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## OUTSIDE COUNSEL

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### **Treatment of Enhanced Earnings Capacity As an Asset Under Equitable Distribution**

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The dissolution of a marriage is indeed a traumatic event. It imposes pain, bitterness, and rejection upon those who endure it. There is economic pain as well: as the economic efficiencies of the marital partnership are lost, both parties may have difficulty maintaining previous living standards. For those of us in the legal profession, the tragedy is more technical in nature: fighting on behalf of individuals whose lives have been shattered by this process, we must attempt to retrieve for them as much of an admittedly shrinking whole as is possible while still crafting laws which embody the reasonableness and fairness our legal system demands. Marital disputes often pose the most difficult legal questions, because it is not uncommon for the equities to lie with both parties.

A prime example of such a problem arises when the enhanced earning capacity of one spouse is the primary asset of the marriage at the time of dissolution. To illustrate, suppose the married couple, in an attempt to maximize the benefits to the partnership, decides to invest in the career potential of one spouse. As part of the plan, the other spouse will support the partnership economically during the interim. Finally, both spouses agree to postpone present consumption by sacrificing present living standards as part of the investment. The nature of the investment is such that the future rewards will far exceed the present sacrifices. However, if the marriage dissolves immediately after the earning potential of the invested in spouse has been enhanced, but before any future rewards have earned, we are left with the following scenario: few, if any marital assets have been accumulated, other than the enhanced earning capacity; a relatively low standard of living achieved during the marriage; and the non-enhanced spouse has demonstrated a level of self-sufficiency which makes support unnecessary to maintain the living standard enjoyed during the marriage. Hence, many non-enhanced spouses in this situation have argued that they are entitled to a share of the enhanced earning capacity.

This article examines how a non-enhanced spouse can be adequately protected without a distributive award, and that the recent path followed by the state of New York beginning with the *O'Brien* case requires either a judicial retreat or a legislative intervention. To contrast the path chosen by the New York judiciary, I will examine the state of the law in New Jersey and in Florida, which both have Equitable Distribution laws similar to New York's but have reached a different solution to this problem.

### **NEW YORK**

In New York, marital dissolution is governed by the Domestic Relations Law. The Equitable Dissolution provision of the DRL was incorporated in an effort to engender fairness to an area of the law which was admittedly archaic. In order to make a distributive award, judges must essentially engage in a three step analysis: first, the property must be classified as either separate or marital; marital property must next be valued; and finally, the judge must equitably distribute all the marital property to the parties.

The New York courts have in recent years significantly broadened what constitutes marital property under DRL Section 236B. The journey down this slippery slope began when the Court of Appeals held that a

professional license is marital property subject to equitable distribution. This is a *per se* rule, regardless of the value such a license ultimately represents. In justifying the expansive approach taken by the Court of Appeals, Justice Simon pointed out that the New York Legislature deliberately went beyond traditional common law notions of property when it drafted the Equitable Distribution Law. This is, however, the only suggestion offered by the court for including a professional license within the Section 236(B)(1)(c) definition of marital property, and it makes Justice Simon's literal reading of Section 236(5)(d),(e) ring hollow.

What has truly opened the floodgates to this unwarranted expansion of the definition of marital property was the court's determination of the value of the professional license. That a license itself has no market value itself is completely irrelevant; its value is the enhanced earning capacity it affords its holder. This standard has led to a barrage of decisions which have significantly expanded the definition of marital property. For example, educational degrees, the increase in value of one spouse's career during marriage, as well as one spouse's celebrity status acquired during marriage, are all now marital property in New York. A recent Supreme Court case not yet heard on appeal has gone so far as to hold that enhanced earning capacity itself is a marital asset subject to equitable distribution. This last holding in particular is so at odds with the notion that post dissolution earnings are the separate property of the spouse who earns them that it cannot be said to reflect the policies underlying the adoption of New York's Equitable Distribution Law.

Justice Simon offers a rather flawed rebuttal to my aforementioned premise in his *O'Brien* opinion. He applies a plain meaning of the words analysis to Section 236 (B)(5)(d)(6)(9)(e) to bring career potential within the realm of marital property. He further states that the legislature intended that a supporting spouse's direct or indirect contribution be "recognized, considered, and rewarded", and that to not allow a distributive award would "frustrate the underlying purposes of the Equitable Distribution Law."

This argument however, is entirely illusory. The same factors used to determine a distributive award which "required" the *O'Brien* court to find that an interest in a profession or professional career potential must be marital property are also factors the court is instructed to consider in determining an award of maintenance. Thus, the reasoning in *O'Brien* could equally be used to justify maintenance as opposed to a distributive award.

In searching for a solution to the enhanced earning capacity problem, it must be remembered that the Supreme Court is also an equity court. Within the bounds of the discretion set for it by the legislature, its primary job is to do justice between the parties. When the circumstances so warrant, the court should make a distributive award of marital assets considering the enhanced earning capacity; otherwise it should award maintenance.

To contrast the maverick position taken by the New York courts and hopefully highlight its obvious shortcomings, I shall now present the more satisfactory solution the courts of New Jersey and Florida have fashioned for this problem.

## NEW JERSEY

In 1971, New Jersey amended its divorce laws, incorporating an equitable distribution of property provision. The new statute gave the courts jurisdiction to distribute assets in any matter deemed equitable, regardless of title, and to award alimony. Public policy concerns which came to light with the explosion of divorces in the 1960's were the driving force behind the changes. While the New Jersey legislature had similarly sought to remedy injustices in its divorce laws, its courts have eschewed the renegade approach adopted across the Hudson and instead sought to achieve greater fairness in the area of enhanced earning capacity acquired during marriage.

Any enhanced earning capacity which results from the attainment of a higher educational degree or professional license is not property subject to equitable distribution in New Jersey. The Supreme Court of New Jersey settled that issue in 1982 when it so held in three separate opinions, all handed down on the same day. The Court endorsed the concepts of rehabilitative alimony as well as reimbursement alimony awards in appropriate circumstances. *Mahoney* was the first and primary case handed down by the Court; in it is the bulk of the rationale, which I will now summarize.

First, *Mahoney* distinguished between intangible assets which are property and therefore subject to distribution (such as goodwill), and those which are not (such as professional degrees and licenses). The latter lack any of the characteristics even an expansive definition of property encompasses; moreover, a professional degree represents nothing more than the possibility (emphasis mine) of future earnings. Calculation of the value of such potential income involved more speculation than the court wished to undertake; additionally, a distributive award of assets acquired by one spouse after divorce cannot be reconciled with the equitable distribution statute's conception of separate property. Furthermore, the finality of a distributive award precludes any later remedy in the event of subsequent unfairness, and as such it is not consonant with the underlying purposes of equitable distribution.

Rather than a distributive award, the court held that alimony was the appropriate remedy. In addition to rehabilitative or reimbursement alimony, the court endorses awards of permanent alimony which take into account enhanced earning capacity. Awards of alimony are modifiable under proper circumstances. In short, this type of enhanced earning capacity is not property within the meaning of the statute, although it is relevant to the issues of alimony and determination of equitable proportions for the distribution of the other marital assets.

Subsequently, the New Jersey Supreme Court held that professional goodwill is property subject to distribution. The court followed the distinction for classifying intangible assets set forth in *Mahoney*. Professional goodwill represents not simply the possibility but the probability, based on existing circumstances, of future income which is neither remote nor speculative. Finally, the court explicitly reaffirmed the *Mahoney* reasoning while citing *Lynn*.

Most recently, the New Jersey Supreme Court decided this issue in the context of celebrity status. The court held that celebrity status was a distributable asset within the meaning of the equitable distribution statute. The court cited *Dugan* in determining that celebrity goodwill is the logical extension of professional goodwill. In addition, the court pointed out that protection of Mr. Piscopo's individual right of publicity cannot be countenanced with not allowing his wife to share in that same interest. Citing *Dugan*, the court held that future earning capacity per se is not goodwill, and that New Jersey law "differs materially from New York's because in New York the value of the license alone is the marital property." In the process, the court explicitly declined to overrule the prior precedents of *Mahoney* and *Lynn*, but instead chose to follow the distinction set forth in *Mahoney*.

## **FLORIDA**

Like New York and New Jersey, Florida's divorce laws contain an equitable distribution provision. However, the enhanced earning capacity issue has posed fewer problems to the Florida courts than it has elsewhere. The Florida courts have consistently held that enhanced earnings attributable to a professional degree or license are not marital property subject to distribution; the celebrity status issue has not yet been decided.

In *Severs v. Severs*, the Fifth District held that a wife had no vested property right in her husband's educational and professional productivity, past and future. The court's decision rested almost exclusively on the Thirteenth Amendment of the United States Constitution. The majority found that "such an award by the trial court would transmute the bonds of marriage into the bonds of involuntary servitude...." The opinion also discussed procedural standards for appellate review not relevant here.

Later that same year, the Third District decided the same issue, coming to the same result. In affirming *Severs*, the *Hughes* court relied extensively on the rationale of the New Jersey Supreme Court's decision in *Mahoney*. According to the court, not only does a professional degree not possess any of the attributes of even a broad definition of property, but the inherent problem in valuing the possibility of future earnings, coupled with the finality of a distributive award make such an award an inappropriate remedy. The court held instead that the husband's education ought to be considered in arriving at the equitable distribution of other assets and in determining the propriety and/or amount of alimony as per Section 61.08(2)(f). This reading of the statute is consistent with that put forth in *Ward v. Ward*, which held that income a spouse is capable of earning may be attributed to him in determining the proper amount of an alimony award. That a professional degree itself is not property subject to distribution has been recently reaffirmed in the case of *Arce v. Arce*.

### **CONCLUSION**

Since *O'Brien* was decided, the New York courts have increasingly blurred the distinction between marital and separate property. By making distributive awards of future enhanced earnings, the courts have ignored the clear legislative intent that post-dissolution earnings be the separate property of the spouse who earns them. Furthermore, because they are non-modifiable, distributive awards may bind the enhanced spouse to a profession not of her choosing and hence perpetrate great injustice. As the New Jersey and Florida courts have aptly demonstrated, such injustice is unnecessary, since the unenhanced spouse can be adequately protected with a maintenance award. In the event that future circumstances turn out different than the Court envisions, maintenance awards may be modifiable upon application by either party. Thus, maintenance awards provide greater equity for both parties. If the Court of Appeals is unwilling to acknowledge this, then the legislature in Albany must unequivocally act to set the record straight.