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McLean v. McLean: North Carolina Adopts the Gift Presumption in Equitable Distribution

Since its enactment in 1981, North Carolina's Equitable Distribution of Marital Property Act[1] (the Act) has caused consternation for the state's courts. In particular, courts wrestled with the Act's definitions of "marital" and "separate" property—two concepts central to the Act's purpose of classifying property upon divorce and distributing it equitably between spouses.[2]

The struggle, taking place for the most part in the North Carolina Court of Appeals, led to the establishment of several presumptions to assist courts in interpreting the Act.[3] In *McLean v. McLean*[4] the North Carolina Supreme Court stepped in, upholding a marital gift presumption[5] in spite of its own recantation of the marital property presumption.[6]

This Note traces the development of North Carolina's Equitable Distribution Act through cases interpreting the statutory definitions of "marital" and "separate" property. Following an examination of the supreme court's most recent significant decision in the area, *McLean v. McLean*, the Note concludes that while the courts' interpretations of the statute have been erratic, *McLean* shows policy is headed in the right direction.

Equitable distribution requires a judge to determine what property is subject to division and then to distribute such property in an equitable manner according to a number of statutory factors.[7] The court classifies property subject to distribution as marital. Property classified as separate is immune from distribution.[8] The statutory definition of marital property is simple; the term includes

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1. Act of July 3, 1981, ch. 815, 1981 N.C. Sess. Laws, 1st Sess. 1184 (codified as amended at N.C. GEN. STAT. § 50-20 (1987)).

2. N.C. GEN. STAT. § 50-20(a) (1987). "Upon application of a party, the court shall determine what is the marital property and shall provide for an equitable distribution of the marital property between the parties in accordance with the provisions of this section." *Id.*

3. *See, e.g.*, Loeb v. Loeb, 72 N.C. App. 205, 324 S.E.2d 33, *cert. denied*, 313 N.C. 508, 329 S.E.2d 933 (1985) (presumption that property acquired during marriage is marital); McLeod v. McLeod, 74 N.C. App. 144, 327 S.E.2d 910, *cert. denied*, 314 N.C. 331, 333 S.E.2d 488 (1985) (separate funds contributed to purchase price of home presumed to be a gift to the marital estate).

4. 323 N.C. 543, 374 S.E.2d 376 (1988). [Although the North Carolina Supreme Court decided *McLean* on December 8, 1988, the Note is included in the 1989 overview because of the significance of the case. Eds.]

5. First enunciated in *McLeod*, the marital gift presumption states that where husband and wife contribute separate funds to purchase property held as tenants by the entirety, the presumption arises that they each make a gift of the separate property to the marital estate. *Loeb*, 72 N.C. App. at 208, 324 S.E.2d at 38.

6. *See* Johnson v. Johnson, 317 N.C. 437, 346 S.E.2d 430 (1986). In a footnote, the supreme court stated that because the General Assembly did not provide for a marital property presumption in the equitable distribution statute, it would not infer one. *Id.* at 454-55 n.4, 346 S.E.2d at 440 n.4. *See also infra* text accompanying notes 71-78.

7. Sharp, *Equitable Distribution of Property in North Carolina: A Preliminary Analysis*, 61 N.C.L. REV. 247, 248 (1983).

8. *Id.* at 249. In other states, classification of property as separate or marital does not limit the courts' capacity to distribute it. In such "all property" states, a spouse's contribution to the acquisition of property is considered as a factor of what constitutes fair distribution. *Id.* at 248-49 & n.8. Even in states that follow an approach similar to North Carolina's, the courts often consider a

all property acquired during marriage and before separation "except property determined to be separate property."[9] The categorization of marital property therefore depends on the definition of separate property—a detailed definition that seems contradictory at times. Separate property includes all property acquired before the marriage and property acquired by one spouse during the marriage by bequest, devise, descent, or gift.[10] The "gift" provision of the separate property definition states, "property acquired by gift from the other spouse during the course of the marriage shall be considered separate property only if such an intention is stated in the conveyance."[11] The "exchange" provision of the statutory definition requires an express intention if "[p]roperty acquired in exchange for separate property" is to be considered marital.[12] Conflict between provisions arises if one piece of property is considered to be both a gift and property acquired in exchange for separate property—for example, a piece of property acquired in exchange for funds inherited by the wife and given to her husband. Theoretically, both provisions would apply creating contradictory presumptions. Case law, therefore, expresses a common-sense, rather than a strict literal, approach to applying the provisions.

North Carolina courts have employed various methods to classify property for equitable distribution. In *Loeb v. Loeb*[13] the court of appeals introduced a "marital property" presumption under which it considered property of questionable status as marital absent clear and convincing evidence of separate status. Later the North Carolina Supreme Court implicitly overruled this presumption in *Johnson v. Johnson*.[14] In the meantime, however, the court of appeals established two methods of classifying property acquired during marriage. The "source of funds" rule[15] and an offshoot of the marital property presumption, known as the "marital gift"[16] presumption or simply the "gift" presumption, appeared as aids in reconciling the gift and exchange provisions of the separate property definition. *McLean* is the supreme court's first definitive acceptance of the gift presumption.

Russell McLean and Carol Haynes McLean married in 1966 and divorced in 1985. During their marriage they bought a house and lot, which they held as tenants by the entirety.[17] Of the 169,973 dollars paid for the property and for

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party's contribution to the acquisition. *See, e.g.*, ARK. STAT. ANN. § 9-12-315(a)(iii) (Supp. 1988); KY. REV. STAT. ANN. § 403.190(1)(a) (Supp. 1988); ME. REV. STAT. ANN. tit. 19, 21722-A(1)(A) (1964).

9. N.C. GEN. STAT. § 50-20(b)(1) (1987).

10. *Id.* § 50-20(b)(2).

11. *Id.*

12. *Id.*

13. 72 N.C. App. 205, 324 S.E.2d 33, *cert. denied*, 313 N.C. 508, 329 S.E.2d 393 (1985).

14. 317 N.C. 437, 346 S.E.2d 430 (1986). *See infra* text accompanying notes 71-78.

15. *See* Wade v. Wade, 72 N.C. App. 372, 325 S.E.2d 260, *disc. rev. denied*, 313 N.C. 612, 330 S.E.2d 616 (1985).

16. *See* Loeb v. Loeb, 72 N.C. App. 205, 324 S.E.2d 33, *cert. denied*, 313 N.C. 508, 329 S.E.2d 393 (1985).

17. *McLean*, 323 N.C. at 544, 374 S.E.2d at 377. Under North Carolina law there is a presumption that real property acquired by a husband and wife is held as a tenancy by the entirety. The North Carolina General Statutes provide:

construction of the house, Mr. McLean contributed 75,311 dollars from funds he inherited from his father.[18]

Following the McLeans' divorce, the trial court classified the home and lot as marital property and ordered it distributed to the husband.[19] Mr. McLean appealed the court's decision categorizing the property as marital,[20] claiming that the amount he contributed to the purchase price from his inherited funds remained separate.[21]

The North Carolina Court of Appeals affirmed the trial court's classification of the home as marital, reasoning that "[b]y placing title to the properties in both names as tenants by the entirety, defendant is presumed to have made a gift of his separate property to the marital estate."[22] Judge Greene dissented from the majority's opinion, arguing that "joint title is irrelevant to the classification of property acquired in exchange for separate property."[23] In Judge Greene's view, the plain language of the statute required an express contrary intent to prove the making of a gift.[24] The two opinions illustrate the conflict between the gift and exchange provisions—the court cannot apply both provisions to the same piece of property without contradiction.

(b) A conveyance of real property, or any interest therein, to a husband and wife vests title in them as tenants by the entirety when the conveyance is to:

(1) A named man "and wife," or

(2) A named woman "and husband," or

(3) Two named persons, whether or not identified in the conveyance as husband and wife, if at the time of the conveyance they are legally married; unless a contrary intention is expressed on the conveyance.

N.C. GEN STAT. § 39-13.6(b) (1984). Tenancy by the entirety is a form of joint ownership unique to married couples. Tenants by the entirety may not destroy the tenancy by transferring their interests individually to another. At the death of one tenant, the survivor's interest "expands to absorb the relinquished ownership of the decedent." T. BERGIN & P. HASKELL, PREFACE TO ESTATES IN LAND AND FUTURE INTERESTS 60 (1984).

18. *McLean*, 323 N.C. at 544, 374 S.E.2d at 377. The McLeans funded the remainder of the costs with proceeds from the sale of their last residence, held as tenants by the entirety, ($39,662.38) and a $55,000 loan. The McLeans also received construction services in return for legal services rendered by Mr. McLean. *Id.* The money Russell McLean spent on the home represented a sizeable amount of the money he inherited which totalled "at least $100,000." Brief for Defendant Appellant at 4, McLean v. McLean, 88 N.C. App. 285, 363 S.E.2d 95 (No.8728DC574).

19. McLean v. McLean, 88 N.C. App. 285, 287, 363 S.E.2d 95, 97, *aff'd*, 323 N.C. 543, 374 S.E.2d 376 (1988).

20. Although the court awarded Mr. McLean the home, classification of the property as separate would remove the house from the marital estate, leaving less property subject to distribution between Mr. and Mrs. McLean.

21. *Id.* at 289, 363 S.E.2d at 98. If successful, the claim would presumably entitle Mr. McLean to the increase in value to the property due to passive appreciation. *Id. See infra* text accompanying note 58 for a discussion of active/passive distinction of appreciation. Mr. McLean also disputed the marital property classification of a note payable to him for the purchase of a house inherited from his father, an office building held by the couple as tenants by the entirety, a promissory note payable to Russell McLean, and 272 shares of corporate stock. *Id.* at 288, 374 S.E.2d at 98. The court concluded that the note was separate property because the gift presumption is not applicable to personal property. *Id.* at 290, 374 S.E.2d at 99. *See infra* text accompanying note 69. The stock was deemed marital because it was given in return for legal services of Mr. McLean. *Id.* at 290-91, 363 S.E.2d at 99. The court considered the office property along with the home but did not elaborate. *Id.* at 288-89, 374 S.E.2d at 98.

22. *Id.* at 289, 363 S.E.2d at 98.

23. *Id.* at 296, 363 S.E.2d at 102 (Greene, J., dissenting).

24. *Id.* (Greene, J., dissenting).

The North Carolina Supreme Court refused to accept Judge Greene's argument. It recognized that the two relevant provisions of the Equitable Distribution statute, the "exchange" provision and the "interspousal gift" provision, were potentially contradictory and therefore created an ambiguity in the statute.[25] Faced with such an ambiguity, the court found it necessary to look to legislative intent in interpreting the statute.[26] Since the Act was a response to the common law, the court reviewed the common law principles that necessitated the statute's enactment. Following this review, the court examined appeals court cases interpreting the equitable distribution statute. It then concluded that the "marital gift presumption . . . is appropriate as an aid in construing N.C.G.S. § 50-20(b)(2)"[27] and affirmed the portion of the court of appeals' decision classifying the McLeans' home as marital.[28] In doing so, it addressed both the gift and exchange provisions in an attempt to reconcile the contradictions arising from their contemporaneous application.

Professor Sally Sharp heralded North Carolina's Equitable Distribution Act as "the greatest change in domestic law of the state since the turn of the century."[29] Before the statute's enactment, North Carolina employed a "title only" approach to distribution of property in which the spouse holding legal title to the property maintained ownership of that property upon divorce.[30] Because the 1981 Act had no predecessor, the courts of this state had no previous decisions interpreting similar statutes to guide them. Many of the equitable distribution decisions therefore reflect common law ideas.

At common law, the "resulting trust" theory prevailed for determining ownership of property purchased by one party and titled in another's name.[31] Generally, when one person paid for land but titled it in another's name, a resulting trust arose in favor of the person furnishing consideration.[32] In other words, the person holding title was said to hold the property in trust for the person who paid for it.[33] However, when the purchaser had a legal or moral obligation to support the title recipient, a presumption arose that the purchaser intended to make a gift of the property.[34] Thus, when a husband paid for land titled in both his name and his wife's, equity presumed that the husband made a gift of the entirety interest to his spouse.[35]

The North Carolina Supreme Court applied this common law gift presump-

25. *McLean*, 323 N.C. at 548, 374 S.E.2d at 379.

26. *Id.* at 548-49, 374 S.E.2d at 380.

27. *Id.* at 551, 374 S.E.2d at 381.

28. *Id.* at 555, 374 S.E.2d at 383. The supreme court also affirmed the court of appeals' means of valuating Mr. McLean's law practice. *Id.* at 555-58, 374 S.E.2d at 383-85.

29. Sharp, *supra* note 7, at 249.

30. For an example of the "title only" theory's unjust results, see Leatherman v. Leatherman, 297 N.C. 618, 256 S.E.2d 793 (1979).

31. Mims v. Mims, 305 N.C. 41, 47, 286 S.E.2d 779, 784 (1982).

32. *Id.*

33. *Id.* at 46, 286 S.E.2d at 783.

34. *Id.* at 47, 286 S.E.2d at 784. This exception was an old one. *See* Thurber v. LaRoque, 105 N.C. 216, 220, 11 S.E. 460, 462 (1890).

35. *Mims*, 305 N.C. at 47, 286 S.E.2d at 784. As originally applied, the presumption did not work in favor of a husband holding title to land paid for by his wife.

tion in 1982 in *Mims v. Mims*.[36] Mr. Mims paid for land and, on the advice of his real-estate agent, titled it in his and his wife's names as tenants by the entirety.[37] The court applied a gift presumption to the transaction, but Mr. Mims successfully rebutted it with evidence that "he at all times intended for the property to be his alone and so advised [his wife] at and before the closing."[38] The court noted in dicta that the state's new Equitable Distribution Act, though not applicable in *Mims*,[39] addressed this issue.[40] The court read the statute to mean that "where 'separate' property is given in exchange for property acquired during the marriage, such new property so acquired" remains separate property.[41]

Soon after *Mims*, the North Carolina General Assembly amended the Equitable Distribution statute to state that property acquired in exchange for separate property shall remain separate regardless of title "and shall not be considered marital property unless a contrary intention is expressly stated in the conveyance."[42] The addition to the statute was likely a reaction to the legislature's fear that *Mims* might serve to defeat any interspousal gift if the gift could be traced to an exchange of separate property.[43] The addition allows express intention to transform separate property into marital property. The legislature, however, did not address the question of whether titling property by the entireties is sufficient to express the required contrary intention. Thus, the amendment may have confused the situation more than it clarified it. The court of appeals eventually interpreted this amended provision in *McLean*, but first attempted, in other cases, to establish methods of identifying separate and marital property in accordance with the new statute.

The court of appeals announced, in *Loeb v. Loeb*,[44] that all property acquired during marriage is presumed to be "marital property."[45] The presumption was rebuttable, however, by "clear, cogent and convincing evidence that the property comes within the 'separate property' definition"[46]—the same standard

36. 305 N.C. 41, 286 S.E.2d 779 (1982).

37. *Id.* at 43, 286 S.E.2d at 781. Mr. Mims paid for the property with a personal check for $69,000. *Id.* at 44, 286 S.E.2d at 782.

38. *Id.* at 59, 286 S.E.2d at 791.

39. *Mims* did not fall under the Equitable Distribution Act because the couple filed for divorce prior to the statute's enactment. The law stated, "[t]his act shall become effective October 1, 1981, and shall apply only when the action for an absolute divorce is filed on or after that date." Act of July 3, 1981, ch. 815, 1981 N.C. Sess. Laws 1st Sess. 1184, 1186 (codified as amended at N.C. GEN. STAT. § 50-20 (1987)). The Mimses were divorced in 1978. *Mims*, 305 N.C. at 45, 286 S.E.2d at 782.

40. *Mims*, 305 N.C. at 53, 286 S.E.2d. at 787. The court reasoned that the Act evidenced the legislature's intention that husbands and wives be treated equally, thereby providing the court with support for the decision to expand the common law gift presumption to work in favor of husbands as well as wives. *Id.* at 56, 286 S.E.2d at 789.

41. *Id.* at 54, 286 S.E.2d at 788.

42. Act of June 29, 1983 ch. 640, § 2, 1983 N.C. Sess. Laws 599, 599 (codified at N.C. GEN. STAT. § 50.20(b)(2) (1987)). *See* McLeod v. McLeod, 74 N.C. App. 144, 157, 327 S.E.2d 910, 918, *cert. denied*, 314 N.C. 331, 333 S.E.2d 488 (1985).

43. Sharp, *The Partnership Ideal: The Development of Equitable Distribution in North Carolina*, 65 N.C.L. REV. 195, 225 n.165 (1987).

44. 72 N.C. App. 205, 324 S.E.2d 33, *cert. denied*, 313 N.C. 508, 329 S.E.2d 393 (1985).

45. *Id.* at 209, 324 S.E.2d at 38.

46. *Id.* at 210, 324 S.E.2d at 39. The court admitted that the chances of overcoming the presumption were small. *Id.* at 211, 324 S.E.2d at 39.

for rebuttal established in *Mims*.[47] Mrs. Loeb claimed that real estate property given to the married couple by her mother was separate property because her mother intended to make a gift to her alone.[48] Mrs. Loeb failed, however, to rebut the presumption of marital property that arose because the property was jointly titled.[49]

Although *Loeb* suggested that the court of appeals held a preference for classifying property as marital, the court did not extend this preference to every circumstance. In *Wade v. Wade*[50] the trial court proclaimed that one asset could consist of both separate and marital property: in that case, a house as marital property and the parcel of land on which it rested as separate property. The court of appeals in *Wade*, however, refused to classify the house and land as two different pieces of property, insisting instead that it constituted an indivisible asset.[51] The court then refused to accept Mr. Wade's suggestion that the entire asset was separate property because the house was an improvement to the land.[52] Mrs. Wade suggested that the court consider the property marital based on a transmutation theory arguing that the commingling of separate property with marital property evidenced an intent to transform or transmute the separate property into marital property:[53] The court rejected her theory also because it found no legislative intent to create such a presumption.[54]

The better approach, the court determined, was to recognize the "dual nature of property that has been acquired with both marital and separate assets."[55] The court remanded the case to the trial court, ordering it to classify the property as separate and marital in proportion to the nature of the respective contributions made in its acquisition.[56] Thus the court established what is known as the "source of funds" test to distinguish marital and separate contributions toward a single asset.[57]

Commentators criticize the court's decision in *Wade* because it failed to establish first and foremost whether property has been "acquired" during the

47. *Id. See* Mims v. Mims, 305 N.C. 41, 59, 286 S.E.2d 779, 791 (1982).

48. *Loeb*, 72 N.C. App. at 211-12, 324 S.E.2d at 39.

49. *Id.* at 213, 324 S.E.2d at 40.

50. 72 N.C. App. 372, 325 S.E.2d 260, *disc. rev. denied*, 313 N.C. 612, 330 S.E.2d 616 (1985).

51. *Id.* at 377, 325 S.E.2d at 267.

52. *Id.* at 379, 325 S.E.2d at 267.

53. *Id.* at 381, 325 S.E.2d at 269. For an example of an application of the transmutation theory, see Lovering v. Seabrook Island Property Owners Ass'n, 289 S.C. 77, 346 S.E.2d 326 (S.C. Ct. App. 1986), *aff'd as modified*, 291 S.C. 201, 352 S.E.2d 707 (S.C. 1987) (land inherited by husband lost its separate status when husband built a home on it during marriage).

54. *Wade*, 72 N.C. App. at 381, 325 S.E.2d at 269.

55. *Id.*

56. Courts use several methods to determine what portion of the total equity is attributed to separate and marital funds. *See, e.g.*, Sharp, *supra* note 7, at 257 & n.58-60 (ratio between non-marital contribution and total contribution, multiplied by total equity equals non-marital property proportion). The courts, however, do not always classify the entire increase in value to separate property accruing during marriage. VALUATION & DISTRIBUTION OF MARITAL PROPERTY § 19.02[3][c] (J. McCahey ed. Supp. 1989) (Generally, marital property does not include increase in value caused by circumstances beyond the parties control, such as inflation.).

57. *See* J.GOLDEN, EQUITABLE DISTRIBUTION OF PROPERTY §§ 1.07, 5.06, 5.07 (1982 & Supp. 1987).

marriage. A proper analysis, one commentator suggests, would establish a firm definition of "acquisition" either as the date on which legal title is acquired or as an "ongoing process of making payment for property." Only after the court finds that property was acquired during the marriage would the court then determine the property to be separate or marital. If it found the property to be separate property, the court would then examine the increase in the property's value in terms of active and passive contributions. Active contributions to the equity would be credited to the marital estate while passive appreciation would remain separate.[58] The *Wade* opinion, in contrast, discusses the difference between active and passive appreciation before determining the separate nature of the property.

Despite *Wade*'s analytical problems, North Carolina courts have continued to use the source of funds approach to distributing property. Contributions made to separate property during the marriage are viewed as property acquired during the marriage and thus categorized as marital property for purposes of equitable distribution. In *McLeod v. McLeod*,[59] however, the court of appeals addressed a somewhat different question concerning the transformation of separate property and created an exception to *Wade*'s source of funds rule. The *McLeod* court recognized that the *Wade* rule "dictate[s] that each party retain as separate property the amount he or she contributed to the down payment."[60] The *McLeod* court declined to apply the rule, holding instead that titling property by the entirety raises a rebuttable presumption of the express intent necessary to transform separate into marital property.[61] Thus if a husband and wife each contribute separate funds to the purchase price of a home they hold as tenants by the entirety, a presumption arises that they each have made a gift of separate property to the marital estate.[62] Unless the presumption is rebutted, application of the source of funds approach is unnecessary.

The *McLeod* court noted that its decision accorded with the *Loeb* marital property presumption, but relied for support more heavily on the arguments of the *Mims* court. The *McLeod* court reasoned that the legislature enacted the equitable distribution statute for the same reasons that compelled the *Mims* court to apply the gift presumption at common law.[63] Therefore, although *Mims* did not claim to interpret the Equitable Distribution Act, that case properly served as the basis for the *McLeod* court's use of a gift presumption.[64] The court also looked *Mims* for a rebuttal standard: clear, cogent, and convincing evidence of contrary intent rebuts the gift presumption.[65] In addition, the court emphasized the special nature of tenancy by the entirety.[66] It also argued that

58. Sharp, *supra* note 43, at 213-14.
59. 74 N.C. App. 144, 327 S.E.2d 910, *cert. denied*, 314 N.C. 331, 333 S.E.2d 488 (1985).
60. *Id.* at 154, 327 S.E.2d at 916.
61. *Id.* at 156, 327 S.E.2d at 918.
62. *Id.* at 154, 327 S.E.2d at 916-17.
63. The court, however, did not elaborate on these motives. *Id.*
64. *Id.* at 153, 327 S.E.2d at 916.
65. *Id.* at 154, 327 S.E.2d at 916-17.
66. *Id.* at 152, 327 S.E.2d at 915.

the decision was not inconsistent with *Wade*, reasoning that the issue of commingling, "the hallmark of transmutation" rejected in *Wade*, was irrelevant to the case because payment for "entireties property may consist solely of separate property of one spouse."[67] In other words, the *McLeod* court refused to address *Wade*'s rejection of the transmutation theory because the issue of transmutation does not arise in cases in which one spouse contributes the entire amount to obtain property, for example, when a spouse pays for the entire down payment of a home. The facts of the case, however, do not fit this description because both spouses contributed funds to the property's acquisition.

Since *McLeod* the court of appeals has applied the gift presumption in favor of husbands in the context of real property[68] but has refused to extend the presumption to personal property.[69] The state supreme court, maintaining the same inconsistent approach to the policies underlying the Act, changed the law regarding the marital property presumption—a move seen by some commentators as an unnecessary departure from the state's adherence to the partnership ideal.[70] In *Johnson v. Johnson*[71] the question of distributing personal property arose once again in regard to a personal injury settlement. For the court, the case provided an opportunity to examine the marital property presumption established by the court of appeals in *Loeb*.

Mrs. Johnson claimed that settlement money received by her husband for personal injuries sustained during the marriage was marital property.[72] The husband disagreed with a marital designation, arguing that the settlement proceeds were separate property because they were acquired in exchange for separate property.[73] Rather than basing its decision on the point during the marriage at which the husband received the payment, the court looked at the purpose for which he received the money[74] and remanded the case for a determination of whether the total amount received represented more than just compensation for losses of the husband's separate property.[75] The court reached this conclusion because some of the money may have compensated medical care

67. *Id.* at 156-57, 327 S.E.2d at 918.

68. Dewey v. Dewey, 77 N.C. App. 787, 336 S.E. 2d 451 (1985), *disc. rev. denied*, 316 N.C. 376, 344 S.E.2d 1 (1986) (separate property contributed by wife to purchase of the marital home considered a gift to the marital estate).

69. Manes v. Harrison-Manes, 79 N.C. App. 170, 338 S.E.2d 815 (1986) (Assets acquired solely by husband but placed in joint bank account not presumed to be a gift to the marital estate. In the same case, however, the court applied the presumption to real property held by the couple as tenants by the entirety.).

70. *See* Note, Johnson v. Johnson: *Personal Injury Awards in Divorce Actions*, 65 N.C.L. REV. 1332, 1352 (1987). *But cf.* Note, *The North Carolina Supreme Court Revokes the Marital Presumption and Adopts the Analytical Approach to the Classification of Personal Injury Settlements*—Johnson v. Johnson, 22 WAKE FOREST L. REV. 931, 932 (1987) (the adoption of the complex analytical approach is praiseworthy).

71. 317 N.C. 437, 346 S.E.2d 430 (1986).

72. *Id.* at 445-46, 346 S.E.2d at 435.

73. *Id.* at 447, 346 S.E.2d at 436 (The court considered personal security along with the right to be free from pain as Mr. Johnson's separate assets.).

74. *Id.* at 451, 346 S.E.2d at 438.

75. *Id.* at 453, 346 S.E.2d at 439.

costs, lost wages, and lost services.[76] In its remand order to the trial court, the supreme court noted that there was no need to apply a marital property presumption to classify the property.[77] The General Assembly did not provide for such a presumption by statute, the court explained, so there was no reason to infer one.[78] This dicta implicitly overruled *Loeb*.[79] Justice Martin, in his concurring opinion, argued that the statute mandated a presumption of marital property for settlement awards "representing the value of a cause of action which arose during the marriage of the parties."[80]

While the supreme court seemed to retreat from the partnership ideal in *Johnson*, the court of appeals continued to advance the policy by consistently applying the gift presumption, in favor of both men and women.[81] Equally well accepted by the court of appeals was the source of funds test it announced in *Wade*.[82] In *McLean*, the supreme court therefore had the opportunity to reestablish an adherence to the partnership ideal and to clarify the acceptable use of the techniques employed by the court of appeals in *Wade* and *McLeod*. Although it accepted the first challenge, the *McLean* court failed to grasp the second opportunity. By stating that *Wade* did not govern because "our Court of Appeals has declined to apply this [source of funds] rule when a spouse uses separate funds to furnish consideration for property conveyed to the marital estate, as demonstrated by titling the property as a tenancy by the entirety,"[83] the *McLean* court dismissed the issue of the source of funds rule.

While the court's result is not incorrect, the *McLeod* argument against the use of the source of funds rule is not strong enough to serve as the state's best authority. *McLeod*, after all, rejected the source of funds rule because it considered the issue of transmutation—an alternative to the tracing method used by the source of funds rule—as irrelevant to cases in which one spouse contributes all of the consideration to the acquisition of property.[84] Neither the facts of *McLean* nor those of *McLeod* illustrate the narrow category of cases in which one spouse contributes the entire consideration to purchase property; the com-

76. *Id.* When the supreme court remanded the case to the trial court to calculate what proportion of the settlement award represented compensation for loss of separate property, it placed the burden on Mr. Johnson, the recipient of the settlement, to prove the amount of the separate portion. *Id.* at 454, 346 S.E.2d at 439-40.

77. *Id.* at 454-55 n.4, 346 S.E.2d at 440 n.4.

78. *Id.*

79. *Id.*

80. *Id.* at 455, 346 S.E.2d at 440 (Martin, J., concurring).

81. *See* Hunt v. Hunt, 85 N.C. App. 484, 355 S.E.2d 519 (1987) (separate funds contributed by wife to family home considered gift to marital estate).

82. *See, e.g.*, Lawrence v. Lawrence, 75 N.C. App. 592, 595, 331 S.E.2d 186, 188, *disc. rev. denied*, 314 N.C. 541, 335 S.E.2d 18 (1985) (real property bought by wife before marriage characterized as part separate and part marital because marital estate invested substantial labor and funds in improving real property); Willis v. Willis, 85 N.C. App. 708, 708, 355 S.E.2d 828, 828 (1987) (property held in title by wife designated part separate, part marital because husband made mortgage payments during marriage).

83. *McLean*, 323 N.C. at 546, 374 S.E.2d at 378.

84. McLeod v. McLeod, 74 N.C. App. 144, 156-57, 327 S.E.2d 910, 918, *cert. denied*, 314 N.C. 331, 333 S.E.2d 488 (1985); *see supra* text accompanying notes 59-67.

mingling of funds is therefore a potential issue in *McLean* and similar cases.[85] The *McLean* court, however, did not elaborate on the source of funds rule although the rule is the alternative to the gift presumption, the method applied when the gift presumption is rebutted, and badly in need of meaningful interpretation.

The court then proceeded to lay the foundation for its reconciliation of the gift and exchange provisions noting the importance of the partnership ideal.[86] Logically, the court noted that "an individual transfer must be considered as either a gift or an exchange"[87] after concluding that the two types of transactions are fairly easy to distinguish. The court explained that " ' "exchange" clearly implies that something of value has been received in return. "Gift," on the other hand, implies the opposite conclusion.' "[88] These definitions do not literally reflect the nature of Mr. McLean's transaction; he did, after all, receive an interest in the home. Categorization of the transaction as a gift, rather than as an exchange, is still in keeping with the legislature's likely intent that the exchange provision not be applied to interspousal gifts.[89] The General Assembly's early amendment to the exchange provision, while not entirely unambiguous when read with the whole, no doubt was an attempt to prevent the "extraordinary" consequences feared by the *McLean* court that "any gift between spouses" would be eliminated from the marital property classification " 'if the gift property could be traced, through exchanges, to separate property.' "[90] The court came closer to stating this argument explicitly when it reconciled its use of the gift presumption with the exchange provision. Titling property by the entireties satisfied the "contrary intention" language of the exchange provision (the language added to the original provision).[91]

In practice, application of the gift presumption is equitable and consistent with the partnership ideal. A spouse contributing separate funds to purchase property for the marital estate, as evidenced by a tenancy by the entirety, makes a conscious decision to use her separate funds for a marital purpose. In contrast is a spouse who happens to own a home before marriage and then accepts marital funds for its upkeep. The latter has not actively sought to change the nature of his property. The result of *McLean*, therefore, is that the gift presumption applies to active contributors of separate funds while passive recipients of marital funds are able to retain their original separate contributions as separate through use of the source of funds method.

If the actively contributing spouse does not so consciously donate her funds to the marital estate, the gift presumption, though still applicable, does not re-

85. Indeed courts frequently apply the gift presumption and the transmutation theories interchangeably because both spouses often contribute separate property to purchase marital property. *See* FAMILY LAW AND PRACTICE ch. 37-08[8] (A. Rutkin ed. 1987).

86. *McLean*, 323 N.C. at 549, 374 S.E.2d at 380.

87. *Id.* at 550, 374 S.E.2d at 381.

88. *Id.* (quoting Sharp, *supra* note 43, at 228 n.187).

89. *See supra* text accompanying notes 42-43.

90. *McLean*, 323 N.C. at 550, 374 S.E.2d at 380-81 (quoting Sharp, *supra* note 7, at 265).

91. *Id.* at 552, 374 S.E.2d at 382.

sult in an unjust solution. For example, if the spouse mentioned above contributes 40,000 dollars of her separate funds to purchase a house shortly after her marriage, the property will be held by her and her husband as tenants by the entirety.[92] Upon divorce the gift presumption will apply and our wife, for practical purposes, will be deemed to have given her husband a 20,000 dollar gift. Use of the presumption reflects the partnership ideal, but if the marriage is short lived, lasting perhaps for only a few months, it is doubtful that either spouse ever truly maintained the altruistic feelings associated with the ideal. This undesirable result, however, can be avoided. Under the equitable distribution statute, when an equal division of marital property is not equitable, the court may distribute the property unevenly in consideration of a number of specified factors and "[a]ny other factor which the court finds to be just and proper."[93] In many states contribution to the acquisition of property is a mandatory statutory factor for consideration.[94] So, even though the gift presumption applies to the home, resulting in its classification as marital, the courts do not have to award the husband 20,000 dollars worth of property upon distribution. When the gift presumption produces an unfair result, the trial court can, and should, use its broad discretion to correct the inequity.

Of course, there are ways for a couple to avoid the application of the gift presumption. Titling the property in a form other than a tenancy by the entirety is one such means.[95] The gift provision itself provides another. That provision states that an interspousal gift will not be considered marital property "if such an intention is stated in the conveyance."[96] Couples may state expressly in their conveyances that the money each spouse contributes to the purchase is to remain separate property in the event of a divorce. If such a precaution is taken, the gift presumption will have no effect on the separate status of the property.

Yet another way of preventing property from being considered marital is to rebut the gift presumption. A post-nuptial agreement, entered into when separate funds are contributed for the acquisition of property, would meet the rebuttal standard. The intent expressed in the agreement would be very similar to the intent that can be stated in the conveyance itself: in the event of divorce, separate property contributed by either spouse to the property's acquisition or improvement shall remain separate property. The statement made in the conveyance itself would avoid a marital designation altogether, while a post-nuptial agreement would rebut the gift presumption that would automatically arise from titling the property by the entireties.

In light of these alternatives, the gift presumption preserves the partnership

92. She could title the property in another form of joint ownership such as a tenancy in common. A tenancy by the entirety, however, provides couples with stability: one spouse may not unilaterally dispose of the property or end the joint tenancy and a survivorship right accrues to the surviving spouse. For our purposes, let us assume our spouse is not aware of the alternatives to a tenancy by the entirety.

93. N.C. GEN. STAT. § 50-20(c)(12) (1987).

94. *See, e.g.*, ARK. STAT. ANN. § 9-12-315(a)(iii) (Supp. 1988); KY. REV. STAT. ANN. § 404.190(1)(a) (Supp. 1988); ME. REV. STAT. ANN. tit. 19, § 722-A(1)(A) (1964).

95. *See supra* note 92 for a discussion of the disadvantages of this approach.

96. N.C. GEN. STAT. § 50-20(b) (1987).

ideal without draconian results. While preservation of the ideal is admirable in its own right, the *McLean* decision is even more significant following on the heels of the rejection of the marital property presumption in *Johnson v. Johnson*.[97] At last, the North Carolina Supreme Court has set a clear standard for the gift presumption.[98] Such clarity is important not only to lower courts but also to the many parties who wish to avoid litigation.[99] Acceptance of the gift presumption, therefore outweighs the shortcomings of the decision. Though the decision does not explain the alternative to the gift presumption and it cannot, without legislating, attempt to rework the confusing language of the exchange provision, the supreme court has reached a praiseworthy conclusion in *McLean*.

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97. The *McLean* court determined that "[b]ecause marital *property* and marital *gift* presumptions are discrete concepts, *Johnson* does not control here." *McLean*, 323 N.C. at 553, 374 S.E.2d at 382.

98. In other states, courts addressing the issue also apply the gift presumption. *See* Farmer v. Farmer, 398 So. 2d 723 (Ala. App. 1981); *In re* Marriage of Butler, 346 N.W.2d 45 (Iowa App. 1988); Carter v. Carter, 419 A.2d 1018 (Me. 1980). Not all courts, however, restrict the presumption to real property. *See, e.g.*, Lynam v. Gallagher, 526 A.2d 878 (Del. 1987) (transfer of shares of stock to joint names presumed to be a gift); *In re* Marriage of Rink, 136 Ill. App. 3d 252, 483 N.E.2d 316 (1988) (bank accounts held in joint tenancy presumed to be a gift before presumption rebutted).

99. "[T]he overwhelming majority of divorcing couples resolve distributional questions . . . without bringing any contested issue to court for adjudication." Mnookin & Kornhauser, *Bargaining in the Shadow of Law: The Case of Divorce*, 88 YALE L.J. 950, 951 (1979). "The primary function of contemporary divorce law [is not to] impos[e] order from above, but rather [to] provid[e] a framework within which divorcing couples can themselves determine their postdissolution rights and responsibilities." *Id.* at 950.