing [Husband's mother]'s testimony "that he was not paying household expenses" through the transfers but that [Husband] "would just give her some money to spend, like he does all the time." [Husband's mother] and [Husband] both testified that [Husband] was repaying his parents for certain expenditures, and [Husband] provided an itemized list of some of the expenditures in his affidavit. Even if using community funds to repay his parents for those expenditures would be legitimate, the district court was not required to ignore that the transfers stopped when the parties exchanged discovery in 2019. [Husband's mother] confirmed that they decided not to continue with the transfers because [Husband] "thought that [the] attorneys don't look at it nicely. They think that I'm - you know, what is happening to the money?" Now, they "make two payments for one credit card." [Husband's mother]'s testimony supports the district court's finding that the transfers were not legitimate uses of community funds.

5. Examples of Constructive Fraud

Examples of spousal misbehavior which have been held to be constructive fraud include:

- The husband's gifts to the educational funds for the children of the marriage were held to be constructive fraud, even though wife knew, but was not fully informed, of the gifts. *In re*

McCurdy's Marriage, 489 S.W.2d 712 (Tex. Civ. App.—Amarillo 1973, no writ).

- The husband used community property to fund a trust for his son from a former marriage and the gift was held to be constructive fraud because the husband failed to meet his burden and prove that the disposition was fair to Wife. *Grant v. Grant*, No. 01-98-00352-CV, (Tex. App. - Houston [1st Dist.], Nov. 24, 1999, no writ)(mem. op.).
- The husband replaced wife as beneficiary of life insurance policy with his girlfriend. The insurance proceeds were held to be community property and the change in beneficiary was held to constitute constructive fraud on the wife's share of the community estate in the absence of a showing of "special justifying factors." *Givens v. Girard Life Ins. Co. of America*, 480 S.W.2d 421 (Tex. Civ. App.—Dallas 1972, writ ref'd n.r.e.)
- The naughty husband went to Puerto Rico with approximately \$53,000, but he testified that he lost some of it gambling and that he gave some of it away, that he spent it very foolishly and that at the time of the trial he did not have any of it. The Court held that "...in the light of the undisputed facts in this case the trial court could not make a fair and just division of the remaining community assets without taking into account Appellant's profligate loss of a large portion of the community estate." *Reaney v. Reaney*, 505 S.W.2d 338, 340 (Tex. Civ. App. - Dallas 1974, no writ).
- During a twenty-five-year marriage, the husband engaged in numerous extramarital affairs which he funded with community funds and he paid for trips, meals, gifts, and hotels for the third parties with community funds. No accounting of the gifts was made to the wife. The trial court found the husband had committed constructive fraud and the ruling was upheld by the Court of Appeals. *Mazique v. Mazique*, 742 S.W.2d 805 (Tex. App. - Houston [1st Dist.] 1987, no writ).
- Wife used community funds to gift the parties' daughter a house for \$279,361 without the husband's consent or agreement. *DiBassie v. DiBassie*, No. 09-20-00287-CV (Tex. App.—Beaumont 11/17/2022, pet. denied)(mem. op.).
- Wife paid her boyfriend to renovate the community property house without husband's consent. Wife told the husband that the boyfriend was staying in a rental property for free to pay him for his services, but two days before closing the boyfriend produced a contract the wife had signed and filed a lien of \$72,463 against the property, which was paid at closing. *Banister v. Banister*, No. 03-21-00517-CV (Tex. App. – Austin, June 13, 2023)(mem. op.).

An example of gifts to children from a prior marriage which were held to not be constructive fraud was *Marshall v. Marshall*, 735 S.W.2d 587 (Tex. App.—Dallas 1987, writ ref'd n.r.e.) (wife's claim of constructive fraud for husband's gifts to his children from a prior marriage was denied where gifts were equal to 11 percent of the husband's total earnings during their brief marriage, and where wife was advised of the gifts and although she did not actively consent, she raised no objection to the gifts at the time they were made).

6. Puntarelli v. Peterson - “Where Did All Those Earnings Go?”

In *Puntarelli v. Peterson*, 405 S.W.3d 131 (Tex. App. - Houston [1st Dist.] 2013, no pet.), the wife asked the age-old question “where did all of the money he earned go?” The wife was awarded a \$196,000 judgment for wasting community funds because the husband could not account for how he spent his significant income during the five years this informal marriage/divorce case was pending. **The important holding from this case is this – the wife did not have to prove any specific improper transfers of community funds. The wife merely had to show that the husband’s expenses were much less than his income and then the burden shifted to the husband to show where the money went.** Proving how one spent money years ago is often not easy, but failure to do so can result in a large judgment, as happened here. Of course, the husband did not help himself by failing to disclose his primary bank account in his sworn inventory or by failing to support the common law spouse during the pendency of the case. The Court of Appeals stated (citations omitted):

While waste claims often are premised on specific transfers or gifts of community property to a third party, a waste judgment can be sustained by evidence of community funds unaccounted for by the spouse in control of those funds.

....

The trial evidence that Puntarelli failed to disclose at least one bank account containing community funds into which his income was deposited, along with his failure to account for or explain the depletion of the community funds in his control over the five-year pendency of the divorce proceedings spent without Peterson’s consent was sufficient to shift the burden to Puntarelli to establish the fairness of his use of these community funds. He did not attempt to meet this burden.

Because we have rejected Puntarelli’s argument that Peterson needed to identify specific transfers of community property (rather than identifying unaccounted-for community funds in Puntarelli’s sole control) to shift the burden to Puntarelli to show the fairness of his use of those funds in his control, and because Puntarelli does not otherwise challenge the trial court’s waste judgment or argue that he established his depletion of community assets was fair to Peterson, we hold that the trial court’s waste judgment was within its discretion.

So, a spouse in a divorce can compare the other spouse’s income to his or her expenses for a specific time period and if there is a significant gap between income and expenses, allege fraud and then sit back and see if he or she can prove how the funds were spent. One tool in such cases is the Financial Information Statement submitted early on in a case at the hearing on temporary orders. If the husband’s FIS shows his monthly expenses are \$6,200 and he brings home \$11,000 a month and yet has no money in savings, the wife should allege constructive fraud and then the husband has the burden to prove how the money was spent. In such a case, the attorney for the husband could use bank and credit card statements and a chart summarizing expenditures to prove the money was all spent for legitimate purposes.

7. Fraud Can Be a Jury Issue

The *Texas Pattern Jury Charges - Family 2024* contains suggested jury instructions and questions related to constructive fraud. For example, this is the suggested instruction and question on constructive fraud by a spouse against the community estate:

206.4A

A spouse may make moderate gifts, transfers, or expenditures of community property for just causes to a third party. However, a gift, transfer, or expenditure of community property that is capricious, excessive, or arbitrary is unfair to the other spouse. Factors to be considered in determining the fairness of a gift, transfer, or expenditure are—

1. *The relationship between the spouse making the gift, transfer, or expenditure and the recipient.*
2. *Whether there were any special circumstances tending to justify the gift, transfer, or expenditure.*
3. *Whether the community funds used for the gift, transfer, or expenditure were reasonable in proportion to the community estate remaining.*

206.4B

QUESTION 1

Was the transfer made by SPOUSE A to THIRD PARTY fair?

Answer “Yes” or “No.”

Answer: _____

If you answered “No” to Question 1, then answer Question 2. Otherwise, do not answer Question 2.

QUESTION 2

State in dollars the value, if any, by which the community estate of was depleted as a result of the transfer made by SPOUSE A to THIRD PARTY.

Answer: \$ _____

8. Remedies for Fraud Against a Spouse

The Texas Supreme Court in *Schlueter v. Schlueter*, 975 S.W.2d 584 (Tex. 1998) held that there is no independent tort cause of action between spouses for damages to the community estate. In *Schlueter* the husband transferred various community assets to his father shortly before he filed for divorce. The wife brought independent tort claims against her husband and father-in-law, seeking

damages for fraud, breach of fiduciary duty and conspiracy in her counterclaim for divorce. Based on favorable jury findings the trial court ordered a disproportionate division of the community estate in favor of the wife and rendered judgment for the wife against the husband and his father for actual and exemplary damages. Because a wronged spouse has an adequate remedy for fraud on the community through the “just and right” property division upon divorce, the Court reversed the tort judgment against the husband and remanded the case for a new division of the marital estate.

The Texas Family Code now provides specific guidance on how a divorce court can remedy fraud committed by one spouse on the other.

Section 7.009 states:

7.009. FRAUD ON THE COMMUNITY; DIVISION AND DISPOSITION OF RECONSTITUTED ESTATE

(a) In this section, “reconstituted estate” means the total value of the community estate that would exist if an actual or constructive fraud on the community had not occurred.

(b) If the trier of fact determines that a spouse has committed actual or constructive fraud on the community, the court shall:

(1) calculate the value by which the community estate was depleted as a result of the fraud on the community and calculate the amount of the reconstituted estate; and

(2) divide the value of the reconstituted estate between the parties in a manner the court deems just and right.

(c) In making a just and right division of the reconstituted estate under Section 7.001, the court may grant any legal or equitable relief necessary to accomplish a just and right division, including:

(1) awarding to the wronged spouse an appropriate share of the community estate remaining after the actual or constructive fraud on the community;

(2) awarding a money judgment in favor of the wronged spouse against the spouse who committed the actual or constructive fraud on the community; or

(3) awarding to the wronged spouse both a money judgment and an appropriate share of the community estate.

So, assume that the current value of the community estate is \$400,000 at the time of divorce trial and the court finds that the wife committed constructive fraud in the amount of \$60,000 against the community estate. The “reconstituted” estate is thus worth \$460,000.

The judge's options are:

1. Award the husband more than 50 % of the community estate while “pretending” the wife still has the \$60,000, which will result in more real assets being awarded to the husband;
2. Awarding the husband a judgment against the wife for some fair portion of the \$60,000. Remember, the wife wasted community funds so she also wasted money that belonged to her as well, so the husband would almost certainly not get a judgment for the full \$60,000.
3. Award both a money judgment and a disproportionate share of the community estate to the husband.

9. Constructive Fraud on the Property Division Spreadsheet

If, for example, a spouse wasted funds on a paramour or cannot account for a large amount of cash, list that as an asset (“funds wasted by Wife” or “cash unaccounted for”) and then award the asset to the spouse who wasted the money or cannot account for the cash. This will have the effect of giving more real, existing assets to the other, injured spouse. You are in effect pretending the spouse who wasted the funds still has the money and so he or she will actually get less in the final division. An example of showing fraud or waste on the property division spreadsheet would be:

Property or Debt	Value	Husband	Wife
Cash taken by wife not accounted for	\$60,000.00		\$60,000.00

10. Claims Against Third Parties

A. Tort Claims

A wife cannot sue her husband for fraud or breach of fiduciary duty as a separate tort in a divorce suit per *Schlueter*. However, some claims against third parties are allowed in divorce cases as a result of a spouse transferring community assets to a family member or paramour. In *Chu v. Hong*, 249 S.W.3d 441, 445 (Tex. 2008), the Texas Supreme Court stated, “...if a third party steals community property, surely either spouse or both can seek recovery in tort for it.”

The Texas Supreme Court in *Schlueter* affirmed the wife's judgment against her former father-in-law for civil conspiracy for helping his son transfer community funds to his father just before the divorce case was filed. The court stated:

With regard to the causes of action against Mr. Schlueter's father, he has not argued that these separate and independent tort claims against him as a third-party defendant should also be abolished. Therefore, we do not reach that issue. We note that the trial court's \$12,850 judgment of actual damages against Mrs. Schlueter's father-in-law was awarded to the community estate. That judgment represents an asset returned to the community estate, making it monetarily whole. Therefore, the trial court, in its just and right division, may not

effect a disproportionate property division solely to make up for that formerly lost asset. However, as we have already discussed, the trial court may take into account Mr. Schlueter's conduct that resulted in a defrauding of the community estate.

975 S.W.2d at 590.

The Texas Supreme Court in *Chu v. Hong* did hold that a third party cannot be sued for conspiracy or assisting a spouse in violating his fiduciary duty to his wife in a situation where the spouse cannot be sued for the same tort because of *Schlueter*. However, in that case, the third-party defendants did not receive the lost community funds. There, the husband sold a community property business without his wife's signature and then sent the sales proceeds to his parents in Korea. The wife sued the couple who purchased the business and their lawyer for conspiring with her ex-husband to defraud the community estate. The Supreme Court stated:

But the question presented here is a narrower one: whether a third party can be held liable in tort when community property is taken by one of the spouses. We answered that question in the negative in *Cohrs v. Scott*.¹ There, a divorcing wife settled all her property claims against her husband, and then sought damages against a third party for helping her husband transfer two cars to a mistress. This Court held that "the fraud having been initiated and carried out mainly by the husband, [the wife] must look primarily to him and his property to right the wrong.

....

Further, if a spouse cannot be liable for tort and punitive damages in a case like this, it is unclear under what theory co-conspirators can. [Wife] argues that [Husband's] fraud against the community estate was still an unlawful act, even though it could only be addressed in the just-and-right property division. But co-conspirators are each responsible for the damage the conspiracy caused; if [Husband's] liability is limited to returning the property or adjusting the community division, the liability of co-conspirators should be as well. Moreover, if one spouse can enlarge the community estate by suing the other's relatives, many acrimonious divorce cases will undoubtedly become more so. **That may be necessary when relatives have community property in their hands**; but when they do not, little is gained by adding third parties if the property can be restored through orders between the former spouses.

....

"Because [Wife] has no tort claim against her former husband under Texas community-property law, she has no conspiracy claim against Chu [the attorney for the couple who bought the community property business] for conspiring in such a tort.

Chu v. Hong, 249 S.W.3d 441, 445-6 (Tex. 2008)(emphasis added).

The Texas Supreme Court in the *Cohrs v. Scott*, 338 S.W.2d 127, 133 (Tex. 1960) cited in *Chu v. Hong* noted that there were cases holding "that where a husband perpetrates a fraud upon the wife by the making of excessive gifts of community property to third persons with a fraudulent intent, she is

¹ 338 S.W.2d 127, 133 (Tex. 1960).

entitled to recover against the property of the husband and against third[-party] possessors." *Cohrs*, 338 S.W.2d at 133. The *Cohrs* court distinguished such cases from the situation before it because the divorced parties in that case before had reached a settlement of the community-property division before the wife sued the ex-husband's mistress. The court said, "The trial court here, in dividing the community property, and the parties in agreeing to such settlement, presumably compensated Mrs. Scott for any loss she may have suffered"

West v. West, 01-11-00051-CV (Tex. App. - Houston [1st Dist.] 2/9/2012)(mem. op.) affirmed a wife's recovery against her husband's parents for conspiring with her husband to defraud her out of community property. The wife alleged that her husband and her former in-laws tricked her into believing that she was making payments on a property she and her husband were buying when in fact the parents owned the property and no sale had actually taken place. The Houston First Court of Appeals cited *Schlueter* and *Chu v. Hong* and held:

Parents who conspire with their children to perpetrate a fraud on the community estate of the children and their spouses may be held liable in a divorce action to the extent of the property wrongfully obtained by the parents. Generally, the remedy available is limited to recovery of the fraudulently obtained property or damages limited to the value of the property transferred.

A defrauded spouse in a divorce would sue a third party, such as his or her spouse's paramour, business partners, or relatives, for fraud, conversion and conspiracy.

The elements of conversion are:

1. The plaintiff owned, possessed, or had the right to immediate possession of personal property;
2. The defendant wrongfully exercised dominion or control over the property;
3. The plaintiff suffered injury.

Burns v. Rochon, 190 S.W.3d 263, 267-8 (Tex. App. - Houston [1st Dist.] 2006, no pet.). Funds held in a bank account can be personal property subject to conversion. *Estate of Townes v. Townes*, 867 S.W.2d 414, 419 (Tex. App. - Houston [14th Dist.]1993, writ denied).

The elements of conspiracy are:

1. The defendant and one or more persons (i.e. - the other spouse);
2. Had a meeting of the minds to take an action;
3. The action was unlawful or constituted an intentional tort, such as fraud or conversion;
4. One of the members of the group committed the unlawful, overt act to further the action; and
5. The action proximately caused injury to the plaintiff.

Chon Tri v. J.T.T., 162 S.W.3d 552, 556 (Tex. 2005).

In a suit against a third party, the injured spouse might allege common-law fraud, fraud by deception or statutory fraud (involving stock or real estate).

Common-law fraud requires proof of:

1. The defendant made a material and false representation to the plaintiff;
2. The defendant knew the representation was false or made the representation recklessly, as a positive assertion, without knowledge of its truth;
3. The defendant made the representation with the intent that the plaintiff act on it;
4. The plaintiff relied on the representation and suffered injury.

Statutory Fraud is based on Texas Business & Commerce Code Sec. 27.01 and must involve stocks or real estate. Statutory fraud is basically the same as common-law fraud except the plaintiff does not have to prove that the defendant knew the representation was false or made the representation recklessly. *Henning v. One West Bank*, 405 S.W.3d 950, 963 (Tex. App. - Dallas 2013, no pet.).

To establish fraud by nondisclosure, appellants must prove:

1. the defendant failed to disclose facts to the plaintiff,
2. the defendant had a duty to disclose those facts,
3. the facts were material,
4. the defendant knew the plaintiff was ignorant of the facts and the plaintiff did not have an equal opportunity to discover the facts,
5. the defendant was deliberately silent when it had a duty to speak,
6. by failing to disclose the facts, the defendant intended to induce the plaintiff to take some action or refrain from acting,
7. the plaintiff relied on the defendant's nondisclosure, and
8. the plaintiff was injured as a result of acting without that knowledge.

Horizon Shipbuilding, Inc. v. Blyn II Holding, LLC, 324 S.W.3d 840, 850 (Tex. App. - Houston [14th Dist.] 2010, no pet.).

B. Constructive Trust

A constructive trust is an equitable remedy created by the courts to prevent unjust enrichment or to compensate the victim of a breach of a fiduciary or confidential relationship. *In re Marriage of Loftis*, 40 S.W.3d 160 (Tex. App.—Texarkana 2001, no pet.). The court will impose a constructive trust over an asset fraudulently conveyed if it is unique or if the estate is inadequate and the asset must be returned to the estate to effect an equitable division. *Hudspeth v. Stoker*, 644 S.W.2d 92 (Tex. App.—San Antonio 1982, writ ref'd). *Hudspeth v. Stoker*, involved a husband who changed the life insurance beneficiary from his former wife to his new wife and so violated his legal duty under the divorce decree, and the appeals court found that the trial court was justified in imposing constructive trust on the proceeds of the policy.

11. Diversion of Community Opportunity

What if the husband owns a separate property corporation that owns several bars and during the marriage he uses that entity to start a new restaurant when he could just have easily used community property and made the restaurant a community asset? A legal theory sometimes suggested by clever lawyers is called “Diversion of Community Opportunity” or the “Community Opportunity Doctrine.” This theory would suggest that the husband in the above example breached his fiduciary duty to his wife and therefore the loss of that new valuable asset to the community estate should be considered in the property division. No Texas cases have adopted that theory and in fact, one older case, *Holloway v. Holloway*, 671 S.W.2d 51, 59-60 (Tex. App. - Dallas 1983, no writ), appears to have rejected that argument.

Here is what one very smart lawyer wrote about this theory over a decade ago and his analysis seems to hold true today:

In Holloway v. Holloway, 671 S.W.2d 51, 59-60 (Tex. App. – Dallas 1983, no writ), the wife accused the husband, as manager of the community estate, of unjustly enriching his separate estate by diverting community funds into separate corporations. Specifically, the wife argued that the husband breached a fiduciary duty owed to the community estate by using separate funds to capitalize the corporations when there were adequate funds in the community estate. *Id.* at 59. However, the Dallas Court of Appeals refused to agree with the wife, stating that in engaging in a new and speculative venture and borrowing funds for that purpose, a married entrepreneur may well consider whether the risk is one that should properly be undertaken by himself alone without jeopardizing the assets of the community estate. *Id.* If the venture turns out to be successful, as it did in *Holloway*, the Dallas appellate court determined that the husband could not be held guilty of breach of a fiduciary duty in the absence of evidence of an intent to defraud the wife. *Id.* at 59-60.

Holloway has been criticized as contrary to the basic principles of the community property system. See, Donald R. Smith, *Diversion of Community Opportunity*, *ADVANCED FAMILY LAW COURSE* (1986). Further, it has been suggested that the theory of “diversion of community opportunity” is meritorious, and should be investigated by the practitioner in the proper case. Cheryl L. Wilson, *Breach of Fiduciary Duty*, p. M-7, *16TH ANNUAL MARRIAGE DISSOLUTION INSTITUTE* (1993). It should be noted, however, that there appears to be no reported Texas case recognizing the diversion of community property theory.

Ted Terry, et al, “Fiduciary Duties of Spouses and Non-Physical Torts” presented at the Annual Meeting of International Academy of Matrimonial Lawyers in March 2000.

Justice Anne McClure in *Sprick v. Sprick*, 25 S.W.3d 7, 15, note 3 (Tex. App. – El Paso 1999, pet. denied) mentioned the doctrine but it was clearly an aside in her concurring opinion:

The community opportunity doctrine derives from the corporate opportunity doctrine and stands for the proposition that a spouse has an obligation to maximize the community estate by taking advantage of an opportunity to invest in a lucrative venture using community, rather than separate, funds.

Texas clearly recognizes the corporate opportunity doctrine, as do most other states. *Imperial Group (Texas), Inc. v. Scholnick*, 709 S.W.2d 358, 365 (Tex. App. – Tyler 1986, writ ref’d n.r.e.); *Alexander v. Sturkie*, 909 S.W.2d 166 (Tex. App. – Houston [14 Dist.] 1995, writ denied).

The corporate opportunity doctrine has been explained as follows:

The corporate opportunity doctrine embodies one of the fiduciary duties owed by directors and officers (and sometimes shareholders) to their corporation. It is a duty of disclosure under the concept of duty of loyalty. Although the doctrine itself requires a fact intensive analysis, the theory behind it is simple. The corporation can act only through its human agents. When an opportunity within the corporation's line of business, or its reasonable expansion or expectancy, comes to an agent's attention, the agent must afford the corporation first crack at it. For example, if a corporation is in the business of buying and selling real estate, and its president (or a director or perhaps a major shareholder) learns of a tract of land that can be bought for a song and flipped at a profit, it is incumbent on the agent to disclose to the corporation the possibility of cashing in on this fantastic opportunity. If the corporation declines, perhaps because the transaction may be viewed by its board as more risky than fantastic, the agent may then seize it personally for better or worse.

Parchman, “Fiduciary Duties: Renouncing the Corporate Opportunity Doctrine,” *Business Law Today*, October 2011.

The “Corporate Opportunity Doctrine” is founded on the fiduciary duty owed by directors and officers to the corporation. Texas recognizes that spouses during a marriage owe each other a fiduciary duty. *Marsh v. Marsh*, 949 S.W.2d 734, 745, n. 4 (Tex. App. – Houston [14th Dist.] 1997, no writ). It certainly seems arguable, therefore, that what is good for corporations should also be used to protect spouses. Thus, the violation of the “Community Opportunity Doctrine” should be a viable claim in some divorces.

12. Fraud is a Factor in Spousal Maintenance

Fraud can be a factor for the trial court to consider in determining the amount and duration of post-divorce spousal maintenance.

Texas Family Code Sec. 8.052 states:

A court that determines that a spouse is eligible to receive maintenance under this chapter shall determine the nature, amount, duration, and manner of periodic payments by considering all relevant factors, including:

(6) acts by either spouse resulting in excessive or abnormal expenditures or destruction, concealment, or fraudulent disposition of community property, joint tenancy, or other property held in common;