**IN THE COURT OF APPEALS OF IOWA**

No. 1-768 / 11-0445
Filed December 21, 2011

**IN RE THE MARRIAGE OF RACHEL A. MCDERMOTT AND STEPHEN J. MCDERMOTT**

**Upon the Petition of**

**RACHEL A. MCDERMOTT,**
Petitioner-Appellee,

**And Concerning**

**STEPHEN J. MCDERMOTT,**
Respondent-Appellant.

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Appeal from the Iowa District Court for Dubuque County, Monica L. Ackley, Judge.

Stephen McDermott appeals from a decree dissolving his marriage to Rachel McDermott. **AFFIRMED AS MODIFIED.**

Jennifer A. Clemens-Conlon of Clemens, Walters, Conlon & Meyer, L.L.P., Dubuque, for appellant.

Susan M. Hess of Hammer, Simon & Jensen, Dubuque, for appellee.

Heard by Sackett, C.J., and Vogel and Eisenhauer, JJ.

**SACKETT, C.J.**

Stephen McDermott appeals from a December 2010 decree dissolving his marriage to Rachel McDermott. Stephen contends the property division was not equitable and his child support obligation should be modified. We affirm and modify the property division and the child support.

**SCOPE OF REVIEW.** Our review is de novo. *See In re Marriage of Zinger*, 243 N.W.2d 639, 640 (Iowa 1976). In undertaking our review, we examine the entire record and decide anew the issues properly presented. *See In re Marriage of Steenhoek*, 305 N.W.2d 448, 452 (Iowa 1981). Although this court is not bound by the findings of the trial court, we give weight to them. *Id*.

**BACKGROUND.** The parties were married in June of 1997 at which time Rachel was twenty-three years old, and Stephen was thirty-four. Stephen was farming with his family at the time of marriage and brought to the marriage some $675,000 in assets including cash, farm machinery, crops, and livestock. Rachel was working as a physical therapist, and brought a $35,000 savings account to the marriage. The couple had six children in less than a decade.[1] Rachel left outside employment at the time of the birth of their first child. She was, during a period of the marriage, able to improve her credentials which assisted her when she re-entered the job market after the couple separated. Stephen continued farming during the marriage and was farming at the time of the dissolution. The family lived on the income from the farming operation. Stephen received substantial assistance from his father in the farming operation and occasional

[1] The oldest child was born in January of 1999 and the youngest in May of 2007.

help from other family members. Neither his father nor other relatives were paid for their assistance. Stephen's parents, siblings, and extended family made efforts to help Stephen succeed in farming. In addition to the free labor, his father sold a farm to the couple for a price below market value. The sale was made with Stephen's siblings' consent and with the understanding Stephen would inherit nothing further from his parents. Stephen and Rachel purchased a farm on contract from Stephen's uncle Patrick, and when Patrick died shortly after the transaction was finalized, the couple found Patrick had left them the balance due on the contract. In addition, Rita, Stephen's aunt, paid the $53,000 inheritance tax due so Stephen and Rachel received the land free and clear from any encumbrances. Stephen also was able to use machinery owned by family members without cost.

At the time of the dissolution, the parties had managed to accumulate a net worth of over two million dollars, in large part because of the farmland acquired from Stephen's family members, which had greatly increased in value.

The parties entered into a pretrial stipulation approved by the district court. The stipulation provided that the parties agreed (1) to share physical care of the children, (2) on the valuation of certain assets, (3) on the valuation of farm equipment owned by Stephen before marriage, (4) on provisions for the children's health insurance[2] and medical expenses,[3] (5) on the division of the dependency exemptions for the children on federal and state income tax returns,

[2] Rachel would maintain the insurance and Stephen would pay her one-half the cost.
[3] These were to be divided equally.

(6) no alimony would be awarded, (7) they would pay their own attorney fees, and (8) they would split the costs of the action fifty/fifty.

The district court was left to address other issues including (1) the division of certain assets and debts, (2) income tax consequences, and (3) the amount of child support to be paid.

The district court gave the farming operation to Stephen, a house purchased after separation to Rachel, and held her responsible for the balance owing on the home as well as some small debts. Stephen was then ordered to pay Rachel $1,087,716 to equalize the property division. The sum was to be paid over either a three or five year schedule with interest accruing on the unpaid balance at the statutory rate. The district court said it arrived at the equalization payment by totaling the appraised value of the land, crops, and farm equipment. Stephen was given the option of paying it in three equal annual installments, or by making an initial payment of $500,000 with the balance to be paid in five equal installments.

In fixing child support the district court found Stephen, because he had no debt, had an average annual income of $55,000 to $70,000, and Rachel earned an annual salary of $65,000. The district court then set the parties' child support obligations that resulted in Rachel being ordered to pay $219 monthly for six children. The amount was to reduce as children no longer qualified for support, and ultimately to reduce to ninety dollars a month when only one child was subject support.

**PROPERTY DIVISION.** Stephen contends the property division was not equitable considering (1) the property he brought to the marriage, (2) the gifts and substantial financial support and other help his extended family has given the couple, (3) the equalization award made by the trial court would force him to sell his farmland because his current operation will not generate the cash flow to allow him to pay Rachel's judgment, and (4) the tax consequences of a sale of the real estate and farm assets need be considered. He argues that his premarital savings were depleted over the years, and if it were not for the labor and financial help from his family who were focused on helping him keep the farm operation viable, the parties would have a minimal net worth. He also contends the district court should not have considered growing crops in valuing the farmland as they were in actuality his income, and not assets of the parties to be divided. He notes Rachel has her income, and she has made no contribution to the crops that were in the field at the time of the dissolution hearing.

Rachel contends the division of assets is equitable. She advances that the concessions on the price of the land and gifts made by Stephen's family were made to her too. She does recognize she would not have benefited in that regard had she not been married to Stephen, and that the land was given so that Stephen could farm it. She also contends we cannot consider the tax consequences of a sale because there was no sale.

The distribution of the property should be made in consideration of the criteria codified in Iowa Code section 598.21(5) (2009). *See In re Marriage of Estlund*, 344 N.W.2d 276, 280 (Iowa Ct. App. 1983). There are no hard and fast

rules governing economic provisions in dissolution actions. *In re Marriage of Vrban*, 359 N.W.2d 420, 423 (Iowa 1984). Precedent is of little value on these issues; our decision must depend upon the particular facts relevant to each issue. *Id*. "The basic rule is that the property division . . . of a dissolution decree must be equitable to both parties." *In re Marriage of Wiedemann*, 402 N.W.2d 744, 747 (Iowa 1987); *see also In re Marriage of Callenius*, 309 N.W.2d 510, 514 (Iowa 1981). "Iowa courts do not require an equal division or percentage distribution." *In re Marriage of Miller*, 552 N.W.2d 460, 463 (Iowa Ct. App. 1996). Our determination turns on what is fair and equitable in each circumstance. *Id.*

**CONSIDERATION OF TAX CONSQUENCES.** We first look to the tax consequences of the district court's decision. In the division of property the tax consequences to a party may be taken into account. Iowa Code § 598.21(5)(j); *see also In re Marriage of Hoak*, 364 N.W. 2d 185, 193 (Iowa 1985).

In *In re Marriage of Hogeland*, 448 N.W.2d 678, 680–81 (Iowa Ct. App. 1989), we addressed a husband's argument that, in failing to consider income tax consequences of a property division, the trial court substantially overvalued the assets allocated to him. We looked to the tax consequences having determined in that case that the payment of a lump sum of cash to a spouse would in all probability require the liquidation of capital assets, and found the income tax consequences of such a sale should have been considered by the trial court in assessing the equities of the property. *Hogeland*, 448 N.W.2d at 680-81. Finding the trial court did not adequately consider the tax consequences of a

liquidation, we considered them as a factor in modifying the economic provisions the decree. *Id.* at 681.

In *In re Marriage of Friedman*, 466 N.W.2d 689, 691 (Iowa 1991), the Iowa court refused to consider that "tax consequences on an illusory[4] future sale of stock."[5] The *Friedman* court discussed *In re Marriage of Hayne*, 334 N.W. 2d 347, 353 (Iowa Ct. App. 1983), where this court did not consider tax liabilities because there was no order to liquidate a Keogh plan, and there were other assets to meet the court's order without liquidation. *Friedman*, 466 N.W.2d at 691. The *Friedman* court also cited *In re Marriage of Dahl*, 418 N.W. 2d 358, 360 (Iowa Ct. App. 1987), where we noted the district court, in dividing the property in a dissolution, shall consider the tax consequents to each party, but noting the tax consequences in that case were essentially the same for both parties. *Id.* at 691.

Rachel points out that pursuant to *Friedman*, 466 N.W.2d at 691, it is not proper to consider income tax consequences absent evidence a sale of property[6] is pending, contemplated, or has been ordered by the court, and argues that *Friedman* dictates that we cannot consider the tax consequences here. We disagree.

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[4] Black's Law Dictionary 763 (8th ed. 2004) defines illusory as "Deceptive; based on a false impression." Webster's New College Dictionary 64 (3d ed. 2005) defines illusion as "a mistaken perception of reality."

[5] But see *Daniel v. Holtz*, 794 N.W.2d 813, 818 (Iowa 2010) where the court noted in determining valuation of real property in selling corporate stock that under certain circumstance a hypothetical buyer of stock would take into account any tax liabilities of the corporation, but refrained from establishing a blanket rule imposing a particular appraisal methodology.

[6] In the *Friedman* case the property was stock. *Friedman*, 466 N.W.2d at 691.

First, it is clear that a sale is contemplated and not illusory. Stephen's income is insufficient to pay the judgment, and this income is also not sufficient to service a mortgage. Consequently, we cannot, as the *Friedman* court did, find a sale to be merely illusionary nor can we, as the *Hayne* court did, find there are other assets to pay the award. The district court decision leaves Stephen with a payment to be made of over a million dollars, and the only assets to pay it are the tools of his husbandry, which carry with them substantial tax consequences if sold. Nor can we find, as the *Dahl* court did, that the parties will have the same tax consequences. If the district court is affirmed Rachel will take the one million dollars in cash free of any tax liability.[7] The entire tax burden of a sale of the farm assets would fall on Stephen.[8]

Stephen introduced reliable evidence that a liquidation of the farm assets would, with taxes and sale expenses, cost about $750,000 leaving him with a property settlement nearly $800,000 less than Rachel's. While it is not only inequitable to Stephen, it also is inequitable to his children and it would substantially decrease his ability to support them.

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[7] 26 U.S.C. section 1041 provides:

> (a) General rule.—No gain or loss shall be recognized on a transfer of property from an individual to (or in trust for the benefit of)—
>
> (1) a spouse, or
>
> (2) a former spouse, but only if the transfer is incident to the divorce.
>
> . . . .
>
> (c) Incident to divorce—For purposes of subsection (a)(2), a transfer of property is incident to the divorce if such transfer—
>
> (1) occurs within 1 year after the date on which the marriage ceases, or
>
> (2) is related to the cessation of the marriage.

[8] Stephen argues that had the district split the assets rather than giving Rachel a dollar amount, the tax burden would fall more equally.

We find the anticipated tax consequences of a lump sum payment to Rachel, without considering the anticipated tax consequences of a liquidation of all or part of the assets, renders the division inequitable, and we address the parties' additional arguments in determining how it should be modified.

**GIFTED PROPERTY.** Stephen contends Rachel should not have benefited from the gifts and concessions made by his family, but that they should have been set aside to him. Rachel correctly argues the gifts and concessions were made one-half to her. She does not contend she is entitled to any of Stephen's gifted property, nor would we find that she should be.

Iowa Code Section 598.21(6) provides:

> Property inherited by either party or gifts received by either party prior to or during the course of the marriage is the property of that party and is not subject to a property division under this section *except upon a finding that refusal to divide the property is inequitable to the other party or to the children of the marriage.*

(Emphasis added.) This section applies to all gifts and inheritances, and does not make any reference to who the donor was. We agree the person who gave the gifts or gave the inheritance is not relevant. Even though the gifts were made to Rachel by Stephen's family, Stephen can make claim against them, or a portion of them, if we find that a refusal to give him Rachel's portion is inequitable to Stephen or his children or both. Gifts and inheritances received by a party during the marriage are the property of that party and not subject to a property division except upon a finding that refusing to divide the property is inequitable. *See In re Marriage of Mentel*, 359 N.W.2d 505, 506 (Iowa Ct. App. 1984).

The requirement to set aside to a party the property which has been received as a gift is not absolute. *See In re Marriage of Thomas*, 319 N.W.2d 209, 211 (Iowa 1982).[9] Exceptions discussed by the court in *Thomas* include, inter alia, unfairness to spouse and children, length of the marriage, and any other matters which tend to negative or mitigate against the appropriateness of dividing the property.

Rachel recognizes, as the evidence shows, that she was only named on the gifts and concessions because she was married to Stephen, and they were made so that Stephen could farm and support his family, including Rachel. The McDermott family naively believed the marriage would prevail, and their sacrifices would enable Stephen to provide for his family. Stephen's ability to do

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[9] *Thomas*, 319 N.W.2d at 211 states:

> As noted, the requirement to set aside to a party the property which has thus been inherited or received as a gift is not absolute. Division may nevertheless occur to avoid injustice. A number of factors might bear on a claim that property should be divided under this exception. These include:
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> (1) contributions of the parties toward the property, its care, preservation or improvement;
>
> (2) the existence of any independent close relationship between the donor or testator and the spouse of the one to whom the property was given or devised;
>
> (3) separate contributions by the parties to their economic welfare to whatever extent those contributions preserve the property for either of them;
>
> (4) any special needs of either party;
>
> (5) any other matter which would render it plainly unfair to a spouse or child to have the property set aside for the exclusive enjoyment of the donee or devisee.
>
> Other matters, such as the length of the marriage or the length of time the property was held after it was devised or given, though not independent factors, may indirectly bear on the question for their effect on the listed factors. Still other matters might tend to negative or mitigate against the appropriateness of dividing the property under a claim that it falls within the exception.

so will be seriously impacted if he is required to make the ordered payment to Rachel. The testimony is that the gifts went to the couple as a family, and Rachel received the benefits as Stephen's wife. It was never intended that Rachel receive the gifts individually.

The evidence also shows that the children will be at a disadvantage if Rachel receives one-half of the property in question because Stephen, who knows only farming, will see his income substantially reduced if he does not have available farmland. And in *In re Marriage of Andersen*, 243 N.W.2d. 562, 564 (Iowa 1976), the court noted in allowing a farmer to retain farmland it is not inconceivable such retention might inure to the eventual benefit of the children. For these reasons and others we find it inequitable to award the value of all of Rachel's gifted and inherited property, which was received from Stephen's family, to her.

**OTHER FACTORS.** Stephen contends there are other factors that make the distribution inequitable. He points out that he brought to the marriage some $650,000 in money, farm equipment, livestock, and crops, and he received no credit for this. We do give consideration as directed by Iowa Code section 598.21(5)(b) to the property he brought to the marriage. Stephen contends considering this factor Rachel should receive a payment of about $194,999.40.

Considering all arguments we believe an equitable distribution to Rachel is $250,000 and order that a judgment in said amount be entered against Stephen and that the judgment should be paid within sixty days.

**CHILD SUPPORT.** Stephen challenges the child support award. Rachel was ordered to pay Stephen $219 in child support, and the amount was to decrease as the number of children subject for support decreased. The court found Rachel had an annual income of $65,000[10] and Stephen had an annual income of $55,000.[11] Stephen contends his average income during the marriage was about $35,000 a year. The court in determining Stephen's income noted he had no debt, and that he purchased equipment at the years' end to lessen his income. Stephen contends the district court did not properly establish his income for purpose of applying the child support guidelines.[12] He argues the equipment was not purchased to decrease income, but was purchased because it was needed.[13] He also argues in one year he sold $9000 worth of trees, which income he will not have in other years, and that in 2009 he minimized improvement and repairs because of the pending dissolution, which increased his reportable income. Rachel contends the amount of child support is fair and Stephen's income was properly computed.

Stephen also contends the district court erred in computing child support in that it allowed Rachel all health insurance costs, but ordered he pay her one-half the cost of the insurance. Rachel contends the health insurance issue was properly calculated. We find no reason to modify the district court's finding of Stephen's income or the issue of insurance cost noting we are not dealing with a

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[10] After the parties' separation Rachel, who had acquired some additional education during the marriage, returned to the workforce.
[11] The fact Stephen will need to sell land and/or accumulate debt will reduce his future income unless he is able to obtain additional land to farm.
[12] It appears the district court took a three-year average.
[13] It does not appear that there is a question of accelerated depreciation.

defined salary, but rather an estimate of future income. We affirm this part of the award of child support.

Stephen further argues the district court erred in providing that the parties share the children's extracurricular activity expenses. He argues it is the parents' right to decide on extracurricular activities. He argues each parent should pay for the extracurricular activities that he or she elects to support.

The child support guidelines take into account the reasonable cost of living, including educational expenses of dependent children, and attempt to balance those costs against the legitimate needs and expenses of the payor parent. *See State ex rel. Epps v. Epps*, 473 N.W.2d 56, 58 (Iowa 1991). In *In re Marriage of Fite*, 485 N.W.2d 662, 665 (Iowa 1992), the court, while finding a child's attendance at a parochial school not unreasonable, did not believe this provided a basis for increasing the payor's support level above the guideline amount considering that parent's income and expenses. *See also In re Marriage of Gordon*, 540 N.W.2d 289, 292 (Iowa Ct. App. 1995).

In *Gordon*, we found the custodial parent's request for additional child support for clothes, school supplies, and summer recreation activities did not support a deviation from the guideline amount. *Id.* We reasoned that these expenses were already considered under the guidelines, and a separate support order covering such expenses was improper absent a finding that the guideline amount would be unjust or inappropriate. *Id.* The trial court there made no such finding, and we were unable to do so after a de novo review of the evidence. *Id.*

Accordingly, we modified the district court decree to remove the additional support obligation for summer activities, clothes, and school supplies. *Id.*

In this case we believe the guidelines take into account the reasonable cost of extracurricular activities, and modify the award to omit the provision that the parents share this expense. *See id*.; *see also Epps*, 473 N.W.2d at 58.

**CONCLUSION.** We modify the property division award and provide that the equalization payment ordered by the district court should be decreased to $250,000, and that the time of payment be modified to sixty days following the issuance of procedendo. We affirm the child support award, but modify to omit the provision that the parents share the expense of extracurricular activities.

Costs on appeal are taxed one half to each party.

**AFFIRMED AS MODIFIED.**