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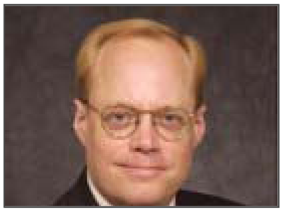

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Harold Hamm's Billion Dollar Divorce And The IRS

The news that Harold Hamm has navigated his divorce means big dollars changing hands, although not as big as had once been projected. Mr. Hamm is worth about $14 billion and is the CEO of Continental Resources. His divorce has been protracted, but now a judge has ordered Mr. Hamm to pay Sue Ann Hamm $995.5 million, roughly $320 million of which is due by the end of 2014. Thereafter, there are to be monthly installments of $7 million or more.

It is unlikely that Mr. Hamm would fail to pay, but to be certain, the court placed a lien on 20 million shares of Continental stock. Of course, Mr. Hamm is probably not feeling too constricted considering that he owns more than six times that number of shares. In fact, the speculation about the future of Continental should come to an end. Existing and prospective shareholders should feel pretty good that this cloud has blown over.

At one time it had seemed possible, perhaps even likely, that Ms. Hamm would collect up to $5 billion from her husband, perhaps crimping if not imperiling his empire. For a time, it seemed that Harold Hamm's divorce could end up being the world's most expensive at over $5 billion. But this payment seems to be a good deal. When you have the assets of Harold Hamm, you can afford to pay $1 billion to resolve a divorce case.


(AP PhotoKevin Cederstrom)

With no prenup, second wife, lawyer and economist Sue Ann Hamm could have received the biggest settlement in history. And then one has to consider taxes. The tax man gets a piece of most transactions, often on both sides of the deal. Divorce, though is tricky.

Despite the huge dollars, the IRS may not get much at first. Even on big dollars it is possible to divorce and not face major tax bills immediately. The tax problems often occur down the road, sometimes in unanticipated ways.

If you divide property between spouses during marriage (or within limits, even post-divorce), Section 1041 of the tax code says there's no tax to either party. Enacted in 1984, it reversed a Supreme Court case that ruled property divisions were taxable. Now, you can divvy up property between spouses however you want (as long as both spouses are U.S. citizens).

But don't assume "tax-free" means there are not big tax consequences. When you divide property, don't only consider the fair market value of the property. You'd better consider the tax basis of the property you divide since that controls *future* taxes.

Example: If the Hamms had divvied up shares, think about tax basis. Mr. Hamm founded Continental Resources in 1967, so his tax basis is likely tiny. If Mrs. Hamm ended up with stock and sells it, she alone is taxable on a whopping gain. If the Hamms divide cash, securities, and houses, with a mixture of high and low bases, each spouse could take some of each. That way the future tax burden will be equalized. But that's tough if most of the value is in the shares and if they are highly appreciated.

Couldn't the parties sell assets to each other as part of their divorce? Yes, but that's tricky and carries risks. Selling assets can trigger gain or loss so unequal basis problems can be avoided. But unless you do it *very* carefully the sale won't be respected for tax purposes. The IRS can disagree and try to tax the later sale too. For more, see How To Make Divorce Less Taxing.

It's worth noting that the tax-free division rule only applies to married couples. If there's no legal marriage there can be no divorce. That means there can be no tax-free division of property. When unmarried couples (same sex or otherwise) divide property it usually triggers taxes just like a sale.

Yet since the parties are just dividing assets, there's no cash to pay the taxes. That makes resolving palimony and cohabitation cases tough from a tax viewpoint. Some people in this quandary actually get married (where it's legally permitted). That way they can promptly get divorced to take advantage of the tax code's tax-free property settlement rule.

Finally, alimony is taxable to the recipient and deductible to the one paying it. Often, the IRS looks for inconsistent treatment by the parties. And there is often confusion about what is alimony and what is property settlement. You can bet that usually, the IRS makes out just fine.

You can reach me at Wood@WoodLLP.com. This discussion is not intended as legal advice, and cannot be relied upon for any purpose without the services of a qualified professional.