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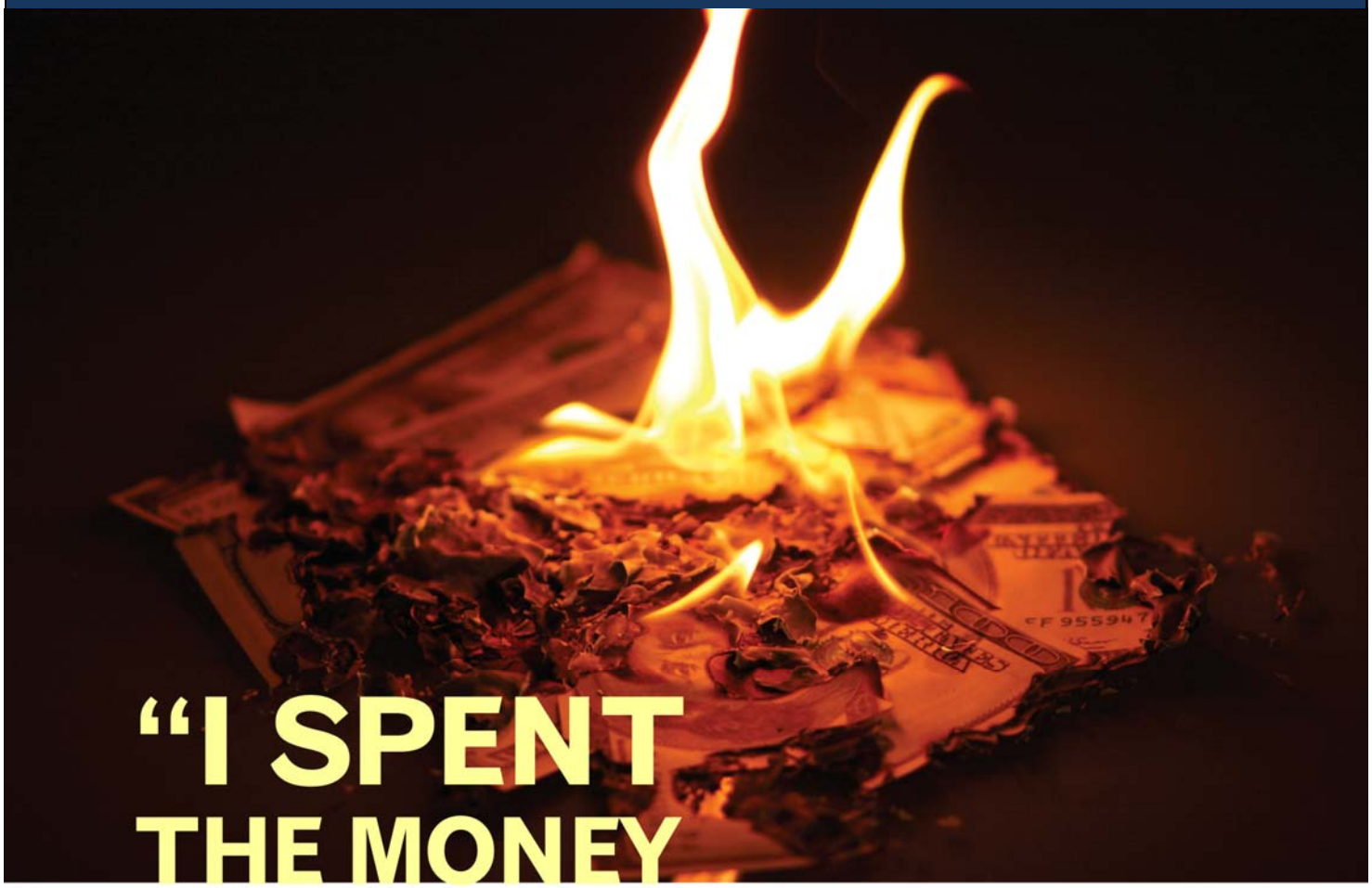
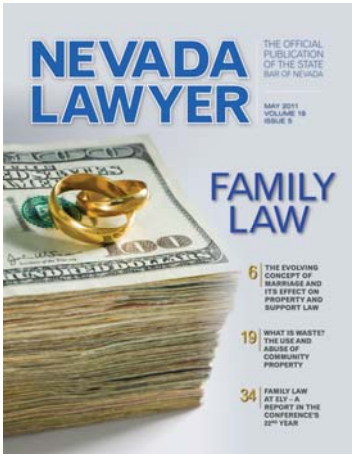


"I SPENT THE MONEY ON WHISKEY, WOMEN AND GAMBLING; THE REST, I WASTED.[1]"



Expanded version of an article that originally appeared in the May 2011 issue of *Nevada Lawyer* magazine.

By Gary R. Silverman, Esq.

The bench and bar classically think of waste as the diamond bracelet and sable coat for a girlfriend, high rise apartment for a mistress, "allowance" for the pool boy or hidden account on the Isle of Wight. Those and other uses of community funds are the subject of this article.

This article discusses what may constitute waste, the potential of unequal division, general or punitive damages, and how the case law and NRCP 16.2 deal with the issue. The sanctions set forth in *Lofgren* and *Putterman*, *infra*, and under NRS 125.150 may be superceded by NRCP 16.2, but still help in analysis of a waste case.

What is Waste?

First, a definition of terms. Lawyers often speak of "waste." Our Supreme Court in its two most recent decisions on the topic speaks of "compelling reasons" to make an unequal division of community property pursuant to NRS 125.150. In those decisions the court also uses the term "waste." Submitted: the terms mean the same; community property spent, conveyed, hidden or otherwise converted by a spouse that, *inter alia*, compels the court in justice and equity to reinstate the property to the community balance sheet and then divide such property as the facts compel.

This article is *not* about sanctions for violation of interim court orders – that is a contempt/sanction issue (though such sanctions are intermingled with the notion of waste in the existing case law and NRCP 16.2). It is *not* about the minefield of seizures, forfeitures and restitution proceedings, even though the subject of those actions is often waste, e.g., a foreign bank account or drug money.[2]

The Remedies for Waste Generally Appear in NRS 125.150(1)(b) and NRCP 16.2

NRS 125.150 provides:

> In granting a divorce, the court...(b) Shall, to the extent practicable, make an equal disposition of the community property of the parties, except that the court may make an

> unequal disposition of the community property in such proportions as it deems just if the court *finds a compelling reason to do so and sets forth in writing the reasons* for making the unequal disposition. [Emphasis added.]

The statute does not set forth any reasons for an unequal division, thus the substantive rules setting out the *rights* under which an unequal division might be ordered lie elsewhere.

NRCP 16.2(A)(1)(B)states:

> If a party intentionally fails to include a material asset or liability in the party's financial disclosure form, the court, after notice and hearing, may impose an appropriate sanction, including but not limited to the following:
>
> (i) An order awarding the omitted asset to the opposing party as his or her separate property or making another form of unequal division of community property;
>
> (ii) An order treating the party's failure as a contempt of court; or
>
> (iii) An order requiring the party failing to make the disclosure to pay the other party's or opposing party's reasonable expenses, including attorney's fees and costs, related to the omitted items.

The hypothesis of this article is that the fiduciary relationship is the source of the *right under which an unequal division might be ordered.*

Spouses are in a fiduciary relationship. NRS 123.070 provides:

> Either husband or wife may enter into any contract, engagement or transaction with the other, or with any other person respecting property, which either might enter into if unmarried, subject in any contract, engagement or transaction between themselves, *to the general rules which control the actions of persons occupying relations of confidence and trust* toward each other. [Emphasis added.]

Also, *Sogg v. Sogg*, 108 Nev. 308, 312 (1992) (even affianced parties are in a presumed fiduciary relationship).

What Kind of Fiduciary Relationship do Spouses Enjoy?

A fiduciary relationship is a fiduciary relationship is a fiduciary relationship, but the *kind* of fiduciary relationship between spouses is that of partners. The law's model for marriage is the partnership model: "It is generally recognized that the marital community is a *partnership* to which both parties contribute. Each spouse contributes his or her industry in order to further the goals of the marriage" (*York v. York*, 102 Nev. 179, 180 (1986)).

Case law reinforces the notion of a fiduciary relationship. Relations of trust and confidence are defined in *Crawford v. Crawford*, 24 Nev. 410 (1899) at p. 417, et. seq.,[3] and *Peardon v. Peardon*, 65 Nev. 717, 767, 201 P.2d 309, 333 (1948). The cases hold that the doctrine of undue influence "reaches every case, and grants relief 'where influence is acquired and abused, or where confidence is reposed'" (*Crawford, supra)*. Absent, perhaps, a prenuptial agreement to the contrary, marriage is such a relationship.[4]

What, exactly, *are* fiduciary duties?

The rules of intra-partnership duties are set out in *Clark v. Lubritz*, 113 Nev. 1089, 944 P.2d 861 (1997)at p. 1095:

> The fiduciary duty among partners is generally one of *full and frank disclosure* of all relevant information for *just, equitable and open dealings at full value and consideration.* Each partner has a *right to know all that the others know*, and each is required to make *full disclosure of all material facts* within his knowledge in anything relating to the partnership affairs. The requirement of full disclosure among partners in partnership business cannot be escaped...Each partner must . . . *not deceive another partner by concealment* of *material* facts. [Emphasis added.]

The *Lubritz* court went on to say: "In addition, *a partner's motives or intent do not determine whether his actions violate his fiduciary duty*...Despite the contractual source of partners' duties inter se, ... it is well established that when a fiduciary duty exists between the parties, and the conduct complained of constitutes a breach of that duty, the claim sounds in tort regardless of the contractual underpinnings. Id. at 1284 n.24 (quoting *Wagman v. Lee*, 457 A.2d 401, 404 (D.C. 1983))" (*Lubritz*, p. 1098). [Emphasis added.]

Under *Putterman* and *Lofgren, infra*, a spouse has a fiduciary duty to account for all community funds. In a case regarding law partners, *Foley v. Morse & Mowbray*,109 Nev. 116, 121 (1993) the court said:

> Foley claims that the court erred when it awarded Morse & Mowbray an interest in three contingency fee cases identified as Father Kenny, Lawyer Johnson, and Cynthia Gifford. In a similar case concerning a law firm dissolution, the California Court of Appeals ruled that every partner must account to the partnership for any benefit and hold as trustee for it any profits derived without the consent of the other partners from any transaction of the partnership or from any use of its property. *Rosenfeld, Meyer & Susman v. Cohen*, 237 Cal.Rptr. 14, 22-23 (Ct.App. 1987).

In *Lofgren*, the court spoke of *intentional* behavior ("...we hold that if community property is lost, expended or destroyed through the intentional misconduct of one spouse, the court may consider such misconduct as a compelling reason..." (at p. 1283).

In *Putterman*, the court spoke of *negligent* behavior ("There are, of course, other possible compelling reasons, such as negligent loss or destruction of community property...", *Putterman* at p. 608.) The duties of a fiduciary apparently include the duty of care.

The question as to what constitutes negligence as between fiduciaries is not clear. Do persons in a fiduciary relationship suffer greater damages if they are negligent with community property? Is there a higher duty than that owed to strangers? Does accidently losing a material sum of community property create a punitive damage claim? Seemingly not under NRS 42.001.

The partnership model should not be exclusive. There is also guardian and ward, and parent and child, e.g., *In Re Tiffany Living Trust 2001*, 124 Nev. Adv. Rep. 8 177 P3d 1060, (2008). As stated, a fiduciary relationship is a fiduciary relationship is a fiduciary relationship.

Burden of Proof: Which Party and What Quantum?

In a fiduciary relationship, the party who gains an advantage over the other must justify that result by clear and convincing evidence, *In re Tiffany Living Trust 2001*, 124 Nev. Adv. Op. ____(2008):

> A presumption of undue influence arises when a fiduciary relationship exists and the fiduciary benefits from the questioned transaction. A fiduciary relationship between Dabney and Jane existed in this case because Dabney's law firm partner Woloson, had prepared Jane's living trust, which benefited Dabney in that he was the beneficiary of Jane's house. Thus, when Dabney substantially benefited from Jane's estate plan, a presumption of undue influence arose.
>
> We have previously noted, in the context of an attorney obtaining a business advantage from a client, that a presumption of impropriety may be overcome only by clear and satisfactory evidence. As it appears that this court has never precisely defined "clear and satisfactory" evidence, we clarify that "clear and satisfactory" evidence is equivalent to "clear and convincing" evidence. Indeed, in *In re Drakulich*, we recognized that clear and convincing evidence must produce "satisfactory" proof that is so strong and cogent as to satisfy the mind and conscience of a common man, and so to convince him that he would venture to act upon that conviction in matters of the highest concern and importance to his own interest. It need not possess such a degree of force as to be irresistible, but there must be evidence of tangible facts from which a legitimate inference . . . may be drawn. Thus, regardless of the terminology used—whether "clear and satisfactory" or "clear and convincing"—as the Tennessee Court of Appeals has noted, "the evidence must eliminate any serious or substantial doubt about the correctness of the conclusions to be drawn from the evidence."
>
> Only this heightened standard can overcome the presumption of undue influence because "[u]nder our case law, when an attorney deals with a client for the former's benefit, the attorney must demonstrate by a higher standard of clear and satisfactory evidence that the transaction was fundamentally fair and free of professional overreaching." This higher standard ensures that the law will protect those who cannot protect themselves. [Fn. omitted.]

In the *Foley* case, *supra*, the court spoke to the burden of proof as follows:

> The court stated that failure to account properly was a burden of proof that rested with the fiduciary who had contravened duties enabling allocation and accounting. *Id.* at 23. Foley, who was in a position to make the allocation, failed to do so. "The most elementary conceptions of justice and public policy require that the wrongdoer shall bear the risk of the uncertainty which his own wrong has created." *Bigelow v. RKO Radio Pictures*, 327 U.S. 251, 265 (1946). Since Foley failed to bear his burden to account, we conclude that the trial court's rulings in favor of Morse & Mowbray with respect to the three contingency fee cases were not erroneous.

Defenses

The usual defenses of contributory negligence, waiver, accord and satisfaction and ratification seem to hold. The issues of statute of limitations and, laches are discussed below. But, at least one defense seems particular to divorce cases:

materiality.

The case for the defense of materiality is *Nixon v. Brown*, 46 Nev. 439 (1923). During marriage U.S. Senator George Nixon conveyed to the City of Winnemucca a hall for various performances. "It is admitted that the property conveyed by the deed of trust was community property, not a portion of a homestead; and that the wife never signed or otherwise consented in writing to the conveyance." The value of the hall and parcel was approximately $50,000. The gift was made as part of a ceremony which his wife attended. "Senator Nixons' wealth at the time of making the gift was estimated at between three and five million dollars, and at the time of his death he was admitted to be a millionaire." After the husband's death, the wife sought to set aside the deed on the grounds she had not signed it and had not consented to the gift. The trial court found "the instrument in question [is]…void for failure on the part of the donor to obtain the written consent of his wife."

Held: reversed. "The first question squarely presents the proposition: Can the husband in Nevada, during coverture, make a gift of a portion of the community property without obtaining the written consent of the wife? A gift negatives any idea of a consideration, either nominal or substantial, to the community interest." The applicable statute, Section 2160 of the Revised Laws of Nevada stated "The husband has the entire management and control of the community property, with the like absolute power of disposition thereof…as of his own separate estate.

Beginning with a discussion of the law of the Visigoths, the Nevada Supreme Court went on to reason as follows:

> "…[Husband] may make a voluntary disposition of a portion of the community property, reasonable in reference to the whole amount, in the absence of a fraudulent intent to defeat the wife's claims.
>
> 2. Whether or not the gift is reasonable or unreasonable, is a question to be decided by the courts in each particular instance, and no hard-and-fixed rule can be laid down as to just what proportion of the community interest can be so disposed of by the husband.
>
> 3. …it is admitted that Senator Nixon, at the time of making the gift, was wealthy; that his wealth was estimated as between three and five million dollars; that at the time of his death he was rated as a millionaire. And we have searched the petition in vain to find an allegation on the part of the respondents that the gift was made with the intention of depriving the wife of her just interest in the community property. *We do not believe it is so large in proportion to the whole estate that a fraudulent intent can be in-*

> *ferred, or that it was unreasonable with reference to the value of the entire estate*. And the acts and conduct of respondent Kate I. Nixon negative any thought that she possessed the idea for a minute that Senator Nixon was in any way attempting to deprive her of any portion of her rightful interest in and to the community property; but on the contrary leads us to the conclusion that she was in full accord with the senator's plans, and that she did not for a moment think the gift was unreasonable, considering their financial circumstances, either at the time it was made or at the time of the senator's death. We therefore must conclude that the instrument in question was not and is not void for the reason that Senator Nixon did not procure his wife's consent thereto in writing.

(Note above in the last paragraph that the court implicitly recognizes the defense of ratification or waiver.)

In *Nixon*, above, the court further states: "For the reasons stated above, and, in view of the order to be made in this case, we deem it unnecessary to pass upon the question of laches, equitable estoppel and the statute of limitations urged by appellants, as being a bar to the action." Implicitly the defenses were held to exist.

The question is whether those defenses are tolled during marriage. As to laches, later case law holds the defense is tolled during marriage (*Cord v. Neuhoff*, 94 Nev. 21, 25 (1978)). As to the statute of limitations, the issue has not been decided.[5] The arguments for and against tolling the statute are well known. With abolition of fault and the easy availability of divorce, the viability of the defense is compelling. Tolling of the statute of limitations would also muddle the claims of waiver or ratification. The argument for tolling is highlighted in the hypothetical case where the husband is wasting the community assets gambling. Should the policy of the law be that a mother of three young children must file for divorce sooner rather than later just to save her claim. The public policy of Nevada is to foster marital accord and discourage marital discord: "The policy of the law is to refrain from fostering domestic discord which may follow from litigation between spouses commenced for fear that the bar of laches would attach by lapse of time" (*Cord v. Neuhoff*, 94 Nev. 21, 25 (1978)). The logic of laches would seem to apply to statutes of repose.

The rule that the statute only begins to run when the victim knew or should have known of the tort or violation of trust would not be impaired.[6]

Remedies

Common law remedies for breach of a fiduciary duty are set forth in *Clark v. Lubritz*, supra:

> Despite the contractual source of partners' duties inter se, … it is well established that

> when a fiduciary duty exists between the parties, and the conduct complained of constitutes a breach of that duty, the claim sounds in tort regardless of the contractual underpinnings. Id. at 1284 n.24 (quoting *Wagman v. Lee*, 457 A.2d 401, 404 (D.C. 1983)).
>
> ...
>
> Therefore, we conclude that the breach of fiduciary duty arising from the partnership agreement is a separate tort upon which punitive damages may be based.
>
> ...
>
> Under NRS 42.001(3), "express malice" is "conduct which is intended to injure a person"; "implied malice" is "despicable conduct which is engaged in with a conscious disregard of the rights ... of others.
>
> ...
>
> a conscious decision was made not to inform Lubritz about the decision to reduce Lubritz's share. For many years appellants "pocketed as profit," a disproportionate distribution, by reducing Lubritz's share and not telling him about the reduction. In addition, appellants concede that the decision not to inform Lubritz of the unequal year-end distribution was "not unconscious or accidental.
>
> Even if there were not clear and convincing evidence of intent to injure, there is certainly clear and convincing evidence here of implied malice in the form of "despicable conduct" accompanied by a "conscious disregard of the rights" of Lubritz.
>
> Because there is ample evidence to support a punitive damage judgment based on malice, we do not consider it necessary to discuss fraud or oppression. We therefore affirm the punitive damage award."

Besides common law tort remedies, another remedy exists under NRS 125.150(1)(b) – unequal division. Those remedies are found in the *Lofgren* and *Putterman* cases. In both *Lofgren v. Lofgren*, 112 Nev. 1282 (1996) and *Putterman v. Putterman*, 113 Nev. 606 (1997, an order of the court was violated and in Putterman the husband had apparently lied to the court. Arguably, other sanctions would be available for perjury and contempt of court, but in both cases the spouse also hid or failed to reveal assets or spent community money on things which apparently did not benefit the community.

In *Lofgren*, the effect of the court's decision was *not* an *un*equal division – there was an *equal* division. Community funds spent and gone were placed on the husband's side of the community balance sheet. He had had the use of the now-phantom funds and at trial those funds were set over to him. At the bottom of the balance sheet and ultimately as the net

result of the decision, all community funds were accounted-for and divided equally.

In *Putterman*, the wife was awarded one-half all known community property and a "valuable" country club membership and "certain stock" (not further described) as a "just and equitable" division. It is not clear if the trial court had "evened up" the community with the missing and unaccounted-for funds or awarded the innocent spouse something more. *If* the country club membership and the stock which the court awarded to the wife were indeed more valuable than the missing property then an unequal division occurred. The facts do not clearly reveal if the membership and stock "evened up" the division or somehow exceeded it on the the wife's side and imposed a sort of penalty on the husband.

In both cases the court deemed the restitution of the phantom monies to be a just result. It is submitted that putting back on the balance sheet that which the malefactor had already enjoyed is simply not an unequal division. It is (1) an *equal* division of funds in the case of the party who simply will not account for them: they may well exist in an overseas account or (2) an equal division of a (usually) finite amount which one of the spouses has already enjoyed, i.e., spent on the diamond bracelet, the fur and the object of his affections. It is submitted that if the court does not sanction the malefactor, there is no incentive *not* to try to steal or hide funds or to spend them on the proverbial chorus girl. Only if there is a sanction from the *post*-division property of the malefactor at the least in the form of an award of fees and costs incurred in determining the breach/defalcation, there is no incentive for the guilty party not to try to get away with the wrong. It is submitted that the courts should create a clear disincentive to the potential tortfeasor (thief).

A hard question arises when the tortfeasor comes forth without the aggrieved party incurring costs and fees, and admits to the defalcation. The answer seems to lie in the language of *Clark v. Lubritz, supra.,* that the taking is what is to be the subject of punitive damages. An award of interest, at the least, should be considered.

Another question arises when the defalcation directly and proximately causes such a shortfall in the community that it cannot take advantage of a business opportunity, e.g., because of the breach not enough cash is available for investment in what turns out to be a lucrative stock offering. Or, when the business opportunity is seized by a spouse who uses her separate property to exploit it; interference with an opportunity. The law of business opportunities is outside the scope of this article, but once the fiduciary approach is adopted, the analysis becomes much easier.

Advantages of Analysis as Breach of Fiduciary Duty v. *ad hoc* Cases

Bruce Shapiro's fine article "Community Waste in Nevada" (*Nevada Family Law Report*, Fall 2010) cites to the various cases defining waste and discusses those activities which in Nevada have not yet been defined as waste, e.g., gambling. His provocative article points out the difficulties in the *Putterman* and *Lofgren* cases–they are essentially an *ad hoc* approach. At bottom, lawyers are predictors: They are asked by their clients to foretell how a court will act on a specific set of facts, whether it be an activity covered by the Federal securities laws, the Internal Revenue Code or covered by our more mundane (exalted?) NRS Chapter 125. When a set of facts is dealt with predictably, those facts tend not to become triable issues because both sides reasonably predict the outcome. Thus, a coherent, overarching rule of law that would permit lawyers to predict the outcome of a set of facts will save the courts time and the clients' money.

The range of human behavior in the waste aspects of family law is so vast that a specific description of what may constitute "waste" or "compelling reasons" is impossible to set forth in either a statute or case rule. But the common law of fiduciary relationships is wide and deep, perhaps because, in part, avarice has always been with us. The law of fiduciaries, having "seen it all," provides substantial guidance to the courts and practitioners. While not every form of deceit has yet been conceived, most have, and those schemes have likely all been discovered and litigated. The body of fiduciary law gives counsel the power to say that while he or she may not be able to describe it, they know a breach when they see it and so will their adversary and the court. Creating a rule with substantial case law behind it permits the courts, the lawyers and clients to predict results from a set of facts and thereby avoid litigation the predictive function that the law exalts.

Therefore, it is submitted that in lieu of an *ad hoc*, case-by-case review, the court should adopt an explicit, forthright rule (or the Legislature amend the statute) which provides that all claims for misbehavior under NRS 125.150(1)(b) be examined in light of the fiduciary duties already imposed on spouses under NRS 123.070. The proposed rule might read: *Any material breach of the duty of good faith, fair dealing and disclosure to the community will be deemed "waste" recoverable by the community and to be divided as justice requires under NRS 125.150(1)(b) and NRCP 16.2, but in no less than full reimbursement to the community, including but not limited to interest, consequential damages, punitive damages, interest and costs and fees incurred in such recovery.*[7]

Will this rule create more litigation, especially in the claim for general or punitive damages? Is that what the law should encourage? Will this rule create more litigation, not less? It is submitted this rule now exists in a fragmented form.

The rule is based in existing case law and statutes and fairly restates the current law from the cases (*Putterman* and *Lubritz)*, the statute (NRS 125.150) and the procedural rule (NRCP 16.2). These claims are endemic in family law practice. It is submitted the Court may want to impose on them order and predictability and end uncertainty and disarray.[8]

Our Legislature has made financial fault an element of marriage and hence divorce. The Legislature has told the courts not to introduce marital misconduct into the division of property or alimony, meaning moral misconduct like adultery. Our Supreme Court has heartily endorsed that statutory command, *Rodriguez v. Rodriguez*, 116 Nev. 993 (2000). But, the Legislature has told the courts that spouses owe each other the highest duties of financial probity and rectitude, NRS 123.070. With those duties necessarily comes the right to enforce them. Ultimately, the law must be a moral force or it will lose the respect of the governed. The matrimonial bar often must advise a client that she is still liable for alimony to an unfaithful spouse who has emotionally abused and degraded her – advice which most Nevadans find difficult to fathom or absorb. Pragmatism purged the law of sanctions for personal moral misconduct, but It has not purged the law of sanctions for financial misconduct. It is submitted the full panoply of sanctions for financial misconduct–restitution of loss, the cost of that restitution, and punitive damages in appropriate cases, are now the law of Nevada and should be vigorously pursued by the bar and awarded by the bench.

(Thanks to Radford Smith, Jim Jimmerson, Marshall Willick, Bob Cerceo and Bruce Shapiro for their review and input. All errors are theirs; the author is blameless.)

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ENDNOTES

1. Attributed to actor George Raft who made, and squandered, about $10 million in his movie career: "Part of the loot went for gambling, part for horses and part for women. The rest I spent foolishly." English soccer star George Best: "I spent a lot of money on booze, birds and fast cars. The rest I just squandered."

2. See "No Honor Among Thieves or Spouses–Issues Confronting the Divorce Spouse in Disgorgement, Forfeiture, and Restitution Proceedings, 44 Fam Law Qtrly, Summer 2010 (ABA).

3. *Crawford,* id.: "Coming now to the question of constructive fraud, we find that our statute provides that either husband or wife may enter into any contract, engagement, or transaction with the other, or with any other person respecting property, which either might enter into if unmarried, subject, in any contract, engagement, or transaction between themselves, to the general rules which control the actions of persons occupying relations of confidence and trust towards each other. (Gen. Stats. 517.)

   The general rule of equity regulating dealings between parties occupying fiduciary relations, or relations of trust and confidence, is

well known. It is said: "In this class of cases there is often to be found some intermixture of deceit, imposition, overreaching, unconscionable advantage, or other mark of direct and positive fraud. But the principle on which courts of equity act in regard thereto stands, independent of any such ingredient, upon a motive of general public policy; and it is designed in some degree as a protection to the parties against the effect of overweening confidence and self□delusion and the infirmities of hasty and precipitate judgment." (Story's Eq. Jur. sec. 307.)

It is also said: "The doctrine to be examined arises from the very conception and existence of a fiduciary relation. While equity does not deny the possibility of a valid transaction between the two parties, yet, because every fiduciary relation implies a condition of superiority held by one of the parties over the other in every transaction between them by which the superior party obtains a possible benefit, equity raises a presumption against its validity, and casts upon that party the burden of proving affirmatively its compliance with equitable requisites, and thereby overcoming the presumption." (Pomeroy's Eq. Jur. sec. 956.)"

4. This creates an issue to consider in the drafting of nuptial agreements.

5. "This court, in *Rupert v. Stienne*, 90 Nev. 397, 528 P.2d 1013 (1974), abrogated the doctrine of interspousal immunity regarding claims arising out of motor vehicle accidents. Prior to *Rupert*, interspousal immunity barred a tort action by one spouse against the other. *Morrissett v. Morrissett,* 80 Nev. 566, 397 P.2d 184 (1964)." *Ziglinski v. Farmers Insurance*, 93 Nev. 23, 24 (1977). The author could find no case in Nevada which abrogates the statute of limitations between spouses or which tolls it.

6. NRS 11.190 (3)(d): "...actions...may only be commenced...[w]ithin 3 years... an action for relief on the ground of fraud or mistake, but the cause of action in such a case shall be deemed to accrue upon the discovery by the aggrieved party of the facts constituting the fraud or mistake." It may be argued the two year statute would apply. That is for another article by another author.

7. This rule would not impair the ability of a court to make an unequal division of community property by reason of a child's or spouse's security for payment of support, etc.

8. The question remains in which court, civil or domestic, such claims might be brought, also.