

Stock options and divorce

Who gets the stock options in case of divorce, and what is the company's role? **Interviewed by Steve Trusty**

You are about to set up or review your stock option incentive plan. Are you giving any thought to the stated purpose of the plan, and how it might affect the outcome of any divorce proceedings for participants in the plan?

"Most companies setting up a stock option plan pay little attention to the purpose of the plan," says Phil Shechter, CPA/ABV, CVA, a partner at Berenfeld Spritzer Shechter & Sheer LLP.

"When the executives of a company adopt a stock option plan they need to focus on the purpose of the plan and consider how it will affect their lives should they divorce."

Smart Business spoke with Shechter for his insights into how stock option plans are treated in divorce proceedings.

Why should executives consider divorce when setting up stock option plans?

According to the U.S. Census Bureau, National Center for Health Statistics, 50 percent of all first marriages, 67 percent of all second marriages and 73 percent of all third marriages end in divorce. Most often, the biggest marital assets subject to division between divorcing spouses are the parties' retirement accounts, marital residence and stock options. Since the marital residence and retirement accounts are easily valued, the more hotly contested issue is the stock options owned by the executive. The issue of contention between the parties is often whether the stock option is a marital asset to be split by the parties or a nonmarital asset to be kept by the executive. The answer lies in the purpose of the stock option plan.

How does the purpose of the plan affect the division of those assets?

The purpose of the plan is the most important issue in determining if the executive is to earn the stock option benefit after divorcing a spouse. Is the stock option a 'post' divorce asset the executive gets to keep or was it 'earned' during the marriage, which makes the stock option a marital asset equally



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divided with the executive's spouse?

The Florida Supreme Court case *Ruberg v. Ruberg* is the law in Florida as it relates to the determination of the marital component of stock options when an executive is getting a divorce. According to *Ruberg*, an analysis of the purpose of the stock option plan must be identified in order to determine whether the executive's spouse is entitled to one-half of the stock options, regardless of whether they are fully vested. If the purpose of the stock option plan is to reward the executive for services that were provided to the company prior to the divorce action with his/her spouse, then the stock option is a marital asset subject to equal division between the spouses, even if the executive is required to work at the company after the filing of the divorce.

If the purpose of the stock option plan is to incentivize the executive to help promote the future profitability of the company, then those stock options that have not vested are not marital property (subject to a coventures formula) and the executive is not required to give his spouse one-half of the options.

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Can you cite an actual example of how this law is applied?

Yes, I can cite a very recent case. In this case, the executive was awarded stock options worth more than \$6 million and would have owed his wife more than \$3 million in stock options. The review of the plan documents reflected a plan purpose to retain and to provide the executive with an incentive to make the company profitable. Both parties' counsel, in this case, agreed that this wording met the *Ruberg* test for future services after the filing of the divorce and only the vested shares were to be split with the executive's spouse. Accordingly, the executive retained \$5.5 million of stock options and his spouse received \$500,000 of options.

Can prenuptial agreements affect the division of stock options?

A prenuptial, or postnuptial, agreement can be drafted to allow the executive to maintain or keep his/her stock option plan, rather than relying on an interpretation of the *Ruberg* case. The agreement has to be drafted to have the executive's spouse waive any interest in the stock option plan. In addition, in an abundance of caution, the executive's spouse must specifically waive any interest in the appreciation of assets within the stock option plan that are created during the marriage, especially created by one spouse's employment activities during the marriage. <<