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The Pasternak & Fidis Reporter

Pasternak & Fidis, P.C.
7735 Old Georgetown Road
Suite 1100
Bethesda, Maryland
20814-6183
301-656-8850
Fax: 301-656-3053
www.pasternakfidis.com

Credit Cards, Protecting Your Credit, and Divorce

by Vicki Viramontes-LaFree

One of the most valuable things a person can have is a good credit rating. Divorcing couples need to have access to credit and to protect their financial security by protecting their credit. During a divorce, a credit rating becomes vulnerable. This article addresses what spouses contemplating divorce should know about their credit card obligations and how to protect against being held liable for a former spouse's debt following a separation.

CREDIT CARD LIABILITY AND PROTECTING YOUR CREDIT

Contrary to what many people believe, one spouse is not liable for the credit card debt of the other spouse unless they are joint cardholders. To be held contractually liable for credit card debt, a person must either be the primary cardholder or a co-applicant on the credit card application. Joint cardholders are jointly liable for the debt and a creditor may demand payment or sue one or both parties for such liability. The Truth-In-Lending Act defines a "cardholder" as "any person to whom a credit card is issued or any person who has agreed with the card issuer to pay obligations arising from the issuance of a credit card to another person." 15 U.S.C. 1602(m). The Act protects consumers against fraudulent or unauthorized use of their credit cards. "Unauthorized use" is defined as use of a credit card by a person other than the cardholder who does not have actual, implied, or apparent authority for such use and from which the cardholder receives no benefit. 15 U.S.C. 1602(o). Absent fraud or an unauthorized use of a credit card, the Act does not limit a cardholder's liability for the charges of a third party.

Credit card agreements are contracts. The use of a credit card may create a legally binding agreement. The agreement between the cardholder and the credit card issuer will contain a description of each party's rights, duties, and liabilities. Some agreements create two separate classifications of customers — recipients of cards with an account number established in their own names usually referred to as "cardholders," and recipients of cards with an account number established in the name of another, commonly referred to as "holders of related cards." Cardholders are generally liable for charges resulting from the "authorized use" of their credit cards by another person. Authorized use occurs when a cardholder voluntarily gives another person permission to use his or her credit card. Even if the person misuses the credit card, by charging more than the cardholder authorized or by incurring charges not contemplated by the cardholder, the cardholder is liable to pay those charges. Courts are divided on whether a cardholder can limit his or her obligation for charges on his or her credit card by another person. Similarly, there is conflicting authority on whether notice to the credit card company that a person has misused the card is sufficient to terminate a cardholder's responsibility for such charges occurring after that notice.

Generally, "holders of related cards" are not liable for charges made by cardholders, but they may be contractually liable for those purchases

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Pasternak & Fidis, P.C.
Attorneys at Law

7735 Old Georgetown Road
Suite 1100
Bethesda, MD 20814-6183
(301) 656-8850
Fax: (301) 656-3053
www.pasternakfidis.com

Business, Real Estate & Litigation Group
N. Alfred Pasternak
Mitchell I. Alkon
Roger A. Hayden, II
J. Michael Conroy
Jason W. Henderson

Divorce & Family Law Group
Anne (Jan) W. White
Linda J. Ravdin
Vicki Viramontes-LaFree
Lucy E. Nichols

Estate Planning & Administration Group
N. Alfred Pasternak
Marcia C. Fidis
Nancy G. Fax
Patrick M. Schoshinski
Lauren D. Krauthamer

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made by them. Prior to applying for a credit card or accepting a card of your spouse, it is important to review the credit card agreement to fully understand your rights and liabilities.

JOHNSON V. MBNA

A recent case illustrates some of the implications for spouses with credit cards after a divorce. In Johnson v. MBNA, 357 F.3d 426 (4th Cir. 2004), Linda Johnson was an authorized user of her husband's MBNA credit card. After their divorce, her ex-husband filed for bankruptcy. MBNA notified Linda Johnson that she was liable for the $17,000 balance as a co-applicant on the account. Johnson notified the three major credit reporting agencies that she disputed her liability. Johnson claimed that the card was not in her name, that she had not applied for the credit card, and that although she was an authorized user she had never used the card. MBNA responded that Johnson was responsible for the debt. Based on that information the account continued to be reported on Johnson's credit report. Johnson prevailed in her claim against MBNA because MBNA did not conduct a reasonable investigation of Johnson's dispute as required by the Fair Credit Reporting Act. Specifically, MBNA did not review its records, including the account application, to determine whether Johnson's claims were correct.

Johnson won $90,000 in damages. But she spent more than three years fighting a big corporation to get her credit fixed. Moreover, she had all the frustration, anxiety and cost of a lengthy litigation process.

STEPS TO AVOID PROBLEMS

Parties considering separation should protect their financial security by making appropriate credit card account changes before they enter into a marital settlement. Steps to consider include:

- Obtain a copy of your credit report from the three major consumer reporting agencies (Experian @ www.experian.com, Equifax @ www.equifax.com, and Trans Union @ www.transunion.com). Use it to verify account balances, identify all credit cards in joint names as well as cards in your name on which your spouse is an authorized user, discover accounts you may have forgotten, determine who is legally liable for any debts, and identify erroneous information that should be corrected.
- Contact all credit card companies and determine whether you are a co-applicant or only an authorized user.
- Obtain copies of all credit card applications.
- Cancel all separate credit cards that you do not use or do not need.
- Terminate your status as an authorized user of your spouse's credit card.
- Consider canceling some or all joint accounts and accounts in your name on which your spouse is an authorized user. In some cases, such as where a spouse has a history of abusing credit, it may be necessary to cut him or her off completely. In others, it may make more sense to reduce the number of joint accounts but to retain some joint credit for a period of time while the parties reconfigure their financial affairs.
- Open new individual accounts, if necessary.
- Notify all credit card companies in writing regarding cancellation of an account or termination of a spouse as an authorized user. Send the notice by certified mail, return receipt.
- Do not accept a credit card company's refusal to close an account. An account that has an outstanding balance will remain open until the balance is paid in full. But a cardholder is entitled to close the account to any new charges.
- Before cutting off your or your spouse's access to joint credit, get legal advice.

DEALING WITH CREDIT CARD DEBT IN MARITAL SETTLEMENT NEGOTIATIONS

When parties have outstanding unsecured debt it is best to resolve responsibility for payment as part of the marital settlement negotiations. A marital agreement allocating responsibility between the spouses is not binding on the credit card company. Both spouses will remain liable to the creditor for the joint debt until it is paid in full. There are several options parties should consider at the negotiation stage:

- Insist that all joint accounts be closed to new charges.

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Important Information for Everyone Who Owns A Permanent Life Insurance Policy

Many permanent life insurance policies will not perform as expected. If you own permanent life insurance policies, you may want to determine whether the policies will last long enough to pay a death benefit.

Permanent life insurance works because in the early years premiums are paid into the policy that are more than the actual "cost" of the policy. What is left after the "cost" of the policy is paid stays in the policy as "cash value" and this amount grows tax-deferred. The growth of the tax deferred cash value is largely dependent on the interest rate (in whole life or universal life) obtained by the carrier, or the investment return (in variable life) obtained in the sub-accounts.

A life insurance policy is sold with a sales illustration that predicts the performance of the policy over a period of time that can last 20, 30, even 40 years or more. The illustrations are typically based on assumptions about the mortality charges and investment returns within the policy. A policy purchased in 1984, for example, would have forecast an interest rate assumption of almost 12%. A policy purchased as recently as ten years ago would have forecast an interest rate of about 8%. Today, many existing universal life policies are actually crediting as low as 4%. How do lower interest rates affect a policy? The premium needed to fund a policy at these lower interest rates may be 50% higher or more than at the higher interest rate. The effect of the interest rate drop we have experienced has left some existing policies woefully underfunded. In some instances, the policies may lapse well before expected mortality.

But the news is not all bad. The "cost" of life insurance — the "mortality charge" — has dropped dramatically, especially in the last decade. Why? We are living longer. Advances in medical science, along with a growing appreciation of the value of exercise and proper diet, have made us a healthier group.

But the lower costs for life insurance cannot be obtained in the older policies. The companies do not call you up and offer to lower your rates. The lower rates are available only in newer, more efficient policies.

What does this mean to you if you own a permanent life insurance policy? It means that it is more important than ever to review your policies to make sure that they still meet the original goals and objectives and that they represent the best value available in the marketplace.

If you have a policy that you feel needs to be reviewed, please give us a call. We can put you in touch with professionals who can analyze your existing policy and provide you with the guidance you need.

This article was adapted from an article written by Lenard S. Cohen, CLU, a certified financial planner practicing in Rockville.

Pasternak & Fidis Speakers Bureau

Are you looking for a speaker for your next meeting? Our experienced attorneys are available to address your business, professional, educational or social group on a variety of topics related to our practice areas. Are you interested in the current and future estate tax laws? How do child custody agreements affect school policies? Is re-financing your home an option you should consider? We can make a presentation tailored to your group covering these or other subjects. Please call our Administrator, Mary Jane Tiedeman to discuss your requirements.

Spotlight on Vicki Viramontes

Vicki Viramontes-LaFree is the most recent lawyer to become a partner in Pasternak & Fidis, having been promoted from associate in January 2005. Simultaneously, she took over as Chair of the firm's Divorce & Family Law Group.

Law is Vicki's second career. As a young girl growing up in Las Cruces, New Mexico, she wrote in her diary about wanting to be either a lawyer or a legal secretary. However, she left undergraduate school in her second year and moved to Albuquerque where she began work at an insurance company. A year later she started at Xerox as the only secretary for a sales department of 25 employees. Over the next 13 years she worked her way up in sales and management with responsibility for a $7 million budget and supervisory authority over a number of people who were much older than she was.

Even though Xerox made it possible to move up without an undergraduate degree, she always wanted to finish her degree. While at Xerox her dad died. That event made her realize she had to decide how she would spend the rest of her life. She quit Xerox and gave herself five years to finish undergraduate school and get her law degree. She took 18-hour semesters, went to summer school and worked weekends. Five years later she had reached her goal of graduating from law school.

Vicki is married to Gary LaFree and they have a daughter, Alix, age 9, and two children from Gary's previous marriage, Andy, age 21, and Katie, age 18. Gary was Vicki's criminology professor at University of New Mexico. They met briefly when Vicki went to complain to

On June 17, 2005 P & F partner, J. Micha of the Maryland State Bar Association a Maryland. Our congratulations to Mike this important organization.

-LaFree

him about the grad student he left in charge of his class while he traveled. She made a point of complaining before she got her grade in the course so her complaint would not seem like sour grapes. Several years later they met again when Vicki was a first year law student and was given a work-study assignment on which Gary was co-directing.

After graduation from law school in 1994, Vicki worked at several jobs, then started her own firm in 1996. As a solo she handled a range of matters, including employment cases, personal injury, estate planning and family law. When her husband was offered an opportunity to join the faculty of University of Maryland, she closed her practice and started over, taking the Maryland Bar and joining Pasternak & Fidis as an associate in the Divorce & Family Law Group.

Among her professional activities, Vicki is a member of the Montgomery County Inns of Court and she is a volunteer with the D.C. Superior Court Self-Help Center. She has taken the National Institute for Trial Advocacy (NITA) intensive trial training course. She has taught continuing legal education programs on division of military retirement benefits at divorce and she has served as a faculty member for advanced training for volunteer family court mediators at D.C. Superior Court.

When she is not practicing law Vicki likes to travel, particularly to France and Italy, play tennis and listen to live music, especially jazz and classical. ●

l Conroy will be installed as President its annual meeting in Ocean City, s he takes on the challenges of leading

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- If there are sufficient assets to do so, pay off joint credit card debt in full from marital assets before division.
- If the marital home or other marital assets are to be sold, require that joint credit card debt be paid from sale proceeds before distribution to the parties.
- Require that the party who agrees to assume responsibility for a joint credit card transfer the balance to a separate credit card.
- A spouse with more resources may agree to use his or her funds to pay off joint debt incurred by an irresponsible spouse and perhaps obtain a trade-off in the negotiations. The cost to do so may be less than the value of a good credit rating that may be lost or the attorney's fees that may be incurred to solve a bigger problem later on.

In the best of all worlds all joint credit card debt would be paid as part of the division of assets, or each party would "refinance" his or her share of joint debt by transferring the account balance to a separate account. Whether or not this is done, an indemnification clause in the marital settlement agreement is customary. A properly drafted agreement will include language that if a spouse is required to make any payment for which the other spouse is responsible, the responsible party will reimburse the other for all resulting costs including attorney's fees. However, an indemnification clause does not provide protection from the creditor; it is binding only on the parties. Thus, an indemnification clause provides minimal protection for the other spouse when the obligated party fails to pay as agreed. In such a circumstance, a financially responsible former spouse will likely pay off the creditor to protect

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NEWS

The Fall/Winter 2004/2005 *MSBA Section of Estate and Trust Law Newsletter* features an article by P & F partner, Marcia Fidis. "Planning for Maryland's Decoupled Estate Tax" reviews the recent changes in federal and state estate tax laws and discusses drafting estate plans in a decoupled environment.

P & F partner, Al Pasternak authored an article in the *Legal Review Supplement* to the April 29, 2005 issue of *The Gazette of Politics and Business*. Al's article, entitled "Business Planning and Organization" stresses the need for every business, large and small, to have a succession plan in place to protect the interests of the stockholders, partners or owners in the event of the death or disability of a principal of the business.

Nancy Fax will become the Chair of the Estate and Trust Law Section of the Maryland State Bar Association for the fiscal year July, 2005 – June, 2006.

P & F partner, Linda Ravdin is quoted extensively in the June, 2005 issue of *Washingtonian* in an article on prenuptial agreements. "Sex, Lies, and Prenups" describes Linda as "one of the nation's leading specialists" in drafting and negotiating prenuptial agreements. She will also be featured later this year in a national advertising campaign for BNA Tax Management. Linda is the author of *Marital Agreements*, a BNA Estates, Gifts & Trusts Portfolio that is considered a standard reference for family law practioners.

The D.C. Bar will host a presentation on July 14, 2005 entitled "Practical Drafting Under the New D.C. Uniform Trust Law" which will include Nancy Fax as a panelist.

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HIPAA Privacy Rules: Unanticipated Consequences

By Lauren D. Krauthamer

Recent rules under the Health Insurance Portability and Accountability Act of 1996 (HIPAA), intended to ensure health information is kept private, have led to unanticipated consequences that could affect many people.

A major goal of the HIPAA rules is to assure that your health information is properly protected. Health care providers cannot provide information about a patient's past, present or future physical or mental health or condition, health care the patient is receiving, or the past, present or future payment for health care received by the patient without the patient's consent. Failure to comply with the HIPAA rules can result in fines of $100 per failure to comply, and criminal penalties can result in monetary fines and imprisonment.

These protections become problematic when situations arise in which family members, friends, or even business associates (in certain cases) need to obtain protected health information. For example, in some families one person may take on the primary responsibility of paying bills. Under the HIPAA rules, a spouse or partner questioning a bill will be unable to obtain information about the health care charges because the rules prevent the health care provider from disclosing information to anyone other than the patient, unless authorized to do so by the patient.

Another obstacle may occur if you have a "springing" power of attorney as opposed to a power of attorney that is immediately effective. A "springing" power of attorney becomes effective when you become incapacitated, but the person designated to legally act on your behalf, the agent, cannot do so until he or she proves your incapacity. In order to prove your incapacity, your agent must obtain a determination from your doctor certifying your disability. Without prior authorization, this is not possible under the HIPAA rules. Therefore, if your agent is not authorized in advance to obtain your medical information he or she may not be able to obtain the determination required for the power of attorney to "spring" into effect. As a result, no one will be authorized to act on your behalf and a guardianship proceeding may be necessary. Your intended agent may have to persuade a court to order the medical provider to release information sufficient to establish your incapacity.

Privacy of medical records is also an issue in fiduciary relationships. At times, it may be necessary to determine whether a fiduciary is under a disability and therefore unable to serve in his or her fiduciary role. Prior to the HIPAA rules, a beneficiary of a trust, for example, might contact the trustee's doctor to request a written determination that the trustee is under a disability so that the named successor trustee could take over. Although not guaranteed a response from the health care provider, due to general privacy concerns, such a question today would not be answered because of the HIPAA rules. Your estate planning and/or business planning documents should contain a provision enabling a beneficiary to remove a fiduciary in the event of the fiduciary's disability and unwillingness to resign. At the same, time the fiduciary's privacy needs to be taken into consideration so that a beneficiary does not abuse the ability to request medical information.

So what can you do to ensure that your medical information is secure yet accessible when necessary? You can complete a HIPAA authorization form and update your estate and/or business planning documents to take into consideration the HIPAA rules. A HIPAA authorization form enables you to designate certain individuals to whom health care providers can release your health information. To learn more about the HIPAA rules and updating your documents, please contact a member of our Estate Planning and Administration Group. ●

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his or her good credit rating. His or her only recourse will be a suit against a spouse who has become insolvent.

Another common provision to include in an agreement is that debts assumed by a former spouse are not dischargeable in bankruptcy. However, like indemnification clauses, these provide minimal protection.

TAX CONSEQUENCES OF DEBT FORGIVENESS

When the debt load is unmanageable, you or your attorney may be able to negotiate with creditors for a reduction, or forgiveness, of credit card debt. Section 108 of the Internal Revenue Code provides that when a taxpayer negotiates forgiveness of an outstanding debt with a creditor, the reduction is taxable income. The creditor must issue the taxpayer a 1099 form reporting this income to the IRS. For example: Jane Taxpayer has a $25,000 balance on her Visa credit card. Jane works out a deal with Visa to pay only $10,000. Visa is required to issue a 1099 to Jane showing taxable income of $15,000. Under some circumstances, such as by proving his or her insolvency to the IRS, the taxpayer may be able to avoid paying income tax on this income. The debt will also continue to appear on the credit report which will show that the ultimate amount paid was less than what was owed.

CONCLUSION

Couples contemplating divorce should take care of their joint credit card debt early on rather than facing the frustration and cost of fixing bad credit later. Spouses should be aware of the credit cards each has or has access to by virtue of their marriage. It is also important to control acquisition of new joint debt. By taking a few simple precautions, an individual going through a divorce can protect his or her credit and avoid credit card related hassles down the road. ●

PASTERNAK & FIDIS, P.C.

NEWS

In March, 2005 Linda Ravdin and Vicki Viramontes-LaFree taught a continuing legal education course sponsored by Legal Services of Northern Virginia on dividing military and federal government pensions at divorce.

Three P & F partners, Marcia Fidis, Nancy Fax and Linda Ravdin, gave presentations at the Maryland Institute for Continuing Professional Education for Lawyers (MICPEL) Advanced Estate Planning Institute in Columbia, Maryland on May 20, 2005. Linda and Marcia spoke on the topic of premarital and domestic partnership agreements, and Nancy reviewed current legislative developments in estate and trust law.

Linda Ravdin published an article in the Maryland State Bar Association's *Family Law News* entitled "No News is Good News: Validity of Premarital Agreements and Cannon vs Cannon."

The Estate Planning and Administration Group welcomes Angela Marrin as a new Probate Paralegal. Angela has over six years of experience handling estate and trust matters for firms in Washington, D.C. and Virginia. She is a graduate of Millersville University of Pennsylvania and is an active Girl Scout leader.

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