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Are RSUs "Income" or "Assets" in Massachusetts Child Support Calculation?

By James M. Lynch | January 26, 2016

Child Support Family Law Divorce Division of Assets Modification

Massachusetts divorce lawyer James M. Lynch discusses RSUs and the Massachusetts Child Support Guidelines in the recently decided Hoegan v. Hoegan case.

On January 22, 2016, the Massachusetts Appeals Court addressed that very question in an appeal of a modification judgment from the Probate & Family Court entitled Hoegen v. Hoegen. The parties were originally divorced in 2010 and, as part of the divorce agreement dealing with pension and retirement funds, Mrs. Hoegen (Mother) waived all claims she might have had in a stock plan through Mr. Hoegen's (Father's) employment. More specifically, in the division of marital assets, Mother waived her entitlement to any part of Father's vested restricted stock units (RSUs) received through his employee stock program. The parties also agreed to a child support order that they stipulated was higher than the presumptive amount of support under the Massachusetts Child Support Guidelines she sought a support amount that included all of Father's income, including income from the award of RSUs. The Probate & Family Court judge, however, entered a child support modification order that excluded Father's RSUs from the calculation and Mother appealed.

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A Parent Cannot Waive Child Support as Part of the Division of Marital Assets

The Appeals Court rejected Father’s argument that Mother waived “all rights, title and interests” in Father’s stock plan in the original divorce agreement and went on to hold that Mother’s waiver of her own rights to marital property “cannot operate to waiver her children’s rights to appropriate child support pursuant to the guidelines” and that parents “may not bargain away the rights of their children to support from either one of them.” Therefore, the Appeals Court held that income relating to the award of RSUs shall be included in the calculation of Father’s child support obligation.

Because the Child Support Guidelines and the public policy underpinning trumped the Father’s waiver argument, the Appeals Court’s ruling on the issue was narrowly confined to the issue of child support. There is, however, a separate body of recent appellate law relating to stock options and whether the Probate & Family Court should consider them as assets or as part of gross income for alimony purposes. That body of case law will be the subject of another blog in the near future.

“Disparity in Standard of Living Between Households”: an Emerging Legal Standard for High Income Child Support Cases?

The Hoegen opinion also includes some interesting commentary from the Appeals Court on how probate court judges should consider “the disparity in the standards of living between the parties’ households” in cases falling outside of the ordinary scope of the Massachusetts Child Support Guidelines. The “disparity between households” consideration has appeared with increasing regularity in appellate opinions addressing higher income child support cases. As if often the case, the “disparity” consideration originated over a decade ago. See Brooks v. Piela, 61 Mass. App. Ct. 731, 734 (2004) (“Implicit in the judge’s consideration of this disparity [in income] is consideration of the children’s needs, defined in the light of [the father’s] higher standard of living”). However, in the last year or so, it seems as if the

Appeals Court has inched closer to declaring the “disparity” consideration a “rule” for cases in which ambiguity surrounds the appropriate level of child support.

In Hoegen, the Court uses the “disparity” consideration to illustrate how a failure to include the father’s RSU income in the child support calculation would “would result in an inequity”. The rule seems to have ever broader application in cases where the parties’ combined gross incomes exceed $250,000, where the Child Support Guidelines state that child support is “discretionary” once the combined income of parties exceeds $250,000 per year. Probate courts have struggled in recent years to determine support in such cases in recent years, where the 2011 Alimony Reform Act seemingly entitles non-parent spouses to greater financial support than similarly situated single parents who are struggling to raise children through child support.

It is worth nothing that a non-custodial parent who earns $250,000 per year will pay maximum child support for one child of $772.00 per week (i.e. $40,144 per year) under the Guidelines. If the same parent earns $500,000 per year, the Guidelines *still* “max out” at $772.00 per week for one child, thus leaving the custodial parent with $459,856/year in income and the custodial parent with $40,144/year in child support. In the latter example, we see where the “the disparity in the standards of living between the parties’ households'” consideration has direct application. Clearly, a non-custodial parent with $459,856/year in income can afford a *substantially* superior lifestyle compared to a custodial parent living off of $40,144/year in child support.

The Hoegen decision, along with other recent opinions, suggests the Appeals Court may be approaching a more comprehensive rule laying out the circumstances and methods by which probate courts should apply the “disparity in households” standards in cases in which the combined gross incomes of the parties exceed $250,000. Indeed, with a new version of the Child Support Guidelines due to be published in August 2016, we expect to see a significant volume of cases addressing all aspects of child support in Massachusetts in upcoming months.

Unvested RSUs: Income or Assets at the time of the Divorce?

The Hoegen decision addresses whether RSUs should be treated as income in a modification action. What about at the time of the divorce? Should unvested RSUs paid to a spouse during the marriage be treated as assets, subject to division, or income from which future alimony or child support can

be paid? Massachusetts courts have struggled with this thorny question for more than a decade. In Baccanti v. Morton, 434 Mass. 787 (2001), the Supreme Judicial Court explained the unique ambiguity of RSUs (and similar stock options) in the context of the income vs. assets debate:

What distinguishes employee stock options from most other assets is the uncertainty of their value: an employee who has been given options may never realize any value from them if their vesting is contingent on continued employment and the employee is no longer employed by the company, or if the value of the stock when the options vest is less than the price at which the options can be exercised. That, however, is simply the nature of the asset and a risk inherent in accepting stock options. Other assets, such as real estate and stock, are also subject to fluctuations in value based on varying economic factors beyond either party's control. … An employee may remain with the company until the options vest and, if the value of the stock has increased, the asset will have value. A judge can provide for this uncertainty by dividing the shares at the time of dissolution and ordering any proceeds from the options to be divided if and when they vest and are exercised. …That way, the husband and the wife share in the rise or fall of the value of the asset.

Granting stock options to employees has become increasingly widespread. … If we concluded that unvested stock options could not be considered marital assets, we would be denying one spouse the right to share in what "may be the most valuable asset between the spouses," and one to which both may have contributed. … Such an unjust result cannot have been the intent of the Legislature. [Citations omitted.]

Ultimately, the court in Baccanti held that unvested stock options can be included in the division of marital assets, despite the requirement than an employee continue his or her employment for a number of years in order for the RSUs to vest. See Wooters v. Wooters, 74 Mass. App. Ct. 839, 843 (2009). ("[C]ommon sense dictates that the income realized from the exercise of stock options should be treated as gross employment income: It is commonly defined as part of one's compensation package, and it is listed on W-2 forms and is taxable along with the other income." If not characterized as such, "a person could potentially avoid his or her obligations merely by choosing to be compensated in stock options instead of by a salary.") (Citations omitted).

However, the Baccanti decision included a major caveat in the treat of stock options and RSUs as assets subject to division, where the SJC *also* held:

[I]f the options were given for efforts to be expended after the marriage, in order to include them in the marital estate, the judge must determine whether the options were nonetheless given for efforts attributable to the marital partnership.

In other words, if the spouse who earned the RSUs can prove that the main purpose of the RSUs was not to reward past performance by the employee, but rather, the RSUs were intended to retain the employee and ensure future performance, then the RSUs might be excluded from the division of assets. Given that treating unvested RSUs as marital property could result in an assignment of 50% of the assets to the spouse, while treating the same RSUs as income would likely result in the spouse receiving no more than 35% of the assets in the form of future support, this is a major distinction.

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