Avoiding Malpractice in Family Law

Presenters:

Thomas Bittner, Schulte, Anderson, Downes, Aronson & Bittner
Laura Rackner, Gearing, Rackner & Engel LLP
Susan Watts, Kennedy, Watts, Arellano, & Ricks LLP

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Portland, Oregon

3.75 MCLE General or Practical Skills Credits
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| Title of CLE Activity: |  
| Avoiding Malpractice in Family Law - 2013 Update |

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  - ___ Access to Justice
  - ___ Child Abuse Rep.
  - ___ Practical Skills
  - ___ Pers. Management Assistance

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  - ___ General
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  - ___ Child Abuse Rep.
  - ___ Practical Skills
  - ___ Pers. Management Assistance

- ☐ Partial Credit. I attended _________ hours of the program and am entitled to the following credits*:
  - ___ General
  - ___ Prof Resp-Ethics
  - ___ Access to Justice
  - ___ Child Abuse Rep.
  - ___ Practical Skills
  - ___ Pers. Management Assistance

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**Credit Calculation:**
One (1) MCLE credit may be claimed for each sixty (60) minutes of actual participation. Do not include registration, introductions, business meetings and programs less than 30 minutes. MCLE credits may not be claimed for any activity that has not been accredited by the MCLE Administrator. If the program has not been accredited by the MCLE Administrator, you must submit a Group CLE Activity Accreditation application (See MCLE Form 2.)

**Caveat:**
If the actual program length is less than the credit hours approved, Bar members are responsible for making the appropriate adjustments in their compliance reports. Adjustments must also be made for late arrival, early departure or other periods of absence or non-participation.
# Avoiding Malpractice in Family Law

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Avoiding Malpractice in Family Law

Scenario

Ann and Andy want a divorce. They have two children, Reggie, a 19 year old college student, and Raejean, a 15 year old high school sophomore. They seek legal advice of their old friend Mr. Rogers.

Ann and Andy have been married for 18 years. Ann, whose parents died before her marriage to Andy, became independently wealthy several years before the marriage. As a result, Ann and Andy signed a prenuptial agreement.

Andy was in the military for fifteen years before he became owner and CEO of Portland Make-It-Right. Ann and Andy own a nice home in Portland, which is one of their primary assets. Andy has good life insurance benefits with Portland Make-It-Right.

Ann and Andy know Mr. Rogers from Andy’s work at Portland Make-It-Right. Mr. Rogers was in-house counsel for the company, until recently when he branched out on his own and opened his own law practice. Ann and Andy used Mr. Rogers last year as their “family attorney” to prepare their estate plan.

During a recent tennis game, Andy mentioned to Mr. Rogers that he and Ann were having problems and they were considering a divorce. Andy asked Mr. Rogers for information about the divorce process, and for a few basic tips.

A few days later, Ann called Mr. Rogers and made an appointment with him. This will be Mr. Rogers’ first divorce case. Ann brought her sister Sylvia to the meeting.

Ann and Sylvia were on-time for their appointment with Mr. Rogers. When they got there Mr. Rogers was not there, and his receptionist and secretary did not know where he was, or when he would be there. Ann and Sylvia decided to wait for Mr. Rogers. He finally arrived one hour later. He rushed through the interview with them. He never fully explained why he was late, and never apologized for keeping them waiting.

Mr. Rogers spoke with Ann and Sylvia at the same time.
QUESTIONS AND ISSUES

(**Note: All resources noted with two asterisks are either new or updated since the 2009 CLE presentation.)

1. Does Mr. Rogers have the experience to handle the case? What if Ann came to Mr. Rogers after having worked for several months with another domestic relations lawyer?

ISSUES FOR DISCUSSION:
- When and how to associate counsel
- Mentoring programs
- Case & client screening
- Do’s & Don’ts for using listserves
- Pitfalls of transferring files from one attorney to another

RESOURCES FOR QUESTION 1:
** Outline – “How to Develop a Successful Practice and Avoid Legal Malpractice,” by Barbara S. Fishleder.


- Oregon State Bar Lawyer to Lawyer Service. This offers an informal mentoring network for lawyers. Resource Lawyers with experience to share are listed according to areas of expertise and geographic location. The Resource Lawyer offers a free 10-15 minute consultation or a “take me to lunch” hour. For more information about being a mentee or a Resource Lawyer, call OSB Referral and Information Services at 503-620-0222, ext. 408.

- OSB Oregon New Lawyers Division New Lawyers Resource List. This is a list of more than 400 new lawyers that are willing to speak with other new lawyers (and law students) about changing practice areas or provide an informal mentoring experience. For more information go to http://www.osbar.org/onld/lawstudents.html.

** Mentoring Programs. The OSB has created a mandatory New Lawyer Mentoring Program for new lawyers. For more information go to www.osbar.org/programs/mentoring/index.html. The Multnomah Bar Association has a voluntary mentor program for new lawyers during their first six years of practice. Program registration is in the fall of each year. For more information call the MBA at 503-222-3275 and speak to Kathy Modie.

** The Oregon Judicial Department (OJD) web site has forms specifically designed for family law cases. Visit http://courts.oregon.gov/ojd/pages/index.aspx, click on Court Forms, then select Family Law Forms from the pull down menu.
** The Oregon Child Support Program of the Department of Justice has child support guidelines, a child support calculator, a parenting time calculator, and many more resources. Visit www.oregonchildsupport.gov and click on Child Support Professionals at the top of the page.

** OSB Family Law Section web site, www.osbfamilylaw.org, has statutes, rules, case law, and other valuable family law material.

** The Oregon State Bar CLE Family Law 2011, was presented April 29, 2011. To order, go to http://osbarcle.org/PDFs/catalog.pdf.

** Multnomah Bar Association offers Annual Family Law Update (March 20, 2013). To order, go to www.mbabar.org.


2. Assume that Mr. Rogers didn’t talk to Ann and Sylvia and only talked to Andy. Assume that Andy wants Mr. Rogers to represent him. Can Mr. Rogers represent Andy? Should he?

** ISSUES FOR DISCUSSION:
- When does the attorney-client relationship begin?
- Filing a co-petition – is it ever advisable?
- Pitfalls of representing friends
- When to check for a conflict of interest
- Entering declined clients’ names into your conflict system
- Resources available to help you improve your system – Professional Liability Fund Practice Management Advisors

** RESOURCES QUESTION 2:
- Professional Liability Fund Practice Management Advisor Article – “Tips, Traps and Resources, Conflicts of Interest,” In Brief, February 2009


- Practice Management Advisors of the Professional Liability Fund

3. Mr. Rogers spoke to Ann in the presence of Sylvia. Does this present any problems?
ISSUE FOR DISCUSSION:
• Waiver of attorney-client privilege

RESOURCES FOR QUESTION 3:
• ORS 40.225 – Evidence Rule 503: Lawyer-Client Privilege
  (www.leg.state.or.us/ors/040.html)

4. Assuming that Mr. Rogers spoke only with Andy (and did not prepare Andy & Ann’s estate plan), what kinds of things should he review in his initial interview?

5. Mr. Rogers does not like paper much. Mr. Rogers doesn’t use fee agreements or engagement letters. Is there a problem? Mr. Rogers doesn’t like to ask for money either. Can he take the case on a contingency fee?

ISSUES FOR DISCUSSION QUESTIONS 4 & 5:
• The intake interview process
• Preparing the client
• Confidential dissolution questionnaire
• Gathering information from client, documents needed from client
• Using fee agreements and engagement letters

RESOURCES FOR QUESTIONS 4 & 5
• PLF domestic relations practice aids. To download, go to www.osbplf.org. Find the loss prevention heading on the left side of the page, then click on Practice Aids and Forms. Then click on Domestic Relations.

  • PLF sample engagement, disengagement, nonengagement and retainer agreements can be found on the PLF web site: www.osbplf.org. Find the loss prevention heading on the left side of the page, then click on Practice Aids and Forms. The engagement and retainer forms can be found under the following categories: Disengagement Letters; Nonengagement Letters; and Engagement Letters.


** Article – “Fee Disputes and Binding Arbitration – Impact on PLF Coverage” by Roger Westendorf, In Brief, June 2009. (www.osbplf.org)

• OSB Formal Ethics Opinion 2005-13, Fee Agreements: Contingent Fees, Domestic Relations. (http://www.osbar.org/ethics/toc.html)
6. Assume that Mr. Rogers did not talk to Andy and he is just representing Ann (and did not previously work on Ann and Andy’s estate plan). Assume that Ann brings to Mr. Rogers’ office a marital settlement agreement that Andy and Ann “worked out” and Ann asks Mr. Rogers to be a “scrivener.”

7. Assume that Mr. Rogers did not talk to Ann or Sylvia and is just representing Andy (and did not previously work on Ann and Andy’s estate plan). Assume that child custody is an issue and Andy is very worried about money. He feels he has none and that Ann is trying to “get more than her fair share.” Andy makes it very clear that he does not want to pay for a private custody evaluation. In fact, Andy tells Mr. Rogers he is sick of fighting and wants to just let Ann have whatever she wants of the assets, custody, and visitation. What steps should Mr. Rogers take?

ISSUES FOR DISCUSSION FOR QUESTIONS 6 & 7:
- Where does a lawyer’s responsibility start and stop?
- Role of attorney when your client doesn’t want to try to get what he/she is entitled to
- If you are sending a letter that documents file or repeats what is said in a meeting with client, can you bill for it? Should you? How?
- Role of attorney when your client has unreasonable expectations
- Getting to settlement
- Limited fee agreements
- Importance of documenting files

RESOURCES FOR QUESTIONS 6 & 7:
- Sample letter to Client – Phyllis Foolhardy (client who is acting against advice of his or her attorney).


- Sample limited representation fee agreement, Form 10-1, Fee Agreement Compendium, 2007 rev., OSB BarBooks online library (www.osbar.org)
8. Assume that Ann and Andy have a prenuptial agreement. What relevance does this have in negotiating a settlement? What if Ann and Andy have a postnuptial agreement. What relevance does this have in negotiating a settlement?

ISSUES FOR DISCUSSION 8:
• Pre and post nuptial agreements

RESOURCES FOR QUESTION 8:
** Article – “Pre and Postnuptial Agreement Tips and Traps” by Joshua Kadish, In Brief, updated November 2012

9. Andy has substantial life insurance available through his employment. Assume that Andy will maintain the life insurance as part of the divorce settlement to secure his child support payments, naming Ann as a beneficiary of the life insurance policy. What steps should Mr. Rogers take? Assume Ann has retained her own attorney. What steps should Ann’s attorney take to protect Ann?

ISSUES FOR DISCUSSION 9:
• Life insurance procedure
• Protecting your client in the event support obligation is not met.
• Can you include something in the judgment that binds the insurance company or bank?

RESOURCES FOR QUESTION 9:
• Relevant statutes: ORS 107.106, 107.810, 107.820

** Avoiding Life Insurance Malpractice in Oregon Dissolution Cases

** Sample Life Insurance Language

** Amending Life Insurance Obligation

** Letter to Life Insurance Company

** Sample Letter from Insurer Acknowledging Notice

** Closing Letter to Client

** Sample Judgment Language – Beneficiaries

** Tupper v. Roan, 349 Or 211, 243 P3d 50 (2010);
• Seim v. Soriano, 94 Or App 67, 764 P2d 591 (1988);
10. Assume that Andy has a substantial military pension that is presently not vested but which will vest in two years based on his continued participation in the military reserves. Is this a marital asset? What other issues does a military pension raise? What needs to be done?

ISSUES FOR DISCUSSION:
• Traps in dividing a military pension

11. Assume that Andy has a substantial 401K Plan through Portland Make-It-Right Company, what questions should Mr. Rogers be asking? What needs to be done? What if Andy has retired and his pension is in payout status – is it property or income? What if Andy has a deferred compensation plan?

ISSUES FOR DISCUSSION:
• Investigating your client’s retirement accounts
• Dividing retirement accounts
  • How will account be divided – should it be specific dollar division or percentage allocation or other method?
  • What will happen to gains/losses.
  • What language should be in Judgment.
• Automatic beneficiary revocation statute (ORS 107.118 – 107.131)
• Filing a Supplemental Judgment (QDRO)
• Property v. income
• Deferred compensation plans

12. With respect to the pension, what happens if Andy’s attorney wants the value of his pension discounted for taxes?

ISSUES FOR DISCUSSION:
• Valuation of pension

RESOURCES FOR QUESTIONS 10, 11, 12:
• ORS 107.105(1)(f)(A)

**Article – “Preserving Survivor Benefits in the Military Pension Upon Divorce” by Clark Williams, November 2012**

**Survivor Benefit Plan Request for Deemed Election**

**Article – “Qualified Domestic Relations Orders: Issues to Consider,” by Daniel M. Ricks, In Brief, February 2009, updated November 2012**
13. Assume that Andy has vested stock options through Portland Make-It-Right which he obtained during the marriage, and unvested stock options which will vest in 5 years. Are these marital assets? What issues should the attorneys be concerned about?

**ISSUES FOR DISCUSSION:**
- Dividing and valuing vested and unvested stock options
- Are they a marital asset?
- When do they vest?
- Are they qualified or not qualified?
- Are there limitations for execution or their sale?
- Is a constructive trust ordered?

14. Assume that Make-It-Right is a new company and the company has several patents waiting for approval. Will these facts affect the property settlement?
# ISSUE FOR DISCUSSION:
- The importance of obtaining a business valuation
- Proving future earning capacity

**RESOURCES FOR QUESTIONS 14:**

**Business Valuation – What You Need to Know – What You Need to Ask (Which Valuation Variables Have the Greatest Impact on Value);** by William V. Mason II

**Business Valuation – Valuation Conceptual Structure,”** by William V. Mason II

**In re Marriage of Slater, 240 Or App 30, 245 P3d 676 (2010)**

15. Assume that Ann and Andy are going to sell their house as part of the dissolution proceedings and that Andy is planning on moving out of the house soon. What issues should be discussed?

**ISSUES FOR DISCUSSION:**
- Importance of the decision to move out or stay in the family home – from the custody & capital gains perspective
- Filing a lis pendens
- Factors a court may consider in requiring a sale
- Negotiating the percentage of capital gains tax
- Hidden expenses accompanying being awarded the family home
- Advantages of selling the family home
- How shall house be evaluated in a fluctuating market?
- How to handle the line of credit that is available against the house if credit market is tight and refinancing not available.

16. Assume that the tax basis for the family home is low because the home has appreciated significantly. What issues should be reviewed with the parties? Assume that the home will be sold at a loss. What issue should be reviewed with the parties?

**ISSUES FOR DISCUSSION:**
- Tax aspects of capital gains or loss on the sale of real property
- Forgiveness of debt: short sale; income
- Getting a real property appraisal

**RESOURCES FOR QUESTIONS 16:**
**Law Alert: Congress Extends Mortgage Forgiveness Debt Relief Through 2013**
17. Assume that Ann is going to get the house and the car. What steps are critical to preserve her rights?

**ISSUES FOR DISCUSSION:**
- Importance of following through and transferring deeds, titles, etc.
- Self executing language in Judgment

18. Assume that the parties purchased the family home with money loaned to them from Ann’s parents. Ann’s parents are on the title to the property. What rights can be raised by Ann’s parents? Assume that Ann’s parents gave her the property prior to the marriage and upon marrying, Ann transferred the property so that Ann and Andy owned it jointly.

**ISSUES FOR DISCUSSION:**
- Do you need to join a party in order to obtain the relief you want? Should you represent them, too? How should you protect yourself from claims of representing a third party.
- Property division post-Kunze
- Marital assets that are held jointly with third parties

**RESOURCES FOR QUESTIONS 15, 16, 17, & 18:**

**OSB Legal Publications, Family Law (2013 revision), Chapter 6.1 Assets,**

- ORS 107.405, ORCP 22, 28, 29
- *In re Marriage of Holemar,* 27 Or App 613, 557 P2d 38 (1976);
- *In re Marriage of McGoldrick,* 85 Or App 412, 736 P2d 622 (1987), *rev den,* 304 Or 55, 742 P2d 1186 (1987);

19. Assume that Ann is angry about the dissolution and that Andy is concerned that she will spend much of the assets before the dissolution is over, and that Andy may end up responsible for some of the debts. What issues should be reviewed?

**ISSUES FOR DISCUSSION:**
- How to protect your client from their soon to be ex-spouse’s bankruptcy
- Protecting your client from their spouse’s “wasting” of assets: restraining orders and other strategies.
RESOURCES FOR QUESTION 19:


20. Assume that there is little cash to split, and that Ann is going to get a money judgment against Andy. What issues does this raise?

**ISSUES FOR DISCUSSION:**
- Importance of timely filing a General Judgment of Dissolution of Marriage
- Timing & procedure for registering judgments in other counties
- Renewal of judgments

21. Assume Andy has an MBA which he earned during the marriage. Assume that Ann was employed during the early years of the marriage while Andy was obtaining an MBA. Can Ann successfully claim a right to spousal support from Andy?

**ISSUES FOR DISCUSSION:**
- Types of support: Transitional, maintenance, compensatory, temporary
- Importance of findings
- Nonmodifiable support orders
- Tax treatment of spousal support
- Spousal support “recapture” rule (front loading)
- Importance of the language of the money award

22. Assume that the parties settle and agree on an amount of spousal support and its duration, what language should be contained in the judgment? When must a support modification be filed?

**ISSUES FOR DISCUSSION:**
- Spousal support judgment language
- Filing spousal support modification before expiration of term for support
- Prepaying of support

23. Andy is concerned about his future earnings and wonders – do support obligations ever terminate completely?

**ISSUES FOR DISCUSSION:**
- Impact of support termination; reinstatement of support
RESOURCES FOR QUESTIONS 21, 22 & 23:

**In re Marriage of Matar, 353 Or 446 (2013)

** In re Marriage of Cassezza, 243 Or App 400, 260 P3d 504 (2011)

• In re Marriage of Cheever and Halperin, 213 Or App 441, 162, P3d 287 (2007),

• In re Marriage of Goertel, 209 Or App 585, 149 P3d 247 (2006)

• In re Marriage of McInnis, 199 Or App 223, 110 P3rd 639 (2005), rev dismissed, 338 Or 681, 115 P3d 246 (2005)

• In re Marriage of Bates, 303 Or 40, 733 P2d 1363 (1987),

• ORS 107.136

• 26 USC §71

24. Assume that Ann and Andy’s case will involve spousal support, child support and property division. What are the various tax implications for each of these awards? Assume that a temporary spousal support amount has been agreed upon by the parties. What should the attorneys do?

25. Assume the divorce will settle in December and that Andy wants to file a joint tax return. How would this affect each party?

26. Assume Ann wants the tax dependency exemption and so does Andy. What factors should be considered in awarding this exemption?

ISSUES FOR DISCUSSION FOR QUESTIONS 24, 25 & 26:
• Limited Judgments versus Temporary Orders
• Tax implications of spousal support, child support and property division
• Temporary spousal support & tax implications
• Joint tax return liability and “Innocent Spouse Relief”
• Capital gains or losses and carryover issues
• Tax aspects of dependency exemptions
• How to properly divide tax exemptions to prevent “wasting” exemptions

RESOURCES FOR QUESTIONS 24, 25 & 26:
**Note: The child support guidelines and child support calculator were revised July 2013. (www.oregonchildsupport.gov.)**


- IRS exemption form


27. Assume that Andy got his own attorney and that you represent Ann. Assume that Ann and Andy are getting tired of attorney fee bills and want to talk directly to each other to work out some of the issues. What is permitted?

**ISSUES FOR DISCUSSION:**
- When is it permissible for clients to speak to each other?

**RESOURCES FOR QUESTION 27:**

28. Assume Ann has disappeared and Mr. Rogers is representing Andy. Mr. Rogers would like to seek an order of default against Ann. What steps should Mr. Rogers take? What if Ann is in the military?

**ISSUES FOR DISCUSSION:**
- How to obtain an order of default

**RESOURCES FOR QUESTION 28:**
- Article – “YES. You DO Need to Know About SCRA (Servicemembers Civil Relief Act)” by V. H. Rogers, *In Brief*, February 2009

**Article – “The Servicemembers Civil Relief Act Is Still Relevant,”** Mark Ronning, July 2013

- Professional Liability Fund CLE, The One for All: What Every Practitioner Must Know About SCRA. To request a CD of this program, go to www.osbpflf.org. On the left side, find the Loss Prevention section, then click on “programs on audio.” Then click on Servicemembers Civil Relief Act. This CLE program is free.

29. The case is over and Mr. Rogers is glad. He wants to just shove the file in the drawer and move on. What should he do?
ISSUES FOR DISCUSSION:
• File closing procedures
• Settlement of property and attorney fees/liens
• Settlement checks – how should the checks be made out?
• How long do the parties have to assert their claims against each other?

RESOURCES FOR QUESTION 29:
• File Closing Checklist (www.osbplf.org) (Practice Aids and Forms – File Management)
• File Retention and Destruction: Guidelines (www.osbplf.org) (Practice Aids and Forms – File Management)
• Article – “Accessing Retirement Benefits After Divorce,” by Paul DeBast
• ORS 87.445 – 87.490 Attorney fee liens

30. Assume that the facts are as they were originally stated in the fact scenario: Mr. Rogers was the family attorney for Ann and Andy. Andy asked Mr. Rogers for a few “tips” during a tennis match and Ann later retained Mr. Rogers to represent her. Assume that a property settlement agreement was worked out and the dissolution was final. Assume that 6 months down the road, Ann has second thoughts about the deal, calls up Mr. Rogers, and complains that he didn’t adequately represent her. What should Mr. Rogers do?

ISSUES FOR DISCUSSION:
• When to call the PLF. What is the difference between calling the PLF and calling the OSB?
• What happens when you call?

RESOURCES FOR QUESTION 30:
• Coping With Legal Malpractice Claims

• Article – “On Being Sued or How It Feels When the Nightmare Happens to You,” In Brief, updated September 2008

• Excerpts from Chapter 15, Oregon Ethical Lawyer, § 48-50 Dealing with Potential or Actual Malpractice Claims

31. Assume that upon completion of this case, Mr. Rogers realizes that he is in need of a vacation. He is so tired that he accidentally leaves his laptop – which has confidential client information on it – on a seat at the airport. When he returns to where he was sitting, the laptop is gone. After inquiring with airport security, he concludes that the laptop has been stolen. What should he do?

ISSUES FOR DISCUSSION:
• What should an attorney do when an electronic device is stolen.
32. Mr. Rogers has become overwhelmed with work and is not making much money. He knows that he needs to do a better job of client screening, but has a hard time doing it. He feels distracted, exhausted and generally unhappy. What can he do?

**ISSUES FOR DISCUSSION:**
- Domestic relations work and burnout
- Resources available to you for free: Oregon Attorney Assistance Program

**RESOURCES FOR QUESTION 32:**
- Article – “Beating the Stressors of Family and Juvenile Law” by Mike Long, OSB Family and Juvenile Law Newsletter, Updated September 2008
- Oregon Attorney Assistance Program brochure; www.oaap.org

33. Mr. Rogers is thinking about accepting credit cards as a form of payment from clients. What should he know about accepting credit cards in his law practice?

**ISSUES FOR DISCUSSION:**
- Accepting credit cards in your law practice

**RESOURCES FOR QUESTION 33:**

34. Assume that Mr. Rogers did not talk to Ann or Andy (and did not previously work on their estate plan). Andy asks Mr. Rogers to “mediate” their divorce. What steps should Mr. Rogers take?

**ISSUES FOR DISCUSSION:**
- Attorney acting as mediator

**RESOURCES FOR QUESTION 34:**
- Frequently Asked Questions About Alternative Dispute Resolution and PLF Coverage (www.osbplf.org) (Policies and Forms Under Primary Coverage)
- PLF exemption guidelines – Alternative Dispute Resolution including Mediator and Arbitrator (www.osbplf.org) (Policies and Forms Under Primary Coverage)
• OSB Formal Ethics Opinion No. 2005-101 Unauthorized Practice of Law: Lawyer as Mediator, Trade Names, Division of Fees with Nonlawyer (http://www.osbar.org/ethics/toc.html)
I. Techniques for Avoiding Malpractice.

Your exposure to legal malpractice can be greatly reduced by making a habit of (1) good client communications; (2) careful case selection; (3) careful client selection; (4) extensive file documentation; (5) understanding and avoiding conflicts of interest; (6) clarifying your fee arrangements and; (7) using a double calendaring system.

A. Client Communications Are Crucial.

Establishing and maintaining a good working relationship with your clients is one of your best protections against a malpractice claim. Our statistics show that 55 percent of malpractice cases are closed without payment to the client. This reflects a large number of clients who have filed a legal malpractice claim even though their lawyer has not made a mistake. For the most part, the filing of these claims by clients is a way for the client to vent frustration with the way he or she has been treated by the lawyer. The following are some suggestions that will help minimize your exposure to legal malpractice claims:

1. Keep Your Client Informed.

Almost everything you do should be transmitted to your client, even if you just send copies marked "for your information." If there is little activity on the case, send a brief status letter to your client. This will let your clients know that you have not forgotten about them and will eliminate unnecessary phone calls to you at your office.

2. Provide Your Clients with a Realistic Assessment of Their Case.

Let your client know your best guess of how long the case process will take and approximately how much it will cost. Let the client know the weaknesses and the strengths of the case. Explain your assessment of the case in terms the client can understand: for example, a 70 percent chance of success also means that 3 times out of 10 the client will lose.

3. Keep a Professional Attitude.

Remember that your client is paying for your services and you are providing a service. You should treat your client with the same respect that you demand and
expect from other service providers. Try to remember how you feel about being uninformed, being put on hold, or being forced to wait. Always:

a. Return phone calls promptly.
b. Be on time for appointments.
c. Avoid taking telephone calls during office conferences.
d. Give your client your full attention - do not interrupt your client’s telephone call by speaking to people in the room.
e. Copy your client with your work product.
f. Show an interest in the client as a person.
g. Bill on a periodic, preferably monthly, basis.

4. Make Certain That Your Client Makes the Decisions in the Case.

It is your job to provide your clients with information. It is the clients’ responsibility to make the decision. DO NOT BE PRESSURED INTO MAKING THE CLIENTS’ DECISIONS FOR THEM. Be sure that you are clear and thorough in outlining the pros and cons of differing options; then let your client decide how to proceed.

5. Never Proceed Without Your Client’s Permission.

Obtain express permission for all of the following:

a. Granting extensions to the adverse party.
b. Stipulating to evidence or testimony.
c. Case settlements.
d. Suggesting settlement figures to the other side.
e. Rejecting a settlement offer.
f. Agreeing to a continuance.
g. Concluding testimony in a litigation matter.

B. Reject Certain Clients and Cases.

Careful client and case screening can eliminate the threat of a legal malpractice suit and greatly reduce the stress in your life. Evaluate potential clients and cases with these factors in mind:

1. The client’s relationship to, and experience with, prior attorneys. Beware of the client who constantly changes attorneys. Look out for the case that has already been rejected by one or more attorneys.

2. The client’s attitude and relationship with other professionals such as doctors, accountants, bankers, and lenders.

3. What is the client’s attitude towards the case? Does he or she wish to proceed
in the case because of the principle and regardless of cost? If you take this case, you may find yourself pressed to pursue a case you do not believe in, or worse, end up with sanctions imposed against you.

4. Has the client contacted multiple government representatives to plead his or her case? Beware of this client.

5. Has the client come to you with a “done deal,” researched the case extensively on his or her own, or caused the matter to be an emergency due to his or her own delay? Does the client always communicate with you in writing?

6. Do you have adequate skill, expertise, and time to pursue this client’s case?

7. Are you handling this case simply because the potential client is a friend, related to a friend, or knows a friend? These cases should be avoided unless you have confidence in your ability to handle the case and have a good feeling and attitude about the potential client. Would you take this case if this client walked in off the street?

8. Are you and the client able to easily agree on a fee and retainer? If not, you may be dealing with a client who is best off represented by someone else.

9. What is your “gut reaction” to this client? If your first impression of the client (or his or her course of action) is unfavorable, think very carefully (i.e., reject the case). Lawyers who are sued for malpractice almost always knew at the outset that they should have rejected the case.

C. Use Letters to Document Information and Clarify Your Relationship.

Your scope of representation (or lack thereof) and your fee arrangements should be thoroughly spelled out in an agreement given to your client at the beginning of your relationship. If you are declining representation, that should also be documented. Sample engagement and nonengagement letters can be downloaded from the PLF Web site at www.osbplf.org.


If you decline representation of a client, you should document your decision not to represent the client. In some instances, you should give serious consideration to sending the letter by certified mail, return receipt requested. If you reject the case and the client later sues you for failing to represent him or her, how will you prove that you advised the client that you would not be taking his or her case? A nonengagement letter is strong proof on your behalf.

Consider these additional guidelines for your letters:
a. Generally explain to the client why you cannot accept the case.

b. Avoid commenting on the merits of the case.

c. If time limits apply to the case, advise the client that time limitations do apply and that it is imperative that the person consult another attorney immediately.

2. Engagement Letters.

If you choose to represent a client, be sure to give the client an engagement letter. The engagement letter should contain the fee arrangements and a clarification of what you are engaged to do. It should contain the following:

a. A description of the work to be performed.

b. An estimated range of fees.

c. Identification of specific costs that will be charged.

d. The hourly rates of individuals assigned to the case.

e. An explanation of how much the client is expected to pay and when.

f. An explanation of billing practices, including charges for travel time, telephone conferences, faxes, photocopies, or other items.

g. If you are holding trust funds, an explanation that you will transfer money from the trust account when you send the bill.

The description of the work to be performed should clarify the scope of your representation. Are you representing the client only on his or her personal injury claim and not on his or her workers’ compensation claim? Are you representing the client only on his or her workers’ compensation claim and not on his or her discrimination claim? The client (and a court) should be able to decipher this information from your engagement letter.

The engagement letter can be used as a fee agreement. If this approach is taken, the client should sign the letter. Another approach is to have the client sign a fee agreement in the initial interview and send a follow-up engagement letter to the client afterwards.


If you wish to terminate the attorney-client relationship, be sure to comply with all of the rules of professional conduct, including ORPC 1.16. Document the termination. Consider sending the letter certified mail, return receipt requested. Follow these guidelines:

a. Advise the client of the general reason for termination of the attorney-client relationship.

b. Avoid commenting on the merits of the case.

c. Advise generally of time limitations and the need to obtain another
attorney.

d. Return client’s papers and a copy of the file. **YOU SHOULD RETAIN THE ORIGINAL FILE OR, AT A MINIMUM, A COPY OF THE FILE.**


Your file should reflect the case history, status, and strategy. Imagine that you suddenly and unexpectedly could no longer practice law. Do your files clearly show what you agreed to do and what advice you gave?

Documenting the file is a way of communicating with your client as well as a way of protecting yourself. Make sure that your client understands what is transpiring and is kept fully informed. Consider these guidelines:

a. Keep your files well organized. This will help you and your staff. It will also greatly reduce your stress.

b. Never proceed without your client’s permission. (See Section I.A. on client communications.)

c. All important advice to the client should be confirmed in writing.

d. Document your advice to the client, especially if the client is proceeding contrary to your advice.

e. Keep notes of telephone conversations and conferences. Make the notes at the time of the conversation or immediately after.

f. Keep all settlement offers and demands on a separate sheet in your files. Document the client’s authority and the communications with the adverse party.

g. Analyze the capacity of your client and determine the best way to document your advice. Should you have the settlement agreement reported by a court reporter to verify your client’s consent? Should your letter be sent certified mail, return receipt requested?

D. **Understand the Conflicts-of-Interest Rules.**

Thoroughly apprise yourself of the applicable rules of professional conduct, including ORPC 1.7, 1.8, and 1.9 pertaining to conflicts of interest. Note that representation of former or current clients is allowed only in specific situations and that the client must give informed consent in writing. ORPC 1.0 defines “informed consent” and “confirmed in writing.”
The following steps should be taken to avoid conflicts of interest:

1. Establish a fail-safe conflict system within the office. If a new client is considered for representation, a memo should be sent around the office identifying the client, parties involved, and nature of transaction. This memo should request that all office staff and attorneys advise you of pertinent information and problems. This measure should be taken in addition to the conflict-of-interest system established in your office. If you need help establishing a conflict-of-interest system, or if you want your current system reviewed, call the Professional Liability Fund’s Practice Management Advisors, Dee Crocker, Beverly Michaelis, or Sheila Blackford. All consultations are free and confidential. Call Dee, Beverly, or Sheila at 503-639-6911 or 1-800-452-1639.

2. Avoid suing prior clients even when allowed under the rules of professional responsibility.

3. Take only one side in a dispute.

4. Receive your compensation in a transaction from only one side.

5. Avoid being both a director and the attorney for the corporation at the same time.

6. Avoid dual representation. For example, do not represent a buyer and seller, landlord and tenant, or trustor and beneficiary at the same time.

7. If dealing with an unrepresented party, send the party a letter documenting whom you represent. Inform the unrepresented person that he or she should obtain independent counsel.

8. Do not act as an escrow agent in any transaction in which you represent a party. OSB Ethics Op Attorney as Escrow Agent No 2005-55.

9. If you are representing multiple plaintiffs or defendants, research the applicable ethics rules. The Ethical Oregon Lawyer § 9 has an excellent discussion on current client conflicts.

E. Clarify Your Fee Arrangements; Use a Fee Dispute Checklist.

Many legal malpractice suits result from counterclaims in response to an attorney’s action to recover fees. The risk of being counter-sued for malpractice is greatly reduced if you take the time to explain your fees to the client at the beginning of your attorney-client relationship, document your agreement, and provide your client with frequent (monthly) fee bills. Your fee bills should be specific and identify the specific
services rendered for the fee charged. Listen carefully to your client’s need for services before you provide a quote of fees. Additionally, consider these guidelines:

1. As a general rule, avoid suing clients for fees. Offer to arbitrate the fee dispute through the Oregon State Bar Fee Arbitration Program or consider other alternative dispute resolution methods.

2. Enter into a written fee agreement early in the course of representation. This can be separate from your engagement agreement, or made a part of it (see section I.B.2.). Be sure that your billing practices include:
   
   a. Providing the client with a written engagement and fee agreement.
   b. Billings that are itemized so that the client can tell what is being done on his or her behalf.
   c. Billing periodically, preferably monthly.
   d. Keeping an accurate time log reflecting daily efforts expended on behalf of the client.
   e. Keeping your compensation arrangement the same throughout the case - do not change your method of compensation in the middle of the case.

The Oregon State Bar Legal Management Section has published a collection of fee agreements in the Oregon State Bar handbook *Fee Agreement Compendium*. This handbook is available through the order desk of the Oregon State Bar 503-684-7413 or 1-800-452-8260 ext. 413.

3. If you decide to sue a client for fees, use the following checklist:
   
   a. Does your law firm stand to gain or lose a substantial amount of money?
   b. Was a good result obtained in the underlying case?
   c. Has an uninvolved experienced attorney reviewed the file for possible malpractice?
   d. Have you offered to arbitrate the claim?
   e. Will a judgment be collectable if obtained?

F. Use a Double Calendar System.

Failure to properly calendar is one of the leading causes of malpractice throughout the United States. This type of malpractice can be avoided by following these suggestions:

1. Every Case Must Be Calendared.

Each and every case in your office should be on your calendar. Calendaring should include litigation time lines, preparation reminders, due dates and follow-
up dates. Smith and Mallen, in their treatise *Preventing Legal Malpractice*, suggest a three-category system for calendaring:

a. dates that must not be missed (such as time limitations);

b. dates that should not be missed (such as follow-up dates); and

c. informational dates.

Take the time to enter the data correctly (e.g.) the statute of limitations is two years from the date of the accident not two years from the client’s office visit).

2. Use a Dual Calendaring System.

You and your secretary should both calendar dates, keeping a matched calendar.

3. Review All Files Every 30 Days.

G. Avoid Personal and Financial Involvement with Clients.

Attorneys should avoid business transactions with clients. If you enter into a business transaction with your client, be sure to comply with ORPC 1.8 and with the Professional Liability Fund Coverage Plan (Exclusion h) which requires that you keep a copy of the written disclosures and consents required by the rule.

The following guidelines should also be considered:

1. Do not give clients investment advice.

2. If you are going to accept stock in lieu of fees, make sure that your fee is reasonable and review PLF coverage plan exclusions f and h.

3. Do not personally guarantee a client’s obligations or have the client personally guarantee yours.

4. Avoid advancing costs whenever possible.

5. Do not date or have an intimate relationship with a client during the course of your representation.

II. Resources Available to You.

A. Educational Material and Information.


5. The Professional Liability Fund *In Brief*, published quarterly.

6. CDs and DVDs on substantive areas of the law, practice management, and personal assistance available through the Professional Liability Fund and other law-related organizations such as the Oregon Attorney Assistance Program, Oregon State Bar, Multnomah Bar Association, Oregon Law Institute, and American Bar Association.

7. The *Fee Agreement Compendium*, published by the Oregon State Bar Law Practice Management Section. To order, call the Oregon State Bar at 503-684-7413 or 1-800-452-8260 ext. 413.

**B. People Available to Assist You.**

1. The Professional Liability Fund claims attorneys - call the PLF claims attorneys at 503-639-6911 or 1-800-452-1639 if you have made a mistake or are concerned that you may be exposed to a legal malpractice claim.

2. The Professional Liability Fund practice management advisors - for assistance with office systems, including docket control, tickler systems, conflict-of-interest systems, mail handling, billing, trust accounting, general accounting, time management, file management, client communications, and computer systems. Call the PLF’s Practice Management Advisors, Dee Crocker, Beverly Michaelis, and Sheila Blackford, at 503-639-6911 or 800-452-1639.

3. The Oregon Attorney Assistance Program - for personal assistance for yourself or for those you care about. OAAP offers support, resource referral, and crisis counseling. Programs include assistance with alcoholism, drug addiction, burnout, career satisfaction, depression, anxiety, gambling addiction, procrastination, relationship issues, stress management, retirement, and time management. Call the OAAP Attorney Counselors, Meloney C. Crawford, Mike Long, Shari R. Gregory, and Douglas Querin, at 503-226-1057 or 1-800-321-6227.

4. The Oregon State Bar General Counsel - call 503-620-0222 (or outside Portland 1-800-452-8260) ext. 359 or 361, for assistance with ethics questions.
III. Suggestions for Avoiding Malpractice.

A. Carefully select your clients and cases. Do not accept cases for which you do not have adequate time, experience, or capital to complete.

B. Get your money up front or establish an alternative means for avoiding fee disputes.

C. Know your own limits. Assess your knowledge, time, and energy. If you are a new attorney, take advantage of the Lawyer to Lawyer services of the Oregon State Bar. Access your local mentor program. Review legal and practical case problems with an experienced attorney.

D. If you share space with another lawyer and do not want to be considered a “firm,” make your independent status clear to your clients so as to avoid liability on the theory of a “de facto” partnership. Call Barbara Fishleder at the PLF if you have questions about sharing office space at 503-684-7425 or 1-800-452-1639.

E. When drafting legal documents, use a comprehensive up-to-date checklist as a starting point for developing your document. Carefully read documents to make sure that the document is appropriate for your client’s specific needs. Beware of boiler-plate computer-generated forms!

F. If you receive a malpractice claim or complaint, call the Professional Liability Fund immediately. Do not represent yourself. Speak with a Professional Liability Fund claims attorney and discuss whether or not the mistake can be corrected. Let the claims attorney guide you on how to tell your client about the possible error, and whether or not you should continue to represent the client.

G. If you or someone you know needs personal assistance or is impaired in his or her ability to practice law, get professional help at once. Call the confidential Oregon Attorney Assistance Program (OAAP) at 503-226-1057 or 1-800-321-6227 and ask for Meloney C. Crawford, Mike Long, Shari R. Gregory, or Douglas Querin.

H. Reach out for help.

1. Call the Professional Liability Fund for assistance and advice on how to handle your potential claim.

2. Call the Professional Liability Fund for free help with your office systems.

3. Take advantage of the Oregon Attorney Assistance Program for assistance with alcoholism, drug addiction, burnout, career satisfaction, depression, anxiety, gambling addiction, procrastination, relationship
issues, stress management, retirement, and time management. Call the OAAP Attorney Counselors, Meloney C. Crawford, Mike Long, Shari R. Gregory, or Douglas Querin 503-226-1057 or 1-800-321-6227.

I. Don’t reinvent the wheel.

The Oregon State Bar and the Professional Liability Fund have numerous excellent sample forms and practice aids. For information about practice aids available from the PLF, call the PLF or visit www.osbplf.org and download the materials.

Caution: The information contained in these materials is general loss prevention advice and is not legal advice. We encourage readers to conduct appropriate research to determine what actions should be taken given their specific circumstances and to call the Professional Liability Fund for assistance.
Conflicts of Interest – Tips, Traps, and Resources:

In Brief, February 2009

Conflicts of Interest: When an individual or entity (Prospective Client) consults with you about possibly forming a client-lawyer relationship, you MUST enter the individual and/or entity’s name into your conflict of interest system, even if you decline to represent the person or entity. You and your firm are then prohibited, under certain circumstances, from representing any other person or entity (Desired Client) with materially adverse interests to the Prospective Client you declined (PCYD). These circumstances are: (1) if the representation is the same or a substantially related matter and (2) if the information divulged by PCYD could be significantly harmful to PCYD in the proposed representation of Desired Client. The exceptions to this rule are: (1) if both Declined Client and PCYD give written informed consent, or (2) if you are screened from participation in the matter and PCYD is promptly notified in writing. To avoid this embarrassing and often costly mistake, be certain to check your conflict system before consultation with a Prospective Client. (See ORPC 1.18 on Duties to Prospective Client.)

Note: If lawyers want to take advantage of the screening option in RCP 1.18, they must be sure to take “reasonable measures to avoid exposure to more disqualifying information than was reasonably necessary to determine whether to represent the prospective client.” See RPC 1.18(d) (2).
Administrative errors, such as missed dates and deadlines, account for the majority of legal malpractice claims. Improving your office systems can substantially reduce your risk of potential claims and enhance the enjoyment of practicing law.

Free and confidential assistance with office systems is available through the Professional Liability Fund’s Practice Management Advisor (PMA) Program. Practice management assistance is available to all Oregon lawyers for a wide range of needs, including:

SETTING UP A LAW PRACTICE
- Deciding the form of entity
- Choosing a location for your office
- Buying a law practice
- Furnishing your office
- Budgeting
- Hiring staff
- Sharing office space
- Referring work and splitting fees

OFFICE SYSTEMS
- Creating and using a conflict system
- Implementing and using a calendaring system
- Setting up periodic file reviews
- Keeping files organized and up-to-date
- Establishing systems for opening and closing files
- Establishing procedures for file retention and destruction
- Minimizing filing time
- Processing mail to minimize lost documents and missed deadlines
- Transitioning to a paperless office

TECHNOLOGY
- Purchasing hardware
- Finding software for docketing, case management, conflict systems, tickler systems, time and billing, general ledger, and trust accounting
- Using pleading templates for Word and WordPerfect

OFFICE MANAGEMENT
- Handling mail and email efficiently
- Creating a procedures manual
- Documenting personnel and office policies and procedures
- Using form books
- Using checklists and other practice aids to simplify workflow
- Establishing blocks of time for uninterrupted work
- Learning to delegate appropriately
- Managing time to reduce stress and improve working conditions

FINANCIAL MANAGEMENT
- Keeping accurate time records
- Preparing and sending billing statements
- Billing to meet clients’ needs
- Developing alternatives to hourly billing (and determining when to use them)
- Tracking client funds
- Understanding trust accounting and general accounting
- Understanding IOLTA and lawyer trust account procedures
- Reconciling accounts
- Disbursing trust funds
Malpractice Prevention

- Disbursing settlement proceeds
- Avoiding overdrafts
- Handling unclaimed property
- Record keeping
- Managing accounts payable and receivable
- Handling collections
- Budgeting
- Managing office overhead

CLIENT RELATIONS

- Selecting cases and clients that are a good match for you
- Using intake and new client information checklists
- Clarifying information about case costs
- Reviewing fee agreements with clients
- Establishing client service policies
- Documenting case information
- Transmitting information to clients
- Creating and meeting realistic client expectations
- Marketing
- Building a solid client base

CLOSING A LAW PRACTICE

- Selecting a “buddy” or “assisting attorney” to help close your practice in an emergency
- Returning files to clients
- Transferring files to other lawyers
- Storing closed files

RESOURCES

- Sample letters and forms
- Practice aids for a wide variety of areas of law
- Audio/video materials
- For these and other resources, visit www.osbplf.org

PRACTICE MANAGEMENT

We are available to assist any law office in Oregon. Reduce your risk of malpractice claims and enhance the enjoyment of practicing law.

Contact the Professional Liability Fund’s Practice Management Advisors:

Dee Crocker – deec@osbplf.org
Beverly Michaelis – beverlym@osbplf.org
Sheila M. Blackford – sheilab@osbplf.org

503-639-6911 or 800-452-1639
Facsimile 503-684-7250
www.osbplf.org

There is no charge for this confidential service.

Practice Management & Malpractice Prevention Assistance

Practice Management Advisors of the Professional Liability Fund

Oregon State Bar
Professional Liability Fund
P. O. Box 1600
Lake Oswego, Oregon 97035
March 3, 2009

Phyllis Foolhardy
12345 SW Anystreet
Anytown, Anystate 99999

Re: Foolhardy and Foolhardy

Dear Phyllis:

Now that this case is coming to a close, I want to confirm my involvement and counsel.

You have negotiated with your husband a settlement of this case without benefit of my counsel. The settlement was without the benefit of any discovery being undertaken by this office to determine the nature and extent of assets and liabilities of the parties or the nature and extent of your husband’s income. As I have previously indicated to you, it is normal due diligence on the part of an attorney to proceed with appropriate discovery. This can include serving requests for production of documents, and subpoenaing and deposing witnesses. Notwithstanding this advice, you instructed me not to so proceed. As a result, I am not able to advise you on the merits of the settlement and have counseled you against proceeding.

You and I have had some discussions regarding the nature and extent of the division of the assets. I understand that, based upon information provided by your husband or within your knowledge, it is your understanding that an equal division of the martial estate has been achieved. Again, I have had no input in determining the accuracy of the numbers or whether or not the assets and liabilities have been fully disclosed. As a result, I am unable to advise you as to the merits of the settlement.

The settlement does not provide for spousal support. In lieu of that, you are awarded $50,000 out of your husband’s half of the net marital estate. You and I have had conversations with respect to this issue, and I have counseled you that the failure to have an award of spousal support in the judgment fully bars you from any claim for spousal support in the future. I have further counseled against your settling this case without the benefit of an award of spousal support.
You have asked me to review the settlement documents prepared by your husband’s attorney. I have done so and have provided my comments under separate cover. The extent of my representation in this case, other than as set forth above, has been with respect to the form of the judgment and not its substance.

Very truly yours,

ZIMMER & BUNCH LLC

Gary J. Zimmer
Pre- and Postnuptial Agreement
Tips and Traps

(Originally published in the June 2006 issue of In Brief, updated November 2012)

Many couples wish to define their marital rights and responsibilities by entering into pre-nuptial or postnuptial agreements. The impetus for such an agreement is frequently a reaction to a bad dissolution of a prior marriage or a result of parental pressure. Some people simply wish to carefully define their financial relationship. Whatever the couple’s motivation, approach these agreements with caution.

In Oregon, prenuptial agreements are authorized by ORS 108.700 to 108.740. Postnuptial agreements are not authorized by statute, and their status is considerably less certain than that of prenuptial agreements. Because of the high incidence of divorce, it is quite possible that a prenuptial agreement you draft will be “put to the test.”

Prenuptial Agreements

Understand the Law. Prenuptial agreements can be very comprehensive in scope. Typically, they address both what happens in the event of a divorce and what happens in the event of death. They can also examine any day-to-day financial arrangements the parties may wish to include. The competent drafter must have a good grasp of both estate planning and domestic relations law. If you are inexperienced in one of these areas, consult with another lawyer who can provide the needed expertise.

Represent Only One Party. Represent only one party to a prenuptial agreement, and insist that the other party have independent counsel. Even if the parties say that they agree about every term of the agreement, their interests are adverse, and it is not permissible for one attorney to represent both parties. Independent representation for each party will increase the likelihood that the agreement will be upheld and will provide an often-helpful second set of eyes during the drafting process. It is good practice, although not required, to have both attorneys sign a certificate stating that they have fully explained the agreement to their clients and that they believe that the clients understand the terms and how their rights are being altered. There is no required format for such a certificate. You can find an example in the OSB CLE Family Law.

Volume II (Dissolution Practice), Chapter 15: Prenuptial, Postnuptial and Marital Settlement Agreements.

Time Carefully. Although a prenuptial agreement in Oregon could be signed just before the organ starts to play the wedding march, this timing makes the parties vulnerable to the contention that the agreement was signed under duress. It is better to have both parties execute the agreement a reasonable period of time before the ceremony. Although Oregon law does not define a “reasonable period of time,” California law requires that prenuptials be signed at least a week before the wedding ceremony.

Family Fairness Act. The Oregon Family Fairness Act (Act) allows for registration of civil unions between same sex couples. The Act provides that persons registered under the Act are entitled to all the benefits of marriage, which presumably includes the right to enter into a premarital agreement. Until the Act is interpreted by case law, it is not completely clear that premarital agreements are available to same sex couples under the Act, but I believe it is reasonably likely.

Disclaimer

In Brief includes claim prevention information that helps you to minimize the likelihood of being sued for legal malpractice. The material presented does not establish, report, or create the standard of care for attorneys. The articles do not represent a complete analysis of the topics presented, and readers should conduct their own appropriate research.
**Draft Carefully.** During the drafting process, advise clients that they are opting out of the complex bundle of marital rights that has developed over centuries and are trying to create a customized bundle that applies only to their situation. Take the time to describe exactly what will happen to complex assets, such as retirement plans, stock options, intellectual property, and business assets.

**CONSIDER HOW THE AGREEMENT MIGHT BE ATTACKED**

A good approach to drafting prenuptial agreements is to consider the four ways in which they might be attacked. First, was the agreement executed involuntarily? Second, is the agreement unconscionable? Third, was the agreement properly drafted? Finally, might the parties have revoked the agreement by their subsequent conduct? I address each of these in turn.

ORS 108.725 sets forth the two statutory grounds under which a prenuptial agreement is not enforceable. The first ground is that a party did not execute the agreement voluntarily. Since last writing this article, the Oregon Court of Appeals has issued Rudder and Rudder, 230 Or App 437, 217 P3d 183 (2010). This case is important because it is the first which invalidates a prenuptial agreement since the inception of the Oregon Prenuptial Agreement Act (UPAA) in 1987. In other words, for over twenty years no appellate court had set aside a prenuptial agreement, which probably led many practitioners, myself included, to be somewhat overconfident about the enforceability of these agreements. The facts of the case were extremely sympathetic to the wife due to a long-term marriage and a last-minute signing of the prenuptial agreement during which the wife had no access to separate counsel. Although the trial court set aside the prenuptial agreement on the grounds of unconscionability, the court of appeals ultimately based its opinion on voluntariness. The opinion is useful because it contains an extensive discussion of the standard, which is subject to a broad range of interpretation.

The second statutory ground, unconscionability, has not yet been treated in Oregon case law. However, Oregon courts have long held that persons engaged to be married have a fiduciary relationship and must act in good faith. The UPAA provides that an agreement can be set aside if it is unconscionable when executed when before execution one party 1) was not provided fair and reasonable disclosure of the other party’s property or financial obligations, 2) did not waive the right to disclosure, and 3) could not have had adequate knowledge of the other party’s property or financial obligations. Obviously, if there is full disclosure of property prior the parties’ signing the agreement, this standard will be difficult to meet. Although full disclosure of each party’s property is not required by statute, such disclosure eliminates any attack based on unconscionability, leaving only lack of voluntary execution as a ground for setting aside the agreement. If parties choose the full disclosure approach, lawyers customarily attach exhibits to the agreement showing each party’s separate property and any property they may hold jointly or intend to make joint following the marriage.

Third, as stated above, prenuptial agreements are complex documents that are difficult to write. A common drafting flaw is failing to adequately describe all of the types of property that a couple has acquired, so that one cannot tell whether a particular asset is marital or not. For a current form of prenuptial agreement that solves this problem, see OSB CLE Family Law, Volume II (Dissolution Practice), Chapter 15, Prenuptial, Postnuptial and Marital Settlement Agreements.

Finally, clients should be made aware that it is possible to revoke a prenuptial agreement by subsequent conduct. In the matter of Marriage of Loomis, 247 Or App 127, 268 P3d 700 (2011) contains a good review of the case law on this topic. Clients should be advised to keep careful records, review the agreement from time to time, live within its terms, and call the lawyers if they have doubts about how any particular financial transaction might affect the agreement. Even the best drafted prenuptial agreement will not be helpful if the parties have kept poor records or acted inconsistently with the document by, for instance, placing assets in joint name without intending to make the assets joint for purposes of the agreement.

Follow-up steps. It is good practice to write clients a closing letter advising them on the above topics. In particular, clients should be told that prenuptial agreements can be modified or terminated, but only in writing. Tearing them up and throwing them in the fireplace or otherwise destroying them will not alter the agreement.

**POSTNUPTIAL AGREEMENTS**

Although many of the comments above about prenuptial agreements also apply to postnuptial agreements, the following additional considerations come into play.

**Include Consideration.** A prenuptial agreement requires no consideration to be enforceable, including any modification or revocation of the agreement. Postnuptial agreements are governed by contract law, which requires consideration to enter into and modify an agreement. The mutual alteration of marital rights may provide adequate consideration, but it is safer to require additional monetary consideration, no matter how minimal.

**Clarify Application.** Postnuptial agreements do not enjoy the statutory authority of prenuptial agreements. Although carefully drafted and reasonable postnuptial agree-
ments may be enforceable, they are considerably less certain than prenuptial agreements. The recent case of In re Marriage of Grossman, 338 Or 99, 106 P3d 618 (2005), had a chilling effect on postnuptial agreements, although the facts of that case are unusual and may not have broad application. In Grossman, the parties executed a postnuptial agreement while contemplating a divorce. After executing the agreement, the parties reconciled and continued to live together for some years. They later divorced, and the validity of the agreement came into question. The Oregon Supreme Court ruled that the agreement was no longer effective, possibly because it would have resulted in an extremely uneven division of property and it was not clear whether the parties intended the agreement to apply to anything other than the divorce impending at the time they executed the agreement.

To avoid the result in Grossman, practitioners should distinguish marital settlement agreements from postnuptial agreements. The former are generally executed in contemplation of a divorce; the latter are not. A postnuptial agreement should clearly provide that it applies to any future divorce, if that is what the parties intend. If it is not their intention, the parties should enter into a marital settlement agreement, which should provide that it applies only to their impending divorce.

Advise Clients About Lack of Certainty. If the parties want to be certain of enforceability, they may need to get divorced, sign a prenuptial agreement, and then remarry. Obviously, this extreme solution will not appeal to most clients. However, to protect yourself, advise clients in writing that a postnuptial agreement may not hold up.

Joshua Kadish

Wyse Kadish LLP

Thanks to William J Howe III, Gevirtz Menashe Larson & Howe, PC, for his assistance with the original version of this article.
107.106 Provisions of order or judgment providing for custody, parenting time, visitation or support of child. (1) An order or judgment providing for the custody, parenting time, visitation or support of a child under ORS chapter 25, 107, 108, 109 or 110 or ORS 419B.400 or 419C.590 shall include:

(a) Provisions addressing the issues of:
   (A) Payment of uninsured medical expenses of the child;
   (B) Maintenance of insurance or other security for support; and
   (C) Medical support for the child under ORS 25.321 to 25.343.

(b) A statement in substantially the following form:

The terms of child support and parenting time (visitation) are designed for the child’s benefit and not the parents’ benefit. You must pay support even if you are not receiving visitation. You must comply with visitation orders even if you are not receiving child support.

Violation of child support orders and visitation orders is punishable by fine, imprisonment or other penalties.

Publicly funded help is available to establish, enforce and modify child support orders. Paternity establishment services are also available. Contact your local district attorney or the Department of Justice at (503) 373-7300 for information.

Publicly funded help may be available to establish, enforce and modify visitation orders. Forms are available to enforce visitation orders. Contact the domestic relations court clerk or civil court clerk for information.

(2) The court or administrative law judge shall ensure the creation and filing of an order or judgment that complies with this section.

(3) This section does not apply to an action undertaken by the Division of Child Support of the Department of Justice or a district attorney under ORS 25.080. [1995 c.800 §9; 1997 c.249 §36; 1997 c.707 §8; 2003 c.73 §49a; 2003 c.75 §83; 2003 c.637 §17; 2009 c.351 §8]

LIFE INSURANCE ON OBLIGOR

107.810 Policy. It is the policy of the State of Oregon to encourage persons obligated to support other persons as the result of a dissolution or annulment of marriage or as the result of a legal separation to obtain or to cooperate in the obtaining of life insurance adequate to provide for the continued support of those persons in the event of the obligor’s death. [1981 c.775 §9]

107.820 Support order as insurable interest; order to obtain, renew or continue insurance; right of beneficiary to purchase insurance or pay premiums. A court order for the payment of spousal or child support whether issued prior to, on or following November 1, 1981, constitutes an insurable interest in the party awarded the right to receive the support. In any case of marital annulment, dissolution or separation, the issue of life insurance shall be determined as follows:
(1) When the judgment creates an obligation of spousal or child support or awards a share of a pension or retirement plan, the judgment may also require that the obligated party maintain any existing insurance policies on the life of the obligated spouse and in which the dependent spouse is named as beneficiary. The judgment may require that the policies be maintained until the obligation is fulfilled. The premiums may be paid by the obligated spouse, and the court may consider the cost of premiums when determining the obligation. Any life insurance policies on the life of the obligated spouse owned by parties outside of the marriage or purchased and held for purposes clearly outside the marriage relationship are exempt from this subsection.

(2) If the party ordered to pay support or a share of a pension or retirement plan has no life insurance policy naming as beneficiary the party ordered to receive either support or a share of a pension or retirement plan, or if an existing policy is inadequate to cover the obligation, the court in a judgment may order that the party ordered to pay shall purchase a life insurance policy naming as beneficiary the party ordered to receive the support or a share of a pension or retirement plan and that the obligated party shall pay premiums on the policy and keep the policy in force until the obligation ends. The obligated spouse has the option of obtaining a nonreducing term life insurance policy or any other type of policy in lieu of using existing policies.

(3) Additionally, the party awarded the right to receive support or a share of a pension or retirement plan may purchase a life insurance policy on the life of the obligated party. In such case the court shall order the obligated party to undergo a physical examination. All rights of policy ownership, including those regarding the extent of coverage, shall be in the party purchasing the policy under this subsection who shall also be responsible for paying the premiums. The provisions of this subsection may be exercised at the time of annulment, dissolution or separation, or at any later time while the obligation continues.

(4) Upon motion of either party, the court shall order a party to renew a life insurance policy allowed to lapse for any reason during the pendency of the suit.

(5) A party who is the beneficiary of any policy under this section upon which the other party is obligated to pay premiums, is entitled, in the event of default by the paying party, to pay the premiums on the policy and to obtain a supplemental judgment for reimbursement of any money so expended. A default in the payment of premiums by the party obligated by the judgment or order is a contempt of the court.

(6) Life insurance retained or purchased by an obligor under subsection (1) or (2) of this section for the purpose of protecting the support, pension or retirement plan obligation shall not be reduced by loans or any other means of reduction until the obligation has been fulfilled. The obligee or the attorney of the obligee shall cause a certified copy of the judgment to be delivered to the life insurance company or companies. If the obligee or the attorney of the obligee delivers a true copy of the judgment to the life insurance company or companies, identifying the policies involved and requesting such notification under this section, the company or companies shall notify the obligee, as beneficiary of the insurance policy, whenever the policyholder takes any action that will change the beneficiary or reduce the benefits of the policy. Either party may request notification by the insurer when premium payments have not been made. If the obligor is ordered to provide for and maintain life insurance, the obligor shall provide to the obligee a true copy of the policy. The obligor shall also provide to the obligee written notice of any action that will reduce the benefits or change the designation of the beneficiaries under the policy. [1981 c.775 §11; 1983 c.728 §5; 1987 c.885 §4; 1993 c.716 §5; 2003 c.576 §131]
Avoiding Life Insurance Malpractice in Oregon Dissolution Cases©

By Paul J. DeBast
DeBast, McFarland & Richardson LLP
9600 SW Barnes Rd., Suite 325
Portland, OR 97225
Phone (503) 297-9600
debast@dmr-law.com

I. Life Insurance as Security for Child and Spousal Support. Oregon law encourages courts to protect child and spousal support against the risk that the payor spouse could die.

A. Public Policy.

1. ORS 107.106. Judgments shall include provisions addressing maintenance of insurance or other security for support [see table 1 for text of statutes].

2. ORS 107.810(1)(a)(B). Divorcing parties are encouraged to cooperate in obtaining life insurance adequate to provide for continued support.

B. Automatic Restraining Order. ORS 107.093 creates an automatic restraining order restraining both parties from:

1. “. . . canceling, modifying, terminating or allowing to lapse for nonpayment of premiums any . . . life insurance policy that names either of the parties or a minor child of the parties as a beneficiary; and

2. “. . . changing beneficiaries or covered parties under any . . . life insurance policy.”

Practice Pointer: Check on the existence and status of life insurance early on in the divorce process. If a policy has lapsed or coverage or beneficiaries have changed, try to correct the problem immediately. Example - what happens if husband allows his $1 million life policy to lapse after the divorce case is commenced and then he dies unexpectedly? Does the attorney have some responsibility?

C. Insurance Alternatives Available to the Court. ORS 107.820 provides that when a judgment creates an obligation of spousal or child support, the court may:

1. Order the obligated spouse to maintain existing insurance policies on the life of the obligated spouse and in which the dependent spouse is named as beneficiary. [ORS 107.820(1)]
2. If the obligated spouse has no life insurance naming the supported spouse as beneficiary, the court may order the obligated party to purchase a policy naming the obligee as beneficiary. (The statute grants the obligor the option of obtaining a nonreducing term policy “or any other type of policy in lieu of using existing policies”). [ORS 107.820(2)]

3. Permit the obligee to purchase a life insurance policy on the life of the obligor. In such case the obligee is responsible for the payment and the court “shall order the obligated party to undergo a physical examination”. [ORS 107.820(3)]

Practice Pointer: Consider adding the following language to confirm a wife’s right to purchase a policy on her ex-husband’s life:

“Wife has an insurable interest in husband’s life and is authorized by ORS 107.810 et seq to purchase insurance on husband’s life should she decide to do so. This includes the right to require that husband submit himself to a physical examination as required by ORS 107.830. Husband shall fully and promptly cooperate with any request made by wife in her effort to purchase insurance on husband’s life.”

*Note: ORS 107.830 provides: “If life insurance is obtained by a former spouse, the person obtaining the policy is responsible for all premiums to be paid.”

4. Order the obligated spouse to renew a policy which was allowed to lapse for any reason during the pendency of the suit.

5. In addition to the statutory alternatives mentioned above, attorneys should consider assigning ownership of an existing policy to the obligee spouse. The obligee then becomes the owner of the policy and is legally entitled to name the death beneficiary and control the flow of policy information thus being assured the death benefit will be paid as expected if the obligor should die. If the policy is expensive, it may be possible to make the insurance premium part of an award of spousal support.

D. Obligee’s Right to Pay Missed Payments. ORS 107.820(5) grants the obligee the right to make payments in the event the obligor defaults on his life insurance payment obligation and to recover the payments via contempt.

E. Obligee’s Duties Where Obligor Retains Ownership of the Policy. If the obligor retains ownership of the insurance, ORS 107.108(6) establishes a procedure whereby the obligee can be assured that the required insurance is actually in place and remains unchanged. The steps are summarized below:
1. The dissolution judgment must describe the insurance obligation including:
   a. The beneficiary;
   b. The dollar amount of insurance required to be maintained;
   c. The name of the insurance company issuing the policy; and
   d. The policy number.

2. The obligee or attorney for obligee must then:
   a. Cause a certified copy of the dissolution judgment to be delivered to the
      life insurance company; and
   b. Request that the life insurance company notify the obligee whenever the
      policyholder takes any action that will change the beneficiary or reduce
      the benefits of the policy or when premium payments have not been
      made.

II. Avoiding the Malpractice Trap Where the Obligor is Required to Obtain or Maintain an
    Insurance Policy.

   A. Typical Dissolution Language Doesn’t Work. Typical life insurance language found
      in many Oregon divorce judgments does not comply with ORS 107.108(6). Typical
      language reads as follows:

      “So long as husband has an obligation to pay child support, he shall
      maintain a life insurance policy insuring his life for at least $150,000
      naming wife as primary beneficiary”.

      The problem is the language does not identify any particular life insurance company or
      policy number, so how can the obligation be enforced?

   B. A Malpractice Case Defines the Standard of Care. Seim v Soriano, 94 Or App 67,
      764 P2d 591 (1988) was an attorney malpractice case arising after the death of an
      obligor who died without leaving the required life insurance in place. Text of the case
      is found at Table 2. The case essentially defined the procedure a divorce lawyer must
      follow in order to protect the obligee against the possibility the obligor will die without
      the insurance being in place:

      “The problem in this case started with the preparation of the dissolution
      judgment by defendant. It requires William to ‘maintain his present life
      insurance policy at the present limits for the minor children.’ We know
      from the record that there never was a policy naming the children as
      beneficiaries; there were at least five policies, some of which, at least,
      had named plaintiff Hively as beneficiary. Before the dissolution,
      William had changed the beneficiaries on those policies to be his
      parents, the Seims. We have no doubt that, if the judgment had described
      the policy or policies, giving the name of the insurer and the policy number
      or numbers and that, if a certified copy of the judgment had been
delivered to the insurer, plaintiffs would have been protected. Plaintiffs, however, do not allege that defendant was negligent in either of those respects. Had they done so, that negligence would have been the direct cause of plaintiffs’ damage. In this action, plaintiffs accept the dissolution judgment as adequate and allege that defendant was negligent in failing to notify the insurer of the terms of the judgment, in failing to instruct plaintiffs to do so and in failing to determine the existence of insurance referred to in the judgment. On this record, even if defendant had done those things, plaintiffs would not have been protected * * * because the judgment does not specifically identify the insurer or the policy number, if the company had received notice of the terms of the judgment, it would not have paid out, or even held up, the proceeds for the benefit of the children.”  Seim, supra at page 71 [emphasis added].

C. Constructive Trusts Often Don’t Work. Most judgments include language which provides that, in the event the payor spouse fails to maintain the required life insurance, a constructive trust will be imposed over the payor’s estate and the life insurance proceeds to secure payment of the insurance obligation. This sounds good but, in practice, it has been difficult for aggrieved plaintiffs to prove facts sufficient to successfully impose the remedy. Tupper v. Roan, 349 Or. 211 (2010) is an example of the problem.

In Tupper, the deceased father had signed a stipulated judgment requiring him to maintain $100,000 of life insurance naming his ex-wife as beneficiary so long as he had an obligation to pay child support. The policy was not in existence at the time the judgment was entered. Subsequently, father began living with another woman (“Danette”). Thereafter, father purchased a life insurance policy with a death benefit of $600,000, naming Danette as sole beneficiary. Father died three months later and Danette received the funds. The ex-wife sued Danette to impose a constructive trust over $100,000 of the policy proceeds. In defense, Danette pointed out that she knew nothing about father’s life insurance obligation. She claimed the insurance was purchased at her urging because she and father had started a business which only generated enough income to pay father. According to her, the policy was purchased as security for money she advanced and to cover her loss of compensation during the relationship.

Before trial the parties filed cross motions for summary judgment. The trial court awarded summary judgment in favor of the ex-wife ruling that $100,000 of the insurance proceeds was subject to a constructive trust. Danette appealed and the Court of Appeals reversed, holding that the trial court should have awarded summary judgment to Danette. Tupper v. Roan, 227 Or App 391, 206 P.3d 237 (2009). The ex-wife appealed to the Supreme Court and that court remanded the case back to the trial court for a trial. The Supreme Court explained that a constructive trust is an equitable remedy, created to divest someone who has been unjustly enriched of property he or she
should not be entitled to retain. The Court identified the following elements a plaintiff must prove in order to prevail on an unjust enrichment claim:

“First, the plaintiff must show that property or a property interest that rightfully belongs to her was taken or obtained by someone else under circumstances that in some sense were wrongful or inequitable. Next, the plaintiff must show that the person who now possesses the property is not a bona fide purchaser for value and without notice. Finally, the plaintiff must establish, with ‘strong, clear and convincing evidence,’ that the property in the hands of that person, i.e., the property upon which she seeks to impose a constructive trust, in fact is the very property that rightfully belongs to her, or is a product of or substitute for that property.” *Tupper v. Roan*, 349 Or. 211 at 223.

The only reported Oregon case where a constructive trust was successfully imposed in this context is *Sinsel v. Sinsel*, 47 Or App 153, 614 P2d 115 (1980). There the deceased father had changed the beneficiary of his only insurance policy in favor of his second wife after he had been ordered to maintain that same policy for the benefit of his children by his first wife. The court found that the second wife was aware of the decree's requirements and of her husband’s acts, but that she was not involved in any “wrongful participation” in those acts. The Court concluded that the second wife had “actual or constructive notice” of her husband’s acts and of their “wrongful nature,” and that a constructive trust could properly be enforced upon her insurance proceeds under those circumstances.

D. **Forms You Can Use to Avoid a Malpractice Claim.**

1. Table 3. Language for the Judgment of Dissolution [page 6-11].
2. Table 4. Example of Supplemental Judgment [page 6-12].
3. Table 5. Letter to Life Insurance Company [page 6-13].
4. Table 6. Example of reply from an insurance company [page 6-14].
5. Table 7. Closing letter example [page 6-15].

III. **Insurance to Secure Support - Other Issues.**

A. **Both Parents May be Required to Provide Insurance for the Benefit of a Child.** *Willey and Willey*, 155 Or App 352, 963 P2d 141 (1998) holds that both parents can be required to maintain life insurance for the benefit of a child. In *Willey*, the mother was awarded custody subject to 50% parenting time for father. She appealed from the trial court’s order that she purchase life insurance for the benefit of the child. She argued
only “the parent ordered to pay child support should be required to provide life insurance.” The Court rejected her argument saying:

“ORS 107.106 requires a judgment providing for custody to include ‘[m]aintenance of insurance or other security for support[,]’ Although wife does not have a net child support obligation, she does have a support obligation under the shared custody child support obligation. We conclude that the court did not err in requiring the insurance here.”<br>Willey at page 357.

B. **Who Should be Named as Beneficiary Where Children are Involved?** In the context of child support, the question of who to name as beneficiary frequently generates conflict. A number of options are available:

1. **Naming the Payee Spouse.** ORS 107.820 states that it is the payee spouse, not the children, who has the insurable interest to be protected:

   “A court order for the payment of spousal or child support constitutes an insurable interest in the party awarded the right to receive the support.”

   Many judges construe this language strictly. When disputes arise over whether wife or the children should be named as the beneficiary, judges frequently hold that it is the wife who is entitled to the support and it is she who should be named as the beneficiary.

2. **Others May be Named as Beneficiary.** Our Court of Appeals has held that courts have discretion in determining who should be beneficiary. For example, in *Stuart and Stuart*, 107 Or App 549, 813 P2d 49 (1991), the wife was awarded child and spousal support. She claimed the trial court erred in allowing husband to name his brother as the beneficiary of his life insurance policy in trust for the children. The Court of Appeals held that courts have discretion in determining who should be beneficiary but that in this case wife should be the beneficiary because the purpose of the policy was to secure the payment of husband's child support obligation.

3. **Children as Beneficiaries.** Despite the language of ORS 108.820, many divorces are settled on a basis whereby the parties agree that the children will be named as the beneficiaries of the life insurance. Such an agreement is enforceable under ORS 107.104 (2) which provides that a dissolution court may enforce the terms of a settlement agreement or stipulated judgment “as contract terms using contract remedies . . . [or] by imposing any remedy available to enforce a judgment, including, but not limited to, contempt.”
4. **Naming a Trustee for the Children.** When parties stipulate that the children should be named as beneficiaries of insurance, they tend not to think about the fact that minors cannot receive direct payment of the money. Instead, a conservator must be appointed to hold and manage life insurance until each child reaches the age of 18. No one seriously believes that an 18 year old will manage money wisely, so many divorcing couples agree that a trustee should be selected to manage the money for the children. This raises the question of who the trustee should be. Consider the following optional language:

> “Until all child and spousal support under this Judgment has been fully paid, husband shall maintain the life insurance on his life described below in full force and effect naming wife as trustee beneficiary for the benefit of all of the parties’ children pursuant to a life insurance trust which the parties shall create.”

OR

> “Until all child and spousal support under this Judgment has been fully paid, husband shall maintain the life insurance on his life described below in full force and effect naming a bank or corporate trustee that performs the function of trustee in the regular course of its business. The terms of the trust shall be set forth in a life insurance trust which the parties shall create.”

[Note: banks will typically decline to act as trustee unless the principal amount of the trust is at least $150,000.]

5. **Using the Term “Irrevocable Beneficiary.”** Frequently we see judgments which require the husband to name his former spouse or children as “irrevocable beneficiary” of the policy. “Irrevocable” means what is says and is generally not what is intended. The proper designation is “primary beneficiary.” Use of the word “irrevocable” can leave the payor husband in a situation where his support obligation is terminated or fully satisfied yet no one else can be named beneficiary because the designation purports to be “irrevocable.”

End
A. PUBLIC POLICY

107.106 Additional requirements of decree. (1) An order or judgment providing for the custody, parenting time, visitation or support of a child under ORS chapter 25, 107, 108, 109 or 110 or ORS 419B.400 or 419C.590 shall include:

(a) Provisions addressing the issues of:

(A) Payment of uninsured medical expenses of the child;

(B) Maintenance of insurance or other security for support; and

(C) Maintenance of health insurance for the child.

* * *

B. LIFE INSURANCE - TO SECURE CHILD OR SPOUSAL SUPPORT

107.810 Policy. It is the policy of the State of Oregon to encourage persons obligated to support other persons as the result of a dissolution or annulment of marriage or as the result of a legal separation to obtain or to cooperate in the obtaining of life insurance adequate to provide for the continued support of those persons in the event of the obligor’s death. [1981 c.775 §§9]

107.820 Support order as insurable interest; order to obtain, renew or continue insurance; right of beneficiary to purchase insurance or pay premiums. A court order for the payment of spousal or child support whether issued prior to, on or following November 1, 1981, constitutes an insurable interest in the party awarded the right to receive the support. In any case of marital annulment, dissolution or separation, the issue of life insurance shall be determined as follows:

(1) When the judgment creates an obligation of spousal or child support or awards a share of a pension or retirement plan, the judgment may also require that the obligated party maintain any existing insurance policies on the life of the obligated spouse and in which the dependent spouse is named as beneficiary. The judgment may require that the policies be maintained until the obligation is fulfilled. The premiums may be paid by the obligated spouse, and the court may consider the cost of premiums when determining the obligation. Any life insurance policies on the life of the obligated spouse owned by parties outside of the marriage or purchased and held for purposes clearly outside the marriage relationship are exempt from this subsection.

(2) If the party ordered to pay support or a share of a pension or retirement plan has no life insurance policy naming as beneficiary the party ordered to receive either support or a share of a pension or retirement plan, or if an existing policy is inadequate to cover the obligation, the court in a judgment may order that the party ordered to pay shall purchase a life insurance policy naming as beneficiary the party ordered to receive the support or a share of a pension or retirement plan and that the obligated...
party shall pay premiums on the policy and keep the policy in force until the obligation ends. The obligated spouse has the option of obtaining a nonreducing term life insurance policy or any other type of policy in lieu of using existing policies.

(3) Additionally, the party awarded the right to receive support or a share of a pension or retirement plan may purchase a life insurance policy on the life of the obligated party. In such case, the court shall order the obligated party to undergo a physical examination. All rights of policy ownership, including those regarding the extent of coverage, shall be in the party purchasing the policy under this subsection who shall also be responsible for paying the premiums. The provisions of this subsection may be exercised at the time of annulment, dissolution or separation, or at any later time while the obligation continues.

(4) Upon motion of either party, the court shall order a party to renew a life insurance policy allowed to lapse for any reason during the pendency of the suit.

(5) A party who is the beneficiary of any policy under this section upon which the other party is obligated to pay premiums is entitled, in the event of default, by the paying party, to pay the premiums on the policy and to obtain a supplemental judgment for reimbursement of any money so expended. A default in the payment of premiums by the party obligated by the judgment or order is a contempt of the court.

(6) Life insurance retained or purchased by an obligor under subsection (1) or (2) of this section for the purpose of protecting the support, pension or retirement plan obligation shall not be reduced by loans or any other means of reduction until the obligation has been fulfilled. The obligee, or the attorney of the obligee, shall cause a certified copy of the judgment to be delivered to the life insurance company or companies. If the obligee or the attorney of the obligee delivers a true copy of the judgment to the life insurance company or companies identifying the policies involved and requesting such notification under this section, the company or companies shall notify the obligee, as beneficiary of the insurance policy, whenever the policyholder takes any action that will change the beneficiary or reduce the benefits of the policy. Either party may request notification by the insurer when premium payments have not been made. If the obligor is ordered to provide for and maintain life insurance, the obligor shall provide to the obligee a true copy of the policy. The obligor shall also provide to the obligee written notice of any action that will reduce the benefits or change the designation of the beneficiaries under the policy. [1981 c.775 §§11; 1983 c.728 §§5; 1987 c.885 §§4; 1993 c.716 §§5; 2003 c.576 §§131]

107.830 Physical examination may be ordered; responsibility for premiums. The court may order a party to undergo a physical examination for the purpose of obtaining life insurance and may order this party to pay any premiums on such policy, except in cases in which the life insurance policy has been obtained under ORS 107.820 (3). If life insurance is obtained by a spouse or former spouse with an insurable interest, the person obtaining the policy is responsible for all premiums to be paid and for the choice of policy type and amount. If either party owns life insurance on the life of the paying spouse, and it is allowed to lapse for any reason during the suit, upon the request of the party receiving support, the paying spouse can be ordered to submit to a physical examination for the purpose of renewing the policy, if such examination is a requirement for renewal. [1981 c.775 §§12]
This was an attorney malpractice case. The defendant attorney had drafted a dissolution judgment on behalf of his client, the wife. The judgment required husband to "maintain his present life insurance policy at the present limits for the minor children." The husband died six months later leaving the insurance benefits to his parents. The client sued the attorney alleging he failed to protect her under ORS 107.820. The specific acts of negligence complained of were:

"(1) He failed to notify the insurance company that insured the life of William Seim of the terms of the Decree of Dissolution.

"(2) He failed to instruct plaintiffs to notify the insurance company that insured the life of William Seim of the terms of the Decree of Dissolution.

"(3) He failed to determine the existence of insurance referred to in the Decree of Dissolution." Seim, supra at page 70.

Defendant attorney offered evidence from the insurance company to the effect that the company would not have honored the decree even if it had received notice of it because it did not clearly describe a policy issued by that company. Based on this evidence, the Court held that the attorney’s mistake was not properly described in the complaint, hence a judgment should be entered for the defendant attorney. As part of its ruling, the Court made the following comments:

“The problem in this case started with the preparation of the dissolution judgment by defendant. It requires William to ‘maintain his present life insurance policy at the present limits for the minor children.’ We know from the record that there never was a policy naming the children as beneficiaries; there were at least five policies, some of which, at least, had named plaintiff Hively as beneficiary. Before the dissolution, William had changed the beneficiaries on those policies to be his parents, the Seims. We have no doubt that, if the judgment had described the policy or policies, giving the name of the insurer and the policy number or numbers and that, if a certified copy of the judgment had been delivered to the insurer, plaintiffs would have been protected. Plaintiffs, however, do not allege that defendant was negligent in either of those respects. Had they done so, that negligence would have been the direct cause of plaintiffs' damage. In this action, plaintiffs accept the dissolution judgment as adequate and allege that defendant was negligent in failing to notify the insurer of the terms of the judgment, in failing to instruct plaintiffs to do so and in failing to determine the existence of insurance referred to in the judgment.[fn3] On this record, even if defendant had done those things, plaintiffs would not have been protected** because the judgment does not specifically identify the insurer or the policy number, if the company had received notice of the terms of the judgment, it would not have paid out, or even held up, the proceeds for the benefit of the children.” Seim, supra at page 71 [emphasis added].
Table 3  
Sample Life Insurance Language to Avoid Malpractice  
The policy name, # and face amount must be stated  
See Seim v Soriano, 94 Or App 67 (1988)

**Life Insurance.** Until all child and spousal support under this Judgment has been fully paid, husband shall maintain the life insurance on his life described below in full force and effect naming wife as primary beneficiary

<table>
<thead>
<tr>
<th>NAME OF COMPANY</th>
<th>POLICY #</th>
<th>FACE AMOUNT</th>
</tr>
</thead>
<tbody>
<tr>
<td>Great Western Life Insurance Co.</td>
<td>A789461</td>
<td>$150,000</td>
</tr>
</tbody>
</table>

Husband shall not borrow money from the insurance policy. Pursuant to ORS 107.820(6), husband shall provide wife with a true copy of the insurance policy described above and shall immediately provide written notice of any action that will reduce the death benefit or change the designation of the beneficiaries under the policy.

Pursuant to ORS 107.820(6) wife shall cause a certified copy of the Judgment dissolving the parties' marriage to be delivered to the applicable life insurance company or companies requesting notification when premium payments have not been made or the insured takes any action that will change the beneficiary or reduce the death benefit payable under the policy. The company shall notify wife whenever a premium payment has not been made or the insured takes any action that will change the beneficiary or reduce the benefits of the policy. In the event husband violates these insurance provisions, a constructive trust shall be imposed over the husband’s estate as well as the proceeds of all insurance owned by husband at the time of his death to secure payment of this insurance obligation.

**Employer Provided Policies**

Practice Pointer: If the insurance is provided via an employer provided policy, it is sometimes difficult to determine who the insurer is and who is responsible for complying with ORS 107.820. Try naming the insurer and the employer and send the letter to both:

- NAME OF COMPANY
  - Aetna Life provided as an employee benefit by Nike, Inc.

**Insurance not yet Purchased**

*Insert the following:*

Husband shall immediately purchase a life insurance policy on his life in the amount stated above. As soon as it is available and not later than 60 days from the date this Judgment is signed by the court, he shall provide the company name and policy number to wife. Thereafter, the parties shall promptly sign a supplemental judgment confirming the policy details so that a copy of the judgment as supplemented may be served on the applicable life insurance company.
This matter came before the court based upon a stipulation of the parties made through their respective attorneys and it appearing from the stipulation that information regarding Petitioner’s life insurance obligation was left blank when it was submitted to this court and that the parties now desire to fill in the missing information.

NOW THEREFORE, IT IS ORDERED AND ADJUDGED that paragraph 18 of the General Judgment of Dissolution of Marriage signed in this case on February 24, 2004 is hereby corrected and supplemented so as to provide the following information regarding petitioner’s life insurance obligation:

<table>
<thead>
<tr>
<th>NAME OF COMPANY</th>
<th>POLICY #</th>
<th>FACE AMOUNT OF INSURANCE</th>
</tr>
</thead>
<tbody>
<tr>
<td>Northwestern Life Insurance Company</td>
<td>A789461</td>
<td>$150,000</td>
</tr>
</tbody>
</table>

Dated this ___ day of ________, 2013.

Circuit Judge

IT IS SO STIPULATED:

Paul J. DeBast OSB #72065
Attorney for Petitioner

Paul Saucy OSB #79374
Attorney for Respondent
August 15, 2004

Northwestern Life Insurance Company CERTIFIED MAIL
720 East Wisconsin Ave. RETURN RECEIPT
Milwaukee, WI 53202 REQUESTED

Re: Northwestern Mutual Life Policy No. 13-856-211 on the life of Ivan Binhad

Ladies and Gentlemen:

This office represents Twila Binhad, the former wife of your policyholder, Ivan Binhad. Enclosed is a court certified copy of General Judgment of Dissolution of Marriage involving your insured, Ivan Binhad. The judgment requires Mr. Binhad to maintain the policy in full force and effect naming Twila Binhad as primary beneficiary.

Pursuant to ORS 107.820(6) Ms. Binhad hereby requests that you notify her whenever Mr. Binhad takes any action that will change the beneficiary, reduce the benefits or when premium payments have not been made. **YOU MUST HONOR THIS REQUEST OR SUFFER LEGAL PENALTIES AND POSSIBLE DAMAGES FOR FAILURE TO DO SO.** Until further notice, any notices you are required to give Ms. Binhad should be sent to the following address:

Ms. Twila Binhad
20715 SW Westview
Portland, Oregon 97229

Very truly yours,

DeBAST, McFARLAND & RICHARDSON LLP

Paul J. DeBast
May 23, 2002

Paul J. Attorney  
9600 S.W. Barnes Rd.  
Portland, OR 97225

0000 0909 0313 2786 1 004 Michael ________

Dear Paul J. DeBast,

Thank you for contacting our office.

I received this decree from an associate Amy Amon who asked me to return it to you for her.

We are returning the divorce decree(s) that was submitted. We have retained a photocopy for our records.

If you have questions or further assistance needs, please contact our office at the telephone number below.

Sincerely,
March 23, 2004

Ms. Twila Binhad
20715 SW Westview
Portland, Oregon 97229

Dear Twila:

Enclosed is a copy of the court's judgment dissolving your marriage. Oregon law provides that your divorce is effective on the day the judge signs it. This is an important document and should be kept in a safe place for future reference. Now that the case is concluded, there are several things I need to tell you about.

ALTERNATE #1 WE REPRESENT OBLIGEE AND WE SENT LIFE INS. LETTER

Your divorce judgment requires Ivan to maintain his $150,000 Northwestern Life Insurance Company policy in force naming you as primary beneficiary. You are supposed to be provided with a copy of the policy. You should let me know if you have trouble getting the policy copy. Oregon law permits you to send Northwestern Life Insurance Company a copy of the Judgment of Divorce and a request for notice if Ivan should fail to perform his duties regarding the policy. Enclosed is a copy of a letter I am sending to Northwestern Life Insurance Company on your behalf. We cannot undertake to keep the insurance company advised as to changes in your address, so this will be your responsibility. It is imperative that you notify the company by certified mail if and when you move so that they can continue to correspond with you.

ALTERNATE #2 LIFE INSURANCE INFORMATION NOT FILLED IN ON JUDGMENT

As you know, the Court's judgment requires Ivan to maintain certain amounts of life insurance on his life naming you as beneficiary. Oregon law gives you the right to send a certified copy of the judgment to his life insurance company. The notice can include a request that the company inform you if the policy is allowed to lapse or the beneficiary is changed. The trouble is that the company name and policy number were not inserted in the appropriate section of the divorce judgment before it was signed by the judge. As a result, if you sent the judgment to the insurance company and gave the notice request, the company would not know that the judgment describes their policy and, hence the company may not honor your request.
This may not seem very important to you now, but if something were to happen to Ivan, you would be very unhappy if the insurance were not in force or the beneficiary clause named someone else other than you or your children. For this reason, I urge you to follow up on this issue and insist that Ivan provide you with the information so that we can fill it in on a supplemental judgment. Once that is done, we can have it signed by a judge and then send a certified copy of the supplemental judgment to the insurance company along with your request for notice if the beneficiary changes or the policy lapses. Some clients tell us they want to avoid further legal expense after the judgment is signed so they do not want us to follow up on the insurance issue and make sure the job is completed. Accordingly, we will not do anything further in terms of trying to force Ivan to complete the supplemental judgment unless you ask us to.

**ALTERNATE # 3 REMINDER FOR OBLIGOR**

**Life Insurance.** Your divorce judgment requires you to maintain certain amounts of life insurance in force. Oregon law requires you to provide (NAME OF FORMER SPOUSE) with a true copy of the policy, as well as written notice of any action you take that will reduce the insurance benefits or change the beneficiaries under the policy. Please let me know if you have questions about this obligation.

------------

**Wills and Death Benefits.** If you currently have a Will, Oregon law provides that your divorce revokes all provisions in your Will which run in favor of Ivan and the effect of the Will is the same as though Ivan did not survive you. You should also know that a remarriage revokes any will you may have. If you do not have a Will, Oregon law provides that your assets pass to children (even if they are too young to handle the money). If a person does not have children, the law says assets pass first to parents and, if parents are not living, then to brothers and sisters and so on down the blood line. I would be happy to help you revise your Will or help you prepare a new Will, Trust or estate plan if you do not have one. **Life insurance**, pension and retirement benefits are typically not affected by the court's judgment. You must change the beneficiary designation on your life insurance and retirement benefits unless you want these benefits to pass to your former spouse upon your death.
Elimination of Rights Upon Death. The property division aspects of this judgment shall become effective immediately. Neither party shall receive property awarded to the other under the terms of this Judgment. To the fullest extent allowed by law, this judgment shall serve as revocation of a party as "beneficiary" and "surviving spouse" on all Individual Retirement Accounts, pensions, 401(k) plans, profit sharing plans, ESOP, and other retirement accounts in the name of the other party, and any designation in any will, trust, and living will that benefits the other party that is now in effect, even if no formal change of beneficiary is made. Except as otherwise provided herein, this Judgment serves as revocation of a party as "beneficiary" and "surviving spouse" on all life insurance policies insuring either party's life in which either party has any ownership interest whatsoever.

*Note ORS 107.121 provides as follows:

Revocation of designation of beneficiary upon entry of judgment. (1) A judgment of dissolution, separation or annulment may revoke a designation of beneficiary made by a principal in favor of a spouse or a relative of the spouse if the designation of beneficiary is revocable as described in subsection (2) of this section.
(2) A designation of beneficiary is revocable for the purposes of this section if the principal at the time of the judgment may, by law or under the terms of the instrument, cancel or change the designation of beneficiary.
(3) A designation of beneficiary is revocable for the purposes of this section without regard to whether the principal is:
   (a) Competent at the time of the entry of judgment; or
   (b) Able to designate the principal in place of the spouse or in place of the relative of the spouse.
(4) The revocation of a designation of beneficiary under this section becomes effective upon entry of the judgment. [2005 c.285 §3]
Beware! Automatic Beneficiary Revocation Law Not Effective for ERISA and Federal Life Insurance and Retirement Benefits

By Clark B. Williams

Be careful in relying on the new “automatic beneficiary revocation” statute, ORS 107.118 - 107.131 (2005 Oregon Laws Chapter 285) as it applies to employer-provided ERISA benefits (both life insurance and retirement benefits) and to federal employment benefits.

This new statute provides that beneficiary designations in favor of a former spouse are automatically revoked if so provided in the judgment of dissolution or unlimited separation. The statute applies broadly to beneficiary designations of all types, expressly including ERISA and federal employment benefits. However, the statute is pre-empted by federal law with regard to those benefits.

So said the U.S. Supreme Court in \textit{Egelhoff v. Egelhoff}, 532 US 141 (2001), involving a similar Washington State statute.

In that case, a Boeing employee died in a car accident two months after divorcing his wife and before removing her as beneficiary of his employer-provided life insurance and retirement benefits. Washington law provided for automatic revocation on divorce of all designations of “nonprobate assets” in favor of a former spouse. Notwithstanding the statute, Boeing paid the benefits to the former wife, and the husband's children by prior marriage brought suit. In a 7-2 decision, the Supreme Court held that the Washington statute was pre-empted by ERISA and confirmed the payment of benefits to the former wife. In its opinion, the Supreme Court recognized that all employer-provided life insurance and retirement benefits are governed by ERISA, and that ERISA itself provides that it “shall supersede any and all State laws insofar as they may now or hereafter relate to any employee benefit plan.”

ERISA requires that each plan shall “specify the basis on which payments are made to and from the plan” and that each plan must be administered “in accordance with the documents and instruments governing the plan.” The Court recognized Congress' goal to allow each ERISA plan to have a nationally uniform system of plan administration. “Differing state regulations affecting an ERISA plan's system for processing claims and paying benefits impose precisely the burden that ERISA preemption was intended to avoid.”

Therefore, Oregon's new statute will not be applicable to ERISA plans, despite its express reference to ERISA. Instead, the terms of the plan will control. Indeed, some plans do provide that, upon receipt of notice regarding the divorce of a participant, beneficiary designations are automatically revoked. However, most plans do not so provide.

So, what is an ERISA plan? Generally, ERISA governs all “qualified retirement plans” and all “welfare benefit plans” sponsored by private sector employers. “Qualified retirement plans” include 401(k) plans, profit sharing plans, defined benefit plans, employee stock ownership plans (ESOPs), money purchase pension plans and cash balance pension plans. “Welfare benefit plans” include non-retirement employee benefits, including life insurance, health insurance, cafeteria plans and vacation pay plans.

However, ERISA does not apply to plans which cover only the business owner and/or the owner's spouse. Therefore, for example, the profit sharing plan of a self-employed real estate agent who has no employees is not an ERISA plan.

Also, ERISA does not apply to deferred compensation plans (also known as 457 plans), stock option plans, SEP-IRAs, SIMPLE plans, 403(b) plans (also known as tax sheltered annuity plans) or IRA accounts. And ERISA does not apply to retirement or welfare benefit plans sponsored by state and local government employers. This would include Oregon PERS. For all these types of plans, the new statute should be fully effective.

The other large group of plans to consider are the federal plans, specifically: the Civil Service Retirement System (CSRS), the Federal Employees Retirement System (FERS), the Thrift Savings Plan (TSP), military
retirement benefits, and Federal Employees Group Life Insurance (FEGLI). The new Oregon statute purports to apply to these programs, as well. However, the effectiveness of the statute on these programs is extremely doubtful. No benefits are paid to a former spouse from CSRS, FERS or military retirement system unless specifically provided in a court order. So as a practical matter, the only systems to be concerned with are TSP and FEGLI.

Specifically, the TSP regulations provide that the beneficiary designation on file with the government at the time of death controls the payments of the TSP account at death.7 And the FEGLI statute does the same.8 There is no provision under either federal scheme for automatic revocation of a designation on divorce. Further, the Office of Personnel Management, which administers FEGLI, has stated, with regard to designations: “... the FEGLI law preempts state law ...”9 So there is little doubt that the new Oregon statute will be ineffective to revoke a designation with respect to a federal employee's TSP or FEGLI benefits.

In summary, don't rely on new ORS 107.118-.131 and the divorce judgment to automatically revoke beneficiary designations for ERISA and federal retirement and life insurance benefits. The new statute is preempted by ERISA and federal law with respect to those benefits. Instead, you should still instruct your clients to affirmatively change their beneficiary designations, and document your file accordingly.

Clark B. Williams is a shareholder of Heltzel, Upjohn, Williams, Yandell, Roth, Smith & Petersen, P.C. in Salem. He has a B.S. from the University of Washington (1976) and a J.D. from Willamette University College of Law (1979). He is a member of the state bars of Oregon (1979) and Washington (1982), the OSB Tax Section, OSB Family Law Section, and the Western Pension Conference. Clark carries an “AV” rating in Martindale-Hubbell (since 1995) and is listed in Best Lawyers in America (since 2001).

Clark is a pension specialist focusing on the design and administration of qualified retirement plans and other employee benefits for Oregon small businesses. He is knowledgeable in federal income tax law and ERISA. He has assisted Family Law Section members and their clients draft and implement well over 1,000 “qualified domestic relations orders,” or QDROs, over the past twenty years. He has been a speaker regarding QDROs at the Oregon Judicial Conference and the OSB Family Law Conference.


Footnotes:

1 Employee Retirement Income Security Act of 1974, as amended, 29 USC 1001 et..seq.
2 29 USC ‘1144(a).
3 29 USC ‘1102(b)(4)
4 29 USC ‘1104(a)(1)(D)
5 532 US at 142, 150.
6 29 CFR ‘2510-3.3
7 5 CFR ‘1651.2. Also 5 CFR ‘1651.4 provides that the exclusive way for a member to change a beneficiary is to complete and file a new beneficiary form or a revocation form. “A will, or any document other than Form TSP-3 or Form TSP-11-B may not be used to change or cancel a beneficiary(ies) of a TSP account.” Id.
8 5 USC ‘8705(a)
IN BRIEF

PRESERVING SURVIVOR BENEFITS IN THE MILITARY PENSION UPON DIVORCE

(Originally published in the May 2004 issue of In Brief as “Divorce and the Military Pension,” updated November 2012)

Attorneys shudder at the prospect of dividing a military pension. They have reasons to. The military seems to go out of its way to make the process difficult. Most military spouses have to fight hard to get a share of the pension and to convince the court to order the military member to elect the Survivor Benefit Plan (“SBP”). The SBP guarantees that the former spouse’s monthly benefits will continue even after the member dies.

The trial court enters a “qualifying court order” under 10 USC §1450(f)(2) after entry of the final judgment of dissolution. It usually has two parts. The first provides for division of monthly retirement benefits as they are paid out. The other requires (hopefully) that the member elect the SBP when the member retires. Most attorneys know enough to send the order to the military finance center right away even though the member is not yet retired. A false sense of security sets in when the military starts making the monthly payment to the former spouse once the member does retire. The problem lies in the fact that the division of the monthly benefit and the SBP are two separate programs. An election must be made on each.

The SBP election is not made until the member actually retires, perhaps many years after the divorce. The military retirement finance center will not honor an order which requires the member to designate the former spouse to receive the SBP. They will only do what their member instructs them to do at that time (e.g., to name the new spouse to receive the SBP or to have no SBP at all), even if those instructions are contrary to the order. The attorney may never know if the member a elected the SBP until the member actually dies and the payment of the monthly payments to the former spouse stop. The member may be in contempt of court for failing to elect the SBP for the former spouse’s benefit, but how do you cite a dead man for contempt?

Most attorneys are also unaware that the entry of a dissolution judgment automatically terminates the previous SBP election of a member who is already retired. To protect the former spouse, the dissolution judgment should require the member to re-elect the SBP naming the now former spouse to receive the after death benefit. The member has one year to affirmatively file what amounts to a “re-election” to again name the now former spouse as the SBP beneficiary. The SBP coverage is lost if the member fails to do so within that one year window.

The solution is this: federal law requires the military to allow a former spouse to protect court ordered SBP benefits by filing a “deemed election” under 10 USC § 1450(f)(3) along with the court order. This “deemed election” must be made on DD Form 2656-10 (Survivor Benefit Plan Request for Deemed Election) and be filed with the appropriate military finance center within one year after the entry of judgment with a court-certified copy of the order which creates the entitlement. This letter must be sent separate (another major trap) from the letter requesting direct payment of the basic military retirement benefits.

The military is particularly difficult to deal with when it comes to dividing retirement ben-

DISCLAIMER

IN BRIEF includes claim prevention information that helps you to minimize the likelihood of being sued for legal malpractice. The material presented does not establish, report, or create the standard of care for attorneys. The articles do not represent a complete analysis of the topics presented, and readers should conduct their own appropriate research.
efits. The financial stakes are high and there are traps which need to be avoided. Remember that there are two different programs, each of which requires its own separate notice. One program divides the monthly retirement benefit. The other deals with the SBP. The “qualifying court order” should address both. Then protect your client’s SBP award by making the “deemed election” in each and every case. Otherwise, the military finance center will honor whatever the member elects at the time of retirement, or will automatically extinguish an existing SBP election if the divorce is after retirement, even if doing so is contrary to the court’s order.

CLARK B. WILLIAMS
HELTZEL WILLIAMS LAW FIRM

In Brief 1996

Revised November 2012
SURVIVOR BENEFIT PLAN (SBP)/RESERVE COMPONENT (RC) SBP REQUEST FOR DEEMED ELECTION

The public reporting burden for this collection of information is estimated to average 20 minutes per response, including the time for reviewing instructions, searching existing data sources, gathering and maintaining the data needed, and completing and reviewing the collection of information. Send comments regarding this burden estimate or any other aspect of this collection of information, including suggestions for reducing the burden, to the Department of Defense, Washington Headquarters Service, Executive Office Directives, Information Management Division, 1155 Defense Pentagon, Washington, DC 20301-1155 (0704-0440). Respondents should be aware that notwithstanding any other provision of law, no person shall be subject to any penalty for failing to comply with a collection of information if it does not display a currently valid OMB control number.

PRIVACY ACT STATEMENT

AUTHORITY: 10 U.S.C. Chapter 73, subchapters II and III; DoD Instruction 1332.42, Survivor Annuity Program Administration; DoD Financial Management Regulation, Volume 7B, Chapter 43; and E.O. 9397 (SSN).

PRINCIPAL PURPOSE(S): Used by a former spouse to deem an election for Former Spouse SBP coverage.

ROUTINE USE(S): To former spouses for purposes of providing information, consistent with the requirements of 10 U.S.C. Section 1450(k)(3), regarding Survivor Benefit Plan coverage.

DISCLOSURE: Voluntary; however, failure to provide requested information within the first year following filing of the court order or filing which requires former spouse SBP coverage will result in delays in initiating, or denial of, former spouse SBP coverage.

GENERAL.

1. Read these instructions carefully before completing the form. Please print legibly.

2. Ensure that you advise the finance center (see item 3 below for address) of your marital status, correspondence and check address changes, at all times. Reserve Component former spouses must notify their personnel center (see item 4 below for address) of their marital status and correspondence address at all times.

3. For those who are deeming an SBP election against a member who is currently serving on active duty or receiving retired pay, mail your election (certified or registered mail with return receipt requested is strongly recommended) to the appropriate Uniformed Services’ designated agents are:

(a) ARMY, NAVY, AIR FORCE and MARINE CORPS: Defense Finance and Accounting Service, U.S. Military Retirement Pay, P.O. Box 7130, London, KY 40742-7130;

(b) COAST GUARD: Commanding Officer (LGL), USCG Personnel Service Center, 444 S.E. Quincy Street, Topeka, KS 66683-3591;

(c) PUBLIC HEALTH SERVICE: Office of Commissioned Corps Support Services, Compensation Branch, 5600 Fishers Lane, Room 4-50, Rockville, MD 20857;

(d) NATIONAL OCEANIC AND ATMOSPHERIC ADMINISTRATION: Same as U.S. Coast Guard.

4. For those who are deeming an SBP election against a Reserve Component member who is not yet receiving retired pay (under age 60), mail your election (certified or registered mail with return receipt attached is strongly recommended) to the appropriate Branch of Service as follows:

(a) ARMY: Commander, Human Resources Command - St. Louis, ATTN: AHRC-PAP-T, 1 Reserve Way, St. Louis, MO 63132-5200;

(b) NAVY: Navy Reserve Personnel Center (PERS 912), 5722 Integrity Drive, Millington, TN 38054;

(c) AIR FORCE: Headquarters, ARPC/DPNSE, 6760 E. Irvington Place, Denver, CO 80250-4020;

(d) MARINE CORPS: Headquarters, U.S. Marine Corps, Separation & Retirement Branch (MMSR-6), 3280 Russell Road, Quantico, VA 22134-5103;

(e) COAST GUARD: Commanding Officer (LGL), USCG Personnel Service Center, 444 S.E. Quincy Street, Topeka, KS 66683-3591.

SECTION I - MEMBER IDENTIFICATION

1. MEMBER NAME (Last, First, Middle Initial)
2. SSN
3. BRANCH OF SERVICE
   a. (X one)
      [ ] ACTIVE [ ] RESERVE
      [ ] NATIONAL GUARD

4. IS MEMBER RETIRED? [ ] YES [ ] NO
5. IF YES, DATE OF RETIREMENT (YYYYMMDD)

SECTION II - FORMER SPOUSE IDENTIFICATION

6. FORMER SPOUSE NAME (Last, First, Middle Initial)
7. SSN
8. ADDRESS (Include ZIP Code)
9. DATE OF BIRTH (YYYYMMDD)

10. MARRIAGE HISTORY

   a. DATE MARRIED TO MEMBER
      (Listed In Item 1 above) (YYYYMMDD)
   b. DATE OF DIVORCE
      (YYYYMMDD)
   c. ARE YOU CURRENTLY MARRIED?
      [ ] YES [ ] NO
   d. IF YES, DATE OF CURRENT MARRIAGE (YYYYMMDD)

DD FORM 2656-10, APR 2009
PREVIOUS EDITIONS OBSOLETE.
**SECTION III - AUTHORITY TO REQUEST DEEMED SBP ELECTION**

11. IS ELECTION MADE PURSUANT TO REQUIREMENTS OF COURT ORDER?  (If "Yes", attach a copy of the document.)  
- [ ] YES  
- [ ] NO

12. IS ELECTION BEING MADE PURSUANT TO WRITTEN AGREEMENT PREVIOUSLY ENTERED INTO VOLUNTARILY AS PART OF OR INCIDENT TO A PROCEEDING OF DIVORCE, DISSOLUTION OR ANNULMENT?  
- [ ] YES  
- [ ] NO

**NOTE:** If you answered "No" to both 11 and 12, above, STOP. You are NOT eligible to request a Deemed SBP election.

13. IF "YES" TO QUESTION 12, WAS SUCH VOLUNTARY WRITTEN AGREEMENT INCORPORATED IN, RATIFIED, OR APPROVED BY A COURT ORDER?  (If "Yes", attach a copy of the document.)  
- [ ] YES  
- [ ] NO

**SECTION IV - DEPENDENT CHILDREN INFORMATION**

14. LIST DEPENDENT CHILDREN  (If required to be covered under court order/agreement)  (List only children resulting from the parties' marriage to each other.)

<table>
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<tr>
<th>a. NAME  (Last, First, Middle Initial)</th>
<th>b. DATE OF BIRTH  (YYYY/MM/DD)</th>
<th>c. SSN</th>
<th>d. RELATIONSHIP  (Son, daughter, stepson, etc.)</th>
<th>e. DISABLED?  (Yes/No)</th>
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15. REMARKS  (Use this space to further explain any item if necessary.  Reference by item number.)  

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**SECTION V - FORMER SPOUSE SIGNATURE**

16. SIGNATURE  

17. DATE SIGNED  (YYYY/MM/DD)
Division of retirement benefits in domestic relations cases is handled either through the inclusion of technical text in the dissolution or separation judgment itself, or more often through entry of a supplemental judgment, commonly called a qualified domestic relations order (QDRO).

**Types of Plans Divisible by QDROs**

The types of retirement plans that are typically divisible by a QDRO are called “tax-qualified” plans. These plans meet specific Internal Revenue Code requirements for favorable tax treatment. Examples include 401(k) plans, profit-sharing plans, and most traditional pension plans, including government plans and church plans.

Most non-qualified retirement plans are not divisible by a QDRO. Typically, these non-divisible plans are “deferred compensation” plans, “executive” plans, or “supplemental” plans. Be especially careful when encountering a plan with those or similar terms in its title.

Although this article will use the term QDRO for convenience, and QDRO is the correct term for the instrument that divides a tax-qualified retirement plan, instruments that divide federal retirement benefits are “court orders acceptable for processing” (COAP), and instruments that divide military benefits are “qualifying court orders.”

**Problems Resulting from Delay**

Problems can arise from procrastination or failure to understand the nature of benefits and how benefits are divided. Practitioners often delay in undertaking discovery of the parties’ retirement benefits, in learning the nature of the retirement benefits, and in dividing the benefits either through the dissolution judgment or through a QDRO. Division of benefits should be done simultaneously with or as soon as possible after the entry of the judgment of dissolution of marriage. The more time that passes before the QDRO is entered, the more things can go wrong. Some things that go wrong cannot be fixed.

- The plan participant might remarry, and his or her new spouse may acquire rights in the plan that cannot be divested by subsequent entry of a stipulated judgment.

- The plan participant might die. Sometimes, it is possible to complete the division of retirement benefits or to secure a survivor benefit following the participant’s death, but not always.

- The plan participant might commence pension benefits, with resulting loss of the opportunity to provide a survivor benefit to the former spouse. The participant might commence benefits earlier than expected due to disability or early retirement. Although the pension plan participant’s benefits still can be divided, the spouse’s benefit payments will cease when the participant dies, and no further payments will be made by the plan to the former spouse.

- The plan participant might cash out benefits in a defined contribution plan, leaving no benefits to transfer to a former spouse.

- The parties might move. It may not be possible to locate a party when it comes time to en-
ter a QDRO to divide the plan benefits. The court may lose personal jurisdiction over a party if enough time elapses, requiring the dissolution to be forwarded to a new jurisdiction where (hopefully) the court will register the judgment for enforcement and enter a QDRO to implement the division of retirement benefits.

- Defined contribution plans change their record keepers and purge old data from time to time. Passage of time can make it impossible to divide benefits in a defined contribution plan by reference to an account balance as of a prior date.

- The former spouse might lose a claim for survivor benefits. The survivor benefit in a military pension must be secured within one year after the dissolution of marriage. If a Federal Employee Retirement System (FERS) or Civil Service Retirement System (CSRS) member is receiving retirement benefits as of the date of dissolution, the dissolution judgment must state that the former spouse will receive the survivor annuity.

- For defined contribution plan accounts, benefits will be paid to the participant’s designated beneficiary. The surviving former spouse’s right to a share of the benefits will be lost if a QDRO is not entered with the court and sent to the plan before the participant dies, unless the participant’s former spouse remained as the beneficiary.

**Preliminary Research – What to Look For**

Obtain a copy of the plan documents. Obtain the name, address, and phone number of the plan administrator. Find out whether the plan administrator has a form of QDRO that the plan desires to be used. If you decide to use the plan’s form of QDRO, be sure you understand its operation.

Determine whether the plan can establish a separate benefit for the alternate payee (typically the former spouse but in some cases a child) independent of the benefits retained by the participant.

- Most qualified defined contribution plans will establish a separate account within the plan for the benefit of the alternate payee. Under most, but not all, defined contribution plans, an alternate payee may elect to receive a distribution of his or her account soon after the QDRO is approved by the plan.

- Before the participant retires, most qualified defined benefit plans will provide a separate interest for the alternate payee (i.e., benefits payable over the alternate payee’s lifetime at a time and in a manner of the alternate payee’s choosing). After the participant retires, nearly all qualified

defined benefit plans require that the alternate payee’s benefits be paid as a shared interest (i.e., benefits payable over the participant’s lifetime, requiring the protection of a post-retirement survivor annuity, if still available).

- Some pensions, including military and federal (FERS or CSRS), Oregon Public Service Employees Retirement Plan (OPSRP) and, in some cases, Oregon Public Employees Retirement System (PERS), do not permit the creation of a separate interest for the alternate payee. The alternate payee’s benefit payments will not commence until the participant’s benefits commence.

**Benefit Payment Considerations**

Make sure you know the payout or benefit options available under the plan. The QDRO cannot provide the alternate payee with any type of benefit or option not otherwise provided by the plan.

- If the plan provides for survivor benefits only to a spouse or former spouse, then a QDRO cannot provide a survivor benefit to a child.

- A QDRO cannot provide for a joint and survivor option with the alternate payee as primary recipient and the new spouse as a survivor beneficiary.

- In a defined benefit plan with an early retirement subsidy, the QDRO cannot require the plan to pay a portion of the subsidy to the alternate payee before the plan participant starts receiving benefits. (If a plan encourages early retirement by only partially reducing benefit payments, the “subsidy” is the difference between the partially reduced payment and a fully reduced payment.)

- The early commencement of benefits from a defined benefit plan to an alternate payee will result in a decrease in monthly benefit payments to the alternate payee.

Under most, but not all, defined benefit plans, an alternate payee may start receiving benefits any time the participant attains (or would have attained) the “earliest retirement age.” “Earliest retirement age” means the earlier of:

1. The date on which the participant is entitled to a distribution under the plan; or
2. The later of:
   a. The date the participant attains age 50; or
   b. The earliest date on which the participant could begin receiving benefits under the plan if the participant separated from service.

**Survivor Benefits**

Survivor benefits are essential to protect the interest of
an alternate payee when dividing most defined benefit plans. The alternate payee usually should be named as the survivor beneficiary for purposes of any pre-retirement death benefits, at least to the extent of the former spouse’s interest in the participant’s retirement benefit.

The alternate payee should almost never be named as the survivor beneficiary for purposes of the post-retirement death benefits in a case where the participant’s lifetime benefits are being divided pursuant to a separate interest QDRO. If the participant has already retired and had commenced receiving retirement benefits, most plans will not allow a change in survivor benefit designation, nor allow a new survivor benefit to be created, nor allow an existing survivor benefit to be cancelled.

Federal pensions (military, FERS and CSRS, and some others) always require a survivor benefit award to protect the alternate payee. In the absence of a survivor benefit award to the alternate payee, the alternate payee’s benefits will cease when the military member or federal employee dies.

**Conclusion**

The most important thing is to resolve the terms of the retirement benefit division at the time you resolve the other issues in the case. If you try the case and do not adjudicate the terms of the division, you may find yourself back in court. Make sure the terms of the retirement benefit division are is-diction over a party if enough time elapses, requiring the dis-solutions spelled out in the dissolution judgment or the marital settlement agreement. Be sure that survivor benefits are ad-dressed as necessary. The QDRO is the technical instrument that effects the division of benefits, but the terms of the mari-tal settlement agreement or the dissolution judgment govern the preparation of the QDRO, and it pays to be precise. If you decide to consult an attorney with expertise in preparing QDROS, engage the attorney early in the case so that you will have the full benefit of the attorney’s counsel.

**Daniel M. Ricks**  
**Kennedy Watts Arellano & Ricks**

*Thanks to Ann Mercer for her assistance with the original version of this article.*
PERS BENEFICIARY DESIGNATIONS

(Originally published in the February 2006 issue of In Brief; updated February 2013)

A little-known section in the Oregon Revised Statutes relating to the distribution of a PERS member’s benefits on the pre-retirement death of the PERS member may surprise you. Assume these facts: Your client, a PERS member, was married to a man who had three children from a previous marriage. Your client has no natural-born or adopted children. The husband dies in 2004, survived by your client and all three of his children.

Your client dies in 2005 before retiring under the PERS system. At the time of your client’s death, her PERS designated beneficiary was her husband. To whom does PERS distribute the funds?

Pursuant to ORS 238.390(5), on the pre-retirement death of your client, PERS will distribute the assets to the personal representative of the deceased husband’s estate. If the husband died intestate, under ORS 112.025(2), half of the PERS account returns to the wife’s estate; the rest will be distributed equally among the husband’s three children. This result—distribution of retirement benefits to the estate of a deceased spouse—contrary to what most estate planners would expect, that is, distribution of assets to the member’s estate. The legislative history of ORS 238.390(5) reveals nothing to indicate that this result was not intended by the Legislature.

Bottom line: If you have a client who participates in the PERS system, and the designated beneficiary predeceases your client, the client should consider changing the beneficiary designation to avoid an unintended result.

Jay Richardson
Buckley LeChevallier, PC

June Wiyrick Flores
Ater Wynne LLP

Our thanks to Daniel Ricks, of Kennedy, Watts, Arellano, & Ricks, LLP, for his assistance with this article.

In the February 2006 edition of In Brief, we informed you about a surprising provision in the Oregon Revised Statutes involving PERS participants and beneficiaries. That provision remains in the current law and is worth reviewing again.

Assume the following: your client is an unretired PERS participant and married to a man with three children from a prior marriage. Your client and her husband have a child together. Your client’s husband dies and, a year later, your client dies. At the time of your client’s death, her husband remained the designated beneficiary of her PERS retirement benefits.

Your client did not change her PERS beneficiary designation before her death. Therefore, ORS 238.390(5) was not applicable.

ORS 238.390(5) does not allow for any investigation into what your client intended regarding the beneficiary of her PERS benefits.

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Therefore, lawyers who have PERS participants or beneficiaries as clients will want to review how ORS 238.390(5) will affect the distribution of PERS benefits upon the death of the PERS participant. Moreover, it is recommended that the lawyer review all of the death benefit provisions of ORS 238.390.

Jay Richardson
Buckley LeChevallier, PC
February 2013
Dividing PERS Retirement Benefits - There Is No “One Size Fits All” Approach Anymore!!

by Clark B. Williams

Introduction

Until recently it was easy to divide PERS benefits in divorce. Before the 2003 Oregon Legislature overhauled the PERS system, it was most common, and also almost always most fair, to simply divide the marital portion of a PERS account in half, and for the “alternate payee” to have a separate account. This is the so-called “up front division method.” This division method also serves to best disentangle the parties. This method has been allowed by Oregon law, ORS 238.465, since 1993.

But since 2003 and with the advent of the Individual Account Plan (IAP) and the Oregon Public Service Retirement Plan (OPSRP), dividing PERS benefits is much more complicated.

First, it is important to note that every PERS member (except a member who terminated employment prior to 2004) now has an IAP account. The IAP account is derived from a contribution by the government employer equal to 6% of the member’s compensation each year, starting in 2004, plus earnings on those contributions each year. Many PERS members now have IAP balances exceeding $30,000. The IAP is in addition to the member’s benefits in Tier One, Tier Two or OPSRP. So every PERS member has two benefits to divide, potentially, in a divorce. The IAP is a different system, and the division is handled separately.

Second, new PERS regulations effective January 1, 2011 must be followed. In particular, new template forms must now be attached to any divorce judgment or supplemental order dividing PERS benefits. The template forms do not replace the need for a judgment or court order dividing benefits specifically in compliance with ORS 238.465. Rather, these template forms are in addition to the judgment or court order and must be completed and attached thereto as exhibits. Further, if only one of a member’s two PERS benefits are being divided (e.g., a member’s Tier One account is being divided but the member is keeping the IAP account), the judgment or order must still incorporate a PERS template form specifying that the benefit being retained is “free and clear” of any claim by the former spouse. So in every case at least two of these forms must be attached to the judgement or court order, one for the IAP and one for the Tier One, Tier Two or OPSRP benefit, as the case may be. PERS will now reject any judgment or order that does not include these forms.

Finally, no longer is it universally true that the “up front division method” is the best, or even fairest, way to divide PERS benefits. Depending on which party you represent, and whether

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1 Special “thanks” go to Paul Saucy, Esq. and to Peter Ungern, Manager of the PERS Specialty Services Section, for their contributions in the writing of this article.

2 The forms can be found at http://www.oregon.gov/PERS/MEM/docs/forms/046fs.pdf?ga=t
the member is “Tier One” or “Tier Two,” your client may be better served to divide PERS benefits at retirement using the “time rule.” That dichotomy will be the focus of the remainder of this article.

This is the first of two articles addressing how best to divide PERS benefits in view of these changes. This first article will focus on dividing Tier One and Tier Two benefits. The second article, to be published in the June edition of the Family Law Newsletter, will focus on dividing IAP accounts and OPSRP benefits.

Understanding Tier One and Tier Two

To best represent your client in dividing PERS benefits, it is important first to understand how the benefits are earned and calculated, and when and how they are paid. I will discuss Tier One and Tier Two separately, because they are very different. In fact, depending on who you represent, the best division method for your client is often opposite for Tier One vs. Tier Two!

Tier One Benefits.

Any employee first employed in a PERS-covered position prior to January 1, 1996 is in Tier One. Tier One employees will receive a lifetime monthly pension benefit (or the lump sum equivalent) equal to the largest amount produced these three alternate methods:

1. **Full Formula.** 1.67% x years of service x FAS (“final average salary”). So, for example, a school teacher who retires with 30 years of service and a final average salary of $5,000/month will receive a benefit of 1.67% x 30 years x $5,000 = $2,500/month under this method.

2. **Money Match.** The member’s PERS account, doubled by the “money match” and then multiplied by an annuity factor that is based on the life expectancy of the member. For a member at age 58, the annuity factor is $7.96/$1,000. Therefore,

3 The “time rule” is also referred to as the “coverture fraction.” It is an arithmetic way of determining each spouse’s interest in the plan benefit by separating out the premarital or postmarital portion of the benefit by multiplying the marital share (usually 50%) by a fraction. The numerator of the fraction is usually the number of years during the marriage that the employed spouse earned credit for service under the retirement plan. The denominator is usually the total years of service under the retirement plan to the point of retirement or termination of employment. For example, 10 years of marriage divided by 20 years of service up to the point of retirement (the last 10 years being postdivorce) multiplied by the marital share (usually 50%) equals the former spouse’s share of the benefit. See Richardson, 307 Or 370, 378–379, 769 P2d 179 (1989) This formula has the effect of treating each year of service during the member’s career as having equal credit in determining the former spouse’s share, even though the benefits may not have accrued uniformly during the employee’s career. That is why the Court of Appeals in Kiser, ___ Or.App. ___ (2001) referred to the “time rule” as the “straight line method.”

4 2.0% for “police or fire” employees
for example, if the school teacher in the above example has an account balance of $175,000 at age 58 and then retires, the teacher’s retirement under this option is $175,000 x 2 x $7.96/$1,000 = $2,786/month.

3. **Formula Plus Annuity.** For members participating in PERS since before August 21, 1981, a third formula applies which is a combination of the first two. The formula is: 1% x years of service x FAS plus the account balance (not doubled) times the annuity factor. In the school teacher example above, the formula would be 1% x 30 years x $5,000 plus $175,000 x $7.96/$1,000 = $2,893/month. In situations where the first two formulas yield a result that is close to each other (as in this example), then this third method (for those in the system before August 21, 1981) yields the best result.

The Full Formula method is a traditional defined benefit formula. The Money Match method is a defined contribution formula. The Formula Plus Annuity method is a blend of both the first two. So whether PERS is behaving as a defined benefit plan or a defined contribution plan is entirely dependent on the prevailing method. This is important to recognize.

**Other Factors.** The following additional factors are important for understanding PERS Tier One benefits:

A. A member’s PERS Tier One account balance is the cumulative total of an annual contribution equal to 6% of the member’s compensation through 2003 (after which time these contributions have been made to the member’s IAP account) plus earnings on that balance each year.\(^5\)

B. The earnings added each year are determined by the PERS Board. Each member has a “regular account” and, if the member chooses, also a “variable account.” The “regular account” is invested more conservatively, and very importantly it has a minimum earnings guarantee of 8% per year.\(^6\) Again, the account balance at any time represents only half (or less) of the total value of the account because the account will be “matched” by an equivalent employer contribution at retirement.

C. The 1990’s produced very strong earnings for PERS accounts. For the five years 1995 - 1999, inclusive, PERS regular accounts earned an average of 15.5% *per annum* and variable accounts earned 26% *per annum*. The result was that the accounts of nearly all PERS members ballooned to the point that the Money Match method prevailed over the Full Formula method nearly every time.

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\(^5\) Originally the contribution came from the member’s after-tax salary (hence, called the “employee contribution”) but since the early 1980’s and as a result of collective bargaining most employee contributions are “picked up” by the government-employers.

\(^6\) The 2003 Oregon Legislature tried to repeal this 8% guarantee, prospectively, but the Oregon Supreme Court ruled that it was constitutionally protected.
According to “PERS By The Numbers,” nearly 90% of the retirees between 1999 and 2004 retired under the Money Match formula, and with an average retirement income of over 90% of final average salary, or FAS.

D. Years of Service after 2003 still count under the Full Service formula, even though no new contributions are being made to member Tier One accounts. The Money Match method continues to predominate. According to PERS by the Numbers, over 60% of retirees in 2007 (the latest year available) retired under the Money Match formula even though no new contributions have been made to Tier One accounts since 2003. However, that trend is reversing. Tier One members who are still many years from retirement may eventually retire under the Full Service formula, particularly those who have significant salary increases after 2003.

E. In an “up front division,” PERS establishes a separate “alternate payee’s” account for the portion of the Tier One account awarded to the former spouse. Because of this, the alternate payee’s benefits are limited to the Money Match method. This is true even if the member eventually retires under the Full Formula method. This is very important to understand. Also, the former spouse’s account is invested strictly in the “regular” account, even if derived partially from the member’s “variable” account.

F. Tier One members can retire at age 58, or at any age with 30 years of service. Tier One members can retire as early as age 55 with a reduction in benefits for early commencement. Benefits are measured in monthly payments for the life of the member (Option 1). The member can elect survivorship options (Options 2, 2A, 3 or 3A) with another spouse or person with a lower actuarially determined monthly benefit, and/or a partial or total lump sum benefit.

G. All monthly benefits are increased annually by the increase each year in the Consumer Price Index (“CPI”), but limited to 2% per year.

Implications for Dividing Tier One Benefits.

Based on the foregoing, it is apparent that a Tier One Member’s best retirement accumulation years are those already in the rear view mirror. In fact, in many cases the

7 http://www.oregon.gov/PERS/docs/general_information/bythenumbers.pdf?ga=t
8 Id., at p. 7
9 Age 55 for “police or fire” employees
10 Age 50 for “police or fire” employees
member’s account balance is still so large, relative to years of service and salary, that the Full Formula method will never catch the Money Match method before retirement. In those cases, the additional years of service from now until retirement count for nothing in terms of Tier One benefits! The member will receive the same benefit if he or she quits now than if the member continues to work until retirement. This is a common phenomena for career Tier One members now in their 50's.

For example, here is a “live case” on my desk right now (I will round off the dates and numbers). Husband has been a Tier One PERS member since 1983, now age 51, with seven years to projected retirement at age 58 in 2018. He earns $75,000/year and has a Tier One account balance of $215,000 as of December 31, 2010. The PERS on-line estimator\(^{11}\) projects that Husband will retire at age 58 with an account balance of $368,000, to be doubled by the Money Match to $736,000, and which will annuitize at $5,845/month. Also according to the estimator, even if Husband’s salary increases to $100,000/year by his retirement in 2018, the Full Formula method would yield only $4,772/month. So the Money Match will be the prevailing formula for him even seven years from now. Husband’s salary would have to increase to at least $123,000/year by his retirement for the Full Formula method to overtake the Money Match method, which is unlikely in this economy. So unless that happens, Husband’s continued service from now until retirement does not increase his final Tier One benefit by one dime. And remember, no contributions have been added to Husband’s Tier One account since 2003. This means that for his 35-year career, from 1983 to 2018, the entirety of his Tier One benefit was earned in the first 20 years of his career, from 1983 thru 2003. His last 15 years from 2004 thru 2018 count for nothing in terms of Tier One benefits!

The divorce will occur in 2011, and I represent Wife. So it is in her benefit, clearly, to use the “up front” 50-50 division. This will give her half of all Husband’s benefits at his retirement. And I can argue, easily, that this is appropriate under these circumstances. Her half of the account balance at retirement will be $368,000, and she would then have her own payment options including lump sum. And this would be in addition to half of Husband’s current IAP account (now about $28,000, so her half is an additional $14,000).

But if I represent the Husband, then I would explain to him that to use an “up front” division is to give away half of the best years. I would explain that it would be better to use the “time rule” to keep the account intact from now until retirement and then divide it on a prorated basis. Under the time rule, wife’s share of the total benefit would be $736,000 x 28 years to date ÷ 35 years total service at retirement x 50% = $294,400. This represents a savings for Husband of $73,600 at retirement. Wife would get 40% of the total benefit, not 50%. The legal basis for this approach is the Kiser case\(^{12}\), which holds that the “time rule” applies to all defined benefit plans. And in the first instance, PERS is a defined benefit plan. The counter-argument, however, is that in this case where the Money Match is the prevailing method, PERS is performing as a defined contribution plan. And therefore it is appropriate to divide the account in half now, as with all defined contribution plans.

\(^{11}\) http://apps.pers.state.or.us/benefitestimator/bencalc_step1_start.asp

\(^{12}\) Cited in footnote 3.
Therefore, when representing a Tier One member, particularly one who is late in his or her career, consider carefully whether it is better to argue for the use of the “time rule” to divide the account balance at retirement, rather than at the time of divorce, so that the member keeps a larger share of his or her eventual Tier One benefit. This is true even in most cases where the Full Formula will catch up to the Money Match in the years immediately before retirement, since the time rule will still normally yield better result for the member. But to be sure, it is best to run the actual numbers of each case thru the PERS on-line estimator.

And if you use the time rule to divide at retirement, then the judgment or supplemental order should address what happens on either death before retirement. And at retirement, if the opposing party is much older or has a shortened life expectancy, then you might consider also having the judgment or order mandate an Option 2 (100% survivor) benefit and to split the payments rather than to split the account. That way, on the first death then the survivor (hopefully your client) can then receive both halves of the benefit for the rest of his or her life.

Tier Two Benefits.

A PERS member is in Tier Two if he or she was first employed between January 1, 1996 and August 28, 2003. Employees first hired after August 29, 2003 are in OPSRP. The benefit structure for Tier Two employees is similar to Tier One. But there are enough differences to turn the typical approach for dividing Tier Two benefits 180 degrees from that for Tier One, as explained below.

These are the basic differences between Tier One and Tier Two

1. The normal retirement age is 60, not 58, for general service (not police or fire) employees.

2. There is no 8% interest guarantee as with Tier One regular accounts. Therefore, for example, in 2008 Tier Two accounts lost over 27% while Tier One regular accounts gained 8%.

3. The retirement formulas are just the Full Formula method and the Money Match method. There is no Formula Plus Annuity method.

Contributions to Tier Two accounts were made, at most, for only eight years, from 1996 thru 2003. Contributions to Tier Two accounts were frozen after 2003, just as for Tier One accounts, with the 6% contributions after 2004 being redirected to new IAP accounts for each Tier Two member. And because of relatively poor earnings results for Tier Two accounts in the last decade, Tier Two accounts are still relatively small.

On the other hand, as with Tier One, continued serviced by Tier Two employees still count under the Full Formula method, which is the same method as for Tier One. As a result, with the passage of time since 2003, Tier Two retirements are increasingly under the Full
Formula method, and that trend will only get stronger with time.

*Implications for Dividing Tier Two Benefits.*

Tier Two employees are often younger, with a longer horizon to retirement. In most cases, the account balance represents only a small fraction of the total retirement likely to be paid to the Tier Two member. An “up front” division limits the alternate payee to the less valuable Money Match method, as with Tier One. And so using an “up front” division method tends to short-change the alternate payee and to preserve the more valuable Full Formula benefits for the member.

I will illustrate with another “live” case on my desk today. Husband is the Tier Two member, having entered PERS on April 1, 2001. His Tier Two account balance was only $13,000 as of December 31, 2009. It is small because it represents contributions just for nine months in 2001 and for the years 2002 and 2003. Again, no new contributions have been made to this account since 2003. Yet as of 2011, Husband has ten years of service under the Full Formula method. Husband is already age 58 and may retire soon. His salary is approximately $55,000 per year. The parties are divorcing now. All Tier Two service is marital.

According to the PERS on-line estimator, were Husband to retire now, the Full Formula method would prevail and award husband a monthly pension of $714/month. But the Money Match method would produce only $224/month. In other words, the value of the account balance is only one-third of the value of the likely benefit based on salary and years of service.

I represent Wife in this case. If I were to divide the account in half, I would limit Wife to an account that would produce only $112/month to her. And Husband would retain the other $602/month. Therefore, I am proposing to use the “time rule” to divide the benefits. And appropriately so, since PERS in this instance is performing as a defined benefit plan. This way, I will insure that wife gets the equivalent of half of the total benefit, or $357/month. This is an additional $245/month to her for the rest of her life, with CPI increases. And she is just 58 herself, so this could mean a lot to her over the years.

Further, because of Husband’s poor health habits and poor genetics, I am drafting the order to mandate that the entire benefit be paid in the form of Option 2, a joint and 100% survivor annuity, which will yield a lower total payment of $632/month. Payments will be split equally for as long as both live. But if Husband dies first as expected, then Wife will receive both halves thereafter for as long as she lives. And in this case, the extra PERS benefits at that time will partially compensate her for loss of spousal support due to his death.

This approach is 180 degrees from the approach taken for Wife in the Tier One example, above.

*Conclusion*
No longer is it sufficient to blindly divide PERS Tier One and Tier Two benefits “up front” at divorce. Practitioners should take time to understand the particular PERS benefits in each case, whether Tier One or Tier Two and the account balances and service credits earned, and to estimate whether the Full Formula or the Money Match method will ultimately prevail at retirement. Practitioners may also need to consider the ages of each party, their likely retirement dates, their relative health and the likelihood that one will survive the other. A loose rule of thumb when representing the alternate payee is to recommend an “up front” division if member is Tier One and a “time rule” division if the member is Tier Two. And the rule of thumb is exactly the reverse when representing the member. But each case should be evaluated on its own merits.

*This article was published in the OSB Family Law Newsletter, April 2011. Reprinted with permission.*
Dividing PERS Benefits - Part II

by Clark B. Williams

This is the second in a two-part series on dividing PERS benefits in a divorce. The first article, published in the April 2011 edition of this newsletter, examined the issues in dividing PERS Tier One and Tier Two benefits. This article will examine the issues in dividing the Individual Account Plan (IAP) and the new Oregon Public Service Retirement Plan (OPSRP).

Every PERS member has two benefits to divide, potentially, in a divorce. The first is the member’s Tier One, Tier Two or OPSRP benefit, as the case may be. The other benefit is the IAP account.

Understanding the Individual Account Plan (IAP)

Every active PERS member (except a member who terminated employment prior to 2004) now has an IAP account. The IAP account is derived from an “employee” contribution equal to 6% of the member’s compensation each year, starting in 2004, plus earnings on those contributions each year. Approximately 70% of PERS members have their 6% employee contributions “picked up” by the governmental employer, so that it is actually paid by the employer and not the employee. For the remaining members, the contribution is a mandatory after-tax deduction from their net paychecks. Many PERS members now have IAP balances exceeding $30,000. The IAP is a different system from Tier One, Tier Two and OPSRP, and the division is handled separately.

The IAP accounts are like 401(k) accounts and other defined contribution plan accounts. They represent “cash in the bank,” so to speak. The value of an IAP account is its balance at any time. This is unlike Tier One accounts and Tier Two accounts, which are worth much more (at least twice, and often even more) than the balance shown on the account statement. This distinction can be lost when looking at a member’s “combined annual statement.” The combined statement will show both the Tier One or Tier Two balance and the IAP balance. The temptation is to add the two balances together to determine total value of the member’s PERS benefits. But that would be mistake - - the two values shown on the combined statement are apples and

1 Special “thanks” go to Paul Saucy, Esq. and to Peter Ungern, Manager of the PERS Specialty Services Section, for their contributions in the writing of this article.

2 Tier One applies to members first employed in a PERS-covered position prior to 1996. Tier Two applies to members first employed between January 1, 1996 and August 28, 2003. OPSRP applies to members first employed on or after August 29, 2003.

The IAP is a giant pooled fund for all participants statewide, and the investments are managed by the Oregon Investment Council. The Council consists of a six-member board made up of four gubernatorial appointees, the State Treasurer and the PERS Executive Director. Because the IAP is managed as a giant single pooled fund, individual members of the IAP cannot self-direct their investments. Everyone in the IAP gets the same rate of return. In 2010, the IAP had a net investment return of 12.13%.

The IAP is valued as a whole, and individual account balances determined, just once per year as of each December 31. A member’s account balance at each December 31 is the sum of the balance as of the prior December 31, plus the investment earnings (less losses) on that balance for the year, plus a new contribution equal to 6% of the member’s compensation for that year. Because this balance is determined only once per year, it is impossible to precisely determine a member’s balance as of any given date during the year. In other words, the IAP is not “daily valued” as are many 401(k) and other defined contribution plans.

IAP accounts are 100% vested at all times. They are fully portable. A member can apply to receive his or her IAP account generally within 90 days after termination of employment. Like any other distribution from a defined contribution plan, the distribution of a member’s IAP account will be subject to income taxes and a potential 10% early distribution penalty for participants under age 59 ½, unless the distribution is rolled to an IRA account. At retirement, the member can elect a lump sum distribution or an IRA rollover, or installments over a 5, 10, 15 or 20 year period. The balance remaining at the member’s death will pass to the member’s designated beneficiary.

Implications for Dividing IAP Accounts.

IAP accounts are easily divided in a divorce. However, the fact that IAP accounts are valued only as of December 31 each year means that IAP accounts can be divided only as of December 31 of any given year. Any order or judgment purporting to divide an IAP account as of a date other than December 31 (e.g., a judgment that purports to divide the account “as of the date of this judgment”) will be ineffective and will be rejected by PERS (unless, in fact, the date of the judgment is December 31).

So, to effectively divide an IAP account as of any other date will require doing some math by hand. You will need to know the prior December 31 value, then add the current year’s 6% contribution to the date of the division, then multiply the sum by the appropriate percentage (typically 50%) and award that amount as a dollar figure as of the prior December 31. So, for example, if a member’s account is to be divided evenly as of June 1, 2011 and the member had

4 See the April 2011 Family Law Newsletter for an explanation of Tier One and Tier Two benefits, and in particular how the account balance is only a fraction of the total value.

5 The applicable regulation for dividing IAP accounts is OAR 459-045-0014.
an IAP account of $25,000 as of December 31, 2010 and has a monthly salary of $3,500 per month, then the appropriate award will be: \[ \$25,000 + (\$3,500/\text{month} \times 5 \text{ months} \times 6\%) \times 50\% = \$13,025 \]. The judgment or order would award that amount as of December 31, 2010.\textsuperscript{6}

This method presents challenges early in each calendar year, before the annual account statements are available for the prior year (e.g., the 2010 combined statements came out the second week of May 2011). However, an estimated IAP earnings rate for each year is usually available on the PERS website\textsuperscript{7} by the end of January, and is normally reliable to within a few hundredths of a percent. So, for example, an equal IAP division to be done as of a judgment dated March 1, 2012 will have to be manually calculated by starting with the December 31, 2010 IAP balance, adding the estimated earnings for 2011 based on estimated rate of return posted on the PERS website, adding the 6% contribution for all of 2011 and for January and February 2012, dividing by two and awarding that amount as a dollar sum as of December 31, 2011.

Once awarded, PERS will segregate the alternate payee’s share into a new IAP account in the alternate payee’s name as of the applicable December 31. The account will also be credited with its share of IAP earnings (less losses) thereafter. The alternate payee can immediately access the account, even though the member cannot if still employed. Any amounts taken directly are subject to tax withholding, as with any qualified plan. Also, the alternate payee’s account can be rolled tax free into an IRA or other qualified plan. Or the alternate payee can leave the account in the IAP as long as he or she wishes.

\textit{Oregon Public Service Retirement Plan (OPSRP)}

OPSRP is a pure defined benefit plan, very similar to private sector defined benefit plans. There is no “account” and no “money match” formula. No lump sum payments are available. Rather, OPSRP provides retirement income for the life of the member and, potentially, for the life of a beneficiary (including a former spouse). Think of it like Social Security.

The OPSRP formula is simple: \(1.5\%\times \text{years of service} \times \text{“final average salary.”}\).\textsuperscript{9} Normal retirement is age 65. A member can retire as early as 55 with an actuarially reduced benefit to reflect that is starting early and will be paid out for a longer time. The reduction in the monthly payment may be as much as 60% to start at age 55 instead of age 65.

\textsuperscript{6} In this example, one might think to be clever by drafting the judgment or order to award “50% of the member’s account as of December 31, 2010 plus $525,” with the $525 being half of the 6% contribution for the first five months of 2011. This would save having to actually know the December 31, 2010 balance and to do the math for a total gross dollar award. But PERS regulations provide that the IAP division must be expressed \textit{either} a percentage or as a dollar amount, and cannot be a combination of both a percentage and a dollar amount.

\textsuperscript{7} See \url{http://www.oregon.gov/PERS/section/financial_reports/financials.html}

\textsuperscript{8} (Age 60 for police and fire employees) This compares to age 60 for Tier Two and age 58 for Tier One (age 50 for police and fire employees).

\textsuperscript{9} (1.8% for police and fire employees.) This compares to 1.67% for Tier One and Tier Two (2% for police and fire employees).
At retirement, five payment options are available:

- the Single Life Option which pays for the life of the member only (like Option 1 under Tier One and Tier Two);
- a Full Survivorship Option which pays for the life of the member and then for the life of a designated beneficiary if the beneficiary survives the member (like Option 2);
- a Full-Survivorship Increase Option which pays for the lives of the member and a designated beneficiary but which increases to a Single Life Option if the beneficiary is the first to die (like the Option 2A “pop-up”);
- a Half Survivorship Option which pays for the life of the member and then 50% thereof for the life of a designated beneficiary if the beneficiary survives the member (like Option 3); and
- a Half Survivorship Increase Option which pays for the life of the member and then 50% for the life of a designated beneficiary if the beneficiary survives but which increases to a Single Life Option if the beneficiary is the first to die (like the Option 3A “pop up”).

The largest monthly amount is paid under the Single Life Option. The other payment options produce slightly smaller payments because they are paid over two lifetimes. A married member is required to elect the Half Survivorship Option unless the spouse of the member, at retirement, consents to an alternate form of payment. All benefits, once payable, will be subject to annual cost of living increases not to exceed 2% per year.

If a member dies before retirement, then only 50% of the accrued benefit is available to be provided to a surviving spouse, former spouse or other beneficiary. The other 50% reverts to the PERS system. This is important to recognize.

**Implications for Dividing OPSRP Benefits.**

As stated earlier, OPSRP applies only to government employees first employed by a PERS covered employer on or after August 29, 2003. And it takes five years of service to vest in OPSRP at all. So only recently have OPSRP benefits become sufficiently valuable to merit being divided instead of being valued and offset in the overall divorce settlement.

OPSRP represents retirement income often decades away and is not immediately available in cash. And for this reason it is still preferable where possible to allow the member to keep the OPSRP benefit and to offset that value against other assets being awarded to the spouse. The OPSRP benefit should be valued actuarially to see if an offset is practicable.

In my experience, particularly for younger members, the value of the OPSRP may be less

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10 The applicable regulation for dividing OPSRP benefits is OAR 459-045-0012.
even than the value of the IAP. So in those cases, it is possible (and usually preferable) to evenly divide a member’s combined PERS benefits by awarding all of the OPSRP to the member, then an equal value of the IAP to the spouse, and to split the balance of the IAP. This will require a valuation of the OPSRP. This allows the spouse to maximize current cash while preserving the long-term benefit for the member, and it serves to best disentangle the parties. I recommend this approach for younger couples.

For those close to retirement, particularly if the alternate payee can wait until the member’s actual retirement to receive his or her share, then it may make better sense to divide the OPSRP at retirement. The alternate payee may prefer a retirement income instead of a cash settlement. And in that situation, the appropriate method to divide the OPSRP is the “time rule” as with any defined benefit plan. Under ORS 238.465, the alternate payee can elect to commence receipt of his or her share of the benefits at any time after the member’s earliest retirement date, even if the member is still working beyond that date.

Under OPSRP, each party is allowed to elect their own benefits separately for their own lifetimes. This is the so-called “separate interest” approach to dividing the benefits. The judgment or order can provide that the alternate payee may elect to commence his or her share at any time on or after the member’s earliest retirement date under OPSRP. The alternate payee must elect to receive benefits, however, no later than when the member does. In a separate interest division, the alternate payee’s benefits will be paid to as a Single Life Option for the alternate payee’s lifetime in an amount which is re-annuitized by PERS using an appropriate actuarial equivalency factor based on the alternate payee’s life expectancy. So the alternate payee will receive life income independent of the member and regardless if whether the member survives thereafter. This means that, unlike Tier One and Tier Two, under OPSRP we don’t need to worry about post-retirement survivor benefits to protect the income stream to the alternate payee if the member dies first. That helps in disentangling the parties (particularly if they are relatively young).

On the other hand, if the parties are close to retirement it might be appropriate to hold the benefits together, mandate a survivorship election (e.g., the Full Survivorship Option), and to split the payments for as long as both parties live until the first death, and with the survivor to receive both halves thereafter for the survivor’s lifetime. This is the so-called “shared payment” approach to dividing benefits. This approach allows the alternate payee to capture the member’s

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11 The “time rule” is also referred to as the “coverture fraction.” It is an arithmetic way of determining each spouse’s interest in the plan benefit by separating out the premarital or postmarital portion of the benefit by multiplying the marital share (usually 50%) by a fraction. The numerator of the fraction is usually the number of years and months during the marriage that the employed spouse earned credit for service under the retirement plan. The denominator is usually the total years and months of service under the retirement plan to the point of retirement or termination of employment. See Richardson, 307 Or 370, 378–379, 769 P2d 179 (1989). This formula has the effect of treating each year of service during the member’s career as having equal credit in determining the former spouse’s share, even though the benefits may not have accrued uniformly during the employee’s career. That is why the Court of Appeals in Kiser, 176 Or.App. 627 (2001) referred to the “time rule” as the “straight line method.”

12 Age 55 for general service workers, and age 53 for police and fire employees with 25 years of service.
income stream, too, at the member’s death if the alternate payee is the survivor. This approach most closely resembles how the benefits would be paid if the parties had not divorced, and the alternate payee may want to argue that he or she is entitled to preserve that expectation. And this approach may be particularly important to the alternate payee if it is likely that the alternate payee will survive the member for a number of years. For example, if the parties are close to retirement and the OPSRP benefit will be $2,000 per month, then rather than a “separate interest” approach allowing each electing $1,000 per month for as long as each lives, it might be better to mandate a Full Survivorship Option so that, perhaps, benefits are paid at $1,800 per month for as long as either party lives. The payments would be split, $900/month to each as long as both live. But then on the member’s death, the alternate payee would continue to receive the full $1,800/month as long as the alternate payee lives thereafter. Likewise, if the member is the survivor, the member will receive the $1,800/month for as long as the member lives thereafter.

PERS allows only one survivor beneficiary at retirement. So if the member expects to remarry before retirement and wishes to name the new spouse to receive survivor benefits, then the member will likely object to the “shared payment” approach and insist on a “separate interest” approach so that the member can provide survivor benefits to the new beneficiary.

If the member is already retired at the time of divorce, then the retirement election “is in concrete” and the best that can be done is to split the payments as they come out. If the member retired with a Single Life Option, then there is no way to protect the alternate payee’s income stream after the member dies. The parties can split the payments for as long as the member lives, but then benefits will stop to both parties when the member dies. If the member retired with a survivorship option, then the judgment or order should expressly preserve the survivorship benefits for the alternate payee. Otherwise, after the divorce the member would be allowed to designate a new beneficiary for the survivor benefits or, if an “increase option” was elected then to “pop up” to the Single Life Option, either of which would deprive the alternate payee of survivor benefits after the member’s death. Also, in all circumstances, the judgment or order should address the possibility that the alternate payee will be the first to die, and what becomes of alternate payee’s share thereafter for as long as the member then lives. The alternate payee can be allowed to designate a beneficiary, or the benefits can revert to the member, as the judgment or order provides.

Similar to private sector plans, the member has to survive until retirement for a full benefit to be payable. For an OPSRP member who dies prior to retirement, only 50% of the benefit is available to the member’s beneficiary (including an alternate payee), and the other 50% is forfeited. So to protect the alternate payee’s expectancy, it is appropriate for the judgment or order to provide that if member dies prior to retirement, the alternate payee be named as survivor beneficiary as to 100% of the marital portion (not just 50%) so that the alternate payee will get the equivalent of a 50% benefit if member had survived to retirement. For example, if an OPSRP member retires with income of $1,600 per month having been previously divorced and if marital share by the time rule fraction is $1,000, then the alternate payee would expect to receive 50% of that or $800 per month. But if the member dies even one month before retirement (and if the alternate payee had not already commenced benefits separately), then only $800 is payable and the other $800/month is simply lost. So to protect the alternate payee, it is necessary to award the
alternate payee pre-retirement survivor benefits equal to 100% of the marital portion, not just 50%, so that the alternate payee still to receive $500/month of the $800/month available. Otherwise, the alternate payee’s share is reduced to $250/month by virtue of the member’s death after divorce and before retirement. Even if the alternate payee receives $500/month, that still leaves the other $300/month available for the member’s new beneficiary, which represents the survivor benefits attributable to service after the divorce.

Reciprocally, under OPSRP, if the alternate payee dies before benefits commence to either party, then the alternate payee gets nothing and all benefits revert back to the member. The alternate payee has to survive at least to the member’s earliest retirement age to receive any OPSRP benefits.

New Template Forms to Attach in Every Instance

Finally, as stated in the first article, and pursuant to new PERS regulations effective January 1, 2011, new template forms must now be attached to any divorce judgment or supplemental order dividing PERS benefits.13 The template forms do not replace the need for a judgment or court order dividing benefits specifically in compliance with ORS 238.465. Rather, these template forms are in addition to the judgment or court order and must be completed and attached thereto as exhibits. Further, if only one of a member’s two PERS benefits are being divided (e.g., a member’s IAP account is being divided but the member is keeping the OPSRP benefit), the judgment or order must still incorporate a PERS template form specifying that the benefit being retained is “free and clear” of any claim by the former spouse. So in every case at least two of these forms must be attached to the judgement or court order, one for the IAP and one for the Tier One, Tier Two or OPSRP benefit, as the case may be. And further, if the member is under restrictions or mandates as to beneficiary designations, additional PERS forms are required to be attached to identify those restrictions or mandates. PERS will now reject any judgment or order that does not include these forms.

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13 The forms can be found at http://www.oregon.gov/PERS/MEM/docs/forms/046fs.pdf?ga=t
Dividing PERS Benefits – A Postscript

By Clark B. Williams

**P.S. to April 2011 Article - PERS will now allow a “separate interest” payment to an Alternate Payee in dividing Tier One and Tier Two benefits.**

As discussed in my April 2011 article, a trend is underway for Tier One and Tier Two benefits to be paid, increasingly so, under the “Full Formula” method rather than the “Money Match” method. The Full Formula is a function of the member’s years of service and final salary, while the Money Match is solely dependent on the member’s account balance. The member’s final retirement will be based on the method that produces the largest benefit. This shift toward the Full Formula is because PERS stopped contributing to Tier One and Tier Two accounts after 2003, yet service after 2003 still counts under the Full Formula method.

Therefore, to best protect the former spouse (“alternate payee”) it may be best to divide the retirement benefit at “back end” when the member retires or when the alternate payee elects to commence benefits after the member’s earliest retirement date, and to calculate the division at that time on the “time rule” (a.k.a. the “coverture fraction”). This is opposed to an “up front” division of the account balance, which then limits the alternate payee to the Money Match method.

And now the news: PERS will now allow a "separate interest" approach to dividing Tier One or Tier Two, whereby PERS will pay alternate payee’s share in the form of a separate annuity for his/her own lifetime, independent of the election chosen by the member. This is welcome news and will help the goal of disentangling the parties.

Specifically, in cases where the parties are divorcing and it is expected that the member's benefit will ultimately be paid on the Full Formula, the judgment or court order can provide that the alternate payee's share will be divided and determined at the time of the member’s retirement (or at the alternate payee's election at or after the member's earliest retirement date) based on the time rule, and that PERS will then actuarially recalculate the alternate payee's share of member’s benefit as a single life annuity for the alternate payee's own lifetime. This allows the parties and the court to avoid having to mandate a survivor benefit form (Option 2, 2A, 3 or 3A) at the time of the member’s retirement in order to assure a lifetime income stream to the alternate payee. And it frees the member to name a new spouse or other beneficiary to receive survivor benefits at the time of his/her retirement.
An illustration may be helpful. These facts are taken from recent a “live case” on my desk, with the numbers rounded off. The divorcing parties are in their early 40’s and husband is a PERS Tier Two member. He became a PERS member in 2001. He has an account balance of $10,000 (representing contributions from 2001 thru 2003) and an IAP account balance of $30,000 IAP (representing contributions from 2004 to date). All benefits are marital. The actuary has calculated that the present value of the Tier Two benefit is $70,000 based on the Full Formula method but only $30,000 under the Money Match method. Therefore, the member’s total PERS benefits are $100,000 ($70,000 for Tier Two and $30,000 for IAP).

In this particular case, the parties are choosing to divide the benefits by assigning the entire Tier Two account balance and $20,000 of the IAP account to wife, with a total value of $50,000. This is because the wife was anxious to maximize current cash. But the parties could have split the IAP evenly and applied the time rule to the Tier Two benefit. Had they chosen that approach, and assuming husband retires 15 years from now, wife would then receive a time rule share equal to 10 years married service ÷ 25 years total service x 50% = 20% of member’s final benefit, then converted to a single life annuity for her own lifetime. That is more in keeping with Oregon caselaw for dividing defined benefit plans, and it may be a better result for wife in terms of income security in the long run.

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Understanding and Dividing PERS Benefits in Divorce

By Clark B. Williams

Question: Can a PERS Tier Two benefit with an $8,000 account balance be worth $150,000?

Answer: Yes, and often so!

This occurred in a case that I was involved in just last week (as I write this). I will explain why later in this article.

My point is that PERS benefits are not what they seem. Often there is much more than meets the eye. So this article will attempt to dispel some of the mystery of the various PERS benefit systems in a way that will help you better understand PERS benefits and better serve your clients.

Every PERS member has two sets of retirement benefits. First, virtually everyone has an IAP account. Second, every member has a benefit from one of these three systems: Tier One, Tier Two or OPSRP. I will address each below.

IAP Accounts.

IAP stands for the Individual Account Plan under ORS 238A.300 et. seq. This is the easiest system to understand. IAP accounts are comprised of the 6% “employee” contributions for all PERS members plus earnings thereon. IAP accounts first started in 2004. The accounts are cash in the bank, so to speak, much like a 401(k) or IRA. However, IAP accounts are not self-directed. Rather, all IAP accounts are invested as a multi-billion dollar pooled fund managed by a Wall Street firm. So the investment earnings are determined, and allocated to individual accounts, only once per year.

For that reason, IAP accounts can be divided on divorce only as of December 31 of any year. If a mid-year division is desired, then the amount to be awarded to an alternate payee must be determined by hand. This is done by determining the alternate payee’s share as of the prior December 31, then adding the alternate payee’s share of the 6% employee contribution (not earnings) for the portion of the calendar year up to the division date, and then to award that sum as a dollar amount to the alternate payee as of the prior December 31. By using the prior December 31 date as the division date, the alternate payee will automatically receive earnings on his/her share going forward.

OPSRP.

This stands for the “Oregon Public Service Retirement Plan” under ORS Chapter 238A and applies only to PERS members first employed after August 29, 2003. OPSRP is a true defined benefit plan. There is no “account balance” as with Tier One or Tier Two. Rather, it is designed to pay a pension (i.e., a stream of payments) at retirement. It is akin to Social Security – no pot of money, only retirement income for life.

1 The exceptions are: (1) anyone who has not worked in a PERS covered position since 2003; and (2) those who are retired or terminated and who have already withdrawn or rolled over their IAP elsewhere.

2 6% of the member’s compensation for the year. For most PERS members, this contribution is made (“picked up”) by the employer even though it is called an “employee” contribution on PERS statements.

3 $3.9 billion at the end of 2011.
In OPSRP the amount of retirement income is strictly a function of the member’s years of service and final average salary. The benefit, payable at age 65, is based on this formula: (years of service) x (1.5%) x (final average salary). So an OPSRP member with 20 years of service will receive a pension equal to 30% of his/her final average salary (20 years x 1.5% = 30%). If final average salary is $4,000/month, then the OPSRP pension will be $1,200/month starting at age 65 and continuing for life. The member can choose joint-and-survivor options with a spouse beneficiary for a slight reduction in the monthly benefit.

What is an OPSRP benefit worth? It could be a lot. An actuary is required to determine the value precisely, and that value will vary with interest rates. But it is not uncommon for the value of a member’s OPSRP benefit to approximate the balance of the member’s IAP account. And an OPSRP is not divisible until the member’s earliest retirement age. Therefore, a good approach to divide an OPSRP member’s PERS benefits is to have the member keep the OPSRP and let the spouse take the IAP. The OPSRP will have to be valued, and the difference from the IAP balance will have to be adjusted in some manner. But that approach best serves the interests of disentangling the parties.

If an OPSRP is to be divided, then the “time rule” approach, as explained in the Kiser⁴ and Stokes⁵ cases, is generally appropriate and most fair. PERS will now re-calibrate the portion assigned to the alternate payee so that it is payable for the alternate payee’s lifetime rather than the member’s lifetime. That is a good and recent development. This “separate interest” division best accomplishes the interest of disentanglement and in most cases eliminates the need to award or be concerned about survivor benefits.⁶

Tier Two.

Tier Two covers members first hired between January 1, 1996 and August 28, 2003. Their account balances are comprised of their 6% employee contributions up thru 2003, plus earnings. And those earnings are not guaranteed (as are Tier One regular accounts, see below).

But here is an important truth - - for nearly all Tier Two members, the balance of a Tier Two member’s account has no bearing on the value of the Tier Two benefit!! Let me say it again – almost always the account balance is irrelevant to value. The actual value is usually much greater.

This is because no new contributions have been added to the Tier Two accounts since 2003 (after which the 6% contributions were diverted to the new IAP accounts). At most, those accounts received six or seven years of contributions. So Tier Two accounts are relatively small. Yet Tier Two members are still earning service credits under the Full Formula, including for service after 2003. Tier

⁴ 176 Or.App. 627 (2001)
⁵ 234 Or.App. 566 (2010)
⁶ One “hole” in OPSRP is that, if after divorce the member dies before retirement and without remarrying, then the benefits of both parties are entirely lost. This would not occur if the parties stay married until the member’s retirement. So a spouse is in a worse position for having become divorced. This may be fixed by legislation. But in the meantime, life insurance on the member’s life in favor of the alternate payee until the member retires may be necessary to cover this contingency.
Two members will receive retirement income based on the higher result of two calculation methods: the Money Match method (based solely on the account balance, doubled) and the Full Formula method (based solely on total years of service and final average salary). And now that nearly 10 years have elapsed since the cut-off of new contributions to Tier Two accounts at the end of 2003, the Full Formula is the prevailing method almost every time. The only exceptions are Tier Two members who left PERS-covered employment before or shortly after 2003.

Tier Two members can retire at age 60 (rather than 65 as under OPSRP) and the formula is 1.67%/year of service (rather than 1.5% under OPSRP). These differences make the Full Formula under Tier Two much more valuable than OPSRP. Therefore, for Tier Two you should have the benefit valued by an actuary every time. You will be surprised.

This is the example first stated above. That member entered Tier One in 2002, so her account received only two years of contributions before the cutoff in 2003, and her account balance now is only $8,000. Yet she has 10 years of service, a very good salary and is close to retirement. Thus, the present value of the total benefit is $150,000, meaning that husband’s 50% marital share is worth $75,000. Husband had no idea! He was about to agree to offset $8,000 of his 401(k) account against her $8,000 Tier Two account. So he was glad to have called me before he agreed to that settlement.

If a Tier Two benefit is to be divided, then generally it is most fair (as with OPSRP) to divide the benefit using the “time rule” approach and to create a “separate interest” for each party at the member’s actual retirement (or when elected by the alternate payee at the member’s earliest retirement date). Tier Two does not have the same “hole” as does OPSRP7 with regard to a pre-retirement death. However, until retirement the benefit is still in one piece, which makes it important to require that the member designate the alternate payee as beneficiary of at least 50% of the marital portion. Once benefits commence to the alternate payee, then each party will have his/her own share for his/her own lifetime and the member can be released from the beneficiary restriction.

Tier One.

Tier One members are those who first started PERS-covered employment before 1996. Their retirement benefits differ from Tier Two in two important respects: (1) normal retirement date is age 58 rather than 60, making the benefit significantly more valuable; and (2) earnings in the “regular” account are guaranteed to be at least 8% per year8. As a result, the account balances of more senior Tier One members often produce a larger Money Match benefit than the Full Formula. For those members, even though no new contributions have been added since 2003, the 8% annual growth in their accounts is out-stripping the additional service credits under the Full Formula. So it is common, still, to find a Tier One member (typically those who started work before 1990) for whom the Money Match method will produce a retirement benefit larger than the Full Formula method.

As a “rule of thumb,” the present value of a Tier One member’s benefit is at least three to four times the present account balance, at today’s interest rates. Here’s why: (1) the regular Tier One account continues to grow at 8% per annum between now and retirement, far above current market

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7 See footnote 6.
8 The 2003 Oregon Legislature tried to take away the 8% earnings guarantee, but in the 2005 Strunk case the Oregon Supreme Court held that the 8% guarantee is constitutionally protected.
(2) at retirement the account will be doubled by the Money Match; (3) the account (as doubled) is then converted to a monthly payment based on a PERS table that also has an 8% interest rate built into it; and (4) the monthly benefit will then receive an annual COLA increase of up to 2% per year for life. As a result, the projected monthly benefit usually has a present value of between three and four times the current account balance.

The present value of a Tier One benefit can be more than four times the account balance if the Full Formula method is the prevailing method to determine the benefit. In other words, the “three to four times account balance” rule of thumb is the “floor” for the present value of a Tier One benefit. If the Full Formula method is projected to provide a higher benefit than the Money Match method, then the present value of the Tier One benefit is proportionately higher.

Whether a Tier One benefit will paid based on the Money Match method or the Full Formula Method should dictate the approach to be taken in dividing the Tier One benefit on divorce. And this takes expert help to determine. If the Full Formula method will prevail, then the “time rule” approach for dividing the benefit is the most balanced approach, just as with Tier Two and OPSRP. But if the Money Match method will prevail, then perhaps it is fair to divide the account “up front” now, so that each party has his/her own account.

But now some strategy: if the Full Formula will prevail in a Tier One case, an astute lawyer representing the member might rather seek to divide the account in half “up front.” That will limit the alternate payee to the Money Match calculation and allow the member to retain the member’s half of the Money Match benefit plus all of the difference in value of the Full Formula over the Money Match. And the reverse is true, too. When the Money Match method will prevail, then to divide the account “up front” means giving away 50% of the final benefit. So if the Money Match method will prevail and if the member will continue working after the divorce, then the lawyer for the member might rather apply the “time rule” division in order to allow the member to keep more than 50% of the final benefit.

Conclusion.

Lawyers addressing PERS benefits in divorce should recognize the differences in the nature and values of the several PERS retirement systems and, where appropriate, seek expert help in evaluating and dividing PERS benefits.

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9 At age 58, the conversion rate is $7.60/$1,000. So for example, a $50,000 account, doubled to $100,000, will convert to a monthly payment of $760/month for life. That is far more than current commercial rates.

10 This COLA adjustment may be limited for higher-paid retirees under legislation now pending in the Legislature.

11 This week (as I write this) I reviewed an actuarial valuation for a 47-year-old Tier One PERS member whose account balance is $67,000 and the present value is $237,000 (almost four times more). This is not uncommon.

12 This article assumes a pre-retirement divorce. This article does not address other additional issues that arise in dividing PERS benefits for members who have already retired and commenced benefits.
BUSINESS VALUATION

WHAT YOU NEED TO KNOW
WHAT YOU NEED TO ASK

WHICH VALUATION VARIABLES HAVE THE GREATEST IMPACT ON VALUE

WILLIAM V. MASON II, ASA, CPA/ABV, CFF
Partner/Shareholder, Jones & Roth, P.C.

Business appraisers should, initially in their report, provide a definition for the standard of value under which the appraisal is being performed. This standard of value is generally fair market value, but it may be fair value, investment value, strategic value or some other standard. In addition, the appraiser should describe the "premise of value". The premise of value is generally "going concern" value, but the valuation premise may also be "assemblage of assets", "liquidation value". The "Going Concern" premise assumes the valuation is based on the assumption that the business will continue to operate as it has in the past, generating revenues from typical operational sources and incurring related expenses. An "Assemblage of Assets" premise assumes the business will not continue, but rather it has stopped operations or soon will stop operations, and a "Liquidation Value" generally reflects sale values of assets less selling expenses and generally income tax consequences.

Following are brief definitions of standards of value applicable under various circumstances.

Fair Market Value

The price, expressed in terms of cash equivalents, at which business interest or property would change hands between a hypothetical willing and able buyer and a hypothetical willing and able seller, acting at arms length in an open and unrestricted market, when neither is under compulsion to buy or sell and when both parties have reasonable knowledge of the relevant facts.

Fair Value

There is no common definition of "fair value". It is generally considered a legal standard that is defined by statute or case law. In shareholder oppression cases in the state of Oregon, ORS 60.551(4) defines fair value as:

"Fair value," with respect to a dissenter's shares, means the value of the shares immediately before the effectuation of the corporate action to which the dissenter objects, excluding any appreciation or depreciation in anticipation of the corporate action unless exclusion would be inequitable.
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This definition has been applied differently. For a court ordered buy-out for oppression, the interest is to be valued without a discount for either minority/lack of control or marketability (Chiles v. Robertson 94 Or App 604, 767 P2d 903 [1989]). For a valuation under the dissenter's appraisal statute, a marketability discount may be appropriate, but no discount is applied for minority/lack of control (Columbia Management Co. v. Wyss, 94 Or App 195, 765 P2d 207 [1989]).

Investment Value

The value to a particular investor based on individual investment application, requirements and expectations.

Liquidation Value

The net amount that would be realized if the business is terminated and the assets are sold piecemeal. Liquidation can be either "orderly" or "forced."

Intrinsic Value

The value that an investor considers, on the basis of an evaluation or available facts, to be the "true" or "real" value that will become the market value when other investors reach the same conclusion. When the term applies to options, it is the difference between the exercise price or strike price of an option and the market value of the underlying security.

Book value

With respect to a business enterprise, book value is the difference between total assets (net of accumulated depreciation, depletion, and amortization, if applicable) and total liabilities as they appear on the balance sheet (synonymous with Shareholder's Equity). With respect to a specific asset, this would be the historical (capitalized) cost less accumulated amortization or depreciation, if applicable, as it appears on the books of account of the business enterprise. As a result, when a business has significant investment in land, buildings, and/or furniture, fixtures, and equipment, the book value only coincidentally will reflect fair market, fair, investment, liquidation or intrinsic values.

In addition to defining the applicable value standard and the valuation date, in a reasonably comprehensive valuation report, the appraiser should provide a discussion of the following:

1. Current economic and market conditions to which the target business is subject;
2. Specific industry conditions and outlook;
3. Historical financial statement analysis of the target business, and history of any previous equity transactions;
4. Adjustments necessary in order to reflect current expectations of cash flows and earnings;
5. Valuation analyses which may incorporate capitalization of cash flows or earnings, comparable market transactions, and adjusted net assets (adjusted to current market values);
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6. Application of appropriate discounts such as minority interest discount, discount for lack of marketability, portfolio discount, blockage discount, etc. and,

7. Overall opinion of value and the weight(s) given to each estimate of value provided in the analysis.

In a perfect world, the reader of these reports understands the relative impact of each assumption that the appraiser has made. The report, if indeed it is as detailed as I have suggested above, should explain all valuation assumptions and their bases. In reality, it probably takes a knowledgeable appraiser to ferret out many assumptions used and sensitivity analysis to determine the relative impact on the resulting opinion of value that changes in the assumptions generate. Most often, you may have only summary reports presented, or you may be presented with an opinion of value only through testimony or some other form of verbal presentation. Are you ready to ask instructive questions which illustrate the impact on value of what may appear to be minor changes? What questions should you ask a jointly retained valuation expert, or your valuation expert, and/or the other side’s expert to insure that all pertinent issues are explored?

You cannot be an expert in all issues pertinent to your client, but you should have a reasonable understanding of the basic concepts in order to help insure that the expert has reasonably analyzed the situation and arrived at a justifiable conclusion. Following are decisions made by the business appraiser which have the greatest impact on the valuation opinion. They are presented in order of magnitude of impact, from the most significant to those of lesser significance. Ask your valuation expert (or the other side’s expert) to explain the basis for the decisions he/she has made relative to these issues. You should be able to determine if the responses are consistent and reasonable.

1. What standard of value is being used in this valuation?

The most prevalent standard of value used is “fair market” value. This is generally defined as the price at which the interest being valued will exchange hands, assuming both parties have knowledge of all relevant facts and neither is under compulsion to act. Fair market value incorporates the concepts of controlling versus minority interest and freely tradable (ready market as in stock exchange) versus no ready market (difficult and time consuming to find a buyer).

The concept of minority interest implies that a value of a non-controlling interest will be discounted below the pro-rata value of the total enterprise value, because the minority interest holder lacks control aspects which create value (e.g. ability to force cash distributions, force liquidation, establish debt structure, make hire and fire decisions). For example, the fair market value of a 10% interest in an enterprise valued at $1 million, given its inherent lack of control, will be less than $100,000 (10% times $1 million).

Marketability also impacts value. An ownership interest which is freely tradable (i.e. is easily converted to cash) is more highly treasured than an interest that does not have a ready market. Liquidity is valued, illiquidity reduces value.

A second standard of value noted above is “fair” value. Fair value opinions generally do not take into account the concept of minority/controlling interest, nor do they incorporate marketability. Generally an opinion of value under this standard would be represented
by the pro-rata value of the total enterprise value. I use the word "generally" because this standard of value, as noted above, is generally defined by the court having jurisdiction.

A third standard of value is "investment" value. The two previous standards of value require an analysis of the general acquisition market, i.e. the total population of potential buyers. Investment value is the determination of the value of the subject interest to a specific investor. This value will vary depending on specifics associated with the individual investor. One investor may value a potential acquisition higher because of synergies they foresee given the acquisition. Another investor may value an interest higher because of markets that may become available as a result of the acquisition. A third investor may value the interest lower because of certain qualitative aspects associated with the subject interest (societal aspects or personal attitudes). Investment value is specific to the entity for which the valuation is performed, and it does not necessarily reflect how the market, in total, would value the subject interest.

The standard of value should be determined by the attorney/arbiter based on the appropriate laws and precedents. Be sure your valuation appraiser is developing an opinion of value based on the appropriate standard. In some instances there may be no required standard of value. Be sure to have your expert prepared to provide your client with an analysis which benefits their circumstances. An error here can result in a material change of value. Applying the "fair market" value standard to a minority interest instead of the "fair" value standard can result in the value estimate being more than 50% less than the "fair value" standard would report.

2. Has the appraiser adequately addressed unrecorded intangible assets and differentiated between enterprise goodwill and personal goodwill in the analysis and in the report?

Given the December 2010, Oregon Court of Appeals decision in Slater v Slate (marital dissolution) "goodwill" analysis has become paramount. While the decision could be limited strictly to family law issues, it may and does apply, in theory and practice, to other valuation purposes. In the decision, the Court recognized that personal goodwill is not a saleable asset. As the name implies, personal goodwill is a personal asset attached to a specific person. I liken it to "bedside manner". The manner in which one person interacts with patients, clients, customers, vendors, etc. is not saleable. An acquirer of a business may try to mimic another, but individual personality traits impact results.

The term "goodwill" is too often incorrectly used to reference all intangible assets. "Blue Sky" is synonymous to "goodwill" when "goodwill" is used in this same general ambiguous manner. Specifically, goodwill is the name for the intangible assets which exist within a business entity that are NOT specifically identifiable. Examples of specifically identifiable intangible assets are: trained workforce; reputation; location, customer lists and files, etc.. When truly valuing goodwill, the values of these other identifiable intangible assets must be determined, because "goodwill" is really a remainder asset.

The general method for valuing the total intangible assets of a business is to value the total business entity, using an income or market approach. The total intangible asset value is the difference between the total entity value and the value of the net adjusted
tangible assets. This difference represents all unrecorded intangible assets. To determine an estimate of the "goodwill" value, all identifiable intangible assets are valued. The total intangible assets' value is reduced by the values of these identifiable intangible assets (yes, the identifiable intangible assets can be valued, publicly traded entities have these valued annually for public reporting purposes), and the remainder is the value of "goodwill".

Even at this level of analysis, "goodwill" remains potentially mislabeled. For most businesses, particularly professional service businesses, (such as medical, accounting, architectural), "goodwill" itself is made up of two parts: personal (non-saleable) goodwill; and, enterprise goodwill (saleable). Enterprise goodwill belongs to the business entity and is saleable. Perhaps, if we can identify all applicable identifiable intangible assets, the remainder "goodwill" will all be personal, however this is generally not the case as business processes, the general component of enterprise goodwill, will remain.

A complete business valuation/appraisal must address goodwill. Regardless of the purpose of the appraisal, assuming it is to determine the fair market value of a business or an interest in a business, personal goodwill and enterprise goodwill must be addressed. Since personal goodwill, by definition, is not saleable, the fair market value of a business must exclude this component. The fair market value of an entity, or an interest in an entity, will include all saleable assets, and enterprise goodwill is saleable. (ASIDE: There are times when appraisers are asked to value a business entity in the hands of a specific owner. When this is the purpose, the resulting value should appropriately be termed "strategic value" rather than fair market value, and this value will incorporate the personal goodwill of the acquiring owner.)

As I noted, there are reasonable means to value identifiable intangible assets, generally based on cash flows, but there are also market approaches (such as comparable royalty rates, cost to train/construct). Since this analysis significantly impacts fair market value, it must be done and either directly addressed in an appraiser's report, or included in the appraiser's work papers.

Appropriate valuation analysis can avoid potential Slater v Slater issues, when litigation is involved, and properly address value when a transaction is being proposed or negotiated.

3. Is there adequate justification for the discount for lack of marketability?

As previously mentioned, liquidity is cherished. It allows an investor to withdraw from an investment, for whatever reason, in a timely manner (generally defined as converting to cash in 3 days). There have been numerous studies attempting to observe discounts associated with the lack of liquidity in investments. All of the studies have been done by referencing the price of publicly traded stock versus the price of the exact (or similar) shares which are subject to certain restrictions on trading. Suffice it to say that these studies have analyzed restricted stock prices (generally issued through options and restricted from public trading for a specified period of time) compared to the same freely tradable stock prices, and they have compared transaction prices of stock before an initial public offering (IPO) and after the offering.
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In general, the median discounts observed have ranged from about 30% to 50%, depending on the particular study and the type of study. Many business appraisers arbitrarily select a percentage discount, such as 40%, without analyzing the specifics associated with their particular engagement.

Valuations of minority interests, under the "fair market" value standard, would almost always be subject to some level of lack of marketability discount. The question to ask is what is the appropriate magnitude of this discount?

Business appraisers may attempt to apply a marketability discount to a controlling interest. This is a contentious topic among those of us in the business appraisal community. This article is not an appropriate forum for this theoretical debate, but the point to be made is the empirical basis for the discount. It is absolutely incorrect to reference the typical restricted stock studies, pre-IPO studies, or studies of option pricing in order to determine the magnitude of the lack of marketability discount applicable to a controlling or total enterprise value. All of these studies relate to minority interests (i.e. per share values) not controlling interests or enterprise values. If the business appraiser believes a lack of marketability discount is appropriate to the controlling interest being valued, there are no empirical studies on which to rely. The analysis will rest on the subjective argument of the appraiser, not on any empirical observations, for there are none as of today.

Clearly the impact of the application of an inaccurate or unjustified marketability discount can be significant. With medians of observed discounts ranging from 30% to 50%, and actual observations exceeding this range, the impact on the resulting opinion of value can be significant.

4. What level of minority interest discount (or the reciprocal control premium) is justifiable?

Minority interest discount reflects the loss in value due to an inability to influence business decisions which impact the cash flows to the minority interest holder. A holder of a pure minority interest cannot: 1) force cash distributions; 2) require entity liquidation to access underlying asset values; 3) require the business entity to provide a job to the holder and receive fair compensation; 4) alter financial structure of the business; 5) adjust controlling owner compensation, perks; etc. A controlling interest effectively can control all of these aspects of the business. We consider the discount associated with the minority interest to be the reciprocal of the control premium associated with the controlling interest.

Minority interest discounts are studied by observing control premiums in the marketplace. Generally, when a publicly traded company is acquired, the acquisition price of the stock is in excess of the current trading price of the stock. When the acquisition price is announced the "control premium" can be developed. If a stock is currently trading for $1 per share, and the announced acquisition price is $1.40 per share, the control premium is equal to the difference in price, $0.40 divided by the $1 traded price, or in this example a 40% control premium. If we observe a price differential of $0.40, and we know the "control price" is $1.40, the observed minority interest discount is $0.40 divided by $1.40, or about 28.6%. This is why we refer to them as reciprocals.
The application of a minority discount assumes that the value to which the discount is applied is based on controlling interest assumptions. The application of a control premium assumes that the value to which the premium is applied has been developed by relying on minority interest assumptions. For example, if a minority interest value is the goal, and it is developed by referencing a pro-rata value of the total enterprise value (enterprise value assumes control), then it is appropriate to apply a minority interest discount to the pro-rata value of the enterprise value. If an enterprise value is the goal, and the value has relied on the values of public exchange traded stocks (minority interests since these are small lot stock prices), then it is appropriate to apply a control premium.

Studies report observed levels of control premiums, and their reciprocal minority interest discounts. The business appraiser must have a logical, justifiable analysis to support the selection of the appropriate minority discount/control premium. The studies report all publicly announced merger and acquisition activity. Many of the announced transactions are not purely financial transactions, rather they are strategic or synergistic acquisitions. When transactions are strategic or synergistic, the observed premia incorporate more than just that associated with control. The business appraiser must not merely pick an observed median of premia/discounts. The premium/discount applied should only reflect control/minority issues. The discount applied should be developed without the taint of strategic acquisition premiums.

Has the business appraiser applied a minority interest discount or control premium based only on pure control aspects? Has the business appraiser applied the appropriate discount or premium to an appropriate base, control or minority, respectively?

5. Is the capitalization rate (the rate of return, required by the investor, adjusted for growth) appropriate?

The basic theoretical valuation model requires that the business appraiser project cash flows available, to the equity holder, for future periods over the business horizon. Each of the periodic cash flows is then discounted back to the present (valuation date) based on the risk of realizing the projected cash flow. This is generally considered to recognize the "time value" of money. A projected cash flow of $110,000 to be received after one year of operations has a present value of $100,000 assuming the rate of return required is 10%. An investor would pay $100,000 today for a cash flow of $110,000 one year off, assuming a 10% annual return rewarded the investor for the risk assumed. The greater the risk (the greater the probability of not achieving that cash flow) is, the greater the rate of return that is required. The same projection of $110,000, one year off, with a greater risk, such that an investor requires a rate of return of 25%, would have a present value of $88,000. In this analysis of cash flow to equity, the term "required rate of return" is synonymous with "discount rate".

When cash flows, available to the investor, grow (positively or negatively) unevenly, the appraiser projects each period's cash flows. When it is reasonable to assume that cash flows will grow at a constant rate, the present value calculation can be simplified to determine the sum of all cash flows once growth can be reasonably assumed to be constant. When this is the case, "the discount rate" is adjusted for the anticipated constant growth rate, and the resulting rate is called the "capitalization rate".
As a result of the method of development of the capitalization rate, there are two potential problem areas, the determination of a reasonable rate of return to the equity holder of the subject business, and the determination of a sustainable long term growth rate. Both rates can and do have significant impact on the ultimate opinion of value. As noted in the example above, a change in the required rate of return from 10% to 25% for the present value analysis one year’s cash flow resulted in a change in value of 12%. Since businesses are assumed to generate cash flows over a period of years, the change in value can be very significant, even with reasonably small changes in the required rate of return. For example, if cash flows to equity are projected to be $50,000 annually, and we assume no growth, the present value of these cash flows, assuming a required rate of return of 20% is reasonable given the risk, is $250,000. If we assume the risk is greater, and it warrants a required rate of return of 25%, the present value is $200,000, a change in the value of 20%. Using the same example, leaving the required rate of return unchanged, but changing a long term growth rate from 10% to 5% will have equally significant changes in value opinions.

The net impact of minor adjustments to the required rate of return in conjunction with apparent minor changes in long term growth rates can also significantly impact opinions of value. For example, increasing a required rate of return by 2 percentage points, while simultaneously reducing growth by 3%, is the equivalent of a change in the required rate of return by 5% while holding growth constant.

What is a reasonable equity rate of return? Appraisers look to observable returns of other investments to determine reasonable rates of return. We call it alternative, but equally risky returns. We incorporate current inflation assumptions in rates of return by using the current long term Treasury bond rate as a building block. The largest of the New York Stock Exchange firms have averaged, over the last 75 years, an annual return to their investors of almost 8% in excess of the 20 year Treasury bond rate. Given the current 20 year Treasury bond rate of approximately 5%, then investors in these very large companies would reasonably expect an average annual return approximating 13% today, when averaged over a long holding period. If these extremely large businesses can provide that kind of return to their investors, why would an investor buy an equity position in a significantly riskier small local business that provides a return less than the 13%. The appraiser developed must exceed this achievable 13% annual long term return. The smallest of the New York Stock Exchange (NYSE) firms, over the same 75 years, have averaged a rate of return, in excess of the Treasury bond rate, of about 12% annually. This means that those "little" NYSE firms (having $100 million or more of revenues annually) would be expected currently, over a long term, to provide an annual rate of return of about 17% (5% plus 12%). If these types of firms with national or international markets, reasonable product diversification and a seasoned management team can provide this level of return to their investors, an investor in a smaller, riskier business would require a return in excess of 17% to account for the increased level of risk. The business appraiser must be ready to explain their selection of an appropriate equity rate of return given rates of return available for alternative investments.

You may have observed that real estate appraisers often use a rate of return associated with their "income approach" approximating 10% annually. Why is this reasonable relative to other investments? That is a reasonable return because there is a "fall back" available to the investor in some types of real estate. If the projected cash flow of the real estate investment does not materialize, the real estate may be sold. You might say
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that the real estate serves as collateral to the investor. If the cash flows from the subject operating business do not materialize as projected, there is no "fall back". The equity holding is not independent from the cash flow, therefore, it requires a greater rate of return to reward the investor for the assumption of greater risk.

In addition to recognizing a reasonable equity rate of return, the long term growth rate must be reasonable. Over a short period of time, perhaps 5 years, it may be possible for a business to achieve cash flow growth of 10% or more. Over the long term, growth rates at 8% to 10%, given current inflation, is almost impossible to achieve. Achievable long term growth rates at that level are difficult because competition enters the market restricting achievable growth rates. It takes a very unique product or service, protected from market encroachment (e.g. patent, copyright) to achieve such a sustained growth rate. The business appraiser must be prepared to defend the selection of the long term cash flow growth rate used in the valuation. If it is reasonable to achieve high near term growth rates, then generally cash flows are projected for the near term years over which this growth is expected to be achieved, until a reasonable long term growth rate is anticipated. Most long term growth rates can be expected to be no more than 2 times inflation or less.

6. Are the market comparables really comparable?

We as business appraisers, like real estate appraisers, look to find comparable business transactions that are measures of business valuation. We would like to find an identical business, or interest in a business, that just sold, allowing us to develop a value for our subject interest based on the recent transaction. Unlike real estate, such transactions are not generally public. We have several sources of data bases which report transactions of entire businesses which we may use. Identifying information is not available, but some basic financial information is available. From this information we develop value measures such as deal price to sales, deal price to equity book value, and deal price to various measures of cash flow. We select transactions in businesses which we consider comparable to our subject business being valued. The question which must be asked, and for which the appraiser must be prepared to defend, is, are the selected transactions comparable? Is a business located in another area of the country comparable? Is a business that does $200,000 a year in revenues, comparable to a business that does $2,000,000 per year? Is a business that generates cash flow to the owner at a rate of 20% of annual sales comparable to a business that returns only 4% to the owner? If the businesses that were sold/purchased are not comparable to the subject business, the merger and acquisition market multiple derived from the transaction will not be comparable.

While these concerns are prevalent in merger and acquisition multiples, they are more acute when the appraiser has selected a publicly traded guideline company or companies as comparable. There are several concerns when developing values for a subject interest based on per share publicly traded prices of comparables. There is the issue of developing a controlling interest value by referencing freely tradable minority interests (per share values). The appraiser must be prepared to support an applied control premium, as discussed previously. The appraiser must also be prepared to defend any adjustment, or lack of adjustment, based on the freely tradable nature of a publicly traded stock.
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How comparable are the selected publicly traded companies to a subject company. If the subject company is a distributor wholesaler, it is generally not comparable to the company that manufactures the products subject to distribution. Clearly size, market area, financial structure (high debt versus low or no debt), and product/service diversification are important factors in determining comparability. A $1 billion revenue per year company is generally not comparable to a subject company that has $5 million in revenues, even when they operate in the same industry. It may be possible to make adjustments to the publicly traded per share multiples to reflect difference in size, financial leverage, etc., but these will be subjective adjustments and the appraiser must be prepared to defend these adjustments.

A last thought on observed publicly traded multiples, and their use to develop the subject company valuation opinion. When the publicly traded comparable company's stock trades for low prices, generally around $1 or less, small movements in stock pricing can create significant movements in the observed price multiples. A stock price that trades at $1 and moves 1/8\textsuperscript{th} has moved 12.5\% in value. A stock price that trades at $4 and moves 1/8\textsuperscript{th} has changed only 2.5\% in value. Appraisers should look for higher priced stocks to avoid these small movements in stock pricing around the valuation date, having a material impact on the resulting opinion of value.

7. Has the appraiser applied all reasonable valuation methodologies in developing his/her opinion of value?

For almost all valuation engagements, at least two approaches to value are applicable. Most interests in operating businesses can be valued using a market approach and an earnings/cash flow approach. Generally, within these categories, there are multiple methods which can be used. If the business appraiser provides only one methodology, the appraiser should be prepared to defend the lack of application of any other method. Uniform Standards of Professional Appraisal Practice require appraisers to be prepared to explain why certain methods were used and why certain other methods were not used. Failure to apply an available technique, without adequate justification, may reveal either an incomplete valuation analysis, or an attempt to purposely influence the results of the analysis.

8. Can the business appraiser explain why the various valuation methodologies used arrive at different value opinions for the same interest?

In a perfect appraisal world, each method used to estimate the value of a closely held business interest, should arrive at the exact opinion of value. We do not necessarily expect an appraisal of an operating business (as versus a holding company) relying on liquidation values of the underlying tangible assets, to equal the value of the business estimated by use of a market or earnings/cash flow approach. The liquidation value approach would generally not incorporate values associated with the business as a going concern, such as goodwill. Goodwill or “blue sky” exists if the business generates a return in excess of what is reasonable from just the tangible assets.

While reality is different from pure theory, we still should expect, for operational entities, market approaches and capitalization of earnings/cash flow approaches similar valuation estimates. When they do not, the appraiser should be prepared to explain why they are not similar. It is inappropriate for the appraiser to merely select a method as
appropriate, without fully explaining why the methods did not yield similar value estimates. It may be appropriate for the appraiser to ultimately select a method, or give greater weight to one method over another, but that appraiser must be able to explain why the difference exists, and why they choose to select a single method, or give greater weight to one method over another. From a very practical standpoint, analysis and reconciliation of value estimate differences by the appraiser can often expose errors, inappropriate assumptions, or inapplicable methods for particular circumstances.

Summary

As I stated at the beginning of this paper, business appraisers generally provide a detailed analysis of many factors influencing their opinion of value. They may spend a significant amount of their report analyzing expense to sales relationships, aberrations in particular years' results, and projecting an immediate year's cash flow projections. They may spend minimal time within their narrative report or testimony on the analysis of applicable discounts or premia, reconciling various value estimates, or explaining the rationale behind the required rate of return or expected growth rates used. The appraiser must be prepared to defend all aspects of their valuation opinion.

It is not uncommon for an appraiser to spend considerable attention to detail in developing projected cash flows to immaterial levels, capitalizing this minutely detailed cash flow, and then haphazardly, and without adequate justification, applying a 40% discount to the total.

Do not be caught up in the appraiser's detail. Be aware of those variables which have the greatest impact on the valuation opinion, and require explanation for the assumptions made.
BUSINESS VALUATION

VALUATION CONCEPTUAL STRUCTURE

WILLIAM V. MASON II, ASA, CPA/ABV, CFF
Partner/Shareholder, Jones & Roth, P.C.

The value of a business interest depends on the future benefits that will accrue to it. The financial benefits from ownership must come from one of the following sources: first, distribution of cash; second, from the sale of the interest; and, third, distribution from the liquidation of assets. In determining the value of a business interest, one should focus on the benefits the shareholder(s)/owner(s) may receive with long term ownership of the securities or interest in question from these three sources. In appraisal terminology, these three sources of return correspond to the income, market, and adjusted net asset value approaches, respectively.

Note the concerns are the financial benefits from ownership of the equity in the business or ownership of the assets of a business which may be subsequently contributed to a newly formed entity continuing to perform the same function. The applied theory used to develop the value of an entity or an interest in an entity: income, market, asset continue to be applied as they have been historically. Appraisers are developing more objective means to derive the underlying value drivers (projections, rates of return, useful life of products and services, etc.). When a buyer looks to acquire a business or an interest in the business, the acquirer is concerned about the assets which are acquired and the assets' ability to continue to generate the historically achieved cash flows. This concern, in addition to the Court's influence through its decisions, has lead the appraisal profession to emphasize the analysis of saleable goodwill. The buyer only wishes to pay for those assets which can be transferred. For litigation purposes, the Court (see Slater v Slater, Oregon Appellate Court decision December 2010) is concerned that fair market values only reflect the value of assets which can be sold. (For a summary of an appraiser's view, of "goodwill" valuation see that section later in this article.)

INCOME

The income approach relies upon developing a "normalized" earnings/cash flow picture, that is, forecasted discrete periodic cash flows of the company being valued. Following the determination of normalized or forecasted earnings/cash flows, the reasonable rate of return to an investor must be determined, given general industry and specific company risks associated with the investment. This is generally done by analyzing observable alternative investment return opportunities which have similar risks, determining a growth rate associated with the target company's cash flow. The fair market value can be determined, by "capitalizing" the anticipated income/cash flows at the appropriate rate of return.

The conceptual basis for this approach comes from the constant growth (Gordon Dividend) model, which is based on the premise that the value of a stream of periodic
cash flows, growing at a constant rate, is the present value of all of the cash flows. To apply this model to business valuation, we define "dividends" as either cash flows available to the equity investor, or as debt free cash flow (cash flow before debt service requirements). We define "dividends" as cash flows available to equity investors if we wish to directly value equity. We define "dividends" as debt free cash flow if we intend on valuing total invested capital (total invested capital is equal to equity plus long term interest bearing debt), because this is the cash pool from which "dividends" could be paid to all invested capital. The definition of "dividends" determines the capitalization rate, which is used to develop value. If "dividends" are defined as cash flow to equity investors, the capitalization rate is developed by referencing the required rate of return of the equity holders, adjusted for anticipated "constant" growth in these dividends, and the resulting value is the equity value. If "dividends" are defined as debt free cash flow, then the capitalization rate is based on the weighted average cost of capital (WACC), adjusted for anticipated "constant" growth in these dividends. The capitalization rate, based on WACC, is developed by 'weighting' the rate required for equity capital with the rate required for debt capital (average interest rate of the interest bearing debt), arriving at a blended rate (WACC). The weighting is based on the amount of debt and the amount of equity associated with the total invested capital. The resulting value is reduced by outstanding debt to estimate the fair market value of equity. The simple assumption used in this model, is that periodic cash flow, "dividends", will grow at a constant rate in perpetuity (which is why this is referred to as the constant growth model).

The present value of a perpetual stream of "dividends" growing at a constant rate is as follows:

\[ V = \frac{D}{r - g} \]

where

- \( V \) = present value of stream of cash flows
- \( D \) = next period projected "dividends"
- \( r \) = required rate of return (either equity or WACC)
- \( g \) = growth rate

Cash flow to equity holders is defined as net income after taxes, adding back non-cash expenses (e.g., depreciation and amortization) less necessary retained cash (e.g., cash used for purchase of capital equipment, principal payments on debt, or retained due to working capital needs). Debt free cash flow is defined as net income before debt service (principal plus interest expense) but after taxes, plus non-cash expenses, less capital expenditures and less any necessary increase in working capital. The tax analysis (as in "after tax") is dependent upon the entity type and the level of "tax effecting".

If the cash flows analyzed are debt free cash flow, the value of total invested capital is developed by capitalizing that projected cash flow the weighted average cost of capital (WACC) adjusted for anticipated annual growth. In developing the WACC (blended rate) the interest rate is adjusted to reflect the deductibility of interest expense for tax purposes. The equity rate return is not adjusted, because dividends are not deductible for tax purposes. When valuing a minority interest, the equity rate and the adjusted debt rate are generally weighted in accordance with the current financial structure to arrive at WACC. When valuing a controlling interest, we generally weight the rates in accordance with industry averages, assuming this represents maximum leverage benefits, to arrive at the WACC.
If the cash flows are not assumed to grow in a constant manner, periodic cash flows are developed until it can be assumed that the cash flow will grow at a constant rate. The value of the business is considered to be the sum of the present values of the discrete cash flow projections (discounted at either the equity rate of return or the WACC depending on the definition of cash flow) plus the "terminal value" discounted to the present. The terminal value (the value of future cash flows once constant growth can be assumed) is developed by using the constant growth model applied to the anticipated cash flow when constant growth is assumed. To value the cash flows projected when growth is not constant, the required rate of return unadjusted for growth is used since growth is incorporated in the discrete period cash flow projections.

MARKET

The second approach, market, is developed differently. The value of the organization can be compared to recent market transactions, that is, sales of similar organizations in the same or similar industry. Statistics such as deal price to gross revenues, deal price to earnings/cash flow, etc. can be developed from the information available regarding these similar organizations that recently sold. Pertinent price ratios can be applied to the target company’s financial results to determine an estimate of fair market value. This is perhaps the most preferable means of developing value for a controlling interest since it is the most objective method. While being preferred, it is difficult or impossible to apply at times. Since most merger and acquisitions occur in the private market, information necessary to develop deal price multiples may not be available or information may be limited. Privately maintained data bases are used, but the number of transactions reported may be limited, depending on the industry in which the target company operates. Minority interest value estimates can be developed from these types of entity multiples, but care must be taken to adjust for the lack of control a minority interest holder has and to adjust for any additional lack of marketability to which the minority interest would be subject that is not already incorporated in the observed market valuation multiples.

When valuing minority interests, the value of an interest may be compared to recent market activity in equity transactions, reported through public exchanges (e.g. NASDAQ or New York Stock Exchange), in similar organizations in the same or similar industry, or subject to similar risks. Statistics such as price earnings ratios, price to cash flow ratios, price to book value, etc. can be developed from public information regarding these public guideline company transactions. Pertinent price ratios are applied to the target interest to determine an estimate of fair market value. This is the most preferable means of developing the estimate of value for a minority interest since it is objective, however, unless the target interest is an interest in a very large company, the result is meaningless because of the lack of comparability of the target company to the companies that are publicly traded due to size, capital structure, product diversification, market area, etc.

When valuing non-controlling interests (50% ownership or less) in real estate holding companies or investment companies, valuation multiples are often developed by analyzing discounted prices at which these interests trade. Discounted price refers to the traded price relative to the pro-rata value of the interest. For example, the pro-rata price of a 10% interest in an entity holding $1 million of real estate would be $100,000.
We can observe minority interest transactions in real estate investment trusts (REITs) and publicly registered real estate limited partnerships (RELPs), and we can measure the transaction price versus its pro-rata value. We might observe a transaction price of $7,000 for a 1% ownership interest in an entity holding $1 million of real estate. This price would reflect a discount from its pro-rata value of 30% (pro-rata value of $10,000 less transaction price of $7,000 divided by the pro-rata value of $10,000). This can provide direct insight into the market price of a similar sized interest in a privately held comparable investment company. We can observe these market discounts for real estate holding companies and for other investment companies, those holding publicly traded equities.

ADJUSTED NET ASSET VALUE

The third method of developing the fair market value of an entity, adjusted net asset value, may also be used. With a marginally profitable company, or a holding/investment company, such as a real estate holding company, the underlying assets would be adjusted to the fair market values, and the resulting value would provide a value approach. With profitable operating entities, generally the whole is greater than the sum of its recorded underlying assets. Profitable operating companies generally have either unrecorded intangible assets, or other assets (probably intangible assets) which have values in excess of stand-alone fair market values because of strategic relationships with other tangible assets as a result of on-going operations. Unrecorded intangible assets may be trained workforce, customer lists or files, exceptional in place management, reputation, location, etc. Often "goodwill" is the name assigned to all of these intangibles, however, technically goodwill exists and has value only to the extent that the value of total intangibles exceeds the sum of the values of the identifiable intangible assets. The identifiable intangible assets would be trained workforce, custom lists and files, reputation, name, management skill, etc. Adjusted net asset value approaches, for a going concern, may value these intangible assets, however the value of the intangible assets is dependent on the anticipated cash flows to be derived from the use of these intangible assets. Since the estimate of value of these intangibles is derived from the same projected cash flows on which the income approach value is developed, using this approach will only reinforce the income approach value. It is will provide false support for the income approach since it is relies on the same basic assumptions.

Holding and investment companies do not have these intangible assets, and as a result, they are valued by appraising the tangible assets of the entity. The appraisal of the tangible assets of the entity is generally done by separate appraisal of these individual assets (real estate, equities, etc.) by referencing their normal market exposure.

GOODWILL/INTANGIBLE ASSET VALUATION

Given the December 2010, Oregon Court of Appeals decision in Slater v Slate (marital dissolution) "goodwill" analysis has become paramount. While the decision could be limited strictly family law issues, it may and does apply, in theory and practice, to other valuation purposes. In the decision, the Court recognized that personal goodwill is not a saleable asset. As the name implies, personal goodwill is a personal asset attached to a specific person. I liken it to "bedside manner". The manner in which one person
interacts with patients, clients, customers, vendors, etc. is not saleable. An acquirer of a business may try to mimic another, but individual personality traits impact results.

As noted previously, the term "goodwill" is too often incorrectly used to reference all intangible assets. "Blue sky" is synonymous to "goodwill" when "goodwill" is used in this same general ambiguous manner. Specifically, goodwill is the name for the intangible assets which exist within a business entity that are NOT specifically identifiable. I have noted above several specifically identifiable intangible assets, such as trained workforce, reputation, location, customer lists. When truly valuing goodwill, the values of these other intangible assets must be determined, because "goodwill" is really a remainder asset.

The general method for valuing the total intangible assets of a business is to value the total business entity, using an income or market approach. The total intangible asset value is the difference between the total entity value and the value of the net adjusted tangible assets. This difference represents all unrecorded intangible assets. To determine an estimate of the "goodwill" value, all identifiable intangible assets are valued. The total intangible assets' value is reduced by the values of these identifiable intangible assets (yes, the identifiable intangible assets can be valued, publicly traded entities have these valued annually for public reporting purposes), and the remainder is the value of "goodwill".

Even at this level of analysis, "goodwill" remains potentially mislabeled. For most businesses, particularly professional service businesses, (such as medical, accounting, architectural), "goodwill" itself is made up of two parts: personal (non-saleable) goodwill; and, enterprise goodwill. Enterprise goodwill belongs to the business entity and is saleable. Perhaps, if we can identify all applicable identifiable intangible assets, the remainder "goodwill" will all be personal, however this is generally not the case as business processes, the general component of enterprise goodwill, will remain.

A complete business valuation/appraisal must address goodwill. Regardless of the purpose of the appraisal, assuming it is to determine the fair market value of a business or an interest in a business, personal goodwill and enterprise goodwill must be addressed. Since personal goodwill, by definition, is not saleable, the fair market value of a business must exclude this component. The fair market value of an entity, or an interest in an entity, will include all saleable assets, and enterprise goodwill is saleable. (ASIDE: There are times when appraisers are asked to value a business entity in the hands of a specific owner. When this is the purpose, the resulting value should appropriately be termed "strategic value" rather than fair market value, and this value will incorporate the personal goodwill of the acquiring owner.)

As I noted, there are reasonable means to value identifiable intangible assets, generally based on cash flows, but there are market approaches (such as comparable royalty rates, cost to train/construct). Since this analysis significantly impacts fair market value, it must be done and either directly addressed in an appraiser's report, or included in the appraiser's work papers.

Appropriate valuation analysis can avoid potential Slater v Slater issues, when litigation is involved, and properly address value when a transaction is being proposed or negotiated.
DISCOUNTS AND PREMIA

Two concerns which must be resolved in order to appropriately develop fair market value estimates, regardless of valuation methodology applied, relate to the nature of the holding being valued, minority interest versus controlling interest, and the liquidity of the investment (i.e. marketability).

Minority Interest Discount and Controlling Interest Premium

When valuing minority interests, the appraiser must be aware of the basis on which the valuation approach rests. When using earnings or cash flows, are the earnings/cash flows those which a minority interest holder generally has access to, or do they reflect only those available to a controlling interest holder? A controlling interest holder can adjust financial structure, control dividends/distributions with regards to timing and amount, alter operating efficiencies, set compensation amounts, hire and fire employees, etc. A minority interest holder has no ability to control any of these issues, and they have influence on these issues only at the discretion of the controlling interest holder(s). The implication of this "control" issue is that if the entity is being valued based on control data, and/or cash flows associated with entire entity transactions' multiples, any minority interest valuation based on this "control" basis will need to be adjusted for the loss of value represented by the lack of control associated with a minority interest holder. This adjustment in value is called the minority interest discount. It is applied only to arrive at a minority interest value when the base value was derived from controlling interest assumptions and analyses. The reciprocal of this "minority interest" discount implies that if the value of a control interest is being developed from minority interest base information, a control premium must be applied to minority value base to properly value a controlling interest. For example, if a total entity value is being developed by referencing observed price/earnings multiples reported on publicly held stocks, the base information is minority interest observations. Price/earnings multiples reported on publicly traded stocks reflect per share, minority interest, prices. A share of stock is a minority interest. It is assumed that imbedded in this "market" price is a minority interest discount, and to properly value a controlling interest, a control premium must be applied to reflect control aspects.

Discount for Lack of Marketability

The other issue which must be considered in any fair market valuation is liquidity of an investment. When we develop values based on alternative, but freely tradable investments, then we have assumed a level of liquidity to the investment. The investor treasures liquidity. Liquidity, for minority interests, is generally defined as the ability to convert an investment to cash in three days. If you own a share of General Electric, you can call your broker, sell the share and retrieve your cash in a three day period. Liquidity is valued because it offers the investor an opportunity to withdraw from an investment in a timely manner, regardless of the reason. All things being equal, an investment is worth more if it is marketable than if it is not, because investors prefer liquidity over lack of liquidity. Lack of liquidity significantly increases the downside risk.

The Wall Street Journal, November 6, 1998, discussed current public markets suffering from low liquidity, even when an "active" market exists. The example cited concerned a
money manager's inability to market bonds issued by Merrill Lynch & Co. In August 1998, following the onset of the Russian financial crisis, professional money managers began fleeing securities with any risk. U.S. Treasury bonds became the investment of choice. In September 1998, the manager of Colonial Asset Management, attempted to sell $1 million of bonds issued by Merrill Lynch & Co. In a market where ordinarily $80 million of Merrill bonds trade on an average day, almost no market existed without discount. Current market value was, based on bond rating, terms, and face interest rate, anticipated at $104. The best offer was $98. This represents a discount of 5.8%, based purely on liquidity concerns (the basis for marketability discount). Liquidity in even high quality publicly traded securities, whether stocks or bonds, is a concern. Significantly reduced liquidity resulting from no public market is an even greater factor.

When an interest in an entity has no ready market, and its value has been developed by either comparison to freely tradable or even partially tradable interests, then the appraiser must be conscious of the diminution in value resulting from the lack of a ready market. This reduction, or adjustment, in value to reflect the relative illiquidity is called a discount for lack of marketability (DLOM), or just marketability discount. Empirical evidence supporting the existence of this discount and the level of the discount is available through numerous published studies.
Applying Kunze to Property Division
Update by Lauren Saucy, June 2013

Oregon law mandates that the allocation of property between spouses at the time of the divorce be “just and proper.” ORS 107.105(1)(f). In 2004, the supreme court clarified the analytical framework set forth by that statute in Kunze & Kunze, 337 Or 122, 92 P3d 100 (2004), breaking it down into a multi-step process.

a. Property Division – Preliminary Determinations

Under ORS 107.105(1)(f), the court may provide in a judgment of dissolution:

“For the division or other disposition between the parties of the real or personal property, or both, of either or both of the parties as may be just and proper in all the circumstances ***”

***
“(C) *** There is a rebuttable presumption that both spouses have contributed equally to the acquisition of the property during the marriage, whether such property is jointly or separately held.”

The first step is to determine into which class of property the specific asset falls. Two classes of property are created under ORS 107.105(1)(f). The distinction between these two classes is determined by when the asset at issue was acquired: before or after the parties’ wedding date. While all property is within the dispositional authority of the court, “marital assets” are the items of property that are acquired “during the marriage” and are therefore subject to the presumption of equal contribution, among other presumptions. ORS 107.105(1)(f)(C); In re Marriage of Stice & Stice, 308 Or 316, 325, 779 P2d 1020 (1989).
Cases often focus on whether a premarital asset increased in value during the marriage. That increase may itself be a marital asset. *In re Marriage of Massee & Massee*, 328 Or 195, 970 P2d 1203 (1999).

Additionally, the 2011 Legislature removed “property acquired by gift” from the class of marital assets subject to the presumption of equal contribution. This subclass of property includes assets acquired by “gift, devise, bequest, operation of law, beneficiary designation or inheritance.” ORS 107.105(1)(f)(D)(ii). Such property must be separately held by the party receiving it “on a continuing basis from the time of receipt.” ORS 107.105(1)(f)(D)(i). This is a legislative reversal of the court of appeal’s decision in *Olesberg & Olesberg*, 206 Or App 496, 502-504, 136 P3d 1202 (2006).

\[
\text{Asset} \\
\downarrow \text{Inheritance} \\
\downarrow \text{Marital asset} \\
\downarrow \text{(acquired during the marriage)} \\
\downarrow \text{Apply presumption of equal contribution} \\
\downarrow \text{Divided with no presumptions}
\]

\[b. \text{ Property Division – Presumption of Equal Contribution} \]

The presumption of equal contribution is rebuttable. The party seeking to overcome the presumption “has the burden of proving by a preponderance of the evidence that the other spouse’s efforts during the marriage did not contribute equally to the acquisition of the disputed marital asset.” *Kunze*, 337 Or at 134. In assessing whether a party has satisfied that burden, the court must “consider both economic and noneconomic spousal contributions, including the contributions of a spouse as a homemaker.” *Id.*

“[T]he court first must determine the magnitude of each spouse’s overall contribution to the acquisition of marital assets from evidence in the record. . . .

“Once the court has determined each spouse’s overall contribution to the acquisition of marital assets, the court compares the respective contributions of the spouses. The ultimate question is whether the spouse seeking to rebut the presumption of equal contribution has proved, by a preponderance of the evidence, that the other spouse did not contribute equally to the acquisition of marital assets.” *Massee*, 328 Or at 205 (emphasis added).

The inquiry about whether a party has rebutted the presumption of equal contribution must focus on the circumstances surrounding the actual act of acquisition. Other considerations, such as whether assets have been commingled with the marital estate, are ordinarily not a consideration in the analysis of whether the statutory presumption of equal contribution has been
rebutted. *Kunze*, 337 Or at 142 n 12. The extent of subsequent commingling of a particular asset is relevant to the issue of rebutting the presumption only when the “act of commingling may preclude the court from identifying that spouse’s separate contribution with sufficient reliability to rebut the statutory presumption that both spouses have contributed equally to the disputed asset.” *Kunze*, 337 Or at 138.

If the presumption is not rebutted, in absence of other considerations, the appropriate division is an equal division. If a party establishes that the presumption of equal contribution is rebutted, that party is “presumptively . . . entitled to receive [that asset] separate from the property division unless other considerations require a different result.” *Kunze*, 337 Or at 145.

c. Property Division – Just and Proper

The third step in the analysis is really the heart of the dissolution because there are no fixed or rigid rules for dividing property, nor is there a particular mathematical formula for the court to follow. After the court has made “its preliminary determination of the appropriate division of the marital assets by applying the statutory presumption[s]” (ORS 107.105(1)(f)), the court must then consider what division of all property, including premarital, inherited, jointly acquired, or otherwise, is “just and proper in all the circumstances.” *Id* at 135. “By contrast to the focus upon the parties’ respective contributions under the statutory presumption, the court’s final inquiry as to the “just and proper” division concerns the equity of the property division in view of all the circumstances of the parties.” *Id*. Equitable considerations may include, among other things:

1. Preservation of assets;
2. Achieving economic self-sufficiency;
3. Needs of the parties and children; and
4. **Commingling**—“the extent to which a party has integrated a separated asset into the common financial affairs of the marital partnership.”

Commingling in particular is a common consideration in the just and proper evaluation. In determining whether an asset has been sufficiently commingled such that an asset may be brought back into the marital division, the court’s main focus should be placed on the intent of the parties. Intent can be demonstrated in a number of ways, including but not limited to: “(1) whether the disputed property was jointly or separately held; (2) whether the parties shared control over the disputed property; and (3) the degree of reliance upon the disputed property as a joint asset.” *Kunze*, 337 Or at 141.

Finally, the court must evaluate whether, under all the circumstances, any inequity would result from the award of the asset to that spouse as separate property. *Id.*

The following chart is illustrative of the complete analysis:

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**d. Property Division Under Kunze**

1. When was property acquired?
   - Before marriage? (Court considers only what is “just and proper”)
   - After marriage? (Rebuttable presumption of equal contribution)
     - Gift/Inheritance? (Excluded from presumption) ORS 107.105(1)(f)(D)
     - Contributed equally to acquisition? (Equal division)
Unequal acquisition? (Court considers only what is “just and proper”)

- Absent other considerations, it is “just and proper” to award asset separately to the party who has overcome the presumption?

- Unequal acquisition can still be divided if any of the following concerns are overriding with regard to a particular asset:
  
  - Consider economic and non-economic contributions (e.g. homemaker; willingness to relocate, etc.).
  - Consider commingling if it affects one side’s ability to identify his/her separate contributions.

2. What is ultimately fair?

- Social and financial objectives of dissolution
- Preservation of assets
- The achievement of economic self-sufficiency for both parties
- Particular needs of the parties and their children
- Commingling – “The extent to which a party has integrated a separately acquired asset into the common financial affairs of the marital partnership through commingling”
The mortgage debt relief provisions for homeowners in the federal tax code, first enacted in 2007, expired at midnight on December 31, 2012. But the fiscal cliff bill enacted at the 13th hour by the Congress extended the relief through the end of 2013.

Because there are still huge numbers of financially distressed homeowners with underwater mortgages, this was one of the biggest issues in the fiscal cliff debate. Had Congress not acted, the tax code would have reverted to its pre-2007 treatment of mortgage principal reductions or cancellations by lenders, whether through loan modifications, short sales, deeds-in-lieu, or foreclosures.

That means that all principal balances unpaid by the homeowner and forgiven by the lender would have been treated as ordinary income to the homeowner. For example, if a lender wrote off $200,000 of mortgage debt to facilitate a loan modification or short sale, the borrower or seller would have been taxed on that $200,000 at regular marginal rates, just as if he or she had earned it as wages.


For further discussion of foreclosures, short sales, and loan modifications, see California Mortgages, Deeds of Trust, and Foreclosure Litigation, chaps 2, 7, and 10 (4th ed Cal CEB).

For further information on CEB’s real property titles, click on the link below.
http://ceb.com/info/Productlistrp.asp
"Bankruptcy often follows divorce, and bankruptcy can wreak havoc on the expectations of a family law lawyer." The Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (BAPCPA) was designed to reduce the impact of bankruptcy filings on domestic relations cases and judgments. This article reviews the 2005 changes in the bankruptcy law that most directly affect domestic relations and discusses some of the cases that have interpreted those provisions.

I. Expansion of What Constitutes Support Obligations - "Domestic Support Obligations"

The Bankruptcy Code historically divided domestic relations obligations into two categories, “alimony, support and maintenance” and “non-support” obligations. The Code treated the former better than the latter in many respects, including discharge and the right to priority in distribution of the bankruptcy estate.

The 2005 amendments expanded the scope of the domestic relations obligations that get preferred bankruptcy and post-bankruptcy treatment. BAPCPA introduced a newly defined term, the “Domestic Support Obligation” (“DSO”). 11 U.S.C.
The term DSO is significantly broader than “alimony, support and maintenance.” However, courts differ in how broadly they interpret the term. For example, in Wisconsin Dep’t of Workforce Development v. Ratliff, 390 B.R. 607 (E.D. Wis. 2008), the court uses the very broad definition of DSO when it held that a debt owed to a governmental unit for overpayment of food stamps was a DSO. By contrast, in In re Hickey, 473 B.R. 361 (Bankr.D.Or. 2012), the court determined that overpayment of food stamps “is a debt for the return of a benefit paid to the Debtor which should not have been paid in the first place. As such, [it] . . . does not constitute a domestic support obligation for purposes of § 523(a)(5).”

There are four requirements that must be satisfied for a debt to be a DSO. The first requirement relates to the identity of the payee - the debt must be “owed to or recoverable by: (i) a spouse, former spouse, or child of the debtor or such child’s parent, legal guardian, or responsible relative; or (ii) a governmental unit.” § 101(14A)(A)(emphasis added). Second, the debt must be “in the nature of alimony, maintenance or support . . . of such spouse, former spouse, or child of the debtor or such child’s parent.” § 101(14A)(B)(emphasis added). Third, the debt must be established by a separation agreement, divorce decree, property settlement, court order, or administrative determination. § 101(14A)(C). Fourth, a nongovernmental
assignee can seek recovery only if the spouse, child, parent, legal guardian, or other responsible relative voluntarily assigned the obligation to that entity for the purpose of collecting the debt. § 101(14A)(D).

The majority of courts addressing how strictly to enforce the requirement that the DSO “be owed to or recoverable by: (i) a spouse, former spouse, or child of the debtor or such child’s parent, legal guardian, or responsible relative; or (2) a governmental unit” have held that the term may include debts payable directly to a third party. See In re Kassicieh, 452 B.R. 467 (Bankr.S.D.Ohio 2010) (collecting cases holding that debts payable directly to third parties may be classified as DSOs and cases holding the opposite).

Several Oregon cases have held that pre-BAPCA cases interpreting the meaning of “alimony, maintenance and support” are relevant. There is a pre-BAPCPA Ninth Circuit Court of Appeals decision that broadly interprets the “alimony, maintenance and support” to include support-type items payable to entities other than those specified in the statute. See In re Chang, 163 F.3d 1138, 1141 (9th Cir. 1998). In Chang, the court held that the identity of the payee did not matter when the amounts payable were in the nature of support for a child. Id. The Ninth Circuit did not consider the identity of the payee critical even though prior to BAPCPA the Bankruptcy Code required

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that, in order for an obligation to be support, it had to be payable to “a spouse, former spouse, or child of the debtor.” § 523(a)(5); Chang, 163 F.3d at 1141. Chang would support applying the same broad reading to DSOs.

Not every obligation between former spouses, and not every payment by a parent for the benefit of a child, qualifies as a DSO. In In re Tracy, 2007 WL 420252 (Bankr. D. Ida. 2007), a non-debtor spouse was awarded a residence in a divorce from the debtor. He then rented the residence back to the debtor. The debtor failed to pay the rent as agreed and filed bankruptcy. The bankruptcy court denied the former husband’s assertion that his claim should be a DSO, because the debt was not “incident to” the divorce. Likewise, a parent who had agreed in his dissolution decree to provide support for his daughters, including college expenses, was not entitled to credit against his DSO for amounts paid for car payments, car insurance, and a trip to Italy for his college student child because, under the facts presented, these items were considered gifts. In re Van Nice 2007 WL 2178069 (Bankr. D. Mont. 2007).

The treatment of DSOs during and after bankruptcy is explored below.

II. Effect of Bankruptcy on State Court Proceedings - The Automatic Stay
The automatic stay is fundamental to the bankruptcy process. It stops most creditor actions to collect debts from the debtor and protects property of the estate. § 362.

Prior to BAPCPA, the automatic stay did not apply to three types of domestic relations proceedings against the debtor: (1) proceedings to establish paternity, (2) proceedings to modify support, and (3) proceedings to collect support from property that is not property of the estate. § 362(b)(2). BAPCPA revised these exceptions by substituting the broader DSO for the term “alimony, support and maintenance.” BAPCPA excepted from the automatic stay eight additional domestic relations proceedings and procedures:

1. child custody or visitation proceedings;
2. divorce proceedings, except to the extent that such proceeding seeks to divide property of the estate;
3. domestic violence proceedings;
4. withholding of income that is property of the estate or the debtor for payment of a DSO;
5. withholding, suspending, or restricting a driver’s, professional, occupational, or recreational license under state law as specified by § 466(a)(16) of the Social Security Act;
6. reporting of overdue support owed by a parent to any consumer reporting agency as specified by § 466(a)(7) of the Social Security Act;

7. intercepting a tax refund as specified in §§ 464 and 466(a)(3) of the Social Security Act or under analogous state law;

8. enforcing a medical obligation as specified under Title IV of the Social Security Act.

§ 362(b)(2)(A)-(G). As a result of these changes, the automatic stay does not stay domestic relations litigation and collection efforts as frequently as it did before BAPCPA.

III. Discharge of Obligations in Bankruptcy

Individuals can file several different types of bankruptcy cases. Chapter 7 is a liquidation case; the debtor gives up his or her non-exempt property and it is liquidated for the benefit of his or her creditors. §§ 701 - 784. Chapter 13 allows individuals with a regular source of income to propose and implement a debt repayment plan. §§ 1301 - 1330. Chapter 12, which is very similar to chapter 13, is the family farmer reorganization chapter. §§ 1201 - 1231. Chapter 11 is a reorganization procedure that is typically used by businesses but increasingly also by individuals. §§ 1101 - 1174. Because chapter 11 is complex and costly, it is usually used by individuals only if they are ineligible for relief under chapters
12 and 13 because the amount of their debts exceed the applicable limits.

The primary objective of most individual bankruptcy debtors is to discharge as much debt as possible. BAPCPA further reduced the ability to discharge debts imposed by family law, thus reducing (but not eliminating) the potential that family obligations would be eliminated through bankruptcy.

A. Chapters 7, 11, 12

At the inception of the Bankruptcy Code in 1979, domestic relations support obligations owed to a spouse, former spouse, or child of debtor were nondischargeable. The pertinent code section, § 523(a)(5), has been amended to expand the scope of what support obligations are nondischargeable. All debts defined as DSOs are nondischargeable. Thus, support obligations owed to a child’s parent, legal guardian, responsible relative, a government agency, or a nongovernmental entity that has been voluntarily assigned the debt are all now nondischargeable. Property settlements and administrative determinations by governmental units have been added to the documents that can be used to establish the existence of DSOs.

In 1994, Congress added property division and other non-support domestic obligations to the list of debts that were nondischargeable in a chapter 7, 11, or 12 bankruptcy if certain

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conditions were met. The debt had to be owed to a spouse, former spouse, or child of a debtor in connection with a domestic relations proceeding and could not fit the definition of “alimony, maintenance or support.” The debtor had to have the ability to pay the debt and the bankruptcy court had to find that the harm to the debtor in paying the debt was less than the harm to the spouse or child if the debt went unpaid. § 523(a)(15) (1993 & Supp. 1995). BAPCPA simplified and streamlined § 523(a)(15). The ability to pay and balancing test were eliminated. Non-support domestic relations obligations are now on an equal footing with support obligations and are also nondischargeable. Additionally, the pre-BAPCPA short statute of limitations for commencing an adversary proceeding in the bankruptcy court to determine the dischargeability of such a debt was eliminated. § 523(c); Fed. R. Bankr. P. 4007(c). There is no longer a statute of limitations on § 523(a)(15) actions provided by the Bankruptcy Code or rules.

The bankruptcy court and the state court now have concurrent jurisdiction to determine whether such a debt is nondischargeable. Counsel will need to remember that the change in the law does not eliminate the need to obtain a judgment determining nondischargeability to prevent any claims that post-bankruptcy collection efforts violate the discharge injunction. § 524(a). The bankruptcy trustee is not a
necessary party in a nondischargeability action, because administration of the estate is not affected by the scope of the discharge the debtor obtains.

Although the nondischargeability action can be commenced in the bankruptcy court without relief from the automatic stay, In re Roxford Foods, 12 F.3d 875, 878 (9th Cir. 1993), relief from the stay should be obtained if the action is going to be filed in the state court before the automatic stay terminates. See § 362(c)(setting out when the automatic stay terminates).

B. Chapter 13

Under chapter 13, individual debtors meet their bankruptcy obligations by voluntarily performing a debt payment plan. Both before and after BAPCPA, a chapter 13 debtor who completes his or her plan discharges non-support domestic obligations. Thus, the domestic relations practitioner will want to remember that bankruptcy can still substantially alter how much may be collectable on a property or debt division judgment that is not support.

Collection of an unsecured non-support domestic obligation during a chapter 13 will be limited by how much is payable under the chapter 13 plan. Such plans last only three to five years and there are often numerous priority and secured debts to pay, leaving little left for unsecured debts, including non-support domestic obligations.

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IV. Changes in the Bankruptcy Code that “Encourage” Debtors to Perform their DSOs

A. Chapter 11, 12, and 13 debtors cannot confirm a plan or obtain a discharge without being current on all DSOs that become due after debtor files bankruptcy

Chapter 11, 12, and 13 cases involve debt repayment plans that often last several years. BAPCPA “encourages” these debtors to remain current on their post-bankruptcy filing DSO obligations (“postpetition DSO”) in two ways. First, Chapter 11, 12, and 13 debtors cannot obtain confirmation of a repayment plan unless the debtor has paid all DSOs that became due postpetition. §§ 1129(a)(14), 1225(a)(7), 1325(a)(8). Second, in chapters 12 and 13, BAPCPA requires debtors to certify that all postpetition DSOs have been paid in order to receive a discharge, which typically is not for three to five years after a case is filed. §§ 1228(a), 1328(a).

B. A Chapter 11, 12, or 13 debtor who fails to pay postpetition DSOs may not be able to remain in bankruptcy

BAPCPA amended the Bankruptcy Code to expressly provide that failure of a chapter 11, 12, or 13 debtor to pay a postpetition DSO is cause for dismissal of the bankruptcy case or conversion to chapter 7 liquidation. §§ 1112(b)(4)(P), 1208(c)(10), 1307(c)(11). Generally, such conversion or dismissal will occur

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only if an interested party brings the default to the court’s attention through a motion to dismiss or convert.

C. The Bankruptcy Code Means Test, Disposable Income, and Family Law

BAPCZA introduced, for the first time, a provision that largely eliminates the option of chapter 7 relief for debtors whose debts are primarily consumer debts and who are able to pay a specified minimum amount to creditors.\textsuperscript{14} § 707(b)(2). This is commonly referred to as the “means test.” Debtors who cannot pass the means test, and who want relief under the Bankruptcy Code, must use chapter 11, 12, or 13, all of which require that the debtor commit three to five years of their \textit{projected disposable income} to fund a creditor payment plan. §§ 1129(a)(15), 1225(b)(1)(C), 1325(b)(1)(B). While calculating the amount of the debtor’s income and expenses for purposes of applying the means test and determining disposable income is an extremely complex endeavor beyond the scope of this article, it is worth noting that not all debtors will have the option of using chapter 7 because they cannot pass the means test. Obligations imposed pursuant to family law play a role in the means test calculations.

In chapter 7 cases, when calculating the debtor’s disposable income, child support and spousal support received by the debtor or the debtor’s spouse are included as income. Official
Bankruptcy Form B22A, lines 8 and 10; §§ 707(b)(2)(A)(i), 101(10A). Monthly expenses, which are deducted from income to determine the debtor’s disposable income, include the monthly amount of any court-ordered child and spousal support plus 1/60 of the amount of any past due DSO. Official Bankruptcy Form B22A, lines 28, 44; § 707(b)(2)(A)(ii), (iv). Chapter 12 follows a similar approach when calculating disposable income. § 1225(b). A debtor who is paying support without a court order may seek to claim such support as an expense by demonstrating special circumstances, Official Bankruptcy Form B22A, line 56; § 707(b)(2)(B). See In re Littman, 370 B.R. 820 (Bankr.D.Id. 2007). It is questionable whether such a deduction is permitted because the Ninth Circuit Court of Appeals has held that in order to qualify as a “special circumstance,” such circumstances must “not only put a strain on a debtor’s household budget, but they [must] arise from circumstances normally beyond the debtor’s control.” In re Egebjerg, 574 F.3d 1045, 1052-52 (9th Cir. 2009).\(^\text{15}\)

Chapters 11 and 13 are more generous to the debtor spouse in that they exclude from income “child support payments, foster care payments, or disability payments for a dependent child . . . to the extent reasonably necessary to be expended for such child,” and the amounts reasonably necessary to support the debtor’s dependents and pay any DSO that is first payable after 2013 Revised Draft
the bankruptcy petition is filed. Official Bankruptcy Form B22C, lines 54 and 60; §§ 1325(b)(2), 1129(a)(15)(B). Like chapter 7, in chapters 11 and 13, the debtor can deduct the monthly amount of current DSOs plus 1/60 of the amount of any past due DSO in calculating disposable income. Official Bankruptcy Form B22C, lines 33, 49; §§ 1325(b)(2)(A)(i), 1129(a)(15)(B). As a result of the difference in how income is calculated, given the same facts a debtor may have a lower disposable income in chapters 11 and 13 than the debtor would in chapter 7. Less disposable income means less money is available for creditors.

V. Treatment of DSOs in the Administration of Bankruptcy Cases

Under the 2005 amendments, certain DSOs have advanced from the seventh priority to the first priority in the distribution of the bankruptcy estate. § 507(a)(1). To qualify for priority treatment the DSO must be both unsecured and a prepetition claim. Id. There are two tiers of DSOs within the first priority. DSOs owed to a spouse, former spouse, child, or their representative (identified in the statute) comes ahead of certain claims for assigned DSOs filed by governmental units. § 507(a)(1)(A) and (B).

Only the bankruptcy trustee and the trustee’s agents will be paid ahead of a priority DSO. § 507(a)(1)(C). This is a practical recognition that it is necessary to pay the trustee if there is going to be any distribution. This provision will
likely discourage attorneys from providing bankruptcy representation to debtors with substantial DSOs, unless attorney fees are paid in full before the case is filed.

In a chapter 7 case, creditors are paid in the order of their priority. § 726. This is not necessarily true in chapter 11, 12, or 13 cases. In re Boler, 2008 U.S. Dist. LEXIS 5131, *4 (M.D. Ala. Jan. 24, 2008).

Generally, a chapter 11, 12, or 13 plan must provide for payment in full of priority claims in order to be confirmed. §§ 1129(a)(9)(B), 1222(a)(2), 1322(a)(2). There is a limited exception in Chapters 12 and 13 for DSOs assigned to governmental units, but only if the debtor proposes a five year plan dedicating all projected disposable income. §§ 507(a)(1)(B), 1222(a)(4), 1322(a)(4). The payment of the priority DSO through a plan is usually made in installments, over several years, often concurrently with the payment of other creditors. This is not changed by the amendments.

As a general rule, trustees have the power to avoid preferential transfers that were made by a debtor to a creditor within 90 days before a bankruptcy petition was filed. § 547(b). Before BAPCPA, bankruptcy law excepted from this rule transfers made as payments of domestic relations support obligations. BAPCPA expanded the types of domestic relations support obligations that a trustee may not avoid under § 547(c)(7) by
substituting the term DSO for “alimony, maintenance and support.”

See § 547(c)(7).

BAPCPA imposed a new duty on chapter 7, 11, 12, and 13 trustees to send certain notices to DSO claimants. Trustees are required to give DSO claimants and child support enforcement agencies two different notices at different times in the case. Both notices contain information that will assist DSO claimants in the collection of their DSOs from the estate and the debtor. See § 704(c)(1), § 1106(c)(1), § 1202(c)(1) and § 1302(d)(1).16

VI. DSO’s and Exempt Property

In administering bankruptcy cases in Oregon, the exemptions available under Oregon law and non-bankruptcy federal law apply. Section 522(c)(1) was amended by BAPCPA to provide that, after bankruptcy, exempt property remains liable for DSOs. This section preempts any state law to the contrary.

This amendment raised the question of whether the bankruptcy trustee could liquidate the debtor’s homestead and other exempt property to satisfy a DSO, even though state law might not allow liquidation of such property.17 Thus far, all of the courts that have considered that question, including one in Oregon, In re Ruppel, 368 B.R. 42 (Bankr. D. Or. 2007), have held that section 524(c)(1) does not give the trustee the right to liquidate exempt property to satisfy a DSO. See Brown, Bankruptcy and Domestic Relations Manual § 10.11 (2010) (cases compiled in n. 5).
VII. Domestic Relations Attorneys May Be Debt Relief Agencies Subject to Bankruptcy Code Requirements

The Bankruptcy Code now regulates the conduct of “debt relief agencies” (hereafter DRA). A DRA includes “any person who provides any bankruptcy assistance to an assisted person in return for the payment of money or other valuable consideration . . .” § 101(12A). Under this definition, attorneys providing “bankruptcy-related services” to consumer debtors are debt relief agencies. Milavetz, Gallop & Milavetz P.A. v. U.S., 130 S.Ct. 1324 (2010).

Attorneys who are DRAs are restricted in giving certain types of advice to their clients, § 526, must provide specific disclosures to the client, § 527, and must comply with certain requirements with respect to their advertising and fee agreements, § 528. While a discussion of the detailed restrictions is beyond the scope of this article, one of difficult aspects of § 526 is that DRAs are prohibited from advising a client to incur more debt. § 526(a)(4). However, the Supreme Court interpreted this limitation relatively narrowly, holding that a DRA is limited “only from advising a debtor to incur more debt because the debtor is filing for bankruptcy, rather than for a valid purpose.” Milavetz, 130 S.Ct. at 1336 (2010).

Conclusion

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BAPCPA significantly reduced, but hardly eliminated, the impact that a bankruptcy filing will have on domestic relations obligations and proceedings. Financially overburdened domestic relations clients will need to be advised regarding how limited their bankruptcy options are before they undertake obligations in a dissolution decree. Attorneys giving such advice need to consider whether they are DRAs and, if so, they must comply with the restrictions applicable to DRAs.

1. Hon. Elizabeth L. Perris is a United States Bankruptcy Judge for the District of Oregon. Juliet M. Kaestner was a law clerk to Judge Perris in during 2005 and 2006 when this article was originally written. This article initially appeared in the OSB Family Law Newsletter, Vol. 24, No. 3, August 2005. Margot Lutzenhiser was a law clerk to Judge Perris and assisted in the 2009 update of this article. Bethany Coleman-Fire is a law clerk to Judge Perris and assisted in the 2013 update of this article.


3. Most of the provisions in the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 became effective on October 17, 2005 and apply to bankruptcy cases filed on or after that date.

4. All statutory references are to the Bankruptcy Code, 11 U.S.C. §§ 101 et seq.

5. Wisconsin Dept. Of Workforce Development v. Ratliff, 390 B.R. 607, 613-614 (E.D. Wis. 2008), discusses the four requirements that must be satisfied before an obligation is a DSO.

6. It is questionable whether Oregon’s recognition of same sex registered domestic partners as having the benefits of marriage under the Oregon Family Fairness Act [Or. Laws 2007 c. 99, § 9(1)] would make obligations imposed pursuant to those provisions DSOs, because the federal Defense of Marriage Act (DOMA) provides

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that, “[i]n determining the meaning of any Act of Congress . . . the word ‘spouse’ refers only to a person of the opposite sex who is a husband or a wife.” 1 U.S.C. § 7. Compare In re Kandu, 315 B.R. 123 (Bankr. W.D. Wash. 2004) (holding that a married same sex couple could not qualify to file a joint bankruptcy petition because, under DOMA, their marriage is not recognized by federal law) with In re Balas, 449 B.R. 567 (Bankr. C.D. Cal. 2011) (holding DOMA unconstitutional and allowing a same-sex couple to pursue their joint petition).


8. Debts that are nondischargeable under § 523(a) are nondischargeable in chapters 7, 11, and 12. §§ 523(a), 727(b), 1141(d), 1228(a).

9. Before BAPCPA, section 523(a)(5) provided that a debt “to a spouse, former spouse, or child of the debtor, for alimony to, maintenance for or support of such spouse or child, in connection with a separation agreement, divorce decree or other order of a court of record” was nondischargeable. § 523(a)(5) (before 2005 amendment).

10. Before BAPCPA, separation agreements, divorce decrees and court orders could be used to establish nondischargeable support obligations. § 523(a)(5) (before 2005 amendment).

11. “Non-bankruptcy courts [had] concurrent jurisdiction to determine dischargeability on grounds other than those contained in paragraphs (2), (4), (6), and (15) of Code § 523(a) [before BAPCPA].” 4 William L. Norton Jr., Norton Bankruptcy Law and Practice § 47:67 (March 2005 Supplement). Under BAPCPA, paragraph (15) was eliminated from the previous sentence. See § 523(c)(1), as amended.

12. After discharge, an injunction protects a debtor against a creditor’s further efforts to recover a discharged debt as a personal liability of the debtor. 4 Lawrence P. King, Collier on Bankruptcy § 524.02 (15th ed. Rev. 2005).

13. If a debtor obtains a chapter 13 discharge after completing a plan, the debtor is able to discharge some debts that would be nondischargeable in chapters 7, 11, or 12. § 1328(a). This is commonly referred to as the “superdischarge,” but BAPCPA substantially eviscerates the superdischarge. If a Chapter 13 debtor is unable to complete his or her chapter 13 plan and is

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granted a hardship discharge under § 1328(b), all of the § 523(a) exceptions to discharge apply. §§ 523(a), 1328(b-c).

14. How much disposable income does an above-median income debtor have to have to fail the means test? The answer is that first one figures out the debtor’s disposable income for five years by multiplying the debtor’s monthly disposable income times sixty (60). Debtors whose disposable income equals or exceeds $11,725 fail the means test. § 707(b)(2)(A)(i)(II). Debtors whose disposable income is less than $7,025 pass the means test. § 707(b)(2)(A)(i)(I). For those debtors whose disposable income is between the two numbers, they will fail the means test if their disposable income equals or exceeds 25% of their unsecured claims not entitled to priority under the Bankruptcy Code. Id.

15. The Egebjerg case holds that repayment of a 401(k) loan was not a “special circumstance because such repayment was neither extraordinary nor rare.

16. The new notice duties of chapter 7, 11, 12, and 13 trustees are identical, except that the chapter 7 trustee has an additional duty to inform the DSO claimant of his or her rights to payment of the DSO. § 704(c)(1)(A)(iii).

17. ORS 18.398 provides that a homestead exemption may be denied under certain circumstances when the judgment being collected is for child support.
Bankruptcy and its Impact on Domestic Relations Practice

Ann K. Chapman
Vanden Bos & Chapman, LLP

Christopher N. Coyle
Vanden Bos & Chapman, LLP
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1. **Introduction**

Seven years after the enactment of the Bankruptcy Abuse Prevention and Consumer Protection Act ("BAPCPA"), bankruptcy practitioners have settled into the new reality created on October 17, 2005 (BAPCPA’s effective date). While a few recent Supreme Court decisions have shed considerable light on the changes wrought by BAPCPA, the majority of the changes have only been addressed by lower courts. As a result, there is a surplus of potential resolutions for many bankruptcy questions with few binding precedents for practitioners to rely. The changes from BAPCPA have been magnified by the continued economic woes forcing many individuals and business into bankruptcy and new practitioners (on both debtor and creditor sides) entering the fray. Despite all these changes, some constants remain: 91% of bankruptcy filers have suffered a job loss, medical event or divorce and 40% of bankruptcies result from medical crises, unemployment or divorces.\(^1\) At the same time, financial stress is attributed as a leading cause of divorce. As more individuals are divorced\(^2\) and more are experiencing financial stress\(^3\), the convergence of bankruptcy and divorce issues has never been greater.

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\(^1\) Elizabeth Warren, et al., The Fragile Middle Class: Americans in Debt (Yale University) (2000).

\(^2\) 10% of the population is divorced, up from 8% in 1990 and 6% in 1980. U.S. Census Bureau

\(^3\) See the economy.
2. **Congratulations - You may be a Debt Relief Agency: Your Obligations under the Bankruptcy Code.**

In some instances, a domestic relations lawyer may provide bankruptcy-related advice; under BAPCPA, there are additional burdens placed upon the attorney with respect to bankruptcy-related advice.

To start with, a “Debt Relief Agency” ("DRA") is deemed to be “Any person who provides any bankruptcy assistance to an assisted person in return for the payment of money or other valuable consideration, or who is a bankruptcy petition preparer under section 110...” 11 U.S.C. § 101(12A) (italics added). This definition includes attorneys, both those that provide direct bankruptcy representation and those who do not practice before the Bankruptcy Court but that advise clients about dischargeability of obligations and/or whether to file bankruptcy. *Milavetz, Gallop & Milavetz, P.A. v. United States*, 130 S. Ct. 1324, 1332-34 (2010) (holding that attorneys were within the definition of DRA); see also *Olsen v. Gonzales*, 350 B.R. 906 (D. Or. 2006) (including family law practitioner as plaintiff regarding BAPCPA’s requirements regarding DRAs).

“Assistance” is further defined as “any goods or services sold or otherwise provided to an assisted person with the express or implied purpose of providing information, advice, counsel, document preparation, or filing, or attendance at a creditors’ meeting or appearing in a case or proceeding under this title” 11 U.S.C. §

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4Exempt are persons who are officers, directors, employees or agents of the person who provides such assistance or of the bankruptcy petition preparer. Also exempt are 501(c)(3) non-profit organizations, a creditor of an assisted person who is assisting in restructuring a debt owed to the creditor, depository institutions, Federal credit unions or State credit unions, authors, publishers, distributors, or sellers of copyright works when acting in such capacity.
101(4A) (italics added). Furthermore, an assisted person is “any person whose debts consist primarily of consumer debts and the value of whose nonexempt property is less than $150,000.” 11 U.S.C. § 101(3) (italics added).

The obligations on DRAs include:

(1) Section 526(a) requires that a Debt Relief Agency may not fail to perform any promised services, make any untrue or misleading statements, misrepresent as to the services to be provided or the risks and benefits of filing bankruptcy, or advise the debtor to incur more debt in contemplation of filing bankruptcy. The prohibition on “advis[ing] the debtor to incur more debt” has been limited to those circumstances in which the “impelling reason for the advice is the anticipation of bankruptcy.” Milavetz, 130 S. Ct. at 1337.

(2) Section 527 requires that a DRA must provide a number of requisite disclosures. These include the written notice from the court clerk that provides descriptions of Chapters 7, 11, 12, and 13, the types of services available from credit counseling agencies, and warnings concerning fraudulent or false statements; a sample is included as Appendix 1. The DRA is also required to provide disclosures with respect to asset valuation, the methodology of determining disposable income, the listing of creditors, and determination of exemptions; a sample is included as Appendix 2.

(3) Section 528 requires that, within five days of providing information to an "assisted person", you are required to execute a written contract
explaining the services to be provided and the cost for these services and provide a copy of the executed contract to the debtor. In addition, in any advertisement of bankruptcy-related services, certain disclosures must be made. 11 U.S.C. § 528; Olsen, 350 B.R. at 919.

3. The Nature of the Claim: Domestic Support Obligations, Property Settlements and Other Obligations.

Pre-BAPCPA, whether labeled as alimony or property settlement, debts that were in fact in the nature of alimony, maintenance, or support were nondischargeable. This included attorney fees awarded that were directly related to child support or alimony. The new law has lumped together all types of these Section 523(a)(5) obligations under the definition of domestic support obligations (DSO) and made them nondischargeable. A DSO is now defined as a debt that is:

1. “[O]wed to or recoverable by — . . . a spouse, former spouse, or child of debtor or such child’s parent, legal guardian, or responsible relative . . . or a governmental unit”;

2. “[I]n the nature of alimony, maintenance or support . . . of such spouse, former spouse, or child of the debtor or such child’s parent, without regard to whether such debt is expressly so designated”; and

3. “[E]stablished . . . by reason of applicable provisions of — . . . a separation agreement, divorce decree, or property settlement agreement; . . . an order of a court of record”; or an administrative determination. 11 U.S.C. § 101(14A)(A)–(C).
In the past, Section 523(a)(5) spawned a lot of litigation where clever domestic relations lawyers would attempt to label property settlements alimony (to avoid discharge in bankruptcy) and alimony as property settlements (to avoid taxation by the recipient). The bankruptcy court was generally willing to look at the actual purpose of the award and discern whether it is in the nature of support or alimony or is actually property settlement; “the court must look beyond the language of the decree to the intent of the parties and substance of the obligation.”  Shaver v. Shaver, 736 F.2d 1314 (9th Cir. 1984). By contrast, state courts were less often willing to look beyond labels, particularly when the property settlement agreement was a negotiated one, and were more likely to leave labels alone and enforce the intent of the parties based upon their choice of labels.

In looking beyond the labels, some of the factors which can be considered to determine whether a debt is in the nature of alimony or support include (i) labels in the agreement; (ii) income and needs of the parties at the time of the obligation; (iii) amount and outcome of property division; (iv) whether the obligation terminates on death; (v) number and frequency of payments; (vi) whether there was a waiver of alimony or support rights in the agreement; (vii) whether there are state court procedures to modify the obligation or enforce it through contempt; and (viii) the tax treatment of the obligation. Our own court just recently published a very comprehensive opinion regarding distinguishing DSOs from property settlements and evaluating the above factors.  Erik v. Nelson, 451 B.R. 918 (Bankr. D. Or. April 22, 2011) (determining a hold-harmless obligation regarding a mortgage, despite some labeling as a DSO, was most properly categorized as a property settlement).  Erik should be contrasted with In re
Maitlen, wherein the 7th Circuit determined the obligation of a debtor to pay a mortgage on the ex-spouse’s home was in the nature of support because the payment was designed to provide support for the ex-spouse. In re Maitlen, 658 F.2d 466 (7th Cir. 1981).

If a debt to a spouse, former spouse, or child is not of the kind described as a DSO, then it may be of the type referred to in Section 523(a)(15) (generally referred to as a "property settlement"). These debts are owed a spouse, former spouse, or child, not of the kind described as a DSO and incurred by the debtor in the course of a divorce or separation or in connection with a separation agreement, divorce decree or other order. 11 U.S.C. § 523(a)(15). This definition encompasses the classic property settlement where one party receives property of the marital estate in exchange for a payment of a sum of money to the other spouse.

A property settlement may be treated much differently than a DSO. The balancing test (basically, which party was poorer) previously used under Section 523(a)(15) to determine if some obligations not related to alimony, maintenance, or support were dischargeable in Chapter 7 has been eliminated. Obligations under 523(a)(15) are nondischargeable in Chapter 7 and in a Chapter 13 "hardship" discharge under Section 1328(b). Such debts are dischargeable in a Chapter 13 in which a debtor receives a normal discharge under Section1328(a). As a result, a client who accepts a larger property settlement instead of a domestic support obligation can be significantly disadvantaged if the former spouse files a Chapter 13 bankruptcy, confirms their plan, completes their proposed plan (which will treat the property settlement as a general unsecured obligation), and receives their discharge.
Finally, a debt may be owed to a spouse, former spouse, or child which is neither a DSO or a property settlement (as defined above). For example, John and Jane are a married couple; both are liable to Bank on an unsecured line of credit. If, prior to a dissolution, John were to file a Chapter 7 bankruptcy, he would be able to discharge his obligation to Bank and his obligation to Jane (for contribution). Then, going into a dissolution, Jane would be the only party liable on the unsecured line of credit. If John and Jane had first been through a dissolution, the divorce decree could assign liability to either party (or both). Assume John was to indemnify Jane, then, going into a bankruptcy, while John could discharge his obligation to the Bank, the obligation to Jane would be nondischargeable in his Chapter 7 as a property settlement under Section 523(a)(15) (but would be dischargeable if John had instead filed under Chapter 13 (11 U.S.C. § 1328(a)). For John, the change in timing of the Chapter 7 bankruptcy filing eliminates some or all of the benefit of a bankruptcy as to the Bank obligation (i.e. the Bank can pursue collection against Jane who can then collect from John).

If a property settlement has not been entered at the time of case filing, it cannot be discharged in bankruptcy. To be a pre-petition obligation, the property settlement must arise before the filing of the bankruptcy case. See, e.g., Arleaux v. Arleaux, 210 B.R. 148 (8th Cir. 1997); In re Miller, 246 B.R. 559 (E.D. Tenn. 2000); In re Berlingeri, 246 B.R. 196 (N.J. 2000); In re Gomez, 206 B.R. 663 (E.D.N.Y. 1997) (cases in a dissolution proceeding was filed and, prior to a property settlement judgment, a bankruptcy was filed).

If the property settlement is entered prior to the bankruptcy being filed (and regardless of whether the dissolution proceeding has completed), in some jurisdictions it
may be considered to be a pre-petition debt and may be dischargeable (in Chapter 13 only). See, e.g., In re Rudy, 2005 Bankr. LEXIS 2834 (E.D.Va. 2005) (a property settlement entered in a dissolution, which was still on-going as to other issues, was dischargeable in bankruptcy filed after settlement entered). Finally, a property settlement stipulation which was read into the record but not yet entered into a judgment was held to be dischargeable. In re Anjum, 288 B.R. 72 (S.D.N.Y. 2003).5

What about obligations that arise post-bankruptcy but pre-plan confirmation in Chapter 13? Unlike the discharge in Chapter 7, which discharges "all debts that arose before the date of the order for relief," Chapter 13 discharges "all debts provided for by the plan." 11 U.S.C. §§ 727, 1328. A debtor may not provide for a post-petition debt that is not the subject of a properly filed and allowed post-petition proof of claim absent creditor consent. E.g. In re Laymon, 360 B.R. 902 (E.D. Ark. 2007). Narrow exceptions are found in Section 1305 for some post-petition taxes and specific consumer debts. Those consumer debts are limited to those necessary for debtor's performance under the plan and for which prior approval could not be sought. In addition, a post-petition claim must be voluntarily filed by the entity holding the claim. In re Cleveland, 349 B.R. 522 (E.D. Tenn. 2006) (citing 8 Collier on Bankruptcy 1322.10 (5th Ed. Rev. 2005)). Since a property settlement would not fit within either category of Section 1305 claims, it would not be possible for a bankruptcy plan to provide for a post-petition obligation that arises under a divorce decree.

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5 This case has been included as a warning not to enter into a stipulation for a property settlement to be entered later; without an analysis of New York domestic relations law and a comparison to Oregon's law as to both effectiveness and jurisdiction, it is unclear as to the persuasiveness of this case. While Daywalt v. Bertrand, 10 Ore. App. 418 (1972), may be sufficient to establish that there are no rights (and thus no claim) until the judgment is entered by the court, a conservative approach advises against either (1) stipulating a property settlement prior to judgment and waiting until a bankruptcy is filed to have a judgment entered or (2) filing a property settlement judgment with an effective date after a (then-proposed) bankruptcy filing.
4. **The Estate and the Automatic Stay: What does the filing of bankruptcy mean (and when can you still proceed)?**

Immediately upon filing of any bankruptcy petition, whether voluntary or involuntary, an automatic injunction goes into effect which prevents most creditor actions against the debtor and the property of the estate. See 11 U.S.C. § 362. The bankruptcy estate consists of nearly all of the “legal or equitable interests of the debtor in property as of the commencement of the case ...” 11 U.S.C. § 541(a)(1) (Section 541 does exclude certain specific interests as outside of the estate). In addition, the estate also includes some types of property acquired after the commencement of the case; this concept and its implications are discussed later in this section.

The automatic stay of Section 362(a) always protects the debtor no matter what type of bankruptcy is filed, but exceptions to the stay exist in certain instances, including a number in the domestic relations arena. Under BAPCPA, proceedings to establish or modify support and proceedings to collect support from property that is not property of the estate are now included in the category of domestic support obligations (defined supra) and are still exempt from the stay. There are now eight additional domestic relations proceedings that are also exempted from the automatic stay:

1. Child custody or visitation proceedings;
2. Divorce proceedings, except to the extent that such proceeding seeks to divide property of the estate;
3. Domestic violence proceedings;
4. Withholding of income that is property of the estate or the debtor for payment of a DSO;
5. Withholding, suspending, or restricting a driver’s, professional, occupational, or recreational license under state law as specified by Section 466(a)(16) of the Social Security Act;

6. Reporting of overdue support owed by a parent to any consumer reporting agency as specified by Section 466(a)(7) of the Social Security Act;

7. Intercepting a tax refund as specified in Sections 464 and 466(a)(3) of the Social Security Act or under analogous state law; and


These changes drastically limit the effect that the automatic stay has on domestic relations proceedings. A bankruptcy will now only stay the division of property aspect of a dissolution proceeding and subsequent post-dissolution proceedings may not be stayed at all.

Obtaining an order for relief from the stay is a simple matter. Relief from the stay protects you and your client from violations of the stay and the bankruptcy courts are generally more than happy to send domestic relations matters back to state court where a judge with specific knowledge in that area can make a determination (or at least another judge can deal with the dissolution).

If relief from the stay is not obtained, divorce proceedings may be bifurcated; the divorce proceedings are held in abeyance on property issues while the proceedings move forward on all issues not affected by the automatic stay. Not obtaining relief from the automatic stay early in the bankruptcy may have the effect of forcing the issues of support to be dealt with separately from the issues of property division (which may be a
good or bad thing, depending on which side you’re on).

Without either relief from stay or bifurcation of the dissolution action, the consequences can be dire. In a recent dissolution case in the tri-county area when the parties failed to obtain an order for relief, the entire general judgment of dissolution of marriage was set aside and “all affirmative relief purportedly granted” was also set aside (including both spousal support and the grant of dissolution itself). The parties had to completely begin the dissolution process anew. Although the family law court had made an award of compensatory spousal support (which would be allowed under the new Section 362 without relief), the court that threw out the dissolution proceeding did not parse through the general judgment to set aside only parts that violated the automatic stay – rather, the entire general judgement was vacated.

In the time since BAPCPA, there are few reported cases concerning the changes to the automatic stay in dissolution proceedings and, given the changes to the Code and the intent of Congress in making those changes, substantive case law may be a long time coming. There appears to be general consensus that while a proceeding seeking an division of property of the estate is enjoined by the automatic stay, the remainder of a dissolution may proceed. Garcia-Lawson v. Garland, 2008 U.S. Dist. LEXIS 100124 (S.D. Fla. 2008) (determining an interlocutory appeal was inappropriate as no significant ground for difference existed because bankruptcy courts have consistently interpreted the automatic stay as applying only to the extent that property of the estate is distributed). However, relief from the automatic stay may not be automatic. In re Exum, 2008 Bankr. LEXIS 485 (Bankr. E. Va 2008). In re Exum is one of the few post-BAPCPA cases involving the changes to the automatic stay; in that case, the
debtor’s spouse sought both a dissolution and the equitable distribution of marital property; the Bankruptcy Court denied her request as the interest of creditors, including joint creditors, outweighed her interest. Notably, the Court did so in spite of the local state court’s local rules against granting dissolutions without an equitable distribution. Fortunately, local practice in Oregon seems to allow bifurcation of dissolution proceedings. As a result, if relief from stay cannot be obtained from the Bankruptcy Court with regard to property division, until the trustee has administered non-exempt assets of the bankruptcy estate or abandoned exempt assets, it may be worthwhile to investigate whether bifurcation of the dissolution to fit within the exceptions to the automatic stay will be sufficient to achieve your client’s short-term goals.

As a result, the automatic stay can be used by the savvy practitioner as an excuse to bifurcate the proceedings to avoid mingling the issues of support and property division or relief can be obtained to purposely co-mingle these issues.

As mentioned earlier in this section, property of the estate includes nearly all of the debtor’s legal or equitable rights in property. In addition, post-petition acquired property is also brought into the bankruptcy estate if acquired by the debtor within 180 days of case commencement as a result of either inheritance, insurance, or a property settlement. 11 U.S.C. § 541(a)(5). This post-petition property of the estate poses a potential trap for family law practitioners: if a debtor becomes entitled to a property settlement within 180 days of the commencement of their bankruptcy case, that property settlement belongs to the estate and will be distributed to unsecured creditors (either by direct collection by the Chapter 7 trustee or by the Chapter 13 plan confirmation requirements regarding the best interest of creditors) rather than being...
retained by the debtor. Further complicating matters, the law in this area is wholly underdeveloped (as the best course of action is to delay any property settlement until after 180 days have elapsed).

For example, while a debtor’s interest in a homestead is exempt (up to the applicable limit), is a debtor’s interest in a property settlement resulting from the now ex-spouse being awarded the entirety of the residence likewise exempt? A trustee would likely argue that the property settlement is simply a money judgment -- a new asset not entitled to any exemption. The debtor could argue that the property settlement was a disposition of the debtor’s homestead interest; with the Ninth Circuit’s recent decision in Wolfe v. Jacobson (In re Jacobson), 676 F.3d 1193, potentially overruling In re Lane, 364 B.R. 760 (Bankr. D. Or. 2007) (which had ruled that a post-petition disposition of the homestead did not impose a reinvestment requirement), the property settlement would be subject to a reinvestment requirement (within one year) or lost to the creditors of the estate. Since few property settlements are paid within one year, reinvestment would prove highly problematic and the value of the property settlement could be disbursed to unsecured creditors at the expense of the debtor. This entire morass would be avoided, however, by simply delaying the property settlement until more than 180 days after the commencement of the bankruptcy case.

5. In re Beverly & In re Bledsoe: A Tale of Two Dissolutions: Fraudulent Conveyances in the Domestic Relations Context

The trustee in bankruptcy may use Section 544 (the so-called “Strong-Arm Clause”) to set aside fraudulent conveyances made by the debtor within one year of
bankruptcy (Section 548) or using state law fraudulent conveyance statutes, via the Strong-Arm Clause (Sections 544(a) and (b)), within four years of bankruptcy (under Oregon law, ORS 95.200, et seq.).

Transfers that were made with actual intent to hinder, delay, or defraud any entity to which the debt was or became indebted may be set aside. Actual intent to hinder, delay, or defraud the creditor often must be shown by circumstantial evidence. Hinder, delay, and defraud all have separate meanings, and each one alone can be a basis for avoiding the transfer. The value given for a transfer can include a wide range of consideration, including the satisfaction or securing of a debt. However, the value must benefit the debtor and thus is more limited than the broad concept of consideration. In re Nelsen, 24 B.R. 701 (Bankr. D. Or. 1982).

If a bankruptcy case is filed after the dissolution is finalized, the trustee may examine whether transfers from the debtor to his former spouse were fraudulent in nature, i.e., transfers for less than fair value. 11 U.S.C. §§ 544, 548. Given the pre-petition planning opportunities present in a dissolution, especially if there is collusion between the spouses, the trustee will carefully examine dissolution judgment. A scenario at one end of the spectrum, along with its predictable result is illustrated in In re Beverly, while another scenario, representing the opposite end of the spectrum, is illustrated in In re Bledsoe. Beverly v. Wolkowitz, 374 B.R. 221 (Cal. BAP 2007); Bledsoe v. Bledsoe, 569 F.3d 1106 (9th Cir. 2009).

In Beverly, the debtor, an attorney facing both a large malpractice judgment and a divorce, colluded with his spouse to divide their community property in such a way that, while both parties received approximately half of the assets, he received primarily
exempt assets while she received non-exempt assets. While the Bankruptcy Court believed that this was merely an aggressive but acceptable exercise in pre-bankruptcy planning, the Bankruptcy Appellate Panel ("BAP") looked at the numerous badges of fraud, the extensive evidence of intent to hinder, delay, or defraud creditors, and their opinion of the likely outcome of a dissolution without the collusive settlement agreement. The BAP stated that "when a pig becomes a hog it is slaughtered," (citing the oft-quoted Dolese v. U.S., 605 F.2d 1146, 1154 (10th Cir. 1979)) and described a series of letters detailing the arrangement to move home equity proceeds out of the grasp of creditors and leave the debtor with only a million-dollar (and wholly exempt) pension plan. The BAP presumed that a California court would divide exempt and non-exempt assets equally; as a result, to the extent that the settlement created a different result which deprived creditors of assets to satisfy their claims, the settlement was a fraudulent conveyance.

When Beverly was decided, it panicked many among both the bankruptcy and family law bars. Because of the discussion of the Uniform Fraudulent Transfer Act (UFTA) in the footnotes, one might conclude that Beverly stood for the proposition that any division of marital assets which was not an equal division of all non-exempt property, regardless of what happens to the exempt property of the marital estate, could be subject to collateral attack by a trustee as a fraudulent conveyance. Thankfully, that does not seem to be the case where there is no evidence of fraud.

In June 2009, the Ninth Circuit decided Bledsoe v. Bledsoe and addressed the same issues of fraudulent conveyance. Bledsoe v. Bledsoe, 569 F.3d 1106 (9th Cir. 2009). After eight years of marriage, Ryan Bledsoe filed for divorce from the debtor,
Jennifer Bledsoe. While Jennifer initially entered an appearance, that appearance was struck after she failed to comply with discovery requirements and court orders in bad faith. Ryan was granted a default judgment; he was awarded items valued at $93,737 while Jennifer was only awarded items valued at $788. After Ryan took 99% of the alleged value, Jennifer filed for bankruptcy; the trustee in her case sought to recover from Ryan half of the combined value of the marital assets.

Like Beverly, the Bledsoe Court agreed that a trustee may attack a judgment, including a divorce judgment, as a fraudulent conveyance. However, in Bledsoe, the trustee plead only a constructive fraud case; under Oregon law, extrinsic fraud is required to attack a judgment. Bledsoe, 569 F.3d at 1109 (citing Greeninger v. Cromwell, 140 Ore. App. 241, 915 P.2d 479, 481-82 (Or. Ct. App. 1996)). The trustee also argued that Jennifer had received less than reasonable equivalent value; the Bledsoe court agreed with the Bankruptcy Court in finding that “a state court’s dissolution judgment, following a regularly conducted contested proceeding, conclusively establishes ‘reasonable equivalent value’ for the purpose of § 548, in the absence of actual fraud.” Bledsoe, 569 F.3d at 1111.

These two cases represent the less than typical way that dissolution cases are conducted. In Beverly, the spouses, while arguing about details, worked together in an actually fraudulent scheme to defraud the husband’s creditors, while in Bledsoe, the spouses were unable to even make it through discovery without a judge signing a default judgment against one of the spouses. Most dissolution cases are negotiated to conclusion without litigation; the remainder are litigated with varying degrees of contentiousness. It appears that as long as there is no evidence of extrinsic fraud on
creditors - and even where there is a “long half” provided to the non-filing spouse, Bledsoe should provide a measure of comfort to the domestic relations practitioner. While it may be important to have bankruptcy counsel in the loop to interpret the possible impact of a bankruptcy filing by a future ex-spouse, as long as there is no active scheme to defraud creditors, the dissolution judgment should stand.


It is not uncommon for a judgment lien to attach to the debtor's residence prior to the debtor filing Chapter 7 or Chapter 13. Section 522(f)(1) provides a mechanism for the debtor to avoid any judgment lien that "impairs" the debtor's exemption. Judicial lien avoidance is the reduction or elimination of a secured claim because it impairs or limits the debtor's exemptions in their property. It applies only to judicial liens (i.e. judgments) and only when the debtor has a permissible exemption. The debtor files a motion (or may include it in their Chapter 13 plan), and if the debtor is successful, the judgment lien will be "avoided" in the bankruptcy. So, for example, a debtor with a $250,000 property owing a first mortgage of $225,000 and a judgment lien of $50,000 can avoid the entirety of the judgment lien because it would impair the debtor’s $40,000 homestead exemption.

This analysis, however, does not apply to the classic marital residence equalizing judgment. Farrey v. Sanderfoot, 500 U.S. 291 (1991). Faced with the scenario where Sanderfoot received the entire marital residence subject to a lien in favor of Farrey (who lost her interest in the property) and then sought to avoid Farrey’s lien as impairing his
homestead exemption, the Supreme Court looked at Section 522 to craft a way around this apparent inequity. The underlying rationale of Sanderfoot is that Farrey took the property subject to the lien and thus, the lien existed prior to the homestead exemption and could not impair it. However, during the time that this case progressed to the Supreme Court, the general practice for equalizing judgment transitioned to having most equalizing judgments instead secured by a note and trust deed; however, this practice has its own set of risks with the rapidly depreciating real estate market allowing for the avoidance of wholly unsecured liens (“strip off”) which can occur in Chapter 13 only.

Section 1322(b)(2) provides that a Chapter 13 plan may modify secured claims (other than claims secured only by a security interest (as defined in Section 101(37)) in the debtor’s personal residence with the exception of secured claims in which the last payment is contractually due within the duration of the Chapter 13 plan). Modifications of secured claims come in two varieties: (1) the cram down or the strip down and (2) the strip off or lien avoidance.

“Cram-down” and “Strip Down” (terms used interchangeably) refer to the bifurcation of a partially secured creditor’s claim into its respective “secured” and “unsecured” components. Sections 506(a) and 1322(b)(2) provides the authority for this bifurcation as it limits a secured claim to the extent the collateral has value. Beyond the collateral value, the creditor has a separate unsecured claim.

Cram-down can be used for secured creditors with a lien against any property of the debtor (i.e. vehicles, rental homes) with few exceptions: purchase money secured creditors of non-business vehicles purchased within 910-days of filing, purchase money secured obligations on personal property within one year of filing and certain security
interests against the debtor’s home. 11 U.S.C. §§ 1325(a)(9), 1322(b)(2).

While Section 1322(b)(2) provides the exception for the debtor’s home, the “exception to the exception” is that the anti-modification clause only applies to mortgages which have their final payment (under the original payment schedule) due after the final payment under the plan. For balloon mortgages on a debtor’s home, the bankruptcy code was amended to include Section 1322(c)(2) which provides specific authority to modify balloon mortgages on the debtor’s principal residence so long as the last scheduled payment is due prior to the final plan payment. However, it is not possible to extend the time for payment beyond the duration of the plan.

“Strip Off” or “lien avoidance” is the related concept under Sections 506 and 1322(b)(2) where there no collateral value to allow for any secured claim, such as in the example of a second mortgage where the real property value is less than the balance owning of the first mortgage; any value giving rise to an allowed secured claim precludes the use of strip off. When there is no value for an allowed secured claim, the lien may be declared void and the claim is then treated as wholly unsecured. Since the claim is wholly unsecured, the creditor does not possess a secured claim against the debtor’s personal residence and the anti-modification provisions above do not apply. Further, since the strip is being done through Sections 506 and 1322, the Chapter 13 debtor also avoids the limitations of Sanderfoot (potentially to the detriment of the property settlement creditor).

7. The Chapter 7 Trustee as DSO Collection Agent.
Following the passage of BAPCPA, additional language added to Section 522 gave rise to the thought that otherwise exempt property could be liquidated by the Trustee to satisfy certain tax and domestic support obligations. The basis for this argument was that Section 522(c)(1) states that property exempted remains liable for debts specified in Sections 523(a)(1) (certain taxes) and Section 523(a)(5) (domestic support obligations). As a result, the trustee, in a Chapter 7 case, sought to liquidate a debtor’s otherwise exempt property for the benefit of a DSO claimant. The debtor objected to this liquidation; the State of Oregon filed a Memorandum in Support of the trustee. In an unpublished opinion, Judge Alley wrote that BAPCPA did not provide the Trustee with authority to liquidate exempt property for the benefit of a DSO claimant. In re Ruppel, Case No. 06-60961-fra7 (Bankr. D. Or. 2007) (unpublished).

8. Conclusion.

These materials have been written to provide domestic relations practitioners with an overview of some of the most common bankruptcy issues that may impact domestic relations practice. The interplay between bankruptcy and domestic relations practice (along with the implications for debtors and spouses) can create a tangled quagmire which, at times, can lead to unhappy clients and claims of malpractice. Bankruptcy counsel would be wise to enlist the aid of domestic relations counsel when domestic relations issues present themselves in a bankruptcy; likewise, domestic relations counsel would be wise to enlist the aid of bankruptcy counsel when bankruptcy issues present themselves in a dissolution.
UNITED STATES BANKRUPTCY COURT

NOTICE TO INDIVIDUAL CONSUMER DEBTOR UNDER § 342(b) OF THE BANKRUPTCY CODE

In accordance with § 342(b) of the Bankruptcy Code, this notice: (1) Describes briefly the services available from credit counseling services; (2) Describes briefly the purposes, benefits and costs of the four types of bankruptcy proceedings you may commence; and (3) Informs you about bankruptcy crimes and notifies you that the Attorney General may examine all information you supply in connection with a bankruptcy case. You are cautioned that bankruptcy law is complicated and not easily described. Thus, you may wish to seek the advice of an attorney to learn of your rights and responsibilities should you decide to file a petition. Court employees cannot give you legal advice.

1. Services Available from Credit Counseling Agencies

With limited exceptions, § 109(h) of the Bankruptcy Code requires that all individual debtors who file for bankruptcy relief on or after October 17, 2005, receive a briefing that outlines the available opportunities for credit counseling and provides assistance in performing a budget analysis. The briefing must be given within 180 days before the bankruptcy filing. The briefing may be provided individually or in a group (including briefings conducted by telephone or on the Internet) and must be provided by a nonprofit budget and credit counseling agency approved by the United States trustee or bankruptcy administrator. The clerk of the bankruptcy court has a list that you may consult of the approved budget and credit counseling agencies.

In addition, after filing a bankruptcy case, an individual debtor generally must complete a financial management instructional course before he or she can receive a discharge. The clerk also has a list of approved financial management instructional courses.

2. The Four Chapters of the Bankruptcy Code Available to Individual Consumer Debtors

Chapter 7: Liquidation ($245 filing fee, $39 administrative fee, $15 trustee surcharge: Total fee $299)

1. Chapter 7 is designed for debtors in financial difficulty who do not have the ability to pay their existing debts. Debtors whose debts are primarily consumer debts are subject to a “means test” designed to determine whether the case should be permitted to proceed under chapter 7. If your income is greater than the median income for your state of residence and family size, in some cases, creditors have the right to file a motion requesting that the court dismiss your case under § 707(b)(2) of the Code. It is up to the court to decide whether the case should be dismissed.

2. Under chapter 7, you may claim certain of your property as exempt under governing law. A trustee may have the right to take possession of and sell the remaining property that is not exempt and use the sale proceeds to pay your creditors.

3. The purpose of filing a chapter 7 case is to obtain a discharge of your existing debts. If, however, you are found to have committed certain kinds of improper conduct described in the Bankruptcy Code, the court may deny your discharge and, if it does, the purpose for which you filed the bankruptcy petition will be defeated.

4. Even if you receive a general discharge, some particular debts are not discharged under the law. Therefore, you may still be responsible for most taxes and student loans; debts incurred to pay nondischargeable taxes; domestic support and property settlement obligations; most fines, penalties, forfeitures, and criminal restitution obligations; certain debts which are not properly listed in your bankruptcy papers; and debts for death or personal injury caused by operating a motor vehicle, vessel, or aircraft while intoxicated from alcohol or drugs. Also, if a creditor can prove that a debt arose from fraud, breach of fiduciary duty, or theft, or from a willful and malicious injury, the bankruptcy court may determine that the debt is not discharged.

Chapter 13: Repayment of All or Part of the Debts of an Individual with Regular Income ($235 filing fee, $39 administrative fee: Total fee $274)

1. Chapter 13 is designed for individuals with regular income who would like to pay all or part of their debts in instalments over a period of time. You are only eligible for chapter 13 if your debts do not exceed certain dollar amounts set forth in the Bankruptcy Code.

2. Under chapter 13, you must file with the court a plan to repay your creditors all or part of the money that you owe them.
using your future earnings. The period allowed by the court to repay your debts may be three years or five years, depending upon your income and other factors. The court must approve your plan before it can take effect.

3. After completing the payments under your plan, your debts are generally discharged except for domestic support obligations; most student loans; certain taxes; most criminal fines and restitution obligations; certain debts which are not properly listed in your bankruptcy papers; certain debts for acts that caused death or personal injury; and certain long term secured obligations.

Chapter 11: Reorganization ($1000 filing fee, $39 administrative fee: Total fee $1039)

Chapter 11 is designed for the reorganization of a business but is also available to consumer debtors. Its provisions are quite complicated, and any decision by an individual to file a chapter 11 petition should be reviewed with an attorney.

Chapter 12: Family Farmer or Fisherman ($200 filing fee, $39 administrative fee: Total fee $239)

Chapter 12 is designed to permit family farmers and fishermen to repay their debts over a period of time from future earnings and is similar to chapter 13. The eligibility requirements are restrictive, limiting its use to those whose income arises primarily from a family-owned farm or commercial fishing operation.

3. Bankruptcy Crimes and Availability of Bankruptcy Papers to Law Enforcement Officials

A person who knowingly and fraudulently conceals assets or makes a false oath or statement under penalty of perjury, either orally or in writing, in connection with a bankruptcy case is subject to a fine, imprisonment, or both. All information supplied by a debtor in connection with a bankruptcy case is subject to examination by the Attorney General acting through the Office of the United States Trustee, the Office of the United States Attorney, and other components and employees of the Department of Justice.

WARNING: Section 521(a)(1) of the Bankruptcy Code requires that you promptly file detailed information regarding your creditors, assets, liabilities, income, expenses and general financial condition. Your bankruptcy case may be dismissed if this information is not filed with the court within the time deadlines set by the Bankruptcy Code, the Bankruptcy Rules, and the local rules of the court.

Certificate of [Non-Attorney] Bankruptcy Petition Preparer

I, the [non-attorney] bankruptcy petition preparer signing the debtor’s petition, hereby certify that I delivered to the debtor this notice required by § 342(b) of the Bankruptcy Code.

Printed Name and title, if any, of Bankruptcy Petition Preparer

Address:

Social Security number (If the bankruptcy petition preparer is not an individual, state the Social Security number of the officer, principal, responsible person, or partner of the bankruptcy petition preparer.)

(Required by 11 U.S.C. § 110.)

Signature of Bankruptcy Petition Preparer of officer, principal, responsible person, or partner whose Social Security number is provided above.

Certificate of the Debtor

I (We), the debtor(s), affirm that I (we) have received and read this notice.

Printed Name(s) of Debtor(s)

Signature of Debtor

Case No. (if known)

Signature of Joint Debtor (if any)
NOTICE TO INDIVIDUAL CONSUMER DEBTOR
UNDER §527(a) OF THE BANKRUPTCY CODE

All information that you are required to provide with a petition and thereafter during your bankruptcy filing is required to be complete, accurate, and truthful;

All assets and all liabilities are required to be completely and accurately disclosed in the documents filed to commence the case, and the replacement value of each asset as defined in section 506 must be stated in those documents where requested after reasonable inquiry to establish such value;

Current monthly income, the amounts specified in section 707(b)(2), and, in a chapter 13 bankruptcy filing, disposable income (determined in accordance with section 707(b)(2), are required to be stated after reasonable inquiry; and

Information that you provide during your case may be audited, and that failure to provide such information may result in dismissal of your case or other sanction, including a criminal sanction.

I have received this disclosure from Vanden Bos & Chapman, LLP.

SIGNATURE

PRINT NAME: __________________________
Dated: __________________________

SIGNATURE

PRINT NAME: __________________________
Dated: __________________________
NOTICE TO INDIVIDUAL CONSUMER DEBTOR
UNDER §527(b) OF THE BANKRUPTCY CODE

IMPORTANT INFORMATION
ABOUT BANKRUPTCY ASSISTANCE SERVICES FROM AN ATTORNEY

If you decide to seek bankruptcy relief, you can represent yourself, you can hire an attorney to represent you, or you can get help in some localities from a bankruptcy petition preparer who is not an attorney. **THE LAW REQUIRES AN ATTORNEY OR BANKRUPTCY PETITION PREPARER TO GIVE YOU A WRITTEN CONTRACT SPECIFYING WHAT THE ATTORNEY OR BANKRUPTCY PETITION PREPARER WILL DO FOR YOU AND HOW MUCH IT WILL COST.** Ask to see the contract before you hire anyone.

The following information helps you understand what must be done in a routine bankruptcy case to help you evaluate how much service you need. Although bankruptcy can be complex, many cases are routine.

Before filing a bankruptcy case, either you or your attorney should analyze your eligibility for different forms of debt relief available under the Bankruptcy Code and which form of relief is most likely to be beneficial for you. Be sure you understand the relief you can obtain and its limitations. To file a bankruptcy case, documents called a Petition, Schedules and Statement of Financial Affairs, as well as in some cases a Statement of Intention needs to be prepared correctly and filed with the Bankruptcy Court. You will have to pay a filing fee to the bankruptcy court. Once your case starts, you will have to attend the required first meeting of creditors where you may be questioned by a court official called a 'trustee' and by creditors.

If you choose to file a Chapter 7 case, you may be asked by a creditor to reaffirm a debt. You may want help deciding whether to do so. A creditor is not permitted to coerce you into reaffirming your debts.

If you choose to file a Chapter 13 case in which you repay your creditors what you can afford over 3 to 5 years, you may also want help with preparing your Chapter 13 Plan and with the confirmation hearing on your Plan which will be before a bankruptcy judge.

If you select another type of relief under the Bankruptcy Code other than Chapter 7 or Chapter 13, you will want to find out what should be done from someone familiar with that type of relief.

Your bankruptcy case may also involve litigation. You are generally permitted to represent yourself in litigation in Bankruptcy Court, but only attorneys, not bankruptcy petition preparers, can give you legal advice.

I have received this disclosure from Vanden Bos & Chapman, LLP.

SIGNATURE

PRINT NAME: __________________________

Dated: _______________________________

SIGNATURE

PRINT NAME: __________________________

Dated: _______________________________
NOTICE TO ASSISTED PERSON ON HOW TO PROVIDE ALL THE INFORMATION AN ASSISTED PERSON IS REQUIRED TO PROVIDE UNDER 11 U.S.C. §§ 521 AND 528 OF THE BANKRUPTCY CODE

The law requires that a “Debt Relief Agency” provide to an “Assisted Person” certain instructions on how to provide information that is required under 11 U.S.C. §§ 521 and 528 of the Bankruptcy Code. Generally speaking, an “Assisted Person” is an individual consumer debtor whose nonexempt assets have a value of less than $150,000. This notice will apply to you generally if the value of your nonexempt assets is less than $150,000 and your debts are primarily consumer debts.

A “Debt Relief Agency” is a person who provides assistance to an “Assisted Person” with respect to a case under the Bankruptcy Code. The statute is unclear as to whether a “Debt Relief Agency” includes an attorney and VBC is therefore providing the disclosures out of an abundance of caution.

In connection with filing bankruptcy, you have the duty to provide the Bankruptcy Court with the following documents and information:

1. A list of your creditors, their full and correct address, the amount owed, a schedule of your assets and liabilities, a schedule of your current income and current expenditures and a statement of your financial affairs in the format required by the court.

   Instructions on How to Comply: Vanden Bos & Chapman, LLP (“VBC”) will prepare the these forms for your review, approval and signature, based on the information you provide to VBC in your client questionnaire. You should determine the amount owed by taking the amount showed as owing on your most recent statement from the creditor. The address that you use should be the address that the creditor has indicated within the last 90 days in any communication to you as the address the creditor will use for notification of a bankruptcy case. If the creditor has not given you a specific address to use for bankruptcy notification, then you should use the address shown on the creditor’s most recent billing statement or other communication to you.

2. Copies of your pay stubs or “Payment Advices” received within sixty (60) days before the date of your bankruptcy petition from any employer of the debtor.

   Instructions on How to Comply: Deliver copies of these documents to VBC. VBC will file “Payment Advices” with the Court at the appropriate time.

3. A statement of the amount of your monthly net income and expenses itemized to show how the amount is calculated.

   Instructions on How to Comply: Complete the income and expenses portion of the client questionnaire that you have been provided with by VBC. VBC will prepare the income statement on the form required by the Court for your review and approval.

4. A statement disclosing any reasonably anticipated increase in income or expenditures over the 12 month period following the date of the filing of the petition.
Instructions on How to Comply: Supply this information on your client questionnaire at the appropriate location. VBC will prepare the appropriate form for the Court for your review and approval. VBC will file the form with the Court at the appropriate time.

5. File with the Clerk of the Court within 30 days of your bankruptcy petition date, a statement of your intention with respect to retention or surrender of property which may be subject to a creditor’s security interest (such as vehicle loans, home mortgages, loans to purchase furniture or appliances, etc.), specifying whether such property is claimed as exempt, whether the debtor intends to redeem the property; or whether the debtor intends to reaffirm the debt secured by such property.

Instructions on How to Comply: Supply this information on the client questionnaire. A legal assistant or an attorney will discuss with you your intention with respect to each piece of property subject to a creditor’s lien or security interest. The statement of intention will be prepared for your signature and filed by VBC with the court as part of your initial bankruptcy schedules.

6. Within 30 days after the first date set for the “meeting of creditors,” you must perform your stated intention with respect to each secured property and execute a reaffirmation, redeem the property, or surrender the property, consistent with your stated intentions.

Instructions on How to Comply: If you intend to reaffirm on any property, you will need to complete a “reaffirmation worksheet,” which will be provided to you as part of your client questionnaire. You will be responsible for returning a reaffirmation work sheet to your attorney. Except in rare instances, VBC does not sign reaffirmations on behalf of clients. If you intend to reaffirm, you will need to appear at a reaffirmation hearing in front of a bankruptcy judge. The judge will decide whether you will be permitted to reaffirm a debt. If you choose to surrender property, you must notify the creditor directly (your attorney will not be involved in this process) of a time and place at which the creditor may take possession of the property. If you wish to redeem the property, which is a one-time lump sum payment based on the value of the property or an amount which you negotiate with your creditor, you should contact the creditor directly to make arrangements for payment of that lump sum redemption amount. If you fail to perform your stated intention within 45 days after the date first set for the meeting of creditors, the bankruptcy stay will expire and the creditor may repossess the property without notice to you.

7. Provide the Court with your certificate from the approved nonprofit budget and credit counseling agency that you completed your pre-bankruptcy credit counseling session. Except in rare cases, the Court will refuse to accept your bankruptcy petition for filing unless the Credit Counseling Certificate is presented at the same time.

Instructions on How to Comply: Provide a copy of your certificate to VBC. VBC will file the document at the time a bankruptcy petition is filed.

8. Provide a copy of the debt repayment plan, if any, developed by you and the nonprofit counseling agency you met with prior to the bankruptcy petition date.
**Instructions on How to Comply**: If you received a written debt repayment plan developed by the nonprofit budget and credit counseling agency, provide a copy of that plan to your attorney at VBC. VBC will file a copy of the plan with the Court.

9. File with the Court a record of any interest that you may have in an education individual retirement account.

**Instructions on How to Comply**: If you have an education individual retirement account (as defined in §530(b)(1) of the Internal Revenue Code), provide your attorney at VBC with a copy of your most recent monthly statement so that the attorney can file it with the court.

10. Provide to the bankruptcy trustee not later than seven (7) days before the date first set for your meeting of creditors, a copy of your federal income tax return, or alternatively, a transcript of such return, for the most recent tax year ending immediately before the commencement of the case.

**Instructions on How to Comply**: Provide a copy of your most recently filed federal income tax return to your attorney with your client questionnaire. The attorney at VBC will provide a copy of your return to your bankruptcy trustee prior to the deadline. You must supply a copy of your tax return to VBC at least 14 days prior to the date of your creditors meeting, or VBC cannot guarantee that the trustee will be provided with your tax return by the seven-day deadline.

11. If requested by the court, the United States trustee, or any party in interest, you must file with the court at the same time filed with the taxing authority, a copy of each Federal income tax return, or alternatively, transcript of such tax return, with respect to each tax year of the debtor ending while the case is pending under Chapter 7, 11, or 13.

**Instructions on How to Comply**: The Bankruptcy Court for the District of Oregon has implemented a local order restricting the rights of creditors to copies of your tax returns. You should provide your attorney with a copy of your tax return for the four (4) years prior to your petition date. Provide your Attorney with a copy of each tax return at the time you file it so long as your case is open. Failure to file tax returns on time and to supply copies on time will result in dismissal of your case. Your attorney will, as appropriate and required by any order of the Court entered in your case, provide a copy of your tax return to any person consistent with such order. It is the intention of the Bankruptcy Court for the District of Oregon to limit the debtor’s obligation to provide tax returns to creditors except in unusual circumstances.

12. In a case filed under Chapter 13, you must provide a copy of your income tax return annually to the Court by April 1 of each calendar year.

**Instructions on How to Comply**: At the same time you file your annual income tax returns (state and federal) with the tax agencies, you should send a copy of those returns to your attorney and to your trustee using the Court-provided address.

13. In a case under Chapter 13 within ninety (90) days after the close of the tax year, you are required to provide a statement, under penalty of perjury, of the income and expenditures of the debtor during the tax year of the debtor most recently concluded.
before such statement is filed, and of the monthly income of the debtor, that shows how income, expenditures, and monthly income are calculated.

Instructions on How to Comply: Your attorney with VBC will provide you with a form on an annual basis for you to complete in order to comply with this requirement. Your attorney will review the results of the form with you and when you and the attorney are satisfied that the form is correct, you will be required to sign the form and the attorney will submit it to your Chapter 13 trustee. Please note that the ninety (90) day deadline is April 1 of each year – or fifteen (15) days prior to the due date of April 15 for filing tax returns.

14. You are required to supply a document that establishes the identity of the debtor, including a driver’s license, passport, or other document that contains a photograph of the debtor. You will also be required to supply the original of your social security card.

Instructions on How to Comply: Bring your driver’s license and your social security card with you to your meeting with your attorney at VBC, so that we may make copies for your file. Bring your original state driver’s license and your social security card with you to present to your trustee at the time of your creditors meeting. If you do not bring proof of identification with you to your creditors meeting, the trustee may continue your meeting to a future date, or may move to dismiss your case.

NOTE: If you fail to supply all of the information which you are required to supply by the dates set forth above or in some cases, within 45 days of the petition date, your case will be automatically dismissed effective on the 46th day after the date of filing the petition. If you are unable to provide the information, it may be possible in some instances to obtain a 45-day extension. You should immediately notify your attorney if you are not able to provide all of the information by the dates indicated.

15. You must provide a valuation of your assets in the schedules.

Instructions on How to Value Assets:

a. Secured Assets. “Secured Assets” are assets that serve as collateral for payment of a specific debt, such as a car loan, a furniture loan or a mortgage on your house. The valuation of secured assets is to be determined on the basis of retail replacement value. Retail replacement value means the price a retail merchant would charge for property of that kind considering the age and condition of the property as of the petition date. This does not mean the price that a retail merchant would charge for new goods, but the price that would be charged for a used good of comparable condition and quality. For example, in a car loan, the valuation of the car would be the Kelley Blue Book retail value.

b. Unsecured Assets. For assets that are not subject to the claim of a security interest, the valuation should be an estimate of what the goods could be sold for by the debtor, typically in a garage sale.

c. Exempt Assets. The language of the Bankruptcy Reform Act is ambiguous. It is unclear whether exempt assets are to be valued at the price at which
they could be sold by the debtor, or valued at the retail replacement value. In order to protect yourself from choosing the wrong valuation standard, VBC will recommend disclosing the standard used on the face of the schedules. Unless directed otherwise, you should use the sale value for all unsecured assets and retail replacement value for secured assets.

16. You must disclose your "Current Monthly Income" to the Bankruptcy Court as that term is defined in the Bankruptcy Code.

**Instructions on How to Determine Current Monthly Income:** Under the Bankruptcy Code definitions, current monthly income includes money that is neither "current" nor "monthly" nor "income." In order to meet your obligation, you should complete the information form provided by VBC, which requires that you disclose all money that you may have received at any time in the six (6) months preceding your bankruptcy petition date from any source. This would include gifts, loans, unemployment compensation, inheritances, disability income, gambling winnings, employer reimbursed expenses, etc.

17. In a Chapter 13 case, disposable income must be calculated in accordance with 11 U.S.C. §707(b)(2).

**Instructions on How to Comply:** VBC will provide you with a worksheet to complete with your income and expenses covering the six (6) months before your petition date and your projections as to your income and expenses in the six (6) months following your petition date. If you provide VBC with the correct and complete information, the bankruptcy software program used by VBC will calculate your disposable income in accordance with §707.


**Instructions on How to Comply:** Determination of which assets may be exempt is a question of law which should not be made without the advice of an attorney. VBC’s website has a list of the most common exempt assets for your review. The best way to ensure compliance with your duty to fully disclose exempt assets is to make sure that your list of assets is entirely correct and complete. An attorney from VBC will review your list with you and identify which of those assets that you listed can be claimed as exempt. With respect to the valuation of exempt assets, the Bankruptcy Reform Act is ambiguous as to the method of valuation. One section of the Bankruptcy Code would suggest that the assets be valued at their current sale value, using a typical “garage sale prices” approach. Another section of the Bankruptcy Code suggests that exempt assets may have to be valued at their retail replacement value, which would be the price at which a retail merchant would sell an item of the same type and condition. VBC believes the correct valuation standards are the garage sale prices for “unsecured” exempt assets (such as clothing, jewelry, etc.) and the "retail replacement value" for “secured” exempt assets, such as cars.
INSTRUCTIONS ON VALUATION OF ASSETS
AND COMPLETION OF BANKRUPTCY SCHEDULES

The first step leading to the filing of a bankruptcy case on your behalf is the filling out of schedules and answering the questions in the Statement of Affairs. I have given you (or you can obtain from our website), our firm questionnaire to assist you in completion of these documents.

Before beginning, please read this letter carefully. It may answer some of the questions you will have. The other disclosures in the Welcome Packet will give you guidance from the statute. Call at any time if you have questions or concerns.

As you do this, there are several things to keep in mind:
All of the information you provide must be complete, accurate, and truthful.

You should make every effort to list every creditor, their most current address, and balance due. Provide me with copies of all these bills or invoices, and documents.

While every page of the schedules is important, some pages will be examined more carefully than others. These are the lists of assets, current income, and current expenses.

**Assets**: Everything that you own should be listed. This includes income tax refunds, personal injury or damage claims, claims that you might think you have against anyone for anything, or persons who owe you money. Not listing an asset can cost you your discharge. It may also stop you from ever recovering on a claim. It needs to be listed even if it is of no value or if it is a liability—for example, that burnt-out 1994 non-running Pacer automobile that does not have an engine. Valuation will be scrutinized.

The general rule is that secured assets are valued at the replacement value for like goods of the same age and condition. This is not the cost to replace a “used item” with a “new” item. It is the price you would pay to replace a “used” item with another “used” item in a similar condition.

If the property is real estate, check sales in the neighborhood when determining value. If possible, have a real estate agent give you a Comparative Market Analysis of your property. Ask for a quick-sale value.
For a car, check the sales price of comparable models in car lists and newspapers, or take the car to a used car lot. The best source may be the “retail value” on kellybluebook.com.

For unsecured household goods, determine the value that you would pay for the items at someone else’s yard sale or at a thrift store or a used furniture or clothing store.

**Income**: The income schedule should be supported by pay stubs and income tax returns for the last two years. If your employer does not provide pay stubs, please bring a copy of your paycheck and ask your employer for its worksheet specifying what is deducted from your gross salary.

The monthly expense schedule should reflect the cost of running your household. Many expenses will have been paid in cash, so you must use a best estimate. Remember to include such items as car maintenance (not just gas), yearly car licenses and taxes, co-pays on medical and prescription drug items, and over-the-counter medications. You may have not been purchasing new clothing. Reasonable expenses for replacing clothing need to be included. If you do not have health insurance, you need to determine exactly what it will cost.

You may discover that your expenses are greater than your income. Because this is a post-bankruptcy expense schedule, you cannot list payments on debts, such as credit cards, that you will discharge. You do need to include expenses that you will have to pay. When in doubt, list the expense and let the attorney decide if the expense is relevant.

Please remember that you are completing these documents for public filing, under penalty of perjury. They can be examined by all sorts of unfriendly people, such as ex-spouses and angry creditors. Concealment of assets and making false statements are federal crimes.

Also remember that the only dumb questions are the ones you do not ask. What you don’t know can get you into a great deal of trouble. It is better to ask the question now than to try to fix it later.
A failure to file a motion to continue or extend an existing spousal support order before termination of support will preclude modification of spousal support. ORS 107.135(1)(a) provides that the court has the power at any time to set aside, alter, and modify any spousal support portion of a judgment. Oregon cases have construed the statute to require that any motion to modify a spousal support award for the extension of support must be filed before the final payment date under the original judgment. Wrench and Wrench, 98 Or App 352 (1989), rev den, 308 Or 608 (1989).

In Wrench, husband was required to make his final payment of spousal support on October 1, 1988. Husband made that payment on October 3, 1988. On October 11, 1988, wife filed a motion to modify the decree to extend the term of support. The trial court dismissed wife’s motion on the ground that the motion was untimely. The court of appeals affirmed, holding that the decree created an obligation to pay the support on the first day of the month. As with a promissory note, when the final payment is made, the obligation is discharged. Therefore, after October 3, 1988, husband had no obligation that would support a modification. The Wrench case stands for the proposition that a modification must be filed before the date the last payment is due, not any time during the final month of the support obligation.

In Harkins and Harkins, 200 Or App 468 (2005), rev den, 340 Or 672 (2006), the court of appeals applied the same principle to prepayment. The court held that a prepayment of spousal support terminates a support obligation and that a motion for modification made after prepay-

When a client wants a spousal support obligation continued beyond the term set in the original judgment, the attorney must file a motion before the last support payment due date and before the support obligation is paid in full. An attorney should file as soon as the substantial change in circumstances is known.

Gary J. Zimmer
Zimmer Family Law LLC
Thanks to Katie A. Carson of Zimmer Family Law, LLC, for her assistance with this article.
WHEN TO FILE SEPARATE RETURNS

Most married couples file joint income tax returns without giving their decision a second thought. However, some circumstances – such as finances, potential liabilities, and marital instability – can create a situation in which one or both spouses are better off filing a separate return.

Joint filing is commonly financially advantageous for two reasons. First, federal joint rates are lower than separate rates and often reduce the tax due from both spouses by more than 15%. Second, joint returns sometimes allow income earned by one spouse to be reduced by losses and deductions generated by the other spouse.

Joint filing, however, makes both spouses jointly and severally liable for any tax due – both the tax shown due on the joint return and any tax due that might later be discovered through an audit. Accordingly, joint filing makes sense when the tax has been or can be promptly paid, and the couple is confident that an audit would not result in additional tax. Some couples, on the other hand, should consider filing separate income tax returns.

This article discusses three situations in which separate filing might make sense: (1) The couple can’t pay the tax due; (2) One spouse is taking aggressive positions on the couple’s return; or (3) The couple is contemplating divorce or separation.

CAN’T PAY THE TAX

In most instances, a household’s tax problems arise from the earnings of just one spouse. If one spouse has incurred more tax liability than the couple can quickly and conveniently pay, the couple should consider filing separate returns. The hefty penalties and interest charged on unpaid taxes make it difficult to retire large tax debts. Low-income households and households experiencing financial problems may have too little discretionary income to keep up with interest and penalty accruals. Couples at all income levels are routinely surprised at how quickly tax liabilities grow to an unmanageable size; a self-employed businessperson, for example, who fails to file three or four years of returns and make the required estimated payments usually has a liability so large that it will be difficult or impossible to pay.

The couple’s instinctive reaction when one spouse has incurred a significant tax is to file a joint return to take advantage of the lower rates. If, however, so much tax has been incurred that the tax will be difficult or impossible to pay, the couple may have to file bankruptcy or pursue a federal or state offer in compromise. (Most income tax liabilities can eventually be discharged in bankruptcy.) If bankruptcy or an offer in compromise seems the likely or only solution, the household may weather the tax collection process ahead more easily if only one spouse is liable for the tax. Separate return filing will keep one of the spouses immune from the tax problem.

The Bankruptcy Code prevents individuals from discharging most tax liabilities during the three-year period following the date the tax return was due. Weathering the collection efforts of taxing agencies during this three-year period can be very difficult. Separate return filing means that the non-liable spouse’s bank accounts, wages, and equity in assets will not be drawn into the tax and bankruptcy processes – a significant benefit to both spouses. It is true that the higher separate tax rates will result in more tax owed for the spouse who earned the income. However, this larger
The amount of tax will not matter if relief is eventually obtained through the subsequent bankruptcy proceeding or offer in compromise.

AGGRESSIVE RETURN POSITIONS

As noted above, joint filing makes both spouses liable for the tax shown due in a return, in addition to any tax that is later discovered through an audit. An individual who believes his or her spouse is taking overly aggressive positions on the return may want to consider filing a separate return to avoid joint liability for taxes due. He or she might be able to invoke state and federal laws that protect innocent spouses, but there is no guarantee of such relief. The best way for an innocent spouse to avoid liability for the aggressive return positions of his or her spouse is not to execute a joint return at all.

Federal and state “innocent spouse relief” is sometimes available for spouses who become liable through an audit for taxes not shown as due on joint returns. 26 USC §6015; ORS 316.368, 316.369. If available, innocent spouse relief extinguishes one spouse’s liability for all or part of the taxes that were previously jointly owed. In most instances, the applying spouse must show that he or she did not know there was additional tax due when the joint return was executed and that relief from the tax liability is equitable in light of the facts and circumstances. Innocent spouse relief has become easier to obtain in the last few years, but the process is by no means convenient or certain. Successfully obtaining innocent spouse relief can be a lengthy and expensive process, as the IRS and the courts apply the requirements stringently.

Obtaining innocent spouse relief for a tax liability that is even more difficult. Only “equitable relief” is generally available for a spouse who signed the joint return knowing that the couple owed unpaid taxes. 26 USC § 6015(f). Equitable relief is generally available only in cases of significant hardship or when the “innocent spouse” signed the return under duress.

DIVORCE

Marital instability is another reason to consider filing separate returns. If a couple experiencing marital difficulties believes that they have paid the tax owed and that there is little chance of additional tax due, joint filing probably still makes sense. If, however, the couple cannot pay the tax owed or if one spouse insists on taking aggressive return positions, they should consider separate filing. Divorce does not undo the joint and several liability created by a jointly filed return.

Divorce and separation agreements often make one spouse responsible for paying taxes that were incurred during the marriage, but these types of agreements between the parties are not binding on taxing agencies. If the spouse who was contractually assigned the joint liabilities incurred during the marriage does not or cannot pay what is owed, the taxing agencies are free to pursue either or both spouses for the full amount of the tax, regardless of the divorce or separation agreement. In that event, the only remedy available to a spouse who is required to pay more tax than required by the divorce or separation agreement is a claim for contribution or indemnification against the other (non-paying) spouse.

If the couple is divorced or legally separated, innocent spouse relief may also be available under 26 USC §6015(c) and ORS 316.368. When relief is allowed under these statutes, the joint tax liability is allocated between the parties. The federal and state statutes allocate the liability
differently. Death of a spouse may also qualify the surviving spouse for innocent spouse relief under these same statutes.

**HEDGING THE BET**

Internal Revenue Code (IRC) Section 6015(b) sometimes allows a couple to hedge their bet on joint versus separate filing by allowing the couple to elect joint rates after initially filing separate returns. The joint election must be made within three years from the due date of the separate returns (not counting extensions), and cannot be made if either spouse has, with respect to the tax year at issue: (1) timely filed a petition in the U.S. Tax Court; (2) commenced a refund suit; (3) entered into a closing agreement with the IRS; or (3) entered into a compromise of a civil or criminal liability. Treas. Reg. 1.6013-2(b). To elect joint rates under IRC Section 6015(b), the IRS only requires that a joint return be filed. A cover letter, however, should accompany the return to clarify that the return is being filed to elect joint rates after separate returns have been filed. This right to later elect joint rates allows a couple undergoing financial difficulties to initially keep one spouse immune from an unpaid tax while still benefiting from the lower joint rates when the couple’s financial difficulties have passed.

Couples who owe significant tax need to weigh the benefits of lower joint rates against the burden of joint liability, particularly if they are struggling with finances or their marriage. If you represent both spouses, be careful with advice on return filing strategies because of potential conflicts. If the spouses become divided on the return filing issue, encourage them to seek independent advice through separate counsel.

Jeffrey M. Wong

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Tax Tips for Family Law Lawyers

Family law attorneys can find themselves in trouble if they are not familiar with tax laws. The following are tips to help family law attorneys avoid some of the biggest traps in this area.

Sale of the Family Home

Under 26 USC §121, an individual may exclude from income up to $250,000 of gain from the sale of a principal residence if he or she owned and occupied the property as a principal residence for two out of the last five years. Married couples filing jointly can exclude up to $500,000 if either spouse meets the two-out-of-the-last-five-years test. A divorced spouse can attach the ownership of the former spouse for purposes of meeting the test but can still only exclude up to $250,000.

**Tax Tip:** It may make sense for the parties to sell a low-basis, highly appreciated residence before the divorce is final to maximize the $500,000, but they must still be married at the end of the tax year to maximize the exclusion.

Spousal Support

Spousal support is tax-deductible to the payor (and taxable income to the payee) under 26 USC §71(a) and §215 if the payments are made in cash and:

1. The payment is received by a spouse or ex-spouse under a divorce or separation instrument;
2. The applicable instrument does not identify the payment as not deductible to the payor and not includable in the income of the payee (an opt-out provision);
3. The payor and payee are not members of the same household when the payment is made (there is a limited exception to this); and
4. There is no liability to make any such payment after the death of the payee ex-spouse.

**Tax Tip:** Make sure that the spousal support is designated to terminate at the death of the payee each time it is referenced, even in the Money Judgment summary. See *Fifithian v. United States*, 90 AFTR2d (RIA) 6210 (9th Cir. 2002), in which the Ninth Circuit affirmed a district court ruling that held payments were not tax-deductible alimony because the Money Judgment section did not state that the spousal support payments terminated at the death of the obligee. Despite such language in the body of the judgment and the property settlement agreement, the court found ambiguity and gave greater weight to the Money Judgment section because it was certified by the lawyers.

**Tax Tip:** Be careful of stair-stepping spousal support down too fast. Under the front-loading rules of 26 USC §71(f), if alimony decreases too rapidly, some portion will be reclassified (recaptured) as property settlement. The calculation is complicated, but be mindful of recapture if the annual alimony amounts decrease by more than $15,000 a year in any of the first three years of payments.

Property Settlement

Under 26 USC §1041, no gain or loss is recognized on the transfer of property between spouses, or between former spouses if the transfer is incident to divorce. A transfer is considered incident to divorce if it occurs within one year of the end of the marriage or is “related to” the cessation of the marriage. Under the regulations, a transfer is presumed “related to” the cessation of the marriage if it is pursuant to a divorce in-
The six-year period is only a presumption. Sometimes transfers incident to divorce need to occur outside the six-year window. In such cases, the divorce instrument should clearly designate the transfer as tax-free under 26 USC §1041.

**Tax Tip:** The redemption of corporate stock or other business interest in a closely held entity can be a trap for the unwary. Unexpected ordinary income dividend treatment may result in taxable income when the transferor assumed that no tax ramifications would occur due to Section 1041.

### Stock Options

Stock options come in two forms for income tax purposes: incentive stock options (ISOs) (See 26 USC §§421-424) and non-qualified stock options. ISOs are generally non-transferrable. See 26 USC §422(b). Stock received from the exercise of an ISO may be transferred incident to divorce, and such transfer will not be a disqualifying transfer. See 26 USC §424(c)(4).

Non-qualified stock options are freely transferrable, unless restricted by the governing instrument. The IRS, in Rev. Rul. 2002-22, held that the transferee spouse will recognize the income from the exercise of a non-qualified stock option.

**Tax Tip:** The exercise of a non-qualified stock option will trigger tax withholdings. Under Rev. Rul. 2004-60, the employer is required to withhold a 25% flat supplemental wage rate for income taxes and additional amounts for FICA and FUTA taxes. The transferee needs to factor these amounts in valuing the options. The transferee will get the credit for the income tax withholding, but the FICA and FUTA taxes are credited to the transferor’s account for purposes of calculating future benefits.

### Dependency Exemptions

The tax laws contain a number of favorable provisions for the support of a dependent child or other dependent. These provisions include the dependent exemption, the child tax credit, the child and dependent care credit, the earned income credit, and the Hope and Lifetime Learning Credits. To qualify as a dependent under 26 USC §152, a child must:

1. Be the taxpayer’s natural or adopted child, stepchild, eligible foster child, sibling, or descendant;
2. Reside with the taxpayer for more than half the year;
3. Be under the age of 19, or 24 if a full-time student, or permanently disabled; and
4. Not have provided more than half of his or her own support.

For purposes of claiming the dependent exemption, under 26 USC §152(d), a taxpayer may claim another individual, who is not the taxpayer’s child, as a qualifying relative if:

1. The individual is related to the taxpayer, including an individual, other than a spouse, who has the same principal place of abode as the taxpayer and is a member of the taxpayer’s household;
2. The individual’s gross income is less than the exemption amount;
3. The taxpayer provides over half of the individual’s support; and
4. The individual is not a qualifying child of the taxpayer or anyone else.

The taxpayer could also claim the Hope and Lifetime Learning Credits for such an individual.

In the divorce context, the custodial parent is entitled to claim a qualifying child unless the custodial parent signs an instrument releasing the right to the dependency exemption to the non-custodial parent. The preferable approach is to have the custodial parent sign an IRS Form 8332. The release of the dependency credit also releases the child tax credit, but not the child care credit, earned income credit, or head of household status.

**Tax Tip:** The custodial parent is defined as the parent with whom the child spends the most overnights. If the parents share equal parenting time, the custodial parent is the parent with the higher income. This rule is only relevant if the custodial parent has not effectively released his or her right to the exemption.

**Tax Tip:** The circuit court handling the divorce has no jurisdiction to allocate the dependency exemption to the non-custodial parent. The divorce decree itself is insufficient, unless it contains all of the information required by the regulations and on IRS Form 8332, including the custodial parent’s signature. See *Mace v. Comm’r*, T.C. Summ. Op. 2005-89.

### Domestic Partners and Unmarried Individuals

Due to the Federal Defense of Marriage Act, P.L. 104-199 (1996), 1 USC §7, registered domestic partnerships are not recognized for federal income tax purposes. In addition, many same-sex and opposite-sex couples for whatever reason
never take the step to register or marry. When these couples split up, payments or transfers of property will not be covered by the tax rules above.

**Tax Tip:** The parties should agree on the tax consequences of any payments or transfers in any settlements. Otherwise, the transferor may issue an IRS Form 1099 to claim a deduction and the transferee will bear the burden of proving that the amounts or property received were gifts or in exchange for property, not compensation income. *See Reynolds v. Comm’r*, T.C. Memo 1999-62, and *Yang v. Comm’r*, T.C. Summ. Op. 2008-56.

MICHAEL C. WETZEL
FITZWATER MEYER, LLP

The author would like to acknowledge David G. Gannett, of David G. Gannett LLC; and the late Joseph Wetzel, for their contributions to the material for this article.
Release/Revocation of Release of Claim to Exemption for Child by Custodial Parent

Name of noncustodial parent

Name of child

Signature of custodial parent releasing claim to exemption

Custodial parent’s SSN

Date

Note. If you choose not to claim an exemption for this child for future tax years, also complete Part II.

Part II Release of Claim to Exemption for Future Years (If completed, see Noncustodial Parent on page 2.)

I agree not to claim an exemption for

Name of child

for the tax year(s).

(Specify. See instructions.)

Signature of custodial parent releasing claim to exemption

Custodial parent’s SSN

Date

Part III Revocation of Release of Claim to Exemption for Future Year(s)

I revoke the release of claim to an exemption for

Name of child

for the tax year(s).

(Specify. See instructions.)

Signature of custodial parent revoking the release of claim to exemption

Custodial parent’s SSN

Date

General Instructions

What’s New

Post-2008 decree or agreement. If the divorce decree or separation agreement went into effect after 2008, the noncustodial parent cannot attach certain pages from the decree or agreement instead of Form 8332. See Release of claim to exemption below.

Definition of custodial parent. New rules apply to determine who is the custodial parent and the noncustodial parent. See Custodial Parent and Noncustodial Parent on this page.

Purpose of Form

If you are the custodial parent, you can use this form to do the following.

• Release a claim to exemption for your child so that the noncustodial parent can claim an exemption for the child.

• Revoke a previous release of claim to exemption for your child.

Release of claim to exemption. This release of the exemption will also allow the noncustodial parent to claim the child tax credit and the additional child tax credit (if either applies). Complete this form (or sign a similar statement containing the same information required by this form) and give it to the noncustodial parent. The noncustodial parent must attach this form or similar statement to his or her tax return each year the exemption is claimed. Use Part I to release a claim to the exemption for the current year. Use Part II if you choose to release a claim to exemption for any future year(s).

Note. If the decree or agreement went into effect after 1984 and before 2009, you can attach certain pages from the decree or agreement instead of Form 8332, provided that these pages are substantially similar to Form 8332. See Post-1984 and pre-2009 decree or agreement on page 2.

Revocation of release of claim to exemption. Use Part III to revoke a previous release of claim to an exemption. The revocation will be effective no earlier than the tax year following the year in which you provide the noncustodial parent with a copy of the revocation or make a reasonable effort to provide the noncustodial parent with a copy of the revocation. Therefore, if you revoked a release on Form 8332 and provided a copy of the form to the noncustodial parent in 2010, the earliest tax year the revocation can be effective is 2011. You must attach a copy of the revocation to your tax return each year the exemption is claimed as a result of the revocation. You must also keep for your records a copy of the revocation and evidence of delivery of the notice to the noncustodial parent, or of reasonable efforts to provide actual notice.

Custodial Parent and Noncustodial Parent

The custodial parent is generally the parent with whom the child lived for the greater number of nights during the year. The noncustodial parent is the other parent. If the child was with each parent for an equal number of nights, the custodial parent is the parent with the higher adjusted gross income. For details and an exception for a parent who works at night, see Pub. 501.

Exemption for a Dependent Child

A dependent is either a qualifying child or a qualifying relative. See your tax return instruction booklet for the definition of these terms. Generally, a child of divorced or separated parents will be a qualifying child of the custodial parent. However, if the special rule on page 2 applies, then the child will be treated as the qualifying child or qualifying relative of the noncustodial parent for purposes of the dependency exemption, the child tax credit, and the additional child tax credit.
Special Rule for Children of Divorced or Separated Parents

A child is treated as a qualifying child or a qualifying relative of the noncustodial parent if all of the following apply.

1. The child received over half of his or her support for the year from one or both of the parents (see the Exception below).

2. Public assistance payments, such as Temporary Assistance for Needy Families (TANF), are not support provided by the parents.

3. Either of the following applies.

a. The custodial parent agrees not to claim an exemption for the child by signing this form or a similar statement. If the decree or agreement went into effect after 1984 and before 2009, see Post-1984 and pre-2009 decree or agreement below.

b. A pre-1985 decree of divorce or separate maintenance or written separation agreement states that the noncustodial parent can claim the child as a dependent. But the noncustodial parent must provide at least $600 for the child’s support during the year. This rule does not apply if the decree or agreement was changed after 1984 to say that the noncustodial parent cannot claim the child as a dependent.

For this rule to apply, the parents must be one of the following.

- Divorced or legally separated under a decree of divorce or separate maintenance.
- Separated under a written separation agreement.
- Living apart at all times during the last 6 months of the year.

If this rule applies, and the other dependency tests in your tax return instruction booklet are also met, the noncustodial parent can claim an exemption for the child.

Exception. If the support of the child is determined under a multiple support agreement, this special rule does not apply, and this form should not be used.

Post-1984 and pre-2009 decree or agreement. If the divorce decree or separation agreement went into effect after 1984 and before 2009, the noncustodial parent can attach certain pages from the decree or agreement instead of Form 8332, provided that these pages are substantially similar to Form 8332. To be able to do this, the decree or agreement must state all three of the following.

1. The noncustodial parent can claim the child as a dependent without regard to any condition (such as payment of support).
2. The other parent will not claim the child as a dependent.
3. The years for which the claim is released.

The noncustodial parent must attach all of the following pages from the decree or agreement.

- Cover page (include the other parent’s SSN on that page).
- The pages that include all of the information identified in (1) through (3) above.
- Signature page with the other parent’s signature and date of agreement.

Example. In 2007, you released a claim to exemption for your child on Form 8332 for the years 2008 through 2012. In 2010, you decided to revoke the previous release of exemption. If you completed Part III of Form 8332 and provided a copy of the form to the noncustodial parent in 2010, the revocation will be effective for 2011 and 2012. You must attach a copy of the revocation to your 2011 and 2012 tax returns and keep certain records as stated earlier.

Noncustodial Parent

Attach this form or similar statement to your tax return for each year you claim the exemption for your child. You can claim the exemption only if the other dependency tests in your tax return instruction booklet are met.

If the custodial parent released his or her claim to the exemption for the child for any future year, you must attach a copy of this form or similar statement to your tax return for each future year that you claim the exemption. Keep a copy for your records.

Note. If you are filing your return electronically, you must file Form 8332 with Form 8453, U.S. Individual Income Tax Transmittal for an IRS e-file Return. See Form 8453 and its instructions for more details.

Specific Instructions

Custodial Parent

Part I. Complete Part I to release a claim to exemption for your child for the current tax year.

Part II. Complete Part II to release a claim to exemption for your child for one or more future years. Write the specific future year(s) or "all future years" in the space provided in Part II.

To help ensure future support, you may not want to release your claim to the exemption for the child for future years.

Part III. Complete Part III if you are revoking a previous release of claim to exemption for your child. Write the specific future year(s) or "all future years" in the space provided in Part III.

The revocation will be effective no earlier than the tax year following the year you provide the noncustodial parent with a copy of the revocation or make a reasonable effort to provide the noncustodial parent with a copy of the revocation. Also, you must attach a copy of the revocation to your tax return. You must also keep for your records a copy of the revocation and evidence of delivery of the notice to the noncustodial parent, or of reasonable efforts to provide actual notice.

Paperwork Reduction Act Notice. We ask for the information on this form to carry out the Internal Revenue laws of the United States. You are required to give us the information. We need it to ensure that you are complying with these laws and to allow us to figure and collect the right amount of tax.

You are not required to provide the information requested on a form that is subject to the Paperwork Reduction Act unless the form displays a valid OMB control number. Books or records relating to a form or its instructions must be retained as long as their contents may become material in the administration of any Internal Revenue law. Generally, tax returns and return information are confidential, as required by Internal Revenue Code section 6103.

The average time and expenses required to complete and file this form will vary depending on individual circumstances. For the estimated averages, see the instructions for your income tax return.

If you have suggestions for making this form simpler, we would be happy to hear from you. See the instructions for your income tax return.
YES. You DO Need to Know About SCRA
(Servicemembers' Civil Relief Act)

Before you skip this article under the impression that you don’t need to know anything about the Servicemembers’ Civil Relief Act (SCRA) (the Act) because you don’t practice “military law,” STOP. Regardless of what area of law your practice involves, SCRA could affect you. SCRA does not regulate one substantive area or particular set of circumstances. The Act focuses on the person—the servicemember—and conveys a wide bundle of rights. As a result, the Act’s reach extends to almost every legal situation the servicemember may encounter in his or her life during deployment.

In early 2009, 3,500 servicemembers of the Oregon National Guard’s 41st Brigade Combat Team will be activated. This will be the largest deployment of military personnel from Oregon since World War II. What does that mean for you? It means that in every case you take, you must consider the implications of SCRA. Any case involving a servicemember on deployment status may be stayed until the servicemember returns to Oregon.

Why? SCRA, previously known as the Soldiers’ and Sailors’ Civil Relief Act (SSCRA), contains numerous protections for servicemembers in civil actions and limited criminal actions. Found at 50 U.S.C. Appendix Sections 501 to 596, the most frequently triggered provisions of the Act are:

- Interest rate reduction on debt upon activation;
- In general, legal proceedings stayed on servicemember’s request or court’s own motion; and
- In particular, family law matters stayed on servicemember’s request or court’s own motion, including child custody and divorce cases.

Although these are the most frequently triggered provisions, many practitioners might be surprised to learn that SCRA affects almost every area of law, including:

- Adoption;
- Criminal law probation violations involving restitution and fines;
- Landlord/tenant actions;
- Life, health, and professional liability insurance;
- Property issues, including personal and business property matters;
- Public lands rights;
- Small claims actions;
- Vehicle purchase contracts; and
- Will contests.

Federal Preemption

In several state SCRA cases, judges decided the case based on Oregon law while either overlooking or trying to explain away the preemptive nature of SCRA. Both of these rationales, however, are erroneous. SCRA, on its face, preempts state law. If a direct conflict exists between SCRA and state law or another federal statute, SCRA protections control.

SCRA protections occur most frequently in child custody cases. More than one Oregon judge has decided that “the best interests of the child” override SCRA protections. However, the Act applies to all state and federal judicial and

Continued on page 2
administrative proceedings. Presumptively, probation violations in criminal law are also covered. Noteworthy is that Congress amended the Act in 2008 and specifically identified child custody proceedings as subject to SCRA protections. Similarly, dissolution proceedings are governed by the Act.

**Requirement to Notify the Court**

The requirement to notify the court of the military status of a party is on the moving party in the case. However, the court should ask, in every case, whether a servicemember is involved. If the answer is “I don’t know,” the case should be continued until that information can be provided. This notice requirement also applies to pending cases that were filed before the servicemember was activated. Although the moving party has ultimate responsibility to inform the court of the military status of the parties, any attorney representing a servicemember should notify the court at the earliest possible opportunity.

Proceeding with the case when an active-duty servicemember is involved will, at the least, result in any judgment being voidable. At most, it may result in a civil or criminal action permitted by SCRA. It may also result in a disciplinary action against the attorney and/or the judge who failed to comply with the Act. Attorneys can use the following Web site to determine the military status of any party to a legal proceeding: [www.dmdc.osd.mil/scra/owa/home](http://www.dmdc.osd.mil/scra/owa/home). (See “Determining a Party’s Military Status,” *In Brief*, August 2007, p. 3.)

**Appointment of Attorneys**

If a party appears to be in active military service and has not yet made an appearance, SCRA requires the court to appoint an attorney to represent the party before it can enter a judgment for the plaintiff. A court must also appoint an attorney to represent an active-duty servicemember if it denies the servicemember’s stay request beyond the initial mandatory 90 days. SCRA, however, does not address where or how a court will locate an attorney to appoint or how the attorney will be paid; SCRA also does not allow the court to appoint an attorney if the servicemember objects.

While the Military Assistance Panel (MAP) of the Oregon State Bar is established to assist servicemembers in legal matters, it will get involved only at the servicemember’s request. As many know, MAP is comprised of more than 150 attorneys located throughout the state who have volunteered their time and services at either low cost or no cost to assist servicemembers and their dependents with legal matters that arise during or around deployment. If MAP receives a request to fill a court appointment, it will attempt to contact the servicemember involved to determine whether he or she wishes to be represented in the pending matter. MAP may be contacted through Kay Pulju, Director of Communications and Public Services, at the Oregon State Bar, at 503-620-0222, ext. 402.

**Proposed Legislation**

The Military Assistance Panel is proposing two pieces of legislation to the Oregon Legislature for the 2009 session. The first proposal adds teeth to SCRA under Oregon law by putting damage provisions and attorney fees in place when an attorney has to file suit to reverse violations of SCRA. The second proposal creates tax credits for attorneys who represent servicemembers pro bono utilizing MAP guidelines.

**SCRA CLE**

On March 6, 2009, the Military Assistance Panel, the Professional Liability Fund, and the Oregon State Bar are co-sponsoring a half-day CLE to provide in-depth information about SCRA. This CLE will be held just before the activation of the 41st Brigade to educate all members of the Oregon legal community about how SCRA provisions are likely to affect their law practices. In addition to an overview of the Act, the CLE will explain the implications of SCRA for practitioners of family law, employment law (Uniformed Services Employment and Reemployment Rights Act or USERRA), consumer law, commercial law, property law, tax law, and administrative law, as well as general civil litigation. See the box below for information on how to register.

> Thanks to Captain Bryan J. Libel and Michael B. Mendelson for their assistance with this article.

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**Free CLE on SCRA**

On March 6, 2009, the OSB Military Assistance Panel (MAP), the Professional Liability Fund, and the Oregon State Bar will present "The One For All: What Every Practitioner Must Know About the Servicemembers' Civil Relief Act" at the Oregon State Bar Center in Tigard. This free half-day CLE will provide an overview of SCRA, a panel of practitioners will discuss how the rules apply to various areas of the law, and a panel of judges will provide tips on how to avoid pitfalls. To download a registration form, go to [www.osbplf.org](http://www.osbplf.org) and click on Upcoming Seminars under Loss Prevention.
The Servicemembers Civil Relief Act Is Still Relevant

The Servicemembers Civil Relief Act (SCRA) (50 U.S.C. App. Sections 501-596) remains an important federal protection that attorneys need to be aware of in daily practice. Although the number of military personnel deployed overseas has recently decreased, Americans continue to serve abroad. The Oregon National Guard as well as Oregon Marine, Army and Air Force Reservists have received notice that over 1000 Oregonians will likely mobilize during the next 18 months. SCRA protections affect not only Servicemembers, but also their spouses/partners, dependents, creditors, landlords, banks, insurance carriers, and many others with contractual, economic, and legal relationships.

The SCRA protections apply to members of the Armed Forces and the Reserve Forces (National Guard and Reserves) who are called to active federal service. The SCRA also applies to members of the Coast Guard as well as officers in the Public Health Services and National Oceanic and Atmospheric Administration while in support of the Armed Forces.

Servicemembers called to active federal service are afforded unique protections under the SCRA in cases of foreclosures, repossessions, evictions, judicial and administrative proceedings, certain lease terminations, and default judgments. Some of the most frequently utilized provisions include the 6% cap on consumer interest rates, the stay of civil or administrative proceedings on the Servicemembers’ request or the court’s motion, and family law matters, including child custody and divorce cases.

Ascertaining Military Status

Given the unique protections and opportunities afforded Servicemembers that touch on numerous areas of the law, as well as the procedural requirements for proceedings involving Servicemembers, the safest practice – no matter what your area of the law – is to ascertain, at the outset of the representation, the military affiliation and status of not only your client, but also of the other party or parties. Counsel for both parties should undertake this inquiry, as the rights and responsibilities of each are affected if either party qualifies for SCRA protections.

One example where this arises frequently is with default judgments. ORCP 69C requires that a party seeking default must file an affidavit or declaration along with the motion supporting that default is appropriate and containing facts sufficient to establish whether the party against whom the order is sought is or is not a person in military service, or stating that the movant is unable to determine whether the party against whom the order is sought is in military service as required by Section 201(b)(1) of the Servicemembers Civil Relief Act, 50 App. U.S.C.A. §521, as amended.

The requirement to notify the court of the military status of a party is on the moving party. However, the court should ask as a matter of course whether a Servicemember is involved. If the moving party does not know the answer, then the court should allow sufficient opportunity for determination. Proceeding with the case or judgment where the Servicemember is unavailable to due to military service will, at the least, result in a voidable judgment. At most, it may result in civil or criminal action permitted under the SCRA.
To find out whether a party is in the military, go to the official Servicemembers Civil Relief Act (SCRA) Website maintained by the Department of Defense at https://www.dmdc.osd.mil/appj/scra/. Enter the party’s last name and Social Security number. Further information is available in the User’s Guide and FAQ sections of the Website.

**SCRA Foreclosure Amendment**

In a nod to economic challenges, a recent update to the federal law impacts foreclosures on Servicemembers’ property. On August 6, 2012, President Obama signed into law the Honoring America’s Veterans and Caring for Camp Lejeune Families Act of 2012, Pub. L. 112-154, 126 Stat. 1165 (2012) which, in part, amended section 303 of the SCRA. SCRA section 303 addresses obligations secured by a mortgage, trust deed, or other security similar to a mortgage on real or personal property owned by a Servicemember.

The provision applies only to obligations that originated before the Servicemember entered into active federal military service under Title 10, U.S.C. and for which the Servicemember is still obligated. (For example, it applies to obligations incurred by National Guard Soldiers before they were called to active federal service.) The recent amendment extended the period during which certain SCRA protections apply.

Effective February 2, 2013:

- a sale, foreclosure, or seizure of property based on a breach of such a secured obligation is not valid if made during the period of military service or within one year thereafter, unless it is made pursuant to a court order or a waiver by the Servicemember; and
- a court may, on its own motion, and shall, upon application by a Servicemember whose ability to comply with the obligation is materially affected by military service, stay the proceedings or adjust the obligation to preserve the interests of all parties at any time during the period of military service or within one year thereafter.

This extension ends December 31, 2014. Beginning January 1, 2015, there will be a period of 90 days after the end of the Servicemember’s military service during which a foreclosure, sale, or seizure of the Servicemember’s property, based on a breach of a mortgage, trust deed, or other security, without a court order or waiver, will not be valid. During this period, a court may also stay proceedings enforcing such obligations. (Office of the Comptroller of the Currency Bulletin, dated November 19, 2012) [http://www.occ.gov/news-issuances/bulletins/2012/bulletin-2012-37.html](http://www.occ.gov/news-issuances/bulletins/2012/bulletin-2012-37.html).

**Oregon Laws Supporting SCRA**

In addition to the federal protections, Oregon has further enhanced Servicemembers’ rights and remedies. Oregon has also taken steps to weave SCRA requirements and protections into common practices. Notice of SCRA rights, for example, has become standard practice.

The 2009 Legislature enacted a couple of laws supporting SCRA. In May 2009, the Oregon National Guard deployed the largest unit to overseas hostilities since WWII. Effective May 8,
2009, the Oregon Legislature authorized attorney fees and minimum damage awards in addition to any other remedy payable to a Servicemember for the enforcement of a right under SCRA. This benefit was intended to encourage Servicemembers of modest means to seek out legal assistance as necessary and to provide an incentive for attorneys to represent Servicemembers in relatively low dollar value cases.

The attorney fees and damages provision of ORS 30.138 was complimented by ORS 30.136, also enacted in 2009, which identified Oregon as the appropriate venue for SCRA enforcement. Any contract term or provision providing for a choice of forum other than Oregon in an agreement entered into by an Oregon Servicemember is voidable at the election of the Servicemember. These provisions apply to prosecution of Servicemember rights when called into active federal service and not when called by the Governor for state emergencies.

**New Oregon Protections for Servicemembers**

Several new bills affecting Servicemembers have already emerged from the 2013 Legislature. At the request of the OSB Military and Veterans Law Section, Senate Bill 125 was introduced relating to contested case hearings. It will require state agencies to provide notice to parties in contested case hearings of the SCRA right to stay proceedings until military service affords reasonable availability to defend. SB 125 was signed into law on June 4, 2013, and becomes effective September 1, 2013.

Relating to criminal proceedings, Senate Bill 124 was proposed by the OSB Military and Veterans Law Section with support of Oregon Criminal Defense Lawyers Association. This bill creates a new mitigating factor that explicitly authorizes courts at sentencing to consider military service. It does so by creating a new ORS 137.090(2), which states: “In determining mitigation, the court may consider evidence regarding the defendant’s status as a servicemember as defined in ORS 135.88.” At least in felony cases, courts will need to make a “substantial and compelling” finding in order to rely on SB 124 to impose a mitigated (downward) departure. ORS 137.671(1); OAR 213-008-0001. For guidance in meeting this requirement, defense counsel should consult established case law supporting reliance on a defendant’s military service as a reason for imposing a mitigated sentence. The bill was signed into law June 6, 2013, and became effective immediately.

The 2013 Oregon Legislature also expanded what is unofficially known as the Oregon SCRA, located in Chapter 399, to address suspension of contractual obligations of Servicemembers called to active federal service or active state service by order of the Governor. House Bill 2083 was introduced at the request of Governor Kitzhaber, M.D. on behalf of the Oregon Military Department. Signed into law on June 18, 2013, with an effective date of January 1, 2014, the new law allows for suspension and reinstatement of contractual obligations without fee, penalty, loss of deposit, or additional cost. The law applies to telecommunications services, Internet services, health spa services, exercise or athletic activities offered by a health club, and certain television services. This law will provide a unique protection to Servicemembers that allows for modification of long-term contracts in which the need to cancel or suspend arises as the result of call to duty.
Additional Resources

In the February 2009 issue of In Brief, the OSB Professional Liability Fund published an article drawing attention to the SCRA and its application to local courts and attorneys: “YES. You DO Need to Know About SCRA.” That article and significant other resources abound to assist local practitioners with application of the SCRA to their client’s situation. See also “Determining a Party’s Military Status,” In Brief, August 2007.

The ABA Standing Committee on Legal Assistance to Military Personnel is a premier resource of attorneys and experiences from around the country. The United States Army Judge Advocate General’s School also published a 2006 Guide to the Servicemembers’ Civil Relief Act, which is a comprehensive overview of the law and application. The Service Members Law Center stands as a premier organization that assists with SCRA enforcement across the nation. The Director of SMLD, CAPT (Ret) Sam Wright, has authored and co-authored over 500 law reviews on areas of law affecting citizen soldiers.

Locally, the Oregon State Bar has attorneys within the Military Legal Assistance Panel and the Military & Veterans Law Section who bring a depth of experience and stand ready to answer questions, provide resources, or assist as needed.

Mark A. Ronning, LTC, JA
Oregon National Guard
Staff Judge Advocate
ACCESSING RETIREMENT BENEFITS AFTER DIVORCE

Tricks and Traps

by Paul DeBast

1. Terms.


*Retirement Equity Act of 1984* ("REA") was adopted to permit distribution of benefits in ERISA controlled retirement plans upon dissolution of marriage. REA added §414(p) to the Internal Revenue Code. REA does not apply to IRAs.

*IRC §414(p)* permits the assignment of rights in most employer sponsored retirement plans through the use of a Qualified Domestic Relations Order ("QDRO").

*Individual Retirement Account* ("IRA") is a trust created for the benefit of an individual. IRAs are not subject to ERISA or REA. IRAs come under the provisions of IRC §408. A QDRO is not required to transfer IRA benefits incident to divorce. All that is needed is a judgment of divorce plus written instructions directing the IRA custodian to implement the division.

*IRC §408(d)(6)* provides that the transfer of an interest in an IRA to a former spouse under a divorce judgment "... is not to be considered a taxable transfer ... and such interest ... is to be treated as an individual retirement account of such spouse, and not of such individual."

2. Protecting the Alternate Payee.

When a Domestic Relations Order is accepted by the plan administrator, it becomes a Qualified Domestic Relations Order ("QDRO"). Only then is the alternate payee spouse assured that the transferred funds are secure. Until then, it is possible that the participant spouse may separate from employment and seek a withdrawal of the entire account balance. To avoid this the careful practitioner should always try to submit the DRO to the court for entry at the same time as the General Judgment of Dissolution.

As an alternative, if the DRO cannot be submitted at the same time, the attorney should consider immediately sending the plan administrator a copy of the General Judgment along with a letter similar in form to the one appearing at page 4 of this material. According to *Trustees of Screen Actors Guild of America v. Tise*, 234 F3d 415 (9th Cir 2000), this form of notice should offer some protection to the alternate payee while the DRO is being prepared.
3. Tax Treatment of Retirement Account Transfers.

A. No Tax Until Withdrawal. Transfers from one spouse to the other incident to divorce are exempt from tax if proper procedures are followed. See IRC §408 (d)(6) and §414(p).

\[Caution - avoid pitfalls!\] The transfer of IRA funds must be from the transferor’s IRA account to the transferee’s IRA account. A transfer from an IRA directly to the other spouse will result in a tax on the transferor. See for example, Jones v. Commissioner, T.C. Memo 2000-219 where a husband had a check issued from his IRA and endorsed it over to his ex-wife. The tax court upheld the IRS position that the withdrawal did not fall under the narrow exception created by IRC §408(d)(6).

B. Ordinary Income Tax Treatment of Withdrawals. Generally, the transferee spouse will pay ordinary income tax on distributions whether the funds received were from an employer sponsored plan (pursuant to a QDRO) or an IRA. See IRC §72.

C. Ten Percent Penalty on Early IRA Withdrawals. If an IRA transfers withdraws funds from an IRA before attaining age 59\(\frac{1}{2}\), a 10% penalty will apply. IRC §72(i). Exceptions exist where the withdrawal is for: (a) higher education costs; (b) first time home purchase; or (c) if the payment is part of a series of equal payments made over the life of the taxpayer. (IRC §72).

D. Ten Percent Penalty Exception for Transferees of Qualified Plans. The 10% early withdrawal penalty imposed on withdrawals from IRAs is not applicable to taxable distributions to an alternate payee made pursuant to a QDRO. IRC §72(1)(2)(C); however, if the alternate payee rolls any portion of the distribution over to an IRA, the 10% penalty applies upon subsequent withdrawal from the IRA prior to age 59\(\frac{1}{2}\).


QDROs can be used to collect alimony and child support obligations from a former spouse even after a divorce has been concluded.

A. DRO Definition References Alimony and Child Support. IRC §414(p)(1)(B) defines a domestic relations order as follows:

"The term ‘domestic relations order’ means any judgment, decree, or order (including approval of a property settlement agreement) which:

(i) relates to the provision of child support, alimony payments, or marital property rights to a spouse, former spouse, child, or other dependent of a participant, and
(ii) is made pursuant to a State domestic relations law (including a community property law)." [Emphasis added.]

B. Examples of State Court Cases Permitting Use of QDRO to collect Alimony and Child Support.

• *Baird v. Baird*, 843 SW 2d 388 (Mo. App. 1992), upheld an ex-wife’s right to obtain a QDRO to collect delinquent child support and alimony from a pension 12 years after the divorce was finalized.

• *Bruns v. Iowa District Court*, 535 NW 2d 157 (Iowa App. 1995), affirmed the issuance of a post-divorce QDRO to collect alimony arrearages.

• *Stinner v. Stinner*, 520 Pa. 374, 554 A 2d 45 (1989), held a former husband’s pension plan could be attached in order to enforce an alimony support obligation.

• *Hogle v. Hogle*, 732 NE 2d 1278 (Ind. App. 2000), affirmed entry of an Indiana QDRO to collect $375,000 in alimony arrears accrued under a California divorce judgment.

CAVEAT: Not all plans recognize that child support payments made pursuant to a QDRO are taxed to the participant and not to the alternate payee.

End
COPING WITH LEGAL MALPRACTICE CLAIMS

The Professional Liability Fund receives over 700 claims each year against lawyers in private practice. This means that the PLF receives a claim for every eight (8) lawyers it covers. Some claims are valid, while others are not. The majority of these lawyers endeavored to do an excellent job for their clients.

Lawyers react in many different ways to having a legal malpractice claim. Some feel remorse for having made an error and are relieved that the Professional Liability Fund is available to make their clients whole. Others feel angry because they feel that a client is unjustly complaining. Regardless of the merit of the claim, legal malpractice claims take the lawyer's time and energy. Most lawyers are not prepared for the reactions they have to a legal malpractice claim. The following answers to frequently asked questions are provided to warn you about the reactions you may experience, and to offer assistance.

Q. After a legal malpractice claim was filed against me, I felt a generally elevated sense of anxiety for a long time. I found myself having sleepless nights, second guessing every thing I did, reluctant to take on anything that I didn't have extensive experience with, and hesitant to bill for any of my services. Is this common?

A. Yes. The elevated sense of anxiety which you described is the most common reaction experienced by lawyers. The sense of anxiety is often experienced because the lawyer was diligently representing the client, was doing his or her best, yet something happened that resulted in a claim being filed.

Q. Does having a claim against me mean that I am a bad lawyer?

A. No. All lawyers make mistakes. Some mistakes are never caught, others do not cause any damage. Regardless of how intelligent, diligent and ethical you are, a mistake can be made or you can do something that prompts a legal malpractice claim. In fact, most legal malpractice claims are against excellent lawyers who have simply made an error, or who have a claim filed against them for some other reason.

Q. Is handling of the legal malpractice claim against me confidential?

A. Yes. Handling of the legal malpractice claim against you is confidential, and information about it will not be relayed by the Professional Liability Fund to anyone without your consent. When a claim for legal malpractice is filed against you, you should never discuss the content of the case with anyone except the PLF claims attorney or defense counsel. This makes it somewhat awkward for those around you, such as your friends and your peers, who may be aware that a claim exists. Although this may feel awkward to you and your peers, it assures that there will be no waiver of the attorney-client or work product privilege.
Although we ask that you do not discuss the facts or merits of the case with anyone other than the PLF or defense counsel, we recognize that having a legal malpractice claim filed against you is often very disturbing and unsettling. You may experience the following feelings and reactions:

- Unusual inhibition in handling your cases
- Losing sight of your case issues
- Feeling like you always make mistakes and never do anything right
- Extreme preoccupation with the mistake
- A sensation that you won’t get a fair evaluation of the case and that no one will listen to your side of the story
- Feeling defensive about your work
- Alienation from your peers and partners
- Afraid to take on new cases or stretch your expertise
- Afraid to make a move on your current cases or deal with your difficult clients
- Not wanting to send your bills to clients
- Hesitant to call back specific clients of yours, thinking that they may be unhappy or want to complain about something
- Avoiding opening your mail or answering your calls
- Reluctant to come into your office
- Reacting differently than you used to to new assignments - feeling pressured to accept new tasks that you "can't" do
- Unproductive - distracted, unorganized, difficulty focusing on your work
- Easily irritated and angry
- Constant fantasizing about getting away
- Experiencing extreme thinking, such as dropping your practice or running away

The Oregon Attorney Assistance Program is available to assist you. This service is free and strictly confidential. Information you provide to OAAP personnel is not shared with the PLF claims staff or your defense counsel. If you are experiencing any of the reactions listed above and you would like additional information or assistance, contact the Oregon Attorney Assistance Program – Meloney Crawford Chadwick 503-226-1057, ext.13; Mike Long 503-226-1057, ext. 11; Shari R. Gregory 503-226-1057, ext. 14; or Doug Querin 503-226-1057, ext. 15. You may also call toll free in Oregon 1-800-321-OAAP.

Q. Do the Professional Liability Fund and the Oregon Attorney Assistance Program provide any programs or workshops for lawyers who have legal malpractice claims?

A. Yes. We have many resources to help you. If you are interested in more information call Barbara S. Fishleder at 503-684-7425 or Mike Long at 503-226-1057, ext. 11.
ON BEING SUED
OR
HOW IT FEELS WHEN THE NIGHTMARE HAPPENS TO YOU

In Brief December 1993

My initial reaction to the lawsuit was utter amazement. I was shocked that my client would have the audacity to take such a drastic step. I felt wronged. I blamed the client, the ungrateful s.o.b. He didn’t even have the courage to call me to discuss the problem. Instead, he rushed off to another attorney and filed suit. The attorney didn’t even check-out the facts with me first. The client’s dissatisfaction was conveyed by the complaint. The local newspaper didn’t miss it either, they managed to print it along with the list of other “lawsuits filed.” I felt totally humiliated.

I just knew that I had given the client an excellent work product. I had witnessed serious mistakes by other lawyers, none of which had generated a claim. I couldn’t believe THE NIGHTMARE was actually happening to me. This was much worse than having a bill questioned, or dealing with an unhappy client directly.

Within a few days of receiving the bad news, my shock and amazement transformed into despair. I began to mistrust my judgment. I became paranoid. I was so afraid of making another mistake and getting sued again that my stress level rose out-of-sight whenever I gave legal advice.

I began to worry, particularly at night. I feared that there were other dissatisfied clients that I was not aware of. I found myself being tentative and inconclusive when dealing with clients. I often felt the need to have my legal conclusions validated by other lawyers in the firm in situations when I should have been able to act on my own. I forced myself to go through my client files for an entire day to determine whether I had made a mistake on any pending cases. I had periodic episodes of fear about the quality of my work. These anxiety attacks would only subside with my thorough re-analysis of the advice that I had given to the client.

I began to wonder how other lawyers, both inside and outside the firm, would perceive the case. I worried that they would assume that I had made a mistake, just because a claim was made. I was scared that they would now think less of me as a lawyer, assume that I couldn’t do a good job, and that their reactions would begin to affect my reputation, compensation and referral base. I feared that other lawyers whom I respected would find out about the case. If they knew about it, how would I convince them of my innocence? In the few instances when another lawyer was aware of the claim and mentioned it to me, I felt a compelling need to explain that I had not made an error. To avoid embarrassment, I never raised the issue with other lawyers. This lack of communication with my friends and colleagues precluded me from realizing that a single malpractice claim would not ruin my reputation, even if I was negligent. It also postponed my eventual discovery that many of those same lawyers also had been sued and had survived the experience.

I lived in a constant state of anxiety. I found myself writing memos to the file constantly – much beyond what is necessary to document the file. It took very little to get my stress
level up. I experienced a significant amount of anxiety when discussing the claim with defense counsel and an unbearable amount in connection with depositions. Minor anxiety attacks occurred whenever I was reminded of the claim. Copies of routine correspondence from my defense counsel managed to make my throat dry and my palms sweat.

As time passed I finally was able to admit that I had made a mistake, and that it wasn’t the end of the world, or my career. I had been fighting to protect my ego, which was actually standing in my way. I finally understood that I could make a mistake and still be a good lawyer. I realized that no uncompensated damage occurred; that we have malpractice insurance so that the client has a remedy. I realized that we all make mistakes. I realized that my friends and colleagues didn’t know how to approach the subject either. There we were – I needed to talk, but was afraid to do so. They were willing to listen, but were afraid to let me know.

I’m still working on forgiving myself and accepting full responsibility, but I know I’m headed in the right direction. I am, and always have been, a good attorney. There is no question in my mind that being sued for malpractice is the most gut-wrenching experience I’ve had to suffer through in my professional practice. I know now that the experience would have been much less of a nightmare, if I had sought counseling early on. A lot of emotions are stirred when you believe that your competence is being held up for the world to scrutinize. Seeking personal assistance would have helped me deal with my fears, and allowed me to be the productive and excellent lawyer that I really am. Instead, I remained frozen in the nightmare – a prisoner to my worst thoughts and beliefs about myself and my abilities.

I eventually did seek help through the OAAP. There I gained strength from the support of colleagues. I realized that I was not alone in my reactions, that many professionals react to malpractice claims by engaging in second-guessing and self-doubts. I found out that having self-doubts after a malpractice claim didn’t mean that I was a bad lawyer; they simply were a very common and human reaction to the situation. Once my head was clear and I was free of my self-inflicted torture, I came to understand the real reason the mistake had occurred – my legal analysis had been correct, but I had not successfully communicated with my client.

I offer this information to the readers of this newsletter because I regret that I didn’t understand what to expect, and that I didn’t know how to ease the pain. I know that reading this won’t change the initial shock that occurs when you first find out about a malpractice claim; but it will prepare you for some of the feelings you may experience. In that way, I hope it will be less of a Nightmare for you. I also hope that you won’t isolate yourself from others. Get counseling, call the OAAP. Talk to your friends, family and peers about your feelings. Believe me – it will help. We are all in this together – we all make mistakes.

Been There and Survived
V. DEALING WITH POTENTIAL OR ACTUAL MALPRACTICE CLAIMS

A. (§15.48) Potential Claim—Lawyer Recognizes Potential Problem, Client Does Not Know About Problem

Every practicing lawyer worries about committing an error in representing a client. Although competent in advising others, a lawyer often is prone to respond emotionally to his or her own problems, including malpractice. The emotional response may be guilt, anger, anxiety, or panic. Impulsive action may worsen the problem. When in doubt, the lawyer should contact the PLF and any applicable excess carrier. The following sequential steps are recommended if malpractice may have occurred and the client does not know it:

1. The lawyer should independently analyze, if possible, whether malpractice may have been committed.

2. If the lawyer either is unable to independently analyze the issues or, after independent and objective analysis, concludes that malpractice may be an issue, the lawyer should contact the PLF and any applicable excess carrier, report the problem, and seek instructions and advice. The lawyer’s failure to inform the carrier may deprive the carrier of an opportunity to give the lawyer good advice or to repair the problem. Furthermore, the lawyer’s failure to inform the carrier may violate the terms of the coverage plan or insurance policy.

3. After consultation with the carrier, the lawyer should advise the client of the existence and nature of the problem. Fundamentally, the following rules apply to any communication to the client of any potential or actual malpractice. The lawyer should:

   a. stick to factual statements as they relate to the problem;

   b. avoid making statements of opinion or judgments about his or her conduct and not yield to the compulsion to “confess”;
(c) encourage the client to seek independent legal advice about the problem;
(d) confirm all oral statements with a letter to the client;
(e) perform further analysis to determine the merit or propriety of continuing to represent the client because a potential or actual conflict may have arisen; this analysis should be done on a case-by-case basis, but in every case the lawyer needs to be sensitive and aware of this potential; and
(f) explore with the professional liability carrier the potential to cure or repair the error.

PRACTICE Tip: A lawyer who has made a mistake that potentially or actually adversely affects the client’s position in a pending matter must consider the potential conflict of interest and the client’s corresponding need for independent counsel. As an example, the lawyer represents a plaintiff in an injury suit and a defense is asserted that is attributable to the lawyer’s action or inaction (e.g., statute of limitations). The conflict issues addressed in subsections (a)(1) and (3) of Oregon RPC 1.7 come into play. If the lawyer can continue to represent the client (Oregon RPC 1.7(b)), the lawyer still must obtain the client’s informed consent as defined in Oregon RPC 1.0(g). See In re Brandt/Griffin, 331 Or 113, 134–135, 10 P3d 906 (2000), which provides guidance on the extent to which disclosure is required.

The lawyer should consider designating another lawyer in the firm as in-house claims counsel or general counsel to oversee the firm’s (and the involved lawyer’s) handling of the problem—including communicating with the PLF and other liability insurers. This strategy accomplishes the following:

1. It provides a more objective handler of the problem within the firm;
2. It reduces the involved lawyer’s sense of isolation while maintaining confidentiality of communications about the problem; and
3. It facilitates the lawyer’s and the firm’s communications with the PLF and excess insurers.

B. §15.49 Lawyer Is Asked to Produce File or Submit to Deposition
Occasionally, a lawyer is asked to produce materials from the files or to give testimony relating to matters that the lawyer previously handled for the client. This request most commonly occurs (1) in a will contest when the lawyer prepared the will in issue or (2) when the former client is now in litigation involving matters relevant to the lawyer’s file or previous representation. However, sometimes the former client is already contemplating a claim, and the new (inquiring) lawyer’s focus is the malpractice claim under investigation—a focus not necessarily communicated to the first lawyer.

A lawyer who receives such a request is well advised to contact the PLF before producing documents or giving interviews, affidavits, or oral testimony. The lawyer should exercise caution for two primary reasons:

(1) Confidences or secrets or other privileges may exist that must be protected or preserved pursuant to Oregon RPC 1.6, and a violation of those duties could lead to liability exposure for the lawyer; and

(2) The lawyer’s file materials or testimony may be relevant to a potential malpractice claim in the future, which may be contemplated by the party seeking documents or testimony.

The PLF has counseled lawyers receiving such requests and has often hired counsel to represent these lawyers in the document-production process or in giving testimony. A lawyer who does not seek counsel before responding may either waive or violate a privilege or unknowingly be set up for a claim arising out of the previous representation. Although the lawyer may be obligated to provide file materials or testimony, the lawyer has a right to and should first seek and obtain the appropriate advice to minimize the risks described above. Because the PLF coverage has no deductible and the attorney fees are usually minimal, there is no disadvantage to the lawyer’s contacting the PLF, assuming that the lawyer is covered by the PLF. When the PLF is not the professional liability carrier, the lawyer should still seek professional representation before responding to requests for documents, oral statements, or testimony.
C. (§15.50) Actual Claim—Accusation, Demand, or Lawsuit by Client or Representative of Client

A lawyer against whom an actual claim is made should follow the following steps:

(1) Immediately notify the PLF and any applicable carrier;

(2) Promptly respond to the carrier’s inquiries regarding facts, documents, or analysis;

(3) Do not communicate with the adverse party or the adverse party’s lawyer without first consulting with the professional liability carrier; and

(4) Accept the new role as client—let the malpractice carrier, the claims lawyer, and the defense lawyer handle the claim.

Oregon lawyers in private practice are strongly encouraged to review the PLF Claims Made Plan, which is published annually in the Oregon State Bar Membership Directory and available directly from the PLF online at <www.osbplf.org>.
Beating The Stressors of Family & Juvenile Law

Family law attorneys tend to be more “people oriented” and often feel at ease dealing with emotionally charged people and issues. Family law practice constantly tests the attorney’s ability to clearly define and limit a professional role and to establish and maintain boundaries in interpersonal relationships with clients. Rather than repeat previously provided information on the stressors practicing attorneys share generally, this article will focus on the stressors that are particular to a family and/or juvenile law practice. For purposes of this article, stress is “the rate of wear and tear within the body.” For simplicity sake, in this article, my references to family law are intended to include the practice of juvenile law as well.

Avoid the Peril of Getting Hooked

As attorneys, we bring to our practice our strengths, professional training and experience, our vulnerabilities and our unresolved personal issues. A family law attorney who has gone through a divorce may have the potential for greater empathy with clients and may also run a greater risk of his or her personal issues getting mixed-up with those of his or her client. An attorney who is predisposed to rescuing others or attempting to solve the problems of others will have a difficult time maintaining a professional boundary and limiting his or her role to being a client’s legal counsel. An attorney who gets emotionally hooked or enmeshed with clients runs a high risk of burnout and of compromising his or her professional role and responsibilities.

It is important for each attorney to recognize the type of clients and issues that “hook” him or her. A signal or red flag that you have been hooked is when you find yourself treating or responding to a particular client differently than your other clients. Examples include finding yourself responding emotionally to a client’s circumstances, becoming preoccupied with or taking a client’s case and circumstances home with you, or agreeing to continue to represent a client who will not be able to pay for your services. Such red flags require an attorney to take a step back and make sure that his or her own issues are not coming into play. This self awareness is critical in avoiding the high stress of client overdependence.

Uncertainty and lack of control are two primary ingredients of stress. To reduce stress, it is important to exercise control over those things you can control and develop acceptance of those things you have no control over. Once you have agreed to represent a client, you actually have no control over your client’s actions and decisions and the stress and grief they cause themselves, you and others. It is critical to evaluate each new client to determine whether their expectations are reasonable. A client whose expectations are unreasonable, who is unable to accept the legitimate claims of the other party or whose primary agenda is to inflict revenge, humiliations or punishment on the other party is going to also place unreasonable expectations, demands and stress on you as his or her attorney.

The initial interview is a good indicator of how stressful the case will be for you. Looking back at my own family law practice, I know that all of my cases which turned out to be “nightmares” had one thing in common - a feeling of doubt or concern early on in the representation. Sometimes I just pushed forward, accepted the case and overruled my concerns and intuition. Other times, I knew I did not want to take the case and I asked for a retainer fee I believed the client could not or would not pay. Unfortunately, too many of those times I guessed wrong, and I had trapped myself into representing the client. This could have easily been avoided if I had listened to my instincts, gathered some gumption, and turned the client away. Instead, the stress in my practice was greatly heightened because I left these important decisions to chance, or worse to someone who I did not want to be a client.

Keeping Your Role in Focus

Family law clients are typically seeking services in response to significant and frequently traumatic life events. They have multiple needs (legal, financial, emotional and parenting to name a few). Once a level of trust is established, they may recruit or solicit the attorney to assist them in responding to all of these needs. It is important to remember that clients are best served, and your professional role is kept clear, if you encourage your clients to do all they can to help themselves resolve their issues and conflicts. This includes taking advantage of community resources for nonlegal needs.
Lawyers are not serving themselves or their clients by taking control of their client’s lives, by making decisions for them, by endeavoring to be their emotional bodyguard, or by protecting them from the evil and wickedness of the opposing party and opposing counsel. This approach maximizes the client’s dependence on the lawyer and causes unnecessary attorney stress and burnout. It leaves the client’s problems and conflicts with the lawyer, instead of the client. It gives the lawyer responsibility for everything, instead of limiting the lawyer’s responsibility to guiding the client through legal issues.

Develop Support

There is a growing body of literature acknowledging that professional helpers who work with the victims of trauma are vicariously traumatized by their exposure to the victimization and struggle of their clients. This vicarious traumatization alters the professional helper’s way of understanding the world, their beliefs about themselves and others, and their beliefs about the core issues of trust, intimacy, safety, self-esteem, independence and personal power. Vicarious traumatization may be an inevitable result of working with trauma survivors.  

To minimize the impact of vicarious traumatization, the family law attorney must have a support system that provides a safe place for him or her to talk about the painful traumas of their clients and the impact it has on them emotionally. This support system might be other attorneys the lawyer practices with, or a significant other, friend, spiritual adviser or therapist. Attending professional conferences and workshops can also provide attorneys supportive professional contacts as well as new skills.

Stressed Clients Need Advice in Writing

Family and juvenile law clients frequently are not functioning well when they come to see you. Some clients are very affected by, and preoccupied by, the life events they are facing. Some clients may suffer additionally from chemical dependency. The client’s personal difficulties reduce the client’s ability to think clearly, to comprehend and recall what has been explained and advised, and to make rational decisions. The family law attorney must make a special effort to assess whether their clients are following the attorney’s explanations. Providing the client with advice in writing gives the client an additional opportunity to review and digest the advice. It gives both the lawyer and the client something to refer to in future discussions, and it gives the lawyer the ability to prove (if need be) that the information was imparted to the client.

Where To Go From Here

Failure to develop a personal plan to manage stress will eventually result in emotional burnout. Some of the major warning signals of burnout are:

- Emotional exhaustion - feeling drained, not having anything to give even before the day begins;
- Depersonalization - feeling disconnected from other people, feeling resentful and seeing them negatively;
- Reduced sense of personal accomplishment - feeling ineffective and perceiving that results achieved are not meaningful;
- Working longer hours but accomplishing fewer results;
- Seeing less of your family and friends;
- Feeling exhausted, irritable, anxious, and beset by physical ills.  

Many lawyers are familiar with the 10 ways to reduce stress and create balance in one’s life:

- Watch your diet
- Exercise
- Learn time management
- Learn relaxation and breathing skills
- Learn to play and have fun
- Use positive thinking and self-talk
- Develop a detached attitude
- Develop your spiritual self
- Develop a sense of humor
- Talk to someone about your stress

Taking care to implement even one of these suggestions, will go a long way toward helping improve your coping ability. Here are some ways you can apply the suggestions to your daily practice. Remember, implementing even one suggestion puts you on the road to stress reduction:

- Cut your workweek to “human” limits, ideally 45 total (not billable) hours;
- If you’re a sole practitioner, use project lawyers to assist you when you’re overloaded, share space with other lawyers, or join a firm in whatever capacity works for you;
- Eliminate areas of the law that drain your energy;
- Drop unprofitable or excessively difficult clients;
- Instead of litigation, consider alternative dispute resolution (mediation and arbitration) to resolve client problems;
- Never take work home;
- Block out specific times each week when you can work on files or other matters, uninterrupted by phone calls, staff and clients;
- Don’t postpone vacation time! Take advantage of regularly scheduled, planned absences from the office;
- Take a sabbatical or leave of absence for at least six to eight weeks to give your mind and body a break;
- Exercise regularly. Physical activity dissipates stress;
- Enroll in a stress management seminar to learn new skills you can use everyday;
- Consult health professionals who can provide personalized programs for stress relief (e.g., osteopathy/chiropractic therapy, therapeutic massage, biofeedback);
- Utilize lawyer assistance programs offered by your state bar association.

Conclusion

The stress of practicing Family and Juvenile Law can be greatly reduced by (1) monitoring your reactions to clients and in cases that trigger your own issues (2) resisting the temptation to do all things for all people (3) develop a network of support for yourself (4) make a special effort to document the file and provide your client with written information and (5) take a step toward better care of yourself.

The Oregon Attorney Assistance Program is available to help you accomplish your goal of stress reduction. If you want more information on this topic, please call the Oregon Attorney Assistance Program (OAAP) at 226-1590. The OAAP is a completely confidential assistance program sponsored by the Professional Liability Fund.

REFERENCES


Updated September 2008
Oregon Attorney Assistance Program

Providing Completely Confidential Assistance to Lawyers and Judges since 1982

What is the Oregon Attorney Assistance Program?
The Oregon Attorney Assistance Program (OAAP) is a confidential service funded by the Professional Liability Fund for all Oregon lawyers and judges. We provide assistance with and referral for problem alcohol, drug, and/or other substance use; stress management; time management; career transition; compulsive disorders (including problem gambling); relationships; depression; anxiety; and other issues that affect the ability of a lawyer or judge to function effectively. The OAAP is also available to Oregon law students.

OAAP attorney counselors are lawyers and professionally trained counselors. As a result, we are able to establish a unique rapport with members of the legal community.

Completely Confidential
All communications with the OAAP are completely confidential and will not affect your standing with the Professional Liability Fund or the Oregon State Bar. No information will be disclosed to any person, agency, or organization outside the OAAP without the consent of the lawyer or judge accessing the program. Contacts with us are kept strictly confidential pursuant to ORS 9.568, PLF Policies 6.150 - 6.300, OSB Bylaw Article 24, ORPC 8.3(c)(3), Oregon Code of Judicial Conduct JR 2-104(c) and Judicial Code of Conduct for United States Judges Canon 3B(5). The only exceptions are: 1) to avert a serious, imminent threat to your health or safety or that of another person and 2) to comply with legal obligations such as ORS 419B.010 and ORS 124.060 (child abuse and elder abuse).

Are there any costs?
All of our services are free, except for a nominal fee charged for some workshops and seminars. If additional professional help is needed, we can serve as a referral resource.

How do I receive assistance?
Call us. We are here to help.

OAAP Attorney Counselors
Shari R. Gregory, LCSW, JD
OAAP Assistant Director
sharig@oaap.org

Kyra M. Hazilla, JD, MSW
kyrah@oaap.org

Mike Long, JD, MSW, CEAP
mikel@oaap.org

Douglas S. Querin, JD, LPC, CADC I
douglasq@oaap.org

503-226-1057
1-800-321-OAAP (6227)

OAAP Executive Director
Barbara S. Fishleder
503-684-7425/barbaraf@oaap.org
Shari R. Gregory is a graduate of Wurzweiler School of Social Work (MSW 1987) and Rutgers School of Law (JD 1992) and received her certificate of Business Management from Portland State University (2003). Her counseling experience includes career counseling, mental health counseling, crisis intervention, group facilitation, transition counseling, and alcohol and drug counseling. She was in private practice specializing in criminal defense law for four years before joining the OAAP staff in 1999. She is the assistant director of the OAAP and a Licensed Clinical Social Worker (LCSW).

Kyra M. Hazilla is a 2006 graduate of the University of Michigan Law School (JD) and School of Social Work (MSW). She was a public defender practicing juvenile law for most of her legal career and also worked as a contract attorney in the areas of personal injury law and civil rights law before joining the OAAP staff in 2014. Her counseling experience includes crisis intervention; working with victims of sexual assault; drug, alcohol, and substance use counseling; mental health counseling; and helping domestic violence survivors and their children. Ms. Hazilla was raised by a family member in recovery.

Mike Long is a graduate of Hastings College of Law, San Francisco, California (JD 1983) and Portland State University (MSW 1991). He was in private legal practice in Portland between 1985 and 1990. Mr. Long worked in alcohol and drug residential treatment from 1990 to 1991 and as a therapist and crisis counselor from 1991 to 1993 before joining the OAAP staff in 1994. He is a Certified Employee Assistance Professional (CEAP) and a coauthor of Lawyers at Midlife: Laying the Groundwork for the Road Ahead (Decision Books, Seattle: 2008).

Douglas S. Querin is a graduate of the University of Oregon (JD 1971) and George Fox University (MA in Counseling 2006). He was in the private practice of law in Portland for over 25 years, working as a trial lawyer in state and federal courts throughout the Pacific Northwest. In recovery since 2002, Mr. Querin joined the OAAP staff in 2006. He is a Licensed Professional Counselor (LPC) and a Certified Alcohol and Drug Counselor (CADC I). Mr. Querin is the 2008 and 2013 recipient of the Oregon Counseling Association Distinguished Service Award.

THE OAAP OFFERS HELP FOR...

- Problem alcohol, drug, and/or substance use
- Recovery support
- Burnout and stress management
- Career transition and satisfaction
- Depression, anxiety, and other mental health issues
- Compulsive disorders including gambling, sex, and Internet addiction
- Procrastination
- Relationship issues
- Retirement planning
- Time management

To speak with an attorney counselor or for more information:

503-226-1057
1-800-321-0AAP (6227)
www.oaap.org