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CHAIR'S COLUMN

A Fond Farewell

by Madeline Marzano-Lesnevich

This is my final column as chair of the Family Law Section. It indeed has been an honor to serve as chair of this extremely active, productive section.

I, of course, wish to thank my fellow officers for all of their assistance and good cheer; all members of the executive committee who came to our monthly meetings and diligently reviewed and discussed proposed legislation important to our practice; all members of our subcommittees who bore the additional burden of researching and reporting to the executive committee on specific topics; all members of the judiciary who support our section; and all retreat-sponsoring friends of the section. I also wish to thank all those in my law firm who have carried the burden of the practice while I devoted myself to section activities; all members of my family who, if not actual members of the section, clearly believe themselves to be honorary members; and, most importantly, my husband, my law partner. But I am not going to thank each of these friends here. I will do so personally and privately.

This year has been, in many respects, a quiet year. This publication, the *New Jersey Family Lawyer*, resurrected itself. It has a strong editorial board, dedicated to providing its readers with thought-provoking editorials and substantive resource material, often on the cutting edge of family law. Family Law Section members pay $15 a year more than other section members in annual State Bar dues. Presumably this surcharge is to cover the cost of producing and distributing this publication. The editorial board recognizes that the New Jersey State Bar Association owes Family Law Section members this publication on a regular, timely basis. Our energetic associate managing editors diligently solicit quality articles for inclusion in this publication. If you wish to write an article, or if there is a subject you believe sufficiently important to the section to be in this publication, please let the editorial board know this. This is your section; this is your publication as well.

This year was the 40th anniversary of the Family Law Section, and we celebrated it at our holiday party in December. We were able to bring together past chairs of the section. It was an extraordinarily heartwarming event. The spirit of camaraderie that permeates this section was evident. Newcomers were made to feel welcome. Earlier chairs of the section conversed with later ones. An ad journal was published to commemorate the event. For those of you who were unable to attend, I would like to share this historic event with you. Please see the roster of past chairs, and picture of those chairs in attendance, published elsewhere in this newsletter.

All section members owe a special debt of gratitude to the earlier chairs of our section, who had the foresight to form our section and the dedication to build our section from a membership of around 30 in 1964 to upwards of 1,200 in 2005.

Later in the year we went to New Orleans for the annual Family Law Retreat. The response to the limited publicity about the retreat was overwhelming. Registration had to be closed. The block of hotel rooms reserved for this event had to be expanded. Approximately 213 people registered for our retreat—a record number. All who attended were made to feel welcome. New friends were made. A spirit of inclusiveness permeated the retreat. In the words of some of the attendees, including certain of those "honorary" section member mentioned above, we "raged."

The success of this retreat, as well as the success of past retreats to Charleston, Santa Fe and Las Vegas, are undoubtedly attributable to our choice of locale, to the affordability of the retreat, to the one-registration-fee-covers all-events policy, and to the spirit of inclusive-

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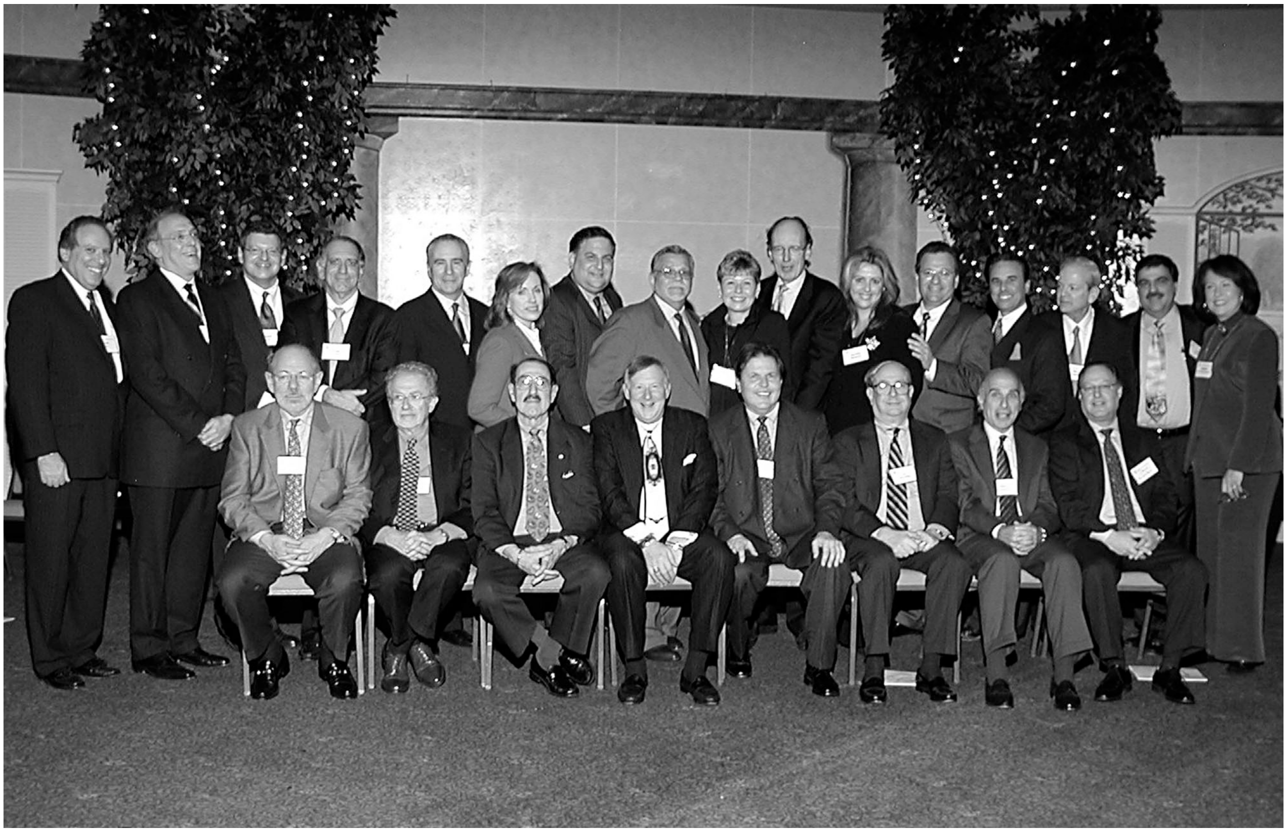
ness of our retreat. Our future chairs are committed to continuing to choose affordable sites for our retreats, and to making all new attendees feel welcome.

The younger members of our section will be the future leaders of this section. It is important that they be given the opportunity to be active in this section. During my tenure as chair, I received many inquiries from other family law practitioners, asking, "How can I get involved?" My response always started with a very pragmatic quote from Woody Allen: "Eighty percent of success is showing up." New family law practitioners should join our Young Lawyers Subcommittee. Your section dues covers membership in the Young Lawyers Subcommittee. But *it isn't enough to just join.* You must actually go to the meetings. All family law practitioners—however long they have practiced—who wish to be more active in our section need to show up. Come to our holiday parties, come to the Tischler dinner, come to the retreats. But while you are there, introduce yourselves, particularly to the officers of the section. The chair of the section appoints members to the executive committee, with the input of the officers as a whole. If you wish to be on the Family Law Section Executive Committee, let the officers know. But if you are to be on the committee, you must show up; you must actively contribute your time and your thoughts to our section; you must be willing to enjoy yourself as well.

As I think back on my year as chair, what I will remember most fondly is the extraordinary camaraderie of our section members. As a new chairmanship begins, what I wish for is a continuation of the growth, success and inclusiveness of the section, and that this section be an example for the State Bar. ■

Family Law Section Chairs



2004–2005	Madeline Marzano-Lesnevich
2003–2004	John DeBartolo
2002–2003	Michael J. Stanton
2001–2002	Cary B. Cheifetz
2000–2001	Lynne F. Newsome
1999–2000	Mark Biel
1998–1999	Neil D. Rosen*
1997–1998	Mark H. Sobel
1996–1997	Patricia M. Barbarito
1995–1996	John P. Paone Jr.
1994–1995	William J. Thompson
1993–1994	John E. Finnerty Jr.
1992–1993	Lynne Strober
1991–1992	John J. Trombadore
1990–1991	Richard A. Russell
1989–1990	James P. Yudes
1988–1989	Myra T. Peterson
1987–1988	Alan M. Grosman
1986–1987	Frank A. Louis
1985–1986	David K. Ansell
1984–1985	David M. Wildstein
1983–1984	Jeffrey P. Weinstein
1982–1983	Lee M. Hymerling
1981–1982	Lee M. Hymerling
1980–1981	Thomas P. Zampino
1979–1980	Anne W. Elwell
1978–1979	Hyman Isaac*
1977–1978	Laurence J. Cutler
1976–1977	Thomas S. Forkin*
1975–1976	Bernard H. Hoffman
1974–1975	Gary N. Skoloff
1973–1974	Gardner B. Miller
1972–1973	Edward S. Snyder
1971–1972	Edward S. Snyder
1970–1971	Richard J. Feinberg*
1969–1970	Monroe Ackerman
1968–1969	Monroe Ackerman
1967–1968	Charles M. Grosman*
1966–1967	Charles M. Grosman*
1965–1966	Charles M. Grosman*

* Deceased

FROM THE EDITOR-IN-CHIEF

Mani v. Mani: The End of Fault or the End of the Beginning of No Fault

by Mark H. Sobel

On April 6, the Supreme Court, in an opinion authored by Justice Virginia Long, provided the Court's insight into the use and the potential misuse of marital fault within the context of determinations regarding alimony in *Mani v. Mani*.[1] A reading of Justice Long's opinion and the opinion of Justice Roberto Rivera-Soto, concurring in part and dissenting in part, provides a unique juxtaposition of the analysis of our body of law in the abstract with the enforcement of that law in practice. By so doing, the opinion sheds enormous light on this issue regarding the insertion of marital fault in matrimonial cases and the myriad of issues it impacts and problems it raises.

Justice Long, an experienced jurist with extensive experience in the area of family law, illustrates her unique knowledge of the relative attention span of most family law practitioners by setting forth the Court's holding clearly and concisely in a few sentences at the beginning of the opinion, stating:

> We hold that marital fault is irrelevant to alimony except in two narrow instances: cases in which the fault has affected the party's economic life; and cases in which the fault so violates societal norms that continuing the economic bonds between the parties would confound notions of simply justice.[2]

Justice Long and the Supreme Court thus set forth only two "narrow instances" for the insertion of marital fault into a divorce action relative to the payment of alimony. The Court's sensitivity to the actual practice of family law is clearly illustrated in its reasoning and ultimate determination in this area. The Court was cognizant of the fact that the litigation of marital fault elevates the intensity level of such cases, polarizes the parties, and prevents prompt and efficient settlement of these matters. Furthermore, the opinion suggests that in the majority of cases the courts may not be the appropriate repository of a determination regarding marital fault. That issue often comes down to the chicken or the egg type argument, where one party has exhibited improper marital behavior, as that would be generally defined, but defends the conduct by claiming it was a reaction to the lack of a marital partnership emanating from the other party.

For a considerable time, in excess of probably 20 years, the utilization of marital fault, its insertion in complaints and counterclaims, and counsel's reliance upon it to extract financial benefit, has slowly but surely withered on the vine and born little to no judicial fruit. As a result, many practitioners in this area, absent a true *Tevis*[3] claim, do not insert that controversy in most of their matrimonial cases. The fear practitioners had, as *Mani* was working its way up the Court's system, was that the Court's acceptance of marital fault as a legitimate and persuasive factor in calculating alimony would open the flood gates of such claims. The sensitivity that the Supreme Court has shown in its analysis of this particular factor is illustrative of the ability of the Court to work within the legislative construct by putting the flesh on the bones of a legislative statute, and thus achieving a set of standards and acceptable parameters for analysis of alimony issues that can be utilized in virtually all of the cases.

The facts in *Mani* are straightforward. The husband appealed, seeking an increased level of alimony from the wife, contending that the trial judge improperly reduced the appropriate alimony amount by relying in part upon the wife's claim of marital fault predicated upon the husband's alleged adultery. The matter was affirmed by the Appellate Division, which, according to the Supreme Court opinion:

> noted that although the trial court did not specifically mention adultery and extreme cruelty as factors in the alimony analysis, it did find that [the wife] had proven the grounds asserted in her complaint. According to the Appellate Division the [husband's] adultery was significant and 'his marital indiscretions warrant consideration in the amount of that award.'[4]

The legal issue, narrowed to its essence, was an analysis of N.J.S.A. 2A:34-23, and specifically that portion of the statute allowing the Court to "consider any other factors which the Court may deem relevant" at arriving at an alimony decision.

The excellent and compelling legal brief submitted by our new chair, Bonnie C. Frost, and her partner, Stephen P. Haller, emphasized that fault should not be considered as a factor, except in the most unique and egregious of circumstances. Ultimately, the Supreme Court, in substantial reliance upon the analysis set forth in that brief, ruled accordingly. Thus the Supreme Court acknowledged that New Jersey has a long history in which "alimony is neither a punishment for the payor nor a reward for the payee."[5] It is that fundamental premise that is endorsed by the Supreme Court in *Mani*.

In reaching its holding, the Supreme Court analyzed the legislative history of this statute within the context of the legislatively created Divorce Law Study Commission, prior to the passage of the Divorce Reform Act.[6] In the commission's final report, it was noted that "fault, when so asserted as a ground from relief will be a proper consideration for the judiciary in dealing with alimony and support."[7] Consideration of fault in an analysis of alimony must include not only focus upon the enumerated factors that may be considered by the Court, but also subsection (g) of N.J.S.A. 2A:34-23, which states:

> In all actions for divorce other than those where judgment is granted solely on the ground of separation, the court may consider also the proofs made in establishing such grounds in determining an amount of alimony or maintenance that is fit, reasonable and just.

The Divorce Study Commission's analysis of that provision provides insight into the reasoning for that language:

> The last sentence of the proposed amendment permits the Court to deny alimony to a spouse who is guilty of the fault grounds for divorce. As long as fault grounds are retained, it is traditional logic that fault should also effect the judicial discretion in awarding alimony. After further study a new commission may conclude that fault has no place in either the provision of grounds for divorce or for determining alimony but, for the time being, the substance of existing law is retained.[8]

The above language seemingly provides an obvious entreé for family law practitioners to insert fault into their cases, hoping to increase or decrease the level of alimony. However, for those of us who have toiled in this area for the past two-plus decades, it is obvious that such excursions were relatively unproductive, and ultimately, in the majority of cases, abandoned. The courts, as practitioners know, do not uniformly exercise their discretion on virtually any subject within the area of family law practice. However, in this area there probably was more uniformity than most.

The Supreme Court, in exercising its judicial discretion, provides clear guidance in *Mani v. Mani*, acknowledging that what we have long thought was appropriate in processing these cases should continue to remain the polestar of virtually all divorce litigation; *i.e.,* that absent the most unusual of circumstances, marital fault is not going to be an element of alimony calculation.

In fact, as the Supreme Court emphasized in its discussion of precedent at pages 21-26 of its opinion, in those cases where fault was utilized as an element, it was more often than not rejected or reversed on appeal.[9] After analyzing existing jurisprudence, the Supreme Court determined:

> Recapping, although our case law has consistently recognized that, under statutory scheme, fault may be considered in calculating alimony, for over a quarter of a century, courts have declined to place their imprimatur on wide range use of fault in that context.

The opinion in *Mani* would appear to provide the death knell for the use of marital fault as a strategic advantage in any particular litigation. In so ruling, the Supreme Court emphasized, as was set forth in *Kinsella v. Kinsella,*[10] that economic factors are going to form the core analysis for the Court in making this type of economic determination. By so doing, the Supreme Court clearly sets forth its belief that the emotional context of a divorce litigation needs to be deemphasized; the psychological and psychiatric aspects of fault regarding the dissolution of the marriage may be better left for others.

While the Supreme Court leaves open the issue of the exact variety of fact patterns in which one of the two exceptions exist, the illustrations provided by the Court show its inclination that such exceptions be just that, exceptions, rather than the rule. The Supreme Court's rationale is set forth as follows:

> Our conclusion flows purely from a relevance perspective. 'Relevant evidence' is 'evidence having a tendency in reason to prove or disprove any fact of consequence to the determination of the action.' ...Given the economic basis of alimony, there can be no quarrel over the notion that fault that has altered the financial status of the parties is relevant in an alimony case...
>
> The same relevance notion does not apply to the oridinary fault grounds for divorce that lurk in the margins of nearly every case and therefore those grounds should not be interjected into an alimony analysis. To do so would distort the application of the principles the Legislature has adopted to secure economic justice in marital cases. Moreover, without concomitant benefit, considering non-economic fault can only result in ramping up the emotional content of matrimonial litigation and encouraging the parties to continually replay the details of their failed relationship. Not only is non-economic fault nearly impossible to factor into an alimony computation, but any attempt to do

> so would have the effect of generating complex legal issues regarding the apportionment of mutual fault, which is present in nearly all cases. That, in turn, would result in the protraction of litigation and the undermining of the goals of no-fault divorce, again without a corresponding benefit.

In so ruling, the Supreme Court both emphasizes its adherence to the belief of judicial discretion and its embracing of the reality of divorce litigation as it has existed for many years within our state.

Much as when I attended law school and first was reading opinions, the following thoughts came to me as I then continued my reading past the majority opinion into the concurrence and dissent of Justice Rivera-Soto. When as a young law student I would read the majority opinion, it would seem so logical until I then reviewed the dissenting opinion, which seemed equally logical. Justice Rivera-Soto's opinion has much to do with an analysis of marital fault and its appropriateness in divorce litigation but, far more, we are impressed by its compelling examination of the interplay between the judicial and legislative branches and the construction by the Court of enactments of our Legislature. As Justice Rivera-Soto states, his primary inability to join the majority opinion flows from his conclusion that:

> I also cannot ignore the plain reading of a statute, disregard completely its clear legislative history and jettison over 30 years of our own jurisprudence.[11]

As Justice Rivera-Soto points out:

> Whether marital fault should be retained as an element of alimony was a matter of debate before the Divorce Law Study Commission, with strong opposition advanced against retaining marital fault as part of the alimony formula.

Justice Rivera-Soto concludes that fault was thus not an oversight by the commission, not ignored by the commission, but was, in fact, examined by the commission and formed a part of the legislative history. By so doing, and by providing within the statute language an analysis of fault for determinations of alimony, the Court has been provided discretion in analyzing such fault, but may not refuse to analyze it altogether. Thus, it appears a reading of the dissent focuses primarily upon what we have come to call strict constructionists, who seek to explain legislative intent but not expand legislative intent. While there clearly is logic to such a position, both upon a purely legal analysis as well as factual examination, the ultimate decision the *Mani* Court was forced to make was one that will allow for an examination of all relevant factors but with an eye toward eliminating unnecessary examination of factors that in most cases could not, in the Court's eye, be deemed relevant.

Mani is an extremely practical decision in an area of law our clients often make impractical. It is an extremely sensitive decision that seeks to maintain a fine balance between the necessity to examine fault but not let the exceptions become the rule. It is, in fact, a melding of legislative intent and judicial interpretation, tempered with reality in our area of practice, reached with an eye not only to the past but, more importantly, to the future. It is established to enable us to provide justice to our constituency as best as we can, keeping in mind the mantra that the Divorce Law Study Commission heard time and time again as the primary criticism of this area: Divorce cases take too long and cost too much.

It is that mantra the Court seemed to have clearly understood in creating this delicate balance in the *Mani* opinion. It is now for us, as practitioners, to determine the acceptable parameters of those two exceptions, and when they are appropriately to be considered as a legitimate element in a divorce action. Whether practitioners consider the door of marital fault to be closing or opening, the *Mani* opinion seemingly makes it clear that the opening is narrow, as it should be. ■

ENDNOTES

1. 183 NJ 70 (2005).
2. *Id.* pg. 1-2.
3. *Tevis v. Tevis*, 79 NJ 422 (1979).
4. *Mani* at 8.
5. *Mani* at 13.
6. N.J.S.A. 2A:34-23
7. *See Divorce Law Study Commission, N.J., Final Report to the Governor and State* (1970) at 7.
8. *See Final Report, supra,* at 94-95 and *Mani v. Mani, supra,* at pg. 19.
9. *See Greenberg v. Greenberg,* 126 N.J. Super. 96 (App. Div. 1973); *Chalmers v. Chalmers,* 65 N.J. 186 (1974); *Nochenson v. Nochenson,* 148 N.J. Super. 448 (App. Div. 1977); and *Lynn v. Lynn,* 165 N.J. Super. 328 (App. Div. 1979). *See also, Mahne v. Mahne,* 147 N.J. Super. 326 (App. Div. 1997), which provides support for consideration of fault prior to the determination in *Nochenson* and *Lynn.*
10. 150 N.J. Super. 276 (1997).
11. *Mani* at pg. 2 of dissent.

FROM THE EDITOR-IN-CHIEF EMERITUS

Mark Biel Receives Tischler Award

by Lee M. Hymerling

It is with great pleasure that we recognize Mark Biel, this year's worthy Tischler Award recipient. Past chair of the Family Law Section, past president of the Atlantic County Bar Association, and past trustee of the New Jersey Bar Association, Mark Biel has left his mark not only on family law, but upon our state's broader legal community.

This publication has long benefited from Mark's contributions as an author and an editor. Our section has long benefited from Mark's leadership. Mark came to be our section chair at a time of great sadness, following Neil Rosen, whose untimely death shocked us all. Mark chaired our section in several of the years of the important work of the Supreme Court Special Committees on Matrimonial Litigation, and assured that the views of the practicing bar were heard and considered.

His contributions, however, go far beyond the tasks that every Family Law Section chair must address. Mark is a leader who gives his all to the task of leading responsibly. A consummate Bar politician, he always advocated within Bar circles for our area of practice and for us, his colleagues. Mark is and has always been a go-to guy. The respect our colleagues in the broader Bar have for Mark can be seen in his appointment to and service as chair of the State Bar's Professional Responsibility Committee; vice-chair of its Judicial and Prosecutorial Appointments Committee; and as a member of the State Bar's Nominating Committee.

His countless years of service to our section, and to the State Bar and his county bar, have been mirrored in Mark's distinguished service as a member of the Supreme Court Committee on Civil and Family Motion Practice, as well as the Supreme Court Family Part Practice Committee.

I have known Mark in many capacities. I have known him as an adversary; a fellow State Bar trustee; a fellow past chair of the section; on several boards and committees; and as a friend. As an adversary, Mark can be formidable, but he never loses his sense of fairness and his recognition that whenever possible a settlement can, and almost always should, be achieved.

There are many things that make Mark stand above the crowd. When a task needs to be done, he is always there, and never says no. When a challenge needs to be met, he figures out a way to perform the task practically and expeditiously. As a friend he is most generous with his time and with his counsel.

Mark came to practice in Atlantic City following military service in Vietnam, where he earned the Bronze Star and the Armed Forces Medal. A combat journalist for *Stars and Stripes*, his professional writing has aided not only clients but also this publication and those who have attended the innumerable Institute for Continuing Legal Education lectures where he has appeared and for which he has written.

The Saul Tischler Family Law Section Award was created in the early 1980s to recognize singular career-long contributions to the advancement of family law in the state of New Jersey. Long ago Mark Biel earned the recognition. We all should congratulate him for his achievement and thank him for the multitude of his contributions. ■

The 2004 Version of the CIS and Marital Lifestyle

by John F. DeBartolo

On September 1, 2004, a modified version of the case information statement (CIS) became mandatory in all family part cases.[1] This latest version of the CIS has been heralded as containing many significant changes that advance the progression of the form as the single most important pleading in a dissolution action.[2] As practitioners, we must always recognize that the form is not an end unto itself, and its completion is more than an exercise in creative bookkeeping. The substantive law, especially what the Supreme Court (who after all, approved the form) has to say about the CIS and marital lifestyle, guides the effective completion of the form for the family lawyer in his or her role as advocate in the pending litigation and for all future modification applications.

More than four years ago, the New Jersey Supreme Court decided the often cited, often analyzed, and frequently misunderstood case of *Crews v. Crews.*[3] While reviewing a dispute arising from a trial court's alimony determination in a contested case, the Court extensively commented upon the importance of marital lifestyle in post-judgment motion practice for a future modification of alimony. Among the most cited passages of *Crews* is the following:

> The *marital standard of living is essential to an analysis of changed circumstances* regardless of whether the original support award was entered as part of a *consensual agreement or of a contested divorce judgment.* The setting of the marital standard of living is equally important in an uncontested divorce. Accordingly, *lest there be an insufficient record for the settlement, the court should require the parties to place on the record the basis for the alimony award including, in pertinent part, establishment of the marital standard of living, before the court accepts the divorce agreement.* In this regard we note that Rule 5:5-2 already requires in divorce actions the filing of a CIS with detailed financial information, and that subsection (c) places a continuing duty on the parties to update the information provided to the court no later than twenty days prior to the final hearing. However, *the CIS information generally reflects a more current financial picture of the parties. It does not necessarily provide information reflective of the standard of living enjoyed during the marriage. Therefore, that information is not a substitute for the parties' stipulation on the marital standard of living.*[4] (emphasis added)

We have all listened to lectures, read articles, and been treated to various suggestions regarding how to satisfy, or alternatively, waive this new judicially created procedural mandate for alimony cases. Ultimately, as discussed below, the Court recognized the practical implications upon daily practice of its *dicta,* and clarified its intent.[5] Nevertheless, the substance of the Court's comments about the CIS, and the observation that the form did not reflect marital lifestyle, deserves examination in light of the modified CIS.

The modified budget pages (pages 3 and 4) of the new CIS, on their face, directly address the concerns of the Court respecting the confusion of "current financial picture" with the "marital standard of living." For years litigants were asked to create a budget of monthly expenses for themselves "and children residing with" them, and a separate listing of "expenses paid for spouse and/or children not residing with" them. The cryptic instructions at the beginning of the budget pages stated that the expenses listed "should reflect the standard of living established during marriage." In practice, the submitted budgets did nothing of the sort. As recognized by Justice Jaynee LeVecchia in *Crews,* the information "generally reflected a more current financial picture of the parties."

The remedy of the Court was the requirement that marital lifestyle either be stipulated or determined independently by the trial court. The war stories from around the state proliferated. Uncontested cases now took hours, or sometimes nearly an entire day, to put through as trial courts conducted lifestyle hearings. Even when stipulations were reached, litigants often did not understand the nature of the stipulation or its consequences. They had, after all, completed CISs and submitted them to the court. Wasn't that enough? Wasn't it clear to the courts that simple mathematics demonstrated that two households could not be maintained at the same level as one joint household with the same level of income? Unfortunately, some alimony recipients, pressured to reach settlement, gave in and stipulated to being able to maintain the marital lifestyle with the amount of alimony when in fact it was not possible to do so. Many attorneys sought to sidestep the lifestyle issue by reserving the determination until the time of a modification application.

In 2003, nearly three years to the day *Crews* was decided, the Appellate Division decided the case of *Weishaus v. Weishaus.*[6] The facts and procedural history of that case highlighted the practical dilemma faced by attorneys and litigants who had settled all issues in a comprehensive and thoughtful manner but who could not agree upon the marital lifestyle.

Mr. and Mrs. Weishaus settled their divorce-related issues, subsequent to the entry of a *pendente lite* support award. The final agreement included payment, by the husband, of term alimony for three years. The attorneys reduced the agreement to writing and went to court to obtain an uncontested divorce.

At the uncontested hearing the trial court listened to testimony from the wife, who stated that she would not be able to maintain the marital lifestyle after the divorce for two primary reasons: the husband's mother would no longer be making contributions to the marriage, and the lifestyle was supported in part by the sale of assets during the marriage. She further testified that the marital lifestyle was accurately reflected in the CIS. The husband testified to his income, which was recognized by all as insufficient on its own to maintain the marital lifestyle. His attorney confirmed the wife's testimony that her generous mother-in-law and the sale of assets greatly supplemented the marital lifestyle.

The trial court then made its findings as follows:

> …I don't see any reduction in lifestyle when I exclude the money that came into the household from his [defendant's] mother which I cannot charge him with having a responsibility to continue so that if she [plaintiff] ever comes back and tries to claim that she can't maintain her lifestyle, she cannot utilize the money that came into the household from his mother as a basis for seeking modification. And with respect to the other items, it seems that they lived on assets. Again, that's another item that I cannot require him or I cannot charge him—for which I can charge him a responsibility. He certainly cannot continue to support his former wife out of assets. So I find there is no actual shortfall in lifestyle and that finding should be included in the Judgment of Divorce.[7]

The wife appealed. The parties settled the appeal at the Appellate Division settlement conference. They agreed to vacate the trial court's findings, agreed that they were unable to agree upon the marital standard of living, and agreed that if either ever made an alimony modification application the trial court would be required to determine marital lifestyle pursuant to *Crews.*

Upon remand, the trial court refused to approve the settlement, specifically because of the deferral of findings or stipulation of lifestyle. A second appeal followed, resulting in a reported decision.[8] The Appellate Division analyzed the case guided by "our Supreme Court's *clear direction in Crews v. Crews*" that:

> …even in uncontested cases, "the court should require the parties to place on the record the basis for the alimony award including, in pertinent part, establishment of the marital standard of living, before the court accepts the divorce agreement." *Crews, supra,* 164 N.J. at 26, 751 A.2d 524. Thus, in determining the "marital standard of living," the trial court must rely on specific evidence detailing the parties' manner of living during the marriage as well as the financial sources underwriting it. [FN1] This record will form the baseline from which to determine any future application for modification of support. *Id.* at 16, 751 A.2d 524. *Even when the parties stipulate as to the marital lifestyle, the stipulation must be definite and certain in its terms and the consent of the parties to be bound by it must be clearly established.*[9] (emphasis added)

The Appellate Division decision continued with directions to trial courts for those cases in which the parties were unable to stipulate to marital lifestyle. The trial court must determine marital lifestyle at the time of the final judgment, and could not defer the determination to a future modification hearing.[10]

> In making this determination, the trial court must see that the record reflects each party's description of their historical lifestyle, including such elements as the marital residence, vacation home, cars owned or leased, typical travel and vacations each year, schools, special lessons, and camps for their children, entertainment (such as theater, concerts, dining out), household help, and *291 other personal services. One method for placing the parties' descriptions in the record would be by means of detailed certifications from each party, with an opportunity for cross-examination on the certifications. Alternatively, the judge may allow the parties' positions to be entered entirely through live testimony. [FN2] In either case, the judge must make detailed findings of fact as to the essential elements of the parties' actual lifestyle, without reliance upon such vague and subjective terms as "middle-class," "working-class," or "upper-class."
>
> FN2. The appropriate period to be covered by the certifications or the testimony will be determined by the judge, and will depend upon the circumstances of the marriage. For example, in a long term marriage with a consistent lifestyle, the last three years of cohabitation may be an appropriate period to consider. Where the parties' financial circumstances were inconsistent from year to year, a different period may be appropriate, all in the judge's discretion.

There was considerable reaction from the bar after this decision. The Appellate Division specifically rebuked those who thought the deferral of marital lifestyle to the modification application satisfied *Crews.* Fortunately, the Supreme Court granted certification; the New Jersey State Bar Association successfully sought *amicus curaie* status, and the Family Law Section briefed and argued before the Court for reversal of the stringent requirements of a stipulation or hearing in every case.

The case moved quickly. The Appellate Division issued its decision on May 20, 2003, *amicus* briefs were filed in the summer and oral argument before the Court was heard on November 19, 2003. On June 9, 2004, the Supreme Court released a unanimous opinion[11] authored by Justice LaVechia, who, of course, authored *Crews*.

In the first sentence of the opinion, Justice LaVechia acknowledged that the justices were "revisiting" their decision in *Crews*. Justice LaVechia framed the issue:

> Specifically, we are asked to reconsider our determination that the finding of the marital standard should be mandatory in every uncontested case that involves a provision for support.[12]

The primary holding of the Supreme Court, and the one that affects most of us on a daily basis, is being viewed as repudiating the *Crews* requirement. In reality, the Court reaffirmed the "economy and efficiency considerations that led to that directive," and only "reluctantly" concluded valid reasons existed to revisit the issue and allow flexibility.[13] The actual holding bears careful consideration and analysis:

> We now hold that in uncontested divorce actions, trial courts must have the discretion to approve a consensual agreement that includes a provision for support without rendering marital lifestyle findings at the time of entry of judgment. Our holding in Crews should no longer be read to require findings on marital lifestyle in every uncontested divorce. A trial court may forego the findings when the parties freely decide to avoid the issue as part of their mutually agreed-upon settlement, having been advised of the potential problems that might ensue as a result of their decision. *Even if the court does decide not to make a finding of marital standard, however, it nonetheless should take steps to capture and preserve the information that is available.*[14] (emphasis added)

Importantly, the retreat from the *Crews* mandate contains three conditions: 1) that a trial court may forego the findings, discretion still rests with the trial court; 2) the parties must freely decide to avoid the issue and must have been advised of the problems, counsel accordingly must continue to address with their clients marital lifestyle issues; and 3) the court should take steps to "capture and preserve" the information that is available, an indication of the enhanced importance of the CIS.

Noting that many suggestions had been advanced in the appeal, the Court referred the question of how best to capture marital lifestyle information efficiently and economically to the Supreme Court Family Practice Committee for its consideration and recommendation. Absent the previously mandated finding of marital lifestyle, the goal became to "preemptively ease the burden on parties and the courts when future modification applications arise following an uncontested divorce."[15] Unknown to the justices when they decided *Weishaus* was that the practice committee was actively reworking the CIS. It is respectfully submitted that the new CIS provides the mechanism to address the Court's concerns, as well as capture information about the other issue presented by the *Weishaus* appeal.

The second issue presented in *Weishaus* dealt with the source of funds to support marital lifestyle. Contributions from the husband's mother and leveraging of assets enabled Mr. and Mrs. Weishaus to create their disputed lifestyle. Although the holding obviated the need for the trial court to make lifestyle findings, and the Supreme Court did not need to address the source of the parties' income, the Court nevertheless noted the following:

> The finding of the marital standard is just that—a finding that is put to use in one of two settings: at the time of the court's equitable determination of an initial alimony award…, or later when a party seeks a modification of alimony. In the determination of the marital standard, the court establishes the amount the parties needed during the marriage to maintain their lifestyle. That is separate from the identification of the source of funds that supported that lifestyle, although that information is of use to a court when making an alimony award, or later when deciding a changed-circumstance application. In making either of those determinations, the court necessarily will consider whether there are sufficient presently available funds to sustain the marital standard. If so, then the court may order that that standard be maintained. But if not, due in part to the loss of previous sources of income that cannot be replenished from other sources, then obviously the marital standard cannot be maintained. In this case, a fact-sensitive determination concerning the parties' marital standard and an appropriate amount of alimony is unnecessary because the parties have reached agreement on alimony payments and have agreed to disagree on marital lifestyle.[16]

The new CIS is the appropriate tool to capture and preserve marital lifestyle information and to provide information about the funding of lifestyle. It is respectfully submitted that no other form or procedure is necessary, and the practice committee should focus its attention on creating instructions for the proper preparation of the CIS to fulfill the Court's mandate. Several of the changes in the new CIS make it particularly well suited to satisfy the Court's desire to ease the burden

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The Impact of Death on Divorcing and Divorced Spouses, Partners and Other Dependents

by Toby Solomon

Courts have endeavored to create remedies in situations where statutory or case law could leave divorcing and divorced spouses, former partners and other dependents without an equitable result in the event of death. Our courts have demonstrated a preference for fairness and equity over predictability and strict adherence to statutory construction or deference to legislative prerogative. This is particularly true when a decedent leaves the dependent in a situation where his or her property rights would be extinguished because the statute governing such a matter is not directly applicable or binding in a given matter.

Applying principles of fairness and equity, our courts have fashioned appropriate remedies in order to vindicate what it perceives as a wrong. The singular exception has been in preemption cases where federal law governs, such as cases in which the distribution of a pension plan is in issue.

This article gives an overview of cases illustrating our courts' solutions to situations in which an inequitable result may have occurred, but due to our courts' notions of fairness, a just and equitable result was reached.

DEATH *DURING* DIVORCE PROCEEDINGS

In *Carr v. Carr*,[1] the husband died during the pendency of the divorce, leaving his entire estate to his children by a former marriage. The wife brought an order to show cause to substitute the executor of the defendant's estate as defendant, to restrain the disposition of the decedent's estate, to continue *pendente lite* payments, and to request a hearing to resolve the issues of alimony, equitable distribution and fees. The deceased husband's attorney moved to dismiss the complaint and to dissolve the restraints.

The trial court held that the divorce action, and therefore the claims for alimony and equitable distribution, were terminated by Mr. Carr's death. The court reasoned that N.J.S.A. 2A:34-23, which provides for equitable distribution, did not apply.[2] Further, N.J.S.A. 3B:8-1, which provides for the "elective share" of a surviving spouse, was inapplicable as well.[3] The surviving wife's plight was termed a "black hole."[4] The court, however, viewed the action as essentially one of equity, worked outside both statutes for its result, and allowed the wife to amend her complaint to pursue equitable remedies. The wife amended her complaint to state grounds under quasi-contract, *quantum meruit*, and other equitable theories, and applied for leave to appeal, which was granted.

The Appellate Division affirmed the trial court's decision, dismissing the alimony and equitable distribution claims, and held that the trial court correctly construed the equitable distribution and elective share statutes to preclude statutory relief, but that equitable relief was available to the wife.[5]

The Supreme Court granted the wife's petition for certification, and agreed that the wife's entitlement to equitable distribution under N.J.S.A. 2A:34-23 abated with her husband's death, as it terminated the divorce action. Further, pursuant to N.J.S.A. 3B:8-1, she was not entitled to an elective share of his estate. Noting the general theory of equitable remedies calls for relief from the strict legal effects of given situations, and that the court's equitable powers are appropriate in domestic relations cases, the Court held that the constructive trust was an appropriate remedy in this type of case, as it has been recognized that the general principles with reference to unjust enrichment are the basis of constructive trusts, and are also at the basis of quasi-contractual obligations.[6]

In *Groh v. Groh*,[7] the plaintiff husband was 62 years of age at the time of the marriage in 1973, and the defendant wife was 45. The plaintiff retired in 1977. After filing a complaint for divorce in 1994, the plaintiff made an application for expedited discovery and an early trial date as a result of his age and ill health, to videotape his deposition, and to sequester his pension benefits should he die prior to the entry of a final judgment of divorce. The request to sequester his pension benefits was denied, and the plaintiff subsequently died before his deposition could be taken.[8] Thereafter, the plaintiff's son from a prior marriage moved to sequester the plaintiff's pension death benefits until a determination could be made on whether the benefits were subject to equitable distribution. This application was granted.

The defendant then moved to dismiss the plaintiff's complaint and release pension death benefits to her.

The plaintiff's estate argued that since all but four years of the plaintiff's pension was earned prior to the parties' marriage, the defendant would be unjustly enriched if she received the entire death benefit.The estate maintained that the pension death benefits were marital assets, and that the Court should establish a constructive trust pursuant to *Carr; supra*.[9] The defendant argued that the remedy of a constructive trust was intended to benefit a spouse widowed during the pendency of a divorce and not the other spouse's estate, and, therefore, *Carr; supra,* was inapplicable in this matter.[10]

The plaintiff's pension in this case was a qualified plan under the Employee Retirement Income Security Act (ERISA), which mandates that survivor benefits be automatically paid to a surviving spouse upon the death of the participant, unless both parties expressly consent in writing to an alternate payee.[11] ERISA's spendthrift provision also prohibited the assignment or alienation of retirement benefits during the pendency of a divorce.[12]

The Court held that the plaintiff's estate had no legal or equitable basis to invade the pension death benefit, and that the requirements of ERISA required distribution of the entire benefit to the defendant.[13] In this case, the Court was unable to affect an equitable result because federal law always preempts state law.

In the case of *Wasserman v. Schwartz*,[14] the issue of whether an equitable distribution of marital estate assets, including equitable distribution of a husband's pension and retirement accounts, should be permitted when the marriage was terminated by the husband's slaying of the decedent instead of by divorce was one of first impression. Dr. Steven Schwartz was convicted of killing his wife, and was sentenced to 20 years imprisonment. Mrs. Schwartz' estate brought Slayer's Act claims against Dr. Schwartz pursuant to N.J.S.A. 3B: 7-1 *et. seq.* This legislation enunciates the common law principle that is designed to insure that an intentional killer will not be permitted to benefit or profit from his or her wrongful act.

Mrs. Schwartz' estate also brought a wrongful death and survival action claims against Dr. Schwartz for compensatory and punitive damages. Partial summary judgment was entered, finding him liable as a matter of law for the injuries and wrongful death he inflicted upon his wife. The executor of Mrs. Schwartz' estate further argued that her estate should be entitled to an equitable distribution of the marital assets that accumulated during the 10-year marriage, including the retirement and pension plan assets. The executor argued that had the marriage not been terminated by Dr. Schwartz' slaying his wife, the marriage would have been terminated by divorce, and Mrs. Schwartz would have been entitled to equitable distribution of the marital assets. Dr. Schwartz argued that the estate of Roberta Schwartz had no entitlement to any of those assets or other assets.

The court analogized the situation to *Carr, supra*,[15] where the New Jersey Supreme Court relied on equitable grounds to permit the wife to obtain the benefit of assets in the marital estate. The court stated that the estate of Roberta Schwartz was in a similar situation with regard to the majority of the marital assets because of the manner in which those assets were held by the defendant.[16]

The court stated:

> [I]f the Court does not exercise its equitable powers in this matter to recognize Roberta Schwartz' interest in those retirement assets, the Estate of Roberta Schwartz may find itself, like Mrs. Carr, in a black hole.[17]

Quoting *Carr, supra*, the *Schwartz* court stated:

> The Supreme Court further noted that, 'courts should be responsive to legislation as expressive of public policy' and that in the exercise of common law jurisdiction, courts should rely on the public policies that form the basis of legislation even though the legislation itself may not be applicable in a particular matter.[18]

The *Schwartz* court additionally stated that:

> …the legislature's enactment of provisions which prevent a killer from obtaining a survivorship interest in a joint tenancy, or from receiving the benefits of the decedent's estate as a beneficiary…indicated the legislature's willingness to foster the public policy that a slayer should not profit from his crime.[19]

The *Schwartz* court held that it would be a grave injustice to allow the defendant to receive his wife's share of the marital assets that he obtained by killing her, and that public policy cries out against such a result.[20] In its effort to reach an equitable result, the court ruled that Roberta Schwartz' share in the marital property at the time of her death, together with any interest or gains, must be distributed to her estate by the defendant husband.

In the matter of *Kingsdorf v. Kingdorf*,[21] the Court sought a just result. The parties were married in 1984 and had no children together. Each had been previously married. The husband owned real property in Mays Landing, and the wife owned property in Cologne. Both New Jersey properties were subsequently transferred into joint names as tenants by the entirety. The parties thereafter separated, and in September 1999 the husband suffered a stroke, which rendered him completely incapacitated.

In February 2000, the husband's son, Charles, was appointed as guardian of the husband's person and property. The son (the plaintiff) then filed a complaint for divorce on his father's behalf. The only assets at issue were the two properties in Mays Landing and Cologne. The parties agreed that the husband would retain the Mays Landing property and the wife would retain the Cologne property.

At the uncontested hearing on July 12, 2000, the consent final judgment of divorce was signed, and the defendant signed a quitclaim deed transferring her interest in the Mays Landing property. The plaintiff's counsel withdrew his complaint and asked permission to leave so the defendant could proceed on her counterclaim. However, plaintiff's counsel did not reveal to the court, nor to the defendant that the husband had died. In fact, the defendant did not learn of the husband's death until more than four months later. The plaintiff's attorney then filed a motion to enter the divorce judgment *nunc pro tunc* to May 22, 2000, and to allow him, as co-executor of the husband's estate, to sign a quitclaim deed on behalf of the defendant, who would not sign the new deed.

The defendant filed a cross-motion seeking to vacate the final judgment of divorce, to declare the deed to the Mays Landing property null and void, and to make a determination that title to the Mays Landing property had passed to her as the surviving spouse as tenants by the entirety by operation of law. The defendant argued that the plaintiff had committed a deliberate fraud upon the court by failing to disclose that the husband had died. She further claimed that she was induced to give up almost the entire estate to provide for the husband's expensive long-term care at a point in time when the plaintiff and his attorney knew the husband was dead.

The trial court, however, concluded that the parties had reached a valid agreement prior to the husband's death, and that the agreement was enforceable because it was not unconscionable.[22] The defendant appealed.

"[D]eeply troubled" by the deception perpetrated by the plaintiff, the appellate court concluded that the plaintiff's conduct in creating the sham was so reprehensible that the subsequent judgment requiring the defendant to execute a deed in his favor could not be affirmed in the context of the divorce proceedings.[23] This result, the court stated, was dictated by the requirements of fairness and equity.[24] The court held that by virtue of the husband's death, the defendant became the legal owner of both properties, as a result of her right of survivorship, and that although the parties may have reached an agreement prior to the husband's death, it did not necessarily require that the agreement be specifically enforced if equitable considerations and principles suggested a different remedy.[25]

The question before the court in *The Matter of Estate of Noreen Di Bella*,[26] was if a spouse dies intestate while her divorce complaint is pending, who becomes administrator of her estate. Generally, when a person dies intestate the law provides that administration shall be granted to the surviving spouse.[27] Noreen Di Bella filed a complaint for divorce and died during the pendency of the litigation. The issue before the probate part was whether her estranged husband or her son from a prior marriage would be the administrator of Ms. Di Bella's estate.

Tino Di Bella, Noreen's estranged husband, argued that since he was the surviving spouse, he should be named administrator pursuant to N.J.S.A. 3B:10-2, which states: "If any person dies intestate, administration of the intestate's estate shall be granted to the surviving spouse of the intestate." Gabriel Fabius, Noreen's son from a previous marriage, argued that: 1) N.J.S.A. 3B:10-2 does not confer an absolute right on a surviving spouse, and 2) the court cannot apply the statute to reach an illogical result.

In appointing Gabriel as administrator of his mother's estate, the court reasoned that a widow does not have the exclusive right to administer the estate, but instead only has a preference. Further, the court found that in this case the appointment of Noreen's estranged husband as administrator would create a "toxic" conflict of interest. The court stated that if the matrimonial case were to be litigated, it is unclear whether the estranged husband would sit at the plaintiff's counsel table as administrator or the defense table in his personal capacity. It further questioned: If a settlement were to be explored, how could the husband as administrator approve the resolution of a claim against himself? The court also stated that "[o]ne should remain mindful of the fact when a legislative pronouncement, (here N.J.S.A. 3B:10-2) collides with the Rules of Court, (here the Rules of Professional Conduct), the latter will prevail."[28]

THE DEATH OF A FORMER SPOUSE

In *Maquiling v. Estate of Maquiling*,[29] the parties' property settlement agreement obligated the husband to maintain life insurance in the amount of $100,000 for the benefit of his wife. At the time of the husband's death one year later, he had maintained only $50,000 in insurance coverage for the wife's benefit. The court held that the wife could collect from the husband's estate what would have been due her had he complied with the property settlement agreement.[30] The court specifically noted that the agreement contained a provision making it "binding upon the respective heirs and executors of the parties," and stated: "[E]quity looks upon that as done which ought to be done."[31]

In *Jacobitti v. Jacobitti*,[32] the Supreme Court upheld the trial court's order that an 87-year-old divorced man create a trust fund from which monthly alimony payments would be made to his former spouse so long as she lived, even if she outlived her former husband. At the time of the parties' divorce in

1991, the plaintiff husband was 87 years of age, in good health and admittedly had the financial ability to pay any amount of alimony the court "may reasonably fix."[33] In contrast, the defendant wife was 19 years younger, suffered from multiple sclerosis, was confined to a wheelchair, and was totally dependent upon the plaintiff for her support.

The trial court required the plaintiff to pay alimony of $4,200 per month. Rather than requiring the plaintiff to maintain life insurance, the cost of which would be prohibitive due to his age, the court required he create a trust in the amount of $500,000 to secure his alimony obligation.[34] On appeal, the plaintiff argued that the order for a trust was prohibited under N.J.S.A. 2A:34-25, as it required him to pay alimony after his death. The appellate court affirmed the creation of the trust, but remanded the matter so the amount of the trust was "sufficiently funded" to secure the defendant's alimony payments during her lifetime.[35]

Although N.J.S.A. 2A:34-35 provides that "[a]limony shall terminate on the death of the payer spouse," the Supreme Court held given that the legislative intent in the 1988 amendments to the divorce statute to protect former spouses, and given the unique circumstances of this case (*i.e.*, the plaintiff's advanced age and inability to obtain life insurance and the defendant's debilitating physical condition and total dependency on the alimony for her support), the "trust is the appropriate equitable remedy to fulfill the legislature's intent in authorizing life insurance for the protection of a dependent spouse 'in the event of the payer spouse's death.'"[36]

In *Ross v. Ross*,[37] the plaintiff's second wife appealed from an order of the trial court entering qualified domestic relations orders (QDROs) after the death of the plaintiff husband authorizing the distribution of his pension plans and annuity to his former wife. The parties entered into a property settlement agreement, which provided that the defendant wife would receive half of the plaintiff's annuity and pension benefits plus the full amount of survivor benefits under his pension and annuity plans in the event of his death. One month after his divorce from the defendant, the plaintiff married the appellant. The plaintiff then died. one month subsequent to his remarriage.

The plaintiff's annuity and pension plans each stated that in the event of the participant's death, the beneficiary of the survivorship payments would be the participant's spouse, unless agreed to in writing by the spouse. Although the property settlement agreement stated that the defendant would be deemed to be the surviving spouse, the appellant never agreed in writing to this alienation to her survivorship benefits, as required by the plans.

The trial court was satisfied, after hearing the parties' motions, that the respective rights of the parties vested at the time the final judgment of divorce was entered by the court and the property settlement agreement incorporated the agreement into the judgment of divorce.[38]

On appeal, the critical issues were whether the property settlement agreement could itself be considered a QDRO, and whether the QDROs, which were entered after the decedent's death, were valid. The property settlement agreement satisfied the requirements of a QDRO regarding the money purchase plan, as it created a right in the defendant as the alternate payee and further specified the name of the plan and address of the participant and of the alternate payee, the amount or percentage of the money purchase plan to be paid of the participant's benefits, and the period to which the plan applied. However, the court held that the property settlement agreement lacked the requisite specificity regarding the other pension plan, which pursuant to ERISA would be paid to the appellant.[39]

The court further held that the required beneficiary change was not properly made regarding that plan, in that a QDRO was not entered prior to Mr. Ross' death, which would allow the proceeds to be alienated under ERISA. Therefore, the decedent's second wife was entitled to the proceeds of that plan as the decedent's surviving spouse. The court noted that it was obviously more equitable to satisfy the obvious intent of the property settlement agreement; however, survivorship benefits are governed by ERISA unless a valid QDRO or a property settlement agreement satisfies the QDRO prerequisites under the act. Moreover, federal common law preempts state law.

The court noted that the unfortunate result was that equity would not prevail.[40] The court further noted that because the former wife did not receive all of the benefits negotiated for and agreed to in the property settlement agreement by the reason of the impact of federal or state law, she may still be entitled to pursue her claim against other assets—if any remained in the decedent's estate—in order to carry out the intention of the property settlement agreement.[41] Therefore, the QDRO was affirmed regarding the money purchase pension plan allowing the survivor benefits to be distributed to the defendant. Regarding the other pension plan, the trial court was reversed, and was directed to distribute the survivor benefits to the decedent's second wife. With regard to the annuity, the court reversed and vacated the QDRO, but remanded the matter for determination regarding whether it could be alienated under federal or state law, or alternatively reversed and preserved for determination by the federal court should the issue be properly presented in that forum.

In *Knoczyk v. Knoczyk*,[42] the plaintiff wife and defendant husband were divorced on April 8, 1996. According to the final judgment of divorce, the defendant was to pay the plaintiff alimony of $200 per month for five years and then $100 per month until the plaintiff reached the age of 65. In addition, the defendant was required to maintain life insurance to secure his alimony obligation, with $20,000 worth of insurance for the first five years, and $15,000 thereafter, until his alimony obligation terminated. The defendant passed away approximately six-and-a-half years after the divorce. At that time, the plaintiff was 63 years of age and not remarried, and therefore entitled to an additional $2,000 in alimony payments.[43]

After making a claim to the defendant's insurance company for the proceeds of the life insurance policy, the plaintiff learned that the parties' two daughters were the named beneficiaries of the defendant's $15,000 life insurance policy. The plaintiff argued that she was entitled to the entire $15,000 policy because it was part of the bargained-for exchange in the divorce settlement. The executrices of the defendant's estate (the parties' two daughters and beneficiaries of the policy) claimed the plaintiff was only entitled to receive insurance for the remaining amount of alimony due her at the time of the defendant's death.[44]

Although insurance is required as "reasonable security" for alimony in many cases, the court found that there were no cases in New Jersey squarely addressing the issue in this instance where the insurance policy considerably exceeded the remaining alimony obligation. In looking to decisions from other states for guidance, the court held that although the plaintiff had an equitable interest in a portion of the policy proceeds, the insurance policy requirement was not intended to benefit an obligee with a windfall, and therefore the plaintiff was only entitled to $2,000 of the total proceeds.[45] In so holding, the court distinguished the facts of this case from *Jacobitti, supra*, in that there was no indication that the plaintiff in the within matter was dependent upon the $15,000 to maintain or achieve the marital standard of living.[46] The appellate court affirmed the decision for the reasons set forth in the trial court's opinion.

DEATH OF AN UNMARRIED PARTNER

In *The Matter of the Estate of Arthur Roccamonte, Sr.*,[47] the parties met in the 1950s. Arthur Roccamonte Sr. was the owner of a trucking business, was married and had two children. The plaintiff, Mary Sopko, was married with a daughter. Roccamonte pursued the plaintiff, and they embarked on an affair that endured for the rest of his life. At one point during the relationship, the plaintiff left for California because Roccamonte would not divorce his wife, but he convinced her to return and they resumed living together. Roccamonte provided the plaintiff with an affluent lifestyle. However, as time passed the plaintiff became increasingly concerned about her financial future in the event that she survived Roccamonte.

Roccamonte died intestate, and approximately seven months after his death the plaintiff commenced a palimony action against his estate, seeking a lump sum support award. For two years, the only issue was whether the action belonged in the Chancery Division, family part, or the Chancery Division, probate part. It ultimately ended up in the probate part. The plaintiff testified that Roccamonte repeatedly assured her in front of others, who so testified, that she had no cause for worry, as he would see to it that she was provided for during her life. The trial court ruled against her, finding that she failed to make a *prima facie* showing of a valid contract to make a testamentary disposition.[48]

The plaintiff appealed, and the case was dismissed on summary judgment. After a lengthy procedural history, seven years later the Supreme Court heard the matter. The plaintiff had exhausted her assets and, according to her attorney, was living in poverty, entirely dependent upon Social Security payments of under $1,000 per month and food stamps.

The Court relied on *Kozlowski v. Kozlowski*,[49] which was remarkably similar factually to the case, except that Roccamonte died, whereas Mr. Kozlowski left the plaintiff for another woman. In both cases, neither defendant had divorced his wife. Enunciating the principles used in *Kozlowski, supra,* the Court noted that it next applied those principles in *Crowe v. DeGioia*.[50] The Court found that in all three cases the plaintiffs had relied on the promises of the defendants to take care of them and support them for the rest of their lives. In *Kozlowski, supra,* and *DeGioia, supra,* however, the person charged with palimony was still alive to rebut the claim. This was the first time the New Jersey Supreme Court dealt with the issue of whether a promise of support is enforceable against a promisor's estate.

In *Kozlowski, supra,* and *DeGioia, supra,* the plaintiffs were awarded lump sum payments predicated on the present value for reasonable support for the plaintiff's life, based on tables of life expectancy. The *Roccamonte* Court remanded the matter to the Family Division to apportion the estate, ordering the plaintiff be paid a lump sum.[51] The Court applied equitable principles, and reached a decision to insure that one party had not been unjustly enriched and the other unjustly impoverished on account of their dealings.

THE DECEDENT'S OBLIGATIONS TO CHILDREN

The cases in New Jersey make it clear that obligations to one's children do not necessarily terminate upon death.

In *Della Terza v. Estate of Della Terza*,[52] the final judgment of divorce incorporated an agreement between the parties that the husband maintain the child of the marriage, Leah, as beneficiary of his life insurance policy until she became emancipated. After the husband remarried, he filed a designation of beneficiary form naming his present wife as primary beneficiary along with Leah and his child from his second marriage as contingent beneficiaries. An order was thereafter entered upon the wife's motion to provide proof that Leah was named as beneficiary pursuant to the final judgment of divorce. The husband, however, never complied with this portion of the order. He died two years later, and Leah sued, claiming a right to the insurance proceeds.

The basic issue presented in this case was whether an obligation to maintain life insurance for the dependent child as beneficiary incorporated into a judgment of divorce translated into a right on the part of the beneficiary to seek the proceeds of the policy paid to another because the obligor failed to comply with the terms of the judgment.[53] The trial court held that such a provision contained in the judgment of divorce to maintain the child as beneficiary on the life insurance policy until emancipation created an equitable assignment if such a designation has not in fact occurred.[54] The case was one of first impression in New Jersey because the child of the second marriage was directly involved.

The Court held that the trial court's award of the entire proceeds of the insurance benefit of $80,337.88 to Leah was premature, and therefore vacated the trial court decision. The Court held that since the amount of the policy to be maintained was not specified, "fair concepts of equitable assignment and reasonable expectation entitled plaintiff only to the value of the insurance policy at the time of the judgment of divorce enhanced by such increases as may be represented by generally applied salary improvements decedent would have received in the position he then held until the date of his death."[55]

In *Black v. Walker*,[56] Ms. Black and Mr. Walker, who never married, had a child in 1976 and entered into an agreement providing for the support of the child. The agreement, and subsequent amendments, never addressed the payment of the child's college expenses. In 1993, Ms. Black brought an action to compel Mr. Walker to pay for, *inter alia,* the child's college expenses. The request was granted, and Mr. Walker died in 1994.

The Appellate Division upheld the trial court's decision, ordering the decedent's estate to substantially contribute toward his daughter's college costs. In applying New Jersey law, the court stated that New Jersey had a strong interest in ensuring that the child would receive funding from her father's estate for her college education.[57] The court stated:

> Although the importance of this express public policy (education) alone might be enough to tip the scales in favor of applying New Jersey law, other family-law precedent outside the context of the right to college funding, confirms the overriding weight our courts ascribe to a child's New Jersey domicile and residency in the choice-of-law.[58]

In so holding, the court found that the decedent left adequate resources to justify the order, taking into account the needs of his two younger children.[59]

In the matter of *Kiken v. Kiken*,[60] the final judgment of divorce entered on December 22, 1982, provided that the parties would pay for the college education of their child, David, commensurate with their respective income and assets at the time David commenced college. Mr. Kiken died in 1986, when David was nine years old. He left an estate valued between 10 and 16 million dollars. In December 1994, David was granted early admission to the University of Pennsylvania, and his mother sought to compel her former husband's estate to pay the child's college expenses.

The plaintiff, a substitute teacher, asserted that because of the disparity between her income and the value of the decedent's estate, the decedent's estate should pay for the entire cost of David's college education. The executor opposed the motion, arguing that the obligation to pay for David's college expenses terminated on Mr. Kiken's death. The Chancery Division denied the plaintiff's motion, finding that the agreement incorporated into the judgment of divorce did not bind the decedent's estate. The Appellate Division affirmed.

The Supreme Court granted the plaintiff's petition for certification, and held that under N.J.S.A. 2A:34-3, the decedent's estate was bound by its obligation to contribute to the cost of his son's college education.

The Court reasoned that the parental duty of support is an obligation enforceable at law, and that the absence of a provision that the deceased parent's obligation terminates on death, created the inference that the obligated parent intended to bind his estate. Moreover, the statutory scheme suggests that the Legislature contemplated a parent's support obligation to be binding on his or her estate, since it is specifically set forth that alimony terminates upon the death of the payor, but there is no such provision for child support.[61] The Court liberally construed the statutory scheme to reach a result it considered equitable.

CONCLUSION

The above cases illustrate the court's exercise of its inherent equitable jurisdiction to craft equitable remedies. Courts have relied on public policy that forms the basis of legislation even though the legislation itself might not be applicable in a particular matter.[62] ■

ENDNOTES

1. 120 N.J. 336 (1990).
2. *Id.* at 342.
3. *Id.* at 344.
4. *Id.* at 346 n.2.
5. *Id.* at 350-51.
6. *Id.* at 351.
7. 288 N.J. Super. 321, 672 A.2d 262 (Ch. Div. 1995).
8. *Id.* at 263.
9. 120 N.J. 336.
10. *Id.* at 263-64.
11. 28 U.S.C. at 1055(c).
12. 29 U.S.C. at 1056(d).
13. *Id.* at 264.
14. 364 N.J. Super. 399 (Ch. Div. 2001).

15. 120 N.J. at 336.
16. *Id.* at 405.
17. *Id.* at 405-06.
18. *Id.* (*quoting Carr, supra,* 120 N.J. at 350).
19. *Id.* at 407. (*quoting In re estate of Diane L. Hackl,* 604 N.W. 2nd 579 (Wis. Ct. App. 1999)).
20. *Id.* at 409.
21. 351 N.J. Super. 144 (App. Div. 2002).
22. *Id.* at 152.
23. *Id.* at 155.
24. *Id.*
25. *Id.* at 157.
26. 372 N.J. Super. 350 (Ch. Div. 2004).
27. N.J.S.A. 3B:10-2.
28. *Id.* at 6 n.2.
29. 211 N.J. Super. 69 (Law Div. 1986).
30 *Id.* at 73.
31. *Id.*
32. 135 N.J. 571 (1994).
33. *Id.* at 573.
34. *Id.* at 574.
35. *Id.*
36. *Id.* at 574-75 (*citing* N.J.S.A. 2A:34-25).
37. 308 N.J. Super. 132 (App. Div. 1998).
38. *Id.* at 140.
39. *Id.* at 155-57.
40. *Id.* at 158.
41. *Id.*
42. 367 N.J. Super. 551 (Ch. Div. 2003), *aff'd* 367 N.J. Super. 512 (App. Div. 2004).
43. *Id.* at 554.
44. *Id.* at 555.
45. *Id.* at 562-63.
46. *Id.* at 563.
47. 174 N.J. 381 (2002).
48. *Id.* at 388.
49. 80 N.J. 378 (1979).
50. 90 N.J. 126 (1982).
51. *Id.* at 398.
52. 276 N.J. Super. 46 (App. Div. 1994).
53. *Id.* at 49.
54. *Id.*
55. *Id.* at 51.
56. 295 N.J. Super. 244 (App. Div. 1996).
57. *Id.* at 256.
58. *Id.*
59. *Id.* at 263.
60. 149 N.J. 441 (1997).
61. *Id.*
62. *See supra* note 16.

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CIS and Marital Lifestyle

Continued from Page 176

upon parties and trial courts in modification applications.

First, the revised budget pages with the modified two-column approach expressly requires an analysis of joint marital lifestyle expenses and a comparison to current lifestyle. Proper completion of the CIS demands a careful reporting of the expenses during the marriage and expenses at the time of filing. For future applications, the marital lifestyle has been recorded, meeting a primary concern of the Court, and can be quickly copied over. The current lifestyle expenses can be easily compared, and any differences highlighted.

Second, the income questionnaire, a totally new section for the CIS, directly addresses the source of funds for payment of lifestyle expenses. Especially useful as an advocacy tool is question #16, Explanation of Income or Other Information. The answer to this question is the appropriate place to insert information about gifts, sales of assets, etc.

Third, the modified balance sheet of family assets and liabilities also addresses the issue of source of funds. A review of the balance sheet can provide information to the trial court about debt service and the status of family assets. The differentiation between exempt assets and those available for equitable distribution informs the court whether assets not distributed may nevertheless be available for income production to help with alimony needs.

Finally, Part F, Statement of Special Problems, provides an excellent opportunity to set forth specifics about marital lifestyle and its funding, such as "we lived on assets, exercise of stock options, generosity of parents and in-laws" or "my spouse was able to provide travel and meals, working vacations, etc. because of employment" or "she has a half-million frequent flyer miles."

The new CIS, which was not submitted to the Supreme Court before the *Weishaus* decision, is designed to collect precisely the type of information deemed by the Court to be essential for proper consideration of future modification applications. Careful completion of the CIS must be a priority in every case. In recognition of the importance the Supreme Court placed upon the information gathered in the CIS, it is the most important pleading in virtually all dissolution cases. ■

ENDNOTES

1. Rule 5:5-2 mandates filing of a CIS in all family part cases, except in those in which agreement has been reached.
2. Hymerling, 25 *NJFL* 57(2004). Such a statement is presumably more than hyperbole since the author is the longstanding chair of the Family Part Practice General Procedures Subcommittee, and was instrumental in the adoption of the original CIS and every modification in the past 20 years.
3. 164 NJ 11(2000).
4. *Id.* at 26-27.
5. *Weishaus v. Weishaus*, 180 NJ 131 (2004).
6. 360 N.J. Super. 281(App. Div. 2003).
7. 360 N.J. Super. 281, 287.
8. 360 N.J. Super. 281 (App. Div. 2003).
9. *Id.* at 290.
10. *Id.*
11. 180 NJ 131 (2004).
12. *Id.* at 134.
13. *Id.* at 143.
14. *Id.* at 144.
15. *Id.*
16. *Id.* at 145.

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The Art of Valuing and Allocating Real Estate Investments

by Robin C. Bogan

As more investors shift from the stock market to the real estate market, family law practitioners are faced with challenges in valuing and allocating these investments. The thorny briarpatch of real estate investments is fertile ground for creative lawyering. Whether it is a shore house, a condo in Florida, commercial property, new construction, or a rental property, knowing the law, tax implications and your client's investment intentions will enable you to fashion a settlement or advance an argument at trial that is favorable to your client.

Real estate is an attractive investment due to significant tax benefits, such as depreciation write-offs, as well as the ability to generate cash flow.[1] Additionally, real estate can serve as a hedge against inflation.[2] Real estate also has no correlation with the stock or bond markets.[3] According to Lend Lease, a real estate services business, historically, the years of negative returns from stocks and bonds far exceed the years of negative returns real estate has experienced.[4]

To illustrate the shift toward investing in real estate, more investors are considering real estate for inclusion in their investment portfolios.[5] Real estate has outperformed stocks and bonds from the standpoint of the total return per unit of risk.[6] Real estate is an excellent risk reducer in a portfolio with stocks and bonds.[7] Evidence indicates that real estate is attractive to investors seeking to preserve their capital, and who need to earn a comfortable rate of return.[8] Even the governing council for New Jersey's state pension fund voted on November 8, 2004, to adopt a more aggressive investment strategy by moving from stocks and bonds to real estate, hedge funds and non-traded stocks.[9] The resolution provides that 13 percent of the $66 billion pension fund will be invested into these three alternative categories over the next five to seven years.[10]

The family law practitioner must also be aware of the drawbacks associated with real estate investments. In an economic recession, real estate prices can be hit hard, as was demonstrated in the early 1990s.[11] Real estate investments are less liquid, and it may require a longer period of time to sell the property than is required to sell stocks and bonds.[12] There is also risk associated with ownership of real estate. Risks include market risk as well as the reliability of tenants. Valuations of real estate are much more difficult to establish.[13]

Valuing and allocating real estate investments is an art, not a science. As a result, the family law practitioner and the real estate expert must work together in tandem to be successful in persuading a trial judge regarding the proper value and allocation. To provide the best representation of a client with real estate holdings, the family law practitioner must have a working knowledge of real estate valuation techniques, carefully select the real estate expert, determine the dates for valuation, engage in discovery, and analyze and address the tax consequences. Similar to the artist who envisions a painting before picking up a paintbrush, the family law practitioner with a thorough and thought-out approach to real estate holdings will increase the probability of a favorable picture for his or her client.

HAVE A WORKING KNOWLEDGE OF REAL ESTATE VALUATION TECHNIQUES[14]

The methodology the real estate expert utilizes will vary based upon the type and use of the property being valued. For properties that are influenced by owner-occupancy, the favored method of assessing the value of real estate is the sales comparison method.[15] Such properties include single-family homes, multi-family homes, condominiums and commercial property.

This method involves an appraiser locating, researching and comparing recent sales of comparable or similar properties to the property being appraised.[16] In comparing the similar properties to the subject property, the appraiser takes into consideration physical characteristics, amenities, and proximity to subject property, as well as the terms, time and conditions of these sales.[17] Adjustments are made to increase or decrease the price, based on significant differences between the comparable properties to the subject property. A real estate appraiser should introduce evidence of comparable sales through his or her testimony.

It is important for the family law practitioner to recognize that these adjustments reflect the appraiser's *opinion* of market reaction.[18] As a result, like bees to honey, the family law practitioner should hone in on these adjustments during cross-examination.

The income approach is based upon the rental value of the property.[19] This method is most appropriate when the property is acquired to generate income.[20] For example, the income approach would be used to value a 40,000-square-foot office building in which the owner is operating a business. A real estate expert must look through the eyes of an investor in determining value. Income produced by the property can be measured either by the rents the owner actually received or by the rental value of comparable rental property.[21]

The least utilized method of valuation in matrimonial cases is the cost approach.[22] This method is only used when reliable data cannot be obtained by an analysis of comparable sales or the capitalization of income methods.[23] Properties that are valued using the cost approach have unique or special uses, such as laboratory or specialized manufacturing facilities. This valuation technique attempts to relate the cost of reproducing or replacing an existing dwelling to market value.[24] To accomplish this, the replacement cost of the existing dwelling is estimated, and the estimate is adjusted for any accrued depreciation.[25]

The most difficult property to appraise is vacant land. Although valuation of vacant land appears to be a simple task, it has the potential to be very complex.[26] Two pieces of property that appear identical may be completely different, and those differences may have a considerable impact on the property's value. The real estate expert must consider the land's physical, functional, and economic attributes.[27]

Vacant land is more susceptible to fluctuations in value than improved property.[28] Vacant land also experiences greater swings in prices, as well as in the ability to finance acquisition and development costs.[29] Overall, land is a more volatile investment, and thus the date of valuation may be of the utmost importance in such cases.[30]

The real estate expert utilizes the highest and best use analysis to determine the best use for vacant land.[31] Sometimes determining the highest and best use can require considerable research and analysis.[32] There may be zoning restrictions on the property.[33] Easements and encroachments may impact the value.[34] Environmental considerations include wetlands, steep slopes, endangered species, and subsurface characteristics, such as minerals or airspace restrictions.[35]

Zoning, building codes, environmental laws and other land use regulations assist the real estate expert in determining the land's use.[36] Obtaining such information may require the real estate expert to consult with engineers, town planning boards, boards of adjustment, and the Department of Environmental Protection. Tax maps and deeds must also be closely scrutinized to determine whether easements or other restrictions apply.

Before trial, the family law practitioner must be fully familiar with the real estate expert's methodology. The family lawyer must also understand why the real estate expert utilized a particular approach and why other approaches were not used or did not provide an accurate assessment of value. Moreover, the lawyer should be intimately familiar with the real estate expert's research, the purpose of the research, and how the real estate expert's findings impacted the value of the property. The best real estate expert cannot try the case. It is imperative for the family lawyer to fully understand every aspect of the property involved, as well as to raise the appropriate legal arguments, so the real estate expert is able to provide the best presentation concerning value.

SELECTING THE REAL ESTATE EXPERT

An appraisal of real estate is an *estimate* of value. As a result, it is critical to select an appraiser who is qualified and provides a well-developed, documented, and unbiased estimate of value.[37] A review of the cases reveals that the appraiser's credibility and the report's thoroughness and objectivity are the most important factors to convince a court to adopt one party's conclusions over another's.[38]

The appraiser's demeanor and presence is very important. The appraiser selected should be articulate, organized, thorough, and comfortable explaining his or her findings on direct examination. Likewise, the appraiser must persuasively defend his or her findings on cross-examination. If you are considering hiring a real estate expert you have not seen testify, contact other family lawyers who can provide an assessment of the appraiser's strengths and weaknesses during trial. An appraiser who provides an accurate assessment of value may be worth very little if he or she becomes rattled on the witness stand. The appraiser must be able to survive hostile challenge and remain sufficiently credible to persuade a trier of fact that his or her appraisal is a better expression of value than the appraisal put forth by the other party's expert.[39]

Appraisals carry more weight if the appraiser's credentials are unassailable.[40] Credentials include education, experience, visibility, and involvement in professional associations.[41] Experts testifying about the value of the real estate investment may be impeached on their qualifications. It is also important to be knowledgeable about the various ethical and professional codes governing valuation practice and to ensure that the appraiser hired has complied with those codes.

In 1998, Governor Christie Whitman signed a law requiring that appraisals of all real estate must be performed by a licensed or certified appraiser.[42] Thus, important criteria in selecting an appraiser are that he or she is currently licensed or certified, and is in good standing with the New Jersey Real Estate Appraiser Board.[43] Under New Jersey law, there are three licensing levels of appraisers under New Jersey's Real Estate Appraiser Board.[44] Two levels—licensed and certified residential real estate appraisers—may appraise real estate subject to limitations concerning the type of property and value.[45] A certified general real estate appraiser receives a comprehensive license that enables him or her to appraise any and all properties.[46]

Select an expert who is a member of the Appraisal Institute, a professional association of real estate appraisers.[47] The Appraisal Institute awards designations for members who have met rigorous requirements that include educational requirements, passing numerous comprehensive examinations, and experience requirements that include thousands of hours.[48] The MAI designation (member, Appraisal Institute) is held by appraisers who are experienced in valuing commercial, industrial, and residential property, and who advise clients on investing in real estate.[49] The SRA designation (senior residential appraiser) is held by appraisers who specialize in residential real estate.[50]

A few colleges also have advanced degrees in real estate. New York University offers a master of science in real estate.[51] The Wharton School of the University of Pennsylvania provides a Ph.D. program in real estate.[52]

Know the appraiser's background, education, and experience in valuing the type of real estate investment.[53] An appraiser fully qualified to value single-family dwellings may not have the particular knowledge and expertise needed to properly appraise a farm.[54] Additionally, consider whether the real estate expert regularly performs appraisals in the area where the property is located. It is important for the real estate expert to be familiar with the area. Quality of school systems, as well as access to highways, shopping malls, and hospitals, may be important considerations in property valuation.

In most cases, it is more advantageous for your client to hire his or her own real estate expert than to utilize a joint expert. Clearly, this decision is case sensitive, and depends on a client's financial resources and the real estate investments involved. One advantage to a party hiring his or her own expert is that the family lawyer can review an initial draft of the report. If any deficiencies exist in the draft, they can be corrected prior to issuing the final report. For example, if the comparable properties are located too far from the subject property, the family lawyer may ask the appraiser to obtain other comparables that are closer in proximity.

The other advantage is that the family lawyer can utilize the expertise and insight of the real estate appraiser to not only assist with the real estate expert's direct examination, but also to assist with the cross-examination of the other party's expert. The real estate expert should have a tremendous amount of input. The appraiser can also educate the family lawyer regarding the consequences of a possible disposition of the real estate investment.[55] Being aware of all disposition alternatives provides the family lawyer with the tools for creative structuring that may lead to an overall settlement.[56] Retaining an expert, however, does result in increased costs, and the party must quickly clear the hurdle of the initial perception that his or her expert is biased.

If the parties have chosen to utilize one appraiser, on cross-examination the family lawyer should explore the differences between the comparables and the subject property that will change the value in the client's favor. Areas for cross-examination may include differences in neighborhood characteristics, distance from the subject property, date of the sale, length of market exposure, availability of substitute property on the market, as well as other conditions affecting pricing and financing. The family lawyer should also question the appraiser on whether the sale was at arms-length and whether there were any encumbrances at the time of the comparable sale.

If a real estate expert is court appointed or is hired as a joint expert, ideally he or she should be someone who has worked with both attorneys. If both attorneys have had prior favorable dealings with the real estate expert, there is a greater chance that the expert will be able to assist the parties and their attorneys. In most cases, if one expert is being utilized, either cost is an issue or the parties' mind set is to try and resolve the case. The role of the real estate expert then becomes less adversarial and more to assist the parties in working out their differences based upon the real estate expert's findings concerning the property's value. If there is significant real estate involved, or the divorce case is highly contentious, using a joint real estate expert is not recommended.

If a case with a joint real estate expert or court-appointed expert goes to trial, it may be worthwhile to hire another appraiser to review the joint expert's report. The guidance another appraiser could provide to prepare the family lawyer for cross-examination of the joint appraiser is invaluable. The client also avoids having to pay the appraiser to testify.

Selecting a real estate expert should be a carefully planned process that is often glossed over by the family law practitioner. Choosing the right real estate expert may be the difference between a favorable outcome for your client and a disastrous one. Take the time in the beginning of your case to select the real estate expert who is best suited for your case. The planning, research, and preparation in the beginning will assist you in avoiding costly mistakes.

DETERMINING THE DATE FOR VALUATION[57]

In *Painter v. Painter*, the Court held that the termination date for determining property subject to equitable distribution is the date the complaint for divorce is filed.[58] As the case law developed, absent extraordinary circumstances, the date of complaint also determined the date those assets should be valued.[59]

The case of *Bednar v. Bednar* explained that equitable principles required a common valuation date for marital assets such as the date of the complaint or the date of the hearing, but there was no iron-clad rule.[60] The date of evaluation depended on the nature of the asset and any compelling circumstances demanding equitable consideration.[61]

In the 1988 decision of *Scavone v. Scavone*, Judge Conrad W. Krafte wrote a treatise on passive and active assets and the valuation dates that applied depending upon the nature of the asset.[62] The Court defined passive assets as those whose value fluctuations are exclusively from market conditions.[63] Active assets were defined as those involving contributions or efforts toward the asset's growth and development, which directly caused an increase in the asset's value.[64]

In *Scavone*, the controversy was the valuation date of a seat on the New York Stock Exchange, which was solely in the husband's name. The parties stipulated that the seat was a passive asset, the value of which fluctuated with the market, and the increase in value was not due to either party's contributions. The pivotal question was whether this passive asset should be valued as of the date of the divorce complaint in 1985 or the date of distribution in 1988. Applying the principles Judge Krafte articulated in *Scavone*, the Court determined that the proper valuation date was the date of distribution.

The principles that Judge Krafte set forth in *Scavone* after reviewing New Jersey case law is summarized in the following table:

	PASSIVE	**ACTIVE**
Immune Asset (Pre-marital, gift, inheritance)	Not distributable according to *N.J.S.A. 2A:34-23*; not subject to equitable distribution.	1) If the increase in value is brought about solely by efforts of owner, value is not distributable; 2) If the increase in value is partially or wholly due to non-owner's efforts distributable as of *date of distribution*.
Contemplation of Marriage	Distributable and incremental value determined as of *date of distribution*.	Distributable and incremental value determined as of *date of complaint*.
Joint Asset Acquired During the Marriage	Distributable. Valuation as of *date of distribution.*	Guiding principle set forth in *Bednar v. Bednar.*[65] Unless there is fraud or bad faith, incremental value is distributable and value is determined at *the date of distribution* unless the increment results from active participation of one party with no contribution by the other, then the value is determined as of the *date of complaint*.
Asset Acquired During Marriage in One Name	Distributable. Value determined as of *the date of distribution*.	Distributable. Value determined at the *date of complaint*.

Before the real estate expert begins the appraisal process, the family law practitioner must identify and consider: 1) how the property was acquired (in contemplation of marriage, during the marriage, or whether the asset is immune); 2) whether the asset is active or passive; and 3) the position to be advanced regarding the valuation date.

Valuation becomes tricky when there is a dispute over whether the increase in value of an immune asset is active or passive. The typical approach when representing the client alleging that the property is an active asset is to value the asset twice, for the date of the marriage (or the date of acquisition if the asset was acquired during the marriage) and the date of distribution.[66] The difference in value may be subject to equitable distribution.[67] The question then becomes how to determine which portion of the appreciation is passive due to market forces and which portion of the appreciation is active and based upon the efforts of either party. New Jersey law does not provide the family lawyer with direction on how to calculate active or passive increases. This provides an opportunity for creative lawyering.[68]

The real estate expert is the key to providing the basis for the increase. While your client will testify in detail regarding his or her contributions, the real estate expert must provide sufficient credible evidence linking the client's contributions to the increase in value. Additionally, the real estate expert must distinguish between the value created by economic factors alone and the growth in value that was attributed to the parties' respective contributions.[69]

An equally important consideration when representing a non-owner spouse who is claiming that an immune property is an active asset is his or her contributions to the marital partnership. A non-spouse's efforts are not limited to contributions associated with the property itself.[70] In *Valentino v. Valentino,* the Appellate Division affirmed the trial court's decision to award 10 percent of a mini strip mall to the wife that the husband acquired prior to the marriage and then used as a gas station.[71] In awarding the wife 10 percent of the increase in value, the trial court considered that while the husband devoted his time to the gas station the wife cared for the children, maintained the home, and worked part-time.[72] The court recognized that the wife's contributions to the home and children allowed the husband to work at his business and pay down the mortgage on the property.[73]

Further, *Sculler v. Sculler,* a case of first impression, set forth the burden of proof that applies when a non-titled spouse seeks distribution of an immune active asset.[74] The trial court explained that initially the spouse asserting immunity bears responsibility for establishing the immunity.[75] Once that immunity is proven, the appreciation will be immune unless the non-titled spouse can demonstrate that the increase was due to the efforts (either completely or partially) of the spouse requesting equitable distribution of the increase.[76] Again, the real estate expert's involvement is priceless in assisting the family lawyer to meet this burden.

While entire articles have been written on valuation dates and active and passive increases, identifying the issues is an important first step. At the very beginning of a matrimonial case involving real estate, determine your position on the appropriate valuation date. If your client is contending that property is active or passive, discuss with your real estate expert what additional appraisals or research must be performed to strengthen the position most desirable to your client.

ANALYZE AND ADDRESS TAX CONSEQUENCES[77]

To achieve the best result for your client through trial advocacy or settlement negotiation, understanding the tax consequences associated with real estate investments is imperative. The key is to first consult an accountant. The accountant should meet with the client to determine the client's preferences concerning selling or keeping real estate investments. After taking those preferences into consideration, as well as the potential tax benefits or ramifications associated with holding or transferring those investments, the accountant should provide the client with alternatives and recommendations on whether property should be retained, sold, or distributed. As part of this analysis, the accountant should also determine hypothetical tax consequences, even if there is not a foreseeable event to trigger the tax.

Being informed concerning the provisions of the Internal Revenue Code and how those provisions could affect your client is also advantageous. For example:[78]

1. Section 121(b) allows exclusion of up to $500,000 of capital gain on the sale of a primary residence if you are married and file a joint return or $250,0000 if you file an individual return. To qualify for this exclusion, you must live in your principal residence for two out of the five years before it is sold. Thus, tax planning for the real estate investor may include moving into an investment property that is subject to capital gains, utilizing that property as a primary residence for two years, and then selling the property.
2. Under Section 1031 of the Internal Revenue Code, if an investor owns property and wants to sell that property to purchase another piece of real estate, there is a way to defer paying capital gains tax. Known as the Starker exchange (or like-kind exchange), it requires an investor to identify a replacement property within 45 days of selling the relinquished property, and to close within 180 days of the previous sale. The investor is prohibited from having any access to the sale proceeds from the relinquished property. The sale proceeds must be held in escrow. If the exchange is successful, the tax basis of the relinquished property becomes the tax basis of the replacement property. Thus, payment of capital gains is delayed. Until recently, an investor, after effectuating a Starker exchange, could move into the property for two years and claim the Section 121(b) exclusion. Section 641 of the American Jobs Creation Act of 2004 recently plugged that loophole.[79] Now an investor effectuating a Starker exchange who moves into the subject property cannot claim the Section 121(b) exclusion unless he or she has resided in the property as his or her primary residence for at least a five-year period.
3. Section 453A of the Internal Revenue Code provides a special way of reporting gains from sales of property when at least one payment is received in a tax year after the date of sale. This is known as the installment sale method. Under this method, gains are prorated and recognized over the years in which payments are actually received. Generally, the amount of taxable gain in a given year is determined by multiplying the payments received in that year by the gross profit percentage on

the total sale. The gross profit percentage is the total profit (total price less total cost) divided by the gross selling price.

4. If your client owns rental real estate and has historically shown income in excess of $100,000, they may be subject to the Passive Activity Rules (Section 469). In general, a rental activity is treated as a passive activity. The provisions of Section 469 of the code place restrictions on the amount of losses from rental real estate that can be currently deducted. Passive activity losses are instead carried over indefinitely until they can be applied against passive activity income. It is important to note that, if rental real estate with these *suspended* losses is transferred incident to a divorce, the cost basis of the transferred interest is increased by the amount of the unused losses. This may change your calculation of the projected gain or loss on the sale of rental real estate.
5. If your client is a real estate dealer, certain restrictions apply. Real estate dealers are considered to be in the trade or business of buying and selling real estate. Generally (there are specific exceptions), dealers in real estate cannot take advantage of the installment sale provisions discussed earlier, but must report income from the sales of real estate in the year the sale occurs, regardless of when the proceeds are actually received, according to Section 453. Additionally, dealers in real estate cannot take advantage of the lower capital gains rates enjoyed by most individuals on the sale of long-term capital assets, unless the property is clearly being held for investment purposes, according to Section 1236. Dealers in real estate must otherwise report income from real estate sales as ordinary income. These are general rules; however, certain exceptions to these rules may apply depending upon the specific circumstances.
6. Publication 504 explains tax rules for individuals who are divorced or separated from their spouse.[80] Publication 544 provides information concerning the tax consequences of the sale or disposition of assets.

Potential tax implications are not limited to federal taxes, thus consulting your accountant about New Jersey taxes is also important. While many state laws mirror those of the federal government, this is not universal. In New Jersey, for example, there is no distinction between capital gain income and other sources of income such as wages, interest, and dividends. All income is subject to the same tax rate. Further, New Jersey does not allow capital losses to be deducted, but instead only allows such losses to be recognized to the extent of capital gain. This is not always the case in other states.

After the accountant has identified the client's options and set forth potential tax implications, the next step is to determine the trial or negotiation strategy that is most favorable to the client under New Jersey's law on equitable distribution of property. The New Jersey Legislature has provided that when equitably distributing property the court is to consider the "tax consequences of the proposed distribution to each party."[81] Similarly, New Jersey case law directs our courts to consider tax implications in ascertaining an equitable distribution of property.[82] The New Jersey Supreme Court in *Painter v. Painter* held that it is not improper for a court to give appropriate consideration to legitimate tax considerations to ensure that the most equitable distribution of property is attained.[83] Almost 10 years later, in *Dugan v. Dugan*, the court concluded that "potential federal tax consequences should be considered in determining equitable distribution."[84]

It was not until *Orgler v. Orgler* was decided in 1989 that the Appellate Division provided guidance on how potential tax consequences should be addressed.[85] The court held that "hypothetical tax consequences upon the future sale or transfer of marital assets should not be deducted from present value for equitable distribution purposes."[86] In *Orgler*, the husband argued that the trial court erred in not deducting hypothetical taxes he may pay on the future sale of the assets distributed to him.[87]

After reviewing the reasoning from out-of-state cases, the court determined that the hypothetical tax was "simply too speculative to permit a reduction in value."[88] The court reasoned that there may never be a sale or transfer of the asset during the ex-spouse's lifetime.[89] Upon the ex-spouse's death, the basis of the asset would be stepped-up to the property's fair market value resulting in no tax consequences.[90] Furthermore, if the asset is subsequently sold, the taxes incurred would depend on the "tax rate applicable at that time and the ex-spouse's tax bracket."[91] The court concluded that deducting hypothetical taxes from present value frustrates the trial court's basic function to assure that the most equitable distribution of property interests is attained.[92]

Orgler stands for the following proposition: Actual tax consequences should be deducted and theoretical taxes are to be *considered* in the distribution, but not subtracted in the valuation analysis.[93] Thus, if the court directs parties' real estate investments to be sold, or the parties agree to sell an investment property, the actual taxes and costs associated with the sale must be deducted. In contrast, theoretical tax consequences should affect the percentage allocation of the asset being distributed, not the value.[94]

There has been little direction given to the bench or bar regarding how a court is to consider theoretical taxes on a distribution issue. In *Goldman v. Goldman*, the Appellate Division affirmed the trial court's decision to award the defendant 40 percent of the plaintiff's interest (instead of 50 percent) in a real estate investment to account for hypothetical taxes.[95] Clearly, the basic premise is that the more speculative the tax consequences, the less impact on the percentage.[96] The larger the potential impact or the more certain that there will be tax ramifications upon a sale, the greater impact on reducing the percentage of the real estate investment being distributed.[97]

If you are representing a client who intends to take title to a real estate investment, present the court with information concerning the basis. The occupying spouse will incur capital gains on the other spouse's gain. In 2003, the maximum tax rate for net long-term capital gains were reduced from 20 percent to 15 percent and from 10 percent to five percent for taxpayers in a 10 percent or 15 percent bracket.[98]

It is also important to obtain all records necessary to determine the title holder's tax basis despite whether hypothetical taxes are considered. When the property is subsequently transferred long after the divorce, there may be little communication between the parties when the property is subsequently transferred or the records may be discarded by the non-title holding spouse.[99]

When advocating that hypothetical tax consequences should affect the percentage allocation, there are two important considerations. First, the age of the recipient spouse:[100] The older the recipient, the more likely the asset will be sold.[101] Second, the amount of the theoretical tax:[102] The greater the theoretical tax, the more unfair it is to not take that significant liability into consideration.[103] It is also important to discern whether the parties had any plans or expectations concerning any future sale of the real estate investment. Did the parties intend to sell the property to pay for their child's college education? Past practice is also an important indicator. If the parties had a practice of flipping properties, there is a greater chance of theoretical taxes being considered than if the parties owned a two-family home that they rented for the last 10 years.

The tax issues associated with real estate investments must not be ignored. You should have your client consult with a qualified tax advisor to discuss all potential pitfalls and opportunities relevant to your client's unique situation. It is incumbent upon counsel to introduce evidence regarding all tax consequences, even if there is not a foreseeable event that would trigger the tax. The hypothetical tax consequences are contingent liabilities that should be the subject of expert testimony.

Effective lawyering requires a more detailed presentation. This argument, although made infrequently, is supported by the statute and tax code and is consistent with equitable principles.[104]

OTHER CONSIDERATIONS: TAX COURT, CO-COUNSEL AND DISCOVERY

To learn more about real estate valuation, a great place to start is by reviewing cases from our state tax courts. Due to the volume of cases involving valuations in tax court, the judges are typically much more experienced in real estate valuation and the nuances associated with valuing property. The judges in tax court invest time in learning valuation and the rules that apply because their caseload requires them to address these issues on a regular basis. While the issues presented in tax court are different and tax courts are more concerned with *economic rent* than equitable distribution, tax court cases provide guidance on how to approach valuing different types of property. Real estate experts find state tax court cases helpful in providing guidelines for valuation.

For a case involving significant real estate holdings, the family law practitioner may want to bring on an attorney as co-counsel whose practice is devoted to real estate valuation. Knowing the limits of your own expertise is an asset. Just as family law practitioners rely on the expertise of accountants for business valuations and on mental health professionals for custody issues, having a full arsenal in a real estate case requires access to someone with expertise in real estate valuation. An attorney with such expertise is also invaluable in preparing the family lawyer for cross-examination of the other party's real estate expert.

Developing a comprehensive discovery plan is vital to preparing a case with a significant real estate component. The same due diligence a family lawyer engages in for business valuations must be employed for real estate valuations. The discovery requested should include documents such as leases, income and expense statements, general ledgers, all agreements in place at the property, covenants not to compete, and a listing of gross sales. The extent of the information requested should be for three to five years, depending on the case.

Depositions should be taken of the key people who have information concerning the property. Those individuals may include property managers, property owners, chief financial officers, contractors, engineers, and tenants. These depositions provide the family lawyer with the opportunity to learn how the properties are being operated and how the funds are being expended.

Discovery, if complete and properly obtained, provides the family lawyer with the total picture of all the components contributing to the property's value. Such information puts the family lawyer on equal footing with the adversary's real estate expert, which is a tremendous advantage in litigation.

CONCLUSION

Valuing and allocating real estate in a matrimonial case is an arduous, multi-dimensional task that must not be underestimated. Prepare by having a working knowledge of real estate valuation techniques. Carefully select your real estate expert. Consult an accountant to advise you and your client of the tax consequences. Determine the legal arguments you intend to raise and the information needed to prove your case. Develop a comprehensive discovery plan to ensure that the proper research is obtained, depositions of key people are taken, and the appropriate appraisals are performed. Work together, in sync, with your real estate expert to prepare for direct examination as well as cross-examination of the other party's expert. The art of valuing and allocating real property can produce beautiful results with planning, preparation, and proper diligence. ■

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What Every Matrimonial Attorney Should Know About Businesses and Their Structure

by Charles F. Vuotto Jr., Brett R. Harris and Scott Maier

Matrimonial attorneys are required to deal with numerous forms of businesses incident to the dissolution of a marriage. This article outlines the various structural forms that businesses can have, and highlights the basic differences in terms of tax reporting, liability and other aspects of administration.

As matrimonial attorneys, we are most interested in determining the following with regard to a business:

- The benefit stream derived by the business owner(s) (e.g., income, distributions, perquisites, etc.); and
- The fair value of the litigant's ownership interest in the business for purposes of equitable distribution.

This article will focus on characteristics of the various forms of business and their respective structures.

Businesses primarily take one of the following forms:

1. Sole Proprietorship
2. General Partnership
3. Limited Partnership
4. C Corporation
5. S Corporation
6. Professional Corporation
7. Limited Liability Company

While other entity forms exist, such as trusts which may be established as investment vehicles and non-profit corporations or unincorporated associations to pursue charitable endeavors, the foregoing comprise the vast majority of entities engaged in for-profit businesses.

In reviewing types of entities, it is important to distinguish between those in which the owners retain personal liability in conjunction with the acts of the business—such as a sole proprietorship and a general partnership—and those entities that absorb the liabilities associated with the business and, for the most part, shield the owners from such exposure personally. The latter, referred to as artificial entities, are structures whose existence arises from public record filings of formation documents with the appropriate governmental office.

Statutory precedence for corporations and limited liability companies in New Jersey has always provided for formation of such entities at the state level. Historically, limited partnerships had been created in New Jersey at the local level by filings with county clerks, but in the 1980s the venue for filing was transferred to the state level, and the county clerks were required to transmit to the secretary of state copies of all limited partnership filings at that time for a transfer of recordkeeping.[1]

In 1998, all commercial recording responsibilities[2] of the New Jersey Secretary of State, including filing of corporate, limited partnership and other business entity documents, were transferred to the New Jersey Department of the Treasury.[3] Although many still refer to filings with the secretary of state, the correct reference is to the New Jersey Department of the Treasury, Division of Revenue.[4]

Since this discussion is directed to matrimonial attorneys, we now address the following areas of each of the aforementioned business structures:

1. Reasons for the different types of entities
2. Method of formation
3. How ownership is maintained and assigned
4. How income is reported to federal and state taxing agencies
5. How the owners receive and report income
6. How distributions are reported
7. How balance sheets (assets/liabilities/retained earnings) are reported.

SOLE PROPRIETORSHIPS

Sole proprietorship (SP) is the most basic business format. In fact, it is not a separate entity but rather refers to a business organization that, in essence, mirrors the individual owning the entity. This form of ownership, for obvious reasons, is only available to a single owner, and may not be used when more than one person (whether the individual is a spouse, family member or unrelated) desires to form a business. The SP has no formal requirements for formation or operation, nor are documents required to be filed with state or municipal entities for creation. However, if the owner will "conduct or transact business under any assumed name, or under any designation, name or style, corporate or otherwise," other than their real name, a trade name certificate must be filed with the clerk of the county or counties where business is transacted.[5]

The SP is the easiest type of business structure to create and maintain in terms of start-up and administrative costs, making it a frequent choice for owners who require a less sophisticated ownership structure. However, since the sole proprietorship model does not constitute a separate entity distinguishable from the individual owner, it affords no shelter to shield the assets of the owner from debts and liabilities arising from liability incurred during the course of the business. The owner is personally responsible and liable for all obligations of the business, irrespective of how much he or she has invested into the venture or how much profit has been derived, if any. Accordingly, this is typically not a business organization format recommended by attorneys to their clients.

Interests in an SP are not transferable in themselves, since no defined interest exists. An individual is, of course, free to convey assets used in the operation of a business, subject to rights of creditors and lienholders. A disadvantage of the individualized nature of ownership of the SP is a lack of continuity for the business beyond the owner's death. No formal dissolution process exists upon the cessation of operations (whether by death of the owner or abandonment of the venture).

For tax reporting purposes, no separate filing is made at the state or federal level for the SP. All profits and losses are personal to the owner. The income and expenses of the business are reported on Schedule C of the individual's income tax return, with the owner being deemed to receive all net income (the bottom line of the business operations). Net income is subject to both income taxes and Social Security taxes. No clear delineation is made to show distributions of profit or income from the business to the owner. Typically, a separate balance sheet is not generated for the SP for income tax purposes.

As an aside, note that, for any business, regardless of form, separate, compiled, reviewed or audited financial statements can be generated, which would include a statement of assets, liabilities and equity/balance sheet for the entity as well as a statement of revenues and expenses. However, since most owners of SPs, in the authors' experience, do not maintain separate balance sheets, determining the value of the ownership interest of a party to a matrimonial action in such a business might be made more difficult, especially in a capital-intensive business.

Practice Tip: Since by definition a *sole* proprietorship is only owned by one individual, the chances that the business owner will be deterred by anything more than feelings of guilt or exposure to the IRS are very small. Certainly there are no business partners to question these expenditures or how they are recorded. Therefore, you can expect to see a significant amount of perquisites being charged on the business's Schedule C, including some unique items such as expenses related to the business use of the owner's residence, travel and entertainment and vehicle expenses.

PARTNERSHIPS

As set forth in the Uniform Partnership Act of 1996 (as adopted in the state of New Jersey),[6] a partnership is an association of two or more individuals to carry on a business for profit, as co-owners. In its most basic form, being a general partnership, the entity arises from the association of the partners rather than from the filing of any formal certificate, but the partners may file a statement addressing certain partnership matters with the Division of Commercial Recording.[7] Partnerships are required to comply with the assumed name certificate requirements imposed on those operating sole proprietorships as discussed above,[8] and also are required to file a statement in the office of the clerk of the county where they are conducting or transacting business if the designation "and company" or "& Co." is used as part of their firm or partnership name.[9]

Partnerships may organize in the form of a limited partnership under the New Jersey enactment of the Uniform Limited Partnership Law of 1976,[10] which requires formation by filing a certificate of limited partnership with the state. There are some attendant start-up costs that do not apply for general partnerships, but the administrative cost to legally form either type of partnership is not overly burdensome because of limited regulation under the statutory authority. In terms of the administrative time and expense required to generate a partnership agreement between and amongst the partners, the partners themselves determine the time and money necessary to affect such a document.

Although a partnership is, in fact, a legal entity distinct from its partners,[11] it is viewed under the law as an aggregate composed of its partners. Members of a general partnership, and general partners of a limited partnership, are fully and severally liable for the debts and obligations of the partnership. Such liability may be in excess of the amounts invested by such partners, and will not be limited to the extent of distributions or allocations to such partners.

A limited partnership addresses certain personal liability issues pertaining to the partners. A limited partner in such an entity maintains personal liability only to the extent of their investment. In other words, a limited partner's investment (of time, reputation and money) may be at risk in that the entity in which they invested may go bankrupt; however, as long as certain statutory definitions are met, the creditors of the limited partnership may not pursue the limited partners of the entity beyond that investment. Having said this, it is imperative that the partners of such a business keep in mind that this business structure has operational limitations, since limited partners cannot be actively involved in managing the business. Limited partnerships have frequently been vehicles for real estate, theatrical or other investments, and also had been prevalent entity choices for those in service industries in light of restrictions on professionals operating under a corporate structure (professionals cannot use an entity to shield personal liability for malpractice).

With the advent of limited liability companies and professional service corporations, the use of limited partnerships has declined in recent years for business entities, although partnerships remain a staple for certain estate planning techniques.

Ownership interests in any type of partnership are not freely transferable, because a change in these interests constitutes a change in the association underlying the partnership. Admission of new partners is also subject to approval of the other partners, so it is unlikely (beyond the cases frowning upon such transfers) that any partnership interest would (or indeed could) be conveyed in a property settlement, although a spouse may have an entitlement to a share in the profits or distributions received from the partnership. This entity type is susceptible to lack of continuity upon the death or dissociation of a partner, which may result in termination of the partnership unless the parties' agreement provides otherwise. A certificate of cancellation must be filed with the state at such time as a limited partnership dissolves and commences winding up the partnership, or at such other time as there are no limited partners.[12]

After dissolution, a partner of the former general partnership may file a statement of dissociation,[13] and a trade name dissolution may be filed relating to any trade name certificates previously filed for the partnership.[14]

Partners' rights to income are based on their respective percentage interests in the partnership, unless otherwise agreed upon. All such arrangements should be explicitly reflected in a written partnership agreement.

Although generally no tax is imposed directly on the partnership itself, every partnership (with narrow exception) must file a federal Form 1065, and any partnership having a New Jersey resident partner or deriving any income, gain, or loss from New Jersey sources must file a New Jersey Partnership Return, Form NJ-1065. Individual partners are subject to tax on their distributive share of the partnership's income, and must report the amount of net income derived from the partnership on their personal income tax return, whether or not the income was actually distributed. The partnership is required to issue Schedule K-1s to each partner showing the partner's distributive share of the partnership's income (loss), distributions, equity, etc. Distributions by the partnership are shown on Form 1065, Schedule M-2 and Schedule K-1, and a balance sheet for the business of the partnership will be found on Schedule L to Form 1065.

Because of the requirement of a balance sheet, as well as additional information which is required by Form 1065 (as opposed to the sole proprietorship's Schedule C), financial data on the value of an owner's interest may be more readily identifiable in matrimonial cases where such valuations are necessary.

Practice Tip: Many of the partnerships you will encounter in your practice are real estate partnerships, which generate rental revenues and related expenses. If you look at such an entity's income tax return, you may see that the entire first page has no amounts filled in. This does not mean that there was no activity or income/loss for that period for the entity. Rental activities are reported on a supporting schedule to the tax return. So look at the Schedule K (page 3) on the return as well as the supporting schedules attached to the return. Also, the partnership (as well as the other entities discussed below) must contain a balance sheet on page 4 of its return. This reveals a lot of information about the entity.

C CORPORATIONS

Corporations for profit are organized in New Jersey under the New Jersey Business Corporation Act.[15] Corporations are creatures of statute, and are created by filing a certificate of incorporation with the state. Upon proper formation, corporations are considered, legally, to be *persons* with certain rights and obligations under the law, as do natural persons, or individuals. Since a corporation is viewed as distinct from its owners, it is able to incur its own liabilities, and the shareholders will be shielded from personal liability, absent extraordinary circumstances, which would justify piercing the corporate veil. In essence, the corporate veil can only be pierced, under the law of most jurisdictions, if the corporation was formed to, or is operated in a way to, defraud creditors of the entity. Otherwise, the liability of the owners is limited to the amount they pay for their shares of stock (similar to that of a true limited partner, as discussed above).

Corporations are managed based on a three-tier structure of shareholders, directors and officers. Shareholders or stakeholders are those with equity/ownership interests in the business: A corporation may have one or many shareholders, and, depending upon the type of corporation, shareholders may be individuals or other distinct entities. Generally, directors are empowered with overall management of the business, and officers carry out the day-to-day operations.

Shareholders elect the directors (who may, but need not be, shareholders), and shareholders retain the right to directly vote on certain material corporate life-cycle events under applicable law. Generally, however, they are not involved, as shareholders, in the decision-making for the business.

The directors have a fiduciary duty to the shareholders and the corporation, and have the power to elect officers to carry out the determinations of the board in the administration of the business.

Corporations range from publicly held corporations, whose shares are traded on the various exchanges or markets, where the board management structure is critical to the ability of the corporation to operate, to closely held corporations, where the shareholders and directors may be similar or identical. In closely held companies, the shareholder may be involved in all aspects of decision-making, but in their dual role as a director, not as a shareholder.

Regardless of the size of the enterprise, the corporate statutes provide for formality of corporate governance, resulting in greater administrative burdens of corporations as compared to other business entities.

Because the ownership of corporations is ultimately vested in the shares of ownership, and not the people owning the shares themselves (a legal distinction which may seem insignificant but one that is the basis for most of the corporate law promulgated), corporations are able to have perpetual existence; the business does not terminate upon transfer of shares or death of owners. Shares in a corporation are freely transferable, absent restriction in an agreement among the shareholders such as buy-sell or shareholder agreements (which are typical in a closely held corporation) and subject to applicable securities laws.

For income tax purposes, unless certain elections are properly filed at the federal and state level, all corporations are considered C corporations. This, as we will discuss below in conjunction with S corporations, is an important distinction to draw. One of the greatest drawbacks of the corporate structure as a C corporation is double taxation (35 percent is the current top marginal federal tax rate for a C corporation; state rates vary).

Income tax is levied upon corporate profits and, in addition, upon dividends or distributions paid to the shareholders (currently taxed at 15 percent for federal purposes and various rates depending upon the state). These dividend taxes are levied at the personal level to the shareholder.

Even though losses for corporations, at the corporate level, may, under certain circumstances, be carried forward or back to other years, these losses cannot be personally carried over to be deducted on the individual's return. Therefore, if the shares are sold before the tax benefit of the losses can be realized, the individual owner may never receive the pecuniary benefit of the losses for income tax purposes.

Corporations report income by filing federal Form 1120. The corporate balance sheet can be found on this form at Schedule L; dividends are reported on Schedule M2.

In New Jersey, corporations are subject to the Corporation Business Tax Act,[16] and must file Form CBT-100 Corporation Business Tax Return. Taxes may also be payable on corporate assets in addition to income, depending upon the jurisdiction. Overall, tax compliance matters for corporations are more burdensome than for other entities. Also, because of all of the state filing requirements, as well as the fact that the corporation is its own legal entity requiring much more time and effort in its maintenance (*e.g.* corporate directors/shareholders meetings must be had and minutes taken and kept, tracking of owners, etc.), the relative administrative costs dwarf those of the partnerships or sole proprietorships.

The actual difference in the tax burdens for a C corporation shareholder as compared to an S corporation or partnership equity holder requires a lot more discussion, which is not relevant for the purposes of this article. However, since the reduction of the top C corporation income tax rate from 40 percent to 35 percent, and the abatement of the dividend rate to 15 percent, the double taxation penalty associated with the C corporation has been greatly mitigated when set against the individual's top federal marginal income tax rates.

A typical matrimonial matter that deals with the existence of closely held businesses usually reflects those businesses owned under the umbrella of an S corporation, not a C corporation. Therefore, the authors will not enter into an extensive discussion of valuation issues for the C corporation at this time. When assessing publicly traded corporate investments, valuation and determination of cash flow are relatively easy to quantify by utilizing public information and trading values as of the date of the matrimonial complaint or date of resolution of the matter.

Practice Tip: Pages 2 and 3 of the corporate income tax return contain a lot of additional essential information about the activities and ownership of the entity. This should, at a minimum, be reviewed by anyone valuing the entity or determining ownership or cash flow from the business. Do not ignore this data just because it is not numerical in nature.

S CORPORATIONS

S corporation refers to those small business corporations that have elected and qualified to be treated as such under federal and state law. An S corporation avoids the double taxation issue as it provides for profits and expenses to be passed through to the individual stockholders, much the same way as in a partnership, generally resulting in no federal income tax to the corporation as an entity. For those that have elected to be treated as an S corporation in the state of New Jersey,[17] the corporate tax is not eliminated; however, New Jersey S corporations pay a lower corporate tax rate, and the shareholders report their *pro-rata* share of S corporation income on their New Jersey individual income tax returns.

S corporations are formed as business corporations and have the same liability protections, organizational structure and corporate formalities. There are limitations, however, regarding which corporations are eligible to be S corporations. For federal tax purposes, they must be a domestic corporation (formed under the New Jersey Business Corporation Act or comparable legislation in other states). Further, the entity must have no more than 75 shareholders. Shareholders must be individuals, estates or certain types of trusts (but no other types of entities); and no non-resident aliens may be shareholders.

Only one class of stock is permitted for S corporations (disregarding differences in voting rights), which makes the structure less attractive to venture capitalists or other investors. In order to be treated as an S corporation, each shareholder must consent to such status and written elections must be filed on applicable federal and state forms within prescribed time periods.

Taxes are reported on federal Form 1120S, which is the same as Form 1120 except with one notable addition, Schedule K and K-1s. Similar to the process for partnerships, Schedule K-1s are issued to Subchapter S shareholders showing pass-through income and distributions. Distributions are shown separately on Schedules K-1. Schedule K is merely all of the Schedules K-1s aggregated on the income tax return.

In valuing an S corporation for purposes of equitable distribution it is important to be aware that an S corporation's *income* is taxed, not the *cash flow* to any particular owner. Therefore, income could be earned (and the applicable income taxes paid) without the distribution of those earnings to the owner in the same period. Conversely, previously taxed earnings might be distributed to the owners of an S corporation in a period where no income is earned. This distinction warrants recognition because the matrimonial lawyer or accountant may be called upon to determine an S corporation's value, based upon income as well as current or past lifestyle or income, based upon cash flow.

Practice Tip: For any entity, it is *essential* (the authors cannot stress this enough) that the professionals studying the financial aspects of that entity understand all of the cash flow out from and into the entity in question. This, therefore, does not only include income from operations, but it also must include consideration of loans in and out of the company as well as distributions made to and contributions made by the owners of the entity. Without a full understanding of these issues, no *meaningful* financial analysis of any business can be completed.

This point is raised because the S corporation's tax return (as well as those of the LLC and partnerships) contains two schedules, which lend an incredible amount of insight into the *other* sources of cash flow. The balance sheet (Schedule L in both instances) shows loan balances (both due to the company and by the company to its creditors) at the beginning of the period and at the end. By exploring the changing loan balances for the entity, one can learn a great deal about funds moving in and out of the entity. Likewise, the Schedule M-2 on these tax returns shows contributions and distributions made by exploring the changes in owners' equity/capital during the period. So take heed, income generated by the entity may have a great deal to do with or may have nothing to do with the actual funds moving into or out of a business.

Finally, even though a sole proprietorship does not generally file a balance sheet as part of its tax reporting, the practitioner should not be shy about asking the owner to supply all of the above-mentioned data in a separate analysis.

The authors note that this tip covers the partnership, S corporation as well as the derivatives of these entity types mentioned below.

PROFESSIONAL CORPORATIONS

Professional corporations are the vehicle for those engaged in activities where negligence may arise from the performance of professional services that cannot be avoided, but liability protection is sought from negligence of others (not under their supervision) and from liabilities not arising from rendering of the professional services. The Professional Service Corporation Act[18] provides for incorporation of an individual or group of individuals to render the same professional service to the public for which such individuals are licensed under applicable law. Examples of personal services that may be rendered are those rendered by accountants, architects, professional engineers, physicians, dentists and attorneys. The individuals are also subject to the requirements of any regulatory bodies particular to their professions.

Only those who are licensed or legally authorized within the state to render the professional service may be shareholders of the entity, with an exception in the statute only for temporary ownership of shares by the estate of a deceased shareholder.[19] Therefore, the shares in a professional corporation could not be conveyed to a spouse in connection with a matrimonial settlement unless the spouse is properly qualified in the applicable profession.

This choice of entity is driven by the type of business to be performed rather than any tax effects. Professional corporations are generally presented as subchapter S corporations, subject to meeting subchapter S eligibility requirements and making proper elections. Otherwise they will be C corporations, as a default. In terms of all of the legal/tax attributes of such corporations, please see the discussions above applying to C and S corporations.

LIMITED LIABILITY COMPANIES

Limited liability companies (LLCs) have recently become a preferred choice of entity, and are the youngest type of business discussed in this article, the New Jersey Limited Liability Company Act having been first enacted in 1993 (and in many other jurisdictions, in similar time periods).[20] LLCs are considered by many to be an ideal combination of the best of several entities—affording the liability protections of corporations but permitting tax treatment like a partnership.

The entity is formed by filing of a certificate of formation with the state, but has minimal filing requirements thereafter. Owners are referred to as members, rather than shareholders; in lieu of directors, LLCs may have managers (or they may be member-managed), and officers can be designated but are not required. The structure affords greater flexibility in operations and management than the cumbersome procedures imposed upon corporations under applicable law. The subchapter S corporation eligibility requirements do not apply, giving potential for unlimited number and types of members and any capital structure desired.

One of the early drawbacks of the structure was that LLCs were only available for businesses with more than one owner, but the statute was revised in 1998 to permit for single-member entities.

Negatives include the lack of developed case law for guidance for operation of the entity and legal rights and obligations of its owners, causing uncertainty that may give discomfort to business owners and investors. The structure also is not always available to professionals, because of its limited liability nature. Interests in an LLC may be transferred, but there are some limitations in the act and they may be restricted by an operating agreement for the entity. Upon termination of the business, a certificate of cancellation is filed with the state.

If the LLC has only one owner, it may be classified for income tax purposes as if it were a sole proprietorship (referred to as an entity to be disregarded as separate from its owner). If there are two or more owners, it will automatically be considered to be a partnership, unless an election is made to be treated as a corporation. Taxes are, therefore, either reported on Schedule C to an individual owner's return for a single member LLC, or otherwise will be on Form 1065 with Schedule K-1s issued to members. Once again, the authors direct you to the appropriate discussion above.

AGREEMENTS BETWEEN AND AMONG OWNERS

As touched upon early in the discussion of partnerships above, for all types of entities other than an SP, some type of agreement is necessary between or among the owners in order for them to come together to form an entity. Such an agreement may involve varying degrees of formality, and may be oral or written. The authorizing statutes do not expressly require a written agreement among business owners beyond the certificates required to be filed with the state. In fact, one of the main purposes of the various statutes is to provide gap fillers to set forth default rules by which entities will be operated in the event that no written agreement exists, or to address such matters that are not within the scope of the agreement among owners.

While the subject matter of agreements can vary greatly, the main topics that arise are the management and operation of the entity; capitalization and contribution requirements; allocation of profits and losses; potential for additional owners to join the entity; and transferability of interests, whether voluntary or involuntary. The authors strongly recommend that attorneys and other professionals involved in matrimonial proceedings specifically review the financial provisions of agreements in order to ascertain the value of the interest in the business. Further, special review should be given to transferability provisions as they often address valuation that may be agreed upon by the owners in certain contexts (buy-outs triggered by a designated event, such as death, disability, retirement, withdrawal or expulsion from the entity), providing for either permissive or mandatory buy-outs.

Agreements may provide for valuation by appraisal, by formula, by reference to certain information in the books and records or financial statements of the entity, or the parties may periodically issue an agreed-upon certificate of value. Some agreements may even include a specific provision to address the disposition of an interest in the event of divorce—an intention of the parties that the interest in the entity not be partitioned or transferred to the spouse in the proceedings. The enforceability of any such provision would depend on its specific terms and the underlying matrimonial action.

The documentation for partnerships is referred to typically as a partnership agreement, agreement of partnership, articles of partnership or joint venture agreement. An agreement for a corporation—whether it be a C corporation, S corporation or professional service corporation—can be under many titles, such as a shareholders agreement, stockholders agreement, buy-sell agreement or cross-purchase agreement. Agreements governing LLCs are usually referred to as operating agreements, although they may be known as membership agreements or limited liability company agreements. None of these documents are required to be filed with the state upon formation of the entity, and are thus not a matter of public record, although they may be disclosed to third parties under certain circumstances, such as to a lender in connection with financing of an entity.

The title of the agreement is not important. Rather, it is critical that discovery requests in a matrimonial action encompass any type of writings that memorialize agreements among business owners, whether they be formal or otherwise, in order to obtain as much information as possible regarding the operations and value of the entity. For example, in the corporate context, agreements among owners may also be reflected in the corporate documents, such as the certificate of incorporation (as filed with the state), bylaws and minutes, which would be included in the corporate record books.

VALUATION ISSUES

One hotly contested issue is currently being discussed in the community of experts pertaining to the valuations of pass-through entities versus those of similar characteristics, which are not pass-through entities (*e.g*. S corporations vs. C corporations). Because this is an ongoing unsettled area of discussion which, in and of itself could take up a chapter in a valuation text book, the technical aspects of the arguments will not be addressed here. However, in essence, the discussion (which has arisen out of the case of *Gross v. Commissioner*[21] and its progeny, cases which deal with federal gift/estate business valuations) can be related as follows.

One school of thought says that the double taxation and higher tax rates associated with the non pass-through entities (*i.e*. the C corporation) makes the future projected income streams, and therefore the values of such entities, less valuable than the same income streams and values of pass-through entities such as S corporations. The other school of thought is that no differences exist; at least no differences so great as to give rise to any adjustment to the entity's value.

Practice Tip: The authors believe that, in light of the reasons stated above (*i.e*. the lower corporate federal tax rates and the lowering of dividend tax rates), there might be a *slight* adjustment (with emphasis on the word *slight*) to value warranted in certain instances. This adjustment, as is the case with all valuation adjustments, should be judged on a case-by-case basis.

CONCLUSION

This article attempts to bring to light the differences, advantages and disadvantages of the various types of business entities that may be formed. The article also attempts to examine these differences in the context of the divorce action, which is a part of daily practice. The authors recommend that further discussion about each of the forms of entity, as well as the associated technical aspects, should be sought, where appropriate, with a professional (*e.g.* a business/transactional attorney, accountant, tax professional, business broker, etc.) whose practice focuses in this area before any decisions regarding forensic investigation, assessments of income/value or transfers are made in any specific instance. ■

*(**Authors' Note**: This article is presented for informational purposes from a New Jersey law perspective and is not intended to constitute legal or tax advice. Every matter has special circumstances requiring its own analysis by legal counsel and tax advisors. The views expressed in this article are personal to the authors and do not necessarily represent those of their firms or their respective clients.)*

ENDNOTES

1. N.J.S.A. 42:2A-13.
2. The Division of Commercial Recording was established pursuant to N.J.S.A. 52:16A-35.
3. The transfer occurred as the result of Reorganization Plan No. 004-1998 issued by the Office of Governor, Christine Todd Whitman, on March 30, 1998, codified at N.J.S.A. 13:1B-15.111.
4. For more information regarding state filing procedures including online business services, refer to the New Jersey Business Gateway at www.state.nj.us/njbgs/index.html.
5. N.J.S.A. 56:1-2.
6. N.J.S.A. 42:1A-1 *et seq.*
7. N.J.S.A. 42:1A-6.
8. *See* text accompanying note 5.
9. N.J.S.A. 56:1-1.
10. N.J.S.A. 42:2A-1 *et seq.*
11. N.J.S.A. 42:1A-9.
12. N.J.S.A. 42:2A-18.
13. N.J.S.A. 42:1A-43.
14. N.J.S.A. 56:1-6.
15. N.J.S.A. 14A:1-1 *et seq.*
16. N.J.S.A. 10A-1 *et seq.*
17. N.J.S.A. 54:10A-5.22a.
18. N.J.S.A. 14A: 17-1 *et seq.*
19. N.J.S.A. 14A:17-10.
20. N.J.S.A. 42:2B-1 *et seq.*
21. T.C. Memo 1999-254, *aff'd* 272 F.3d 333 (6th Cir. 2001).

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Valuing and Allocating Real Estate Investments

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(1974); *Kruger v. Kruger*, 73 N.J. 464, 468 (1977); *Stern v. Stern*, 66 N.J. 340, 348 (1975); *Wadlow v. Wadlow*, 200 N.J. Super. 372, 378 (App. Div. 1985); and *Pacelli v. Pacelli*, 319 N.J. Super. 185, 196 (App. Div. 1999).

83. 65 N.J. 196, 212-13 (1974).
84. 92 N.J. 423, 441 (1983).
85. 237 N.J. Super. 342 (1989).
86. *Id.* at 355.
87. *Id.* at 352.
88. *Id.* at 355.
89. *Id.*
90. *Id.*
91. *Id.*
92. *Id.*
93. Frank A. Louis, Distribution: The Art of Equitable Distribution, Seminar Material: *Handling the Critical Elements of a Divorce Case*, 12 (New Jersey Institute for Continuing Legal Education 1998).
94. *Id.*
95. 275 N.J. Super. 452 (App. Div. 1994).
96. Frank A. Louis, The *Orgler* Decision: What It Means and How to Use It, *NJFL* 4 (1991).
97. *Id.*
98. IRS Publication 544, www.irs.gov.
99. Robert J. Durst, Taxing Concerns in Matrimonial Law, *New Jersey Lawyer, the Magazine*, June 2001.
100. Louis, *supra* note 96.
101. *Id.*
102. *Id.*
103. *Id.*
104. *Id.*

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Allocating Active and Passive Appreciation of a Separate Business Asset for Equitable Distribution

by David M. Wildstein

Under New Jersey law, the typical approach to valuing an active separate[1] business is to value the asset twice: the date of marriage (or when acquired during the marriage) and the date of the filing of the complaint.[2] The difference or appreciated value is subject to equitable distribution. This simplistic method for valuing the enhanced value of a business assumes all businesses actively increased. Part of the growth of a business may be passive in nature, such as a return on capital, market factors, or the effort of third parties that caused the business to grow and flourish during the marriage. The other part is active, such as the effort of either party that caused the business to increase in value.

Although *Berrie v. Berrie*[3] held that the enhanced value of an immune active asset may have passive and active components, there are no New Jersey opinions that have offered any guidance on the method for calculating passive and active increases. This article will summarize New Jersey case law, and explore how community property states and other equitable distribution states address this question.

NEW JERSEY LAW RELATED TO EQUITABLE DISTRIBUTION OF ACTIVE IMMUNE ASSETS

N.J.S.A. 2A:34-23(h) provides in part that:

> The court may…effectuate an equitable distribution of the property, both real and personal, which was legally and beneficially acquired by them or either of them during the marriage. However, all *such property, real, personal or otherwise legally or beneficially acquired during the marriage by either party by way of gift, devise or intestate succession shall not be subject to equitable distribution*... (emphasis added).

In the seminal case of *Painter v. Painter*[4] the Court interpreted the statute as saying that:

> Clearly any property owned by a husband or wife at the time of marriage will remain the separate property of such spouse and in the event of divorce will not qualify as an asset eligible for distribution.… *We also hold that if such property owned at the time of the marriage, later increases in value, such increment enjoys a like immunity*. Furthermore, the income or other usufruct derived from such property, as well as any asset for which the original property may be exchanged or into which it, or the proceeds of its sale, may be traceable shall similarly be considered the separate property of the particular spouse.[5] (emphasis added).

Despite this bright line rule, which would have eliminated equitable distribution of the appreciated value of an active immune asset, the infamous footnote 4 of the decision added much confusion:

> The immunity of incremental value to which we refer is not necessarily intended to include elements of value contributed by the other spouse, nor those for which the husband and wife are jointly responsible.[6]

Although there are inconsistencies in our cases related to this footnote, it now means that direct contributions from a non-owning spouse serving as a homemaker, confidant and caretaker of children entitles a spouse to share in the appreciated value of the asset. A short summary of the evolution of this concept follows.

In *Scherzer v. Scherzer*[7] the court dealt with the equitable distribution of stocks of a premarital corporation owned by the husband. The court noted that:

> The stock in question, unlike ordinary marketable securities, necessarily derived its value in large part from defendant's personal participation in the business.…The value of defendant's interest in the corporation which predated the marriage is, of course, immune from distribution. However, any increase in value occurring after the marriage should be considered eligible *to the extent that it may be attributable to the expenditures of the effort of plaintiff wife. The theory is that a homemaker's contribution cannot be given a monetary worth and its value may be gleaned from the earnings of the employed spouse.*[8] (emphasis added).

Two years later, in *Mol v. Mol*,[9] the Appellate Division held that while the plaintiff wife was "not entitled to share in the portion of enhancement in the value of a home which was due solely to inflation or other economic factors and to which she did not contribute in any way," the trial judge must distinguish between "that portion of growth and value which was the result of independent economic factors alone such as inflation and that portion to which plaintiff contributed or for which husband and wife were jointly responsible."[10]

Thereafter, in *Gibbons v. Gibbons,*[11] the court noted that:

> The non-remunerated efforts of raising children, making a home, performing a myriad of personal services and providing physical and emotional support are, among other non-economic ingredients of the marital relationship, *at least as essential to its nature and maintenance as are the economic factors, and their worth is consequently entitled to substantial recognition. Thus, the extent to which each of the parties contributes to the marriage is not measurable only by the amount of money contributed to it during the period of its endurance, but rather by the whole complex financial and non-financial components contributed.*[12] (emphasis added).

The confusion related to footnote 4 of *Painter* was finally settled in *Weiss v. Weiss*.[13] The court explicitly held that the wife's efforts as a homemaker and caretaker entitled her to equitable distribution of the premarital asset that had increased in value.[14] In essence, the decision reflected the court's philosophy that marriage is a joint enterprise akin to a partnership.[15]

The same year that *Weiss* was decided, Judge Conrad Krafte rendered an opinion on *Scavone v. Scavone*.[16] Although the case dealt with a passive asset that was acquired during the marriage and the issue related to the date of valuation, the court used this as an opportunity to write a treatise on passive and active assets. The court defined passive assets as "those assets whose value fluctuations are based exclusively on market conditions."[17] An active asset was defined as an asset that involves "contributions and efforts towards their growth and development which directly increased their value."[18] Surprisingly, the court held, contrary to prior opinions, that when an immune active asset increases in value due solely to the efforts of the owner, that value is undistributable.[19] "Conversely, when such value is derived, in part or in whole, from the efforts of the non-owner, it is subject to distribution."[20] For example, where the non-owner spouse contributes by way of a mortgage paydown, a 100 percent immune asset is transformed to an asset subject to equitable distribution, for limited purposes.[21]

In *Berrie,*[22] the trial court granted the husband's motion ***in limine*** to bar the wife from seeking equitable distribution of 53.1 percent of the husband's premarital publicly owned stock in Russ Berrie and Company. The husband argued that any increase in the stock was due to market conditions of publicly traded stock, and had nothing to do with his efforts.[23] At the time of the divorce, the husband was chief executive officer of the company, which employed 2,300 workers, 800 salespersons and 200 managers with five subsidiaries, 12 distribution centers and a worldwide market.[24] Despite the magnitude of the company and the market forces, the court held that there was no question that a single person's efforts can influence the growth and success of a business that is public or private.[25] As the business grows, however, the question becomes more one of fact, depending on how closely the individual is identified with the business entity.[26]

The court remanded this matter for a plenary hearing to have expert testimony relating to Mr. Berrie's impact upon the value of the stock, notwithstanding the fact that there may also be market forces that increase the value of the stock.[27] The court further held that there may be passive and active components in the enhanced value of public stock.[28]

In *Valentino v. Valentino*,[29] the court distributed to the non-owning spouse 10 percent of a premarital mini strip mall that was used as a gas station after the dissolution of a 12-year marriage. Although the court quoted *Scavone* concerning an immune active asset not being distributed if it was solely increased through the owner's efforts, the court nevertheless noted that the wife made contributions to the home and children, which allowed the husband to work at his business. Hence, the court ordered a distribution of 10 percent of the business.

The decision did not explain the basis of the 10 percent award or whether the court's award determined equitable distribution based on a percentage of the increase in the appreciation of the asset, or whether the court was taking a percentage of the entire value of the property.

In his article on the distributability of premarital assets, Frank Louis commented on *Valentino* as follows:

> *Valentino* clearly confirms that the non-economic contributions of a spouse can create a right to share in post-marital appreciation unless the appreciation was not created by *either* spouse, *i.e.*, interest on a bank account, appreciation of real estate, or publicly traded stock. Marital effort, as *Valentino* confirms, includes non-economic contributions such as raising children, maintaining a home. Yet, how this value is to be distributed should logically be effected by the fact that the asset itself was not created during the marriage. For example, in *Valentino*, the percentage received by the non-titled spouse was probably *less* than what she would have received had the asset been the initial product of the parties' hopes, dreams and marital efforts from inception.[30]

In summary, the law is now clear: Non-economic contributions by a non-owning spouse to an immune active marital asset are sufficient to afford the non-owning party a right to share in the appreciation of the asset.

However, if all or part of the appreciation of a business is passive in nature, that portion of the business shall be exempt from equitable distribution.

BURDEN OF PROOF

In *Sculler v. Sculler*,[31] a case of first impression, the court addressed the burden of proof when a non-owning spouse is seeking equitable distribution of an immune active asset.

The court set forth the burdens as follows:

> If a spouse asserts that an asset is immune, he or she bears the burden of establishing such immunity. Once the immunity is proven, any increase in value will also be immune unless it is shown that the increase was due, in whole or in part, to the efforts of the spouse seeking equitable distribution of the increase...proof that an asset is immune from equitable distribution raises a rebuttable presumption that any subsequent increase in value will also be immune. The burden then shifts to the non-owner spouse to demonstrate that (1) there has been an increase in the value of the asset during the term of the marriage; (2) the asset was one in which had the capacity to increase in value as a result of the parties effort (an active immune asset); and (3) the increase in value can be linked in some fashion to the efforts of the non-owner spouse.[32]

This opinion mandates that the non-owning spouse has the burden of proving that the increase in value was "linked in some fashion to the efforts of the non-owning spouse."[33] This appears inconsistent with N.J.S.A. 2A:34-23.1, which provides, in pertinent part, that, "it shall be a rebuttable presumption that each party made a substantial financial or non-financial contribution to the acquisition of income and property while the party was married."

This opinion also places the burden of proof on the non-owning spouse to prove that the business actively increased during the marriage.[34] This burden seems misplaced since the owning spouse has all the knowledge and information about the business and would be in a better position to prove whether it was active or passive.

This argument would be analogous to *Ozolins v. Ozolins*,[35] where the court placed the burden on the cohabiting spouse to prove that there was no economic benefit or detriment derived from the cohabitation. The court relied on *Frantz,*[36] which held that it would be unreasonable to place the burden of proof on a party not having access to the evidence necessary to support that burden of proof.[37]

Its noteworthy that the Virginia Code Section 20-107.3(a)(3)(a) provides in pertinent part:

> For the purpose of this subdivision, the non-owning spouse shall bear the burden of proving that (i) contributions of marital property or effort were made and (ii) the separate property increased in value. *Once this burden of proof is met, the owning spouse shall bear the burden of proving that the increase in value of some portion thereof was not caused by contributions of marital property or personal effort*. (emphasis added).

OTHER EQUITABLE DISTRIBUTION STATES

Since New Jersey case law offers no guidance or model to quantify passive and active appreciation of an immune active asset, an examination of other equitable distribution states was undertaken.

Despite an exhaustive search, no cases were located. Clearly, the cause of a business's appreciation is fact sensitive. There is no precise formula or consistent approach that will determine why a business increased in value. Following is a summary of various case law, which will underscore relevant facts that may bear upon passive increases in the value of a business.

MARKET FORCES

Inflation[38]

Inflation is changes in the value of money over time, which would be deemed passive appreciation. There is a paucity of cases on this subject. In general, inflation and fluctuations in the nationwide economy are not considered relevant in valuing passive increases in an asset. The reason is simple: "Like a flower, a business must be tended to if it is to flourish."[39] If inflation is used for any calculation that will isolate a passive asset, it should not be based on a national rate of inflation, but rather be focused on the specific industry that is being evaluated.[40]

In *Anthony v. Anthony*,[41] the court rejected the owner spouse's request to reduce the active immune asset's value by inflation. The court held that where the parties' economic partnership has existed in the marketplace influenced by inflation, it is appropriate to have the property reflect inflation's impact upon the partnership's assets. It should be noted, however, that under the Pennsylvania Divorce Codes, 23 P.S. Section 401e, the increase in the value of an active immune asset during the marriage is defined as marital property subject to distribution.

The Increase is Due to Efforts of Third Parties

If the owner spouse does not actually work in a business, he or she has no ability to influence or impact upon the value of that business. Therefore, all appreciation would be deemed passive. A prime example would be an absentee owner who leaves the management of the business to hired employees.[42]

In most cases where the owning spouse played a pivotal role in the business, appreciation in the value of the business is active (*e.g.* when the owner is among the top managers of the company). However, persons who occupy lower positions in companies, even as high-middle management, have generally been treated as having no affect upon the increase in the value of the business.[43] But, perhaps, one could argue that an outstanding individual may have a dramatic affect upon the performance of a company. For example, someone who develops software that saves the company significant money, or someone who creates an invention that becomes very profitable to the company.

In *Berenberg v. Berenberg*,[44] the husband owned 49 percent of the business for which he worked as a vice president and director of operations. The husband's father was the CEO and main shareholder of the business. The husband argued that he did not actively cause the increase in business. The court held that the appreciation in his stock was active.[45]

These cases demonstrate that notwithstanding a large number of third parties involved in a business, the appreciation may still be active. It should be noted that the recent surge in shareholder actions to dismiss top executives of unsuccessful large companies demonstrates that successful individual management can make a difference in large entities.

In many instances, the efforts of third parties may be relevant to the appreciation value that is equitably distributed. In *Decker v. Decker*[46] the husband was a high-level executive of a large public company. Although he was one of five key executives, he was considered "first among equals." The company provided more life insurance for him than any other executive. Ultimately, he became president of the company. Despite these facts, the court held that he was one of five other managers, and only 20 percent of the appreciation was attributable to the husband's efforts.

In *Ellis v. Ellis*[47] the court held that the husband who worked with five of his siblings in the business contributed to 20 percent of the appreciation, which was equivalent to 20 percent of the sales figures for which he was responsible. In other words, his effort was directly attributable to the percentage of gross revenues he created. In a large company, this would be totally impractical, since no one individual produces more than a small fraction of the company's overall revenues.

In *Innerbichler v. Innerbichler*[48] despite the fact that the husband owned only 51 percent of a company, which employed many people, the court held that the husband's extraordinary expertise caused the appreciation to be active.

In *Robbie v. Robbie*[49] the husband was the general manager of the Miami Dolphins football team. The evidence is uncontroverted that he mainly carried out decisions made by the team's owner and head coach. Nevertheless, the court held that all the appreciation in the husband's stock was marital property.

In *Mayhaw v. Mayhaw*[50] the court held that although a business may reap substantial benefits from the labor of others, some of whom may have been selected, trained or directed by the owner, the court must consider the degree to which they acted under the overall supervision of the spouse.

Marital Contributions Made to Separate Assets

If marital funds are contributed to a separate asset, that contribution is deemed active. Otherwise, a devious spouse may divert marital funds for the improvement and contributions to a separate property.[51]

Negotiating Skills is Active Effort

In *Dujack v. Dujack*[52] the court held that the talents of the husband in negotiating the sale of the business was a significant effort that caused the appreciation and the value of the asset.

Other Economic Forces

In *Hoffman v. Hoffman*[53] the husband manufactured water cooling towers. In light of the fact that legislation increased the demand for cooling towers, business increased. The court held that the appreciation was passive and separate property. An argument could be made, however, that Mr. Hoffman was wise enough to anticipate legislative changes, and that his skill and acumen to develop and remain in this business was an active effort. Similarly, in another government action, the public road constructed across the husband's separate property, increased the value of the farm dramatically. Again, the court held that it was a passive asset.[54]

In *Nordberg v. Nordberg*[55] appreciation was caused by fluctuations in the international currency market, and was deemed passive. In *Myers v. Myers*[56] appreciation caused by favorable change in the dollar/yen exchange ratio was deemed passive.

Similarly, in *Jolis v. Jolis*,[57] the court held that a wife is not entitled to equitable distribution in the increase of the value of her husband's business where the increase in value was the result of, among other items, an explosion in the demand for diamonds.

COMMUNITY PROPERTY APPROACH

For over 75 years, many community property states, particularly California, have addressed the allocation of passive and active appreciation of a separate business.[58] Similar to New Jersey, the underlying philosophy of community property law is to view marriage as an economic partnership akin to a joint enterprise. Under community property law, the partnership encompasses all property generated during marriage by the effort of each spouse, and both spouses are awarded an equal interest.[59] If the increase in a separate asset is passive, it is not a part of the community estate as long as no community resources were used for the asset. If the asset increases due to the effort of either party, it is part of the community.

The time, toil and talent of each spouse is perceived to be a community asset.

To reach a fair result, community property law created the doctrine of reimbursement: "The fundamental purpose of the doctrine is to bring back into the community estate value which was created by community contributions, but which took the form of appreciation in the value of a separate asset."[60]

Two approaches used by most community property states to allocate active from passive increases are enunciated in the California cases of *Pereira v. Pereira*[61] and *Van Camp v. Van Camp*.[62]

Pereira *Approach*

The *Pereira* approach provides a reasonable annual rate of return for the separate capital invested in the business. The value of this capital, plus the annual rate of return on the capital, is the separate property claim. The community property claim is the amount, if any, by which the value of the business at dissolution exceeds the separate property claim.[63]

For example, if the business, prior to marriage, had capital invested into it totaling $100,000, the reasonable rate of return was six percent per annum, the marriage lasted 10 years and the business is now worth $500,000, the appreciated value of the business subject to community property would be $340,000, or $500,000 (value of business) minus $100,000 (capital) minus $60,000 (10 years of reasonable return on $100,000 at six percent).

In *Pereira,* at the time of the marriage, the defendant husband had invested $15,500 in a successful saloon and cigar business.[64] After the marriage, this fund remained in the business and contributed to its success.[65] The Supreme Court of California recognized the importance of this premarital investment in the success of the business, and articulated the policy for crediting the defendant for his capital investment as follows:

> It is true that it is…clearly shown that the principal part of the large income was due to the personal character, energy, ability, and capacity of the husband. This share of the earnings was, of course, community property. *But without capital he could not have carried on the business. In the absence of circumstances showing a different result, it is to be presumed that some of the profits were justly due to the capital invested.* There is nothing to show that all of it was due to defendant's efforts alone. The probable contribution of the capital to the income should have been determined from all of the circumstances of the case, and *as the business was profitable it would amount at least to the usual interest on a long investment well secured.*[66]

California courts have applied the legal rate of interest to the capital.[67] In a New Mexico case, the court applied the "rate of interest the community would have had to pay for a loan of such capital."[68] New Mexico and California courts have also considered "the prevailing rate of a well-secured investment."[69]

Courts have also applied the "normal growth rate of businesses of the type owned by the spouse during the period involved in the geographical area where the business is located."[70] This "average rate of return" approach allows the court to apply different rates of return to different types of separate property businesses.[71]

After the Court determines the reasonable rate of return, additional complex issues arise, such as whether the rate of return should be compounded and whether the business's goodwill at the time the asset is acquired should be included in calculating the value of the business at the time of dissolution.[72] In addition, courts have adopted different approaches to computing the "increase in value" during the marriage.[73]

> Most courts have applied *Pereira* by comparing the value of a business at the time of marriage to the value at the time of dissolution by using a fixed rate of return.[74]

However, Nevada courts have adopted a year-by-year accounting.[75]

Van Camp *Approach*

The other method for valuing the enhanced value of a separate business is called the *Van Camp* formula. This method gives the community estate the difference between the compensation received and reasonable compensation for the effort performed.

For example, if the business owner's compensation is $100,000 per year and reasonable compensation would be $150,000 a year, the difference of $50,000 would be multiplied by the number of years of the marriage and be subject to community property. The remainder of the business would be separate property.

In *Van Camp,* at the time of the marriage, the defendant husband was a successful businessman as president and manager of Van Camp Sea Food Company.[76] The California Court of Appeals articulated the following explanation in support of its new approach to distribution of property:

> While it may be true that the success of the corporation of which defendant was president and manager was to a large extent due to his capacity and ability, nevertheless without the investment of his capital in the corporation he could not have conducted the business, and while he devoted his energies and personal efforts to making it a success, he was by the corporation paid what the evidence shows was an adequate salary, and for which another than himself with equal capacity could have been secured. Had such course been pursued and defendant contented himself merely with the receipt of dividends from the business, the character of the dividends as separate property could not have been

> questioned. Instead, however, of doing this, he entered upon the duties as manager of the corporation, gave his exclusive time and efforts thereto, for which he received [a salary].…It is impossible to say what part of the enormous dividends paid by the Van Camp Sea Food Company should be apportioned to the skill and management thereof and what part should be apportioned to the investment of the capital and the favorable conditions under which business was conducted.…*In view of the fact that [defendant] was adequately paid by the corporation for his services, such compensation… must be deemed the extent of his personal earnings, and the balance of the profits derived from the business accredited to the use of the capital invested therein, in the same manner as though he had not been employed by the corporation.*[77]

Van Camp has since been interpreted to allocate to the community an *annual sum* equal to the salary that would have to be paid an employee rendering services equivalent to the husband's minus the salary or compensation received by that employee.[78]

In an Arizona case, *Rowe v. Rowe,*[79] the court of appeals affirmed the trial court's application of *Van Camp.* Although the court found that the predominant cause of growth was due to the owner's efforts, it did not award any of the appreciation in the business to the wife. The court reasoned that other factors caused the growth in the business, such as the marketing efforts of a manufacturer the company represented, population growth, inflation, increased consumer buying power, demand for electronics and sales efforts by third parties.

The court concluded that 75 percent of the enhanced value was active effort. However, since the community had received 75 percent of the distributable earnings, including distributions, pension and profit sharing distributions, the community had been fairly compensated.

In affirming the trial court, the appellate court stated, "our courts have previously recognized that a community may be fairly compensated by salaries and draws received prior to dissolution."[80] In essence, the court held that the work effort of the husband was compensated by way of income and assets derived from the business during the marriage, which presumably both parties shared or will share as part of the community property.

Van Camp and *Pereira* are very early cases; yet, they are still followed in community property states today. In *Beam v. Bank of America,*[81] the California Supreme Court discussed the importance of these cases at great length. ***However, the California Supreme Court noted that despite the adoption of these two approaches, "our courts have developed no precise criterion or fixed standard" for apportioning such property.***[82] The Court further instructed that courts can follow either approach:

> In applying this principle of apportionment the court is not bound either to adopt a predetermined percentage as a fair return on business capital which is separate property (the *Pereira* approach) nor need it limit the community interest only to a salary fixed as the reward for a spouse's service (the *Van Camp* method) but may select whichever formula will achieve substantial justice between the parties.[83]

When the appreciation is mostly active, *Pereira* is preferred; when the appreciation is mostly passive, *Van Camp* is preferred.[84] In his article, J. Thomas Oldham proposes the following approach when selecting either the *Pereira* or *Van Camp* method:

> As a general rule, courts should determine whether the increase in value during marriage was primarily due to a spouse's efforts or due to separate property capital. If the former is true, the approach should be applied that yields the greatest community claim. If capital is the most significant factor, the approach that yields the largest separate property claim should be chosen.[85]

Both approaches may be unfair. Under *Pereira*, the non-owning spouse could argue that the return on the capital was brought about as a result of his or her spouse's active effort. *Van Camp* is unfair because no matter how much the business appreciates or depreciates, the court only looks at the difference between reasonable compensation and actual compensation.

CONCLUSIONS

Under New Jersey law and other jurisdictions, appreciation of a separate or immune business is equitably distributed provided it is caused by direct or indirect marital contributions. Efforts of a non-owning spouse as a homemaker and caretaker of children is an indirect contribution that entitles that spouse to equitable distribution of the enhanced business asset.

New Jersey and other equitable distribution states have not developed a formula to allocate passive and active increases in a separate business that is subject to equitable distribution. Nevertheless, New Jersey law does immunize passive appreciation of a separate asset. The case law of other equitable distribution states underscores the need to critically examine the facts and circumstances that gave rise to the appreciation of the business. Some factors that have been upheld in equitable distribution states include: the impact of third parties, changes in government regulations, market fluctuations, inflation, and consumer demand.

Community property states have relied on the *Van Camp* or *Pereira* approach to develop a formula for calculating the active and passive portion of the increase in a separate asset. Although these methods may be popular in community property states, no equitable distribution states have adopted either method.

The formula approach oversimplifies the evaluation without analyzing the myriad of facts that caused the increase.

The cause or reason for a separate asset's appreciation is relevant to both the valuation of the asset (to exclude passive increases) and the statutory factors relevant to the distribution of the asset. Pursuant to N.J.S.A. 2A:34-23.1(i), the court is directed, when equitably distributing assets, to consider "the *contributions* of each party to the acquisition, dissipation, preservation, depreciation, or *appreciation* in the amount or value of the marital property, as well as the contribution if the party is a homemaker." (emphasis added).

In either case, each party to an action must vigilantly marshal all relevant facts related to the passive or active appreciation of a separate business subject to equitable distribution. ■

ENDNOTES

1. A separate asset is also known as an immune asset, *Scavone*, 230 N.J. Super. 482 (Ch. Div. 1988) and includes premarital, gifted or inherited assets. Hereinafter a separate asset shall also be called an immune asset.
2. *Scherzer v. Scherzer*, 136 N.J. Super. 397 (App. Div. 1975).
3. 252 N.J. Super. 635 (App. Div. 1991).
4. 65 N.J. 196 (1974).
5. *Painter*, 65 N.J. at 214.
6. *Id.*
7. 136 N.J. Super. 397 (App. Div. 1975).
8. *Id.* at 400-01.
9. 147 N.J. Super. 5 (App. Div. 1977).
10. *Id.* at 9.
11. 174 N.J. Super. 107 (1980), *rev'd on other grounds*, 86 N.J. 515 (1981).
12. *Id.* at 112-13.
13. 226 N.J. Super. 281 (App. Div. 1988) *cert. den'd.* 114 N.J. 287 (1989).
14. *Id.* at 289-90.
15. *Rothman v. Rothman*, 65 N.J. 219, 229 (1974).
16. 230 N.J. Super. 482 (Ch. Div. 1988), *aff'd* 243 N.J. Super. 134 (App. Div. 1960).
17. *Id.* at 486.
18. *Id.* at 487.
19. *Id.*
20. *Id.* at 488.
21. *Id.* at 488 (*citing Griffith v. Griffith*, 185 N.J. Super. 382, 385 (Ch. Div. 1982).
22. 252 N.J. Super. 635 (App. Div. 1991).
23. *Id.* at 642.
24. *Id.* at 641.
25. *Id.* at 643.
26. *Id.*
27. *Id.* at 649.
28. *Id.* at 644.
29. 309 N.J. Super. 334 (App. Div. 1998).
30. Frank A. Louis, Premarital Assets: Proving and Defending Against Claims of Distributability, at 19, Family Law Symposium (1999).
31. 348 N.J. Super. 374 (Ch. Div. 2001).
32. *Id.* at 380-81.
33. *Id.* at 381.
34. *Sculler*, 348 N.J. Super. at 381.
35. 308 N.J. Super. 243 (App. Div. 1998).
36. 256 N.J. Super. 90, 93 (App. Div. 1992).
37. Brett R. Turner in his article Distinguishing Between Active and Passive Appreciation in Separate Property: A Suggested Approach, 13 No. 5 *Div. Lit.* 73, May 2001, notes at page 5 that:

    > Nationwide, case law is divided on who bears the burden of proof in classifying appreciation in separate property. One group of states places the burden of proof upon the spouse who claims that the appreciation is active. *See Waring v. Waring,* 747 S.2d 252 (Miss. 1999); *Knapp v. Knapp,* 874 S.W. 2d 520 (Mo. Ct. App. 1994)...Another group of states places the burden of proof upon the spouse who claims that the appreciation is passive. *See...Cockrall v. Cockrall,* 124 AZ 50, 601 P. 2d 1334 (1979); *Massis v. Massis,* 551 So. 587 (Fla. Dist. Ct. App. 1989)...

38. In *Somers v. Somers,* 203 A.D. 2d. 975; 611 N.Y.S. 2d. 971 (1994), the court held that government inflation statistics could be used as a basis for determining what portion of the appreciation of real estate was due to inflation or other market forces.
39. Brett R. Turner, Distinguishing between Active and Passive Appreciation as Separate Property, A Suggested Approach, 13 No. 5 *Div. Lit.* 73 (May 2001).
40. *Id.*
41. 355 Pa. Super. 589 (1986).
42. *See Oxley v. Oxley,* 695 S. 2d. 364 (Fla. Dist. Ct. App. 1997) (Appreciation of the value of the business was entirely nonmarital. Even though the husband was the chief executive officer, most of the real management work was done by third parties, and the husband had medical problems which apparently limited his ability to manage the company.).
43. *Porter v. Porter,* 67 Ariz. 273, 195 P. 2d. 132 (1948).
44. 474 N.W. 2d. 843 (Minn. Ct. App. 1991).
45. *See also, Smith v. Smith,* 197 W.Va. 505, 475 S.E. 2d. 881 (1996).
46. 17 Va. App. 12, 435 S.E. 2d. 407 (1993).
47. 235 A.D. 2d. 1002, 653 N.Y.S. 2d. 180 (1997).
48. 132 Md. App. 207, 752 Ap.2d. 291 (2000).
49. 654 So. 2d. 616 (Fla. Dist. Ct. App. 1995).
50. 197 W.Va. 290, 475 S.E. 2d. 382 (1996).
51. *Tibbetts v. Tibbetts,* 2000 M.E. 210, 762 A.2d. 937 (Me. 2000), *Hall v. Hall,* 462 A.2d. 1179, 1182 (Me. 1983).
52. 221 A.D. 2d. 712, 632 N.Y.S. 2d. 895 (1995).
53. 676 S.W. 2d. 817 (Mo. 1984).
54. *Harrison v. Harrison,* 912 S.W. 2d. 124 (Tenn. 1995).
55. 658 A.2d. 217 (M.E. 1995).
56. 70 Haw. 143, 764 P. 2d. 1237 (1988).
57. 98 A.D. 2d. 692, 470 N.Y.S. 2d. 584 (1st Dep't. 1983).
58. The eight community property states are Arizona, California, Idaho, Louisiana, New Mexico, Nevada, Texas, and Washington. David W. Reinecke, *Community Property Issues for Non-community Property Practitioners,* SH092 ALI-ABA 1129, 1132 (June 2003). In addition, Wisconsin follows a marital property system that is a form of community property, and in 1998, Alaska adopted an elective community property system. *Id.* at 1132-33. It is important to note that Texas follows a different method of classification than other community property states. Bee Ann Smith, The Partnership Theory of Marriage: A Borrowed Solution Fails, 68 *Tex. L. Rev.* 689, 710 (March 1990). This approach is called the inception-of-title rule that is described as follows:

    > Under this doctrine, a separate asset brought into the marriage remains exclusively separate property, even if community funds or labor enhance its value or contribute to its purchase. This rule also applies to separate property acquired dur-

ing marriage by gift or inheritance or from the proceeds of separate property. The rule advocates a snapshot test of ownership based on the marital property rights on the day that title or claim of title arose. This classification is fixed forever and may not be altered by subsequent contributions of time or funds. The inception-of-title rule permits only one adjustment: reimbursement, an equitable remedy based on unjust enrichment. Reimbursement is justified when the funds or energies of the marital estate benefit one spouse without the community's receiving an equivalent benefit. *Id.* at 710.

59. J. Thomas Oldham, Symposium: The Continuing Evolution of American Community Property Law: Separate Property Businesses That Increase in Value During Marriage, 1990 *Wis. L. Rev.* 585 (May/June 1990).
60. *Id.*
61. 156 Cal. 1 (Cal. 1909).
62. 53 Cal. App. 17 (1921).
63. Oldham, *supra* at 587 (internal citations omitted). It is important to note that both Arizona and Nevada formerly adopted an all or nothing approach to computation, which focused on the "primary cause of an increase in value of a business during marriage." Oldham, *supra* at 592.

If the primary cause was the separate property capital, the increase was separate property; if the primary cause was the effort of one or both spouses, the increase was community property. Pursuant to this approach, courts developed rules of thumb for different types of businesses. An increase in value of a hotel or a nursery was deemed separate property; in contrast, increases in the value of pool halls, restaurants, saloons or bakeries were considered community property. This all or nothing approach was not considered sufficiently precise in most community property states. Indeed, both Arizona and Nevada finally abandoned it. Most courts and writers agree that the all or nothing approach is not a good rule. *Id.* (internal citations omitted).

64. *Pereira,* 156 Cal. at 6.
65. *Id.* at 7.
66. *Id.*
67. *Id. See Pereira, supra* (seven percent interest); *Price v. Price,* 217 Cal. App. 2d 1 (1963) (seven percent interest); *Weinberg v. Weinberg,* 67 Cal. 2d 557 (1967) (seven percent interest); *Elliott v. Elliott,* 162 Cal. App. 2d 350 (1958) (six percent interest); *Margolis v. Margolis,* 115 Cal. App. 2d 131 (1952) (six percent interest)).
68. *Id.* at 601, n.90 (*citing Gillespie v. Gillespie,* 84 N.M. 618 (1973)).
69. *Id.* (*citing Jones v. Jones,* 67 N.M. 415 (1960); *Randolph v. Randolph,* 118 Cal. App. 2d 584 (1953); *In re Neilson's Estate,* 57 Cal. 2d 733 (1962)).
70. *Id.* at 601, n.91 (*citing In re Marriage of Folb,* 53 Cal. App. 3d 862 (1975)).
71. *Id.* at 601-02.
72. *Id.* at 603.
73. *Id.*
74. *Id.*
75. *Cord v. Cord,* 94 Nev. 21, 27 (1978).
76. *Van Camp,* 53 Cal. App. at 24.
77. *Id.* at 28-29.
78. *Cord v. Cord,* 94 Nev. 21 (1978).
79. 154 Ariz. 616, 620 (1987).
80. *Id.* at 621.
81. 6 Cal. 3d 12 (1971).
82. *Id.* at 18.
83. *Id.*
84. Turner, *supra.*
85. Oldham, *supra* at 588-89 (internal citations omitted).

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