



# Fine Print

A Quarterly Publication of The Ohio State Bar Association  
and Our Members

Issue 35 • Spring 2008

## Divorce Victim: Family Business?

By Charles R. Schaefer

Divorce is the end of a marriage. But the divorce process and the divorce itself has fallout, including the family's business, the enterprise that provides the family's financial support.

Often the family's business is one of the largest marital assets. Generally, most of the family's wealth, net worth and support is tied to the family's business. At least one and often both of the partners in a marriage are owners, employees or participants in the family business.

When both spouses are working in the family's business, the personal and financial effect of divorce can be more severe than if only one spouse participates. If both partners are active in

the family's business and working together, the divorce process itself can lead to many destructive forces invading the business from personal recriminations to financial feuding. Moreover, family businesses are not easily divided, so it is difficult for divorcing spouses to take a piece and "go their separate ways." Generally one partner gets to keep the business and pays the other for his or her share. Perhaps

divorcing spouses' need for money and liquidity explains why, according to an October 31, 2005 *Business Week* article ("Good Divorce, Good Business" by Michelle Conlin), 10 percent of divorced spouses continue working together after the divorce.

Is it ever possible to prevent divorce from harming the family business? Perhaps not, but divor-

cing spouses can take certain steps to protect the business as much as possible so that it can continue to generate income for the newly separated family.

Prenuptial agreements can also protect a family's business in some instances. Children who are in line to receive stock in the family's business should be urged to have a prenuptial agreement before they marry. While enforceability may be challenged and the judge may compensate divorcing spouses in other ways, setting a valuation procedure and dealing with later acquired



## New Proposed Regulations For Cafeteria Plans

By Jason A. Rothman

On August 6, 2007, the Internal Revenue Service issued new Proposed Regulations on cafeteria plans under Internal Revenue Code Section 125. While the previous regulations were not clear and not well enforced, the new Proposed Regulations are very specific, and the failure of an employer to comply with them can result in significant tax consequences for both the employer and its employees. This article addresses some of the key issues that employers must understand regarding their cafeteria plans.

Generally, a cafeteria plan allows employees to elect to contribute a

*Cont. on page 2*

*Cont. on page 2*

**Divorce Victim**, cont. from page 1

stock and appreciation in stock owned at the time of marriage, can help to minimize disruption of the business if a divorce occurs.

Even with a prenuptial agreement, a necessary objective is to find ways to divide the business's wealth without actually dividing the business. For example, when adult children are working in the business and are the designated successors, this division sometimes can be achieved by giving part or all of the family's business to the next generation. In this way, both spouses find some assurance that

the family's business wealth (or at least much of it) will not end up benefiting a new spouse. Moreover, assuming there are enough other assets, the divorcing spouses feel they have "split" the business by giving it to their children yet leaving the business intact.

Agreements among business owners can provide for mandatory buyback of ownership in the event of a divorce using a discounted valuation and/or extended payment terms in order to preserve the business and protect its assets. A buy-out may not work with a majority

shareholder involved in a divorce, because it would shift control. It can, however, be effective to protect the business when minority shareholders are involved in the divorce and can protect against having to sell assets or borrow heavily to pay off one of the divorcing spouses.

---

*Charles R. Schaefer is an attorney with the Cleveland firm of Walter & Haverfield LLP.*

**Cafeteria Plans**, cont. from page 1

portion of their salary, on a pre-tax basis, toward certain employer-provided benefits such as group-term life insurance, medical/health coverage (including health flexible spending arrangements), dependent care assistance programs, and adoption assistance programs.

Among the significant modifications/clarifications from previous guidance on cafeteria plans under the new Proposed Regulations are:

- explicit and detailed written plan document requirements, including a long list of items that a written cafeteria plan must contain and the requirement to adopt plan amendments before the date they are effective;

- additional guidance on the cafeteria plan nondiscrimination rules;
- guidance related to debit cards and grace periods for using health flexible spending arrangement money after the end of a plan year;
- detailed substantiation rules for expense reimbursements; and

- rules for implementing "evergreen" elections and automatic enrollment.

The new Proposed Regulations specifically provide that, if a plan does not satisfy the new Proposed Regulations under Code Section 125, in form or in operation, the plan will be disqualified. If a cafeteria plan is disqualified, employees will be subject to taxation on the benefits under the plan. Unfortunately, the new Proposed Regulations provide no guidance as to how to correct plan failures identified by an employer, even though minor plan failures due to administrative errors are not unusual. Such errors, even if minor, can produce very negative conse-

quences. For example, if an employer's plan allowed an employee to make an improper mid-year election change, the plan would be disqualified and all participants would have to include the pre-tax contributions as made after tax (and thus taxable.) Employers must, therefore, make

sure a plan is compliant and must perform their own nondiscrimination testing to insure that the plan does not discriminate in favor of highly compensated employees (in 2008, employees who receive \$105,000 or more in compensation) with respect to eligibility, benefits and contributions. For more information about the Proposed Regulations, visit <http://www.ustreas.gov/press/releases/hp526.htm>.

As a practical matter, the new Proposed Regulations are proposed to take effect January 1, 2009, and the IRS will issue Final Regulations sometime in the future. These Final Regulations may or may not relax some of the requirements under the Proposed Regulations, including an extension of the effective date. That being said, employers should consider the effect of the new Proposed Regulations on their cafeteria plans based on the Regulations' requirements and effective date.

---

*Jason A. Rothman is an attorney in the Cleveland office of the national labor and employment law firm of Jackson Lewis LLP.*

**The new Proposed Regulations are very specific, and the failure of an employer to comply with them can result in significant tax consequences for both the employer and its employees.**