

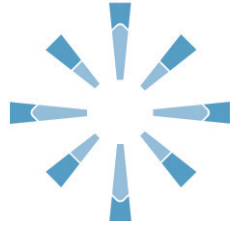
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Financial Issues In Family Law Cases



Presented By:
Cheryl F. Shuffield, CPA/ABV/CVA, CFF

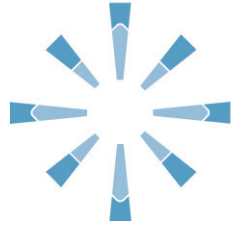


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The Family Lawyer's Lament – And a Practical Guide to Avoiding Malpractice Claims and Unhappy Clients





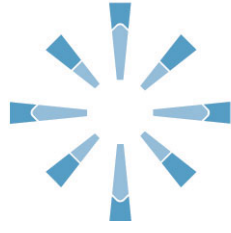
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**The Discovery is Answered,
The Depositions Complete,
Your Client's Ready to Split the
Sheets.**



**She'll take what he's offered,
No more questions asked.
She'll high five her friends,
And walk away with a grin.**



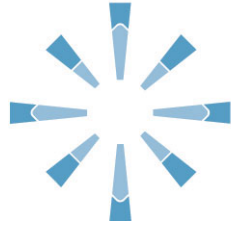
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**Before you agree, rest assured of this
fact.....**

**In just a few weeks, she'll definitely
look back.**

**She'll question your judgment, your
skills and acumen,**

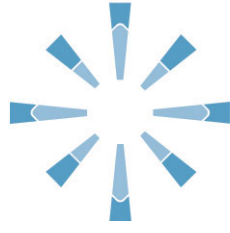


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**And complain loud and long
To all of her friends.**

**Will she call Tim Dudley and
consider a claim?**



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**And if she does,
WHO WILL YOU BLAME?**

Financial Due Diligence Checklist

Were all assets identified and divided?

Were marital assets appropriately valued?

Were all separate assets identified and secured?

Were opposing party's non-marital asset claims verified? Marital Contributions valued and offset?

Financial Due Diligence Checklist

Were liquidated and contingent liabilities identified and assigned?

Valued at a date consistent with asset valuation dates?

Release secured or arranged for if assigned to opposing party?

Financial Due Diligence Checklist

Was an equal division of the marital estate bargained for and received?

Were your client's risk factors identified, discussed, and documented?

Were your client's income needs reasonably quantified?

Financial Due Diligence Checklist

Were your client's needs for liquidity met?

Was the opposing party's income for support critically analyzed?

Were your client's short and long term cash flow needs discussed?

Does your client have a realistic game plan if they weren't met?

Financial Due Diligence Checklist

Has your client been advised to meet with a financial advisor to ensure her long term financial needs are attended to?

Has your client been advised to revise her will?

Financial Due Diligence Checklist

Was tax planning used to maximize cash flow in settling support issues?

Were tax consequences associated with property division fully explored?

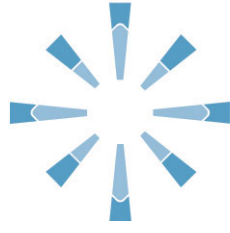
Was any deferred tax burden equally shared and/or fully explained?

Contingent tax liability discussed and allocated by agreement?

Financial Due Diligence Checklist

Are future obligations to pay support or effect the property division appropriately secured?

If not, did you carefully draft and require your client to read and acknowledge an “eyes wide open” letter enumerating any failures to fully explore the marital estate, evenly divide the marital estate, potential changes in support, and any other risk factors that may have kept you up the last few nights?



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SEARCH FOR ASSETS

Review several years income tax returns for interest, dividends, and pass through income to identify assets.

Compare assets identified with financial statements filed with lenders.

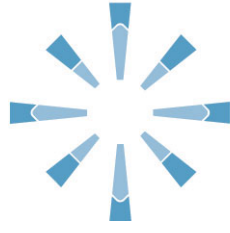
Track assets from period to period. If any assets drop, they should appear as sales on Sch D or Form 4797 of that year's tax return.

Compare values reported period by period.

Search real estate and personal property records on-line.

Review bank account records for franchise tax payments.

Search secretary of state's records for associated entities.



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SEARCH FOR ASSETS

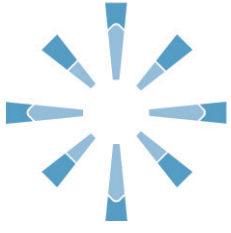
Review Employee Benefits Handbooks.

Review bank records for significant payments to insurance companies, investment banking firms, cashed checks, payments of estimated taxes, and any unusual payees.

Obtain credit card statements for all accounts identified by opposing party or through search of cancelled checks.

If formal discovery has not been completed by the settlement date, consider having each party sign disclosure statement under oath.

Review recent payroll records to determine whether excess withholdings were made.



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Some Commonly Overlooked Assets

Accrued Vacation Pay

Accrued Bonuses

Unused Balances in Flexible Benefits Plans

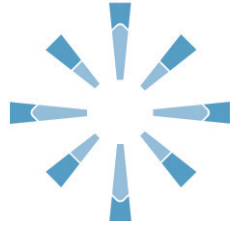
Health or Medical Savings Accounts

Unfunded Deferred Compensation Plans

Cash Value of Life Insurance

Savings Bonds

Work in Process



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More Commonly Overlooked Assets

Annuities

Tax Refunds

Overpaid Current Year Tax Estimates

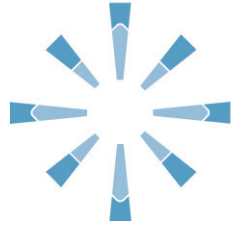
Credit Balances on Credit Cards or Open Accounts

Unused Tax Attributes (Loss and Credit Carry forwards)

Balances in 529 Plans (Susceptible to Change of Beneficiary)

Past Due Notes Receivable

Prepaid Merchant Cards



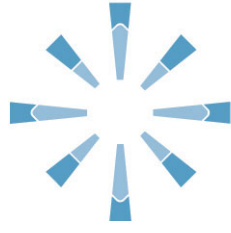
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And a few More - Not So Common

Stock Options

Phantom Stock Plans

Frozen Retirement Plans



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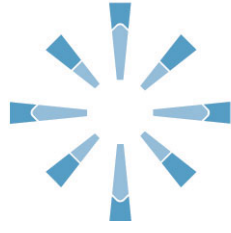
Marital Contributions to Increases in Value of Marital Property

**Payment of purchase money indebtedness during the
marriage.**

Physical improvements made during the marriage.

**Efforts of the non-owner spouse contributory to the increase
in value.**

**Efforts of the owner spouse contributory to the increase in
value and not adequately compensated.**



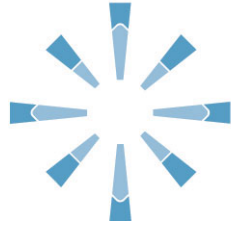
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Transmutation of Separate Property

A marital interest may be successfully asserted in separate property, particularly when the spouse owning the property is active in managing the property or business interest.

If your client is the owner of separate property which has appreciated during the marriage, you will need to consider factors other than personal efforts which contributed to the appreciation. Examples: inflation, overall increase in stock market valuations (P:E Ratios), location of an attractive asset near commercial real estate for reasons other than owner's efforts (i.e., "passive appreciation").



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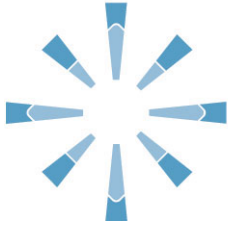
Some Valuation Risks

Reliance on unqualified appraiser

Reliance on a buy sell agreement

Use of a “stale” appraisal

**Failure to value marital interests in “mixed classification”
assets**



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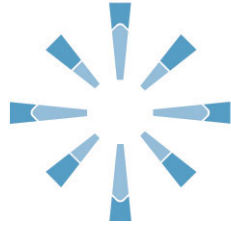
Some Valuation Risks

Failure to quantify increase in appreciation of mixed classification assets during the marriage through accepted valuation techniques.

Differing valuation dates for liquid assets and liabilities

Failure to apply fair market value standard

Failure to apply valuation discounts where appropriate



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Your Client's Risk Factors

Can future support obligations be secured?

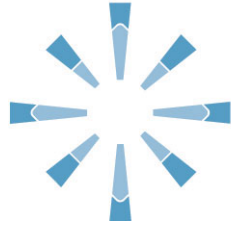
Can assets received be properly managed?

Will assets received cash flow?

And if not, how will shortfall be met?

Will closely held business interests be diluted if future capital calls are not met?

Beware of highly leveraged assets!

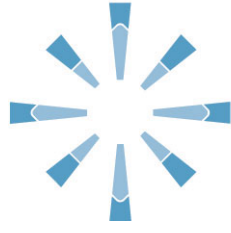


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Income Available for Support SELF EMPLOYED PAYORS

- Were two prior and the current year's earnings analyzed?**
- Were all benefits measured and included in income?**
- Were expenditures reviewed for personal expenses?**
- Were earnings that were not distributed from a C corporation added to reported income?**
- Were earnings distorted due to any change in accounting method?**
- Were earnings decreased through acceleration of expenses?**



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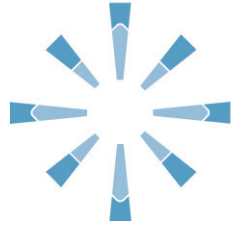
Income Available for Support **SELF EMPLOYED PAYORS**

Were earnings decreased through deferral of income?

Was depreciation taken in excess of economic decline?

Were personal assets depreciated?

Were hobby losses deducted?



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Income Available for Support MILITARY PAYORS – NONTAXABLE BENEFITS CONSIDERED?

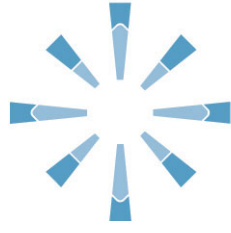
Basic allowance for housing

Basic Allowance for subsistence

Combat Zone Compensation

Disability Retirement Benefits

Any other veterans benefits administered by USDVA



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TAX CONSEQUENCES OF PROPERTY DIVISION

Identify “hot” assets.

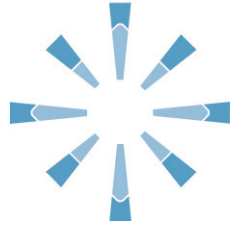
Quantify deferred taxes on assets in the estate.

Determine character of potential deferred income.

Consider tax attributes such as capital loss carry forwards – Match assets with capital appreciation to party with the attribute to offset.

Consider an unequal distribution of hot assets to shift income tax to lower bracket spouse.

If income shifting is not desirable, pursue equal distribution of hot assets.



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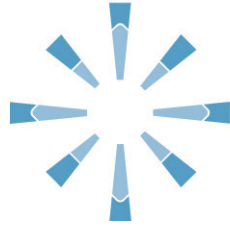
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CONSIDER TAX CONSEQUENCES IN CLAIMING DEPENDENTS

With two or more children in joint custody arrangements, it is possible for each parent to claim head of household status.

The higher income spouse may receive no income tax benefit from claiming a child if income exceeds \$200,000.

Lower earning spouse may be giving up both benefit of exemptions and refundable credits if exemption is shifted to higher income spouse.



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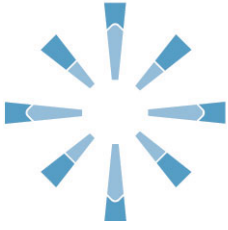
Tax Planning with Dependent Children

For example, Jane & John have two children between the ages of 14 and 16.

Their divorce will be finalized during the 2009 tax year.

John will report \$331,001 in gross income while Jane will report \$36,617.

As of December 31, 2009, both Jane and John remain unmarried.

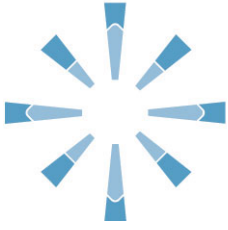


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	Jane Dependents	Jane No Dependents
Filing Status:	Head	Single
Personal Exemptions:	3	1
AGI	\$36,617	\$36,617
Standard Deduction	(8,350)	(5,700)
Personal Exemptions	<u>(10,950)</u>	<u>(3,650)</u>
Taxable Income	17,317	27,267
Regular Tax	2,000	3,673
Less: Child Credit	<u>(2,000)</u>	<u>0</u>
Total Federal Taxes	0	\$3,673
Tax Savings:	\$3,673	

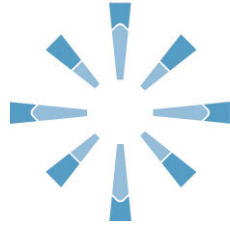


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	John Dependents	John No Dependents
Filing Status:	Head	Single
Personal Exemptions:	3	1
Adjusted Gross Income	\$331,001	\$331,001
Standard Deduction	(8,350)	(5,700)
Less: Exemptions	<u>(7,299)</u>	<u>(2,433)</u>
Taxable Income	315,352	322,868
Regular Tax	85,885	91,689
Alt Min Tax	3,295	0
Less: Child Credit	<u>0</u>	<u>0</u>
Total Federal Taxes	\$89,180	\$91,689
Tax Savings:	\$2,209	



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Planning to Maximize Post Divorce Cash Flow

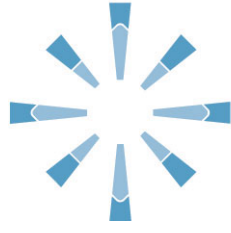
If the \$36,000 reported by Jane is alimony, John would pay \$12,000 less in Federal Taxes.

Jane's taxes would not increase assuming no other income.

The parties on a combined basis would generate additional cash flow of over \$15,000 annually by virtue of some simple tax planning moves.

Combined after tax cash flow continues to increase in this example as alimony increases, up to the point that taxable income is equalized.

Another tool to use to equalize income is to distribute "hot" ordinary income assets to wife, followed by a sale.



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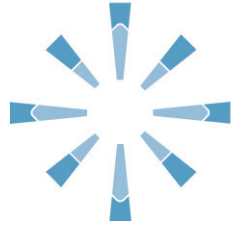
Securing a Long Term Payout

Use life insurance to secure support obligations. A trust is the ideal named beneficiary to ensure creditors cannot reach proceeds.

Another method to ensure future support is to include a requirement to retain the spouse as the named beneficiary on a retirement account until satisfaction of the support obligation.

To the extent possible, use unencumbered assets to secure property division payments.

If unencumbered assets are not available, select assets based on risk assessments. Consider degree of leverage, cash flow, potential for appreciation, and secured party's ability to manage the asset if received in liquidation of the obligation.



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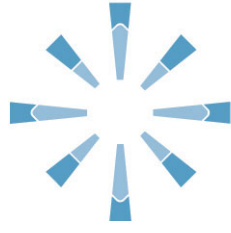
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Dividing Retirement Accounts

In settlement agreements, consider using “all retirement benefits” as opposed to naming specific plans when dividing equally, in the event a plan has been overlooked.

In Arkansas, vested military retirement benefits are subject to division in a divorce, but non vested benefits are not. Burns v Burns, 312 Ark. 61 (1993)

The Court cannot circumvent this rule by awarding alimony as a substitute for awarding non vested retirement pay. Holaway v Holaway, 70 Ark. App. 240 (2000)



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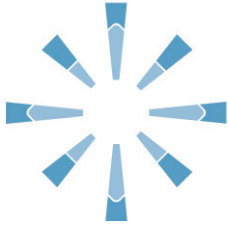
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Dividing Retirement Accounts

Defined benefit plans are most accurately divided based on division of future benefits.

Future benefits can be estimated and reduced to present value under the “immediate offset method”. This is a subjective process that requires estimation of future tax rates, life expectancies, and an appropriate interest rate to determine present values. Sufficient assets must be available for offset to equalize division.

In some defined benefit plans, it is possible to make a pre-retirement designation regarding survivor benefits. Such a designation required by the decree protects the non-employee spouse against loss of benefits in the event the employee spouse dies before retirement. Ask about this plan feature!



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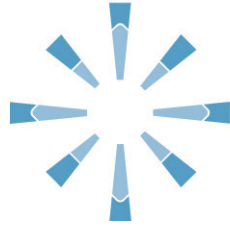
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Dividing Retirement Accounts

It is not uncommon to find that non-marital contributions were made to a retirement account. In such cases, a thorough search should be made for records which support an allocation between marital and non-marital interests in the plan assets.

Arkansas state courts cannot enforce the transfer of assignment of future payments of Social Security benefits pursuant to USC §407(a). *Gentry v Gentry*, 327 Ark.266 (1997)

But in making a determination of alimony, the court should consider the total income, from whatever source, including SS payments of both parties. *Cochran v Cochran*, 7 Ark App. 146 (1983)



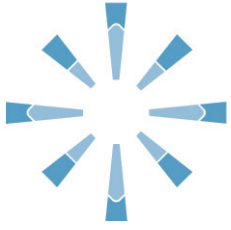
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Dividing Retirement Accounts

In some plans, you may find that the contributions are not made until the following plan year. Be certain that the plan administrator has accounted for any accrued contributions receivable.

**Qualified Domestic Relations Orders are required by all plans governed by ERISA. This excludes IRA accounts and military retirement pay. Examples of appropriate language and related law and requirements are set forth by the Garnishment Operations, Defense Finance and Accounting Service, Cleveland, OH 44199.
<http://www.dod.mil/dfas>**



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Thank you for sharing your time today.

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