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FAMILY LAW

Smoking Out Hidden Assets

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All family law practitioners should become familiar with the case of *Ziegelheim v. Apollo*, 128 N.J. 250 (1992) and the various obligations it creates for attorneys, particularly as to efforts to identify assets that a spouse may have attempted to spirit away.

The Court ruled that a lawyer's duty to his or her client includes a "careful investigation of the facts of the matter, the formulation of a legal strategy, the filing of appropriate papers and the maintenance of communication with the client." Id. at 261. See *Passanante v. Yoymark*, 138 N.J. Super. 233, 238-239 (1975). With respect to "concealed assets," the Court stated:

> Mrs. Ziegelheim should have been allowed to prove that *Apollo negligently failed to discover certain assets concealed by her former husband.* (emphasis supplied)

To suggest that this decision creates a duty for lawyers to locate hidden assets that have been concealed by a party simply is not fair. However, it does create an obligation to obtain information from the client and other witnesses, to the extent they have the ability to provide it, regarding potential fertile fields of inquiry to be pursued in discovery.

Matrimonial attorneys should make sure they have access to, and familiarity with, forensic financial and investigatory experts. Forensic experts are of assistance not only in valuing assets, but in helping to uncover them. The expert can also be relied upon to assist in the development of effective ways to present the evidence that is discovered.

The lawyer and forensic expert must form a "presentation team" to plan the case and develop a theme from beginning to end. Lawyers without access to such experts are inviting disaster for themselves and their clients. However, it is a too broad a leap to go from recognizing a duty of inquiry and investigation to imposing a duty to find.

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Timing

There are several devices and approaches for lawyers to consider in matrimonial cases when attempting to locate assets and identifying things of value.

Traditionally, forensic experts ask for five years of business and personal records, preceding the complaint for divorce. Usually, courts also will require this information for the same length of time. However, the traditional "five year" inquiry should not limit the lawyer, since there could be substantial changes to the financial picture, by way of "divorce planning" before such time.

Therefore, when interviewing a client, it is appropriate for a lawyer to attempt to determine the commencement date of serious marital difficulties. This date may coincide with the adverse spouse behaving in a fashion that was in some way financially isolating. It naturally follows that this is the time when there is a motivation to change economic patterns.

A lawyer should attempt to determine when the client noticed things being done differently, either with respect to the manner in which finances were being handled, records maintained, or when an atmosphere in the home changed and things became more secret. If this date can be established, the attorney and the forensic expert have a good starting point of inquiry for information.

Clients often report vast lengths of time as to when they believe there was a serious problem in their relationship. A matrimonial attorney should realize that not every dissatisfaction with the relationship occasions a reasonable belief that secreting or concealment is taking place. In addition, courts may not allow a review of 10 to 15 years and the records may not reasonably be available.

However, in *Kothari v. Kothari*, 255 N.J. Super 500 (App.

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Div. 1992) the Appellate Division approved a review and accountability of assets expended and dissipated as far back as the start of the marriage. Accordingly, it is important to inquire of your client about dates when he or she began to feel things were going away or when there was suspicion.

A matrimonial lawyer must develop the skill and sensitivity to debrief clients with respect to relevant events, patterns, and suspicions. At the same time, the lawyer should assist clients in developing evidence about the reasonable suspicions and to let go of beliefs about which there is simply no evidence.

Pendente Lite Applications

One of the most important phases of a matrimonial case is the pendente lite phase when orders are put in place effecting asset maintenance and support levels. These orders may affect the way a client lives, and the corresponding anxiety level, during the entire length of the case. An inappropriate pendente lite disposition may prematurely end the search for hidden assets because of the pressure created on the disadvantaged spouse. On the other hand, an appropriate pendente lite determination will allow the investigation to proceed methodically.

As attorneys, the object of pendente lite is to maintain, as closely as possible, the marital lifestyle as the case winds its way to resolution. It is therefore essential to present a complete picture to the court, which will make a decision that sets the tone for the entire case before trial without testimony or cross-examination. When representing a dependent or disadvantaged spouse who is married to a spouse whose level of earnings is not accurately reported in the tax returns, a lawyer needs to offer enough information in support of the lifestyle at the pendente lite level to persuade the court that his or her client's version of reality is the truth. This presentation must be sufficient to rebut the assertions of an adversary relying on the tax returns.

This task is not easy at this point in the litigation. Expert investigations are not likely to be completed, or even started. Accordingly, an attorney will not be afforded the opportunity to rely upon an expert to persuade the court about the client's contentions. If the trial court enters an award based upon tax returns that fail to tell the whole story, although a lawyer may be able to redress it retroactively at final hearing, the client will suffer the frustration and anxiety of insufficient finances throughout the litigation. The result, at this early stage, may be that a client is unable to "weather the storm" of the litigation and may acquiesce to the adverse spouse's inequitable demands.

Therefore, a matrimonial attorney should be creative in the pendente lite presentation. When pictures of elegant homes, fancy cars and extravagant amenities are submitted to the court in support of a lifestyle argument, it is difficult to assert, convincingly, that the minimal income reflected on the tax return demonstrates that which is available. The old saying "a picture is worth a thousand words" can easily translate, in a lifestyle case, to "a picture is worth thousands of dollars."

Conversely, if an excessive pendente lite award is made, the damage can be as devastating to the morale of a payer spouse as the damage to the morale of a payee spouse because of an inadequate award.

At the pendente lite phase of the case, a lawyer should also be in a position to argue and preserve the claim for an accounting in the event the structure or quantity of marital assets diminishes after, or shortly before, the onset of the litigation.

In some other states, the filing of a divorce complaint automatically puts in place restraining orders and preliminary injunctions with respect to the use of marital assets without judicial application having to be made. In New Jersey, an order in place preventing hypothecation and dissipation of marital assets except in the ordinary course of business may be appropriate pendente lite.

However, the failure to obtain such an order does not bar an argument at final hearing for an accounting for utilization of marital assets, not only pending the litigation, but even before it started. In *Kothari*, Judge Melvin Antell wrote that dissipation may occur even before a complaint is filed and the assets dissipated may subsequently be distributed as a form of indebtedness from one spouse to the other. The accounting approved by the Appellate Division encompassed transactions that went back to the beginning of the marriage.

Pre-Filing Strategy

In some instances, a lawyer should try to protect assets that may disappear upon an attempt being made to secure them. This situation may arise when cash or other fungible assets are purchased during the marriage with no clear payment trail and that remain in the exclusive control of the adverse spouse.

Obviously, notice to an adversary of a request for restraints creates a risk of loss. This occurrence will leave an attorney with no way of proving the assets' existence beyond the testimony of the client, which would, no doubt, be contradicted at trial, leaving the determination as purely a credibility issue. The best way to safeguard these assets is to secure them before they disappear.

The most common method is an order to show cause filed ex parte for a preliminary injunction and authorization to the county sheriff's department to serve the order on the defendant and remove the valuable items. Obviously, there is always the risk that the court will require notice to the adversary, thereby defeating the very purpose of the ex parte application. In some cases, there may simply be no other choice, especially if the asset is in

the exclusive control of the adverse spouse.

If an application is made, a matrimonial attorney must be sure to carefully present the facts to the court, so that based upon the evidence presented, the court feels compelled to act. Corroborative certifications demonstrating the existence of cash or other items of value (coins, jewelry, etc.) based on clear personal knowledge usually present a powerful evidentiary base.

If there have been well-documented threats to dissipate the assets or threats of cutting off the client in the event of a divorce, lawyers should be creative in their approaches to protect such assets.

However, in other instances, where there are large cash holdings, bearer bonds, or other assets located in a safe deposit box, protection can be achieved some times without resort to the court. If there have been well documented threats to dissipate the assets or threats of "cutting off" the client in the event of a divorce, lawyers should be creative in their approaches to protect such assets.

One plan may involve securing a credible, neutral third party to accompany the client to the safe box to remove and inventory such assets. Obviously, advocating a position of "self help" could backfire because the other side could assert that there was much more present than had been taken by your client and seek to blame your client for dissipation.

Therefore, the presence of neutral and credible third-party witnesses prevents such an accusation from being readily accepted. In addition, the attorney should contemporaneously notify the adversary that such assets are being held in "escrow" due to the often made threats of dissipation and provide the adversary with an opportunity to perform an inspection. Using this approach, the property is protected and the adverse spouse is not able to make false accusations against your client with respect to dissipation.

Characterization of Asset Eligibility And Changes in Value

Discovery and investigation through third party subpoenas and forensic experts is not the only way of identifying or locating assets in matrimonial cases.

Proper analysis with respect to the eligibility or ineligibility of assets is important in terms of preserving the marital estate or protecting separate assets that do not belong in the marital estate. An improper characterization or analysis of the issue of eligibility may, in effect, result in loss of an asset and value for the client.

It is well-established that inherited or gifted assets are ineligible for equitable distribution. There also is a line of cases that address how a change in value of an eligible asset after the filing of a complaint for divorce may or may not be subject to distribution after a complaint is filed. If there is a change in value of an eligible individually titled asset attributable to the efforts of the titled spouse, then ordinarily the value change is not eligible for distribution, whether it is a loss or a gain. See *Wadlow v. Wadlow*, 200 N.J. Super. 372 (App. Div. 1985); *Bednar v. Bednar*, 193 N.J. Super. 330 (App. Div. 1984).

On the other hand, if the change is attributable to the benign forces of the marketplace, such as a change in real estate values, then the new value is eligible for allocation, whether it is an increase or decrease. For example, if the marital home increased in value after a complaint was filed due to the benign forces of the market and not the effort of either party, it would be valued as of the date of the trial, not as of the date of the filing of the complaint for divorce. *Scavone v. Scavone*, 230 N.J. Super. 482 (Ch. Div. 1988), aff'd, 243 N.J. Super. 134 (App. Div. 1990).

This concept also probably applies to an individually titled ineligible asset. If an asset was premarital, gifted or inherited, but increased in value because of marital energy or the labor and effort of one of the owners, then the change in value between the date of the receipt of the asset and the date of a divorce complaint would be eligible for distribution.

Conversely, if the asset was a "passive" asset, subject to appreciation due to the benign forces of the market, it would not be eligible. Title is of little relevance with respect to this analysis, but the source of the asset and why it changed in value after acquisition is relevant.

A matrimonial lawyer must be aware not only that an asset changed in value, but *why* it changed in value. Without a basis for an opinion, even the finest expert offers evidence that is nothing more than a net opinion. *Parker v. Goldstein*, 78 N.J. Super. 472, 483-84 (App. Div. 1963); *Buckalew v. Grossbard*, 87 N.J. 512, 524 (1981); *Johnson v. Salem Corp.*, 97 N.J. 78, 91 (1984).

Sometimes assets change in value because of different reasons that include both activities and efforts by the owner and the benign forces of the marketplace. A parties' hard work in one economic climate may have no impact on value and in another economic climate, may cause material change. See *Berrie v. Berrie*, 252 N.J. Super. 635 (App. Div. 1991). In *Berrie*, the court opined that the change in value of an asset may have multiple causes, both passive and active in nature, and that experts could be called to opine on such distinctions. Two examples of these approaches are as follows:

• Assume vacant land of many acres is purchased before a complaint is filed. Assume further that before the complaint if filed, preliminary subdivision approvals are obtained for construction of 50 to 100 town homes. The complaint is then filed and the final subdivision approvals are obtained shortly thereafter.

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At the time of divorce, the property is worth substantially more than the purchase price of the vacant land because of the existence of completed and semi-completed town homes. Is the value of the property at complaint filing only what its cost was shortly before the complaint was filed? An argument can be made that the value of the property when the complaint was filed with preliminary subdivision approvals in place, is far greater than the cost of the property without the approvals. An expert likely would support that view.

An expert would likely also opine that the difference between preliminary approvals and final subdivision approvals usually is de minimis, simply a rubber-stamping of the preliminary approvals with minimal effort. Therefore, that the final approvals are obtained post-complaint does nothing to contribute significantly to the value in place at the time of the complaint, which value was created by obtaining the preliminary subdivision approval.

[bullet] Property acquired in one parties' name subsequent to the complaint typically would be ineligible for distribution if it was purchased or acquired with post-complaint savings or other ineligible monies. However, suppose the property is purchased entirely through a loan encumbered by a mortgage against other eligible marital assets. Clearly, the marital partnership is a venture capitalist with risk that should also give the opportunity for gain and participation in the investment. If the borrowed money was obtained without a mortgage on marital assets, through submissions of a financial statement that contained marital holdings, then one can argue that the marital estate contributed to and was part of the basis upon which the lender relied in making the loan. That should equitably entitle the other spouse to participate in the investment.

The Adversary's Records As a Discovery Tool

Rule 5:5-1(c) allows depositions to be taken as a matter of course of any person or party, excluding family members under the age of 18, in a Family Part action. A useful discovery tool in proving hidden income or assets is the proper service of a subpoena upon the adverse party's counsel to obtain copies of their invoices, ledgers, and copies of the instruments used to pay for legal services to the adverse law firm. There is nothing privileged about such information.

Moreover, there is no question that the attorney must have this information. Rule 1:21-6(b)(1) provides that all attorneys who practice in this state are to maintain records in a current status for a period of seven years which specifically identify "the date, *source* and *description* of each item deposited as well as the date, *payee* and purpose of each disbursement." (emphasis supplied).

One could make an argument that invoices are privileged because there may be commentary on the invoice that would reveal privileged attorney/client communications. However, the fact and amount of the payments and the account used to make them, are relevant evidence in a divorce case. The invoices easily can be redacted to eliminate commentary that would otherwise breach the attorney/client privilege. *Jadlowski v. Owens Corning*, 283 N.J. Super. 199 (App. Div. 1995).

Thus, your adversary has records that will identify the source of each payment received from his client. If the adverse spouse is paying his lawyer through an undisclosed account, through a third party, through another business or with cash, then that information should be discoverable.

Corporate Maneuvering

It is important for a lawyer to instruct the expert to review books and records of a corporation owned by an adverse spouse to determine if there is any corporate maneuvering designed to affect valuation. The expert should carefully review the accounts payable and accounts receivable to inquire whether third parties are holding monies due to the business that are not booked as accounts receivable, but simply are being held by the third party. Conversely, the experts should review whether suppliers or third parties are being pre-paid or overpaid for services rendered.

It is also important to inquire as to related companies, purportedly owned by third parties, who are not parties to the divorce case, but who may have connection to one of the divorce litigants. The transactions between the two companies may not be at arm's length. A sampling review of the books and records of each corporation should be requested to be sure that transactions are being reported in a parallel fashion and not inconsistently.

Moreover, transactions between these corporations may need to be compared to transactions with unrelated companies with respect to pricing. A determination may be necessary as to whether expenses from the related "unowned" corporation are being paid by the eligible corporation thereby diminishing the earnings and nevertheless benefitting one of the parties in an undisclosed fashion.

Similarly, both the expert and the attorney should consider whether the adverse party is referring or declining business in favor of, or otherwise "diverting corporate opportunity" to, third party corporations of which such party has no titular record interest, or to a corporation acquired by the diverting spouse after the complaint was filed. Of course, it is also important to investigate and determine whether the corporation is being used to pay personal expenses. ■