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PHOTOGRAPHY:**

*The Decisive
Moment*



What's All the Fuss?

Why Can't Divorcing Spouses Just Divide Community Assets Equally?

by Kathleen A. McCarthy, J.D.

"Justice?—You get justice in the next world, in this world, you have the law."

—William Gaddis,
A Frolic of His Own

Married couples typically take an all-for-one and one-for-all approach when acquiring assets. After all, they are in partnership and building a future for better or for worse. Although there are limited exceptions—for example, in the case of separate property or gift—Arizona considers all the labor, effort, and earnings during marriage to be community property. For the most part, community property must be divided equally. That's the law. But making the cut can be a messy process. The court can mix and match a smorgasbord of approaches, including sale of assets, continued cotenancy, or swapping assets, equalizing any difference with cash. This jagged path to equality leads to lots of angst and questions, some of which follow.

Does our home have to be sold?

The short answer is no. But if there is a contentious battle over its value, the court could allow a bidding war between the spouses or order the home to be sold. In the case of a buyout, the court will not discount the home's value, because no closing costs or commissions will be incurred. Just remember, deeding the property to your spouse will not relieve you of the underlying mortgage. Only the lender can do this, which usually requires refinancing by the owner spouse.

Can I receive half of the retirement accounts without paying a penalty?

Yes, as long as you roll over your share to another IRA. A taxpayer freebie available only to divorcing couples is that the nonemployee spouse may be able to take his or her share of a 401(k) in cash penalty-free, although

income taxes will be levied.

What happens if community assets change value after divorce papers are served?

Unless an increase is due to one spouse's postservice work efforts, or a decrease is solely the fault of one party, each person takes an equal share of the increase or decrease regardless of whose name the asset is in.

If the community paid disability insurance premiums, am I entitled to my spouse's disability benefits?

No. This is a harsh result, but no matter how much the community paid in premiums, postdivorce disability benefits go solely to the disabled party.

When is an equal division of financial accounts not equal?

This is not a trick question. Liquidity and taxes are big game-changers. Some people prize liquidity over funds tied up in a risky investment. Although the transfer of assets in a divorce does not in and of itself trigger tax consequences, when the asset is sold, taxes will matter. For example, a residence worth \$300,000 may not trigger any gain when it is sold, but the distributions from a \$300,000 retirement account may be substantially taxed. The assets theoretically have equal values at the time of divorce, but they certainly are not equal when cashed in.

Am I entitled to half of my spouse's predivorce accumulated sick/vacation benefits?

Probably. Arizona has not yet decided this question, but most other community property states treat these benefits as divisible in divorce.

What about future severance benefits and unvested stock options?

These are community property if they were earned during the marriage, regardless of whether or not they are vested.

Is my spouse entitled to proceeds from my personal injury suit?

Not if it represents compensation for your pain, suffering, or other personal damages. However, the community is entitled to the amount paid for medical bills, out-of-pocket costs, or lost earnings during the marriage.

Does a term life insurance policy with no cash value have value?

It may sound counterintuitive, but the answer is yes. A term policy can offer a surviving ex-spouse a safety net against community creditors. If the insured spouse has significant health problems, the policy may have “viatical value.” It may sound perverse, but an investor may buy the policy, effectively betting on the insured person’s premature death.

Should I just let my spouse have a nonsalable asset, such as underwater real estate?

“No market” does not equate to “no value.” Depending on the cost to maintain the property, it may be worth co-owning it. Markets tend to correct over time. You may regret it if you let your spouse have it for nothing, but it subsequently sells for a lot.

Is the ring my spouse gave me on Mother’s Day community property?

This is an emotionally charged issue. Unfortunately, the answer is uncertain, but courts generally treat gifts of jewelry made by one person for a special occasion (as opposed to investment jewelry) as a gift and not community property.

Do frequent flyer miles have value?

Absolutely. They are divisible—it just takes some work. While you are at it, make sure you get half the points earned via your jointly held credit-card reward programs, too. A vacation can be healing after working through a contentious divorce.

Equal division is the law. But it doesn’t mandate a chiseled cut. The ragged edge of a chainsaw will do as long as justice is achieved. It is hoped we get both the law and justice in this world!

(This article is for informational purposes only and is not a substitute for legal advice. Please consult with an attorney and financial/tax advisors for advice regarding your specific property issues.)

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