

FINAL EXAMINATION

Except where indicated otherwise, assume all events and transactions described in this examination occurred in California.

PART I (60 POINTS)

Herb and Wendy were married in California in 1999. On January 1, 2003, Herb became employed by XYZ Corporation, a publicly held corporation, as a project manager.

Effective January 1, 2005, Herb was granted the right to purchase 1500 shares of XYZ Corporation at \$10 per share. The grant provided that the options could be exercised as of the following dates as to the following number of shares:

Block 1: January 2, 2007: 500 shares.

Block 2: January 2, 2008: 500 shares.

Block 3: January 2, 2010: 500 shares

The Stock Option Plan, which existed before Herb began working at XYZ, contained the following language describing the purposes of the Plan:

- 1. To encourage its employees to perform their duties as effectively and efficiently as possible, and**
- 2. To provide additional compensation to its employees for their contributions to any success the company was able to achieve.**

On January 2, 2007, XYZ stock was worth \$110 per share. That day, Herb exercised his option to purchase all of the shares in Block 1. As provided in the Stock Option Plan, XYZ immediately purchased his stock for \$110 per share, resulting in a profit of \$50,000 to Herb. Herb immediately deposited the proceeds in the parties' joint checking account. With Wendy's prior knowledge, he then combined the \$50,000 with an additional \$75,000 he had inherited in 2006 and spent the total of \$125,000 to improve a commercial rental building which he had also inherited in 2006.

Immediately before the commercial building was improved, it had been appraised in connection with a possible refinance for \$500,000. Herb eventually sold the building in June of 2008 for \$750,000. He deposited the funds in a bank account used for building expenses; title to that account was in his name alone.

On January 2, 2008, XYZ stock was worth \$160 per share. That day, Herb exercised his option to purchase all of the shares in Block 2. Again the company immediately purchased his shares, which this time resulted in a profit of \$75,000.

The \$75,000 was deposited into a new account, in the names of both parties, at Wells Fargo Bank. They referred to it as the “XYZ stock proceeds account.” The funds in this account were spent as follows:

- \$35,000 was used to purchase a piece of bare land in Amador County, on which the parties planned to build a retirement home.
- \$15,000 was used to open a brokerage account at Charles Schwab in Herb’s name alone.
- \$25,000 was used to pay for a trip to Europe, which the parties took in the summer of 2008.

Beginning in October 2008, XYZ began having financial difficulties. For the first time since he joined the company, Herb did not receive a Christmas bonus (which in the past had been quite generous). Nor did he receive a raise effective January 1, 2009 after having received large raises effective January 1, 2006, January 1, 2007, and January 1, 2008.

XYZ’s financial difficulties were followed by problems in Herb and Wendy’s marriage. The parties separated on July 1, 2009.

On July 2, 2009, without telling Wendy, Herb instructed Charles Schwab to liquidate all of the holdings in the Charles Schwab account (which were now worth only \$12,000 due to the economic downturn) and write him a check for the balance. He deposited the \$12,000 in an account at Merrill Lynch in his name alone, and then purchased 200 shares of XYZ stock, which was then selling for \$60 per share.

On January 2, 2010, XYZ stock was worth \$40 per share. That day, and without notifying Wendy, Herb exercised his option to purchase all of the shares in Block 3. Again the company immediately purchased his shares, which this time resulted in a profit of \$15,000. Herb deposited the proceeds into his Merrill Lynch account.

You are representing Wendy in the action for marital dissolution which was filed on August 1, 2010. During the course of discovery, you learn that the bank account in Herb’s name for the commercial building expenses contains \$250,000; that the value of the Amador County bare land is now \$30,000; and that the value of the Merrill Lynch account (to which nothing was contributed except the proceeds of the Schwab account and the proceeds of the January 2010 stock option exercise) is \$10,000. You also learn about the stock-option transactions of 2007, 2008, and 2010; the use of the proceeds of

each, as described above; and Herb's liquidation of the Schwab account immediately after the parties' separation.

Please advise Wendy with regard to the following issues:

1. What is the characterization of the proceeds of each of the stock options transactions (2007, 2008, and 2010)? 10 POINTS

1. What rights, if any, does Wendy have to any of the funds in the bank account related to the commercial building? 15 POINTS

2. As to the Amador County bare land:

a. What is the characterization of that property? 5 POINTS

b. If it is awarded to Herb, at what value will he receive it? 5 POINTS

c. If it is awarded to Wendy, at what value will she receive it? 5 POINTS

3. What rights does Wendy have arising out of Herb's creation of, and later addition to, the Schwab account? 20 POINTS

PART II (40 POINTS)

Alice and Barbara, who had been living together since August 2004, registered their domestic partnership on March 1, 2005. As of the date of the registration, Alice was an associate in a large San Francisco law firm. Her area of specialization was intellectual property.

Alice opened her solo law practice on September 1, 2005. She limited her practice to intellectual property law.

On March 1, 2009, Alice moved out and moved in with Cynthia, with whom she has lived continuously from that time.

On April 1, 2009, Alice acquired a new client, Daniel. Daniel was an author who had written two modestly successful, self-published, cookbooks and was working on a third. Alice was hired to obtain a copyright for the new cookbook, secure a commercial publisher for it, and negotiate a contract with that publisher.

From May 2009 through September 2010 Alice and Barbara saw each other from time to time. In June 2009 they attended the symphony together, using tickets they had purchased with Alice's earnings. In August 2009 they attended an art show, and in October 2009 they attended a play at the Curran Theater.

Alice attended Thanksgiving dinner at the former partnership residence in November 2009 (a gathering of 15 people), and Barbara celebrated Christmas at Alice and Cynthia's residence in December 2009.

Between May 1, 2009 and September 30, 2010, Alice stayed overnight at the former partnership residence on an average of three nights per month, one of which was Christmas Eve 2009.

Alice and Barbara continued to co-own the family residence, which was acquired in August 2005 as tenants in common. In April 2009 they cancelled their three joint credit cards and divided their joint savings account, which contained \$200,000 at that time. However, they kept their joint checking account open and Alice continued to deposit funds into that account on a monthly basis to allow Barbara to pay joint expenses such as the home mortgage, property tax, homeowners' insurance, a health insurance policy that covered both of them, and an auto insurance policy that covered each party's vehicle. In two letters and six e-mails from Alice to Barbara sent between May 2009 and September 2010, Alice referred to these monthly deposits as "support." Barbara also referred to them as "support" in one letter and four e-mails from her to Alice.

From May 2009 through September 2010, Barbara dated several other women, two of whom stayed over at the former partnership residence on nights when Alice was not staying there. One of Barbara's dating partners, Elyse, actually lived with Barbara for about two weeks in July 2009. However, the relationship didn't work out and the two of them called it off when Elyse moved out.

On August 15, 2009, Barbara bought a lottery ticket with funds she received from an ATM withdrawal made from the parties' joint checking account. A year later, she learned that this ticket had won her a cash prize of \$1,000,000. She did not immediately tell Alice about her winnings, but she put the \$1,000,000 in a savings account into which no other funds were deposited. Barbara has made no withdrawals from that account.

In September 2009, Alice negotiated a book deal for Daniel. His third cookbook, published in May 2010, became a best seller. The book led to a multi-book deal from the same publisher; a web site for Daniel which now receives heavy traffic and is quite profitable; and a TV show broadcast by the Food Network beginning in November 2010. In turn, Daniel's success resulted in a lot of lucrative work for Alice, who was still a solo practitioner. Her practice, of course, became more profitable than it had ever been, and Alice was now earning far more than she had ever previously earned from the practice of law.

On September 1, 2010, Barbara met Frances. It was love at first sight and Frances moved in with Barbara on September 20, 2010. Barbara immediately told Alice about this relationship shortly after Frances moved in, after which Alice stopped seeing Barbara and ceased staying over at the house.

On November 1, 2010, Barbara filed a Petition for the dissolution of the Registered Domestic Partnership. In January 2011, the parties exchanged Preliminary Declarations of Disclosure. Barbara's Preliminary Declaration of Disclosure contained information about both the savings account containing the lottery winnings, and the source of the funds in that account.

Alice and Barbara have agreed to have a joint forensic accountant value Alice's law practice.

Please answer the following questions and explain your answers:

1. What is the characterization of the bank account containing the lottery winnings? 30 POINTS
2. What is the correct date for valuing Alice's law practice? 10 POINTS

END OF EXAMINATION