VALUATION AND DISTRIBUTION IN CHANGING TIMES

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Judges and matrimonial practitioners alike now recognize they can no longer rigidly apply archaic law to the uncontrovertibly new and unpredictable economic times in selecting a proper valuation date for an active business asset that needs to be equitably distributed. This CLE lecture is designed to explain why the historical precedent that formerly dictated the determination of a proper valuation date has eroded in response to our volatile economy.

I. Valuation Date

Domestic Relations Law §236 Part B, Subdivision 4, paragraph B provides:

> As soon as practicable after a matrimonial action has been commenced, the court shall set the date or dates the parties shall use for the valuation of each asset. The valuation date or dates may be anytime from the date of commencement of the action to the date of trial.

The New York State Legislature in its Memorandum that accompanied the DRL legislation in 1980 recognized the flexibility that courts must have in fixing a valuation date. It reads:

> An important aspect of the legislation is the flexibility which is incorporated due to the tremendous variation in marital situations and the equities involved. Flexibility, rather than rigidity, is essential for the fair disposition of a given case.

While DRL §236(B)(4)(b) appears to invite motion practice, until recently, practitioners observed certain seemingly hard and fast valuation date rules that seemed to obviate that motion practice.

II. Active v. Passive Assets

Historically, the courts applied a simple test in determining whether a particular asset should be valued as of the date of commencement or the date of trial. Essentially, if the asset's growth or decline was in part attributable to the efforts of the spouse in control of that asset, then the proper valuation date was almost universally set as of the date of the commencement. In contrast, those assets that grow or decline based solely on market fluctuations, were and will continue to be valued as the date of trial. *See, Grunfeld v. Grunfeld*, 94 N.Y.2d 696, 731 N.E.2d 142 (2000); and *McSparron v. McSparron*, 87 N.Y.2d 275, 662 N.E.2d 745 (1995).

The predicate for these distinctions is to protect the non-titled spouse from a downward manipulation of the value during the pendency of the action and to protect the titled spouse from the distribution of post-commencement appreciation due solely to the titled spouses' efforts.

Set forth below are several cases that illustrate this dichotomy:

- In *Ferraioli v. Ferraioli,* 295 A.D.2d 268, 744 N.Y.S.2d 34 (1st Dept. 2002) the Appellate Division held that a securities account managed by husband was an "active" asset and would be valued as of date the wife commenced her divorce action rather than the trial date, although the husband was prohibited from removing the funds from the account as a result of the *pendente lite* stipulation with his wife and despite the fact that the account sustained significant losses during period of overall stock market decline. Because the husband made all transaction decisions reflecting his own investment strategies, he was charged with the responsibility for the losses caused by both his trades and market fluctuation.

- In *Naimollah v. DeUgarte,* 18 A.D.3d 268, 795 N.Y.S.2d 525 (1st Dept. 2005), the court held that capital losses from account managed by wife's broker would be considered active, rather than passive, for purposes of distributing marital property upon divorce.

- In *Daniel v. Friedman,* 22 A.D.3d 707, 803 N.Y.S.2d 129 (2nd Dept. 2005), the Second Department affirmed the trial court's date of commencement valuation date despite economic downturn during the pendency of the action where the business was rebounding and there were signs of potential positive growth for the future.

- In *Kerzner v. Kerzner,* 264 A.D.2d 338, 694 N.Y.S.2d 49 (1st Dept. 1999), the First Department held that a date of commencement valuation was appropriate for a sole proprietorship where the value of the business was greatly affected by the husband's participation.

Like the date of trial valuation date routinely given to the marital residence, businesses that are linked to real estate market fluctuations have often been valued as of the date of trial.[1]

- In *Wegman v. Wegman,* 123 A.D.2d 220, 509 N.Y.S.2d 342 (2nd Dept. 1987), the Second Department realized that with some assets a commencement date valuation may be inappropriate. In *Wegman,* the action was commenced in 1981 and the trial on the economic issues did not occur until 1985. The court held:

> During a delay of this kind, many assets, <u>particularly businesses such as that involved in the case at bar</u>, may experience fluctuations that might dramatically change the logic of the distribution. Under such circumstances, the valuation of assets close to the time of trial may result in the formulation of an award consistent with the purpose of equitable distribution and insure that each spouse receives a fair share of the family assets accumulated while the marital relationship endured.

[1] *Morton v. Morton,* 69 A.D.3d 693, 892 N.Y.S.2d (2nd Dept. 2010).

- In *Smerling v. Smerling*, 177 A.D.2d 429, 576 N.Y.S.2d 271 (1st Dept. 1991) the Court held that although the value of an active asset should generally be valued as of date of commencement, the trial court did not abuse its discretion in valuing husband's chain of movie theaters as of date of sale, which occurred during pendency of divorce action; while there was evidence that husband enhanced value of chain, increase in value was never quantified by husband's expert and it was clear that increase was primarily due to market conditions.

- In *Sagarin v. Sagarin*, 251 A.D.2d 396, 674 N.Y.S.2d 127 (2nd Dept. 1998), the Court held that the valuation of husband's business as of trial where the business' value declined because of economic forces outside of husband's control.

- In *Butler v. Butler*, 256 A.D.2d 1041, 683 N.Y.S.2d 603 (3rd Dept. 1998), the Court valued the husband's business as of the date of trial, holding that:

  > The Husband's business was properly valued at the time of trial in divorce action where the valuation at date action was commenced would have been inequitable; husband filed for bankruptcy after commencement of action but before trial, a valuation as of commencement of action would have resulted in inaccurate income, revenue and asset valuations, due to the forced sale of business assets at an auction ordered in the bankruptcy proceeding, and the bankruptcy was not attempt by husband to avoid financial consequences of divorce.

The Courts seldomly applied a trial date valuation for small businesses absent an indisputable business collapse.

III. Economically Volatile Times

In the advent of the 2009 catastrophic collapse of AIG, Lehman Brothers, Citigroup, among many other privately held and publicly traded businesses, a new valuation order emerged that acknowledges that economic fluctuations affect the value of a spouse's business just like real estate market fluctuations affect the value of our homes.

Virtually all small businesses have had to endure the ripple effects of a down economy that they did not create to shortchange their spouse. In the context of 2009 matrimonials, many divorcing business owners suffered an unavoidable and bona fide diminution in revenues that legitimately crippled some and destroyed others. Acknowledging that the traditional approach would prove inequitable, judges have now become more receptive to that reality and more flexible in their approach to the valuation date issue.

Commenting recently in their New York Law Journal article, *Setting Valuation Dates for Marital Property in a Global Economic Crisis.* 10/14/2009 N.Y.L.J. 4, (col.1) about the need for a new approach to valuation, Allan E. Mayefsky and Alyssa A. Rower stated:

> "The obvious weakness with the "active/passive" analysis is that it takes courts away from an individualized, case by case analysis and toward a rigid, inflexible approach that ceases to produce equitable results when economic conditions change. As Ralph Waldo Emerson has written, " A foolish consistency is the hobgoblin of little minds". There is growing evidence that bubble and crashes are not anomalous and a steady framework is needed. Between 1945 and 2001 the average business cycle, the periodic but irregular up and down movement in economic activity was a little over 5.5 years. Therefore, a New York divorce that takes more than two or three years is likely to overlap a major shift in the economy. A rule that disregards business cycles and assumes the rise and fall in the value of 'active' assets is always caused by the efforts of one spouse in untenable."

Heeding the thoughtful valuation discourse that has emerged, the Appellate Division most recently held in *Morton v. Morton,* 69 A.D.3d 693, 892 N.Y.S.2d (2nd Dept. 2010) that:

> The lower court erred in valuing marital assets, which consisted of multiple business entities which owned commercial real estate properties and acted as the landlord for industrial and manufacturing tenants, as of the date of commencement of the action rather than as of the date of trial. In that case, the husband proffered evidence that a decrease in the value of assets since the date of commencement of divorce action was attributable to market forces and, thus, was passive in nature, and there was no evidence that a decline in the value of assets was due to dissipation or wasteful conduct on the part of the defendant.

Similarly, in a NYSBA Family Law Review article written by Martin P. Randisi entitled *How to Apply the Principles of Business Valuation During This Recession.* (Spring 2009, Vol. 41, No.1), he opined:

> It has often been said that the simplest explanation of value is "The value of a business is the present value of the *future* cash flows." The emphasis here is on the future cash flows. The fear in this recession is that appraisers, attorneys, and judges may just think the typical valuation report which uses the historical past as a proxy (such as the average earnings of the last five years) to estimate cash flow is the only way to do it. Well, in today's recession that method will most likely not be accurate.

IV. Valuation Date Motion Practice

Absent a pretrial determination on the valuation date issue, to play it safe, attorneys are obliged to present evidence on a value as of the date of commencement and as of the date of trial. That double valuation effort is not likely to be avoided through motion practice. A sampling of our edited and scaled down motion practice is annexed as **Exhibit "A"**, along with the decisions rendered by two different judges in the context of two cases where each of the business owners complained about a post-commencement downturn in business and sought the Court's intervention on the valuation date conundrum. As the pertinent portions of those decisions read, whatever happens to a business between commencement and trial now matters. Unfortunately, an issue of fact can be raised regarding the willful conduct of the titled spouse that precludes a resolution on papers alone.

A. Economic Factors Need to be Highlighted

(i) If the Court grants a hearing on the valuation issue, request that Court to take judicial notice of articles recounting the depressed or unpredictable state of the general economy - - have your client clue you in on relevant industry-wide data and publications.

(ii) The presentation of the decline of a small business must be explicit and logical. Any unavoidable decrease in revenue or increase in expenses or a business owner's inability to obtain needed credit needs to be fully explicated to avoid the contrary 'RAIDS' acronym - - i.e. Recently Acquired Income Deficiency Syndrome. Again, the practitioner must be mindful that before 2009, the Courts viewed a businessman's tale of woe as presumptively contrived or orchestrated. Indeed, to achieve his best result, a businessman is understandably apt to convolute a diminishment in business profits. Hence, the Courts traditionally resolved that intellectual dilemma by rejecting the businessman whine. For example, in *Elliot F. v. Anthony S.F.,* (9/4/2007 N.Y.L.J. 20, (col.1) the court held that where the defendant divested himself of assets and significantly reduced his income, he converted the case "into what some in the legal profession so cynically refer to as a "RAIDS" case, i.e. 'Recently Acquired Income Deficiency Syndrome'. Be thorough in your utilization of the business bookkeeper and accountant in your trial presentation. Wherever a downward trend can be established it helps to establish that the decline is bona fide and more than a business hiccup.

In part to remedy the potential inequity of choosing an improper valuation date, judges have begun a trend that has delighted the alleged 'monied' spouse. Awards to the non-titled spouse of an equitable share of the value of a business, professional license, advanced degree or other judicially identified asset that enhances the holder's earning potential, are now on a steady decline.

V. Percentages of Distributions

Set forth below are a healthy sampling of Appellate Division's handiwork in valuing and distributing businesses and "enhancements". Be alert to the fact that professional medical, dental and chiropractic practices are often susceptible to a valuation method known simply as a 'rule of thumb' that often are the offspring of historical sales of similarly situated practices.

A. Distributions of Business Interests

- *Kerrigan v. Kerrigan*, 3/15/2010, NYLJ, p. 28 (col. 6), the Second Department affirmed a **35%** distribution of the appreciation of the plaintiff's business interests.

- *Rodriguez v. Rodriguez*, 2010 NY Slip Op 00944 (2nd Dept. 2010), the Second Department affirmed a **30%** distribution of the husband's enhanced earnings derived from his medical license and **25%** of the husband's medical practice.

- *Peritore Peritore*, 66 A.D.3d 750, 888 N.Y.S.2d 72 (2nd Dept. 2009), the Second Department reduced the plaintiff's entitlements in defendant's dental practice from **40%** to **15%**.

- *Ciampa v. Ciampa*, 47 A.D.3d 745, 850 N.Y.S.2d 190 (2nd Dept. 2008), the Second Department affirmed a 35% distribution of the husband's business interests to the wife where she was the primary caretaker of the parties' children and abandoned her career as an attorney.

- *Harris v. Harris*, 242 A.D.2d 558, 662 N.Y.S.2d 532 (2nd Dept. 1997) In a short term marriage of 4 years, wife was awarded **10%** of husband's dental practice where she showed only minimal contributions to the practice.

- *Arvantides v. Arvantides*, 64 N.Y.2d 1033, 489 N.Y.S.2d 58 (1985) the Court of Appeals held that in a long term marriage where the wife was a homemaker, she was entitled to 25% of the husband's dental practice.

- *Morton v. Morton,* 130 A.D.2d 558, 515 N.Y.S.2d 499 (2nd Dept. 1987) the wife was awarded 33% of husband's podiatry practice, where husband attended podiatry school during the marriage and the parties were married 19 years.

- *Kohl v. Kohl*, 6 Misc.3d 1009, 2004 WL 3106726 (N.Y. Sup.) Wife was awarded **35%** of husband's business as an independent contractor where it was a long term marriage of 25 years and wife was a homemaker.

B. **Distribution of Enhanced Earnings**

As the cases set forth below illustrate, the percentage of the equitable distribution of EEC's are on a more noticeable decline:

- *O'Halloran v. O'Halloran*, 58 A.D.3d 704, 873 N.Y.S.2d (2nd Dept. 2009) **20%**

  (where the Second Department held that 20% was proper.)

- *Kriftcher v. Kriftcher*, 59 A.D.3d 392, 874 N.Y.S.2d 153 (2nd Dept. 2009) **10%**

  (where the wife's minimal contributions to the husband's attainment of his degree and one license entitled her to only ten percent of the present value of the attainment of enhanced earnings.)

- *Guha v. Guha*, 61 A.D.3d 634, 877 N.Y.S.2d 151 (2nd Dept. 2009) **5%**

  (where the evidence at trial established that the husband made minimal financial contributions to the marriage and he failed to demonstrate that he made substantial contributions to the wife's attainment of her license to practice medicine in the United States.)

- *Mairs v. Mairs*, 61 A.D.3d 1204, 878 N.Y.S.2d 222 (3rd Dept. 2009) **25%**

  (where the Wife was entitled to 25% value of husband's medical license and practice, during the marriage, husband successfully completed undergraduate studies, attended medical school, earned medical degree, and completed internship and residency, after which he established successful medical practice, and while husband pursued his medical career - wife gave birth to the parties seven children, cared for them, managed the household and earned a salary that was for a time the principal source of the family's income, she also relocated the family from Utah to Philadelphia and later to New York to allow husband to pursue his medical studies and obtain medical license, and when, husband entered private practice, wife managed the practice.)

- *Jayaram v. Jayaram*, 62 A.D.3d 951, 880 N.Y.S.2d 305 (2nd Dept. 2009) **35%**

  (where the Second Department held Wife was entitled to 35% where she made substantial indirect contribution by supporting the husband's educational endeavors, working full-time and contributing her earnings to the family, being the primary caretaker of the parties' children, cooking family meals, and participating in household responsibilities.)

- *Schwartz v. Schwartz*, 67 A.D.3d 989, 890 N.Y.S.2d 71 (2nd Dept. 2009) **10%**

  (Where the Second Department held wife only made modest contributions to husband's enhanced earnings capacity from securities licenses during the marriage.)[2]

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[2]Enhanced Earnings Case Chart from "Tracking Enhanced Earnings" by Ronnie P. Gouz & Benjamin E. Schub, 1/25/2010, NYLJ p. 11.

Judge v. Judge, 48 A.D.3d 424, 851 N.Y.S.2d 639 (2nd Dept. 2008) **25%**

(where the Second Department held that based on the testimony of the parties, husband was entitled to 25% of the enhanced earnings of wife's MBA degree)

Higgins v. Higgins, 50 A.D.3d 852, 857 N.Y.S.2d 171 (2nd Dept. 2008) **0%**

(where the Second Department held that where only modest contributions are made by the nontitled spouse toward the other spouse's attainment of a degree or professional license, and the attainment is more directly the result of the titled spouse's own ability, tenacity, perseverance, and hard work, it is appropriate for courts making an equitable distribution in divorce cases to limit the distributed amount of that enhanced earning capacity. Here, husband failed to show that his contributions were substantial. Although he made some efforts to help, he never made career sacrifices or assumed a disproportionate share of household work as a consequence of wife's education; rather wife worked full time while attending school, funded some of her own educational costs, and was still the primary caregiver for the parties' children.)

Kaplan v. Kaplan, 51 A.D.3d 635, 857 N.Y.S.2d 677 (2nd Dept. 2008) **30%**

(where the Second Department held that an award of 30% of husband's dental practice and license was proper; the award took into account the limits of the wife's involvement with the practice and the attainment of the dental license, while not ignoring the direct and indirect contributions that she made).

Wiener v. Wiener, 57 A.D.3d 241, 868 N.Y.S.2d 197 (1st Dept. 2008) **10%**

(where the First Department held that 10% was proper.)

Simmons v. Simmons, 57 A.D.3d 1400, 871 N.Y.S.2d 559 (4th Dept. 2008) **15%**

(where the Fourth Department held that 15% was proper.)

Spreitzer v. Spreitzer, 40 A.D.3d 840 N.Y.S.2d 658 (2nd Dept. 2007) **20%**

(where the Second Department held that husband was entitled to 20% of value of wife's nurse practitioner degree and license constituting the enhanced earning capacity achieved by wife during the marriage, based upon husband's substantial economic as well as noneconomic contributions to the attainment of that enhanced earning capacity.)

Ochs v. Ochs, 40 A.D.3d 1061, 837 N.Y.S.2d 290 (2nd Dept. 2007) **25%**

(where the Second Department held that wife was entitled to a 25% share, rather than a 50% share, of the enhanced earning capability represented by husband's law degree and license, where wife supported husband during his last year and a half of law school, but did not sacrifice any educational or employment opportunities to do so.)

O'Donnell v. O'Donnell, 41, A.D.3d 447, 836 N.Y.S.2d 703 (2nd Dept. 2007) **30%**

(where the Second Department held that wife was entitled to 30% of husband's law degree based upon her contribution.) The court referred to but did not enumerate the specific contributions that influenced the "pot luck" percentage awarded to the non-titled spouse."

Midy v. Midy, 45 A.D.3d 543, 846 N.Y.S.2d 220 (2nd Dept. 2007) **25%**

(where the Second Department held that husband's contributions did not warrant an award of 50% of the wife's enhanced earning capacity resulting from her attainment of a master's degree in speech pathology during the course of the marriage where there was no evidence that the husband sacrificed any career opportunities during the time the wife was pursuing her degree; rather an award of 25% of the wife's enhanced earning capacity was appropriate.)

VI. The 'Double Dipping' Phenomena[3]

Exhaustive scholarly analyses on the double-dipping or double-counting phenomenon have adorned the pages of various legal publications since its initial recognition in *McSparron v. McSparron,* 87 N.E.2d 275, 639 N.Y.S.2d 265, 662 N.E.2d 745 (1995). As we all know, in *McSparron*, the Court of Appeals held that maintenance awards are not to be drawn from the income stream that was relied upon in the calculation of the value of an equitably distributed marital asset. And, as an integral part of that decision, the *McSparron* Court wisely cautioned the lower courts to be vigilant in fashioning maintenance awards to avoid double-dipping:

> Moreover, care must be taken to ensure that the monetary value assigned to the license does not overlap with the value assigned to other marital assets that are derived from the license such as the licensed spouse's professional practice. The courts must also be meticulous in guarding against duplication in the form of maintenance awards that are premised on earnings derived from professional licenses. *McSparron* at 286.

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[3] Much of this part of the written materials is taken from the article "A Keane Double-Dipping Miscalculation and the Vanishing Monied Souse" By Peter J. Galasso, Jeffrey L. Catterson and Joel Rakower; NYSBA Family Law Review, Winter 2008, vol. 40, No. 4.

Five years later, in *Grunfeld v. Grunfeld*, 94 N.Y.2d 696, 731 N.E.2d 142, 709 N.Y.S.2d 486 (2000), the Court of Appeals amplified the *McSparron* admonition as follows:

> Most significantly for the case at hand, *McSparron* also cautioned lower courts to "be meticulous in guarding against duplication in the form of maintenance awards that are premised on earnings derived from professional licenses" *(id.)*. To allow such duplication would, in effect, result in inequitable, rather than equitable, distribution. In contrast to passive income-producing marital property having a market value, the value of a professional license as an asset of the marital partnership is a form of human capital dependant upon the future labor of the licensee. The asset is totally indistinguishable and has no existence separate from the projected professional earnings from which it is derived. To the extent, then, *705 that those same projected earnings used to value the license also form the basis of an award of maintenance, the licensed spouse is being twice charged with distribution of the same marital asset value, or with sharing the same income with the nonlicensed spouse. *Grunfeld* at 704.

In both *McSparron* and *Grunfeld*, the proscription against double dipping was applied with equal force to the enhanced earnings that was produced by a law license. Those same double dipping safeguards were eventually applied to the dynamic between the value of a professional practice, like a law firm or medical practice, or of a business where the valuation was dependent on the conversion of the projected future income stream. As the Second Department held in both *Sodaro v. Sodaro*, 729 N.Y.S.2d 731 (2nd Dept. 2001), and *Murphy v. Murphy*, 6 A.D.3d 678, 775 N.Y.S.2d 370 (2nd Dept. 2004), when a business or practice is valued by converting a projected future income stream into a present value, that income stream is not to be utilized in the calculation of a maintenance award.

Heeding the direction given by *McSparron, Grunfeld,* and its progeny, matrimonial practitioners began to get a handle on the double-dipping dynamic and the arithmetic to be invoked in cases where a spouse attained a professional license during the marriage and thereafter utilized that license to create a practice that further enhanced his earnings. In constructing the valuation equations, forensic accountants would first calculate the actual as opposed to reported annual income of the owner of the professional practice. From that amount, a statistically based 'reasonable compensation' figure of the license holder is subtracted to arrive at the 'excess earnings' that the owner derives from the practice. If the license was obtained before the marriage, the arithmetic pertinent to the forbidden income stream would end here. However, if the license was obtained during the marriage, then the license value would be equitably distributed as well, resulting in the exclusion of two distinct income streams from the calculation of maintenance. To compute the value of enhancement derived from the license, the income of a comparably situated college student would be subtracted from the statistically higher average income of the license holder thereby identifying projected future income stream that would be unavailable in calculating an award of maintenance.

By way of example, assume that:

(i) Jake attained his law license and established his law practice during the marriage;

(ii) Jake earns $400,000 per year from his practice;

(iii) A comparably situated associate earns $200,000 per year; and

(iv) A comparably situated college graduate earns $100,000 pear year.

Based upon *Sodaro*, if the value of Jake's practice is equally distributed to his wife, then only $200,000 will be deemed available for an award of maintenance. If the value of Jake's license is also equally distributed to his wife, then a total of $100,000 of Jake's $400,000 annual income will be deemed available for an award of maintenance. Prior to *Keane v. Keane,* it seemed to make perfect sense that a spouse could not be permitted extract a share of the value of the title holder's license or practice, which are the vehicles that drive up one's earnings, and then also receive a second benefit from that asset, by sharing in the income created by that asset.

As contrasted with the double dipping issue in the context of a professional practice or service oriented business, *Keane v. Keane,* 8 N.Y.3d 115, 861 N.E.2d 98, 828 N.Y.S.2d 283 (2006), involved the equitable distribution of two real property assets. Specifically, the marital residence was awarded to the wife, while the parties' commercial building of comparable value was awarded to the husband. While the potential value of the marital residence as a rental was disregarded, the income actually generated by the commercial building was viewed as available income for the purposes of awarding the wife maintenance. Despite the husband's double-dipping lament, the Court of Appeals held:

> We do not see why an inquiry as to double counting should depend on the valuation method used. After all, any valuation of an income-producing property will necessarily take into account the income-producing capacity of that property. To prevent any income derived from any income-producing property from being "double counted" would, therefore, **4 significantly limit the trial court's considerable discretion in equitably distributing marital property and awarding maintenance. Significantly, we have already differentiated between a professional license and tangible income-producing property, because "where a professional license is at issue, '[t]he asset is totally indistinguishable and has no existence separate from the projected professional earnings from which it is derived' (*Grunfeld v Grunfeld*, 94 NY2d 696, 704 [2000]). Hence, a trial court must convert the enhanced earnings attributable to the license into a monetary marital asset to achieve equitable distribution. In contrast, a court can transfer title to real or

personal property in order to equitably distribute the asset" (Holterman v Holterman, 3 NY3d 1, 9 n 5 [2004]).

*122 We agree with dissenting Justice Goldstein that this distinction applies here.

Double counting may occur when marital property includes *intangible* assets such as professional licenses or goodwill, or the value of a service business. As we said in *Grunfeld*, "[i]n contrast to passive income-producing marital property having a market value, the value of a professional license as an asset of the marital partnership is a form of human capital dependant upon the future labor of the licensee" (94 NY2d at 704). It is only where "[t]he asset is totally indistinguishable and has no existence separate from the [income stream] from which it is derived" (*id.*) that double counting results.

Here, the rental property was split between the parties for distributive purposes. The rental income from that property was then considered in determining maintenance.

The property will continue to exist, quite possibly in the husband's hands, long after the lease term has expired, as a marketable asset separate and distinguishable from the lease payments. The mortgage payments, in contrast, were properly distributed as an asset and not counted for maintenance purposes because the payments themselves *were* the marital asset. (*Keane* at 121).

Many matrimonial practitioners were troubled by the *Keane* myopia, given the incongruency of awarding each party a million dollar asset, yet reserving for the wife a maintenance interest in the million dollar asset awarded to the husband. Clearly, the type of asset awarded should not confer an advantage upon one spouse over another. However, that is precisely what *Keane* concluded.

In *Griggs v. Griggs*, 44 A.D.3d 710, 844 N.Y.S.2d 351 (2nd Dept. 2007), the Second Department adapted the *Keane* analysis to the husband's medical practice and concluded that the husband's total income from the already equitably distributed practice was fair game in determining the maintenance to be awarded to the wife, which obviously conflicts with the Second Department's decision in *Sodaro,* where the value of a psychiatric practice was addressed and the double-dipping into its value proscribed. In rejecting the double-dipping contentions of the husband, the Second Department in *Griggs* stated:

> The plaintiff's contention that the court "double-counted" his Practice is without merit. The Court of Appeals recently held that the prohibition against double counting does not apply where, as here, the asset to be distributed is a "tangible income-producing asset," rather than an intangible asset, such as a professional license, the value of which can only be determined based on projected earnings (*see* Keane v. Keane, 8 N.Y.3d 115, 119, 828 N.Y.S.2d 283, 861 N.E.2d 98).

Judging by the absence of discussion on the issue, it appears that the *Griggs* panel failed to recognize that the hypothetical sale of a professional practice logically and economically relegates the titled spouse to a statistically based reasonable compensation level. In doing so, *Griggs* reversed the enlightened compartmentalization of the income of an owner or partner in a professional practice that was historically observed by forensic accountants in identifying the income stream created by a professional practice. The equation simply recognized the difference between the earnings of a business owner and a similarly experienced employee-professional.

Lawyers whose practices are substantial enough to justify hiring associates generally earn more than those lawyers who are his employees. Since law practices are not saleable except under certain defined circumstances, under *Griggs*, the Court can now award the non-titled spouse an interest in the value of the business, which is based on the same earnings that *Griggs* will now allow the Court to consider in calculating the maintenance award. Before *Griggs*, the excess earnings of the professional derived from the practice would have been excluded from maintenance award consideration. Indeed, if *Griggs* is to be followed, the only income stream that is to be excluded going forward is the income stream created by the license acquired during the marriage and which was previously equitably distributed.

It should be noted that in *Griggs*, the valuation methodology adopted by the forensic accountant did not reference the excess earnings produced for the owner of the professional practice being valued. As a result, no 'income stream' was identified in the valuation methodology that could be 'double dipped'. Misguidedly following *Keane*, the *Griggs* Court has effectively vitiated a double dipping concern in cases involving the equitable distribution of the value of a medical practice. Hence, despite *Keane* dicta that double dipping adjustments should not depend on the valuation methodology adopted by the valuator, the *Griggs'* Court applied *Keane* in narrowing the double dipping pool to cases involving licenses and other specified educational attainments that have the tendency to enhance one's earnings. By virtue of *Griggs*, professional practices that can be sold by reference to a formula that does not consider the owner's enhanced earnings will no longer warrant double dipping adjustments in the calculation of a maintenance award.

Returning once again to the twisted dictum of *Keane*:

> Double counting may occur when marital property includes *intangible* assets such as professional licenses or goodwill, or the value of a service business. As we said in *Grunfeld*, "[i]n contrast to passive income-producing marital property having a market value, the value of a professional license as an asset of the marital partnership is a form of human capital dependant upon the future labor of the licensee" (94 NY2d at 704). It is only where "[t]he asset is totally indistinguishable and has no

> existence separate from the [income stream] from which it is derived" (*id.*) that double counting results.

A potential key to the Keane, Griggs debacle lies within an often overlooked segment of appraisal reports provided for professional practices. It is referred to as the standard of value. The standard and premise of value typically assigned to a business entity in a divorce action within New York State is "fair market value" on an ongoing basis and assumes the premise of value in use; that is, one considers the business on the basis of an ongoing enterprise, on an "as is, where is" basis. The term "fair market value" is often defined as the most probable price that the business should bring if exposed for sale on the open market as of the valuation date. It assumes that the buyer and seller are each acting prudently and knowledgeably and that the price is not affected by any undue stimulus.

Unfortunately, the term "Fair Market Value," while holding standard acceptance by each of the four departments within New York as to non-service oriented businesses, is not so for professional or service oriented businesses, e.g., a solo practice neurosurgeon who, for all intents and purposes, cannot sell his/her practice. As an additional example, prior to the adoption of DR 2-111 in 1996, a lawyer in New York could not sell a legal practice and recognize "goodwill" (that amount which exceeds the net tangible assets of the practice or equity). Yet for purposes of a matrimonial dissolution, each has been assigned a value at times associated with the "goodwill" of the practice under the guise of the definition of fair market value. However, the term fair market value is a misnomer in that said definition recognizes that the asset can indeed be sold, recognizing in certain instances the existence of various discounts such as for a minority interest and marketability discounts.

A minority interest discount is measured in terms of the relative degree of control a minority owner has over the operation and important decisions made on behalf of the company. The concept of marketability, however, deals with the liquidity of an ownership interest, that is, how quickly and easily it can be converted to cash if the owner chooses to sell.

If one considers the fact that some professional practices cannot, in reality, be sold to a third party, then the resultant discount for lack of marketability would have to be 100%, hence, no value in terms of fair market value (at the very least, as to its application to the existence of goodwill). However, based upon case law in New York State, the application of discounts for minority interests and marketability have not been applied under the standard of value known as "Value to the Holder" which recognizes personal or professional goodwill.

The concept of "Value to the Holder" recognizes a form of human capital dependant upon the future labor of the licensee which is totally indistinguishable and has no existence separate from the [income stream] from which it is derived. Thus, it would appear that should the appraiser deviate from the standard of "fair market value" the concept of double dipping reappears. It is then incumbent upon the attorney to work with the appraiser to identify if, and to what extent the goodwill is personal in nature and not transferable and again within the realm of double dipping and the spirit of McSparron and Grunfeld.

To suggest in this economic climate that the courts have lost their way would be a colossal understatement. The so-called monied spouse has already been beaten down unmercifully by the absurd judicial recognition of intangible assets that only New York State continues to include on the marital balance sheet. In that regard, Justice Smith's dissent in *Holterman v. Holterman*, 3 N.Y.3d 1, 814 N.E.2d 765, 781 N.Y.S.2d 458 (2004), condemning the majority's misallocation of the monied spouse's earnings in that case, seems to have represented the beginning of the end of the monied spouse:

> "[The majority has imposed] a very significant burden on defendant–to require him, for several years, to pay to his ex-wife more than two thirds of his net income, and even in the more distant future to pay her as much as he keeps for himself. Defendant's brief in this Court contains the following chart, which summarizes the burden on him in the first year following Supreme Court's award:
>
> Income
> $181,837 ________________
>
> Minus FICA (1233)
> ($ 7,403) ________________
>
> Minus Maintenance
> ($35,000) ________________
>
> Minus Taxes
> ($46,882) ________________
>
> Minus Child Support
> ($34,875) ________________
>
> Minus Equitable Distribution (with interest)
> ($21,288) ________________
>
> Minus Attorney's Fees
> ($20,000) ________________

NET MONEY AVAILABLE FOR DEFENDANT APPELLANT

$16,389

> Plaintiff's brief notes, correctly, that the $20,000 attorneys' fee payment is a one-time obligation. With that exception, *17 however, plaintiff takes no issue with the above-quoted calculation. Even if the attorneys' fees are ignored, defendant is left with approximately $36,000 of a pretax income of $181,000.
>
> It is true that the burden on defendant remains at this level only for four years after the award; after that, child support will be reduced because the parties' older child will become emancipated, and a year later maintenance will drop to a lower level pursuant to Supreme Court's order. But even then, the burden will be a major one. My own calculations suggest that, assuming defendant's income does not much change (and again ignoring the attorneys' fee award) defendant is required to pay more than two thirds of his after-tax income to plaintiff for the first four years; some 60% in the fifth year; about half of it in years 6 through 10; and nearly a third of it for five years after that. It is not until 15 years after the award that defendant's obligations (at that point consisting only of maintenance) diminish to something like 12% of his income (calculating both the income and the obligations on an after-tax basis).
>
> When income-producing property is owned by a husband or wife who is divorced, it is often appropriate to order part or even all of it equitably distributed to the other spouse. When that is done, however, it makes no sense at all to calculate child support as though no such distribution had occurred–as though the transferring spouse still owned the asset and received the income it generated. Yet the majority concludes that this irrational procedure is required by the CSSA–as indeed it would be, except that the CSSA expressly permits departure from its formula to avoid an "unjust or inappropriate" result. *(Holterman* at 776).

To appreciate how pugnacious the law has become to the alleged monied spouse, the reader is invited to consider the following real world scenario in the context of an oppressive body of law. Suppose a husband brings to the marriage a $300,000 annual income as a highly paid associate in a New York City law firm. Having had two children with his previous wife, the husband pays annual support totaling $100,000 to his first wife over the first seven years of his marriage to his second wife.

Five years into his second marriage, the husband goes out on his own and over the next five years establishes his own general practice on Long Island and earns $300,000 from the practice by year ten. In year eleven, his second wife, who did not work during their marriage and who is now 53 years old, seeks a divorce, equitable distribution and lifetime maintenance.

As part of her attorney's letter-demand, the wife seeks one-half the value of his practice, which the forensic accountant determines is saleable at 1 times gross revenue or $600,000. As the cherry on her sundae, the wife demands a maintenance award based on the $300,000 derived from the practice. After eleven years of marriage, assuming a 50-50 division of marital estate, your client could owe his second wife a distributive award of $650,000 with 9% interest and pursuant to *Keane* be compelled to pay her lifetime maintenance based on income of $300,000.

If Dr. Holterman thought that he was left with virtually nothing for his own needs, consider the fate of the so-called monied spouse in our hypothetical, who now recognizes that being the monied spouse in New York State has become part of an evolving judicial vanishing act.

Subsequent to our article, the Second Department, in *Rodriguez v. Rodriguez*, 2010 NY Slip Op 00944 (2nd Dept. 2010), appeared to recognize the absurdity of utilizing the same income stream to obtain a value of a medical practice and to calculate maintenance in holding the lower court erroneously "double counted" the plaintiff's income in valuing his medical practice and remitted the matter to the trial court for recalculation.

However, less than a month later, in *Kerrigan v. Kerrigan*, 3/15/2010 NYLJ, p. 28, col 6, the Second Department, in citing to *Keane, supra,* and *Griggs, supra,* held:

> The plaintiff's contention that the Supreme Court engaged in "double dipping" with respect to the award of maintenance is without merit, as the plaintiff's business constitutes a tangible, income producing asset, rather than an intangible asset.

And the double-dipping beat goes on.