BEAN KINNEY & KORMAN PC

BUSINESS LAW NEWSLETTER

MARRIAGE, DIVORCE, AND YOUR BUSINESS

By James W. Korman, Esq.

A divorce is an occasion of great personal trauma. Virginia business owners should be aware that a change in marital status could also have a major impact on business assets.

Virginia is not a community property state; it is an equitable distribution ("e.d.") state. That means that any asset acquired during marriage, unless it was inherited or received as a gift, (from someone other than a spouse) is presumed to be martial property. This is true whether the asset is held in the name of one spouse, or is in joint names. In either event, the asset is presumed to be marital if it was acquired at any time between the date of the marriage and the date the husband and wife finally separate. All marital property is subject to equitable distribution by the court when a marriage breaks up.

Let's consider an example. Suppose a couple married in 1980. Thereafter, one spouse started a new business, incorporated that business, and retained 50% of the shares of stock while a business partner owned the other 50%. Even though the fifty percent of the shares held by the spouse are in his or her name alone, the shares are marital property because they were acquired during the marriage.

While the 50% of the stock held by the spouse is a marital asset, it does not necessarily follow that that spouse will lose the shares in an equitable distribution. In Virginia, the court first determines which property is separate and which is marital. It also decides, based on the evidence, how much each marital asset is worth. Finally, the judge determines what share of the marital assets each party will receive. But the judge can literally divide only marital assets that are in joint names. That division can be in kind (the wife gets some of the marital widgets, and the husband gets some), or by a sale of the asset and a division of the proceeds of sale. It is not unusual, for example, for the court to order that the former marital residence be sold, and after expenses of same, the net proceeds to be split between the husband and wife.

Since Virginia is not a community property state, marital assets are not necessarily divided 50/50. The judge in the hypothetical may order 45% of the business owner's shares to be allocated to the business owner's spouse. If so, the business owner has a choice: give the spouse 45% of the shares of stock, or give that spouse cash in an amount equal to that 45%, based upon the court's determination of the value of those shares at the equitable distribution hearing.

(CONTINUED ON PAGE 2)

THE INS AND OUTS OF CONFESSION OF JUDGMENT PROVISIONS

By Jennifer Brust, Esq.

Litigation can be costly and unpredictable for a small business owner. Is there a way to keep costs down and still protect your interests? Consider inserting a Confession of Judgment provision in your standard contract. Most bankers and transactional types are aware of the value of Confession of Judgment ("COJ") provisions, but many business people do not realize how helpful and cost-effective they can be.

A COJ provision can give you a giant step forward on the sometimes lengthy and expensive path to obtaining a judgment. Under Virginia and Maryland law, a COJ provision gives you the right to appoint an agent of your own choosing for the other party to the contract. If that other party fails to comply with the terms of the contract, the agent - known as the "attorney-in-fact" - is authorized to ask the court to enter an immediate judgment against the breaching party.

The procedures for confessing judgment differ significantly in Virginia and Maryland. In Virginia, the process is non-judicial, meaning that no judge is involved. The attorney-in-fact appears in the Clerk's Office of the appropriate Circuit Court with the proper documents and filing fee. Once certain procedural formalities are completed, judgment is entered by the Clerk. Thereafter, the breaching party is served with notice of the entry of the judgment.

(CONTINUED ON PAGE 3)

MEET OUR NEWEST ATTORNEYS . . .

Bean Kinney & Korman is pleased to announce that Frank Lyman and Tracy Meyer have joined the firm.

FRANCIS FRANK LYMAN

Frank Lyman is a graduate of Manhattan College (B.S.), the State University of New York College at Plattsburgh (M.A, cum laude), and the George Washington University Law School (J.D., with honors). He is admitted to law practice in Virginia, the District of Columbia, and New York. Much of his practice is devoted to structuring, negotiating, and documenting commercial transactions. He also counsels and represents clients in the on-going operation of their businesses, including contractual relationships with all their stakeholders; local, state and Federal government taxation and regulation; and the purchase, sale, lease, and use of real estate and equipment. A significant portion of Mr. Lyman's expertise and experience has been in the areas of energy finance, production, distribution, and regulation, including electricity industry restructuring. He has practiced law in Washington, D.C., Arlington, Virginia, and upstate New York. He also served for several years as General Manager and General Counsel of Cogen Energy Technology, an independent producer of electricity and steam in New York State.

TRACY A. MEYER

Tracy Meyer graduated from the University of Northern Colorado, Honors Program, in 1992 (B.A., with departmental honors in Political Science, magna cum laude). She received her law degree from the Washington College of Law, American University (J.D.), in 1995. She concentrates her practice in civil litigation with a focus on domestic relations matters. She is admitted to practice in Virginia, the District of Columbia and the following federal courts: United States District Court for the Eastern District of Virginia and the United States Court of Appeals for the Fourth Circuit.

MARRIAGE, DIVORCE, AND YOUR BUSINESS

(CONTINUED FROM PAGE 1)

This process allows the business owner to structure an offer to preserve the business: equity in the marital home or a cash payment may be transferred in lieu of the actual shares. An offer of this sort must be accepted by the spouse, or, failing that, approved by the court; a requirement designed is to avoid the situation where one spouse offers the other all of his "dog" stocks to satisfy an e.d. award.

What factors determine the percentage of each marital asset the court will give to the husband and to the wife? The Virginia Code lists ten factors the court must consider. They are:

1. How much did each spouse contribute to the family? Both monetary and non-monetary contributions are considered
2. How much did each spouse contribute, in both monetary and non-monetary terms, to acquiring and maintaining the asset?
3. How long were the parties married?
4. The age and physical condition of the parties.
5. The cause of the marital break up.
6. How and when specific items of marital property were acquired.
7. The debts, how they arose, and the property that secures the debts.
8. Whether or not the assets are liquid.
9. The tax consequences to each spouse.
10. And the catchall: such other factors as are necessary or appropriate for the court to make its decision.

There are no percentages or weights assigned to each of these criteria. The statute is not intended to be a mathematical formula. Instead, it prescribes guidelines within which the trial judge exercises his or her discretion.

In the case of a business that is not publicly traded on a stock exchange, there will always be valuation issues. These are typically resolved through the testimony of experts selected by the parties and their counsel to evaluate the business. Since there are various accepted methods of performing such evaluations, and because facts and figures can be subject to differing interpretations, careful selection and preparation of an expert is critical. Occasionally, a spouse attempts to hide or improperly transfer assets in order to avoid the effect of the statute. Competent counsel can discover that kind of chicanery. If judge thinks one party is playing games, the consequences can be dire.

Parties to a divorce should also be aware that a settlement or court award might have significant tax consequences, particularly when retirement accounts are divided. The marital property rule also applies to 401k and IRA accounts. Any part of a retirement plan, IRA, or stock option plan obtained prior to marriage can be considered separate property. However, to the extent that the account accrued during the marriage, it is subject to equitable distribution. Tax penalties arising from the division of retirement accounts can be avoided by having the lawyers prepare a Qualified Domestic Relations Order ("QDRO"). The QDRO has the effect of transferring the interest in the plan or account to the benefit of the other spouse without triggering the penalties that would otherwise accrue.

In most cases, vigorous settlement efforts are recommended. An agreement between the parties is the best way to retain some control over the result. If counsel cannot reach an acceptable resolution, mediation may provide the answer. The divorce process is always stressful, but with proper planning, a party to a divorce can minimize the disruption and economic impact on his or her business. ◈

ARBITRATION AND CONTRACT INTERPRETATION

By James V. Irving, Esq.

In previous editions of this newsletter we have commented on the predilection of most courts to order arbitration in any circumstance in which it can be said that the parties have agreed to that alternative form of dispute resolution. In a recent case, the Supreme Court of Virginia has sanctioned that trend by deeming arbitration required in a case where the clause at issue was drafted in arguably permissive terms.

TM Delmarva Power, LLC v. NCP of Virginia, LLC involved a dispute between two entities that had formed a limited liability company to construct, finance, own, and operate a power plant on the Eastern Shore of Virginia. Their joint venture agreement included a provision entitled "Dispute Resolution" that contained the following language: "in the case of material dispute between the parties, any party *may* seek to have the dispute resolved by conciliators" (emphasis added). A provision in the following sub-section stated that if the dispute could not be resolved by conciliators, then "either party *may* commence arbitration" (emphasis added).

After substantial completion of the project, a dispute arose regarding capitalization of certain expenses and the authority of TM Delmarva to hire accountants and auditors for the joint venture's LLC. NCP initiated conciliation procedures in accordance with the agreement. When those efforts failed, it filed suit in the Accomack County Circuit Court. TM Delmarva responded with a motion to compel arbitration, and the dispute boiled down to a semantic analysis of the "may….may" construction in the two-pronged dispute resolution clause. The Circuit Court accepted NCP's reasoning, ruling that arbitration was not required and that NCP was entitled to proceed with it legal remedies. That ruling was immediately appealed by TM.

As it had below, NCP argued the traditional rule of interpretation that holds that the use of the word "may" makes a provision permissive rather than mandatory. By a 4 to 3 majority, the Supreme Court disagreed, accepting TM Delmarva's closer parsing of the dispute resolution clause. Justice Donald W. Lemon's opinion was handed down on January 11, 2002.

Justice Lemon agreed that either party had the discretion to choose arbitration if conciliation was not successful, but concluded that, while arbitration was optional, once conciliation broke down and the arbitration option was exercised by either party, the non-exercising party's participation in the process was compelled.

Justice Lemon held that two other, familiar principles of contract interpretation superceded the traditional understanding of the word "may." He held that the "plain meaning" of the dispute resolution provision, taken as a whole, accorded with TM's interpretation; and gave effect to the time-honored principle that contract interpretation must attempt to give meaning to all words and phrases in the contract. In Lemon's view, regarding the arbitration clause as permissive renders it, in essence, meaningless, since arbitration is always an option if both parties agree, irrespective of the existence of an arbitration clause.

Lemon concluded that the Court's holding was consistent with other, similar cases from federal courts as well as from the state courts of Maine, Kentucky, and California, and accorded with the Commonwealth's public policy in factor of arbitration. Three justices filed a closely reasoned dissent that included a telling point related to the public policy in favor of arbitration: Justice Lacy noted that it is Virginia's policy to construe arbitration agreements broadly *after* an agreement to arbitrate has been found to exist; not to stretch the law to find them where they might not have been intended.

TM Delmarva not only reinforces the judicial commitment to upholding arbitration agreements, it also reminds us that contract issues are not infrequently resolved based on a parsing of language not unfamiliar to high school English students. Justice Lemon relied on the maxim that all words and phrases in a contract must be given effect whenever possible; we are reminded to choose each word and phrase in our contracts with commensurate care. ◈

THE INS AND OUTS OF CONFESSION OF JUDGMENT PROVISIONS *(CONTINUED FROM PAGE 2)*

The breaching party has twenty-one days from the date of service in which to file a Motion to Set Aside the Confession of Judgment. If no Motion to Set Aside is filed, the judgment becomes final, just as if a Judge had entered the Order from the bench. There is no requirement that the attorney-in-fact be a licensed attorney. However, confessing judgment is a legal proceeding and it may be worth a few dollars to make sure it is handled properly.

Under Maryland law, confessing judgment is a slightly more elaborate process. The Confessor must actually file a lawsuit asking the Court to enter a Confession of Judgment Order against the defaulting party. Assuming the documents are in order (and the filing fee paid), the Court will enter the Order. The Defendant has thirty days from the date of service in which to file a Motion to Vacate the Confession of Judgment. Again, if no Motion is filed, the judgment becomes final.

What happens if a Motion to Vacate is filed? The down side of confessing judgment is that Courts are generally willing to set the judgment aside if the breaching party contests it. However, the savings in terms of filing costs and attorney's fees when compared to the cost of a traditional lawsuit makes the tactic worth pursuing. Even if it is set aside, the case is set on the trial docket, just as if a regular lawsuit had been filed.

Unlike Maryland and Virginia, the District of Columbia does not have specific statutes authorizing confessions of judgment. Although cases exist in which confession of judgment provisions were upheld, the practice is generally disfavored by the District of Columbia courts. ◈

BEAN KINNEY & KORMAN PC
ATTORNEYS

2000 North 14th Street
Suite 100
Arlington, Virginia 22201

PHONE: (703) 525-4000

FAX: (703) 525-2207

We're on the Web!
See us at: **www.beankinney.com**

About Our Organization . . .

For over four decades, Bean, Kinney & Korman has been a leading Northern Virginia law firm that has continuously grown and diversified to meet the needs of its expanding community of clients and their increasingly complex legal needs. While we have grown in size and greatly expanded the depth and breadth of our capabilities, we have remained committed to those fundamental elements of value that are integral to our practice philosophy: experience, versatility, dedication to service, flexibility and efficiency.

Our responsive and exceptional quality service, coupled with our sensitivity to client needs, has established a professional reputation in which we take great pride. We are dedicated to achieving exceptional results for our clients in every matter we are entrusted to handle, mindful of each client's resources and unique circumstances. Delivering greater value to our clients day in and day out is how we will continue our reputation as one of the most highly regarded law firms in the Washington metropolitan region.

BEAN KINNEY & KORMAN PC
ATTORNEYS
2000 NORTH 14TH STREET, SUITE 100
ARLINGTON, VIRGINIA 22201