

Money, Money Everywhere, But Not a Cent for Support

A QDRO can be an effective enforcement tool to collect support arrears—and settle difficult cases.

A Qualified Domestic Relations Order (QDRO) authorizes the division of retirement assets between spouses from qualified retirement plans, incident to a divorce, without immediate income tax consequences. QDROs are typically used as a component of an equitable distribution plan to divide marital assets at the time of a comprehensive settlement or after trial of a matrimonial action. However, in appropriate cases, a QDRO can also be thought of as an effective enforcement remedy.

Our recent client, Mrs. Elizabeth Paxe (a fictitious name), was the beneficiary of our innovative use of a QDRO to bring her recalcitrant husband into line and to effectuate the ultimate settlement of her divorce on favorable terms.

Mr. Paxe paid himself a relatively modest annual salary of \$250,000, but supplemented his family's lifestyle by having his business pay for many living expenses, including household help, entertainment, travel, automobile, private plane and boat expenses.

Mr. Paxe's interest in the family business and the marital apartment were acquired before the marriage and were individually owned by Mr. Paxe. In addition, he owned several minority interests in real estate investments (in partnership with members of his family) and had pension assets valued at \$750,000 held in an IRA rollover account.

Although Mrs. Paxe did not individually own any property, it had appeared to her that her financial security and her husband's ability to support her could not be questioned. Yet, when her marriage began to disintegrate after eight years, her financial security was jeopardized.

When Mr. Paxe decided to end the marriage, he claimed that his business had suffered financial reversals and that he and his wife had to "cut back" on their expenses. Suddenly, he could no longer "afford" continued payment of support consistent with their marital lifestyle, because his "salary" had been reduced due to alleged business reversals. He unilaterally eliminated his wife's credit card privileges and instituted a household "austerity" budget. Meanwhile, he continued to travel first class to Europe and the Far East "on business", dined out nightly in fashionable restaurants and continued to play golf at the country club, "entertaining" business clients.

To all outward appearances, the Paxe family was extremely well-to-do. They lived in a \$2 million cooperative apartment on the upper east side of Manhattan, regularly traveled first class around the world, lavishly entertained, enjoyed their privately owned yacht and corporate jet, and rented summer homes in the Hamptons.

Mr. Paxe, along with his parents and siblings, owned a manufacturing business with annual gross revenues in excess of \$25 million.

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Mr. Paxe claimed that his interest in the business, the cooperative apartment and virtually all of his other assets were acquired before their marriage and were, thus, his "separate property," not subject to "equitable distribution" in the event of a divorce.

Mr. Paxe moved out of the apartment and drastically reduced the money available to Mrs. Paxe for support. She thereupon started a divorce action and asked the Court for temporary support and interim legal and appraisal fees. Mr. Paxe's claim of "instant poverty" was summarily rejected by the Court, which awarded Mrs. Paxe generous temporary support, consistent with their marital lifestyle, and substantial legal and appraisal fees.

Mrs. Paxe expected that her life would return to a semblance of normalcy. However, her husband had no intention of honoring his Court-ordered obligations or of making his wife's life comfortable or normal. He irregularly and haphazardly paid a fraction of the Court-ordered support and refused to pay any portion of the Court-ordered legal fees. In response to the income execution served on his business, Mr. Paxe reduced his "salary," thus rendering that enforcement remedy largely ineffectual.

Since he was in exclusive control of his and his wife's assets and income, Mr. Paxe knew that he had very substantial leverage. He intended to delay a final judicial resolution of the parties' divorce and prevent his wife from living her accustomed lifestyle while the case wended its way through the Court system. Mr. Paxe knew that the case could take years before a trial would commence and that his wife would be forced to incur tens of thousands of dollars in legal fees, thus reducing her ultimate recovery.

Despite the obvious gamesmanship being perpetrated, effective and timely enforcement remedies were limited. Contempt proceedings require that an evidentiary hearing be held, and such a hearing (a trial)

ordinarily could not be scheduled or conducted for six months or longer. Obtaining a money judgment would not assure payment of current Court-ordered support, since collection depended upon locating and liquidating "attachable" assets. Sequestration and receivership of the corporate stock in the business were not likely to be granted, since Mrs. Paxe lacked the requisite expertise to run the business.

Confronted with the foregoing, we sought to devise a strategy which would timely collect the sums past due and owing, secure the wife's current and ongoing support payments, and minimize the legal fees that would necessarily be (and intended by Mr. Paxe to be) incurred in protracted enforcement litigation. The purpose was to confront and defeat Mr. Paxe's strategy and, thus, accelerate the comprehensive settlement of the case.

Our strategy was implemented by moving for the entry of a Qualified Domestic Relations Order, which directed the transfer of \$276,000 to Mrs. Paxe from Mr. Paxe's IRA and charged said sum to Mr. Paxe's interest in the IRA. The QDRO sought to authorize the payment of all accrued but unpaid support and the unpaid legal and appraisal fees and to provide a fund for future support payments. However, since the funds in an IRA are pre-tax dollars, when such funds are disbursed, income taxes and pre-retirement penalties are due and payable.

This remedy, if granted by the Court, would have produced very adverse consequences to Mr. Paxe. For every dollar satisfied in this manner, over two dollars of IRA funds would be required. At the time the motion was made, Mr. Paxe owed \$60,000 of accrued support and \$50,000 of awarded legal and accounting fees. This \$110,000 obligation would require the expenditure of roughly \$276,000 in IRA funds to satisfy it.

The making of the motion and the potential significant charge to Mr. Paxe's substantial

For every judgment dollar satisfied from an IRA, over two and one-half dollars are required.

IRA brought Mr. Paxe and his attorney to the negotiating table. A favorable settlement quickly followed.

Matrimonial litigation is often a vexing and expensive undertaking. The successful representation of clients going through the

crisis of marital discord often requires the use of innovative and cost-effective strategies. Inquiries can be directed to Allan Mantel, head of the firm's matrimonial department. Kevin M. McDonough, Esq. assisted in the preparation of this article.

■ Tax Free Exchange Provisions Should Be in Your Real Estate Contract

Sellers of realty should always consider having a provision in the contract of sale giving them the right to exchange their real property for other realty on a tax free basis, as permitted under Section 1031 of the Internal Revenue Code. If, at the time of closing, the seller decides not to complete an exchange, the provision will have no effect and the seller will receive the full sale proceeds. If the seller decides to exchange, then the proceeds (or a portion designated by seller) will be directed to the exchange escrow agent to be used for the purchase of the replacement property.

If the seller does not designate a replacement property within 45 days after the closing in the manner required or if the seller revokes all designations made within that time period, the proceeds will be returned to the seller. If the seller has designated a replacement property, the monies cannot be removed from the escrow until (a) seller closes on the

replacement property, (b) 181 days from the date of the original sale, or (c) the occurrence of a condition that relates to the exchange and is beyond the Seller's control.

Depending on the closing date of the original sale, the seller may benefit from the exchange escrow even if there is no exchange. If the proceeds are not released from escrow in the year of the sale then the sale would not be reported until the following tax year and any tax on the sale would be deferred accordingly. If only part of the proceeds were put into escrow for an exchange and no exchange occurred, the seller would have an installment sale as to the portion released from escrow in the following tax year. This can be done, however, only if the seller has a *bona fide* intent to exchange.

The above is a brief summary and not intended to be a legal opinion. Please consult one of our partners for more information.

■ Estate and Gift Tax Reform in New York State

Effective February 1, 2000, the New York Estate Tax will equal the amount of the credit that the Federal government allows for death taxes payable to a State ("Federal State Death Tax Credit"). At present, the New York rate is much higher (up to 21% on large estates).

This effectively means that for New York persons dying after that date the estate's overall Federal and New York State estate tax burden should be the same as if New York

imposed no estate tax. This change will bring New York in line with "retirement" states such as Florida or Arizona or the other "soakup" states that also key the estate tax to match the Federal State Death Tax Credit.

The estate tax "phase-down" begins with a partial reduction in the tax for decedents dying on or after October 1, 1998.

Effective January 1, 2000, the New York Gift Tax is repealed.

New York has amended its Estate Tax to bring it in line with "retirement states."

■ Charitable Contributions of “Qualified Appreciated Stock”

Under the 1997 Federal Tax Act, taxpayers have until June 30, 1998 to donate “Qualified Appreciated Stock” (stock that is traded on an established securities market) to a private foundation to receive a charitable deduction for the full fair market value. This is a temporary exception to the general rule, which limits the deduction to the adjusted basis of the property. Under the old law, this

exception expired on May 31, 1997. Taxpayers with low basis publicly traded stock and charitable inclinations thus have additional time to establish a private foundation using Qualified Appreciated Stock or to make a contribution of such stock to an existing private foundation. Please call Bob Howard or Mary DeMarco Abrams or your attorney at the firm if you would like more information.

■ “Mail Box Rule” For IRS Filings Extended to Private Mail Carriers

The IRS has approved the following private delivery services under the “timely mailing as timely filing/paying” rule: Airborne Express (Overnight Air Express Service, Next Afternoon Service, and Second Day Service); DHL Worldwide Express (DHL Same Day Service and DHL USA Overnight); Federal Express (FedEx Priority Overnight, FedEx Standard Overnight, and FedEx 2 Day); and United Parcel Service (UPS Next Day Air, UPS Next Day Air Saver, UPS 2nd Day Air, and UPS 2nd Day Air A.M.). Formerly, only the United States Postal Service qualified. The list will be updated periodically. Consult us for more details.

■ Condo Boards May Now Borrow Money

Under a recently enacted law, Condominium Boards may now borrow money for repairs, maintenance, additions, improvements, working capital, bad debts or other similar purposes. Section 339-jj of the Real Property Law provides that a Condominium can grant a Lender a security interest in the common charges payable by Unit Owners to secure repayment. Borrowing requires approval by a majority of unit owners, and authorization by the Declaration or By-Laws. In order to determine whether a particular Condominium can borrow for a specific purpose, you should consult with your legal advisor at the firm.

■ Recent Representations

■ Hofheimer Gartlir & Gross, LLP successfully defended a publicly traded pharmaceutical company in an arbitration brought by a patent holder challenging our client’s drug development activities. Hofheimer Gartlir & Gross, LLP has substantial experience in intellectual property licensing disputes.

■ Hofheimer Gartlir & Gross, LLP represented the purchaser of the assets of McCrory Corporation. After obtaining Bankruptcy Court approval of the transaction in August, we closed the \$51 million deal and a related \$35 million revolving credit loan on Sept. 30, 1997. Hofheimer Gartlir & Gross, LLP will serve as general counsel to the new operating entity.

■ Hofheimer Gartlir & Gross, LLP represented the sellers of 810 Seventh Avenue, a 42 floor Manhattan office building, in a transaction that took under four months from bids to closing. Randy Kohana of RAK Group and Ernest Haas of Insignia/Edward S. Gordon Co. were the sellers’ brokers. HG&G partner Jerry Morganstern, assisted by Stephen Soleymani, handled the transaction on behalf of the selling entity, working with Herman Abbott, its Manager.

About Hofheimer Gartlir & Gross, LLP

The firm conducts a general commercial practice. Our principal practice areas are:

- real estate
- corporate and securities law
- general business and commercial law
- cooperative and condominium matters
- financial institutions (loan transactions, leasing, acquisitions, credit restructuring, workouts and foreclosures)
- estate planning
- trust and estate administration
- general litigation
- matrimonial and family law
- taxation

Clients of the firm range from major financial institutions and public corporations to closely-held businesses, individuals and families.

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