

CHAPTER FOUR

Financial Aspects of Marriage

MOST PROPERTY THAT IS ACQUIRED DURING THE MARRIAGE is considered marital or community property. For example, wages earned by the husband and wife during marriage generally are considered marital property. If one or both spouses buy a house or establish a business during the marriage, that usually will be marital property, particularly if the house or business is purchased with the husband's and wife's earnings.

Separate property is property that each spouse owned before the marriage. Separate property also includes inheritances and gifts (except perhaps gifts between spouses) acquired during marriage. During and after the marriage, each spouse may keep control of his or her separate property. Each spouse may buy, sell, and borrow money on his or her separate property. Income earned from separate property, such as interest, dividends, or rent generally are classified separate property. However, in some states that recognize community property, these profits may become marital property.

Separate property can become marital property if it is mixed with marital property. If, for example, a wife owned an apartment building before the marriage and she deposited rent checks into a joint checking account, the rent money probably would become marital property, although the building is likely

to remain the wife's separate property as long as she kept it in her name. If the wife changed the title on the building from her name alone to the names of both herself and her husband, that probably would convert the building into marital property. In addition, if one spouse put a great deal of work into the other spouse's separate property, that could convert the separate property into marital property, or it could give the spouse who contributed the work a right to some form of payback. [Chapter 9](#) will discuss how courts divide marital property in a divorce.

A husband and wife may own property together during the marriage. This occurs automatically in **community property states**. Ten states--Alaska, Arizona, California, Idaho, Louisiana, Nevada, New Mexico, Texas, Washington, and Wisconsin, as well as Puerto Rico--use the community property system. These jurisdictions hold that each spouse shares equally the income earned and property acquired during a marriage. This is true even if one spouse supplied all the income. In the other states, spouses generally share property under one of the following three forms of co-ownership:

- **Joint tenancy.** A form of ownership that exists when two or more people own property that includes a **right of survivorship**. Each person has the right to possess the property. If one partner dies, the survivor becomes the sole owner. Any two people--not just spouses--may own property as joint tenants. A creditor may claim the debtor's interest in joint tenancy property.

- **Tenancy by the entirety.** Allowed only in some states, tenancy by the entirety is a type of co-ownership of property by a husband and wife. Like joint tenancy, it includes a right of survivorship. But a creditor of one spouse may not **attach** (seize) the property. Each party usually must consent to the sale of the property. Divorce may result in a division of the property.
- **Tenancy in common.** This form of co-ownership gives each person control over his or her share of the property, and the shares need not be equal. The law does not limit tenancy in common to spouses. A tenancy in common has no right of survivorship; when one spouse dies, his or her share passes to the heirs, either by will or state laws.

Tenancy rules vary from one state to another. Some tenancies are complex and must be created in a precise manner; otherwise the courts may not enforce them.

Debts

Husbands and wives may be responsible for debts incurred by the other depending on the nature of the debt as well as where the couple resides. If both husband and wife have co-signed for the debt, both will be responsible for paying it. For instance, assume the husband and wife apply together for a charge card. If both sign the application form and promise to pay the charge bills, both will be responsible for paying off the balance to the credit card company or store, even if only one of them made the purchases and the other disapproved.

Similarly, if a husband and wife co-sign on a mortgage for a home, both of them are potentially liable to the mortgage company, even if one of them no longer lives in the home. In community property states, a husband and wife may likewise be responsible for debts incurred by the other.

A husband and wife also can be responsible for each other's debts, even if they have not co-signed, if the debt is considered a **family expense**. Some states have **family expense statutes** that make a husband or wife liable for expenses incurred for the benefit of the family, even if the other spouse did not sign for or approve of the expense in advance. Still other states impose the family expense obligation by common law without a statute. Thus, if the wife charged groceries at a local store or took the couple's child to a doctor for care, the husband could be liable because these are expenses for the benefit of the family.

On the other hand, if the wife runs up bills for a personal holiday or the husband buys expensive coins for his coin collection, the other spouse normally would not be liable unless he or she co-signed for the debt. Again, in community property states, a husband or wife generally is liable for the debts of the other.

Each spouse, however, generally is not liable for debts the other spouse brought into the marriage. Such debts belong to the spouse who incurred them.

In many states, however a debt incurred before marriage (including a child support debt) could be collected against marital property of a new marriage. Thus, for example, if a man was \$15,000 behind in support to children of a first marriage, but the man owned a house or bank account in joint tenancy

with his second wife, those assets might be taken by a court to pay off the old debt. If the second wife is worried about the first wife or other creditors from the first marriage placing a claim on assets of the second marriage, the second wife should keep most of her property in her own name rather than in joint tenancy with her husband.

If one spouse owns a business and the other does not, the spouse who does not own the business normally would not be liable for business debts unless the non-owner co-signed on the debt or the couple resided in a community property state.

It is common for institutions that lend money to small businesses to want personal guarantees of payment from the owner of the business, and not just from the business itself. In the event the debt is not paid, lenders would like as many pockets to reach into as a possible. If the owner of the business owns a home, the lender may want to use the home as collateral for the business loan. That means that the spouse of the business owner, along with the business owner, may be asked to sign a paper allowing use of the home as collateral. Thus, the home could be lost if the business cannot pay off its debts.

Wives and husbands are entitled to open credit accounts in their individual names. Creditors cannot require a spouse to co-sign on an account unless the party seeking credit lives in a community property state, in which case both signatures can be required since spouses are liable for each other's debts incurred during the marriage.

Taxes

If the husband's and wife's names and signatures appear on a state or federal personal income tax return, both are liable for the taxes. If a couple files jointly, the Internal Revenue Service generally holds each spouse responsible for the entire debt.

In some circumstances, a spouse who signed a joint tax return can be excused from liability if the spouse can prove that he or she is an **innocent spouse**. A wife or husband can be considered an innocent spouse if he or she did not know--and had no reason to know--that the tax return understated the true tax.

That is often hard to prove. For example, the *Wall Street Journal* reported a case in which the wife of an IRS auditor did not know that her husband was taking bribes, but neither did she ask how they could afford expensive education for their children and country club dues on his government salary. The wife, as well as the husband, was found liable, for \$150,000 in unpaid taxes and penalties. (The husband also went to jail.)

On the other hand, a wife who relied on her husband and a certified public accountant to file a proper tax return, was held not to be liable when a deduction for one of the husband's tax shelters was not allowed by the IRS. If a married person wants full protection against possible liability for inaccurate tax returns filed by his or her spouse, the best approach is to file as "married filing separate return." That, however, usually results in a higher combined tax payments for the husband and wife than if they filed a joint return.

A married couple's income tax payments may be higher or lower than the taxes would be if the couple remained single depending on the income levels of each spouse. If one spouse has a high taxable income and the other spouse has a relatively low taxable income, they will generally pay less income tax if they are married and filing a joint return than if they are single and filing as single persons.

For wives and husbands who both have high incomes, their combined tax will be higher when they file as married persons than if they file as two single persons. Members of Congress periodically promise to remove the "marriage penalty" from federal income tax laws, but as of early 2001, that has not happened.

Years ago, there were stories about financially well-off married couples who would go to the Caribbean each December, obtain a divorce, file tax returns as single persons for that year to save money, and then remarry in the new year. Such a practice could be regarded as tax fraud. In any case, the savings are not as great as they were in years past.

Sidebar:

GIFTS BETWEEN SPOUSES

One spouse may make gifts to the other spouse in any amount without paying federal gift taxes if the spouse is a U.S. resident. However, it must be an outright gift or set up as a proper trust. Most, but not all, state laws have done away with taxes on gifts between spouses.

The same is not true with respect to gifts to other family members or to persons outside the family. Gifts to children, other relatives, people outside the family, and trusts may be taxable if they exceed a certain amount per year. Under federal tax law, one person may give someone other than a spouse up to \$10,000 per year without paying any tax on the gift. A married couple could give \$20,000 to a person each year without paying a gift tax. Both single people and married couples can make an unlimited number of tax-free gifts each year. However, if some or all of the gifts are made above the allowable dollar amounts, the overage will be deducted from the \$675,000 federal estate tax credit that all Americans have as of 2000 and 2001 (it will go up by increments to \$1 million by 2006). So, if the annual gifts exceeded the permissible amount by \$30,000, then the gift maker would have only a \$645,000 credit, and his or her estate would be liable for taxes on that \$30,000 to the extent that the estate exceeded \$645,000.

[End of Sidebar]

Doing Business Together

Wives and husbands, of course, can do business together. They can be business partners, just as any other two people, whether related or not. They could set up a corporation and both be owners and employees of the corporation; they could form a partnership; or one could own the business and employ the other. Wages and benefits, including health insurance and retirement plans, can be paid, just as they would for any other employee.

If wages and benefits are being paid to a spouse or child, the amount usually should not be more than what is reasonable or fair market value. If artificially high payments are made, the business could get into trouble with the Internal Revenue Service.

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