LJN LAW JOURNAL NEWSLETTERS

The Matrimonial Strategist®

An ALM Publication

Volume 29, Number 9 • September 2011

New Laws in Texas Address Financial Matters

By Jonathan J. Bates

On June 17, Gov. Rick Perry, R-TX, signed into law two bills of keen interest to family lawyers in that state. They address spousal maintenance and fraud on the community estate.

Spousal Maintenance

In some limited situations, Texas law permits a court to order post-divorce payments, known as spousal maintenance, from one spouse to the other. H.B. 901 significantly has modified Chapter 8 of the Texas Family Code, which is the section that authorizes spousal maintenance.

Many of the changes are essentially refinements of terminology, such as further emphasis that spousal maintenance is only authorized for individuals who lack sufficient property to provide their own minimum reasonable needs. The new changes also clarify language providing that maintenance is authorized only in marriages of at least a 10-year duration, in instances of violence within the family unit, and/or when the spouse is incapable of providing for the spouse's minimum reasonable needs because of an incapacitating physical or mental disability.

Further, the new Family Code provisions clarify the rebuttable presumption that spousal maintenance is not warranted unless the spouse seeking support

continued on page 6

How to Deal with the Distribution of Intellectual Property Assets in Divorce

By Judith L. Poller and Elizabeth Warner

Relationships are challenging. Add to the mix the dynamic of a spouse who is creative (the "Creative Spouse"), and must rely in large part on his or her spouse to provide both financial and personal support (the "Supporting Spouse") for a dream to be realized. The passage of time with no success may lead to heightened tensions as the Supporting Spouse demands that the Creative Spouse wake up and share the burdens of financial responsibility. This financial tension may ultimately lead to a divorce.

While it may be relatively clear-cut to determine the value of real property, financial accounts and even a professional practice, when a Supporting Spouse and a Creative Spouse divorce, the question may arise as to how to distribute the value of the intellectual property or "celebrity status" that the Creative Spouse created during the marriage (the "Creative Asset"). Some Creative Assets may already have a market-defined value at the time of commencement, while some may only have an expectancy of value. This article considers what rights, if any, a Supporting Spouse may have in the value of a Creative Asset.

Distributing the Value of a Creative Asset When There Is an Income Stream

First, consider how to distribute the value of a Creative Asset that is already generating income and has a market-defined value at the time of divorce. In this scenario, the Creative Spouse is generally receiving income pursuant to an agreement with a third party (the "Income Generating Agreement"). An Income Generating Agreement can be structured in many different ways — for example as a licensing agreement or a joint venture agreement — but essentially, the Creative Spouse has sold, licensed or assigned all or part of his or her interest in the Creative Asset to a third party. These agreements present a reasonably clear solution because the asset has a readily identifiable value that the couple can divide.

continued on page 2

In This Issue

IP Assets in Divorce .. 1
Financial Matters In Texas 1
File Jointly? Or Not ... 3
Promulgating a Standing Order 5
Judge Draws a Reprimand 7

IP Assets

continued from page 1

Each spouse can receive a share of the future income stream from the Income Generating Agreement.

There is an abundance of case law dividing future income streams from such agreements, for many different types of intellectual property. *See, e.g., In re Marriage of Coiffi*, No. H028588 & H029712, 2007 Cal. App. Unpub. LEXIS 4294 (Cal. Ct. App. May 29, 2007) (dividing future royalty streams in a patent to digital communication computer technology); *Maloy v. Maloy*, No. M2006-02463-COA-R3-CV, 2008 Tenn. App. LEXIS 56 (Tenn. Ct. App. Jan. 31, 2008) (affirming the division of future royalties in musical works). Companies distributing royalties may be able to divide the royalties and send the Supporting Spouse his or her share directly. If the income from a Creative Asset must first flow to the Creative Spouse, any distribution of income to the Supporting Spouse should adjust for income taxes the Creative Spouse will incur.

Unforseen Consequences

Even when the parties agree to this arrangement, however, attorneys should take heed of unforeseen consequences. While courts typically only recognize a Supporting Spouse's right to share in the economic benefits of the Creative Asset, as opposed to a right to have managerial control of the Creative Asset (*Rodrigue v. Rodrigue*, 218 F.3d 432 (5th Cir. 2000)), this right to share in the economic benefits can extend far beyond the Income Generating Agreement. In *In re Marriage of Worth*, 195 Cal. App. 3d 768, 241 Cal. Rptr. 135 (Cal. Ct. App. 1987), where the parties had entered into a settlement agreement entitling the Supporting Spouse to one-half of the future income stream from a work, the court held that by virtue of the Supporting Spouse's one-half entitlement, she was also entitled to one-half of an infringement damages award. In *Miner v. Miner*, No. 13-01-659-CV, 2002 Tex. App. LEXIS 5841 (Tex. App. Aug. 8, 2002), the court ruled that a Supporting Spouse's percentage interest in an income stream resulted in the same percentage interest in the income streams from derivative works. When drafting a settlement agreement, be sure to be as specific as possible regarding the Supporting Spouse's entitlement to future income in order to avoid future litigation.

Dividing a Creative Asset When a Third Party has Invested in the Creative Asset, But There is No Income

Next, consider how to distribute the value of a Creative Asset when a third party has invested in the Asset but it is not yet generating income. In recording contracts or book deals, for example, the Creative Spouse will often contract with a third-party before the Creative Asset is fully developed. In these types of contracts, the third party advances the money to develop the Creative Asset, advances that are set off against future royalties that may (or may not) be realized. In return, the third party buys the option to exploit (or reject) the Creative Asset once it is complete. Courts have tended to go in different directions in addressing this issue. In *Schroeder v. Schroeder*, No. FSTFA044001474, 2006 Conn. Super. LEXIS 2780 (Conn. Super. Ct. Sept. 11, 2006), the Creative Spouse had entered into a book deal concerning a book that had been researched, but not yet written at the

continued on page 4

Judith L. Poller, a member of this newsletter's Board of Editors, is a partner and Co-Chair of the Family Law Group at Pryor Cashman LLP. She was recently named among the Top 50 Female Lawyers in New York City by *Super Lawyers Magazine* - Metro Edition. **Elizabeth Warner** is an associate in the firm's matrimonial group.

The Matrimonial Strategist®

CHAIRMAN ..... Willard H. DaSilva, DaSilva Hilowitz & McEvily LLP, Garden City, NY
EDITOR-IN-CHIEF ..... Stephanie McEvily
EDITORIAL DIRECTOR ..... Wendy Kaplan Stavinoha
MARKETING DIRECTOR ..... Jeannine Kennedy
GRAPHIC DESIGNER ..... Louis F. Bartella

BOARD OF EDITORS

LAURENCE J. CUTLER ..... Fox Rothschild LLP, Roseland, NJ
MARY CUSHING DOHERTY ..... High Swartz LLP, Norristown, PA
PAUL L. FEINSTEIN ..... Paul L. Feinstein Ltd., Chicago
LYNNE GOLD-BIKIN ..... Weber Gallagher Simpson Stapleton Fires & Newby LLP, Norristown, PA
DAVID A. MARTINDALE Ph.D. ..... Forensic Psychological Consulting, St. Petersburg, FL
CHARLES J. McEVILY ..... DaSilva Hilowitz & McEvily LLP, Garden City, NY
KAREN MEISLIK ..... Meislik & Meislik, Montclair, NJ
MARK MOMJIAN ..... Momjian Anderer, LLC, Philadelphia
JEREMY D. MORLEY ..... (Private Practice), New York
JUDITH L. POLLER ..... Pryor Cashman LLP, New York
LLEWELYN G. PRITCHARD ..... Helsell Fetterman LLP, Seattle, WA
CURTIS J. ROMANOWSKI ..... (Private Practice), Metuchen, NJ
ROBERT E. SCHLEGEL ..... Houlihan Valuation Advisors, Indianapolis, IN
ERIC L. SCHULMAN ..... Schiller DuCanto and Fleck LLP, Lake Forest, IL
MARTIN M. SHENKMAN ..... (Private Practice), New York
LYNNE STROBER ..... Mandelbaum, Salsburg, P.C., West Orange, NJ
TIMOTHY M. TIPPINS ..... (Private Practice), Latham, NY
THOMAS R. WHITE 3rd. ..... University of Virginia School of Law, Charlottesville, VA
WILLIAM R. WRIGHT ..... Wright Law Firm, P.A., Jackson, MS

The Matrimonial Strategist® (ISSN 0736-4881) is published by Law Journal Newsletters, a division of ALM.
Telephone: (877) 256-2472
Editorial e-mail: wampolsk@alm.com
Circulation e-mail: customercare@alm.com
Reprints: www.almreprints.com

The Matrimonial Strategist 023146
Periodicals Postage Paid at Philadelphia, PA
POSTMASTER: Send address changes to:
ALM
120 Broadway, New York, NY 10271

Published Monthly by:
Law Journal Newsletters
1617 JFK Boulevard, Suite 1750, Philadelphia, PA 19103
www.ljnonline.com

ALM
An Integrated Media Company

Joint Filing

continued from page 3

Fraudulent Activity

While an election that meets either of the above qualifications will result in at least partial indemnification for an "injured and innocent spouse," fraudulent activity or actual knowledge of erroneous filings on the part of the spouse seeking relief will negate any opportunity that he or she had to claim status as an "injured and innocent spouse."

The Service has maintained that spouses electing for relief must make an election with clean hands or they, too, will be subject to liability, fees, interest, penalties and perhaps sanctions. A spouse filing such tax returns cannot have knowledge or awareness of under reporting and then claim innocence once the Service assesses a deficiency. In other words, a husband or wife may not enjoy the benefits of all of the income and suddenly try to claim "innocent and injured spouse." It is only where the one with the money is putting it in a separate pocket and it is not being spent during the marriage that "innocent and injured spouse" can even arise.

Conclusion

The issue of a joint filing is a complicated one — and one that is usually not within the expertise of a divorce lawyer. Tax advice should be sought from an accountant who has the expertise to know the Tax Code and all its regulations and give the appropriate advice on the filing. Often, the prudent attorney will suggest that the parties sign a tax indemnification agreement, supposedly to alleviate this exposure to the spouse whose income is not in question. However, an indemnification letter is effective only with regard to acts between husband and wife. Consequently, where the husband agrees to indemnify the wife, in the event the IRS reviews the return and assesses penalties, the wife is not protected from liability but must assert her claims against the husband. From the government perspective, the wife will still be responsible for potential taxes, interest, penalties and legal fees. She will then have to sue the husband to reimburse her for any taxes, interest, penalties and legal fees that she has been required to pay. As this article points out, tax issues are beyond the expertise of most matrimonial attorneys. The accountants and their advice really become essential in these cases.

—❖—

IP Assets

continued from page 2

time of the commencement of the divorce action. The court considered the book deal and stated that "[t]he book contract and payments thereunder are assets," but it ultimately did not give the Supporting Spouse an interest in it, given the couple's considerable wealth. *But see Michel v. Michel*, 484 So.2d 829 (La. Ct. App. 1986) (awarding Supporting Spouse a share of the profits from the Creative Spouse's book deal, even though the book in question was only in outline form at the time of commencement).

When faced with this kind of scenario, a good framework for determining how much a Supporting Spouse should receive is to use the formula some courts use in a divorce for the division of stock options. *See, e.g., DeJesus v. DeJesus*, 90 N.Y.2d 643, 687 N.E.2d 1319, 665 N.Y.S.2d 36 (1997). As with unexercised stock options, here there is an agreement for potential future income that was entered during the marriage, but will not generate income until post-judgment, income that is contingent on the Creative Spouse's post-commencement efforts. This stock option formula divides the amount of time from the contracting date to the date of commencement by the total time from the contract date to the date of the receipt of benefits under the contract. Applying this formula would give a Supporting Spouse a percentage of future income steams in the Creative Asset equivalent to the percentage of time that the contract existed during the marriage. To arrive at the "total time" denominator in the above formula, attorneys should look to the projected times estimated in the third-party agreement for the Creative Asset to be complete. Also, the Creative Spouse's attorney should always ensure that the Supporting Spouse's interest does not trigger before the third party has fully recouped its advances.

Dividing the Creative Asset When There Is No Market-Defined Value

Even where no third party has demonstrated an interest in the Creative Asset and any future income or value from the Creative Asset is contingent on myriad factors, including luck, the Supporting Spouse may still be entitled to a share of the Creative Asset.

There is a body of case law that suggests that in this scenario, the correct result is to allot the Supporting Spouse a percentage of any future benefit that may be realized, if, as and when the Creative Spouse receives such benefit. In *Gulbrandsen v. Gulbrandsen*, 22 So.3d 640 (Fla. Dist. Ct. App. 2009), where the Creative Spouse had co-developed a device with a pending patent application, instead of attempting to obtain a share of the device's future value based on estimates or based on the time and expense put into its development, the Supporting Spouse argued for an in-kind share. The court awarded the Supporting Spouse 12.5% of any future benefits from the patent, if any were ever realized. Other courts have made similar percentage distributions of intellectual property assets that have yet to be exploited. *See, e.g., In re Marriage of Monslow*, 259 Kan. 412, 912 P.2d 735 (Kan. 1996).

There is, however, a counterveiling body of case law that suggests that where there is no readily ascertainable value to a Creative Asset, it is too speculative to divide. In *VanWormer v. VanWormer*, No. 186493,

continued on page 8

IP Assets

continued from page 4

2005 Va. Cir. LEXIS 15 (Va. Cir. Ct. Feb. 25, 2005), the court refused to award the Supporting Spouse any portion of the Creative Spouse's patent where no royalties from the patent had been received. In *Zander v. Zander*, FA 9700745875, 1999 WL 711503 (Conn. Super. Ct. Aug. 30, 1999), the court refused to award the Supporting Spouse an interest in the Creative Spouse's unsigned song recordings where they had no present market value.

Perhaps the best reasoning to apply in this scenario should parallel intellectual property law. Under federal intellectual property law, any work can be registered for protection, regardless of whether it has an established monetary value. In fact, under patent law, even if the work is not registered, priority is given to the person who conceived of an invention first and continued to work on it with reasonable diligence. 35 U.S.C. § 102. However, an unfinished work cannot receive intellectual property protection. Thus, matrimonial law should recognize the divisibility of the Creative Asset, even if it has not "sold," based on its stage of development. Where the Creative Asset is developed enough to receive recognition under federal intellectual property law, it is an asset worth splitting in the divorce. However, if the Creative Asset must undergo many structural changes before it can receive protection, it is too tangential and speculative for valuation in divorce. In other words, if no third-party has expressed interest in the song and the Creative Spouse is still working on the lyrics, the song should not be divided.

Dividing the Value of the Creative Spouse's Career

Even if there is no Creative Asset that federal intellectual property law would protect, the Supporting Spouse still may be entitled to some credit.

For example, New York and New Jersey both recognize "celebrity status" as enhanced earning capacity, which is a divisible marital asset in divorce. *Elkus v. Elkus*, 169 A.D.2d 134, 572 N.Y.S.2d 901 (1st Dep't 1991); *Piscopo v. Piscopo*, 231 N.J. Super. 576, 555 A.2d 1190 (N.J. Super. Ct. Ch. Div. 1988), aff'd 232 N.J. Super 559 (N.J. Super. Ct. App. Div. 1989). In former New York Mayor Rudy Guiliani's divorce action, the court held that though the Mayor's then-unsigned book deal, worth $2.7 million, was negotiated post-commencement and could not be considered a marital asset for equitable distribution, the court could consider the unsigned book deal in determining the Mayor's celebrity status as it indicated his future enhanced earning capacity, which was a divisible marital asset. *Anonymous v. Anonymous*, 01/10/2002 N.Y.L.J. 21, col. 2 (Sup. Ct. N.Y. Co. Jan. 10, 2002). That said, most states do not recognize celebrity status as a marital asset. *See, e.g., In re Marriage of McTiernan*, 133 Cal. App. 4th 1090, 35 Cal. Rptr. 3d 287 (Cal. Ct. App. 2005). Even in New York and New Jersey, the Supporting Spouse has many hurdles to overcome in order to receive credit for the Creative Spouse's enhanced earning capacity. In *Sterling v. Sterling*, No. 310833/99, 2001 WL 968262 (Sup. Ct. N.Y. Co. July 31, 2001), aff'd 303 A.D.2d 290, 757 N.Y.S.2d 530 (1st Dep't 2003) the court indicated that it would only consider a Creative Spouse's celebrity status as a divisible marital asset if the Creative Spouse was able to "consistently obtain lucrative work." It refused to characterize the Creative Spouse's fame as a marital asset where she was merely a soap opera actress, or "average entertainer."

Under federal intellectual property law, any work can be registered for protection, regardless of whether it has an established monetary value.

Alternatively, a Supporting Spouse may have a claim to share in the Creative Spouse's future publicity rights (*i.e.*, the Creative Spouse's right to commercially exploit his or her identity). *See* David Westfall and David Landau, "Publicity Rights as Property Rights," 23 *Cardozo Arts & Ent. L.J.* 71 (2005). This, for example, would give a Supporting Spouse an interest in the Creative Spouse's future endorsement deals. However, this position is largely untested in the matrimonial arena.

A Supporting Spouse's attorney should be careful when negotiating for a share of a Creative Spouse's enhanced earning capacity or publicity rights. Claiming these interests is difficult and expensive to prove in court.

Conclusion

While dividing the interest in intellectual property assets can be complicated, there are creative ways to provide some structure to make sense of the chaos. Unfortunately, the downside is that there may not be the finality in divorce, which is necessary for couples to move on with their lives. However, fairness may dictate that the financial benefits from a Creative Asset flow to both the Creative Spouse and the Supporting Spouse post-judgment.

—❖—