REPTL
REAL ESTATE, PROBATE & TRUST LAW
SECTION OF THE STATE BAR OF TEXAS

REPORTER

Volume 55, No. 3

CLICK ON THE TITLE BELOW TO JUMP TO ARTICLE

CONTENTS

CURRENT DEVELOPMENTS

FEATURED ARTICLES

REPTL
REAL ESTATE, PROBATE & TRUST LAW
SECTION OF THE STATE BAR OF TEXAS

REPORTER

The Official Journal of the Real Estate, Probate and Trust Law Section State Bar of Texas
www.reptl.org

ABOUT

The REPTL Reporter is the official journal of the Real Estate, Probate and Trust Law Section of the State Bar of Texas (REPTL). It is published by REPTL to provide education and information for REPTL members in the areas of real estate, probate, trust, guardianship, tax and water law. A copy of each issue is furnished to the members of REPTL as part of their section dues.

DISCLAIMER

REPTL presents the information in *The REPTL Reporter* as a service to its members. Opinions expressed herein are solely those of the respective authors and are not the opinions of the State Bar of Texas or REPTL. While the information in *The REPTL Reporter* addresses legal issues, it is not legal advice. Due to the rapidly changing nature of the law and REPTL's reliance on information provided by outside sources, REPTL makes no warranty or guarantee concerning the accuracy or reliability of the content of *The REPTL Reporter.*

CONTACT

To contact us about *REPTL Reporter* content, please email the Editor-in-Chief, Gerry W. Beyer. For general issues pertaining to the section, email the State Bar Sections Department at sections@texasbar.com

PRIOR ISSUES

REPTL members may access prior issues at www.reptl.org. This newsletter is password protected and you must be a member of the REPTL section to access this newsletter. To resolve any password issues, please email our webmaster.

EDITOR-IN-CHIEF

Gerry W. Beyer
Governor Preston E. Smith Regents Professor of Law
Texas Tech University School of Law
1802 Hartford Ave.
Lubbock, TX 79409-0004
voice (806) 834-4270
e-mail gwb@professorbeyer.com
web http://www.ProfessorBeyer.com
blog http://www.beyerblog.com
SSRN (articles) http://ssrn.com/author=461383
Twitter Gerry_Beyer

Follow REPTL on Your Favorite Social Media sites

POTPOURRI

Gerry W. Beyer
Texas Tech University School of Law
Lubbock, Texas
gwb@professorbeyer.com

So, Tell Me How You Really Feel!

After Texan Leslie Ray Charping died on January 30, 2017, his family published an obituary expressing their real feelings. Here are a few excerpts. "He leaves behind 2 relieved children; a son . . . and daughter, Shiela Smith . . . along with six grandchildren and countless other victims including an ex wife, relatives, friends, neighbors, doctors, nurses and random strangers. At a young age, Leslie quickly became a model example of bad parenting combined with mental illness and a complete commitment to drinking, drugs, womanizing and being generally offensive. . . . Leslie's hobbies included being abusive to his family, expediting trips to heaven for the beloved family pets and fishing . . . . Leslie's life served no other obvious purpose, he did not contribute to society or serve his community and he possessed no redeeming qualities besides quick whited [sic] sarcasm which was amusing during his sober days. . . . Leslie's passing proves that evil does in fact die and hopefully marks a time of healing and safety for all."

See Obituaries: Leslie Ray Charping, CARNESFUNERALHOME.COM (last visited Apr. 25, 2017).

Pod People

Not quite the same as the classic 1978 movie *Invasion of the Body Snatchers* starring Donald Sutherland and Spock (aka Leonard Nimoy), but nonetheless, creepy. As explained in the article cited below, "The Capsula Mundi concept, from designers Anna Citelli and Raoul Bretzel, uses an egg-shaped burial pod made from biodegradable starch plastic as the coffin, in which the body is placed in a fetal position and buried under the ground. A tree (or tree seed) is then planted over the top of the pod, which will use the nutrients from the decomposing body as fertilizer for its growth." Just think, if you plant a fruit tree and then eat the fruit, you could actually say, "It's people" in the style of Frank Thorn (Charlton Heston) in *Soylent Green*.

See Derek Markham, *Egg-shaped Burial Pods Feed the Trees and Turn Cemeteries Into Forests*, TREEHUGGER.COM (Sept. 19, 2014).

Coffee King's "Urn"

When Renato Bialetti, the purveyor of aluminum stovetop espresso makers, died last year, he was cremated and his ashes placed in a giant Moka pot at his funeral in Montebuglio, Italy. I just hope his family does not inadvertently start using the pot to brew coffee some morning when the sleep fog has not yet risen.

See *Ashes of Italian 'Coffee King' Put in Giant Espresso Pot*, FOXNEWS.COM (Feb. 20, 2016).

INTESTACY, WILLS, ESTATE ADMINISTRATION, AND TRUSTS UPDATE

Gerry W. Beyer
Texas Tech University School of Law
Lubbock, Texas
gwb@professorbeyer.com

Will Contests – Lack of Formalities

In re Estate of Romo, 503 S.W.3d 672 (Tex. App.—El Paso 2016, no pet. h.).

Contestants claimed that a will previously admitted to probate was invalid because the testator lacked testamentary capacity or executed the will when subjected to undue influence. After testimony at the trial that the witnesses did not attest in the testator's presence as required by Estates Code § 251.051(3), the court granted contestant's motion for a directed verdict that the will was invalid.

The appellate court affirmed. The court explained that only a will which meets all Texas requirements may be admitted to probate. It was irrelevant that the trial was centered around two other grounds for finding the will to be invalid.

Moral: A court may set aside a will for failure to comply with the requirements of a valid will even if the contestant does not raise that ground in the pleadings.

Will Contests – Lack of Capacity

Tex. Capital Bank v. Asche, No. 05-15-00102-CV, 2017 WL 655923 (Tex. App.—Dallas Feb. 17, 2017, no pet. h.) (mem. op.).

The trial court determined that the testator lacked capacity to execute multiple estate planning documents over a period of time spanning over a decade. In addition, the trial court found that the testator was subjected to undue influence.

The appellate court made an exhaustive review of the evidence, which included both medical and lay testimony. Although there was "unquestionably conflicting evidence" about testator's capacity, the court explained that it may not substitute its judgment for that of the jury. The court then concluded that the evidence was legally and factually sufficient to support the jury's finding that the testator lacked capacity. Accordingly, the court did not need to address the undue influence issue.

Moral: Once a jury determines a testator's capacity to execute a will, it will be difficult to have that finding overturned on appeal unless the jury's finding is against the great weight of the evidence.

Estate Administration – Late Probate

Byerley v. McCulley, No. 12-16-00124-CV, 2017 WL 605089 (Tex. App.—Tyler Feb. 15, 2017, no pet. h.).

The probate court admitted Testatrix's will to probate nineteen years after her death. The court determined that Applicant was not in default for probating the will within four years of the date of Testatrix's death and that service was made by posting. Heir sought a bill of review asserting that he did not receive sufficient notice.

The appellate court agreed and granted the bill of review. Applicant claimed that under the law at

the time of Testatrix's death, service for a late probate by posting was sufficient. PROB. CODE § 128(a). Heir asserts that the law applicable when Applicant filed the will for probate governs which requires service on heirs whose addresses can be ascertained with reasonable diligence. EST. CODE § 258.001.

The court recognized that when the law was changed to require service in 1999, the legislation contained a savings clause providing that the change to require service on the heirs upon a late probate applied only if the person died on or after September 1, 1999. PROB. CODE § 128B. However, when Probate Code § 128B was repealed and replaced by Estates Code § 258.001, there was no express savings clause. Because there was no savings clause and the text of § 258.001 does not limit the applicability of the notice requirements, notice to the heirs was required. Accordingly, admitting the will to probate after only notice by posting was a substantial error justifying the issuance of a bill of review.

Moral: Applicants for a late probate need to provide notice to the heirs regardless of when the testator died.

Trusts – Parties

Tex. Capital Bank v. Asche, No. 05-15-00102-CV, 2017 WL 655923 (Tex. App.—Dallas Feb. 17, 2017, no pet. h.) (mem. op.).

The trial court determined that a settlor lacked capacity to create a trust. However, the contestant failed to join the trustee of the trust as a party. Accordingly, the appellate court reversed because "[i]t is well established that suits against a trust must be brought against its legal representative, the trustee." The fact that the same entity was a party to the lawsuit as the settlor's executor was insufficient as "[e]xecutor and trustee are separate and distinct capacities."

Moral: A trust is not a legal entity that can sue or be sued. In any action involving a trust, the trustee in his/her/its representative capacity must be made a party.

GUARDIANSHIP UPDATE

Chasity W. Cooper
Crain, Canton & James
Houston, Texas
ccooper@craincaton.com

Motion to Show Authority; Standing

Ross v. Sims, No. 03-16-00179-CV, 2017 WL 672458 (Tex. App.—Austin Feb. 15, 2017, no pet. h.) (mem. op.).

In *Ross*, three children were fighting over the guardianship of their ninety-one-year-old mother, Mrs. Sims. The trial record shows that Mrs. Sims was suffering from mild to moderate dementia before she had a stroke and subsequently executed a power of attorney appointing her daughter Suzanne as her agent. Suzanne then relocated Mrs. Sims from her home, filed an eviction proceeding against her brother, Harold, who was residing in Mrs. Sims's home, hired Ross to represent herself and Mrs. Sims, and created a trust transferring Mrs. Sims's property to Ross as trustee.

Harold filed an application for appointment of guardian of Mrs. Sim's person and requested his sister, Cynthia, be appointed guardian of Mrs. Sims's estate. Cynthia joined in the application. Mrs. Sims, through her attorney Ross, filed an answer contesting the guardianship. The trial court appointed an attorney and guardian *ad litem* and authorized an independent medical examination. Harold and Cynthia filed a motion to show authority, challenging Ross's authority to represent Mrs. Sims.

A hearing was held on the motion to show authority, where the court psychiatrist testified that Mrs. Sims did not have decision-making capacity after her stroke. The court orally granted the motion to show authority, removed Ross from representing Mrs. Sims in the guardianship, and instructed him to turn over all documents to the attorney *ad litem*.

Harold and Cynthia then filed a motion to set trial on the nonjury docket. Ross filed a plea in intervention pursuant to Texas Rules of Civil Procedure 60, alleging he had standing and capacity to intervene as a person interested in the welfare of Mrs. Sims pursuant to Texas Estates Code §§ 1002.018 and 1055.001. He contested the need for the appointment of a guardian and argued Harold and Cynthia were disqualified. He also filed a response to the nonjury trial setting, arguing he had previously paid a jury fee and demanded a jury trial. Harold and Cynthia filed a motion to strike Ross's plea in intervention and jury demand.

Despite the court's ruling that Ross had no authority to represent Mrs. Sims, Ross proceeded to file pleadings in the eviction lawsuit and represent that he, as trustee, was the owner of Mrs. Sims's house. Thus, Harold and Cynthia filed an application for an emergency ex parte temporary restraining order and temporary injunction to enjoin the withdrawal of Mrs. Sims's funds or the transfer of her property. The trial court granted the TRO against Ross and Suzanne and precluded them from withdrawing money from Mrs. Sims's accounts or transferring her property. Ross filed an answer and demanded a jury trial.

At the hearing, the trial court granted Harold and Cynthia's motions to strike Ross's intervention and jury demand, finding that it was not timely and that his position was adverse to Mrs. Sims's, relying on Texas Estates Code §§ 1055.001 and 1055.003(c), which give the court discretion to grant or deny the intervention of an interested party if that intervention would unduly prejudice the adjudication of the original parties' rights. The court further instructed Ross that he was not a party and to "have a seat in

the gallery." Eventually the court signed orders declaring the power of attorney was invalid along with all subsequent transfers of Mrs. Sims's property and ordered all funds be transferred to the county court for Mrs. Sims's benefit.

A guardianship trial was eventually had and the court appointed Cynthia permanent guardian of Mrs. Sims's person and estate. Although Ross did not participate in the trial, he did file a motion for new trial and a supplement to same, which were both overruled by operation of law.

Ross appealed. Harold and Cynthia argued that the appeal should be dismissed because Ross lacked standing because he was not a party to the underlying suit. However, the appellate court found that when Ross filed a plea in intervention and was subsequently served with a TRO and temporarily enjoined by the trial court, he was a party to the guardianship proceeding and had standing to appeal.

On appeal, Ross attempted to argue that his due process rights were violated. The appellate court first looked at whether there was essentially a Takings Clause violation when the trial court voided the trust and ordered the funds be transferred to the court's registry. The appellate court found his arguments were without merit, as he cited no authority to support that he, as trustee, was entitled to just compensation when the funds were ordered from the trust to the court registry. Ross further argued that his due process was violated when he was denied a trial on the merits before the court voided the trust and ordered the funds returned to the court's registry. The appellate court again found this argument to be without merit.

The appellate court found that although the right to be heard is a fundamental concept to due process, a party's right to due process does not mean that a case may never be disposed of before a trial. *See* *Soefje v. Jones*, 270 S.W.3d 617, 625 (Tex. App.—San Antonio 2008, no pet.). In fact, the record reflected that Ross was afforded an opportunity to meaningfully participate at the hearing regarding his authority to represent Mrs. Sims and at the hearing regarding the motion to strike his plea in intervention and jury demand and the temporary injunction. And, the appellate court found that Ross cited no authority to support his position that he was entitled to a jury trial in a guardianship proceeding.

Further, the appellate court found that once his plea in intervention was struck, his request for a jury trial as an intervener was moot. Thus, based on the appellate court's review of the record, it concluded that Ross failed to show his due process rights were violated when the trial court voided the trust and ordered the funds be placed with the trial court for Mrs. Sim's benefit or that any such violation resulted in an improper judgment in the guardianship proceeding or prevented him from presenting his case on appeal. Therefore, the appellate court affirmed the trial court's orders.

Priority of Guardian; Disqualification

In the Matter of the Guardianship of Fairley, No. 04-16-0096-CV, 2017 WL 188103 (Tex. App.—San Antonio Jan. 18, 2017, pet. filed) (mem. op.).

In *Fairley*, ward's wife and daughter both filed applications to be appointed his permanent guardian. The trial court found that daughter lacked just cause to contest wife's application and ordered daughter to deposit security for probable costs in the proceeding with the clerk. Daughter failed to comply and the trial court dismissed her application.

A trial was had on wife's application, where daughter's counsel argued that her application was erroneously dismissed. During the trial, daughter's counsel agreed that wife had priority to serve as guardian absent disqualification and argued that the issue to a jury should be whether wife was

qualified. The court heard testimony regarding wife's prior management of ward's affairs under his medical and financial powers of attorney and determined it was in his best interest to appoint wife guardian.

On appeal, daughter argued that the dismissal of her application prevented her from participating in the trial on wife's application and from being considered her father's guardian. However, the appellate court found that the record reflected daughter's counsel appeared on her behalf at the trial, requested relief from the court, and had an opportunity to cross examine the wife. Although daughter sought to prove wife was disqualified, she offered no evidence of same at the trial.

The appellate court relied on Texas Estates Code § 1104.001 that states if an incapacitated person's spouse is eligible to be the guardian, then the spouse is "entitled to guardianship in preference to any other person." Because daughter failed to argue on appeal that that wife was ineligible or disqualified, the appellate court found that wife is entitled the be ward's guardian as a matter of law. The appellate court further found that the dismissal of daughter's application did not result in an improper judgment or prevent her from presenting in the case.

Accordingly, the appellate court held that any error in dismissing daughter's application or ordering her to provide security was harmless and affirmed the trial court's order.

Bill of Review; Motion for New Trial

In re Ludington, No.01-16-00411-CV, 2017 WL 219162 (Tex. App.—Houston [1st Dist.] Jan. 19, 2017, no pet.) (mem. op.).

In *Ludington*, decedent was under a guardianship prior to his death. The administrator of decedent's estate petitioned the court for a bill of review challenging an order it previously entered approving the guardian's final account and discharging him and the surety from liability. Administrator alleged that the guardian failed to account for all of the ward's assets, income, and certain loans that were made to decedent.

The trial court held an evidentiary hearing on administrator's petition at which time she announced she was ready to prove her case. She attempted to offer evidence, which was excluded upon objections. The parties then had a discussion regarding the background of the case and made opening statements discussing the issues that related to administrator's claims. The trial court indicated that before it could rule on her petition, it would need to review all of the prior guardianship orders. Administrator offered to provide those orders to the court, but did not ask the court to consider additional exhibits, witness testimony, object that she had not had sufficient time to make her case, move for a continuance, or ask that the record remain open.

Administrator subsequently filed a post-hearing brief whereby she attached the requested guardianship orders, along with accounts, inventories, and other filings related to the guardianship. Her brief acknowledged that the court had already heard and considered her petition and this brief was offered to address arguments raised at the hearing. She again did not argue that she had not been afforded the opportunity to present her case, offer additional exhibits or testimony, or request an additional hearing be held. The surety filed a response to the brief and characterized the previous hearing as a bench trial and argued administrator failed to call any witness or offer any admissible evidence and therefore, her petition should be denied.

The trial court subsequently denied administrator's petition for statutory bill of review. Administrator moved for a new trial on the grounds that she had not been afforded the opportunity to

present her case. The surety argued that administrator failed to obtain rulings on her exhibits, call witnesses, request a continuance, or argue that she had not been afforded adequate time to present her case, and there was no basis for the trial court to vacate its order. The trial court agreed and administrator's motion was denied.

On appeal, administrator agued the trial court did not permit her to present certain evidence that would have proved her right to a bill of review. The appellate court disagreed and found that the trial court record showed she was given the opportunity to present evidence at the hearing, through her supplemental brief, and could have filed a reply to the surety's response brief alleging that she failed to meet her burden of proof. The appellate court found that if administrator felt that she was prevented from presenting her evidence at the hearing, she should have objected and made an offer of proof at the hearing and filed a reply to the surety's reply brief providing evidence in support of her petition.

Administrator further argued that the trial court abused its discretion when it ruled before she announced that she had rested her case, relying on Texas Rules of Civil Procedure 262 and 265. The appellate court disagreed and found that those rules only prevent a trial court from ruling before the petitioner is allowed to present evidence, which administrator was allowed to do in this instance.

Finally, the appellate court found that administrator's motion for new trial failed to identify any specific evidence she intended to offer and why it would have been dispositive, and the record did not contain any indication that reopening the evidentiary hearing would have changed the outcome.

Accordingly, the appellate court overruled administrator's sole issue on appeal and affirmed the trial court's order.

ELDER LAW UPDATE

Lori A. Leu
Leu & Peirce, PLLC
Plano, Texas
lieu@leulawfirm.com

Medicaid Planning and the Unauthorized Practice of Law

One of the scams affecting elderly individuals and their families, which could also affect unwitting attorneys, is the unauthorized practice of law by nonattorneys who assist elderly clients in qualifying for Medicaid benefits to fund long-term care. Individuals who engage in such activities often call themselves "Medicaid planners" or "Medicaid specialists," thus, implying a special skill that the Texas legislature has declared constitutes the practice of law. Medicaid planning is more than simply providing general advice about Medicaid eligibility. It involves an in-depth analysis of medical and financial circumstances, and often includes complex asset restructuring.

Medicaid planning is legal when done by an attorney licensed in the State of Texas. However, Medicaid planning by a nonattorney is criminal. The Texas Human Resources Code defines the unauthorized practice of law in the context of Medicaid planning:

> (a) A person who is not licensed to practice law in Texas commits an offense if the person charges a fee for representing or aiding an applicant or recipient in procuring assistance from the state agency administering the assistance.
>
> (b) A person commits an offense if the person advertises, holds himself or herself out for, or solicits the procurement of assistance from the state agency administering the assistance.
>
> (c) An offense under this section is a Class A misdemeanor.

TEX. HUM. RES. CODE § 12.001. A Class A misdemeanor is punishable by a fine up to $4,000, one year in jail, or both for all parties involved in the scheme. TEX. PENAL CODE § 12.21.

As set forth in § 12.001, it is a crime for nonattorneys not only to represent or assist an applicant in obtaining Medicaid benefits for a fee, but to even advertise themselves and their services to the public. In some cases, nursing homes become involved and may subject themselves to criminal charges as well for their role in directing elderly individuals and their families to unauthorized planners.

Nonattorneys often attempt to appear legitimate by claiming to work with attorneys. In most cases, however, these attorneys never actually meet with the elderly clients or their families and are merely "lending" their name, and taking a fee, to establish legitimacy for the criminal. Attorneys who participate in such schemes are subjecting themselves to disciplinary consequences, in addition to the potential claim of criminal activity. The Texas Disciplinary Rules of Professional Conduct provide as follows: "A lawyer shall not . . . assist a person who is not a member of the bar in the performance of activity that constitutes the unauthorized practice of law." TEX. DISCIPLINARY RULES PROF'L CONDUCT R. 5.05(b).

The policy behind this law stems from the complicated nature of Medicaid planning and the high stakes for the elderly individuals involved. This area of practice is full of legal intricacies that can have serious ramifications for the financial well-being of the elderly clients. Consequences for faulty planning can include the denial of benefits, a penalty period, or tax liability. All of this at a time when these

elderly individuals' finances are the most vulnerable. The Texas Chapter of the National Academy of Elder Law Attorneys has formed a committee, headed by Marian Rosen, a litigation attorney with Rosen & Spears, to investigate and pursue violators who are placing elderly citizens at risk. In addition, violators should be reported to the local district attorney and, if they are complicit attorneys, to the State Bar of Texas.

In composing this article, author referenced "Medicaid Planning Legal Only if Offered by Attorney," written by Wesley E. Wright and Molly Dear Abshire, Certified Elder Law Attorneys, which appeared in the Summer 2016 edition of the Texas Chapter of the National Academy of Elder Law Attorneys' Newsletter.

Will Modification and Reformation—a Treasured Tool in an Elder Law Attorney's Toolkit

Texas courts have long exercised a statutory and common law authority to modify or terminate trusts. The Texas Trust Code provides an avenue for a trustee or a beneficiary of a trust to petition the court to modify the terms of the trust to prevent waste, correct a mistake, or achieve tax objectives, in furtherance of the settlor's intent. TEX. TRUST CODE § 112.054. Executors of wills probated in Texas have not enjoyed that privilege until the 2015 legislative changes authorizing judicial modification and reformation of wills. Even now, two years later, many attorneys are not aware of this potential treasure that can be used to both correct drafting errors and the problems that arise from our inability to predict future needs and circumstances of beneficiaries.

Historically, Texas courts have held that a will cannot be reformed after the testator's death. In *San Antonio Area Foundation v. Lang*, the Texas Supreme Court applied the plain meaning rule, noting that the court must focus on the exact words used by the testator, rather than the testator's intent, when interpreting a will. *San Antonio Area Found. v. Lang*, 35 S.W.3d 636, 639 (Tex. 2000). The court held that extrinsic evidence is not admissible when there is no ambiguity in the will. *Id*.

The 2015 Texas Legislature effectively overruled the Texas Supreme Court's decision in *Lang* with the passage of the new Subchapter J of Subtitle F, §§ 255.451-.455 of the Texas Estates Code. These new provisions allow a personal representative of a decedent's estate to petition a court to modify or reform a will to address an administrative issue, achieve the testator's tax objectives, qualify a beneficiary for government benefits, or correct a scrivener's error. TEX. ESTATES CODE § 255.451. Only a personal representative has the authority to request modification or reformation of a will; however, the personal representative has no duty to seek modification or reformation or inform the beneficiaries of the option to do so. TEX. ESTATES CODE § 255.455. Contrary to the Texas Trust Code's modification statute, a beneficiary of a will does not have standing to petition the court for modification or reformation. *See* TEX. ESTATES CODE §§ 255.451-.455.

While many of the advantages and disadvantages are still to be seen in likely litigation over the extent of the statute, elder law attorneys across Texas are excited about a short, but significant, phrase in the statute: "to qualify a distributee for government benefits." TEX. ESTATES CODE § 255.451(a)(2). It is not uncommon for a beneficiary to be healthy and financially independent at the time a testator executes a will and for the testator to not anticipate a beneficiary's future need for and receipt of public benefits. Prior to the passage of Texas Estates Code § 255.451, a beneficiary who was on public benefits and received an inheritance under a will was required to create a self-settled or third-party special needs trust and fund that trust with the inheritance from the decedent's estate within the month of receipt to avoid jeopardizing his or her public benefits. Thanks to the new Judicial Modification or Reformation of Wills statute, the executor of the decedent's estate can ask the court to modify the will

to create a testamentary special needs trust and authorize the executor to fund the trust with the portion of the estate that would pass to any beneficiary receiving public benefits. In addition, if the will includes a supplemental needs trust, but contains an insufficient distribution standard, the court can modify the will by adding or changing specific provisions so that the trust complies with the Social Security Administration's extensive regulations of special needs trusts.

Only time will tell how treasured of a tool in the elder law attorney's toolkit the Judicial Modification or Reformation of Wills statute will be.

ESTATE AND GIFT TAX UPDATE – PART 1

Laurel Stephenson
Davis Stephenson, PLLC
Dallas, Texas
laurel@davisstephenson.com

IRS Makes Syndicated Conservation Easement Transaction a "Listed Transaction"

Notice 2017-10 (2016).

The IRS has warned that certain conservation easements entered into after 2009 will be "listed transactions," effective as of December 23, 2016. The targeted transaction entails a conservation easement described either in written or promotional materials as offering an opportunity to investors to purchase an interest in a pass-through entity holding real property providing the investor with the possibility of a charitable deduction equal to or in excess of two and one-half times the invested amount via the entity's contribution of a conservation easement encumbering the property to a tax-exempt organization. The promised charitable deduction is obtained via (i) an inflated appraised value of the real property premised on "unreasonable conclusions about the development potential of the real property" and (ii) a reduction in value resulting from the easement (the deduction amount). Transactions "substantially similar" to the targeted transaction are also now "listed transactions."

Anyone who invested in the described or a substantially similar transaction must file a disclosure of such with the IRS for each tax year with an open period of limitations as of December 23, 2016. Individuals participating in the capacity as a "material advisor" (e.g., an attorney or accountant who promoted and/or organized the transaction, as well as an appraiser who prepared the facilitating appraisal) must also report a transaction and maintain a list of investors. See Notice 2017-10 for details on the required reporting, including deadlines.

Investors and material advisors are subject to penalties for noncompliance, which may also result in extended periods of limitations for investors. "Appropriate corrective action" is recommended for individuals who filed tax returns reflecting the purported tax benefits.

Final Regulations Issued Modifying Regulations Involving Basis Rules to Incorporate Coordinating References to IRC § 1022

82 Fed. Reg. 6235 (Jan. 19, 2017).

Proposed regulations were issued on May 11, 2015, outlining amendments to various existing regulations to update them to address the impact of Internal Revenue Code (IRC) § 1022. Those proposed regulations have been adopted as final without any substantive changes effective as of January 19, 2017.

IRC § 1022 provided the "modified carryover basis system" applicable with regard to estates of decedents who died in 2010 and opted pursuant to § 301(c) of the Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 not to be subject to Chapter 11 of the Internal Revenue Code. For recipients of property from an electing estate, the basis of that property is consequently governed by IRC § 1022 and not by IRC § 1014. Various existing regulations have now been revised to clarify that result. While most of the affected regulations have been revised simply with a reference to IRC § 1022, certain regulations were revised with additional detail (including an example) to clarify the applicability of IRC § 1022 in the referenced context.

IRS Addresses Tax Treatment of Trust Created in Divorce

I.R.S. Priv. Ltr. Rul. 201707007 (Feb. 17, 2017).

PLR 201707007 provides a nice roadmap for divorcing spouses in structuring a division of the marital property that accommodates one spouse's desire for ultimate ownership of a particular asset and the other spouse's desire to receive its income for a period of time.

As outlined in the ruling, divorcing spouses agreed in a proposed settlement agreement to husband's creation of a trust for wife providing her with an entitlement to all trust income and discretionary distributions of principal, with the remaining trust property reverting to husband (or his estate) upon wife's death. In exchange, wife proposed to relinquish all of her marital rights and property claims. Husband funded the trust in part with stock he evidently wished to retain ultimate ownership of because he prohibited the trustee from distributing the shares to wife or selling shares to facilitate a distribution of principal.

The IRS ruled that the transfer of the shares to the trust would be a "transfer incident to a divorce" and accordingly not result in any gain or loss to husband pursuant to IRC § 1041(a) as long as the spouses finalized the settlement agreement and the transfer of shares occurred within six years of the entry of the final judgment of divorce.

The IRS further ruled that husband's transfers of the shares to wife's trust would be deemed made for full and adequate consideration in money or money's worth pursuant to IRC § 2516 (and therefore would not constitute a taxable gift), provided that a final judgment of divorce occurred within the three-year period beginning on the date one year prior to the execution of the settlement agreement. The IRS correspondingly ruled that IRC § 2702 would not apply for purposes of determining that husband made a gift in conjunction with establishing the trust.

Lastly, the IRS concluded that husband's reversion would result in inclusion of the trust property on hand at the time of his death pursuant to IRC § 2036, subject to a reduction for wife's outstanding income interest if she survived him (valued in accordance with the tables provided in Treas. Reg. § 20.2031-7).

Tax Court Evaluates Expert Witness Testimony in Conjunction with Valuation of "Old Master" Paintings

Estate of Eva F. Kollsman, et. al. v. Comm'r, T.C. Memo. 2017-40 (2017).

The court's analysis of expert witness testimony in *Kollsman* serves as a reminder that hiring an expert with good credentials does not guarantee ultimate success in supporting a returned value if he or she does not have a well-reasoned basis for his or her conclusions, which should ideally be supported by comparable sales.

Ms. Kollsman died in 2005 owning two "Old Master" paintings that were in less than pristine condition. The estate engaged a vice president at a well-known auction house to appraise the paintings. He valued the paintings at $500,000 (the Maypole) and $100,000 (the Orpheus) with heavy discounting to the paintings' values to account for their dirty condition and the "bowed condition" of the Orpheus. The estate's appraiser did not rely upon any comparable sales.

The IRS's appraiser assigned a significantly higher value to each painting based upon comparable sales but without any discounting to account for either painting's dirty condition or the "bowed condition" of the Orpheus.

The court disregarded the valuations of the estate's appraiser, in part based upon what the court felt was an apparent conflict of interest, concluding that he may have assigned each painting a lower value to encourage the estate to engage the auction house's services in auctioning the paintings. The court also noted that the estate's appraiser failed to take into account what the court considered to be sufficiently comparable sales offered by the Service's appraiser in support of his higher values for the paintings.

The court further found that the estate's expert overstated the effect of the paintings' dirty condition on their value and the risks associated with cleaning them, noting that the art restorer hired by the executor informed him prior to the restoration work that he felt the paintings could be cleaned "with relative ease." The court concluded that information would have been considered by the willing buyer and willing seller in negotiating a sales price for each painting and would likely result in only a minimal discount.

The court also found that the estate appraiser failed to account for the Maypole's sale a few years later at a price five times that of the returned value. The estate's expert argued the sale was irrelevant in establishing the Maypole's date of death value because it took place after the painting had been cleaned and after a dramatic increase in the market for Old Master paintings. However, the court was unpersuaded that the sale should be disregarded entirely.

Ultimately, the court rejected the estate appraiser's valuation of each painting and accepted the Service's valuations, subject to the court's discounting of each painting by 5% to reflect the risks (albeit minimal) associated with restoring them. The court applied an additional discount to the Orpheus's value to reflect both its slightly "bowed condition" as well as a question regarding its attribution to the purported artist, as neither concern had been taken into account by the Service's expert in valuing the painting.

ESTATE AND GIFT TAX UPDATE – PART 2

Jason Flaherty
Brink Bennett Flaherty PLLC
Austin, Texas
jflaherty@bbfaustin.com

IRS Issues Procedures to Recalculate Remaining Applicable Exclusion Amounts and GST Exemptions to Extent Used for Transfers by or to Same-Sex Spouses

Notice 2017-15 (Jan. 17, 2017).

As a result of the Supreme Court's decision in *United States v. Windsor*, 133 S. Ct. 2675 (2013), recognizing same-sex marriages, the IRS will now allow taxpayers in same-sex marriages to recoup the prior application of the Applicable Exclusion Amount or GST exemption to transfers by or to a same-sex spouse. Notice 2017-15 provides that same-sex couples who were married under state law at the time of a gift from one spouse to another or a transfer to a spouse on death, regardless of the domicile of the parties, may apply the unlimited marital deduction for both gift and estate tax purposes to recalculate the remaining Application Exclusion Amount or GST exemption, even if the statute of limitations has run on the relevant return. Any claims for credits or refunds for any overpayment of tax must be made within the applicable limitations period for filing such a claim under Internal Revenue Code (IRC) § 6511.

Ruling Allows Late Allocation Out of Automatic GST Exemption Allocated to GRATs

I.R.S. Priv. Ltr. Rul. 2017-05-002 (Feb. 3, 2017).

In PLR 2017-05-002, the taxpayer created and funded a total of twelve GRATs over a two-year period. The taxpayer hired a tax professional to prepare and file a Form 709 United States Gift (and Generation-Skipping Transfer) Tax Return for the years at issue and relied on the tax professional to elect out of the automatic allocation of GST exemption to the transfers to the GRATs. However, in preparing the gift tax returns for two of the years at issue, the tax professional inadvertently failed to elect out of the automatic allocation of GST exemption to the GRATs under § 2632(c)(5)(A)(i)(II).

The IRS ruled that the requirements of IRC § 301.9100-3 were satisfied and, therefore, the personal representatives of taxpayer's estate were granted an extension of 120 days to file supplemental Forms 709 to elect out of the automatic allocation rules of IRC § 2632(c)(1) for the transfers to the GRATs.

IRS Rules that Court Reformation of IRA Beneficiary Designation Cannot Create a Designated Beneficiary for Purposes of Rollover

I.R.S. Priv. Ltr. Rul. 2017-06-004 (Feb. 10, 2017).

In PLR 2017-06-004, the decedent maintained an individual retirement account (IRA) that named an *inter vivos* trust as beneficiary. However, no record could be found of the trust. The decedent's will named his surviving spouse as beneficiary of his entire estate. The IRS ruled that despite a state law reformation of the beneficiary designation for the IRA to name the surviving spouse as the beneficiary, the surviving spouse was not a "designated beneficiary" for purposes of IRC § 408(d)(3). Because the decedent died before his required beginning date and without a designated beneficiary, the entire interest in the IRA must be distributed using the five-year rule described in IRC § 401(a)(9)(B)(ii).

Late Filing Penalty Waived Because of Reasonable Reliance on Advice of Tax Professional

Estate of Hake v. U.S., 119 AFTR 2d 2017-727 (M.D. Pa. Feb. 20, 2017).

In *Hake*, two executors filed the estate tax return for their mother's estate on the date that their tax attorney advised them it was due but which was in fact, six months late. The tax attorney erroneously advised the executors that the due date to file the return had been extended for one year when in fact, it had been extended for only six months. Under IRC § 6651(a)(1), when a taxpayer fails to file a tax return by the due date, including any extension of time for filing, a late penalty applies "unless it is shown that such failure is due to reasonable cause and not due to willful neglect." The court held that the taxpayer demonstrated "reasonable cause" when, in reliance upon the advice of counsel, the taxpayer filed a return "after the actual due date but within the time the adviser erroneously told him was available." The court also recognized that its holding was contrary to the holdings of other courts not within the Third Court of Appeals.

Failure to File FBAR Was Willful Despite Voluntary Disclosure

U.S. v. Bohanec, 118 AFTR 2d 2016-5537 (C.D. Cal. Dec. 8, 2016).

A federal district court's ruling in *Bohanec* is a reminder of the severe penalties that can be imposed for a willful failure to report an interest in a foreign bank account by filing a Report of Foreign Bank and Financial Accounts (FBAR). If a foreign account holder "willfully" failed to report a foreign account on an FBAR, the maximum penalty is increased from $10,000 to the greater of $100,000 or 50% of the balance in the account at the time of violation. The court concluded that the account holders willfully failed to report their interest in foreign bank accounts and imposed a penalty equal to the greater of $100,000 or 50% of the balance in the account at the time of the violation.

MARITAL PROPERTY AND HOMESTEADS UPDATE

Jason A. Cox
Galligan & Manning
Houston, Texas
jcox@galliganmanning.com

Community Property Subject to Husband's Sole Management, Control, and Disposition and Constituted a Valid Sale Even Without Wife's Signature

Ifiesimama v. Haile, No. 01-15-00829-CV, 2017 WL 1173885 (Tex. App.—Houston [1st Dist.] Mar. 30, 2017, no pet. h.).

Tamuno Ifiesimama (Husband) and Tamunnoibuomi Ifiesimama (Wife) decided to sell their home in Stafford, Texas, in 2013. Daniel Haile (Haile) and Wongelawit Alemu (Alemu) made an offer on the house, which Husband accepted, signing a sales contract and setting a closing date.

The contract contained the following term: "If Seller fails to comply with this contract, Seller will be in default and Buyer may (a) enforce specific performance, seek such other relief as may be provided by law, or both, or (b) terminate this contract and receive the earnest money, thereby releasing both parties from this contract."

The parties also executed an "Intermediary Relationship Notice," which identified both Husband and Wife as the sellers and Haile and Alemu as the buyers. Both Haile and Alemu signed this agreement, as did Husband; Wife did not sign this agreement or the sales contract. The "Intermediary Relationship Notice" is the only document in the record that indicates that Wife may have had any interest in the property.

At the closing, Husband signed documents as Wife's attorney-in-fact; however, he later revealed at the closing that he did not actually have power of attorney for Wife. The closing fell through, and Haile and Alemu did not receive title to the property.

Haile and Alemu brought claims against Husband and Wife for specific performance of the sales contract as well as injunctive relief prohibiting Husband and Wife from selling the property to another buyer.

A bench trial was held and the court found in favor of Haile and Alemu, ordering that they recover costs, their earnest money deposit, and attorney's fees from Husband and Wife even though only Husband signed the sales contract. The trial court further ordered that Husband and Wife convey the property to Haile and Alemu.

Husband and Wife appealed on several grounds, including a claim that there was insufficient evidence that both Husband and Wife breached the sales contract.

On appeal, Husband and Wife argued that because the property was their community property, that Husband lacked the authority to sell Wife's interest in the property; they also argued the Haile and Alemu had notice of Wife's interest in the property and that without her signature on the sales contract the property could not be sold.

The court looked to §§ 3.003 and 3.102 of the Texas Family Code, which provide (in part) that during marriage, "each spouse has the sole management, control, and disposition of the community property that the spouse would have owned if single" and that such "property is subject to the joint

management, control, and disposition of the spouses, unless the spouses provide otherwise by power of attorney in writing or other agreement."

The appellate court also cited § 3.104(a) for the proposition that "'[d]uring marriage, property is presumed to be subject to the sole management, control, and disposition of a spouse if it is held in that spouse's name, as shown by muniment, contract, deposit of funds, or other evidence of ownership . . .'" Relevant also was the language in this section stating that "[a] third person dealing with a spouse is entitled to rely on that spouse's authority to deal with the property if: (1) the property is presumed to be subject to the sole management, control, and disposition of the spouse; and (2) the person dealing with the spouse is not a party to a fraud on the other spouse and does not have actual or constructive notice of the spouse's lack of authority."

The appellate court found it was undisputed that Husband and Wife purchased the property during their marriage, admitting into evidence a copy of the deed of trust signed by Husband, which listed him as the sole borrower, but which also included the following provision:

> BORROWER(S)' SPOUSE(S): The undersigned hereby joins in this Security Instrument for the sole purpose of encumbering, subordinating, conveying and/or waiving any current or potential interest in the Property. By signing below, the undersigned encumbers, subordinates, conveys and/or waives any and all rights, interests or claims in the Property, including, but not limited to, homestead, dower, marital or joint-occupancy rights. No personal liability under the Note is hereby incurred by the undersigned joining spouse.

Wife's signature appears under this provision. The appellate court found this constituted a waiver of any interest she might have had in the property and cited § 3.104(a) of the Texas Family Code for the proposition that property is presumed to be subject to the sole management, control, and disposition of a spouse if it is held in that spouse's name.

Therefore, as to this issue, the appellate court concluded that Haile and Alemu presented evidence that the property was subject to Husband's sole management, control, and disposition and that they did not have notice that Husband lacked authority to sell the property on Wife's behalf. The appellate court also found that Husband and Wife did not demonstrate that Wife was a necessary party to the sales contract and that the contract was not valid without her signature and Haile and Alemu entered into a valid and enforceable contract with Husband.

"Separate Property Recital" Negates Community-Property Presumption and Creates in Its Place a Rebuttable Presumption of Separate Property

Cardenas v. Cardenas, No. 13-16-00064-CV, 2017 WL 1089683 (Tex. App.—Corpus Christi 2017, no pet. h.) (mem. op.).

Husband and Wife married in 2008 and moved into a house located at 113 Dorothy Street in Cuero, Texas (113 Dorothy). It was undisputed at trial that Husband acquired this property before their marriage. Five years later, Husband took out a loan of $30,000, which Wife used to purchase a second house at 115 Dorothy Street (115 Dorothy). Their relationship ended in 2014 and Wife moved into 115 Dorothy, filing for divorce shortly thereafter.

At a bench trial in 2015, the trial court found that 115 Dorothy was Wife's separate property. Among several other issues, Husband appealed that Wife failed to prove by clear and convincing evidence that 115 Dorothy was a gift.

It was undisputed at trial that the $30,000 loan was taken out in Husband's name only and that Wife used the proceeds from that loan to purchase 115 Dorothy. At trial, it was also shown that the general warranty deed for 115 Dorothy listed the grantee as "[Wife], a married woman dealing with her sole and separate property."

On appeal, the appellate court cited § 3.003 of the Texas Family Code for the proposition that all property possessed by either spouse on dissolution of marriage is presumed to be community property; the appellate court also cited case law establishing that the burden of overcoming this presumption requires proof by clear and convincing evidence from the party asserting otherwise.

The appellate court further recognized case law that held that "a presumption of separate property arises where the instrument of conveyance contains a separate property recital," which can be a statement "in an instrument that the consideration comes from the separate property of a spouse or that the property is transferred to a spouse as the transferee's separate property or for the transferee's separate use." The appellate court stated that "[s]uch a 'separate property recital' negates the community-property presumption and creates in its place a rebuttable presumption of separate property."

Applying the law to the facts of this case, the appellate court found that because the general warranty deed for 115 Dorothy listed Wife as the grantee, dealing with "her sole and separate property," that there was an expressly stated purpose to make the property part of Wife's separate estate, creating a rebuttable presumption that 115 Dorothy was Wife's separate property. The court ultimately found Husband's testimony was insufficient to overcome this presumption.

COMMERCIAL AND RESIDENTIAL LANDLORD-TENANT LAW UPDATE

Jnana Settle
The Settle Law Firm
Dallas, Texas
thesettlelawfirm@gmail.com

The Court Holds That a Non-Conspicuous Limitation of Damages Provision is Nonetheless Binding Against a Party if Course of Dealing and Attorney Representation Indicate That the Party Was Aware of, and Understood the Meaning of, the Contents of the Provision.

McKinney/Pearl Rest. Partners, L.P. v. Metro. Life Ins. Co., No. 3:14-CV-2498-B, 2017 U.S. Dist. LEXIS 36777 (N.D. Tex. Mar. 15, 2017).

The Facts

Tenant in this case sued Landlord for consequential damages under a variety of claims that amounted to an alleged failure of Landlord to keep and maintain the structural system of the building in good condition and repair. Instead of attacking specific elements in Tenant's causes of action, Landlord asserted the affirmative defenses of waiver and ratification. Under the facts, Tenant and Landlord had signed not just the initial lease but also a renewal and both Second and Third Amendments.

Section 17 of the Lease, titled "Landlord's Default/Tenant's Remedies," provides in pertinent part as follows:

> Tenant's remedies for default hereunder and for breach by Landlord of any of its obligations hereunder will be limited to a suit for actual and direct damages and/or injunction. . . . The liability of Landlord to Tenant for any default by Landlord under the terms of this Lease shall be limited to only Tenant's actual direct damages therefor . . . . In no event shall Landlord be liable to Tenant for consequential, punitive or special damages (or any similar types of damages) by reason of a failure to perform (or a default) by Landlord hereunder or otherwise.

The Holding

The court agreed with Tenant that normally a waiver provision must be conspicuous to be binding, and that the provision in the original lease did not meet the requirements. The waiver provision was not in bold, caps, or any other contrasting font. It was contained on pages twenty-four and twenty-five of a thirty-eight-page lease with almost 100 extra pages of exhibits and amendments. However, the court cited an earlier decision that allows such a disclaimer to be effective if it is shown that the plaintiff had actual knowledge of the disclaimer. *Am. Eagle Ins. Co. v. United Techs. Corp.*, 48 F.3d 142, 146 (5th Cir. 1995) (citing *Cate v. Dover Corp.*, 790 S.W.2d 559, 561 (Tex. 1990)). In the instant case, actual knowledge and, furthermore, understanding of the waiver was evidenced by the facts that Tenant was represented by competent counsel, never claimed to be ignorant of the existence of the provision, and encountered the provision in multiple documents.

What to Take Away

It behooves drafters to remember that waiver provisions should receive special treatment in leases. However, all parties must be aware that an argument based upon lack of special treatment in drafting

has an uphill battle to survive evidence of actual knowledge of the provision. In commercial transactions where a Tenant is likely to be represented by counsel, it is highly unlikely that an argument of ignorance would pass muster. Furthermore, the more times that a party has encountered the provision, the less likely that the court will be able to resist some side eye when that party claims the provision should not apply.

Summary Judgment for Bank/Landlord Was Proper in This Case Because in Texas, the Issue of Possession of Real Property is Separate from the Issue of Immediate Right to Its Possession.

Henderson v. Wells Fargo Bank, N.A., No. 05-16-00471-CV, 2017 Tex. App. LEXIS 1833 (Tex. App.—Dallas Mar. 3, 2017, no pet. h.) (mem. op.).

The Facts

Bank in this case became Landlord for the property, and prior borrowers became tenants-at-sufferance, when terms of the deed of trust kicked in post-foreclosure. As in many Texas deeds of trust, the one in this case specifically provided that if the borrowers should fail to vacate the property after a foreclosure, then the borrowers become tenants-at-sufferance. Tenants refused to vacate, claiming defects in the foreclosure process, and appealed the forcible detainer action that was resolved in favor of Bank/Landlord.

The Holding

In Texas, issues of title and possession can be, and often are, treated with separately. A forcible detailer suit decides only the issue of possession and cannot speak to the merits of a title issue. *Yarbrough v. Household Fin. Corp. III*, 455 S.W.3d 277, 280 (Tex. App.—Houston [14th Dist.] 2015, no pet.). The Tenants attempted to frame their argument as a jurisdictional one, claiming that the lower court had no jurisdiction over possession because such possession was based upon a defective transference of title to Bank/Landlord. The court rejected this argument and held to existing law, which says that post-foreclosure the Bank/Landlord had a right to possession as a matter of law, and any challenge to title must come in a separate action.

What to Take Away

Try as they might, tenants in Texas have virtually no luck arguing title issues in forcible detainer suits. Wrongful foreclosure and other title-related suits must be brought separately except in the rarest of cases. *See In re Gallegos*, No. 13-13-00504-CV, 2013 Tex. App. LEXIS 13876, 2013 WL 6056666, at *5 (Tex. App.—Corpus Christi Nov. 13, 2013, orig. proceeding) (mem. op.) (holding that the issues of possession and title may be intertwined when the deed of trust creating the tenancy was void due to forgery).

Texas Legislators Consider Several Bills Affecting the Rental Housing Industry.

The 85th legislative session is in full swing and several bills affecting the rental housing industry are coming up for consideration in both the house and the senate. Although it is impossible to know which bills will still be kicking as of the time of this printing, at least a few of the following issues will likely still be making their way through the process in May:

- SB 873 and its companion, HB 1964, concern water billing disputes between landlords and tenants. The bills would require tenants with water billing disputes to bring a complaint to the Public Utility Commission of Texas (PUC) prior to filing a lawsuit against their landlord. Currently,

tenants have the option of filing a lawsuit prior to bringing any complaint to the PUC.

- HB 2992 would make it a crime to pass a pet off as a service animal for purposes of gaining access, permission, or benefits that a disabled person with a legitimate service animal would receive. This would include anyone claiming that a pet is a service animal to skirt rental property restrictions on pets. The Texas Apartment Association is supporting this bill.
- HB 1966 would prevent landlords from prohibiting either a tenant or a tenant's guest from carrying a concealed handgun in the tenant's dwelling, in a vehicle parked on the property, or when traveling to and from a vehicle and the dwelling.

CONDOMINIUM, TIME-SHARE, AND HOMEOWNER ASSOCIATION DEVELOPMENTS

Clinton F. Brown
Roberts Markel Weinberg Butler Hailey, PC
Austin, Texas
cbrown@rmwbhlaw.com

Where Insurance Proceeds are Insufficient, Special Assessments Levied Against Unit Owners to Pay for Reconstruction of Condominium Units Damaged by a Casualty are Mandatory Under Chapter 81 of the Texas Property Code

Akhtar v. Leawood HOA, Inc., 508 S.W.3d 758 (Tex. App.—Houston [1st Dist.] 2016, no pet. h.).

Leawood HOA, Inc. (the Association) is a condominium association in Harris County, Texas, governed by various documents including a declaration. In September of 2008, Hurricane Ike made landfall in the Houston, Texas area and damaged the Association's buildings including roofs, gutters, and siding (the Common Elements).

The Association had an insurance policy in place covering the Common Elements with a $500,000 deductible or 2% of the insured value of the property governed by the Association. The insurance proceeds were insufficient to complete the repairs to the Common Elements. The Association relied on the declaration in assessing each owner a special assessment according to each owner's proportionate interest in the Common Elements.

Mr. Akhtar owned five units within the Association and failed to pay the special assessment on five of the units. The Association sued Mr. Akhtar in justice court where a judgment was rendered from the bench in favor of the Association. Mr. Akhtar appealed to the county court arguing the special assessment was invalid as the Association failed to conduct a vote of the members prior to levying such assessment. The county court held a bench trial and found for the Association awarding assessments, court costs, and attorney's fees. Mr. Akhtar appealed.

On appeal, Mr. Akhtar contended the special assessment was invalid as the Association failed to obtain a two-third vote of all members approving the assessment.

The court of appeals stated that because the Association was created in 1983, it is governed by both Chapter 81 and Chapter 82 of the Texas Property Code. Chapter 81 governs condominium regimes created before January 1, 1994. Chapter 82 governs condominium regimes created after January 1, 1994, and certain sections of Chapter 82 also apply to pre-1994 condominium regimes.

In contracts, the common meaning for the term "may" is permissive while the term "shall" is mandatory. Similarly, in statutes, "'"May" creates discretionary authority or grants permission or a power,' while '"Shall" imposes a duty'" unless the context indicates otherwise.

Using the common meaning of the term "shall", the court of appeals turned to interpreting article VI of the Association's declaration. Article VI addressed reconstruction of the Common Elements in the event of a casualty. If less than sixty-six and two-thirds of the Common Elements are damaged, the Association had a duty, through use of the term "shall," to repair the Common Elements using insurance

proceeds. In the event such proceeds were insufficient, the Association had a further duty to recover such deficiency against all owners.

The court of appeals found Mr. Akhtar's reliance on article V misplaced as that article addressed permissive and not mandatory special assessments. Because these special assessments resulted from a casualty, article VI and not article V of the declaration controlled.

Finally, the court of appeals turned to § 81.206 of the Texas Property Code, which imposed a statutory duty on the Association to repair the Common Elements by providing, in pertinent part, that "if a building in a condominium regime is damaged by a casualty against which it is insured, the proceeds of the insurance policy shall be used to reconstruct the building." Furthermore, the court of appeals found that if insurance proceeds are insufficient for such repair, § 81.206 imposed a duty on Mr. Akhtar to pay his proportionate share of the repairs.

Accordingly, the court of appeals affirmed the trial court's judgment.

Former and Current Condominium Directors are Generally Entitled to Immunity Protections Against Unit Owners under the Texas Charitable Immunity and Liability Act

Brown v. Hensley, No. 14-14-00981-CV, 2017 Tex. App. LEXIS 727 (Tex. App.—Houston [14th Dist.] Jan. 26, 2017, no pet.).

The Landing Council of Co-Owners (the Association) was a nonprofit condominium association in the City of El Lago, Texas (the City), near Clear Lake and Galveston Bay. It consisted of approximately 6.71 acres of land with 156 condominium units and various amenities. In September of 2008, Hurricane Ike brought high winds and flooding to the Galveston Bay area, including the Association.

Thereafter, in April of 2009, the City declared the Association substantially damaged and out of compliance with City building codes. No action was taken by the Association and in April of 2010, the City declared the buildings within the Association substandard and a public nuisance demanding the buildings be repaired or demolished. In December of 2010, a fire destroyed four of the seventeen buildings within the Association. Thereafter, the Association obtained a permit to demolish the buildings, which occurred in April of 2011.

In September of 2010, six current or former unit owners (the Owners) sued the Association and various board members (the Board Members) for demolishing the buildings rather than repair them alleging breach of contract, negligence, gross negligence, breach of the duty of good faith and fair dealing, and breach of fiduciary duty, among other causes of action.

The Board Members filed a joint motion for summary judgment arguing the claims asserted would not support personal liability against them and that they were entitled to immunity under the Texas Charitable Immunity and Liability Act (the Act). The Board Members also sought to strike voluminous records attached to the Owners' response to the motion for summary judgment arguing they failed to identify the specific evidence within the records, creating a fact issue.

The trial court struck the records, granted the motion for summary judgment dismissing all claims against the Board Members, and granted a joint motion to sever the dismissed claims from the remaining claims against the Association. The Owners appealed.

On appeal, Owners contended the Board Members were not entitled to statutory immunity under the Act. The Board Members responded, indicating the Act did apply and Owners failed to raise any

statutory exceptions to the Act or that there was a duty owed by the board to the Owners individually, as opposed to the Association generally.

It was undisputed that the Act includes homeowners associations within the definition of charitable organizations, and board members are considered volunteers under the Act. Under the Act and subject to exceptions, "a volunteer of a charitable organization is immune from civil liability for any act or omission resulting in death, damage, or injury, if the volunteer was acting in the course and scope of the volunteer's duties or functions, including as an officer, director, or trustee within the organization."

The Owners asserted that while the Board Members may generally fall within the protections of the Act, the Act does not apply to claims brought by members of the Association against the Association's board pursuant to § 84.007(b) of the Act. This section provides that the Act "does not limit or modify the duties or liabilities of a member of the board of directors or an officer to the organization or its members and shareholders."

The court of appeals rejected this argument, finding that this exception applies only to "a derivative action on behalf of the Association or [] a class action on behalf of all unit owners." Because Owners' lawsuit was neither, the exception did not apply. Further, the court of appeals could not determine whether any fiduciary duty owed to the members arose out of the governing documents of the Association, because they were not included within the appellate record as Owners failed to contest the trial court ruling striking their summary judgment evidence on appeal.

The court of appeals held the trial court did not err in granting Board Members' motion for summary judgment based on the immunity exception under the Act as the evidence established Board Members were members of the board for the Association, the Association was a charitable organization, and Board Members were making decisions on behalf of the Association. The court of appeals acknowledged supporting case law indicating that "[f]or immunity purposes, a person is acting within the scope of his authority if he is discharging the duties generally assigned to him even if the specific act is wrong or negligent."

Accordingly, the court of appeals affirmed the trial court's judgment.

TITLE MATTERS UPDATE

Jeremy T. Brown
Irelan McDaniel PLLC
Dallas, Texas
jbrown@imtexaslaw.com

Inclusion of Additional Leases Not Included in Original Mortgage Held Material for Purposes of Correction Deed Statute

Tanya L. McCabe Trust v. Ranger Energy LLC, 508 S.W.3d 828 (Tex. App.—Houston [1st Dist.] Dec. 22, 2016, pet. filed).

In August 2008, Tomco Energy, PLC executed an assignment and bill of sale to Mark III Energy Holdings, LLC (Mark III) to "'six of the eight oil and gas leases which are collectively known as the "Saratoga Leases".' The parties stipulated that '[d]ue to an inadvertent error, two of the Saratoga Leases were omitted' from an 'Exhibit A'" attached to the 2008 assignment, known as the McShane Fee and Brice leases. Mark III borrowed $4 million from Peoples Bank to finance the purchase. Mark III executed a financing statement security agreement and mortgage (the 2008 Mortgage) to secure the loan and like the 2008 assignment, it omitted the McShane Fee and Brice leases (the Leases). Three years later, Mark III assigned its interests in these leases to two trusts (the Trusts).

Mark III fell behind on its loan payments and Peoples Bank filed a foreclosure suit. To resolve that dispute, Mark III paid the bank $750,000 and executed a renewed and modified deed of trust in 2012. That renewed deed of trust included a substantively identical Exhibit A to the original 2008 mortgage, and therefore, it also omitted the McShane Fee and Brice leases. Soon afterwards, Peoples Bank realized the omission and recorded a revised version of the 2012 deed of trust, adding the word "corrected" to the front page and adding the two other leases to the property description. It also filed revised versions of the 2008 Mortgage to make this same change.

Neither Peoples Bank nor Mark III signed these corrected versions. Instead, the bank simply used the signature pages from the original documents and sent copies to Mark III after filing. Two months later, Peoples Bank and Mark III entered into a second settlement agreement that stated the bank had a right to foreclose on the property listed in the revised 2013 instruments. Peoples Bank transferred its security interest to Ranger Energy, who then foreclosed.

In May 2013, Ranger Energy filed a declaratory judgment action asserting that the foreclosure sale extinguished the Trusts' interest in the Leases. Both parties moved for summary judgment, and the trial court rendered judgment in favor of Ranger Energy. The Trusts appealed, arguing that 2013 revised documents did not comply with the correction instrument statutes as a matter of law, and therefore, Ranger Energy lacked a security interest in the Leases.

The Texas Property Code allows correction of nonmaterial and material changes to real property instruments. The statute specifies that a person with personal knowledge of the transaction may make "a nonmaterial change that results from inadvertent error, including the addition, correction, or clarification of: (1) a legal description prepared in connection with the preparation of the original instrument but inadvertently omitted from the original instrument." TEX. PROP. CODE § 5.028(a-1)(1). In addition, only parties to the original contract may execute a correction instrument that makes material changes, which include a "correction to . . . add . . . land to a conveyance that correctly conveys other land." TEX. PROP. CODE § 5.029 (a). Thus, the distinction of material and nonmaterial is important because

a nonmaterial change may be affected by someone with personal knowledge of the transaction, while a material change may only be affected if the correction instrument is signed by the parties to the transaction or their heirs or successors.

It was undisputed the parties to the transaction did not execute the 2013 correction instrument, so the appeal turned on whether the addition of the Leases was an "addition" of a legal description or whether it "add[ed] . . . land to a conveyance that correctly conveys other land." The court of appeals held it was the latter, relying on the Texas Supreme Court decision *Myrad Properties, Inc. v. LaSalle Bank National Ass'n*, 300 S.W.3d 746 (Tex. 2009). In *Myrad*, the court held that a correction deed could not be used to convey two parcels of land at a nonjudicial foreclosure sale after the original deed unambiguously had conveyed only one of the mortgaged parcels. *Id*. at 750-51. The legislature responded to *Myrad* by enacting §§ 5.027 through 5.031 of the Texas Property Code, codifying the circumstances in which a correction instrument may be used, and despite *Myrad*'s concerns, expressly permitting material changes to be made through a correction instrument.

The court of appeals characterized the 2013 revisions as purporting to add property interests in two leases that previously were not listed. And it held that "the addition of land to a conveyance that correctly conveys other land is a material change." *Ranger Energy LLC*, 508 S.W.3d at 842 (citing TEX. PROP. CODE § 5.028(a)). Therefore, it reversed the trial court and remanded the case.

The majority did not, however, explain how the "addition of" legal description could be reconciled with its holding. Presumably, under this court's view, if a conveyance was missing a legal description in total, the addition of a legal description would be considered a nonmaterial change. But if a legal description was included and conveyed at least some property, then any addition to that legal description to convey more property would be a material change that must be signed by the parties to the transaction.

Justice Evelyn V. Keyes dissented. She found it was undisputed that Tomko conveyed the leases to Mark III in 2008. Because of this contemporaneous conveyance, the correction instrument did not, in her view, "add to" land in a prior conveyance and therefore was nonmaterial and valid. *Id*. at 854 (Keyes, J. , dissenting).

Railroad Deed with Ambiguous Granting Clause Interpreted to Only Convey Easement Despite Presence of Fee Simple Language

BNSF Ry. Co. v. Chevron Midcontinent, LP, No. 08-16-00119-CV, 2017 WL 1076540, (Tex. App.—El Paso Mar. 22, 1017, no pet. h.).

Chevron struck oil in Upton County, Texas, beneath a BNSF-owned railroad. BNSF sued Chevron for trespass to try title, arguing a 1903 deed gave the company not just a right of way easement, but the entire strip of land described in the deed in fee simple absolute. Chevron contended the deed only gave BNSF a right of way to pass trains over the strip, and everything below the land was free and clear of any BNSF interest.

The granting clause in 1903 deed stated as follows:

> WITNESSETH, That the said party of the first [Goode], for and in consideration of One Dollar . . . and of the benefits which will accrue to the party of the first part by reason of the construction of a line of railroad over the land hereinafter described . . . has GRANTED, BARGAINED, SOLD and RELINQUISHED, and by these presents does GRANT, BARGAIN, SELL, RELINQUISH and CONVEY unto the said party of the second part [Panhandle], and unto its

> successors and assigns, for a right of way, that certain strip of land hereinafter described, as the same has been finally located over, through or across the following tracts of land situated in Upton County in the State of Texas . . . .

Id. at *1. The deed then described a line traced by surveyors across various plots of land between various train stations. Using the line as a reference, the deed described the width of the right of way as follows:

> The said railway right of way being 100 feet wide on each side of the center line thereof except [for certain sections where the right of way varies between 50 feet and 150 feet] ... Said railway right of way containing an area of 28 and 55/100 acres. Together with the right and privilege of taking and using all of the wood, water, stone, timber and other materials on said strip of land, or appertaining thereto, which may be useful or convenient in the construction and maintenance of said railway or any part thereof.

Id. The 1903 deed ended with the following habendum clause: "TO HAVE AND TO HOLD the said premises, together with all appurtenances thereunto belonging, in fee simple, unto the said part of the second part [Panhandle] its successors and assigns forever." *Id*.

The court of appeals accepted BNSF's argument that in Texas, "right of way" is not a legal term of art with a set definitive meaning when used in a deed and can be used in two different ways: (1) to describe a party's right of passage over a tract of land; and (2) "to describe that strip of land which railroad companies take upon which to construct their road-bed." *Id*. at *3. The court cited three cases in which conveyances to railroads had conveyed fee simple title, rather than a simple right of way passage right. *Id*. (citing "*Brightwell v. Int'l-Great N. R.R. Co.*, 49 S.W.2d 437, 439-40 (1932) (deed conveyed 200-foot-wide strip of land in fee simple); *Calcasieu Lumber Co. v. Harris*, 13 S.W. 453, 453-54 (1890) (deed conveyed 100-foot-wide strip of land to railroad in fee simple); *Right of Way Oil Co. v. Gladys City Oil, Gas & Mfg. Co.*, 157 S.W. 737, 739 (1913) (noting that while historically railroad rights-of-way were usually conveyed as easements, the 'land . . . may [also] be conveyed in fee; therefore the character of the title conveyed must be determined by the words used and the attending facts and circumstances')").

The court explained that the Texas Supreme Court set forth the rule of construction in these circumstances in 1952 in *Texas Electric Railway Co. v. Neale*:

> [A] deed which by the terms of the granting clause grants, sells and conveys to the grantee a 'right of way' in or over a tract of land conveys only an easement . . . [but] a deed which in the granting clause grants, sells and conveys a tract or strip of land conveys the title in fee, even though in a subsequent clause or paragraph of the deed the land conveyed is referred to as a right of way.

Id. at *4 (quoting *Texas Elec. Ry. Co. v. Neale*, 252 S.W.2d 451, 453 (1952)).

BNSF argued that use of the word "a strip of land" in the granting clause was conclusive, and relying on *Neale*, the clause "for a right of way," merely referenced a purpose that was not intended to modify the interest conveyed. *Id*. at *5. The court explained that *Neale* only stated that a statement of purpose "in a subsequent clause or paragraph of the deed" does not alter the interest conveyed in the granting clause. It did not, however, provide that a statement of purpose included in the granting clause itself lacked any effect on the interest conveyed. In the court's view, including right of way in the granting clause along with "that certain strip of land" rendered the granting clause ambiguous, and therefore, the

Neale rule did not apply. Because the granting clause was ambiguous, the court found it necessary and proper to examine the remaining parts of the deed as a whole to glean the grantor's intent.

Reading the deed as a whole, the court found Chevron's interpretation that only an easement was conveyed was the only reasonable conclusion based on the following facts:

- The opening recitals recognized the value of having a railway pass "over" the land";
- The phrase "right of way" appears directly in front of phrase "that strip of land";
- The clauses describing the conveyance described the right of way "[o]ver, through, and across" the land;
- The deed specifies that the conveyance also included a right to use the resources on the right of way, which would be unnecessary if the grantor intended to convey fee simple title; and
- The habendum clause referenced "the said premises," instead of "property," which suggested conveyance of only an easement.

Chevron argued the "fee simple" language in the habendum clause was not inconsistent with these other parts of the deed because it was simply a characterization of the duration of the easement. Chevron relied on other jurisdictions' interpretation of "easements in fee simple" to mean that the easement is held in perpetuity and may be disposed of at will. The court was unwilling to go that far, and simply held that the habendum clause's "fee simple" language should be disregarded because it conflicts with the remainder of the deed when read as a whole. *Id*. at *8.

Buyer Held to Have Constructive Notice of Abstract of Judgment Filed Against Party with Two Surnames

Austin v. Coface Seguro de Credito Mex., S.A. de C.V., 506 S.W.3d 707 (Tex. App.—Houston [1st Dist.] 2016, pet. filed).

In this appeal, the court of appeals addressed whether differences in naming conventions nullify notice of an abstract of judgment. A bank obtained a judgment in Mexico and later registered it in Texas state court, using the debtor's full name, which included a first and a second surname "Rafael Augusto Martin Ojeda Miranda." When the bank abstracted the authenticated judgment in the county records, the county clerk indexed the judgment under the last name "Mirandas," instead of "Miranda;" thus, the record index recited "Mirandas Rafael Augusto Martin Ojeda." In other words, the abstract of judgment was not indexed under the other surname "Ojeda." In July 2013, Carolyn P. Austin purchased the property from the judgment debtor by way of a warranty deed naming "Rafael Ojeda and wife, Liyian E. Cordova" as grantors. At the preclosing meeting, the judgment debtor produced a passport showing his full name. The title search did not search the real property records using either the name "Miranda" or Rafael Augusto Martin Ojeda Miranda," and neither the buyer nor the title company discovered the abstracted judgment before closing. When the bank sought to foreclose on the property, the owner filed suit, seeking a declaration that the bank's abstract of judgment lien did not encumber the property.

The owner contended that the bank was obligated to secure an index under the first surname listed in the abstract of judgment to enforce its lien on the property, because the warranty deed that conveyed the property named the seller by his first name and first surname only. The bank responded that the chain of title for the property includes the debtor's full name as it is contained in the abstract of judgment. On cross-motions for declaratory relief, the trial court found in favor of the bank.

The court of appeals affirmed but declined to address whether the abstract of judgment needed to be indexed under both the paternal and maternal surnames because other parts of the chain of title provided record notice of the name in which the abstract of judgment was indexed. In particular, the real property records included a notice of lis pendens, which identified the judgment debtor by his full name and alternatively included "Rafael Ojeda." *Id*. at 713. Because of this, the court of appeals held that the owner and title company had constructive knowledge of the judgment debtor's full name, because it was contained both in the abstract of judgment and in the real property records indexed under either surname. *Id*.

PROPERTY TAX LAW UPDATE

John Brusniak
Brusniak Law PLLC
Dallas, Texas
john@txtax.com

If an Appraisal District Creates Separate Account Numbers to Cover Parts of a Complex Facility, Then a Taxpayer May Challenge Any of Those Parts Under an Equality Theory Without Challenging the Entire Value of the Facility.

Valero Refining-Tex. L.P. v. Galveston Cent. Appraisal Dist., No. 15-0492 (Tex. Feb. 24, 2017).

Appraisal district assigned different account numbers to a variety of the components of a property owner's refinery including pollution control equipment. The property owner appealed some of the accounts on the basis of inequality to district court. On appeal, the Texas Supreme Court rejected the appraisal district's argument that a taxpayer must appeal the entire valuation of a complex facility stating, "If the component parts of a property cannot be valued in isolation, then as a matter of law, separate tax accounts are not appropriate. It follows that if tax accounts are appropriate, then, as a matter of law, the property in each account can be valued in isolation." It further rejected the appraisal district's argument that the only reason the taxpayer failed to include pollution control equipment in its suit was because it was trying to lower the value of the property: "While the District complains that Valero has excluded PCE values to obtain a more favorable result, one would expect a party to do exactly that."

An Appraisal District May Not Assess Pooled Mineral Interests That Are Located Outside Its County Lines If the Lease Authorizes Pooling But Not Cross-Conveyances of Interests.

Chambers v. San Augustine Cnty. Appraisal Dist., No. 12-15-00201-CV (Tex. App.—Tyler Feb. 8, 2017, no pet. h.).

Taxpayers owned land in Shelby county and entered into oil and gas leases. Their interests were pooled with production units located in San Augustine County. The San Augustine County Appraisal District sent a notice of appraised value to the taxpayers. Taxpayers protested claiming the district did not have the right to appraise their property because it was located in Shelby County. The taxpayers pointed to language in their leases that allowed pooling but prohibited cross-conveyances of their interests. The court of appeals ruled that taxation was contingent upon the wording of the leases. "Giving effect to all language of Appellants' leases, we conclude, as a matter of law, that the leases authorize pooling but prohibit cross-conveyance of interests. . . . Accordingly, SCAD failed to establish that Appellants owned an interest in pooled minerals located in San Augustine County."

Property Owners Are Not Required to Specify Grounds of Relief in a Petition For Review Of an Appraisal Review Board Order.

United Airlines, Inc. v. Harris Cnty. Appraisal Dist., No. 14-15-01014-CV (Tex. App.—Houston [14th Dist.] Dec. 6, 2016, pet. filed).

Taxpayer owned personal property in Harris County. Taxpayer protested the value of its property before the appraisal review board and filed an appeal to district court. In its original petition, it claimed

the appraised value of the Property was excessive and attached the orders from the appraisal review board hearing. The Taxpayer later amended its petition and removed its claim for excess appraisal and added a claim for unequal appraisal and reattached the same orders. The appraisal district filed a plea to the jurisdiction asking the court to dismiss the case, claiming the court did not have jurisdiction over the excessive appraisal claim since the filing of the amended petition acted as a dismissal of the original petition, and because the unequal claim was not timely filed within the sixty-day deadline for seeking judicial review. The Taxpayer then filed a second amended petition, again pleading a claim under excessive appraisal, and again reattaching the same orders. Additionally, the Taxpayer filed a motion to withdraw its first amended petition, or in the alternative, motion to reinstate its original petition, claiming the first amended petition was filed in error. In response, the district court dismissed the case. On appeal, the court ordered the case reinstated. "In adopting the current tax protest mechanism, this court has noted 'the legislature rejected hypertechnical requirements for challenges to appraisal values.' . . . Indeed, nothing in either the Tax Code or the case law requires a party to include its grounds of relief in a petition for review in order to invoke the jurisdiction of the trial court. . . . Further, sections 42.25 and 42.26 do not address whether a party must plead relief under these provisions . . . . Moreover, other parts of the Tax Code demonstrate that stating the particular grounds for appeal is not jurisdictional and need not be contained in the petition. . . . Finally, there are no consequences in Chapter 42 for failing to plead a particular ground for relief, which supports the conclusion that pleading certain grounds is not a jurisdictional requirement to maintain an ad valorem tax appeal."

Owners of Land May Be Taxed Separately on the Value of Their Surface Estates and the Value of Salt Water Disposal Wells Located on the Land from Which They Are Deriving Revenue.

Parker Cnty. Appraisal Dist. v. Bosque Disposal Sys., LLC, No. 02-15-00343-CV (Tex. App.—Fort Worth Dec. 1, 2016, pet. filed).

Taxpayers owned land on which saltwater disposal wells were located. A third-party appraisal firm hired by the appraisal district valued the wells separately from the surface estate based on an income approach to value. After exhausting administrative remedies, taxpayer sued claiming that the procedure was illegal because the value of the wells was subsumed within the valuation of the surface estate and that the assessment of the disposal wells absent their severance from the land constituted a double tax assessment. The court of appeals disagreed citing both the Tax Code and judicial precedent and ruled that at least some "aspects of real property can be taxed separately even though all are part of the same surface tract." It went on to say that "it is not the severance of the surface and subsurface estates by conveyance that gives a taxing authority the right to assess different types of property interests." And it concluded that the interest taxed was not intangible in nature because the appraisal district did not value the permit allowing the use of the disposal wells, but rather it valued the income that was received from the use of the separate estate.

Affirmatively Asking an Appraisal Review Board to Deny a Protest Is the Same As Failing To Appear At the Hearing and Results In a Failure to Exhaust Administrative Remedies; Taxing Units Do Not Have Standing to Sue Under the Tax Equity Provisions of the Tax Code; Governmental Entity Must Demonstrate a Specific Injury to Itself to be Able to Sue an Appraisal District.

City of Austin v. Travis Cent. Appraisal Dist., No. 03-16-00038-CV, (Tex. App.—Austin Nov. 10, 2016, no pet.).

The City of Austin filed suit against the appraisal district, the state of Texas, and all property owners

of vacant land and certain commercial real property within Travis County. The City of Austin claimed that the appraisal district's appraisals of vacant and commercial real property in Travis County were unequal when compared to other categories of property for tax year 2015. The trial court dismissed the lawsuit for lack of jurisdiction. The City of Austin claimed certain categories of properties had been undervalued in tax year 2015, due to reductions made during protest hearings, which reduced the median value in violation of the constitutional requirement that property be taxed at its market value and taxation be equal and uniform. The court of appeal determined that the City of Austin failed to establish an injury sufficient to establish standing. The claims brought by the City of Austin are provisions of the tax code that provide taxpayers the right to protest their appraisals. Sections 41.43(b)(3) and § 42.26(a)(3) do not provide a taxing unit any authority to implement these sections. The Tax Code also provides limited authority to governmental entities to challenge determinations made by an appraisal district. To appeal to a district court, a taxing unit must exhaust its administrative remedies. The City of Austin failed to exhaust its administrative remedies in this case because, even though it appeared at the protest hearing, it did not present a case on the merits of the challenge, and instead presented a joint motion requesting the Appraisal Review Board to deny its protest. Since the City of Austin appeared at the hearing solely to ask the Appraisal Review Board to deny its protest, the Appraisal Review Board was deprived of the opportunity to make a decision based on the merits of the protest. The court of appeals affirmed the trial court's ruling and found that the City of Austin's dispute was over tax policy, which is not to be determined by a court, but better suited for the legislature.

REAL ESTATE & OIL AND GAS TAX UPDATE

Edward E. Hartline
Oaks, Hartline & Daly, LLP
Houston, Texas
hartline@ohdlegal.com

Taxpayer Did Not Show Dedication in Excess of 750 Hours and Therefore, was Not Considered a Real Estate Professional

Rapp v. Comm'r, U.S.T.C. 2017-14 (2017).

In *Rapp*, the taxpayer was involved as an employee of two firms in the development of commercial real estate. Taxpayer worked full time in connection with this activity. Taxpayer was the property manager for his five rental properties but did not provide any evidence about how much time he spent on his rental activities during the year. Taxpayer did not own any interest in the two real estate businesses that employed him but he had been told he might receive an equity interest if he developed an independent project. It was clear that the taxpayer spent well over 750 hours during the year working as an employee of the real estate companies. The provisions of § 469(c)(7)(D)(ii) indicate that personal services performed by an employee shall not be treated as performed in real estate trades or businesses. However, if the taxpayer owns more than 5% of the entity for which he is an employee then the hours can be counted. In this case, it was found that the taxpayer did not show that he dedicated in excess of 750 hours per year toward the management of his personal real estate portfolio and therefore, was denied a deduction for the losses incurred on the rental real estate.

Taxpayer Determined to be Real Estate Professional and Thus, Real Estate Losses were Not Barred from Being Claimed

Zarrinnegar v. Comm'r, 113 T.C.M. 1148 (2017).

In *Zarrinnegar*, the taxpayers were again attempting to deduct losses incurred in connection with rental real estate. In this case, both taxpayers were dentists who shared a staggered dental practice. The government contended that the taxpayers were not real estate professionals and did not spend the requisite hours in connection with their real estate rental activity and also kept inadequate records of charges for supplies and how they are related to their dental practice. Petitioner husband worked at real estate brokerage activities in addition to his dental practice. He spent hundreds of hours on brokerage-related activities including brokers' tours, listing searches, open houses, property viewing, and client meetings. It was clear that petitioner spent more than 1,000 hours on the real estate business. In determining the number of hours husband spent in the real estate activities, the court noted that contemporaneous time reports, logs, or similar documents are not required. The number of hours can be shown by reasonable means, which can include the identification of the services performed over a period of time and the approximate number of hours performing such services during such period based upon appointment books, calendars, and narrative summaries. A post-event ballpark guesstimate is not sufficient, but neither is a contemporaneous time log required. The court's finding was that the Petitioner worked more hours on his real estate activities than he did on his dental practice and thus, qualified as a real estate professional and thus, losses on his rental real estate activities were allowed. However, Taxpayers were penalized for keeping insufficient records concerning expense deductions related to their dental practice.

IRS Adds Matters to its No Ruling List

Rev. Proc. 2017-3.

Internal Revenue Service was discussing additional matters which were to be added to its no ruling area. One of the areas involved the tax consequences of shared appreciation mortgage loans in which a taxpayer borrowing money to purchase real property pays a fixed rate of interest on the mortgage loan below the prevailing market rate and will also pay the lender a percentage of the appreciation value of the real property upon termination of the mortgage. The Service said that this would be a no ruling area if the facts are not similar to those described in Revenue Ruling 83-51. This revenue ruling describes three separate situations where money was advanced to a taxpayer under a shared appreciation mortgage arrangement. In each case, the loan bore current interest plus some share of the appreciation payable at the time the property was transferred or the loan paid off. In one of the transactions, the taxpayer had the shared appreciation mortgage for the full term of the shared appreciation loan and at the end of that loan, the taxpayer refinanced the loan and paid a percentage of the appreciation to the shared appreciation mortgage loan holder. In this situation, the taxpayer was not allowed to deduct the contingent interest on the shared appreciation mortgage loan because pursuant to the refinancing, the loan was not deemed "paid" and thus, the contingent interest was not deductible. In the other two instances, the property was transferred or the loan was paid off. To reach a position consistent with rulings issued by the Internal Revenue Service, on a shared appreciation mortgage loan, for the contingent interest to be considered deductible under § 163, the loan must be "paid" at the termination of the shared appreciation mortgage.

A CONSERVATION EASEMENT ON CAMP RIO: HOW IDEA PUBLIC SCHOOLS, INC. TRANSCENDED TAX INCENTIVES

Jesus "Jesse" Barba Jr.
Mayfair | Rioco
McAllen, Texas
jbarba@rioco.com

In late 2016, the award-winning charter school system, IDEA Public Schools, secured ownership of an eighty-five-acre tract of land nestled just inside the city limits of Brownsville, Texas. It was a historic moment for the public school and the conservation sector. Not only would public school students in the Rio Grande Valley benefit from an outdoor classroom facility, a rare piece of South Texas earth could be preserved for those students.

It is also extraordinary for its unique intersection of a public charter school, conservation easement holder, and private landowner. Historically, the eighty-five-acre facility had been known as Camp Lula Sams. For several generations, it served as a well-known retreat for Girl Scouts of the Rio Grande Valley. Over the years, however, it became used less often and eventually fell into disrepair. In 2001, a group of investors purchased the facility to hold for future use. In the meantime, they held private instructions on environmental resources at the Camp. Eventually, it became evident that classes in ecology would never fully support the steadily increasing march of taxes and maintenance costs. Inevitably, the Camp had to be sold.

The owners, however, faced a conundrum if it wished to preserve the environmental aspects of the property. As investors, they had to be fully compensated for their ownership and could not deplete its value through a property restriction on use, yet they knew they had to preserve the Camp for its unique wildlife habitat and native forestry. A conservation easement would satisfy the latter. The former could only be satisfied if a buyer was willing to pay fair market value for fee simple title but still agree to assume an enormous restriction on the land.

This proposition to restrict use yet demand full market value would be difficult for traditional developers to accept. A conservation easement typically devalues the property from 40% to 60% of its commercial value/potential. In addition, the conservation easement is accompanied by a slew of additional land burdens. Effectively, the landowner conveys away the development rights to the property, dramatically reducing its development potential, obviously, and also its use. Furthermore, from a business standpoint, given the ever-present challenges of taxes and maintenance, the property would still need to yield adequate revenues to pay for its own existence. Under these circumstances, there is a naturally dramatic winnowing of interested buyers.

Enter IDEA Public Schools. Chartered in 2001, it has grown from a small campus of 187 students in tiny Donna, Texas, to nearly 30,000 enrolled in the fall of 2016. In the Rio Grande Valley alone, there are 21,000 students in thirty-one schools as of 2016. By 2022, IDEA schools are projected to have 100,000 students in over eighty-seven different campuses. It is a growing program that considers itself an education innovator. As luck would have it, IDEA had been seeking a location to apply an adventure-based, outdoor learning environment to augment its growing ensemble of campuses. And, this new owner would not mind a property restriction, such as a conservation easement, that placed conservatorship of the land into its own business plan for expanding the school system.

Typically, a property owner would seek out a conservation easement donation to obtain certain

favor tax incentives. Interestingly, there was no use for the traditional tax-based incentives for this conservation easement donor. Whereas a conservation easement donor could claim a favorable tax credit, as a 501(c)(3) corporation, the nonprofit could not enjoy those tax privileges. They would be inapplicable.

To allow for the tax deductions, the conservation easement must qualify under several related guidelines. I.R.C. § 170(h). First, the conservation must be protected in perpetuity, meaning forever. Treas. Reg. § 1.170A-14[g][4]. Second, the CE holder itself must qualify. Typically, these are nonprofits that have a conservation-centric mission, such as the Valley Land Fund, the holder of the Camp Rio easement. And third, the grant must be done for a "conservation purpose." Here, the law becomes a little more technical. In a nutshell, the CE may be either for outdoor recreation, protection of natural habitat, preservation of open space, or preservation of historically important land. The taxpayer seeks those pathways to obtain a tax deduction.

For example, a taxpayer holding land (typically open space or wildlife land) can seek the tax deduction for its donation of the conservation easement. Assume there is a ranch valued at $4,000,000, with a conservation easement coming off that land valued at $1,200,000. This would imply a 30% reduction in property value because of the donated conservation easement. The IRS would allow the tax payor to take tax deductions up to 50% of the donor's adjusted gross income (or AGI). If the donor earns $150,000 in AGI, then allowed deduction would be $75,000. Should that donor continue to earn $150,000 in AGI for the next several years, then that taxpayer would only deduct $75,000 over the next fifteen years when he or she has exhausted the $1,200,000 contribution.

Had the public school sought out the special tax treatment, it would need to demonstrate its intent of the charitable gift. Under the Treasury Regs, the donor must (i) obtain a qualified appraisal (described under typical gift guidelines under IRS Form 8283), (ii) commission a baseline study of the "conservation values" on the land, and (iii) record a conservation easement document that grants the easement to a qualified land trust. Treas. Reg. §1.170A-14[g][5].

It will be also important for the landowner to have all other interest on the land subordinated, including mortgagees and surface mining. As holders of superior rights, these interested parties would render the conservation easement meaningless if they could simply demolish the surface estate or foreclose against the CE. Surprisingly, it is not terribly difficult to secure a subordination from a lienholder. Mortgagees simply look to the value of the collateral and whether sufficient equity exists to justify a foreclosure against a burdened real property. Similarly, a surface use waiver can be obtained from the mineral estate holder. There may be some research to confirm who has the executory rights to sign off on the subordination. However, a mineral interest holder can be persuaded to keep the mineral rights as part of a pool, just not exercise the surface for the actual drilling operation. If it's possible that the executory rights or other mineral rights remain so disperse as to be remote, the IRS does allow the property owner to forego the subordination if he can prove up this possibility in a mineral remoteness report.

In the case of Camp Rio, the landowner met all the requirements for a true conservation easement and went through the motions to substantiate the conservation easement. The conservation values were documented: the land has a thriving Sabal Palms forest as well as rare species of birds and animals. IDEA then established a conservation purpose, being the protection of the native plants and wildlife. The school even conveyed its mineral rights, which it obtained from the prior landowner, to the Valley Land Fund, which qualified as the conservation easement. It was truly a collaborative effort that benefited all the interested parties.

While the school could not benefit from making an adjustment to its taxable income, the exercise of creating the conservation easement resulted in more than just the protection of the land. The value of the easement came from enhancing the use of the outdoor classroom and in the long-term economic value in preserving the economic landscape of the property. No short-term future development could displace the conservation values from the students sent to learn at Camp Lula Sams. Neither could the land be threatened into development by creditors or prospective partners, seeking a short-term gain on a current asset. This also serves as an immeasurably valuable consideration for an organization that relies partially on secured financing for its school funding. The economic value, therefore, resides not in a mere IRS tax deduction but rather in promoting the exceptional benefits of an outdoor classroom, forcing economic value from a long-term hold, and neutralizing risk to the organization.

There are, therefore, economic benefits to the land owner from a conservation easement that transcends the tax incentives. There are tax incentives to the traditional conservation easement to be sure. However, alternative uses of the conservation easement can follow such innovative approaches as well.

GAME OF ETJS: MUNICIPAL ANNEXATION AND EXTRA-TERRITORIAL JURISDICTION

Kevin Pierce
SMU Dedman School of Law
Dallas, Texas
Kpierce@smu.edu

STUDENT WRITING CONTEST

Honorable Mention – Real Estate 2016

In the State of Texas, a conflict is being fought on the local and legislative level. It pits residents who have chosen to live free from the confines of local government with municipalities that seek to increase their territory and their tax revenue. The law relating to municipal law and extraterritorial jurisdiction affects millions of Texans but, outside of the attorneys who specialize in this area, it remains somewhat of a black box for the outside observer. But with an understanding of the fundamentals, an attorney can gain the foundation to be proficient in this interesting and evolving area of the law.

The main hub of statutory provisions relating to ETJs are codified under Chapter 42 of the Texas Local Government Code (TLGC), but references to the extraterritorial jurisdiction of a town, city, or municipality can be found throughout all the Texas codes. The term "extraterritorial jurisdiction" as a discrete concept with directly quantifiable borders did not exist until 1963, when the Texas Legislature passed HB 13, which came to be known as the Municipal Annexation Act.[1]

The ETJ of a municipality is the unincorporated area contiguous with its corporate limits.[2] The size of extraterritorial jurisdiction that a given municipality has is determined by the number of inhabitants in that municipality.[3] Generally, the ETJ area is expanded every time the boundaries of a municipality grow, typically by means of annexation.[4] As a general rule, municipalities may only annex land that is within its ETJ, though there are exceptions.[5] The ETJ of a municipality may also expand if the property

[1] TEX. REV. CIV. STAT. ANN. art. 970a.

[2] *Id*.

[3] *Id*.

[4] TEX. LOC. GOV'T CODE § 42.022(a).

[5] *Id*. § 43.051.

owner, who is contiguous with the ETJ boundary of a municipality, petitions that municipality include the property in the municipality's ETJ.[6]

Main Entities Involved in ETJs and Annexation

There are three main groups that municipal annexation affect the most: municipalities, land developers, and residents. Municipalities directly deal with their ETJ more than any other entity. Municipalities can be broken up into two main types, home-rule municipalities and general-law municipalities, which is an important distinction particularly regarding municipal annexation and will be explored further below. Land developers often work within a municipality's ETJ for their projects. Developing land for projects, such as housing divisions, in a municipality's ETJ allows developers to have the reasonable certainty that their division will be annexed into a growing municipality, which is a selling point for home builders, but at the same time not be directly limited by a municipality's development standards or be subject to the municipality's tax levies during the development and construction periods. Finally, residents who reside in the ETJ might not be very important to the formation of annexation law, but they are the most impacted group when it comes to annexations.

Home-Rule and General-Law Cities

There are two main types of municipalities in Texas: home-rule municipalities and general-law municipalities.[7] General-law municipalities only have the powers specifically granted to them by the Texas Local Government Code.[8] Conversely, home-rule municipalities may give themselves whatever powers they wish through the use of a charter, so long as the provisions of the charter are not in conflict with any prohibition in the Code.[9] General-law municipalities can only annex areas that volunteer for annexation, with narrow exceptions.[10] Conversely, home-rule municipalities have far greater latitude to annex areas in their ETJ involuntarily, subject to certain exceptions.[11] General-law municipalities have additional restrictions to the annexation process.[12]

Nature of Extraterritorial Jurisdiction in Texas

Many Texans lived in a municipality's ETJ and do not realize it. While the ETJ of a municipality is subject to municipal actions, it is not a part of the municipality. Municipalities typically prepare and intend to grow as new residents arrive and having areas "prepped" for future annexation smooths the process along. Residents in ETJs pay no taxes to the correlating municipality. Tax revenue is a major incentive to municipalities that are seeking to increase tax revenue and annexation is one efficient way to increase their tax base.

---

[6] *Id*. § 42.022(b), which allows homeowners who are worried about an encroaching municipality from another direction taking them up by annexation to expand ETJ. By placing themselves in the ETJ of a municipality that cannot or most likely will not expand (such as a general-law municipality boxed in by other municipalities), they prevent their property from being annexed into any city.

[7] *See id.* § 5.

[8] *See generally id.* §§ 6-8.

[9] *See generally id.* § 9.

[10] *Id*. § 43.033.

[11] *Id*. § 43.034.

[12] *Id*. § 43.032.

There are some situations where municipalities do not seek to annex territory. Small towns have their own governing boards and they serve at the will of their voters and an influx of new voters may change the political makeup of the governing body. Further, if the area is sparsely populated, or geographically remote, the cost to provide full municipal services may outweigh the anticipated tax revenue.

How is the ETJ Formed and How Does It Grow?

The amount of ETJ ranges from a one-half mile from the city boundaries to five miles from the city boundaries, and the inhabitant amount necessary to have an ETJ of five miles requires a minimum of 100,000 inhabitants.[13] The actual range of a municipality's ETJ is not a perfect circle around a municipality. Municipalities do not annex in neat or tidy sections and because the ETJ of one municipality cannot intrude upon a neighboring municipality's ETJ, determining the ETJ boundary of a given municipality can be troublesome and messy.[14]

Municipal Annexation

Annexation is an orderly process of acquisition of territory around a municipality. Annexation of territory in a municipality's ETJ is primarily covered under Chapter 43 of the TLGC.[15] Subject to exceptions (of which there are many), a municipality may only annex land that is (1) contiguous with its corporate boundaries and (2) within its ETJ.[16] In general, municipalities annex area that is exempt from annexation plans, which are municipal council-approved documents that identify land that will be annexed within a certain period. Most annexations therefore occur under Subsection C-1 in § 43 of the TLGC, which describes the process for annexing territory that is not required to be part of an annexation plan.[17]

Nonannexation Plan Municipal Annexation

A municipality can involuntarily annex land upon which there are less than 100 tracts.[18] A home-rule municipality may present, if it chooses or is required under its charter, an election item to its voters to annex land.[19] There are certain procedural requirements the municipality must follow, but the requirements are very loose and if the municipality's charter is broad, the municipal government has great flexibility in how it goes about annexing property.[20] General-law municipalities, on the other hand, must always submit the annexation proposal to the voters.[21]

A municipality cannot just choose to annex as far as it can reach at any given time. The statutory rule is that a municipality cannot annex area that totals more than 10% of the area of its own

[13] *Id*. § 42.021(a).

[14] *Id*. § 42.022(c).

[15] *See id*. § 43.

[16] *Id*. § 43.051.

[17] *Id*. § 43 C-1.

[18] *Id*. § 43.052(h)(1).

[19] *Id*. § 43.022(a).

[20] *Id.*

[21] *Id*. § 43.023(c).

incorporated area as of January 1 of that year.[22] A municipality must also conform to certain requirements as to the actual size of the territory it wishes to annex. It may not annex any land that is less than 1,000 feet wide at its narrowest point, subject to exceptions for land that is contiguous on two sides by the municipality or the land petitions for annexation.[23] Before a municipality can begin the annexation process proper, it must hold hearings for the public to have the opportunity to speak regarding the annexation.[24] There are requirements as to where the hearings are held and the manner they are held in.[25]

Landowners may also petition a municipality for annexation.[26] They still must be within the ETJ of municipality and contiguous.[27] A landowner may choose to petition to be annexed to enjoy the voting rights of a municipality resident, or to receive services to the landowner's property.

Prevention of Annexation

Hearings are required to be held before a municipality may annex an area, and that presents an opportunity for the affected landowners and residents to make their voices heard.[28] If it becomes politically untenable due to public outcry, an annexation may be prevented. With enough political pressure, a landowner may carve himself out of an annexation and stay isolated on his property.

Post-Annexation

Following the annexation, municipalities are obligated to provide services, or have services provided, to the newly annexed areas. Prior to annexation, a municipality is required to have prepared a service plan that shows the municipality is prepared to provide necessary services to its new residents.[29] Small municipalities may strike deals with land developers or counties to have services provided to their new residents.

Municipalities are also prohibited by statute from preventing landowners from continuing to use their land in a way that was legal at the time of annexation.[30] The municipality may prevent such use, however, if it is a regulation of a few select matters, such as a public nuisance, would prevent imminent destruction of property, firework sales, or a sexually-oriented business.[31]

Disannexation

The TLGC provides multiple opportunities for areas that have been annexed to remove themselves from the municipality through disannexation.[32] A successful disannexation prevents the area from being

[22] *Id*. § 43.055(a).
[23] *Id*. § 43.054.
[24] *Id*. § 43.063.
[25] *Id.*
[26] *Id*. § 43.052(h)(2).
[27] *Id*. § 43.052.
[28] *Id*. § 43.063.
[29] *Id*. § 43.056(a).
[30] *Id*. § 43.002(a).
[31] *Id*. § 43.002(c).
[32] *Id*. § 43.141.

annexed again by the municipality for ten years.[33] Voters in the annexed area may petition a municipal body for disannexation if they have not been provided services in accordance with the statutes.[34] General-law municipalities must hold an election and vote upon the disannexation proposed for reasons other than failure to have services provided.[35]

Select Issue: Tricks of the Trade in Annexation

As with all complex statutes, various statutory provisions, regulations, and rules create gray areas and unintended options the legislature may not have intended, but of which savvy municipalities have taken advantage.

There exists an interesting "back door" to annexing land when a general-law municipality is unable to get around an area that is not volunteering to be annexed. The default rule is a municipality may only annex land that is contiguous with the city boundaries and within its ETJ.[36] But, a municipality may annex land that it owns, regardless of its location under § 43.051 of the TLGC.[37] This creates an interesting possibility. If a municipality wants to annex a strip of property, but because of an uncooperative landowner cannot annex it directly into its city boundary, the municipality can acquire ownership of a piece of land on the other side of the uncooperative landowner that is contiguous and adjacent to the desired piece of land. Once the municipality owns that piece of land, it uses the power in § 43.051 to annex that owned piece of land. Assuming the municipality is still within its ETJ, it now meets the default requirements to annex land.[38] The annexed chunk of land is part of the municipal boundaries, and it is within the ETJ. That newly-created contiguity allows the municipality to annex the desired piece of land without having to deal with the uncooperative landowner that initially blocked the municipality. The various rules of annexation have been added piecemeal over the years, and an attorney looking to find creative solutions should look for those overlaps of different provisions of the code.

Select Issue: Nonannexation Development Agreement for Ag-Exempt Landowners

Section 43.035 of the TLGC seems relatively innocuous, but is the seed from which endless frustration has risen.[39] The statute requires municipalities to offer a development agreement to landowners who use their land as, and has been appraised as, an agricultural, wildlife management, or timber land (an ag-exempt property).[40] A development agreement is an agreement between the municipality and landowner that specifies how a given piece of land may or may not be developed during a specified time.[41] The development agreement must allow the landowner to maintain its extraterritorial status, but would be subject to regulations not interfering with the ag-exempt use.[42] The

[33] *Id*. § 43.141(c).

[34] *Id*. § 43.141(a).

[35] *Id*. § 43.143.

[36] *Id*. § 43.051.

[37] *Id.*

[38] *See generally id.*

[39] *Id*. § 43.035.

[40] *Id.*

[41] *Id*. § 212.172.

[42] *Id*. § 43.035.

statute also allows area contiguous with land subject to the development agreement to be considered contiguous to the municipality for the purposes of future annexation.[43]

However, this does not mean that landowners can stonewall municipalities from annexing them by forcing these development agreements. The statute only requires that the development agreement be offered; if the landowner declines, the landowner is then subject to annexation.[44] Moreover, there is nothing in the statute that states what *cannot* be put in the agreement.[45] This presents the opportunity for what are known as "poison pill" provisions, similar to poison pills found in the legislative process. By adding in a provision so onerous to a landowner, a municipality can effectively guarantee the denial of the development agreement. There further has not been any determination that the development agreement must be drafted and offered in good faith. A conceivable limitation to a municipality's choosing to use poison pill provisions is the risk of raising the ire of interested and influential agricultural interests that may move the legislature to give the statute more bite, but that point has not been reached yet.

Conclusion

Ultimately, it remains to be seen what annexation and ETJ law will do over the coming decades, but as Texas continues to grow in population, annexations will continue to be a growing area of opportunity for attorneys to capitalize on. With a firm foundation to build off of, understanding and working in ETJs can be another tool in an attorney's toolkit. For further learning, the Texas Municipal League is an invaluable source of knowledge and should be consulted at https://www.tml.org/.

[43] *Id*. § 43.035(c).

[44] *Id*. § 43.035(b)(2).

[45] *See generally id.*

NOT GETTING MARRIED TODAY: AN OVERVIEW OF COMMON LAW MARRIAGE

Lisa Hoge
Texas Tech University School of Law
Lubbock, Texas
lnhoge@gmail.com

REPTL
REAL ESTATE, PROBATE & TRUST LAW
SECTION OF THE STATE BAR OF TEXAS

STUDENT WRITING CONTEST

Honorable Mention – Probate 2016

I. Introduction

Society tends to judge couples that choose to remain unmarried, even if they have sensible reasons for not formalizing their relationship.[1] However, their desire to avoid a formal marriage does not prevent them from becoming—intentionally or not—common-law married in certain states.[2] An estate planning or family law attorney should be aware of the laws regarding common-law marriage and the potential ramifications for a client.

The story of rapper Iggy Azalea illustrates how a person can be unaware of a common-law marriage and need legal advice.[3] Her former boyfriend, Maurice Williams, filed for divorce claiming that the couple was common-law married under Texas law.[4] He claims they lived together for a time and held themselves out as a married couple.[5] She denies these claims and says that Mr. Williams is seeking to turn a six-month relationship into an easy payday.[6]

This article hopes to help attorneys plan a defense for a client like Ms. Azalea by providing an overview of the history of common-law marriage and discussing the current state of the law within the United States.[7] It will also discuss the benefits of marriage, with a particular focus on the financial

---

[1] *See* Bella DePaulo, *Top 8 Reasons Not to Marry*, PSYCHOL. TODAY (Nov. 19, 2013).

[2] *See infra* Part III.A.

[3] *See Iggy Azalea Has Never Been Married but Ex Boyfriend Wants a "Divorce"*, SAN DIEGO DIVORCE ATT'Y BLOG (Nov. 3, 2014).

[4] *Id.*

[5] *Id.*

[6] *Id.*

[7] *See infra* Parts II-IIIA.

aspects.[8] Finally, this article will conclude with a discussion of the Social Security Administration's requirements for proving a common-law marriage, emphasizing how they place a burden on both applicants and employees.[9]

II. Historical Overview

While the concept of common-law marriage likely dates back much further, informal marriages have existed since at least the sixteenth century.[10] The *Decretum de Reformatione Martrimonni* supports this claim.[11] The Council of Trent passed this decree on November 11, 1563.[12] It dealt a serious blow to informal marriages in Italy by declaring that a priest and at least two other witnesses were required to be present at a valid marriage ceremony.[13]

The law in England during that same time period was much more liberal about common-law marriages.[14] It allowed a marriage to be formed merely through word of assent.[15] This was known as entering into a marriage contact "per verba de praesenti."[16]

Scotland was even more lax on marriage formalities.[17] Many young English couples eloped across the border to escape disapproving parents.[18] In fact, parental consent was not required for those below twenty-one, and girls as young as twelve could legally marry.[19] The minimum age for boys was fourteen until it jumped to sixteen in 1929.[20]

The United States began enacting marriage laws on a state-by-state basis as early as 1639.[21] In Massachusetts, men were required to present a marriage certificate to the proper authorities for recording.[22] The law was later taken a step further with a requirement that all marriages take place before a magistrate or other authorized person.[23] This essentially abolished the possibility of being common-law married in Massachusetts.[24]

New York took a more liberal approach than Massachusetts. In 1809, a New York court upheld a

---

[8] *See infra* Part IV.

[9] *See infra* Parts V.

[10] Jennifer Thomas, *Common Law Marriage*, 22 J. AM. ACAD. MATRIM. LAW 151, 154 (2009).

[11] *Id.*

[12] *Id.*

[13] *Id.*

[14] *Id.*

[15] *Id.*

[16] *Id.*

[17] *Scottish Way of Birth and Death*, U. OF GLASGOW (last visited Oct. 19, 2015).

[18] *Id.*

[19] *Id.*

[20] *Id.*

[21] Commonwealth v. Munson, 127 Mass. 459, 461 (1879).

[22] *Id.*

[23] *Id.*

[24] *See id.*

marriage based on words of assent.[25] This is likely because New York based their laws on the English common law, which had long recognized common-law marriage.[26] It was not the only state to base its approval of common-law marriage on the English common law, as Texas would later use similar reasoning.[27]

Texas actually adopted the English common law after England abolished common-law marriage.[28] However, case law later clarified that Texas had adopted an older United States version of English common law that still recognized common-law marriage.[29] This allowed Texas to justify upholding the tradition of common law marriage.[30]

The United States Supreme Court upheld the continuation of common-law marriage in 1877.[31] They declared that marriage is a common right.[32] The only way a state can abolish common-law marriage is by specifically indicating so through legislation.[33] A later section will discuss the statutes of those states that still allow common-law marriage.[34]

Between 1875 and 1917, many states abolished common-law marriage for a variety of social reasons.[35] Ten more states would follow between 1921 and 1959.[36] Some of these reasons included fear of interracial marriages, concern with fraudulent claims, and a perceived threat to the institution of marriage.[37]

Only four states have abolished common-law marriage since 1959.[38] This seems to indicate that those social concerns became less importance as society changed. Common-law marriage has actually survived two semi-recent attempts to abolish it in Texas.[39] This brings us to a discussion of the current state of common-law marriage in modern-day America.[40]

III. Current State of the Law

A. The Law

---

[25] Fenton v. Reed, 4 Johns. 52 (N.Y. Ch. 1809).

[26] Cynthia Grant Bowman, *A Feminist Proposal to Bring Back Common Law Marriage*, 75 OR. L. REV. 709, 720 (1996).

[27] MICHAEL ARIENS, LONE STAR LAW 157 (2011).

[28] *Id.*

[29] *Id.*

[30] *Id.*

[31] Meister v. Moore, 96 U.S. 76 (1877).

[32] *Id.* at 81.

[33] *In re* McLaughlin's Estate, 30 P. 651, 654 (Wash. 1892).

[34] *See infra* Part III.A.

[35] *See* Bowman, *supra* note 26, at 731-32.

[36] *Id.* at 740.

[37] *Id.*

[38] *Id.*

[39] *See* ARIENS, *supra* note 27, at 157-58.

[40] *See infra* Part III.A.

There are currently thirteen states with statues regarding common-law marriage.[41] Five of those states will only recognize a common-law marriage if it was entered into prior to a certain date. [42] That date will vary between the states.[43] Because of that severe restriction, those five states (Pennsylvania, Ohio, Indiana, Georgia, and Florida) are considered to have abolished common-law marriage for all practical purposes.[44]

Colorado has taken the opposite approach.[45] Rather than only recognizing common-law marriages entered into before a certain date, Colorado only recognizes common-law marriages entered into after September 1, 2006.[46] Both parties must be at least eighteen at the time of marriage, and no other law may prohibit the marriage.[47] Those requirements apply even if the common-law marriage was entered into outside of Colorado.[48]

Other states besides Colorado have statutes actively allowing common-law marriage.[49] New Hampshire and Texas are good examples of how a typical common-law marriage statute is written.[50] The New Hampshire statute states that "[p]ersons cohabiting and acknowledging each other as husband and wife, and generally reputed to be such, for the period of 3 years, and until the decease of one of them, shall thereafter be deemed to have been legally married."[51]

The Texas statute requires either a signed declaration of marriage or mutual agreement, co-habitation, and representing oneself as married.[52] The Texas Supreme Court upheld these requirements in 2013.[53]

Utah has a statute nearly identical to the Texas one.[54] The most significant difference is that Utah does not allow a common-law marriage to be formed by signing a declaration of marriage.[55] The other notable difference is that Utah allows a common-law marriage to be established up to one year after the termination of the relationship.[56] Iowa, Kansas, Montana, and South Carolina are the only other states that still actively allow common-law marriage, at least under certain circumstances.[57]

---

[41] *Common Law Marriage By State*, NATI'L CONF. OF ST. LEGIS (Aug. 4, 2014).

[42] *Id.*

[43] *Id.*

[44] *Id.*

[45] COLO. REV. STAT. ANN. § 14-2-109.5 (West 2015).

[46] *Id.*

[47] *Id.*

[48] *Id.*

[49] *Id.*

[50] N.H. REV. STAT. ANN. § 457:39 (2015); TEX. FAM. CODE ANN. § 2.401 (West 2015).

[51] N.H. REV. STAT. ANN. § 457:39 (2015).

[52] TEX. FAM. CODE ANN. § 2.401(a)(1)-(2).

[53] Grigsby v. Reib, 105 Tex. 597 (1913); *See* ARIENS, *supra* note 27.

[54] UTAH CODE ANN. § 30-1-4.5 (West 2015).

[55] *Id.*

[56] *Id.*

[57] *Common Law Marriage By State*, *supra* note 41.

Statutes are not the only way for a state to recognize common-law marriage.[58] Some states have common-law marriage as part of their case law.[59] Rhode Island and Alabama are prime examples of this approach.[60]

The leading case on common-law marriage in Rhode Island is *Demelo v. Zompa*.[61] This case holds that a couple must have "seriously intended to enter into the husband-wife relationship."[62] Additionally, their conduct must have been "of such a character as to lead to a belief in the community that they were married."[63] These two requirements can be proven by "inference from cohabitation, declarations, reputation among kindred and friends, and other competent circumstantial evidence."[64]

Alabama law can also be easily summarized.[65] Alabama requires proof of "(1) capacity; (2) present, mutual agreement to permanently enter the marriage relationship to the exclusion of all other relationships; and (3) public recognition of the relationship as a marriage and public assumption of marital duties and cohabitation" to show a common-law marriage.[66]

Oklahoma actually has contradictory law regarding common law marriage.[67] It has a statute requiring a formal marriage license, which would seem to bar common-law marriage.[68] However, common-law marriage has been upheld in the Oklahoma courts on more than one occasion.[69] It remains to be seen if and how the state intends to clarify this discrepancy. [70] In the meantime, an Oklahoma lawyer might face confusion arguing a common-law marriage case, which provides an excellent segue into our next topic.[71]

B. How to Argue for Your Client

The best place to start when faced with a common-law law marriage issue is to gather clear and convincing evidence that the couple were or were not common-law married.[72] Courts have been known to recognize many different things as evidence of a common-law marriage.[73] This might include financial documents, use of a common last name, insurance policies, and testimony from third parties.[74]

---

[58] *Id.*

[59] *Id.*

[60] *Id.*

[61] Demelo v. Zompa, 844 A.2d 174 (R.I. 2004).

[62] *Id.*

[63] *Id.*

[64] *Id.*

[65] Gray v. Bush, 835 So. 2d 192 (Ala. Civ. App. 2001).

[66] *Id.* at 194.

[67] *Common Law Marriage By State*, *supra* note 41.

[68] OKLA. STAT. ANN. TIT. 43, § 43-4 (West 2015).

[69] *Common Law Marriage By State*, *supra* note 41.

[70] *See id.*

[71] *See infra* Part III.B.

[72] David Tracy, *Common Law Marriage in Oklahoma*, DIVORCENET (last visited Oct. 22, 2015).

[73] *Id.*

[74] *Id.*

There are three common ways to repute a common-law marriage.[75] The first is to offer evidence that an element of the common-law marriage statute for the state where the marriage was formed was not met.[76] Alternatively, an attorney could produce proof that one or both of the parties was not legally competent at the time of the marriage.[77] Some possible reasons for incompetence include being insane or underage.[78] Finally, the third possible defense is to allege that one or both parties were already married at the time of the marriage.[79]

Courts have a preference towards marriage and view cohabitation and reputation within the community as particularly persuasive evidence.[80] Because of this preference towards marriage, common-law marriages continue to be recognized even if the couple moves to a state where common-law marriage is abolished.[81] This means that attorneys in all states need to consider whether their client may be common-law married.[82] The attorney also needs to make sure that a client who is common-law married understands the need for formal divorce should the couple ever split.[83] Finally, all attorneys should be aware of what marital benefits their client may be entitled to, which is our next topic of discussion.[84]

IV. Marital Benefits

Common-law spouses enjoy the same financial benefits as a traditionally-married couple.[85] These include employment benefits, tax exemptions, ability to both claim tax deductions for mortgage interest and children, and eligibility for Social Security benefits.[86]

Employment benefits are an important advantage of being married as many people receive health insurance through their spouse's employer.[87] Employers who offer spousal benefits generally extend this benefit to common-law spouses.[88] Additionally, any children from the relationship can be added to the insurance plan as dependents.[89]

Some insurance companies or employers may require a signed affidavit before adding a common-

---

[75] Adam Kielich, *Do I Need a Divorce for my Common Law Marriage in Texas?*, THE KIELICH L. FIRM (Jan. 14, 2015).

[76] *Id.*

[77] *Id.*

[78] *Id.*

[79] *Id.*

[80] *In re* Benjamin, 34 N.Y.2d 27 (1974).

[81] *Common Law Marriage*, NAT'L PARALEGAL C. (last visited Oct. 26, 2015).

[82] *See id.*

[83] *Id.*

[84] *See infra* Part IV.

[85] Katie Adams, *Marriage vs. Common Law: What It Means Financially*, INVESTOPEDIA (Feb. 15, 2010).

[86] *Id.*

[87] *See Health Care Benefits: Common Law Marriage: How Does Common Law Marriage Affect Health Insurance?*, SOCIETY FOR HUM. RESOURCE MGMT. (Mar. 25, 2015).

[88] *Id.*

[89] *Id.*

law spouse to an insurance plan.[90] Others may require evidence of the marriage.[91] Once again, this evidence may include things like a joint tax return, a joint mortgage, or any other paperwork where the couple holds themselves out as a marital unit.[92]

Common-law married couples are also entitled to certain tax benefits.[93] Arguably, the most important of these is the marital exemption from the gift tax.[94] This states that an individual may transfer property to the individual's spouse as a gift and then deduct that amount from the individual's total taxable gifts.[95] The biggest caveat is that the receiving spouse must be a citizen of the United States to claim this deduction.[96]

One of the other major tax benefits of marriage is the increased estate tax exemption.[97] If a person dies with an estate valued over a certain amount, the person's heirs are required to pay taxes at a high rate on the excess amount.[98] However, married couples are allowed a much larger estate before the estate tax kicks in.[99] In 2015, an estate tax was owed on any estate of more than $5.43 million (if single) or $10.86 million (if married).[100] The applicable tax rate was 40%.[101] As you can see, marriage greatly benefited any couple with an estate in the $5-10 million range.[102]

The last major tax benefit of marriage involves deductions for children and for mortgage interest.[103] A hypothetical is helpful to explain the child deduction. An unmarried couple lives together and has two children.[104] One wishes to claim the standard child deduction on his/her taxes, while the other wishes to use the child to claim the Earned Income Tax Credit (EITC) on his/her taxes.[105] Who gets to claim the children?

The answer is that only one parent gets to claim a specific child.[106] So, either one parent claims both children, or each parent claims one child in this scenario.[107] If both parents attempt to claim the

---

[90] *Id.*

[91] *Id.*

[92] *Id.*

[93] *Publication 17 (2014)*, INTERNAL REVENUE SERVICE (last visited Oct. 26, 2015).

[94] I.R.C. § 2523 (West 2015).

[95] *Id.*

[96] *Id.*

[97] *Gift Tax and Estate Tax*, EFILE.COM (last visited Oct. 26, 2015).

[98] *Id.*

[99] *Id.*

[100] *Id.*

[101] *Id.*

[102] *See id.*

[103] *See supra* Part IV.

[104] *Qualifying Child of More Than One Person, AGI and Tiebreaker Rules*, EARNED INCOME TAX CREDIT (last visited Oct. 27, 2015).

[105] *Id.*

[106] *Id.*

[107] *Id.*

same child, there is a tiebreaker rule that the IRS can apply.[108] Assuming that the child lived with each parent equally throughout the year, the parent with the higher adjusted gross income (AGI) is allowed to claim the child.[109] Needless to say, marriage would solve this messy situation by allowing the couple to file together and jointly benefit from all possible deductions and credits from both children.[110]

We finally come to the mortgage interest deduction.[111] Mortgage interest can be deducted from the homeowner's taxes under certain conditions.[112] As you will see below, there are distinct advantages to being married when it comes to mortgage interest deduction.[113]

Interest on a mortgage taken out to buy, build, or improve your home after October 13, 1987, may be fully deducted only if the total debt from all mortgages, including any grandfathered debt, amounts to $1 million or less for married couples and $500,000 or less for singles or married couples filing separately.[114]

Mortgages taken out after October 13, 1987, for reasons other than to buy, build, or improve your home must total $100,000 or less for married couples and $50,000 or less for singles or married couples filing separately. They must also total less than the fair market value of your house minus the value of all grandfathered debt and all post-October 13, 1987 mortgage debt.[115]

Now, it is time to discuss one of the most well-known marital benefits—Social Security.[116] "A married person can collect retirement benefits based on his or her own earning from work, or an amount equal to 50 percent of the other spouse's retired worker benefit—whichever is the higher amount."[117] Two examples are helpful to illustrate that concept.[118]

"Mrs. Williams will get a retirement benefit of $1,200 a month based on her work record. Mr. Williams is entitled to a retirement benefit of $500 a month based on his own work history. He will receive his own $500, plus an additional $100, to bring his total to $600 a month, based on 50 percent of Mrs. Williams' benefit. Total family benefits for the Williams household will be $1,800 a month."[119]

"Mrs. Rodriguez is entitled to a retirement benefit of $1,100 a month based on her work history. Her husband will get a benefit of $1,400, which would provide a spousal benefit of $700. Mrs. Rodriguez receives her own benefit of $1,100 a month, because that is the larger of the two amounts. Total family retirement benefits: $2,500 a month."[120]

---

[108] *Id.*

[109] *Id.*

[110] *Eight Facts about Filing Status*, IRS (Jan. 13, 2011).

[111] *See supra* Part IV.

[112] James E. McWhinney, *Tax Deductions on Mortgage Interest*, INVESTOPEDIA (Feb. 08, 2006).

[113] *Id.*

[114] *Id.*

[115] *Id.*

[116] *See supra* Part IV.

[117] Social Security, Marriage, and Divorce, NAT'L ACAD. OF SOC. INS. (last visited Oct. 27, 2015).

[118] *Id.*

[119] *Id.*

[120] *Id.*

As you can see, Social Security greatly favors married couples.[121] However, the Social Security Administration wants to be sure that couples are truly legally married, and has enacted regulations to help determine that.[122] This brings us to a discussion of the Social Security Administration's burdensome requirements to prove a common-law marriage.[123]

V. Social Security Requirements

The Social Security Administration (SSA) makes it easy to prove a traditional ceremonial marriage.[124] A ceremonial marriage may be proven by a "certified copy of the public record of the marriage; . . . [a] certified copy of the religious record of the marriage; or . . . [t]he original marriage certificate."[125] Nearly all couples will be able to produce one of those documents.

If the couple is unable to produce one of those documents, a signed statement from the officiant who performed the wedding or "[o]ther evidence of investigative value" may suffice.[126] That type of evidence may include things like photographs, newspaper announcements, or witness statements.[127]

In contrast, a common-law marriage is difficult to prove.[128] Let us begin by looking at just part of the actual regulations.[129]

"Evidence to prove a common-law marriage in the States that recognize such marriages must include: . . . [i]f the husband and wife are living, a statement from each and a statement from a blood relative of each; . . . [i]f either the husband or wife is dead, a statement from the surviving widow or widower and statements from two blood relatives of the decedent; or . . . [i]f both a husband and wife are dead, a statement from a blood relative of the husband and from a blood relative of the wife."[130]

This is obviously a complicated process, but it gets even more involved when you read the specifics in more detail.[131] The regulations go on to state that each spouse must submit a Statement of Marital Relationship and that, if the husband and wife are still living, a blood relative from each side must submit a Statement Regarding Marriage.[132]

The Statement of Marital Relationship form is a four-page document.[133] While most of the form is yes or no questions, the majority of yes responses require further explanation.[134] This form is required

---

[121] *See id.*

[122] *See infra* Part V.

[123] *See infra* Part V.

[124] *Evidence of Ceremonial Marriage*, SOC. SEC. HANDBOOK (last visited Oct. 27, 2015).

[125] *Id.*

[126] *Id.*

[127] *Id.*

[128] *See id*.

[129] *Id.*

[130] *Id.*

[131] *Development of Common-Law (Non-Ceremonial) Marriages*, SOC. SEC. PROGRAM OPERATIONS MANUAL SYS. (Oct. 13, 2013).

[132] *Id.*

[133] *Statement of Marital Relationship*, SOC. SEC. ADMIN. (Jul. 2015).

[134] *Id.*

of both spouses, despite the fact that their answers will be (nearly) identical.[135]

Meanwhile, there is also the Statement Regarding Marriage.[136] This is required of one blood relative on each side.[137] What makes this form potentially complicated is the whole blood relative issue. There are dozens of reasons why a person might not have blood relatives, and the SSA specifically states that a relationship by marriage or adoption is insufficient.[138] There is no explanation of why a blood relative's testimony is perceived as more reliable than testimony from a nonblood relative or friend.[139]

The SSA did anticipate that a couple might have issues accessing blood relatives and does have an alternative process.[140] If a couple does not have enough blood relatives to fulfill the requirements, they may have another person who knows them well fill out the paperwork.[141] However, they must submit additional paperwork explaining why they were unable to use a blood relative.[142]

The process is further complicated when a couple is unable to obtain a Statement Regarding Marriage from anyone at all.[143] The SSA does provide its employees with instructions on how to handle this situation when both spouses are still living, although it notes that very few circumstances will justify using alternative procedures, and the couple will have to provide documentation about their unique circumstances.[144]

To wrap up this section, the following instructions show exactly what is expected of an employee faced with the task of proving a common-law marriage.[145]

"Develop each form independently of the others. Answer all items on each form fully but concisely and in the person's own words. Clarify all ambiguous answers and reconcile all conflicts. Explain any ambiguous answers on a report of contact form or Report of Contact (RPOC) screen. Get a supplemental statement over the person's signature, as needed. Obtain corroborating evidence (e.g., mortgage or rent receipts, insurance policies, medical records, bank records) to substantiate the fact that the couple considered and held themselves out as husband and wife."[146]

This list does not even include how to handle complex issues such as common-law marriages established outside of the United States.[147] The SSA has provided its employees with separate instructions on how to handle those complex situations, but they are beyond the scope of this article.[148] However, they do help illustrate the challenges that SSA employees face when handling a common-law

[135] *Development of Common Law (Non Ceremonial) Marriages*, *supra* note 131.

[136] *Id.*

[137] *Id.*

[138] *Id.*

[139] *Id.*

[140] I*d.*

[141] *Id.*

[142] *Id.*

[143] *Id.*

[144] *Id.*

[145] *Id.*

[146] *Id.*

[147] *Id.*

[148] *Id.*

marriage case.[149]

VI. Conclusion

Common-law marriage is a complex issue that can vary greatly from state to state.[150] It is important for couples to understand the benefits they may be entitled to as a common-law married couple.[151] However, some of the benefits may be challenging to receive, and Social Security is by far most difficult.[152]

It is time for the SSA to reevaluate its guidelines. It should begin by allowing nonblood relatives to provide evidence of a common-law marriage.[153] If it is unwilling to take that step, the SSA should at least adequately and publicly explain its rationale behind this policy.

The SSA should also reconsider why both parties are required to fill out the Statement of Marital Relationship form.[154] There seems no benefit to this, as couples will likely fill out their forms together. This greatly reduces the chances that conflicting answers will expose some lie, which is likely the SSA's rationale behind this policy.

In conclusion, a common-law marriage may be right for many couples. However, these couples need to fully understand several things: what it takes to form a common-law marriage, what it takes to end a common-law marriage, and the potential difficulties behind proving such a marriage.[155] It is the job of a good attorney to properly educate these couples and make sure they are prepared for the future in every way possible.

[149] *See supra* Part V.

[150] *See supra* Part III.A.

[151] *See supra* Part IV.

[152] *See supra* Part V.

[153] *See supra* Part V.

[154] *See supra* Part V.

[155] *See supra* Parts III-IV.

POTPOURRI

Gerry W. Beyer
Texas Tech University School of Law
Lubbock, Texas
gwb@professorbeyer.com

So, Tell Me How You Really Feel!

After Texan Leslie Ray Charping died on January 30, 2017, his family published an obituary expressing their real feelings. Here are a few excerpts. "He leaves behind 2 relieved children; a son . . . and daughter, Shiela Smith . . . along with six grandchildren and countless other victims including an ex wife, relatives, friends, neighbors, doctors, nurses and random strangers. At a young age, Leslie quickly became a model example of bad parenting combined with mental illness and a complete commitment to drinking, drugs, womanizing and being generally offensive. . . . Leslie's hobbies included being abusive to his family, expediting trips to heaven for the beloved family pets and fishing . . . . Leslie's life served no other obvious purpose, he did not contribute to society or serve his community and he possessed no redeeming qualities besides quick whited [sic] sarcasm which was amusing during his sober days. . . . Leslie's passing proves that evil does in fact die and hopefully marks a time of healing and safety for all."

See Obituaries: Leslie Ray Charping, CARNESFUNERALHOME.COM (last visited Apr. 25, 2017).

Pod People

Not quite the same as the classic 1978 movie *Invasion of the Body Snatchers* starring Donald Sutherland and Spock (aka Leonard Nimoy), but nonetheless, creepy. As explained in the article cited below, "The Capsula Mundi concept, from designers Anna Citelli and Raoul Bretzel, uses an egg-shaped burial pod made from biodegradable starch plastic as the coffin, in which the body is placed in a fetal position and buried under the ground. A tree (or tree seed) is then planted over the top of the pod, which will use the nutrients from the decomposing body as fertilizer for its growth." Just think, if you plant a fruit tree and then eat the fruit, you could actually say, "It's people" in the style of Frank Thorn (Charlton Heston) in *Soylent Green*.

See Derek Markham, *Egg-shaped Burial Pods Feed the Trees and Turn Cemeteries Into Forests*, TREEHUGGER.COM (Sept. 19, 2014).

Coffee King's "Urn"

When Renato Bialetti, the purveyor of aluminum stovetop espresso makers, died last year, he was cremated and his ashes placed in a giant Moka pot at his funeral in Montebuglio, Italy. I just hope his family does not inadvertently start using the pot to brew coffee some morning when the sleep fog has not yet risen.

See *Ashes of Italian 'Coffee King' Put in Giant Espresso Pot*, FOXNEWS.COM (Feb. 20, 2016).

INTESTACY, WILLS, ESTATE ADMINISTRATION, AND TRUSTS UPDATE

Gerry W. Beyer
Texas Tech University School of Law
Lubbock, Texas
gwb@professorbeyer.com

Will Contests – Lack of Formalities

In re Estate of Romo, 503 S.W.3d 672 (Tex. App.—El Paso 2016, no pet. h.).

Contestants claimed that a will previously admitted to probate was invalid because the testator lacked testamentary capacity or executed the will when subjected to undue influence. After testimony at the trial that the witnesses did not attest in the testator's presence as required by Estates Code § 251.051(3), the court granted contestant's motion for a directed verdict that the will was invalid.

The appellate court affirmed. The court explained that only a will which meets all Texas requirements may be admitted to probate. It was irrelevant that the trial was centered around two other grounds for finding the will to be invalid.

Moral: A court may set aside a will for failure to comply with the requirements of a valid will even if the contestant does not raise that ground in the pleadings.

Will Contests – Lack of Capacity

Tex. Capital Bank v. Asche, No. 05-15-00102-CV, 2017 WL 655923 (Tex. App.—Dallas Feb. 17, 2017, no pet. h.) (mem. op.).

The trial court determined that the testator lacked capacity to execute multiple estate planning documents over a period of time spanning over a decade. In addition, the trial court found that the testator was subjected to undue influence.

The appellate court made an exhaustive review of the evidence, which included both medical and lay testimony. Although there was "unquestionably conflicting evidence" about testator's capacity, the court explained that it may not substitute its judgment for that of the jury. The court then concluded that the evidence was legally and factually sufficient to support the jury's finding that the testator lacked capacity. Accordingly, the court did not need to address the undue influence issue.

Moral: Once a jury determines a testator's capacity to execute a will, it will be difficult to have that finding overturned on appeal unless the jury's finding is against the great weight of the evidence.

Estate Administration – Late Probate

Byerley v. McCulley, No. 12-16-00124-CV, 2017 WL 605089 (Tex. App.—Tyler Feb. 15, 2017, no pet. h.).

The probate court admitted Testatrix's will to probate nineteen years after her death. The court determined that Applicant was not in default for probating the will within four years of the date of Testatrix's death and that service was made by posting. Heir sought a bill of review asserting that he did not receive sufficient notice.

The appellate court agreed and granted the bill of review. Applicant claimed that under the law at

the time of Testatrix's death, service for a late probate by posting was sufficient. PROB. CODE § 128(a). Heir asserts that the law applicable when Applicant filed the will for probate governs which requires service on heirs whose addresses can be ascertained with reasonable diligence. EST. CODE § 258.001.

The court recognized that when the law was changed to require service in 1999, the legislation contained a savings clause providing that the change to require service on the heirs upon a late probate applied only if the person died on or after September 1, 1999. PROB. CODE § 128B. However, when Probate Code § 128B was repealed and replaced by Estates Code § 258.001, there was no express savings clause. Because there was no savings clause and the text of § 258.001 does not limit the applicability of the notice requirements, notice to the heirs was required. Accordingly, admitting the will to probate after only notice by posting was a substantial error justifying the issuance of a bill of review.

Moral: Applicants for a late probate need to provide notice to the heirs regardless of when the testator died.

Trusts – Parties

Tex. Capital Bank v. Asche, No. 05-15-00102-CV, 2017 WL 655923 (Tex. App.—Dallas Feb. 17, 2017, no pet. h.) (mem. op.).

The trial court determined that a settlor lacked capacity to create a trust. However, the contestant failed to join the trustee of the trust as a party. Accordingly, the appellate court reversed because "[i]t is well established that suits against a trust must be brought against its legal representative, the trustee." The fact that the same entity was a party to the lawsuit as the settlor's executor was insufficient as "[e]xecutor and trustee are separate and distinct capacities."

Moral: A trust is not a legal entity that can sue or be sued. In any action involving a trust, the trustee in his/her/its representative capacity must be made a party.

GUARDIANSHIP UPDATE

Chasity W. Cooper
Crain, Canton & James
Houston, Texas
ccooper@craincaton.com

Motion to Show Authority; Standing

Ross v. Sims, No. 03-16-00179-CV, 2017 WL 672458 (Tex. App.—Austin Feb. 15, 2017, no pet. h.) (mem. op.).

In *Ross*, three children were fighting over the guardianship of their ninety-one-year-old mother, Mrs. Sims. The trial record shows that Mrs. Sims was suffering from mild to moderate dementia before she had a stroke and subsequently executed a power of attorney appointing her daughter Suzanne as her agent. Suzanne then relocated Mrs. Sims from her home, filed an eviction proceeding against her brother, Harold, who was residing in Mrs. Sims's home, hired Ross to represent herself and Mrs. Sims, and created a trust transferring Mrs. Sims's property to Ross as trustee.

Harold filed an application for appointment of guardian of Mrs. Sim's person and requested his sister, Cynthia, be appointed guardian of Mrs. Sims's estate. Cynthia joined in the application. Mrs. Sims, through her attorney Ross, filed an answer contesting the guardianship. The trial court appointed an attorney and guardian *ad litem* and authorized an independent medical examination. Harold and Cynthia filed a motion to show authority, challenging Ross's authority to represent Mrs. Sims.

A hearing was held on the motion to show authority, where the court psychiatrist testified that Mrs. Sims did not have decision-making capacity after her stroke. The court orally granted the motion to show authority, removed Ross from representing Mrs. Sims in the guardianship, and instructed him to turn over all documents to the attorney *ad litem*.

Harold and Cynthia then filed a motion to set trial on the nonjury docket. Ross filed a plea in intervention pursuant to Texas Rules of Civil Procedure 60, alleging he had standing and capacity to intervene as a person interested in the welfare of Mrs. Sims pursuant to Texas Estates Code §§ 1002.018 and 1055.001. He contested the need for the appointment of a guardian and argued Harold and Cynthia were disqualified. He also filed a response to the nonjury trial setting, arguing he had previously paid a jury fee and demanded a jury trial. Harold and Cynthia filed a motion to strike Ross's plea in intervention and jury demand.

Despite the court's ruling that Ross had no authority to represent Mrs. Sims, Ross proceeded to file pleadings in the eviction lawsuit and represent that he, as trustee, was the owner of Mrs. Sims's house. Thus, Harold and Cynthia filed an application for an emergency ex parte temporary restraining order and temporary injunction to enjoin the withdrawal of Mrs. Sims's funds or the transfer of her property. The trial court granted the TRO against Ross and Suzanne and precluded them from withdrawing money from Mrs. Sims's accounts or transferring her property. Ross filed an answer and demanded a jury trial.

At the hearing, the trial court granted Harold and Cynthia's motions to strike Ross's intervention and jury demand, finding that it was not timely and that his position was adverse to Mrs. Sims's, relying on Texas Estates Code §§ 1055.001 and 1055.003(c), which give the court discretion to grant or deny the intervention of an interested party if that intervention would unduly prejudice the adjudication of the original parties' rights. The court further instructed Ross that he was not a party and to "have a seat in

the gallery." Eventually the court signed orders declaring the power of attorney was invalid along with all subsequent transfers of Mrs. Sims's property and ordered all funds be transferred to the county court for Mrs. Sims's benefit.

A guardianship trial was eventually had and the court appointed Cynthia permanent guardian of Mrs. Sims's person and estate. Although Ross did not participate in the trial, he did file a motion for new trial and a supplement to same, which were both overruled by operation of law.

Ross appealed. Harold and Cynthia argued that the appeal should be dismissed because Ross lacked standing because he was not a party to the underlying suit. However, the appellate court found that when Ross filed a plea in intervention and was subsequently served with a TRO and temporarily enjoined by the trial court, he was a party to the guardianship proceeding and had standing to appeal.

On appeal, Ross attempted to argue that his due process rights were violated. The appellate court first looked at whether there was essentially a Takings Clause violation when the trial court voided the trust and ordered the funds be transferred to the court's registry. The appellate court found his arguments were without merit, as he cited no authority to support that he, as trustee, was entitled to just compensation when the funds were ordered from the trust to the court registry. Ross further argued that his due process was violated when he was denied a trial on the merits before the court voided the trust and ordered the funds returned to the court's registry. The appellate court again found this argument to be without merit.

The appellate court found that although the right to be heard is a fundamental concept to due process, a party's right to due process does not mean that a case may never be disposed of before a trial. *See* *Soefje v. Jones*, 270 S.W.3d 617, 625 (Tex. App.—San Antonio 2008, no pet.). In fact, the record reflected that Ross was afforded an opportunity to meaningfully participate at the hearing regarding his authority to represent Mrs. Sims and at the hearing regarding the motion to strike his plea in intervention and jury demand and the temporary injunction. And, the appellate court found that Ross cited no authority to support his position that he was entitled to a jury trial in a guardianship proceeding.

Further, the appellate court found that once his plea in intervention was struck, his request for a jury trial as an intervener was moot. Thus, based on the appellate court's review of the record, it concluded that Ross failed to show his due process rights were violated when the trial court voided the trust and ordered the funds be placed with the trial court for Mrs. Sim's benefit or that any such violation resulted in an improper judgment in the guardianship proceeding or prevented him from presenting his case on appeal. Therefore, the appellate court affirmed the trial court's orders.

Priority of Guardian; Disqualification

In the Matter of the Guardianship of Fairley, No. 04-16-0096-CV, 2017 WL 188103 (Tex. App.—San Antonio Jan. 18, 2017, pet. filed) (mem. op.).

In *Fairley*, ward's wife and daughter both filed applications to be appointed his permanent guardian. The trial court found that daughter lacked just cause to contest wife's application and ordered daughter to deposit security for probable costs in the proceeding with the clerk. Daughter failed to comply and the trial court dismissed her application.

A trial was had on wife's application, where daughter's counsel argued that her application was erroneously dismissed. During the trial, daughter's counsel agreed that wife had priority to serve as guardian absent disqualification and argued that the issue to a jury should be whether wife was

qualified. The court heard testimony regarding wife's prior management of ward's affairs under his medical and financial powers of attorney and determined it was in his best interest to appoint wife guardian.

On appeal, daughter argued that the dismissal of her application prevented her from participating in the trial on wife's application and from being considered her father's guardian. However, the appellate court found that the record reflected daughter's counsel appeared on her behalf at the trial, requested relief from the court, and had an opportunity to cross examine the wife. Although daughter sought to prove wife was disqualified, she offered no evidence of same at the trial.

The appellate court relied on Texas Estates Code § 1104.001 that states if an incapacitated person's spouse is eligible to be the guardian, then the spouse is "entitled to guardianship in preference to any other person." Because daughter failed to argue on appeal that that wife was ineligible or disqualified, the appellate court found that wife is entitled the be ward's guardian as a matter of law. The appellate court further found that the dismissal of daughter's application did not result in an improper judgment or prevent her from presenting in the case.

Accordingly, the appellate court held that any error in dismissing daughter's application or ordering her to provide security was harmless and affirmed the trial court's order.

Bill of Review; Motion for New Trial

In re Ludington, No.01-16-00411-CV, 2017 WL 219162 (Tex. App.—Houston [1st Dist.] Jan. 19, 2017, no pet.) (mem. op.).

In *Ludington*, decedent was under a guardianship prior to his death. The administrator of decedent's estate petitioned the court for a bill of review challenging an order it previously entered approving the guardian's final account and discharging him and the surety from liability. Administrator alleged that the guardian failed to account for all of the ward's assets, income, and certain loans that were made to decedent.

The trial court held an evidentiary hearing on administrator's petition at which time she announced she was ready to prove her case. She attempted to offer evidence, which was excluded upon objections. The parties then had a discussion regarding the background of the case and made opening statements discussing the issues that related to administrator's claims. The trial court indicated that before it could rule on her petition, it would need to review all of the prior guardianship orders. Administrator offered to provide those orders to the court, but did not ask the court to consider additional exhibits, witness testimony, object that she had not had sufficient time to make her case, move for a continuance, or ask that the record remain open.

Administrator subsequently filed a post-hearing brief whereby she attached the requested guardianship orders, along with accounts, inventories, and other filings related to the guardianship. Her brief acknowledged that the court had already heard and considered her petition and this brief was offered to address arguments raised at the hearing. She again did not argue that she had not been afforded the opportunity to present her case, offer additional exhibits or testimony, or request an additional hearing be held. The surety filed a response to the brief and characterized the previous hearing as a bench trial and argued administrator failed to call any witness or offer any admissible evidence and therefore, her petition should be denied.

The trial court subsequently denied administrator's petition for statutory bill of review. Administrator moved for a new trial on the grounds that she had not been afforded the opportunity to

present her case. The surety argued that administrator failed to obtain rulings on her exhibits, call witnesses, request a continuance, or argue that she had not been afforded adequate time to present her case, and there was no basis for the trial court to vacate its order. The trial court agreed and administrator's motion was denied.

On appeal, administrator agued the trial court did not permit her to present certain evidence that would have proved her right to a bill of review. The appellate court disagreed and found that the trial court record showed she was given the opportunity to present evidence at the hearing, through her supplemental brief, and could have filed a reply to the surety's response brief alleging that she failed to meet her burden of proof. The appellate court found that if administrator felt that she was prevented from presenting her evidence at the hearing, she should have objected and made an offer of proof at the hearing and filed a reply to the surety's reply brief providing evidence in support of her petition.

Administrator further argued that the trial court abused its discretion when it ruled before she announced that she had rested her case, relying on Texas Rules of Civil Procedure 262 and 265. The appellate court disagreed and found that those rules only prevent a trial court from ruling before the petitioner is allowed to present evidence, which administrator was allowed to do in this instance.

Finally, the appellate court found that administrator's motion for new trial failed to identify any specific evidence she intended to offer and why it would have been dispositive, and the record did not contain any indication that reopening the evidentiary hearing would have changed the outcome.

Accordingly, the appellate court overruled administrator's sole issue on appeal and affirmed the trial court's order.

ELDER LAW UPDATE

Lori A. Leu
Leu & Peirce, PLLC
Plano, Texas
lieu@leulawfirm.com

Medicaid Planning and the Unauthorized Practice of Law

One of the scams affecting elderly individuals and their families, which could also affect unwitting attorneys, is the unauthorized practice of law by nonattorneys who assist elderly clients in qualifying for Medicaid benefits to fund long-term care. Individuals who engage in such activities often call themselves "Medicaid planners" or "Medicaid specialists," thus, implying a special skill that the Texas legislature has declared constitutes the practice of law. Medicaid planning is more than simply providing general advice about Medicaid eligibility. It involves an in-depth analysis of medical and financial circumstances, and often includes complex asset restructuring.

Medicaid planning is legal when done by an attorney licensed in the State of Texas. However, Medicaid planning by a nonattorney is criminal. The Texas Human Resources Code defines the unauthorized practice of law in the context of Medicaid planning:

> (a) A person who is not licensed to practice law in Texas commits an offense if the person charges a fee for representing or aiding an applicant or recipient in procuring assistance from the state agency administering the assistance.
>
> (b) A person commits an offense if the person advertises, holds himself or herself out for, or solicits the procurement of assistance from the state agency administering the assistance.
>
> (c) An offense under this section is a Class A misdemeanor.

TEX. HUM. RES. CODE § 12.001. A Class A misdemeanor is punishable by a fine up to $4,000, one year in jail, or both for all parties involved in the scheme. TEX. PENAL CODE § 12.21.

As set forth in § 12.001, it is a crime for nonattorneys not only to represent or assist an applicant in obtaining Medicaid benefits for a fee, but to even advertise themselves and their services to the public. In some cases, nursing homes become involved and may subject themselves to criminal charges as well for their role in directing elderly individuals and their families to unauthorized planners.

Nonattorneys often attempt to appear legitimate by claiming to work with attorneys. In most cases, however, these attorneys never actually meet with the elderly clients or their families and are merely "lending" their name, and taking a fee, to establish legitimacy for the criminal. Attorneys who participate in such schemes are subjecting themselves to disciplinary consequences, in addition to the potential claim of criminal activity. The Texas Disciplinary Rules of Professional Conduct provide as follows: "A lawyer shall not . . . assist a person who is not a member of the bar in the performance of activity that constitutes the unauthorized practice of law." TEX. DISCIPLINARY RULES PROF'L CONDUCT R. 5.05(b).

The policy behind this law stems from the complicated nature of Medicaid planning and the high stakes for the elderly individuals involved. This area of practice is full of legal intricacies that can have serious ramifications for the financial well-being of the elderly clients. Consequences for faulty planning can include the denial of benefits, a penalty period, or tax liability. All of this at a time when these

elderly individuals' finances are the most vulnerable. The Texas Chapter of the National Academy of Elder Law Attorneys has formed a committee, headed by Marian Rosen, a litigation attorney with Rosen & Spears, to investigate and pursue violators who are placing elderly citizens at risk. In addition, violators should be reported to the local district attorney and, if they are complicit attorneys, to the State Bar of Texas.

In composing this article, author referenced "Medicaid Planning Legal Only if Offered by Attorney," written by Wesley E. Wright and Molly Dear Abshire, Certified Elder Law Attorneys, which appeared in the Summer 2016 edition of the Texas Chapter of the National Academy of Elder Law Attorneys' Newsletter.

Will Modification and Reformation—a Treasured Tool in an Elder Law Attorney's Toolkit

Texas courts have long exercised a statutory and common law authority to modify or terminate trusts. The Texas Trust Code provides an avenue for a trustee or a beneficiary of a trust to petition the court to modify the terms of the trust to prevent waste, correct a mistake, or achieve tax objectives, in furtherance of the settlor's intent. TEX. TRUST CODE § 112.054. Executors of wills probated in Texas have not enjoyed that privilege until the 2015 legislative changes authorizing judicial modification and reformation of wills. Even now, two years later, many attorneys are not aware of this potential treasure that can be used to both correct drafting errors and the problems that arise from our inability to predict future needs and circumstances of beneficiaries.

Historically, Texas courts have held that a will cannot be reformed after the testator's death. In *San Antonio Area Foundation v. Lang*, the Texas Supreme Court applied the plain meaning rule, noting that the court must focus on the exact words used by the testator, rather than the testator's intent, when interpreting a will. *San Antonio Area Found. v. Lang*, 35 S.W.3d 636, 639 (Tex. 2000). The court held that extrinsic evidence is not admissible when there is no ambiguity in the will. *Id*.

The 2015 Texas Legislature effectively overruled the Texas Supreme Court's decision in *Lang* with the passage of the new Subchapter J of Subtitle F, §§ 255.451-.455 of the Texas Estates Code. These new provisions allow a personal representative of a decedent's estate to petition a court to modify or reform a will to address an administrative issue, achieve the testator's tax objectives, qualify a beneficiary for government benefits, or correct a scrivener's error. TEX. ESTATES CODE § 255.451. Only a personal representative has the authority to request modification or reformation of a will; however, the personal representative has no duty to seek modification or reformation or inform the beneficiaries of the option to do so. TEX. ESTATES CODE § 255.455. Contrary to the Texas Trust Code's modification statute, a beneficiary of a will does not have standing to petition the court for modification or reformation. *See* TEX. ESTATES CODE §§ 255.451-.455.

While many of the advantages and disadvantages are still to be seen in likely litigation over the extent of the statute, elder law attorneys across Texas are excited about a short, but significant, phrase in the statute: "to qualify a distributee for government benefits." TEX. ESTATES CODE § 255.451(a)(2). It is not uncommon for a beneficiary to be healthy and financially independent at the time a testator executes a will and for the testator to not anticipate a beneficiary's future need for and receipt of public benefits. Prior to the passage of Texas Estates Code § 255.451, a beneficiary who was on public benefits and received an inheritance under a will was required to create a self-settled or third-party special needs trust and fund that trust with the inheritance from the decedent's estate within the month of receipt to avoid jeopardizing his or her public benefits. Thanks to the new Judicial Modification or Reformation of Wills statute, the executor of the decedent's estate can ask the court to modify the will

to create a testamentary special needs trust and authorize the executor to fund the trust with the portion of the estate that would pass to any beneficiary receiving public benefits. In addition, if the will includes a supplemental needs trust, but contains an insufficient distribution standard, the court can modify the will by adding or changing specific provisions so that the trust complies with the Social Security Administration's extensive regulations of special needs trusts.

Only time will tell how treasured of a tool in the elder law attorney's toolkit the Judicial Modification or Reformation of Wills statute will be.

ESTATE AND GIFT TAX UPDATE – PART 1

Laurel Stephenson
Davis Stephenson, PLLC
Dallas, Texas
laurel@davisstephenson.com

IRS Makes Syndicated Conservation Easement Transaction a "Listed Transaction"

Notice 2017-10 (2016).

The IRS has warned that certain conservation easements entered into after 2009 will be "listed transactions," effective as of December 23, 2016. The targeted transaction entails a conservation easement described either in written or promotional materials as offering an opportunity to investors to purchase an interest in a pass-through entity holding real property providing the investor with the possibility of a charitable deduction equal to or in excess of two and one-half times the invested amount via the entity's contribution of a conservation easement encumbering the property to a tax-exempt organization. The promised charitable deduction is obtained via (i) an inflated appraised value of the real property premised on "unreasonable conclusions about the development potential of the real property" and (ii) a reduction in value resulting from the easement (the deduction amount). Transactions "substantially similar" to the targeted transaction are also now "listed transactions."

Anyone who invested in the described or a substantially similar transaction must file a disclosure of such with the IRS for each tax year with an open period of limitations as of December 23, 2016. Individuals participating in the capacity as a "material advisor" (e.g., an attorney or accountant who promoted and/or organized the transaction, as well as an appraiser who prepared the facilitating appraisal) must also report a transaction and maintain a list of investors. See Notice 2017-10 for details on the required reporting, including deadlines.

Investors and material advisors are subject to penalties for noncompliance, which may also result in extended periods of limitations for investors. "Appropriate corrective action" is recommended for individuals who filed tax returns reflecting the purported tax benefits.

Final Regulations Issued Modifying Regulations Involving Basis Rules to Incorporate Coordinating References to IRC § 1022

82 Fed. Reg. 6235 (Jan. 19, 2017).

Proposed regulations were issued on May 11, 2015, outlining amendments to various existing regulations to update them to address the impact of Internal Revenue Code (IRC) § 1022. Those proposed regulations have been adopted as final without any substantive changes effective as of January 19, 2017.

IRC § 1022 provided the "modified carryover basis system" applicable with regard to estates of decedents who died in 2010 and opted pursuant to § 301(c) of the Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 not to be subject to Chapter 11 of the Internal Revenue Code. For recipients of property from an electing estate, the basis of that property is consequently governed by IRC § 1022 and not by IRC § 1014. Various existing regulations have now been revised to clarify that result. While most of the affected regulations have been revised simply with a reference to IRC § 1022, certain regulations were revised with additional detail (including an example) to clarify the applicability of IRC § 1022 in the referenced context.

IRS Addresses Tax Treatment of Trust Created in Divorce

I.R.S. Priv. Ltr. Rul. 201707007 (Feb. 17, 2017).

PLR 201707007 provides a nice roadmap for divorcing spouses in structuring a division of the marital property that accommodates one spouse's desire for ultimate ownership of a particular asset and the other spouse's desire to receive its income for a period of time.

As outlined in the ruling, divorcing spouses agreed in a proposed settlement agreement to husband's creation of a trust for wife providing her with an entitlement to all trust income and discretionary distributions of principal, with the remaining trust property reverting to husband (or his estate) upon wife's death. In exchange, wife proposed to relinquish all of her marital rights and property claims. Husband funded the trust in part with stock he evidently wished to retain ultimate ownership of because he prohibited the trustee from distributing the shares to wife or selling shares to facilitate a distribution of principal.

The IRS ruled that the transfer of the shares to the trust would be a "transfer incident to a divorce" and accordingly not result in any gain or loss to husband pursuant to IRC § 1041(a) as long as the spouses finalized the settlement agreement and the transfer of shares occurred within six years of the entry of the final judgment of divorce.

The IRS further ruled that husband's transfers of the shares to wife's trust would be deemed made for full and adequate consideration in money or money's worth pursuant to IRC § 2516 (and therefore would not constitute a taxable gift), provided that a final judgment of divorce occurred within the three-year period beginning on the date one year prior to the execution of the settlement agreement. The IRS correspondingly ruled that IRC § 2702 would not apply for purposes of determining that husband made a gift in conjunction with establishing the trust.

Lastly, the IRS concluded that husband's reversion would result in inclusion of the trust property on hand at the time of his death pursuant to IRC § 2036, subject to a reduction for wife's outstanding income interest if she survived him (valued in accordance with the tables provided in Treas. Reg. § 20.2031-7).

Tax Court Evaluates Expert Witness Testimony in Conjunction with Valuation of "Old Master" Paintings

Estate of Eva F. Kollsman, et. al. v. Comm'r, T.C. Memo. 2017-40 (2017).

The court's analysis of expert witness testimony in *Kollsman* serves as a reminder that hiring an expert with good credentials does not guarantee ultimate success in supporting a returned value if he or she does not have a well-reasoned basis for his or her conclusions, which should ideally be supported by comparable sales.

Ms. Kollsman died in 2005 owning two "Old Master" paintings that were in less than pristine condition. The estate engaged a vice president at a well-known auction house to appraise the paintings. He valued the paintings at $500,000 (the Maypole) and $100,000 (the Orpheus) with heavy discounting to the paintings' values to account for their dirty condition and the "bowed condition" of the Orpheus. The estate's appraiser did not rely upon any comparable sales.

The IRS's appraiser assigned a significantly higher value to each painting based upon comparable sales but without any discounting to account for either painting's dirty condition or the "bowed condition" of the Orpheus.

The court disregarded the valuations of the estate's appraiser, in part based upon what the court felt was an apparent conflict of interest, concluding that he may have assigned each painting a lower value to encourage the estate to engage the auction house's services in auctioning the paintings. The court also noted that the estate's appraiser failed to take into account what the court considered to be sufficiently comparable sales offered by the Service's appraiser in support of his higher values for the paintings.

The court further found that the estate's expert overstated the effect of the paintings' dirty condition on their value and the risks associated with cleaning them, noting that the art restorer hired by the executor informed him prior to the restoration work that he felt the paintings could be cleaned "with relative ease." The court concluded that information would have been considered by the willing buyer and willing seller in negotiating a sales price for each painting and would likely result in only a minimal discount.

The court also found that the estate appraiser failed to account for the Maypole's sale a few years later at a price five times that of the returned value. The estate's expert argued the sale was irrelevant in establishing the Maypole's date of death value because it took place after the painting had been cleaned and after a dramatic increase in the market for Old Master paintings. However, the court was unpersuaded that the sale should be disregarded entirely.

Ultimately, the court rejected the estate appraiser's valuation of each painting and accepted the Service's valuations, subject to the court's discounting of each painting by 5% to reflect the risks (albeit minimal) associated with restoring them. The court applied an additional discount to the Orpheus's value to reflect both its slightly "bowed condition" as well as a question regarding its attribution to the purported artist, as neither concern had been taken into account by the Service's expert in valuing the painting.

ESTATE AND GIFT TAX UPDATE – PART 2

Jason Flaherty
Brink Bennett Flaherty PLLC
Austin, Texas
jflaherty@bbfaustin.com

IRS Issues Procedures to Recalculate Remaining Applicable Exclusion Amounts and GST Exemptions to Extent Used for Transfers by or to Same-Sex Spouses

Notice 2017-15 (Jan. 17, 2017).

As a result of the Supreme Court's decision in *United States v. Windsor*, 133 S. Ct. 2675 (2013), recognizing same-sex marriages, the IRS will now allow taxpayers in same-sex marriages to recoup the prior application of the Applicable Exclusion Amount or GST exemption to transfers by or to a same-sex spouse. Notice 2017-15 provides that same-sex couples who were married under state law at the time of a gift from one spouse to another or a transfer to a spouse on death, regardless of the domicile of the parties, may apply the unlimited marital deduction for both gift and estate tax purposes to recalculate the remaining Application Exclusion Amount or GST exemption, even if the statute of limitations has run on the relevant return. Any claims for credits or refunds for any overpayment of tax must be made within the applicable limitations period for filing such a claim under Internal Revenue Code (IRC) § 6511.

Ruling Allows Late Allocation Out of Automatic GST Exemption Allocated to GRATs

I.R.S. Priv. Ltr. Rul. 2017-05-002 (Feb. 3, 2017).

In PLR 2017-05-002, the taxpayer created and funded a total of twelve GRATs over a two-year period. The taxpayer hired a tax professional to prepare and file a Form 709 United States Gift (and Generation-Skipping Transfer) Tax Return for the years at issue and relied on the tax professional to elect out of the automatic allocation of GST exemption to the transfers to the GRATs. However, in preparing the gift tax returns for two of the years at issue, the tax professional inadvertently failed to elect out of the automatic allocation of GST exemption to the GRATs under § 2632(c)(5)(A)(i)(II).

The IRS ruled that the requirements of IRC § 301.9100-3 were satisfied and, therefore, the personal representatives of taxpayer's estate were granted an extension of 120 days to file supplemental Forms 709 to elect out of the automatic allocation rules of IRC § 2632(c)(1) for the transfers to the GRATs.

IRS Rules that Court Reformation of IRA Beneficiary Designation Cannot Create a Designated Beneficiary for Purposes of Rollover

I.R.S. Priv. Ltr. Rul. 2017-06-004 (Feb. 10, 2017).

In PLR 2017-06-004, the decedent maintained an individual retirement account (IRA) that named an *inter vivos* trust as beneficiary. However, no record could be found of the trust. The decedent's will named his surviving spouse as beneficiary of his entire estate. The IRS ruled that despite a state law reformation of the beneficiary designation for the IRA to name the surviving spouse as the beneficiary, the surviving spouse was not a "designated beneficiary" for purposes of IRC § 408(d)(3). Because the decedent died before his required beginning date and without a designated beneficiary, the entire interest in the IRA must be distributed using the five-year rule described in IRC § 401(a)(9)(B)(ii).

Late Filing Penalty Waived Because of Reasonable Reliance on Advice of Tax Professional

Estate of Hake v. U.S., 119 AFTR 2d 2017-727 (M.D. Pa. Feb. 20, 2017).

In *Hake*, two executors filed the estate tax return for their mother's estate on the date that their tax attorney advised them it was due but which was in fact, six months late. The tax attorney erroneously advised the executors that the due date to file the return had been extended for one year when in fact, it had been extended for only six months. Under IRC § 6651(a)(1), when a taxpayer fails to file a tax return by the due date, including any extension of time for filing, a late penalty applies "unless it is shown that such failure is due to reasonable cause and not due to willful neglect." The court held that the taxpayer demonstrated "reasonable cause" when, in reliance upon the advice of counsel, the taxpayer filed a return "after the actual due date but within the time the adviser erroneously told him was available." The court also recognized that its holding was contrary to the holdings of other courts not within the Third Court of Appeals.

Failure to File FBAR Was Willful Despite Voluntary Disclosure

U.S. v. Bohanec, 118 AFTR 2d 2016-5537 (C.D. Cal. Dec. 8, 2016).

A federal district court's ruling in *Bohanec* is a reminder of the severe penalties that can be imposed for a willful failure to report an interest in a foreign bank account by filing a Report of Foreign Bank and Financial Accounts (FBAR). If a foreign account holder "willfully" failed to report a foreign account on an FBAR, the maximum penalty is increased from $10,000 to the greater of $100,000 or 50% of the balance in the account at the time of violation. The court concluded that the account holders willfully failed to report their interest in foreign bank accounts and imposed a penalty equal to the greater of $100,000 or 50% of the balance in the account at the time of the violation.

MARITAL PROPERTY AND HOMESTEADS UPDATE

Jason A. Cox
Galligan & Manning
Houston, Texas
jcox@galliganmanning.com

Community Property Subject to Husband's Sole Management, Control, and Disposition and Constituted a Valid Sale Even Without Wife's Signature

Ifiesimama v. Haile, No. 01-15-00829-CV, 2017 WL 1173885 (Tex. App.—Houston [1st Dist.] Mar. 30, 2017, no pet. h.).

Tamuno Ifiesimama (Husband) and Tamunnoibuomi Ifiesimama (Wife) decided to sell their home in Stafford, Texas, in 2013. Daniel Haile (Haile) and Wongelawit Alemu (Alemu) made an offer on the house, which Husband accepted, signing a sales contract and setting a closing date.

The contract contained the following term: "If Seller fails to comply with this contract, Seller will be in default and Buyer may (a) enforce specific performance, seek such other relief as may be provided by law, or both, or (b) terminate this contract and receive the earnest money, thereby releasing both parties from this contract."

The parties also executed an "Intermediary Relationship Notice," which identified both Husband and Wife as the sellers and Haile and Alemu as the buyers. Both Haile and Alemu signed this agreement, as did Husband; Wife did not sign this agreement or the sales contract. The "Intermediary Relationship Notice" is the only document in the record that indicates that Wife may have had any interest in the property.

At the closing, Husband signed documents as Wife's attorney-in-fact; however, he later revealed at the closing that he did not actually have power of attorney for Wife. The closing fell through, and Haile and Alemu did not receive title to the property.

Haile and Alemu brought claims against Husband and Wife for specific performance of the sales contract as well as injunctive relief prohibiting Husband and Wife from selling the property to another buyer.

A bench trial was held and the court found in favor of Haile and Alemu, ordering that they recover costs, their earnest money deposit, and attorney's fees from Husband and Wife even though only Husband signed the sales contract. The trial court further ordered that Husband and Wife convey the property to Haile and Alemu.

Husband and Wife appealed on several grounds, including a claim that there was insufficient evidence that both Husband and Wife breached the sales contract.

On appeal, Husband and Wife argued that because the property was their community property, that Husband lacked the authority to sell Wife's interest in the property; they also argued the Haile and Alemu had notice of Wife's interest in the property and that without her signature on the sales contract the property could not be sold.

The court looked to §§ 3.003 and 3.102 of the Texas Family Code, which provide (in part) that during marriage, "each spouse has the sole management, control, and disposition of the community property that the spouse would have owned if single" and that such "property is subject to the joint

management, control, and disposition of the spouses, unless the spouses provide otherwise by power of attorney in writing or other agreement."

The appellate court also cited § 3.104(a) for the proposition that "'[d]uring marriage, property is presumed to be subject to the sole management, control, and disposition of a spouse if it is held in that spouse's name, as shown by muniment, contract, deposit of funds, or other evidence of ownership . . .'" Relevant also was the language in this section stating that "[a] third person dealing with a spouse is entitled to rely on that spouse's authority to deal with the property if: (1) the property is presumed to be subject to the sole management, control, and disposition of the spouse; and (2) the person dealing with the spouse is not a party to a fraud on the other spouse and does not have actual or constructive notice of the spouse's lack of authority."

The appellate court found it was undisputed that Husband and Wife purchased the property during their marriage, admitting into evidence a copy of the deed of trust signed by Husband, which listed him as the sole borrower, but which also included the following provision:

> BORROWER(S)' SPOUSE(S): The undersigned hereby joins in this Security Instrument for the sole purpose of encumbering, subordinating, conveying and/or waiving any current or potential interest in the Property. By signing below, the undersigned encumbers, subordinates, conveys and/or waives any and all rights, interests or claims in the Property, including, but not limited to, homestead, dower, marital or joint-occupancy rights. No personal liability under the Note is hereby incurred by the undersigned joining spouse.

Wife's signature appears under this provision. The appellate court found this constituted a waiver of any interest she might have had in the property and cited § 3.104(a) of the Texas Family Code for the proposition that property is presumed to be subject to the sole management, control, and disposition of a spouse if it is held in that spouse's name.

Therefore, as to this issue, the appellate court concluded that Haile and Alemu presented evidence that the property was subject to Husband's sole management, control, and disposition and that they did not have notice that Husband lacked authority to sell the property on Wife's behalf. The appellate court also found that Husband and Wife did not demonstrate that Wife was a necessary party to the sales contract and that the contract was not valid without her signature and Haile and Alemu entered into a valid and enforceable contract with Husband.

"Separate Property Recital" Negates Community-Property Presumption and Creates in Its Place a Rebuttable Presumption of Separate Property

Cardenas v. Cardenas, No. 13-16-00064-CV, 2017 WL 1089683 (Tex. App.—Corpus Christi 2017, no pet. h.) (mem. op.).

Husband and Wife married in 2008 and moved into a house located at 113 Dorothy Street in Cuero, Texas (113 Dorothy). It was undisputed at trial that Husband acquired this property before their marriage. Five years later, Husband took out a loan of $30,000, which Wife used to purchase a second house at 115 Dorothy Street (115 Dorothy). Their relationship ended in 2014 and Wife moved into 115 Dorothy, filing for divorce shortly thereafter.

At a bench trial in 2015, the trial court found that 115 Dorothy was Wife's separate property. Among several other issues, Husband appealed that Wife failed to prove by clear and convincing evidence that 115 Dorothy was a gift.

It was undisputed at trial that the $30,000 loan was taken out in Husband's name only and that Wife used the proceeds from that loan to purchase 115 Dorothy. At trial, it was also shown that the general warranty deed for 115 Dorothy listed the grantee as "[Wife], a married woman dealing with her sole and separate property."

On appeal, the appellate court cited § 3.003 of the Texas Family Code for the proposition that all property possessed by either spouse on dissolution of marriage is presumed to be community property; the appellate court also cited case law establishing that the burden of overcoming this presumption requires proof by clear and convincing evidence from the party asserting otherwise.

The appellate court further recognized case law that held that "a presumption of separate property arises where the instrument of conveyance contains a separate property recital," which can be a statement "in an instrument that the consideration comes from the separate property of a spouse or that the property is transferred to a spouse as the transferee's separate property or for the transferee's separate use." The appellate court stated that "[s]uch a 'separate property recital' negates the community-property presumption and creates in its place a rebuttable presumption of separate property."

Applying the law to the facts of this case, the appellate court found that because the general warranty deed for 115 Dorothy listed Wife as the grantee, dealing with "her sole and separate property," that there was an expressly stated purpose to make the property part of Wife's separate estate, creating a rebuttable presumption that 115 Dorothy was Wife's separate property. The court ultimately found Husband's testimony was insufficient to overcome this presumption.

COMMERCIAL AND RESIDENTIAL LANDLORD-TENANT LAW UPDATE

Jnana Settle
The Settle Law Firm
Dallas, Texas
thesettlelawfirm@gmail.com

The Court Holds That a Non-Conspicuous Limitation of Damages Provision is Nonetheless Binding Against a Party if Course of Dealing and Attorney Representation Indicate That the Party Was Aware of, and Understood the Meaning of, the Contents of the Provision.

McKinney/Pearl Rest. Partners, L.P. v. Metro. Life Ins. Co., No. 3:14-CV-2498-B, 2017 U.S. Dist. LEXIS 36777 (N.D. Tex. Mar. 15, 2017).

The Facts

Tenant in this case sued Landlord for consequential damages under a variety of claims that amounted to an alleged failure of Landlord to keep and maintain the structural system of the building in good condition and repair. Instead of attacking specific elements in Tenant's causes of action, Landlord asserted the affirmative defenses of waiver and ratification. Under the facts, Tenant and Landlord had signed not just the initial lease but also a renewal and both Second and Third Amendments.

Section 17 of the Lease, titled "Landlord's Default/Tenant's Remedies," provides in pertinent part as follows:

> Tenant's remedies for default hereunder and for breach by Landlord of any of its obligations hereunder will be limited to a suit for actual and direct damages and/or injunction. . . . The liability of Landlord to Tenant for any default by Landlord under the terms of this Lease shall be limited to only Tenant's actual direct damages therefor . . . . In no event shall Landlord be liable to Tenant for consequential, punitive or special damages (or any similar types of damages) by reason of a failure to perform (or a default) by Landlord hereunder or otherwise.

The Holding

The court agreed with Tenant that normally a waiver provision must be conspicuous to be binding, and that the provision in the original lease did not meet the requirements. The waiver provision was not in bold, caps, or any other contrasting font. It was contained on pages twenty-four and twenty-five of a thirty-eight-page lease with almost 100 extra pages of exhibits and amendments. However, the court cited an earlier decision that allows such a disclaimer to be effective if it is shown that the plaintiff had actual knowledge of the disclaimer. *Am. Eagle Ins. Co. v. United Techs. Corp.*, 48 F.3d 142, 146 (5th Cir. 1995) (citing *Cate v. Dover Corp.*, 790 S.W.2d 559, 561 (Tex. 1990)). In the instant case, actual knowledge and, furthermore, understanding of the waiver was evidenced by the facts that Tenant was represented by competent counsel, never claimed to be ignorant of the existence of the provision, and encountered the provision in multiple documents.

What to Take Away

It behooves drafters to remember that waiver provisions should receive special treatment in leases. However, all parties must be aware that an argument based upon lack of special treatment in drafting

has an uphill battle to survive evidence of actual knowledge of the provision. In commercial transactions where a Tenant is likely to be represented by counsel, it is highly unlikely that an argument of ignorance would pass muster. Furthermore, the more times that a party has encountered the provision, the less likely that the court will be able to resist some side eye when that party claims the provision should not apply.

Summary Judgment for Bank/Landlord Was Proper in This Case Because in Texas, the Issue of Possession of Real Property is Separate from the Issue of Immediate Right to Its Possession.

Henderson v. Wells Fargo Bank, N.A., No. 05-16-00471-CV, 2017 Tex. App. LEXIS 1833 (Tex. App.—Dallas Mar. 3, 2017, no pet. h.) (mem. op.).

The Facts

Bank in this case became Landlord for the property, and prior borrowers became tenants-at-sufferance, when terms of the deed of trust kicked in post-foreclosure. As in many Texas deeds of trust, the one in this case specifically provided that if the borrowers should fail to vacate the property after a foreclosure, then the borrowers become tenants-at-sufferance. Tenants refused to vacate, claiming defects in the foreclosure process, and appealed the forcible detainer action that was resolved in favor of Bank/Landlord.

The Holding

In Texas, issues of title and possession can be, and often are, treated with separately. A forcible detailer suit decides only the issue of possession and cannot speak to the merits of a title issue. *Yarbrough v. Household Fin. Corp. III*, 455 S.W.3d 277, 280 (Tex. App.—Houston [14th Dist.] 2015, no pet.). The Tenants attempted to frame their argument as a jurisdictional one, claiming that the lower court had no jurisdiction over possession because such possession was based upon a defective transference of title to Bank/Landlord. The court rejected this argument and held to existing law, which says that post-foreclosure the Bank/Landlord had a right to possession as a matter of law, and any challenge to title must come in a separate action.

What to Take Away

Try as they might, tenants in Texas have virtually no luck arguing title issues in forcible detainer suits. Wrongful foreclosure and other title-related suits must be brought separately except in the rarest of cases. *See In re Gallegos*, No. 13-13-00504-CV, 2013 Tex. App. LEXIS 13876, 2013 WL 6056666, at *5 (Tex. App.—Corpus Christi Nov. 13, 2013, orig. proceeding) (mem. op.) (holding that the issues of possession and title may be intertwined when the deed of trust creating the tenancy was void due to forgery).

Texas Legislators Consider Several Bills Affecting the Rental Housing Industry.

The 85th legislative session is in full swing and several bills affecting the rental housing industry are coming up for consideration in both the house and the senate. Although it is impossible to know which bills will still be kicking as of the time of this printing, at least a few of the following issues will likely still be making their way through the process in May:

- SB 873 and its companion, HB 1964, concern water billing disputes between landlords and tenants. The bills would require tenants with water billing disputes to bring a complaint to the Public Utility Commission of Texas (PUC) prior to filing a lawsuit against their landlord. Currently,

tenants have the option of filing a lawsuit prior to bringing any complaint to the PUC.

- HB 2992 would make it a crime to pass a pet off as a service animal for purposes of gaining access, permission, or benefits that a disabled person with a legitimate service animal would receive. This would include anyone claiming that a pet is a service animal to skirt rental property restrictions on pets. The Texas Apartment Association is supporting this bill.
- HB 1966 would prevent landlords from prohibiting either a tenant or a tenant's guest from carrying a concealed handgun in the tenant's dwelling, in a vehicle parked on the property, or when traveling to and from a vehicle and the dwelling.

CONDOMINIUM, TIME-SHARE, AND HOMEOWNER ASSOCIATION DEVELOPMENTS

Clinton F. Brown
Roberts Markel Weinberg Butler Hailey, PC
Austin, Texas
cbrown@rmwbhlaw.com

Where Insurance Proceeds are Insufficient, Special Assessments Levied Against Unit Owners to Pay for Reconstruction of Condominium Units Damaged by a Casualty are Mandatory Under Chapter 81 of the Texas Property Code

Akhtar v. Leawood HOA, Inc., 508 S.W.3d 758 (Tex. App.—Houston [1st Dist.] 2016, no pet. h.).

Leawood HOA, Inc. (the Association) is a condominium association in Harris County, Texas, governed by various documents including a declaration. In September of 2008, Hurricane Ike made landfall in the Houston, Texas area and damaged the Association's buildings including roofs, gutters, and siding (the Common Elements).

The Association had an insurance policy in place covering the Common Elements with a $500,000 deductible or 2% of the insured value of the property governed by the Association. The insurance proceeds were insufficient to complete the repairs to the Common Elements. The Association relied on the declaration in assessing each owner a special assessment according to each owner's proportionate interest in the Common Elements.

Mr. Akhtar owned five units within the Association and failed to pay the special assessment on five of the units. The Association sued Mr. Akhtar in justice court where a judgment was rendered from the bench in favor of the Association. Mr. Akhtar appealed to the county court arguing the special assessment was invalid as the Association failed to conduct a vote of the members prior to levying such assessment. The county court held a bench trial and found for the Association awarding assessments, court costs, and attorney's fees. Mr. Akhtar appealed.

On appeal, Mr. Akhtar contended the special assessment was invalid as the Association failed to obtain a two-third vote of all members approving the assessment.

The court of appeals stated that because the Association was created in 1983, it is governed by both Chapter 81 and Chapter 82 of the Texas Property Code. Chapter 81 governs condominium regimes created before January 1, 1994. Chapter 82 governs condominium regimes created after January 1, 1994, and certain sections of Chapter 82 also apply to pre-1994 condominium regimes.

In contracts, the common meaning for the term "may" is permissive while the term "shall" is mandatory. Similarly, in statutes, "'"May" creates discretionary authority or grants permission or a power,' while '"Shall" imposes a duty'" unless the context indicates otherwise.

Using the common meaning of the term "shall", the court of appeals turned to interpreting article VI of the Association's declaration. Article VI addressed reconstruction of the Common Elements in the event of a casualty. If less than sixty-six and two-thirds of the Common Elements are damaged, the Association had a duty, through use of the term "shall," to repair the Common Elements using insurance

proceeds. In the event such proceeds were insufficient, the Association had a further duty to recover such deficiency against all owners.

The court of appeals found Mr. Akhtar's reliance on article V misplaced as that article addressed permissive and not mandatory special assessments. Because these special assessments resulted from a casualty, article VI and not article V of the declaration controlled.

Finally, the court of appeals turned to § 81.206 of the Texas Property Code, which imposed a statutory duty on the Association to repair the Common Elements by providing, in pertinent part, that "if a building in a condominium regime is damaged by a casualty against which it is insured, the proceeds of the insurance policy shall be used to reconstruct the building." Furthermore, the court of appeals found that if insurance proceeds are insufficient for such repair, § 81.206 imposed a duty on Mr. Akhtar to pay his proportionate share of the repairs.

Accordingly, the court of appeals affirmed the trial court's judgment.

Former and Current Condominium Directors are Generally Entitled to Immunity Protections Against Unit Owners under the Texas Charitable Immunity and Liability Act

Brown v. Hensley, No. 14-14-00981-CV, 2017 Tex. App. LEXIS 727 (Tex. App.—Houston [14th Dist.] Jan. 26, 2017, no pet.).

The Landing Council of Co-Owners (the Association) was a nonprofit condominium association in the City of El Lago, Texas (the City), near Clear Lake and Galveston Bay. It consisted of approximately 6.71 acres of land with 156 condominium units and various amenities. In September of 2008, Hurricane Ike brought high winds and flooding to the Galveston Bay area, including the Association.

Thereafter, in April of 2009, the City declared the Association substantially damaged and out of compliance with City building codes. No action was taken by the Association and in April of 2010, the City declared the buildings within the Association substandard and a public nuisance demanding the buildings be repaired or demolished. In December of 2010, a fire destroyed four of the seventeen buildings within the Association. Thereafter, the Association obtained a permit to demolish the buildings, which occurred in April of 2011.

In September of 2010, six current or former unit owners (the Owners) sued the Association and various board members (the Board Members) for demolishing the buildings rather than repair them alleging breach of contract, negligence, gross negligence, breach of the duty of good faith and fair dealing, and breach of fiduciary duty, among other causes of action.

The Board Members filed a joint motion for summary judgment arguing the claims asserted would not support personal liability against them and that they were entitled to immunity under the Texas Charitable Immunity and Liability Act (the Act). The Board Members also sought to strike voluminous records attached to the Owners' response to the motion for summary judgment arguing they failed to identify the specific evidence within the records, creating a fact issue.

The trial court struck the records, granted the motion for summary judgment dismissing all claims against the Board Members, and granted a joint motion to sever the dismissed claims from the remaining claims against the Association. The Owners appealed.

On appeal, Owners contended the Board Members were not entitled to statutory immunity under the Act. The Board Members responded, indicating the Act did apply and Owners failed to raise any

statutory exceptions to the Act or that there was a duty owed by the board to the Owners individually, as opposed to the Association generally.

It was undisputed that the Act includes homeowners associations within the definition of charitable organizations, and board members are considered volunteers under the Act. Under the Act and subject to exceptions, "a volunteer of a charitable organization is immune from civil liability for any act or omission resulting in death, damage, or injury, if the volunteer was acting in the course and scope of the volunteer's duties or functions, including as an officer, director, or trustee within the organization."

The Owners asserted that while the Board Members may generally fall within the protections of the Act, the Act does not apply to claims brought by members of the Association against the Association's board pursuant to § 84.007(b) of the Act. This section provides that the Act "does not limit or modify the duties or liabilities of a member of the board of directors or an officer to the organization or its members and shareholders."

The court of appeals rejected this argument, finding that this exception applies only to "a derivative action on behalf of the Association or [] a class action on behalf of all unit owners." Because Owners' lawsuit was neither, the exception did not apply. Further, the court of appeals could not determine whether any fiduciary duty owed to the members arose out of the governing documents of the Association, because they were not included within the appellate record as Owners failed to contest the trial court ruling striking their summary judgment evidence on appeal.

The court of appeals held the trial court did not err in granting Board Members' motion for summary judgment based on the immunity exception under the Act as the evidence established Board Members were members of the board for the Association, the Association was a charitable organization, and Board Members were making decisions on behalf of the Association. The court of appeals acknowledged supporting case law indicating that "[f]or immunity purposes, a person is acting within the scope of his authority if he is discharging the duties generally assigned to him even if the specific act is wrong or negligent."

Accordingly, the court of appeals affirmed the trial court's judgment.

TITLE MATTERS UPDATE

Jeremy T. Brown
Irelan McDaniel PLLC
Dallas, Texas
jbrown@imtexaslaw.com

Inclusion of Additional Leases Not Included in Original Mortgage Held Material for Purposes of Correction Deed Statute

Tanya L. McCabe Trust v. Ranger Energy LLC, 508 S.W.3d 828 (Tex. App.—Houston [1st Dist.] Dec. 22, 2016, pet. filed).

In August 2008, Tomco Energy, PLC executed an assignment and bill of sale to Mark III Energy Holdings, LLC (Mark III) to "'six of the eight oil and gas leases which are collectively known as the "Saratoga Leases".' The parties stipulated that '[d]ue to an inadvertent error, two of the Saratoga Leases were omitted' from an 'Exhibit A'" attached to the 2008 assignment, known as the McShane Fee and Brice leases. Mark III borrowed $4 million from Peoples Bank to finance the purchase. Mark III executed a financing statement security agreement and mortgage (the 2008 Mortgage) to secure the loan and like the 2008 assignment, it omitted the McShane Fee and Brice leases (the Leases). Three years later, Mark III assigned its interests in these leases to two trusts (the Trusts).

Mark III fell behind on its loan payments and Peoples Bank filed a foreclosure suit. To resolve that dispute, Mark III paid the bank $750,000 and executed a renewed and modified deed of trust in 2012. That renewed deed of trust included a substantively identical Exhibit A to the original 2008 mortgage, and therefore, it also omitted the McShane Fee and Brice leases. Soon afterwards, Peoples Bank realized the omission and recorded a revised version of the 2012 deed of trust, adding the word "corrected" to the front page and adding the two other leases to the property description. It also filed revised versions of the 2008 Mortgage to make this same change.

Neither Peoples Bank nor Mark III signed these corrected versions. Instead, the bank simply used the signature pages from the original documents and sent copies to Mark III after filing. Two months later, Peoples Bank and Mark III entered into a second settlement agreement that stated the bank had a right to foreclose on the property listed in the revised 2013 instruments. Peoples Bank transferred its security interest to Ranger Energy, who then foreclosed.

In May 2013, Ranger Energy filed a declaratory judgment action asserting that the foreclosure sale extinguished the Trusts' interest in the Leases. Both parties moved for summary judgment, and the trial court rendered judgment in favor of Ranger Energy. The Trusts appealed, arguing that 2013 revised documents did not comply with the correction instrument statutes as a matter of law, and therefore, Ranger Energy lacked a security interest in the Leases.

The Texas Property Code allows correction of nonmaterial and material changes to real property instruments. The statute specifies that a person with personal knowledge of the transaction may make "a nonmaterial change that results from inadvertent error, including the addition, correction, or clarification of: (1) a legal description prepared in connection with the preparation of the original instrument but inadvertently omitted from the original instrument." TEX. PROP. CODE § 5.028(a-1)(1). In addition, only parties to the original contract may execute a correction instrument that makes material changes, which include a "correction to . . . add . . . land to a conveyance that correctly conveys other land." TEX. PROP. CODE § 5.029 (a). Thus, the distinction of material and nonmaterial is important because

a nonmaterial change may be affected by someone with personal knowledge of the transaction, while a material change may only be affected if the correction instrument is signed by the parties to the transaction or their heirs or successors.

It was undisputed the parties to the transaction did not execute the 2013 correction instrument, so the appeal turned on whether the addition of the Leases was an "addition" of a legal description or whether it "add[ed] . . . land to a conveyance that correctly conveys other land." The court of appeals held it was the latter, relying on the Texas Supreme Court decision *Myrad Properties, Inc. v. LaSalle Bank National Ass'n*, 300 S.W.3d 746 (Tex. 2009). In *Myrad*, the court held that a correction deed could not be used to convey two parcels of land at a nonjudicial foreclosure sale after the original deed unambiguously had conveyed only one of the mortgaged parcels. *Id*. at 750-51. The legislature responded to *Myrad* by enacting §§ 5.027 through 5.031 of the Texas Property Code, codifying the circumstances in which a correction instrument may be used, and despite *Myrad*'s concerns, expressly permitting material changes to be made through a correction instrument.

The court of appeals characterized the 2013 revisions as purporting to add property interests in two leases that previously were not listed. And it held that "the addition of land to a conveyance that correctly conveys other land is a material change." *Ranger Energy LLC*, 508 S.W.3d at 842 (citing TEX. PROP. CODE § 5.028(a)). Therefore, it reversed the trial court and remanded the case.

The majority did not, however, explain how the "addition of" legal description could be reconciled with its holding. Presumably, under this court's view, if a conveyance was missing a legal description in total, the addition of a legal description would be considered a nonmaterial change. But if a legal description was included and conveyed at least some property, then any addition to that legal description to convey more property would be a material change that must be signed by the parties to the transaction.

Justice Evelyn V. Keyes dissented. She found it was undisputed that Tomko conveyed the leases to Mark III in 2008. Because of this contemporaneous conveyance, the correction instrument did not, in her view, "add to" land in a prior conveyance and therefore was nonmaterial and valid. *Id*. at 854 (Keyes, J. , dissenting).

Railroad Deed with Ambiguous Granting Clause Interpreted to Only Convey Easement Despite Presence of Fee Simple Language

BNSF Ry. Co. v. Chevron Midcontinent, LP, No. 08-16-00119-CV, 2017 WL 1076540, (Tex. App.—El Paso Mar. 22, 1017, no pet. h.).

Chevron struck oil in Upton County, Texas, beneath a BNSF-owned railroad. BNSF sued Chevron for trespass to try title, arguing a 1903 deed gave the company not just a right of way easement, but the entire strip of land described in the deed in fee simple absolute. Chevron contended the deed only gave BNSF a right of way to pass trains over the strip, and everything below the land was free and clear of any BNSF interest.

The granting clause in 1903 deed stated as follows:

> WITNESSETH, That the said party of the first [Goode], for and in consideration of One Dollar . . . and of the benefits which will accrue to the party of the first part by reason of the construction of a line of railroad over the land hereinafter described . . . has GRANTED, BARGAINED, SOLD and RELINQUISHED, and by these presents does GRANT, BARGAIN, SELL, RELINQUISH and CONVEY unto the said party of the second part [Panhandle], and unto its

> successors and assigns, for a right of way, that certain strip of land hereinafter described, as the same has been finally located over, through or across the following tracts of land situated in Upton County in the State of Texas . . . .

Id. at *1. The deed then described a line traced by surveyors across various plots of land between various train stations. Using the line as a reference, the deed described the width of the right of way as follows:

> The said railway right of way being 100 feet wide on each side of the center line thereof except [for certain sections where the right of way varies between 50 feet and 150 feet] ... Said railway right of way containing an area of 28 and 55/100 acres. Together with the right and privilege of taking and using all of the wood, water, stone, timber and other materials on said strip of land, or appertaining thereto, which may be useful or convenient in the construction and maintenance of said railway or any part thereof.

Id. The 1903 deed ended with the following habendum clause: "TO HAVE AND TO HOLD the said premises, together with all appurtenances thereunto belonging, in fee simple, unto the said part of the second part [Panhandle] its successors and assigns forever." *Id*.

The court of appeals accepted BNSF's argument that in Texas, "right of way" is not a legal term of art with a set definitive meaning when used in a deed and can be used in two different ways: (1) to describe a party's right of passage over a tract of land; and (2) "to describe that strip of land which railroad companies take upon which to construct their road-bed." *Id*. at *3. The court cited three cases in which conveyances to railroads had conveyed fee simple title, rather than a simple right of way passage right. *Id*. (citing "*Brightwell v. Int'l-Great N. R.R. Co.*, 49 S.W.2d 437, 439-40 (1932) (deed conveyed 200-foot-wide strip of land in fee simple); *Calcasieu Lumber Co. v. Harris*, 13 S.W. 453, 453-54 (1890) (deed conveyed 100-foot-wide strip of land to railroad in fee simple); *Right of Way Oil Co. v. Gladys City Oil, Gas & Mfg. Co.*, 157 S.W. 737, 739 (1913) (noting that while historically railroad rights-of-way were usually conveyed as easements, the 'land . . . may [also] be conveyed in fee; therefore the character of the title conveyed must be determined by the words used and the attending facts and circumstances')").

The court explained that the Texas Supreme Court set forth the rule of construction in these circumstances in 1952 in *Texas Electric Railway Co. v. Neale*:

> [A] deed which by the terms of the granting clause grants, sells and conveys to the grantee a 'right of way' in or over a tract of land conveys only an easement . . . [but] a deed which in the granting clause grants, sells and conveys a tract or strip of land conveys the title in fee, even though in a subsequent clause or paragraph of the deed the land conveyed is referred to as a right of way.

Id. at *4 (quoting *Texas Elec. Ry. Co. v. Neale*, 252 S.W.2d 451, 453 (1952)).

BNSF argued that use of the word "a strip of land" in the granting clause was conclusive, and relying on *Neale*, the clause "for a right of way," merely referenced a purpose that was not intended to modify the interest conveyed. *Id*. at *5. The court explained that *Neale* only stated that a statement of purpose "in a subsequent clause or paragraph of the deed" does not alter the interest conveyed in the granting clause. It did not, however, provide that a statement of purpose included in the granting clause itself lacked any effect on the interest conveyed. In the court's view, including right of way in the granting clause along with "that certain strip of land" rendered the granting clause ambiguous, and therefore, the

Neale rule did not apply. Because the granting clause was ambiguous, the court found it necessary and proper to examine the remaining parts of the deed as a whole to glean the grantor's intent.

Reading the deed as a whole, the court found Chevron's interpretation that only an easement was conveyed was the only reasonable conclusion based on the following facts:

- The opening recitals recognized the value of having a railway pass "over" the land";
- The phrase "right of way" appears directly in front of phrase "that strip of land";
- The clauses describing the conveyance described the right of way "[o]ver, through, and across" the land;
- The deed specifies that the conveyance also included a right to use the resources on the right of way, which would be unnecessary if the grantor intended to convey fee simple title; and
- The habendum clause referenced "the said premises," instead of "property," which suggested conveyance of only an easement.

Chevron argued the "fee simple" language in the habendum clause was not inconsistent with these other parts of the deed because it was simply a characterization of the duration of the easement. Chevron relied on other jurisdictions' interpretation of "easements in fee simple" to mean that the easement is held in perpetuity and may be disposed of at will. The court was unwilling to go that far, and simply held that the habendum clause's "fee simple" language should be disregarded because it conflicts with the remainder of the deed when read as a whole. *Id*. at *8.

Buyer Held to Have Constructive Notice of Abstract of Judgment Filed Against Party with Two Surnames

Austin v. Coface Seguro de Credito Mex., S.A. de C.V., 506 S.W.3d 707 (Tex. App.—Houston [1st Dist.] 2016, pet. filed).

In this appeal, the court of appeals addressed whether differences in naming conventions nullify notice of an abstract of judgment. A bank obtained a judgment in Mexico and later registered it in Texas state court, using the debtor's full name, which included a first and a second surname "Rafael Augusto Martin Ojeda Miranda." When the bank abstracted the authenticated judgment in the county records, the county clerk indexed the judgment under the last name "Mirandas," instead of "Miranda;" thus, the record index recited "Mirandas Rafael Augusto Martin Ojeda." In other words, the abstract of judgment was not indexed under the other surname "Ojeda." In July 2013, Carolyn P. Austin purchased the property from the judgment debtor by way of a warranty deed naming "Rafael Ojeda and wife, Liyian E. Cordova" as grantors. At the preclosing meeting, the judgment debtor produced a passport showing his full name. The title search did not search the real property records using either the name "Miranda" or Rafael Augusto Martin Ojeda Miranda," and neither the buyer nor the title company discovered the abstracted judgment before closing. When the bank sought to foreclose on the property, the owner filed suit, seeking a declaration that the bank's abstract of judgment lien did not encumber the property.

The owner contended that the bank was obligated to secure an index under the first surname listed in the abstract of judgment to enforce its lien on the property, because the warranty deed that conveyed the property named the seller by his first name and first surname only. The bank responded that the chain of title for the property includes the debtor's full name as it is contained in the abstract of judgment. On cross-motions for declaratory relief, the trial court found in favor of the bank.

The court of appeals affirmed but declined to address whether the abstract of judgment needed to be indexed under both the paternal and maternal surnames because other parts of the chain of title provided record notice of the name in which the abstract of judgment was indexed. In particular, the real property records included a notice of lis pendens, which identified the judgment debtor by his full name and alternatively included "Rafael Ojeda." *Id*. at 713. Because of this, the court of appeals held that the owner and title company had constructive knowledge of the judgment debtor's full name, because it was contained both in the abstract of judgment and in the real property records indexed under either surname. *Id*.

PROPERTY TAX LAW UPDATE

John Brusniak
Brusniak Law PLLC
Dallas, Texas
john@txtax.com

If an Appraisal District Creates Separate Account Numbers to Cover Parts of a Complex Facility, Then a Taxpayer May Challenge Any of Those Parts Under an Equality Theory Without Challenging the Entire Value of the Facility.

Valero Refining-Tex. L.P. v. Galveston Cent. Appraisal Dist., No. 15-0492 (Tex. Feb. 24, 2017).

Appraisal district assigned different account numbers to a variety of the components of a property owner's refinery including pollution control equipment. The property owner appealed some of the accounts on the basis of inequality to district court. On appeal, the Texas Supreme Court rejected the appraisal district's argument that a taxpayer must appeal the entire valuation of a complex facility stating, "If the component parts of a property cannot be valued in isolation, then as a matter of law, separate tax accounts are not appropriate. It follows that if tax accounts are appropriate, then, as a matter of law, the property in each account can be valued in isolation." It further rejected the appraisal district's argument that the only reason the taxpayer failed to include pollution control equipment in its suit was because it was trying to lower the value of the property: "While the District complains that Valero has excluded PCE values to obtain a more favorable result, one would expect a party to do exactly that."

An Appraisal District May Not Assess Pooled Mineral Interests That Are Located Outside Its County Lines If the Lease Authorizes Pooling But Not Cross-Conveyances of Interests.

Chambers v. San Augustine Cnty. Appraisal Dist., No. 12-15-00201-CV (Tex. App.—Tyler Feb. 8, 2017, no pet. h.).

Taxpayers owned land in Shelby county and entered into oil and gas leases. Their interests were pooled with production units located in San Augustine County. The San Augustine County Appraisal District sent a notice of appraised value to the taxpayers. Taxpayers protested claiming the district did not have the right to appraise their property because it was located in Shelby County. The taxpayers pointed to language in their leases that allowed pooling but prohibited cross-conveyances of their interests. The court of appeals ruled that taxation was contingent upon the wording of the leases. "Giving effect to all language of Appellants' leases, we conclude, as a matter of law, that the leases authorize pooling but prohibit cross-conveyance of interests. . . . Accordingly, SCAD failed to establish that Appellants owned an interest in pooled minerals located in San Augustine County."

Property Owners Are Not Required to Specify Grounds of Relief in a Petition For Review Of an Appraisal Review Board Order.

United Airlines, Inc. v. Harris Cnty. Appraisal Dist., No. 14-15-01014-CV (Tex. App.—Houston [14th Dist.] Dec. 6, 2016, pet. filed).

Taxpayer owned personal property in Harris County. Taxpayer protested the value of its property before the appraisal review board and filed an appeal to district court. In its original petition, it claimed

the appraised value of the Property was excessive and attached the orders from the appraisal review board hearing. The Taxpayer later amended its petition and removed its claim for excess appraisal and added a claim for unequal appraisal and reattached the same orders. The appraisal district filed a plea to the jurisdiction asking the court to dismiss the case, claiming the court did not have jurisdiction over the excessive appraisal claim since the filing of the amended petition acted as a dismissal of the original petition, and because the unequal claim was not timely filed within the sixty-day deadline for seeking judicial review. The Taxpayer then filed a second amended petition, again pleading a claim under excessive appraisal, and again reattaching the same orders. Additionally, the Taxpayer filed a motion to withdraw its first amended petition, or in the alternative, motion to reinstate its original petition, claiming the first amended petition was filed in error. In response, the district court dismissed the case. On appeal, the court ordered the case reinstated. "In adopting the current tax protest mechanism, this court has noted 'the legislature rejected hypertechnical requirements for challenges to appraisal values.' . . . Indeed, nothing in either the Tax Code or the case law requires a party to include its grounds of relief in a petition for review in order to invoke the jurisdiction of the trial court. . . . Further, sections 42.25 and 42.26 do not address whether a party must plead relief under these provisions . . . . Moreover, other parts of the Tax Code demonstrate that stating the particular grounds for appeal is not jurisdictional and need not be contained in the petition. . . . Finally, there are no consequences in Chapter 42 for failing to plead a particular ground for relief, which supports the conclusion that pleading certain grounds is not a jurisdictional requirement to maintain an ad valorem tax appeal."

Owners of Land May Be Taxed Separately on the Value of Their Surface Estates and the Value of Salt Water Disposal Wells Located on the Land from Which They Are Deriving Revenue.

Parker Cnty. Appraisal Dist. v. Bosque Disposal Sys., LLC, No. 02-15-00343-CV (Tex. App.—Fort Worth Dec. 1, 2016, pet. filed).

Taxpayers owned land on which saltwater disposal wells were located. A third-party appraisal firm hired by the appraisal district valued the wells separately from the surface estate based on an income approach to value. After exhausting administrative remedies, taxpayer sued claiming that the procedure was illegal because the value of the wells was subsumed within the valuation of the surface estate and that the assessment of the disposal wells absent their severance from the land constituted a double tax assessment. The court of appeals disagreed citing both the Tax Code and judicial precedent and ruled that at least some "aspects of real property can be taxed separately even though all are part of the same surface tract." It went on to say that "it is not the severance of the surface and subsurface estates by conveyance that gives a taxing authority the right to assess different types of property interests." And it concluded that the interest taxed was not intangible in nature because the appraisal district did not value the permit allowing the use of the disposal wells, but rather it valued the income that was received from the use of the separate estate.

Affirmatively Asking an Appraisal Review Board to Deny a Protest Is the Same As Failing To Appear At the Hearing and Results In a Failure to Exhaust Administrative Remedies; Taxing Units Do Not Have Standing to Sue Under the Tax Equity Provisions of the Tax Code; Governmental Entity Must Demonstrate a Specific Injury to Itself to be Able to Sue an Appraisal District.

City of Austin v. Travis Cent. Appraisal Dist., No. 03-16-00038-CV, (Tex. App.—Austin Nov. 10, 2016, no pet.).

The City of Austin filed suit against the appraisal district, the state of Texas, and all property owners

of vacant land and certain commercial real property within Travis County. The City of Austin claimed that the appraisal district's appraisals of vacant and commercial real property in Travis County were unequal when compared to other categories of property for tax year 2015. The trial court dismissed the lawsuit for lack of jurisdiction. The City of Austin claimed certain categories of properties had been undervalued in tax year 2015, due to reductions made during protest hearings, which reduced the median value in violation of the constitutional requirement that property be taxed at its market value and taxation be equal and uniform. The court of appeal determined that the City of Austin failed to establish an injury sufficient to establish standing. The claims brought by the City of Austin are provisions of the tax code that provide taxpayers the right to protest their appraisals. Sections 41.43(b)(3) and § 42.26(a)(3) do not provide a taxing unit any authority to implement these sections. The Tax Code also provides limited authority to governmental entities to challenge determinations made by an appraisal district. To appeal to a district court, a taxing unit must exhaust its administrative remedies. The City of Austin failed to exhaust its administrative remedies in this case because, even though it appeared at the protest hearing, it did not present a case on the merits of the challenge, and instead presented a joint motion requesting the Appraisal Review Board to deny its protest. Since the City of Austin appeared at the hearing solely to ask the Appraisal Review Board to deny its protest, the Appraisal Review Board was deprived of the opportunity to make a decision based on the merits of the protest. The court of appeals affirmed the trial court's ruling and found that the City of Austin's dispute was over tax policy, which is not to be determined by a court, but better suited for the legislature.

REAL ESTATE & OIL AND GAS TAX UPDATE

Edward E. Hartline
Oaks, Hartline & Daly, LLP
Houston, Texas
hartline@ohdlegal.com

Taxpayer Did Not Show Dedication in Excess of 750 Hours and Therefore, was Not Considered a Real Estate Professional

Rapp v. Comm'r, U.S.T.C. 2017-14 (2017).

In *Rapp*, the taxpayer was involved as an employee of two firms in the development of commercial real estate. Taxpayer worked full time in connection with this activity. Taxpayer was the property manager for his five rental properties but did not provide any evidence about how much time he spent on his rental activities during the year. Taxpayer did not own any interest in the two real estate businesses that employed him but he had been told he might receive an equity interest if he developed an independent project. It was clear that the taxpayer spent well over 750 hours during the year working as an employee of the real estate companies. The provisions of § 469(c)(7)(D)(ii) indicate that personal services performed by an employee shall not be treated as performed in real estate trades or businesses. However, if the taxpayer owns more than 5% of the entity for which he is an employee then the hours can be counted. In this case, it was found that the taxpayer did not show that he dedicated in excess of 750 hours per year toward the management of his personal real estate portfolio and therefore, was denied a deduction for the losses incurred on the rental real estate.

Taxpayer Determined to be Real Estate Professional and Thus, Real Estate Losses were Not Barred from Being Claimed

Zarrinnegar v. Comm'r, 113 T.C.M. 1148 (2017).

In *Zarrinnegar*, the taxpayers were again attempting to deduct losses incurred in connection with rental real estate. In this case, both taxpayers were dentists who shared a staggered dental practice. The government contended that the taxpayers were not real estate professionals and did not spend the requisite hours in connection with their real estate rental activity and also kept inadequate records of charges for supplies and how they are related to their dental practice. Petitioner husband worked at real estate brokerage activities in addition to his dental practice. He spent hundreds of hours on brokerage-related activities including brokers' tours, listing searches, open houses, property viewing, and client meetings. It was clear that petitioner spent more than 1,000 hours on the real estate business. In determining the number of hours husband spent in the real estate activities, the court noted that contemporaneous time reports, logs, or similar documents are not required. The number of hours can be shown by reasonable means, which can include the identification of the services performed over a period of time and the approximate number of hours performing such services during such period based upon appointment books, calendars, and narrative summaries. A post-event ballpark guesstimate is not sufficient, but neither is a contemporaneous time log required. The court's finding was that the Petitioner worked more hours on his real estate activities than he did on his dental practice and thus, qualified as a real estate professional and thus, losses on his rental real estate activities were allowed. However, Taxpayers were penalized for keeping insufficient records concerning expense deductions related to their dental practice.

IRS Adds Matters to its No Ruling List

Rev. Proc. 2017-3.

Internal Revenue Service was discussing additional matters which were to be added to its no ruling area. One of the areas involved the tax consequences of shared appreciation mortgage loans in which a taxpayer borrowing money to purchase real property pays a fixed rate of interest on the mortgage loan below the prevailing market rate and will also pay the lender a percentage of the appreciation value of the real property upon termination of the mortgage. The Service said that this would be a no ruling area if the facts are not similar to those described in Revenue Ruling 83-51. This revenue ruling describes three separate situations where money was advanced to a taxpayer under a shared appreciation mortgage arrangement. In each case, the loan bore current interest plus some share of the appreciation payable at the time the property was transferred or the loan paid off. In one of the transactions, the taxpayer had the shared appreciation mortgage for the full term of the shared appreciation loan and at the end of that loan, the taxpayer refinanced the loan and paid a percentage of the appreciation to the shared appreciation mortgage loan holder. In this situation, the taxpayer was not allowed to deduct the contingent interest on the shared appreciation mortgage loan because pursuant to the refinancing, the loan was not deemed "paid" and thus, the contingent interest was not deductible. In the other two instances, the property was transferred or the loan was paid off. To reach a position consistent with rulings issued by the Internal Revenue Service, on a shared appreciation mortgage loan, for the contingent interest to be considered deductible under § 163, the loan must be "paid" at the termination of the shared appreciation mortgage.

A CONSERVATION EASEMENT ON CAMP RIO: HOW IDEA PUBLIC SCHOOLS, INC. TRANSCENDED TAX INCENTIVES

Jesus "Jesse" Barba Jr.
Mayfair | Rioco
McAllen, Texas
jbarba@rioco.com

In late 2016, the award-winning charter school system, IDEA Public Schools, secured ownership of an eighty-five-acre tract of land nestled just inside the city limits of Brownsville, Texas. It was a historic moment for the public school and the conservation sector. Not only would public school students in the Rio Grande Valley benefit from an outdoor classroom facility, a rare piece of South Texas earth could be preserved for those students.

It is also extraordinary for its unique intersection of a public charter school, conservation easement holder, and private landowner. Historically, the eighty-five-acre facility had been known as Camp Lula Sams. For several generations, it served as a well-known retreat for Girl Scouts of the Rio Grande Valley. Over the years, however, it became used less often and eventually fell into disrepair. In 2001, a group of investors purchased the facility to hold for future use. In the meantime, they held private instructions on environmental resources at the Camp. Eventually, it became evident that classes in ecology would never fully support the steadily increasing march of taxes and maintenance costs. Inevitably, the Camp had to be sold.

The owners, however, faced a conundrum if it wished to preserve the environmental aspects of the property. As investors, they had to be fully compensated for their ownership and could not deplete its value through a property restriction on use, yet they knew they had to preserve the Camp for its unique wildlife habitat and native forestry. A conservation easement would satisfy the latter. The former could only be satisfied if a buyer was willing to pay fair market value for fee simple title but still agree to assume an enormous restriction on the land.

This proposition to restrict use yet demand full market value would be difficult for traditional developers to accept. A conservation easement typically devalues the property from 40% to 60% of its commercial value/potential. In addition, the conservation easement is accompanied by a slew of additional land burdens. Effectively, the landowner conveys away the development rights to the property, dramatically reducing its development potential, obviously, and also its use. Furthermore, from a business standpoint, given the ever-present challenges of taxes and maintenance, the property would still need to yield adequate revenues to pay for its own existence. Under these circumstances, there is a naturally dramatic winnowing of interested buyers.

Enter IDEA Public Schools. Chartered in 2001, it has grown from a small campus of 187 students in tiny Donna, Texas, to nearly 30,000 enrolled in the fall of 2016. In the Rio Grande Valley alone, there are 21,000 students in thirty-one schools as of 2016. By 2022, IDEA schools are projected to have 100,000 students in over eighty-seven different campuses. It is a growing program that considers itself an education innovator. As luck would have it, IDEA had been seeking a location to apply an adventure-based, outdoor learning environment to augment its growing ensemble of campuses. And, this new owner would not mind a property restriction, such as a conservation easement, that placed conservatorship of the land into its own business plan for expanding the school system.

Typically, a property owner would seek out a conservation easement donation to obtain certain

favor tax incentives. Interestingly, there was no use for the traditional tax-based incentives for this conservation easement donor. Whereas a conservation easement donor could claim a favorable tax credit, as a 501(c)(3) corporation, the nonprofit could not enjoy those tax privileges. They would be inapplicable.

To allow for the tax deductions, the conservation easement must qualify under several related guidelines. I.R.C. § 170(h). First, the conservation must be protected in perpetuity, meaning forever. Treas. Reg. § 1.170A-14[g][4]. Second, the CE holder itself must qualify. Typically, these are nonprofits that have a conservation-centric mission, such as the Valley Land Fund, the holder of the Camp Rio easement. And third, the grant must be done for a "conservation purpose." Here, the law becomes a little more technical. In a nutshell, the CE may be either for outdoor recreation, protection of natural habitat, preservation of open space, or preservation of historically important land. The taxpayer seeks those pathways to obtain a tax deduction.

For example, a taxpayer holding land (typically open space or wildlife land) can seek the tax deduction for its donation of the conservation easement. Assume there is a ranch valued at $4,000,000, with a conservation easement coming off that land valued at $1,200,000. This would imply a 30% reduction in property value because of the donated conservation easement. The IRS would allow the tax payor to take tax deductions up to 50% of the donor's adjusted gross income (or AGI). If the donor earns $150,000 in AGI, then allowed deduction would be $75,000. Should that donor continue to earn $150,000 in AGI for the next several years, then that taxpayer would only deduct $75,000 over the next fifteen years when he or she has exhausted the $1,200,000 contribution.

Had the public school sought out the special tax treatment, it would need to demonstrate its intent of the charitable gift. Under the Treasury Regs, the donor must (i) obtain a qualified appraisal (described under typical gift guidelines under IRS Form 8283), (ii) commission a baseline study of the "conservation values" on the land, and (iii) record a conservation easement document that grants the easement to a qualified land trust. Treas. Reg. §1.170A-14[g][5].

It will be also important for the landowner to have all other interest on the land subordinated, including mortgagees and surface mining. As holders of superior rights, these interested parties would render the conservation easement meaningless if they could simply demolish the surface estate or foreclose against the CE. Surprisingly, it is not terribly difficult to secure a subordination from a lienholder. Mortgagees simply look to the value of the collateral and whether sufficient equity exists to justify a foreclosure against a burdened real property. Similarly, a surface use waiver can be obtained from the mineral estate holder. There may be some research to confirm who has the executory rights to sign off on the subordination. However, a mineral interest holder can be persuaded to keep the mineral rights as part of a pool, just not exercise the surface for the actual drilling operation. If it's possible that the executory rights or other mineral rights remain so disperse as to be remote, the IRS does allow the property owner to forego the subordination if he can prove up this possibility in a mineral remoteness report.

In the case of Camp Rio, the landowner met all the requirements for a true conservation easement and went through the motions to substantiate the conservation easement. The conservation values were documented: the land has a thriving Sabal Palms forest as well as rare species of birds and animals. IDEA then established a conservation purpose, being the protection of the native plants and wildlife. The school even conveyed its mineral rights, which it obtained from the prior landowner, to the Valley Land Fund, which qualified as the conservation easement. It was truly a collaborative effort that benefited all the interested parties.

While the school could not benefit from making an adjustment to its taxable income, the exercise of creating the conservation easement resulted in more than just the protection of the land. The value of the easement came from enhancing the use of the outdoor classroom and in the long-term economic value in preserving the economic landscape of the property. No short-term future development could displace the conservation values from the students sent to learn at Camp Lula Sams. Neither could the land be threatened into development by creditors or prospective partners, seeking a short-term gain on a current asset. This also serves as an immeasurably valuable consideration for an organization that relies partially on secured financing for its school funding. The economic value, therefore, resides not in a mere IRS tax deduction but rather in promoting the exceptional benefits of an outdoor classroom, forcing economic value from a long-term hold, and neutralizing risk to the organization.

There are, therefore, economic benefits to the land owner from a conservation easement that transcends the tax incentives. There are tax incentives to the traditional conservation easement to be sure. However, alternative uses of the conservation easement can follow such innovative approaches as well.

GAME OF ETJS: MUNICIPAL ANNEXATION AND EXTRA-TERRITORIAL JURISDICTION

Kevin Pierce
SMU Dedman School of Law
Dallas, Texas
Kpierce@smu.edu

STUDENT WRITING CONTEST

Honorable Mention – Real Estate 2016

In the State of Texas, a conflict is being fought on the local and legislative level. It pits residents who have chosen to live free from the confines of local government with municipalities that seek to increase their territory and their tax revenue. The law relating to municipal law and extraterritorial jurisdiction affects millions of Texans but, outside of the attorneys who specialize in this area, it remains somewhat of a black box for the outside observer. But with an understanding of the fundamentals, an attorney can gain the foundation to be proficient in this interesting and evolving area of the law.

The main hub of statutory provisions relating to ETJs are codified under Chapter 42 of the Texas Local Government Code (TLGC), but references to the extraterritorial jurisdiction of a town, city, or municipality can be found throughout all the Texas codes. The term "extraterritorial jurisdiction" as a discrete concept with directly quantifiable borders did not exist until 1963, when the Texas Legislature passed HB 13, which came to be known as the Municipal Annexation Act.[1]

The ETJ of a municipality is the unincorporated area contiguous with its corporate limits.[2] The size of extraterritorial jurisdiction that a given municipality has is determined by the number of inhabitants in that municipality.[3] Generally, the ETJ area is expanded every time the boundaries of a municipality grow, typically by means of annexation.[4] As a general rule, municipalities may only annex land that is within its ETJ, though there are exceptions.[5] The ETJ of a municipality may also expand if the property

[1] TEX. REV. CIV. STAT. ANN. art. 970a.

[2] *Id*.

[3] *Id*.

[4] TEX. LOC. GOV'T CODE § 42.022(a).

[5] *Id*. § 43.051.

owner, who is contiguous with the ETJ boundary of a municipality, petitions that municipality include the property in the municipality's ETJ.[6]

Main Entities Involved in ETJs and Annexation

There are three main groups that municipal annexation affect the most: municipalities, land developers, and residents. Municipalities directly deal with their ETJ more than any other entity. Municipalities can be broken up into two main types, home-rule municipalities and general-law municipalities, which is an important distinction particularly regarding municipal annexation and will be explored further below. Land developers often work within a municipality's ETJ for their projects. Developing land for projects, such as housing divisions, in a municipality's ETJ allows developers to have the reasonable certainty that their division will be annexed into a growing municipality, which is a selling point for home builders, but at the same time not be directly limited by a municipality's development standards or be subject to the municipality's tax levies during the development and construction periods. Finally, residents who reside in the ETJ might not be very important to the formation of annexation law, but they are the most impacted group when it comes to annexations.

Home-Rule and General-Law Cities

There are two main types of municipalities in Texas: home-rule municipalities and general-law municipalities.[7] General-law municipalities only have the powers specifically granted to them by the Texas Local Government Code.[8] Conversely, home-rule municipalities may give themselves whatever powers they wish through the use of a charter, so long as the provisions of the charter are not in conflict with any prohibition in the Code.[9] General-law municipalities can only annex areas that volunteer for annexation, with narrow exceptions.[10] Conversely, home-rule municipalities have far greater latitude to annex areas in their ETJ involuntarily, subject to certain exceptions.[11] General-law municipalities have additional restrictions to the annexation process.[12]

Nature of Extraterritorial Jurisdiction in Texas

Many Texans lived in a municipality's ETJ and do not realize it. While the ETJ of a municipality is subject to municipal actions, it is not a part of the municipality. Municipalities typically prepare and intend to grow as new residents arrive and having areas "prepped" for future annexation smooths the process along. Residents in ETJs pay no taxes to the correlating municipality. Tax revenue is a major incentive to municipalities that are seeking to increase tax revenue and annexation is one efficient way to increase their tax base.

---

[6] *Id*. § 42.022(b), which allows homeowners who are worried about an encroaching municipality from another direction taking them up by annexation to expand ETJ. By placing themselves in the ETJ of a municipality that cannot or most likely will not expand (such as a general-law municipality boxed in by other municipalities), they prevent their property from being annexed into any city.

[7] *See id.* § 5.

[8] *See generally id.* §§ 6-8.

[9] *See generally id.* § 9.

[10] *Id*. § 43.033.

[11] *Id*. § 43.034.

[12] *Id*. § 43.032.

There are some situations where municipalities do not seek to annex territory. Small towns have their own governing boards and they serve at the will of their voters and an influx of new voters may change the political makeup of the governing body. Further, if the area is sparsely populated, or geographically remote, the cost to provide full municipal services may outweigh the anticipated tax revenue.

How is the ETJ Formed and How Does It Grow?

The amount of ETJ ranges from a one-half mile from the city boundaries to five miles from the city boundaries, and the inhabitant amount necessary to have an ETJ of five miles requires a minimum of 100,000 inhabitants.[13] The actual range of a municipality's ETJ is not a perfect circle around a municipality. Municipalities do not annex in neat or tidy sections and because the ETJ of one municipality cannot intrude upon a neighboring municipality's ETJ, determining the ETJ boundary of a given municipality can be troublesome and messy.[14]

Municipal Annexation

Annexation is an orderly process of acquisition of territory around a municipality. Annexation of territory in a municipality's ETJ is primarily covered under Chapter 43 of the TLGC.[15] Subject to exceptions (of which there are many), a municipality may only annex land that is (1) contiguous with its corporate boundaries and (2) within its ETJ.[16] In general, municipalities annex area that is exempt from annexation plans, which are municipal council-approved documents that identify land that will be annexed within a certain period. Most annexations therefore occur under Subsection C-1 in § 43 of the TLGC, which describes the process for annexing territory that is not required to be part of an annexation plan.[17]

Nonannexation Plan Municipal Annexation

A municipality can involuntarily annex land upon which there are less than 100 tracts.[18] A home-rule municipality may present, if it chooses or is required under its charter, an election item to its voters to annex land.[19] There are certain procedural requirements the municipality must follow, but the requirements are very loose and if the municipality's charter is broad, the municipal government has great flexibility in how it goes about annexing property.[20] General-law municipalities, on the other hand, must always submit the annexation proposal to the voters.[21]

A municipality cannot just choose to annex as far as it can reach at any given time. The statutory rule is that a municipality cannot annex area that totals more than 10% of the area of its own

[13] *Id*. § 42.021(a).

[14] *Id*. § 42.022(c).

[15] *See id*. § 43.

[16] *Id*. § 43.051.

[17] *Id*. § 43 C-1.

[18] *Id*. § 43.052(h)(1).

[19] *Id*. § 43.022(a).

[20] *Id.*

[21] *Id*. § 43.023(c).

incorporated area as of January 1 of that year.[22] A municipality must also conform to certain requirements as to the actual size of the territory it wishes to annex. It may not annex any land that is less than 1,000 feet wide at its narrowest point, subject to exceptions for land that is contiguous on two sides by the municipality or the land petitions for annexation.[23] Before a municipality can begin the annexation process proper, it must hold hearings for the public to have the opportunity to speak regarding the annexation.[24] There are requirements as to where the hearings are held and the manner they are held in.[25]

Landowners may also petition a municipality for annexation.[26] They still must be within the ETJ of municipality and contiguous.[27] A landowner may choose to petition to be annexed to enjoy the voting rights of a municipality resident, or to receive services to the landowner's property.

Prevention of Annexation

Hearings are required to be held before a municipality may annex an area, and that presents an opportunity for the affected landowners and residents to make their voices heard.[28] If it becomes politically untenable due to public outcry, an annexation may be prevented. With enough political pressure, a landowner may carve himself out of an annexation and stay isolated on his property.

Post-Annexation

Following the annexation, municipalities are obligated to provide services, or have services provided, to the newly annexed areas. Prior to annexation, a municipality is required to have prepared a service plan that shows the municipality is prepared to provide necessary services to its new residents.[29] Small municipalities may strike deals with land developers or counties to have services provided to their new residents.

Municipalities are also prohibited by statute from preventing landowners from continuing to use their land in a way that was legal at the time of annexation.[30] The municipality may prevent such use, however, if it is a regulation of a few select matters, such as a public nuisance, would prevent imminent destruction of property, firework sales, or a sexually-oriented business.[31]

Disannexation

The TLGC provides multiple opportunities for areas that have been annexed to remove themselves from the municipality through disannexation.[32] A successful disannexation prevents the area from being

[22] *Id*. § 43.055(a).
[23] *Id*. § 43.054.
[24] *Id*. § 43.063.
[25] *Id.*
[26] *Id*. § 43.052(h)(2).
[27] *Id*. § 43.052.
[28] *Id*. § 43.063.
[29] *Id*. § 43.056(a).
[30] *Id*. § 43.002(a).
[31] *Id*. § 43.002(c).
[32] *Id*. § 43.141.

annexed again by the municipality for ten years.[33] Voters in the annexed area may petition a municipal body for disannexation if they have not been provided services in accordance with the statutes.[34] General-law municipalities must hold an election and vote upon the disannexation proposed for reasons other than failure to have services provided.[35]

Select Issue: Tricks of the Trade in Annexation

As with all complex statutes, various statutory provisions, regulations, and rules create gray areas and unintended options the legislature may not have intended, but of which savvy municipalities have taken advantage.

There exists an interesting "back door" to annexing land when a general-law municipality is unable to get around an area that is not volunteering to be annexed. The default rule is a municipality may only annex land that is contiguous with the city boundaries and within its ETJ.[36] But, a municipality may annex land that it owns, regardless of its location under § 43.051 of the TLGC.[37] This creates an interesting possibility. If a municipality wants to annex a strip of property, but because of an uncooperative landowner cannot annex it directly into its city boundary, the municipality can acquire ownership of a piece of land on the other side of the uncooperative landowner that is contiguous and adjacent to the desired piece of land. Once the municipality owns that piece of land, it uses the power in § 43.051 to annex that owned piece of land. Assuming the municipality is still within its ETJ, it now meets the default requirements to annex land.[38] The annexed chunk of land is part of the municipal boundaries, and it is within the ETJ. That newly-created contiguity allows the municipality to annex the desired piece of land without having to deal with the uncooperative landowner that initially blocked the municipality. The various rules of annexation have been added piecemeal over the years, and an attorney looking to find creative solutions should look for those overlaps of different provisions of the code.

Select Issue: Nonannexation Development Agreement for Ag-Exempt Landowners

Section 43.035 of the TLGC seems relatively innocuous, but is the seed from which endless frustration has risen.[39] The statute requires municipalities to offer a development agreement to landowners who use their land as, and has been appraised as, an agricultural, wildlife management, or timber land (an ag-exempt property).[40] A development agreement is an agreement between the municipality and landowner that specifies how a given piece of land may or may not be developed during a specified time.[41] The development agreement must allow the landowner to maintain its extraterritorial status, but would be subject to regulations not interfering with the ag-exempt use.[42] The

[33] *Id*. § 43.141(c).

[34] *Id*. § 43.141(a).

[35] *Id*. § 43.143.

[36] *Id*. § 43.051.

[37] *Id.*

[38] *See generally id.*

[39] *Id*. § 43.035.

[40] *Id.*

[41] *Id*. § 212.172.

[42] *Id*. § 43.035.

statute also allows area contiguous with land subject to the development agreement to be considered contiguous to the municipality for the purposes of future annexation.[43]

However, this does not mean that landowners can stonewall municipalities from annexing them by forcing these development agreements. The statute only requires that the development agreement be offered; if the landowner declines, the landowner is then subject to annexation.[44] Moreover, there is nothing in the statute that states what *cannot* be put in the agreement.[45] This presents the opportunity for what are known as "poison pill" provisions, similar to poison pills found in the legislative process. By adding in a provision so onerous to a landowner, a municipality can effectively guarantee the denial of the development agreement. There further has not been any determination that the development agreement must be drafted and offered in good faith. A conceivable limitation to a municipality's choosing to use poison pill provisions is the risk of raising the ire of interested and influential agricultural interests that may move the legislature to give the statute more bite, but that point has not been reached yet.

Conclusion

Ultimately, it remains to be seen what annexation and ETJ law will do over the coming decades, but as Texas continues to grow in population, annexations will continue to be a growing area of opportunity for attorneys to capitalize on. With a firm foundation to build off of, understanding and working in ETJs can be another tool in an attorney's toolkit. For further learning, the Texas Municipal League is an invaluable source of knowledge and should be consulted at https://www.tml.org/.

[43] *Id*. § 43.035(c).

[44] *Id*. § 43.035(b)(2).

[45] *See generally id.*

NOT GETTING MARRIED TODAY: AN OVERVIEW OF COMMON LAW MARRIAGE

Lisa Hoge
Texas Tech University School of Law
Lubbock, Texas
lnhoge@gmail.com

REPTL
REAL ESTATE, PROBATE & TRUST LAW
SECTION OF THE STATE BAR OF TEXAS

STUDENT WRITING CONTEST

Honorable Mention – Probate 2016

I. Introduction

Society tends to judge couples that choose to remain unmarried, even if they have sensible reasons for not formalizing their relationship.[1] However, their desire to avoid a formal marriage does not prevent them from becoming—intentionally or not—common-law married in certain states.[2] An estate planning or family law attorney should be aware of the laws regarding common-law marriage and the potential ramifications for a client.

The story of rapper Iggy Azalea illustrates how a person can be unaware of a common-law marriage and need legal advice.[3] Her former boyfriend, Maurice Williams, filed for divorce claiming that the couple was common-law married under Texas law.[4] He claims they lived together for a time and held themselves out as a married couple.[5] She denies these claims and says that Mr. Williams is seeking to turn a six-month relationship into an easy payday.[6]

This article hopes to help attorneys plan a defense for a client like Ms. Azalea by providing an overview of the history of common-law marriage and discussing the current state of the law within the United States.[7] It will also discuss the benefits of marriage, with a particular focus on the financial

---

[1] *See* Bella DePaulo, *Top 8 Reasons Not to Marry*, PSYCHOL. TODAY (Nov. 19, 2013).

[2] *See infra* Part III.A.

[3] *See Iggy Azalea Has Never Been Married but Ex Boyfriend Wants a "Divorce"*, SAN DIEGO DIVORCE ATT'Y BLOG (Nov. 3, 2014).

[4] *Id.*

[5] *Id.*

[6] *Id.*

[7] *See infra* Parts II-IIIA.

aspects.[8] Finally, this article will conclude with a discussion of the Social Security Administration's requirements for proving a common-law marriage, emphasizing how they place a burden on both applicants and employees.[9]

II. Historical Overview

While the concept of common-law marriage likely dates back much further, informal marriages have existed since at least the sixteenth century.[10] The *Decretum de Reformatione Martrimonni* supports this claim.[11] The Council of Trent passed this decree on November 11, 1563.[12] It dealt a serious blow to informal marriages in Italy by declaring that a priest and at least two other witnesses were required to be present at a valid marriage ceremony.[13]

The law in England during that same time period was much more liberal about common-law marriages.[14] It allowed a marriage to be formed merely through word of assent.[15] This was known as entering into a marriage contact "per verba de praesenti."[16]

Scotland was even more lax on marriage formalities.[17] Many young English couples eloped across the border to escape disapproving parents.[18] In fact, parental consent was not required for those below twenty-one, and girls as young as twelve could legally marry.[19] The minimum age for boys was fourteen until it jumped to sixteen in 1929.[20]

The United States began enacting marriage laws on a state-by-state basis as early as 1639.[21] In Massachusetts, men were required to present a marriage certificate to the proper authorities for recording.[22] The law was later taken a step further with a requirement that all marriages take place before a magistrate or other authorized person.[23] This essentially abolished the possibility of being common-law married in Massachusetts.[24]

New York took a more liberal approach than Massachusetts. In 1809, a New York court upheld a

---

[8] *See infra* Part IV.

[9] *See infra* Parts V.

[10] Jennifer Thomas, *Common Law Marriage*, 22 J. AM. ACAD. MATRIM. LAW 151, 154 (2009).

[11] *Id.*

[12] *Id.*

[13] *Id.*

[14] *Id.*

[15] *Id.*

[16] *Id.*

[17] *Scottish Way of Birth and Death*, U. OF GLASGOW (last visited Oct. 19, 2015).

[18] *Id.*

[19] *Id.*

[20] *Id.*

[21] Commonwealth v. Munson, 127 Mass. 459, 461 (1879).

[22] *Id.*

[23] *Id.*

[24] *See id.*

marriage based on words of assent.[25] This is likely because New York based their laws on the English common law, which had long recognized common-law marriage.[26] It was not the only state to base its approval of common-law marriage on the English common law, as Texas would later use similar reasoning.[27]

Texas actually adopted the English common law after England abolished common-law marriage.[28] However, case law later clarified that Texas had adopted an older United States version of English common law that still recognized common-law marriage.[29] This allowed Texas to justify upholding the tradition of common law marriage.[30]

The United States Supreme Court upheld the continuation of common-law marriage in 1877.[31] They declared that marriage is a common right.[32] The only way a state can abolish common-law marriage is by specifically indicating so through legislation.[33] A later section will discuss the statutes of those states that still allow common-law marriage.[34]

Between 1875 and 1917, many states abolished common-law marriage for a variety of social reasons.[35] Ten more states would follow between 1921 and 1959.[36] Some of these reasons included fear of interracial marriages, concern with fraudulent claims, and a perceived threat to the institution of marriage.[37]

Only four states have abolished common-law marriage since 1959.[38] This seems to indicate that those social concerns became less importance as society changed. Common-law marriage has actually survived two semi-recent attempts to abolish it in Texas.[39] This brings us to a discussion of the current state of common-law marriage in modern-day America.[40]

III. Current State of the Law

A. The Law

---

[25] Fenton v. Reed, 4 Johns. 52 (N.Y. Ch. 1809).

[26] Cynthia Grant Bowman, *A Feminist Proposal to Bring Back Common Law Marriage*, 75 OR. L. REV. 709, 720 (1996).

[27] MICHAEL ARIENS, LONE STAR LAW 157 (2011).

[28] *Id.*

[29] *Id.*

[30] *Id.*

[31] Meister v. Moore, 96 U.S. 76 (1877).

[32] *Id.* at 81.

[33] *In re* McLaughlin's Estate, 30 P. 651, 654 (Wash. 1892).

[34] *See infra* Part III.A.

[35] *See* Bowman, *supra* note 26, at 731-32.

[36] *Id.* at 740.

[37] *Id.*

[38] *Id.*

[39] *See* ARIENS, *supra* note 27, at 157-58.

[40] *See infra* Part III.A.

There are currently thirteen states with statues regarding common-law marriage.[41] Five of those states will only recognize a common-law marriage if it was entered into prior to a certain date. [42] That date will vary between the states.[43] Because of that severe restriction, those five states (Pennsylvania, Ohio, Indiana, Georgia, and Florida) are considered to have abolished common-law marriage for all practical purposes.[44]

Colorado has taken the opposite approach.[45] Rather than only recognizing common-law marriages entered into before a certain date, Colorado only recognizes common-law marriages entered into after September 1, 2006.[46] Both parties must be at least eighteen at the time of marriage, and no other law may prohibit the marriage.[47] Those requirements apply even if the common-law marriage was entered into outside of Colorado.[48]

Other states besides Colorado have statutes actively allowing common-law marriage.[49] New Hampshire and Texas are good examples of how a typical common-law marriage statute is written.[50] The New Hampshire statute states that "[p]ersons cohabiting and acknowledging each other as husband and wife, and generally reputed to be such, for the period of 3 years, and until the decease of one of them, shall thereafter be deemed to have been legally married."[51]

The Texas statute requires either a signed declaration of marriage or mutual agreement, co-habitation, and representing oneself as married.[52] The Texas Supreme Court upheld these requirements in 2013.[53]

Utah has a statute nearly identical to the Texas one.[54] The most significant difference is that Utah does not allow a common-law marriage to be formed by signing a declaration of marriage.[55] The other notable difference is that Utah allows a common-law marriage to be established up to one year after the termination of the relationship.[56] Iowa, Kansas, Montana, and South Carolina are the only other states that still actively allow common-law marriage, at least under certain circumstances.[57]

---

[41] *Common Law Marriage By State*, NATI'L CONF. OF ST. LEGIS (Aug. 4, 2014).

[42] *Id.*

[43] *Id.*

[44] *Id.*

[45] COLO. REV. STAT. ANN. § 14-2-109.5 (West 2015).

[46] *Id.*

[47] *Id.*

[48] *Id.*

[49] *Id.*

[50] N.H. REV. STAT. ANN. § 457:39 (2015); TEX. FAM. CODE ANN. § 2.401 (West 2015).

[51] N.H. REV. STAT. ANN. § 457:39 (2015).

[52] TEX. FAM. CODE ANN. § 2.401(a)(1)-(2).

[53] Grigsby v. Reib, 105 Tex. 597 (1913); *See* ARIENS, *supra* note 27.

[54] UTAH CODE ANN. § 30-1-4.5 (West 2015).

[55] *Id.*

[56] *Id.*

[57] *Common Law Marriage By State*, *supra* note 41.

Statutes are not the only way for a state to recognize common-law marriage.[58] Some states have common-law marriage as part of their case law.[59] Rhode Island and Alabama are prime examples of this approach.[60]

The leading case on common-law marriage in Rhode Island is *Demelo v. Zompa*.[61] This case holds that a couple must have "seriously intended to enter into the husband-wife relationship."[62] Additionally, their conduct must have been "of such a character as to lead to a belief in the community that they were married."[63] These two requirements can be proven by "inference from cohabitation, declarations, reputation among kindred and friends, and other competent circumstantial evidence."[64]

Alabama law can also be easily summarized.[65] Alabama requires proof of "(1) capacity; (2) present, mutual agreement to permanently enter the marriage relationship to the exclusion of all other relationships; and (3) public recognition of the relationship as a marriage and public assumption of marital duties and cohabitation" to show a common-law marriage.[66]

Oklahoma actually has contradictory law regarding common law marriage.[67] It has a statute requiring a formal marriage license, which would seem to bar common-law marriage.[68] However, common-law marriage has been upheld in the Oklahoma courts on more than one occasion.[69] It remains to be seen if and how the state intends to clarify this discrepancy. [70] In the meantime, an Oklahoma lawyer might face confusion arguing a common-law marriage case, which provides an excellent segue into our next topic.[71]

B. How to Argue for Your Client

The best place to start when faced with a common-law law marriage issue is to gather clear and convincing evidence that the couple were or were not common-law married.[72] Courts have been known to recognize many different things as evidence of a common-law marriage.[73] This might include financial documents, use of a common last name, insurance policies, and testimony from third parties.[74]

---

[58] *Id.*

[59] *Id.*

[60] *Id.*

[61] Demelo v. Zompa, 844 A.2d 174 (R.I. 2004).

[62] *Id.*

[63] *Id.*

[64] *Id.*

[65] Gray v. Bush, 835 So. 2d 192 (Ala. Civ. App. 2001).

[66] *Id.* at 194.

[67] *Common Law Marriage By State*, *supra* note 41.

[68] OKLA. STAT. ANN. TIT. 43, § 43-4 (West 2015).

[69] *Common Law Marriage By State*, *supra* note 41.

[70] *See id.*

[71] *See infra* Part III.B.

[72] David Tracy, *Common Law Marriage in Oklahoma*, DIVORCENET (last visited Oct. 22, 2015).

[73] *Id.*

[74] *Id.*

There are three common ways to repute a common-law marriage.[75] The first is to offer evidence that an element of the common-law marriage statute for the state where the marriage was formed was not met.[76] Alternatively, an attorney could produce proof that one or both of the parties was not legally competent at the time of the marriage.[77] Some possible reasons for incompetence include being insane or underage.[78] Finally, the third possible defense is to allege that one or both parties were already married at the time of the marriage.[79]

Courts have a preference towards marriage and view cohabitation and reputation within the community as particularly persuasive evidence.[80] Because of this preference towards marriage, common-law marriages continue to be recognized even if the couple moves to a state where common-law marriage is abolished.[81] This means that attorneys in all states need to consider whether their client may be common-law married.[82] The attorney also needs to make sure that a client who is common-law married understands the need for formal divorce should the couple ever split.[83] Finally, all attorneys should be aware of what marital benefits their client may be entitled to, which is our next topic of discussion.[84]

IV. Marital Benefits

Common-law spouses enjoy the same financial benefits as a traditionally-married couple.[85] These include employment benefits, tax exemptions, ability to both claim tax deductions for mortgage interest and children, and eligibility for Social Security benefits.[86]

Employment benefits are an important advantage of being married as many people receive health insurance through their spouse's employer.[87] Employers who offer spousal benefits generally extend this benefit to common-law spouses.[88] Additionally, any children from the relationship can be added to the insurance plan as dependents.[89]

Some insurance companies or employers may require a signed affidavit before adding a common-

---

[75] Adam Kielich, *Do I Need a Divorce for my Common Law Marriage in Texas?*, THE KIELICH L. FIRM (Jan. 14, 2015).

[76] *Id.*

[77] *Id.*

[78] *Id.*

[79] *Id.*

[80] *In re* Benjamin, 34 N.Y.2d 27 (1974).

[81] *Common Law Marriage*, NAT'L PARALEGAL C. (last visited Oct. 26, 2015).

[82] *See id.*

[83] *Id.*

[84] *See infra* Part IV.

[85] Katie Adams, *Marriage vs. Common Law: What It Means Financially*, INVESTOPEDIA (Feb. 15, 2010).

[86] *Id.*

[87] *See Health Care Benefits: Common Law Marriage: How Does Common Law Marriage Affect Health Insurance?*, SOCIETY FOR HUM. RESOURCE MGMT. (Mar. 25, 2015).

[88] *Id.*

[89] *Id.*

law spouse to an insurance plan.[90] Others may require evidence of the marriage.[91] Once again, this evidence may include things like a joint tax return, a joint mortgage, or any other paperwork where the couple holds themselves out as a marital unit.[92]

Common-law married couples are also entitled to certain tax benefits.[93] Arguably, the most important of these is the marital exemption from the gift tax.[94] This states that an individual may transfer property to the individual's spouse as a gift and then deduct that amount from the individual's total taxable gifts.[95] The biggest caveat is that the receiving spouse must be a citizen of the United States to claim this deduction.[96]

One of the other major tax benefits of marriage is the increased estate tax exemption.[97] If a person dies with an estate valued over a certain amount, the person's heirs are required to pay taxes at a high rate on the excess amount.[98] However, married couples are allowed a much larger estate before the estate tax kicks in.[99] In 2015, an estate tax was owed on any estate of more than $5.43 million (if single) or $10.86 million (if married).[100] The applicable tax rate was 40%.[101] As you can see, marriage greatly benefited any couple with an estate in the $5-10 million range.[102]

The last major tax benefit of marriage involves deductions for children and for mortgage interest.[103] A hypothetical is helpful to explain the child deduction. An unmarried couple lives together and has two children.[104] One wishes to claim the standard child deduction on his/her taxes, while the other wishes to use the child to claim the Earned Income Tax Credit (EITC) on his/her taxes.[105] Who gets to claim the children?

The answer is that only one parent gets to claim a specific child.[106] So, either one parent claims both children, or each parent claims one child in this scenario.[107] If both parents attempt to claim the

---

[90] *Id.*

[91] *Id.*

[92] *Id.*

[93] *Publication 17 (2014)*, INTERNAL REVENUE SERVICE (last visited Oct. 26, 2015).

[94] I.R.C. § 2523 (West 2015).

[95] *Id.*

[96] *Id.*

[97] *Gift Tax and Estate Tax*, EFILE.COM (last visited Oct. 26, 2015).

[98] *Id.*

[99] *Id.*

[100] *Id.*

[101] *Id.*

[102] *See id.*

[103] *See supra* Part IV.

[104] *Qualifying Child of More Than One Person, AGI and Tiebreaker Rules*, EARNED INCOME TAX CREDIT (last visited Oct. 27, 2015).

[105] *Id.*

[106] *Id.*

[107] *Id.*

same child, there is a tiebreaker rule that the IRS can apply.[108] Assuming that the child lived with each parent equally throughout the year, the parent with the higher adjusted gross income (AGI) is allowed to claim the child.[109] Needless to say, marriage would solve this messy situation by allowing the couple to file together and jointly benefit from all possible deductions and credits from both children.[110]

We finally come to the mortgage interest deduction.[111] Mortgage interest can be deducted from the homeowner's taxes under certain conditions.[112] As you will see below, there are distinct advantages to being married when it comes to mortgage interest deduction.[113]

Interest on a mortgage taken out to buy, build, or improve your home after October 13, 1987, may be fully deducted only if the total debt from all mortgages, including any grandfathered debt, amounts to $1 million or less for married couples and $500,000 or less for singles or married couples filing separately.[114]

Mortgages taken out after October 13, 1987, for reasons other than to buy, build, or improve your home must total $100,000 or less for married couples and $50,000 or less for singles or married couples filing separately. They must also total less than the fair market value of your house minus the value of all grandfathered debt and all post-October 13, 1987 mortgage debt.[115]

Now, it is time to discuss one of the most well-known marital benefits—Social Security.[116] "A married person can collect retirement benefits based on his or her own earning from work, or an amount equal to 50 percent of the other spouse's retired worker benefit—whichever is the higher amount."[117] Two examples are helpful to illustrate that concept.[118]

"Mrs. Williams will get a retirement benefit of $1,200 a month based on her work record. Mr. Williams is entitled to a retirement benefit of $500 a month based on his own work history. He will receive his own $500, plus an additional $100, to bring his total to $600 a month, based on 50 percent of Mrs. Williams' benefit. Total family benefits for the Williams household will be $1,800 a month."[119]

"Mrs. Rodriguez is entitled to a retirement benefit of $1,100 a month based on her work history. Her husband will get a benefit of $1,400, which would provide a spousal benefit of $700. Mrs. Rodriguez receives her own benefit of $1,100 a month, because that is the larger of the two amounts. Total family retirement benefits: $2,500 a month."[120]

---

[108] *Id.*

[109] *Id.*

[110] *Eight Facts about Filing Status*, IRS (Jan. 13, 2011).

[111] *See supra* Part IV.

[112] James E. McWhinney, *Tax Deductions on Mortgage Interest*, INVESTOPEDIA (Feb. 08, 2006).

[113] *Id.*

[114] *Id.*

[115] *Id.*

[116] *See supra* Part IV.

[117] Social Security, Marriage, and Divorce, NAT'L ACAD. OF SOC. INS. (last visited Oct. 27, 2015).

[118] *Id.*

[119] *Id.*

[120] *Id.*

As you can see, Social Security greatly favors married couples.[121] However, the Social Security Administration wants to be sure that couples are truly legally married, and has enacted regulations to help determine that.[122] This brings us to a discussion of the Social Security Administration's burdensome requirements to prove a common-law marriage.[123]

V. Social Security Requirements

The Social Security Administration (SSA) makes it easy to prove a traditional ceremonial marriage.[124] A ceremonial marriage may be proven by a "certified copy of the public record of the marriage; . . . [a] certified copy of the religious record of the marriage; or . . . [t]he original marriage certificate."[125] Nearly all couples will be able to produce one of those documents.

If the couple is unable to produce one of those documents, a signed statement from the officiant who performed the wedding or "[o]ther evidence of investigative value" may suffice.[126] That type of evidence may include things like photographs, newspaper announcements, or witness statements.[127]

In contrast, a common-law marriage is difficult to prove.[128] Let us begin by looking at just part of the actual regulations.[129]

"Evidence to prove a common-law marriage in the States that recognize such marriages must include: . . . [i]f the husband and wife are living, a statement from each and a statement from a blood relative of each; . . . [i]f either the husband or wife is dead, a statement from the surviving widow or widower and statements from two blood relatives of the decedent; or . . . [i]f both a husband and wife are dead, a statement from a blood relative of the husband and from a blood relative of the wife."[130]

This is obviously a complicated process, but it gets even more involved when you read the specifics in more detail.[131] The regulations go on to state that each spouse must submit a Statement of Marital Relationship and that, if the husband and wife are still living, a blood relative from each side must submit a Statement Regarding Marriage.[132]

The Statement of Marital Relationship form is a four-page document.[133] While most of the form is yes or no questions, the majority of yes responses require further explanation.[134] This form is required

---

[121] *See id.*

[122] *See infra* Part V.

[123] *See infra* Part V.

[124] *Evidence of Ceremonial Marriage*, SOC. SEC. HANDBOOK (last visited Oct. 27, 2015).

[125] *Id.*

[126] *Id.*

[127] *Id.*

[128] *See id*.

[129] *Id.*

[130] *Id.*

[131] *Development of Common-Law (Non-Ceremonial) Marriages*, SOC. SEC. PROGRAM OPERATIONS MANUAL SYS. (Oct. 13, 2013).

[132] *Id.*

[133] *Statement of Marital Relationship*, SOC. SEC. ADMIN. (Jul. 2015).

[134] *Id.*

of both spouses, despite the fact that their answers will be (nearly) identical.[135]

Meanwhile, there is also the Statement Regarding Marriage.[136] This is required of one blood relative on each side.[137] What makes this form potentially complicated is the whole blood relative issue. There are dozens of reasons why a person might not have blood relatives, and the SSA specifically states that a relationship by marriage or adoption is insufficient.[138] There is no explanation of why a blood relative's testimony is perceived as more reliable than testimony from a nonblood relative or friend.[139]

The SSA did anticipate that a couple might have issues accessing blood relatives and does have an alternative process.[140] If a couple does not have enough blood relatives to fulfill the requirements, they may have another person who knows them well fill out the paperwork.[141] However, they must submit additional paperwork explaining why they were unable to use a blood relative.[142]

The process is further complicated when a couple is unable to obtain a Statement Regarding Marriage from anyone at all.[143] The SSA does provide its employees with instructions on how to handle this situation when both spouses are still living, although it notes that very few circumstances will justify using alternative procedures, and the couple will have to provide documentation about their unique circumstances.[144]

To wrap up this section, the following instructions show exactly what is expected of an employee faced with the task of proving a common-law marriage.[145]

"Develop each form independently of the others. Answer all items on each form fully but concisely and in the person's own words. Clarify all ambiguous answers and reconcile all conflicts. Explain any ambiguous answers on a report of contact form or Report of Contact (RPOC) screen. Get a supplemental statement over the person's signature, as needed. Obtain corroborating evidence (e.g., mortgage or rent receipts, insurance policies, medical records, bank records) to substantiate the fact that the couple considered and held themselves out as husband and wife."[146]

This list does not even include how to handle complex issues such as common-law marriages established outside of the United States.[147] The SSA has provided its employees with separate instructions on how to handle those complex situations, but they are beyond the scope of this article.[148] However, they do help illustrate the challenges that SSA employees face when handling a common-law

[135] *Development of Common Law (Non Ceremonial) Marriages*, *supra* note 131.

[136] *Id.*

[137] *Id.*

[138] *Id.*

[139] *Id.*

[140] I*d.*

[141] *Id.*

[142] *Id.*

[143] *Id.*

[144] *Id.*

[145] *Id.*

[146] *Id.*

[147] *Id.*

[148] *Id.*

marriage case.[149]

VI. Conclusion

Common-law marriage is a complex issue that can vary greatly from state to state.[150] It is important for couples to understand the benefits they may be entitled to as a common-law married couple.[151] However, some of the benefits may be challenging to receive, and Social Security is by far most difficult.[152]

It is time for the SSA to reevaluate its guidelines. It should begin by allowing nonblood relatives to provide evidence of a common-law marriage.[153] If it is unwilling to take that step, the SSA should at least adequately and publicly explain its rationale behind this policy.

The SSA should also reconsider why both parties are required to fill out the Statement of Marital Relationship form.[154] There seems no benefit to this, as couples will likely fill out their forms together. This greatly reduces the chances that conflicting answers will expose some lie, which is likely the SSA's rationale behind this policy.

In conclusion, a common-law marriage may be right for many couples. However, these couples need to fully understand several things: what it takes to form a common-law marriage, what it takes to end a common-law marriage, and the potential difficulties behind proving such a marriage.[155] It is the job of a good attorney to properly educate these couples and make sure they are prepared for the future in every way possible.

[149] *See supra* Part V.

[150] *See supra* Part III.A.

[151] *See supra* Part IV.

[152] *See supra* Part V.

[153] *See supra* Part V.

[154] *See supra* Part V.

[155] *See supra* Parts III-IV.