

## Businesses on divorce

### **How do I start the process?**

It is important to take good, specialist advice from a family lawyer and then an accountant. Think about what you want to get out of the business, both now and in the future as the financial settlement needs to be built around your objectives and your needs, in a way that is fair to both of you.

Ensure you look at your options for protecting your business if you are the business owner. If you are not the business owner, consider the best ways for you to **claim a fair share** without damaging the continuity of the business.

There are more complex and specific issues if the business concerned is a farm. Your solicitor will be able to advise on this.

### **What sort of issues may affect a family business on divorce?**

Businesses form a central part of financial proceedings and discussions on divorce and form part of the assets to be shared.

The family courts, rather than the commercial courts, deal with the business when there is a divorce. This applies whether it is a trading firm, a company or a partnership.

The courts routinely ask that businesses and business interests be valued as part of the financial disclosure exercise.

Problems can arise when an unrealistic amount of emphasis is put on the value of the business, as there is danger of when dividing up the family assets. Valuing business interests is very difficult.

### **How do courts usually approach a family business?**

The courts, if possible, will usually leave the business with the business owner and the other spouse will be compensated with a larger share of the other assets and/or maintenance. Often this is what the couple themselves want.

It is very difficult to put a value on a business and so it can often be hard to ascertain whether an agreement is fair, especially as it is difficult to know whether the business will succeed in the future.

The courts can be flexible and it is possible to share the income or to divide shares. Ideally, the courts prefer not to leave all the illiquid assets with one person and the liquid assets with the other. But in practice, they often do just that.

### **How do I deal with the business in my divorce settlement?**

Every case is different and so it is important to be clear in what approach you want to take. Therefore, it will be important to think about the following points:

- The income that the business produces

- The standard of living that the business provides – both in real terms and the income or dividend stream
- Any property/assets that the business owns and their value
- The company or business pension and what value that has, either in savings, in property or in shares
- Is it possible to extract capital sums from the business to provide money for housing?
- Is it possible to borrow against the business or its assets?
- The ownership of the business and whether this is shared. If shared, is this with family members who would act together by agreement or with people outside the family whose interests are different?

### **Does the business have to be valued?**

If the business has no underlying capital value and is merely an income stream with nothing to sell then it does not need valuing, it can be shared by way of a maintenance order.

It is usual to ask for the business to be valued if one spouse owns the business outright or has a significant shareholding in the business. Before any action is taken, this should be discussed with an experienced family lawyer first. Valuing a business is very difficult and an expert, specialist accountant is usually instructed to do this.

### **Does it matter who owns the business?**

The court is more likely to treat the business as a family asset if the business is owned outright by one spouse (or even by both spouses).

If the business is owned by several people, and the divorcing spouse has a minority shareholding, then it will be the value of the shareholding that is relevant on divorce. The court is less likely to ask for assets of the business to be sold if several people share ownership as to do so would damage the interests of people outside the marriage and that would not be fair to them.

Some businesses, even though they are companies, are treated as “quasi partnerships”. In other words, the court will assume that the owners will all act by agreement. There would not be any discount or reduction in the value of a shareholding therefore because of it being a minority shareholding.

### **Does the business have to be sold?**

It is very unusual, although possible, for the courts to order a business to be sold. It is more likely that a court will order the non business owning spouse to have more of the property or cash owned outside the business and/or order maintenance to be paid out of the income stream from the business.

Taking these discussions to court can be extremely costly and time-consuming and so it is vital to get expert legal advice from the outset to try and avoid this. During discussions the lawyers and spouses need to work out how best the benefits from the business can be shared.

### **What do I do next?**

The first step should be to take independent legal advice from a speciality family lawyer as soon as possible.

The business owner can sometimes panic and make changes to the business. If these changes are designed to be obstructive to the negotiation process, then these changes can damage your position with the proceedings. However, there may be sensible steps that can be taken to reduce the risk on divorce.

If you are the non business owner and you believe that changes are being made to cut you out or you think the borrowings are too large then you need to seek legal advice as quickly as possible. It is possible to ask a court to set aside arrangements which are designed to limit your claims.

The best outcome for everyone is to reach an agreement amicably and without unnecessary legal costs. The best way to achieve this is to seek good legal advice as early as possible so they can help you to achieve your objectives for you and your family.

Think about the questions raised in this section before you meet with a solicitor, as this is what they will be asking you when you meet.

## Claiming a fair share of the family business

### **What should I consider when preparing a claim against the family business on divorce?**

If you are not actively involved in the business, it is easy to feel powerless when divorce happens. However, with good legal advice this need not be the case. Your solicitor will help you to find out all you need to know about the business so that you are prepared for any negotiations.

You will need to consider:

- Whether you want to share the benefits that flow from the business, i.e. the income and the lifestyle in particular
- Whether you want to share ownership and decision making within the business
- Whether you would like to remain outside the business and away from the possible risk and stress

### **What should I do first?**

Firstly, it is a good idea to write down everything you know about the business – you'll probably be surprised about how much that is.

Consider the following:

- The key figures in the business, i.e. owners, influential figures, key decision makers.
- Has anything changed in the business recently, i.e. premises, structure etc.
- What was the intention behind setting up the business?
- Does the business support your current lifestyle and does this need to continue?

By looking at the above points with your solicitor you will both have a clear picture of where the wealth of the business lies and what aspects of the business are important to you.

### **What should I aim to achieve from the divorce settlements regarding the family business?**

From the outset, it is very important to consider what you want to achieve from the proceedings in regard to the business as this will affect how your solicitor will approach the case.

- Do you want an income stream and, if you do, do you want the shares themselves, which produce a dividend, or are you happy to receive maintenance? (Note that you will lose maintenance if you re-marry).
- Did you want a share of the ownership of the business and so a share of the money if it is sold in the future?
- Are you hoping to be able to pass the business on to your children? Is this feasible with your own financial needs?

### **Do I need to go to court to share the business assets?**

It may be possible to negotiate a good financial settlement without going to court; however this often depends on the attitude of your spouse and whether you think you can achieve your objectives without going to court.

### **Do I need my own accountant to help value the business?**

Often an independent joint expert will value the business on behalf of the court, but you may wish to speak to an accountant of your own. Your solicitor can advise you on the best approach to take.

Having your own accountant allows you to have someone take a look at the accounts and assess how well the business is doing and what your best options are in regard to the business.

### **When should I take legal advice?**

Not all divorce lawyers will have the specialist experience required to deal with businesses on divorce. It is important to have a family law specialist that can deal with this area of law.

Seek legal advice early on to ensure that you are giving yourself the best opportunity to achieve your objectives – as quickly and least costly as possible.

## **Protecting your business**

### **What should I do first?**

It is important to get the right legal advice as this is a highly specialised area of law.

Early on, you and your solicitor must get a firm grip on this aspect of your case. That way, you stand a better chance of directing the way the case goes, rather than merely reacting to what the court is asking or what your spouse is demanding.

### **Why do I need to protect my business?**

One of the worst things for a business is the owner getting a divorce.

The business itself comes under intense scrutiny. How much is it worth? How much income can it produce? Should it be producing more? The business may well be valued, and that process in itself involves some high stakes, since the outcome will be highly influential in court or in discussion.

Other people may have different ideas about your business that conflict with your own plans. It is often the case that judges will look at liquidity within a business and the possibility of that being paid out to meet housing or other claims of the wider family on divorce. This can be particularly problematic if that liquidity was going to be used as the “seed corn” for future business development.

### **What do I need to consider?**

It is very important that you take advice before you take actions to protect the business. If you are seen to be moving assets or shareholdings simply to avoid future claims on divorce then this will damage your case considerably. The courts also have powers to set aside transactions that are specifically designed to do this.

It is worth bearing in mind a number of broad principles:

- It will help if your business is kept entirely separate from your private assets. It will help, too, if the family home has not been used to secure borrowing within the business.
- It is sometimes tempting to involve a spouse in the business, not least for tax purposes. There is a balance to be struck; involving your spouse helps them to make a claim, by having been involved in the business and so having contributed to its success. Against that, it is a pity not to use income tax reliefs by appointing them as director, company secretary, or another role within the business.
- If an outside third party has joint ownership of the business, then this helps on divorce as the courts are unlikely to do anything that will negatively impact third parties and their livelihood not involved in the divorce. If the business is entirely owned by a spouse then the courts will treat it like any other asset and divide it equally – unless there is good reasons not to.
- A pre-nuptial agreement or post-nuptial agreement can be helpful in limiting claims against a business. It may be too late by the time you get to the divorce, for obvious reasons. But if you have planned well ahead, at the time you get married or subsequently (perhaps when inheriting a business), getting the agreement of your spouse not to make damaging claims against the business can be helpful.

### **Should I fight or should I negotiate the claims against the business on divorce?**

You need to understand what might happen if you go to court: how the process works and what it costs. You also need to think about what the outcome might be in a court and assess what you are prepared to do on a voluntary basis to avoid it. You also need to think about what you need to get out of any negotiations, i.e. do you need an income? Do you need to have full control of the business? What is the best route to achieve these objectives?

The critical thing is for the business owner to set the agenda for the discussions. Doing nothing will inevitably mean a claim is made against you and the business – and the agenda for those claims will be out of your control.

### **What should I do next?**

Whether the divorce seems a way off or the process has already started, it is important to get legal advice as soon as possible. Arrange to see a specialist family lawyer and prepare well in advance. It could help to protect your business if you understand what to do and what not to do.

## **Checklist for protecting your business on divorce**

It is important that everybody involved has a clear understanding of your business as every business is unique.

The process of financial disclosure demands very specific information to be supplied. The paperwork usually asks for the last two years' accounts and your projected income.

Here are some things for you to think about when presenting your case:

### **Who owns the business?**

It will effect how the courts treat the business if it is owned by one person as opposed to shared ownership with people outside of the family.

### **Who set up the business and when?**

Was the business set up by you before the marriage? If so then you can argue that it is a non-matrimonial asset, making it less likely to be part of the equal sharing of the assets.

If your spouse has made a contribution, then say so. Often this can be exaggerated or overemphasised by

the spouse, and it will put it more into context if you have stated it plainly – neither exaggerating it nor understating it.

### **What is the position about selling shares?**

The Memorandum and Articles of Association may place limitations on selling shares to third parties rather than to the founding members of the business.

### **What are the main financial benefits you would draw from the business?**

It makes a difference as to whether the business is capital heavy and income light (perhaps a farming business) as against capital light and income heavy (perhaps a consultancy business). The courts approach cases differently if there are assets that could be sold without damaging the business. Alternatively, the courts may think more in terms of maintenance orders if it is a professional practice or some form of income-producing business with little underlying capital.

### **What are the strengths and weaknesses of the business?**

Do a SWOT analysis – describe the strengths of the businesses, its weaknesses, the opportunities you have as a business and the threats that face your business. It helps the court to know what the underlying market conditions are, although it is unwise to exaggerate the problems too much. The court will naturally expect the blackest picture to be painted and will pay less attention if the threats are more apparent than real.

### **What are your plans for the business?**

The courts always want to know why a business is structured as it is and what plans the couple had for it during the marriage. This can be very influential.

The court may not wish to disrupt the plans that you had for the business merely because of a divorce. It helps to share with the court, therefore, what your plans are and what you are trying to achieve.

### **Is yours a “develop to sell” business?**

Some businesses develop particular projects – perhaps software – which are developed with a view to taking it to the market as soon as possible. The approach of the court may be to make orders so that such developments can be tracked, with some of the later profits being shared with your spouse.

### **Do you intend to sell your business when you retire?**

Again, you may have a longer term view before selling the business. No doubt the purchaser of the business will want you to stay in it for a while, so the divorce settlement may be structured around that. Alternatively, it may be too long to wait, or it may be unfair to allow any ex-spouse to benefit from many years of post-divorce business development.

### **Is the business going to be passed to the next generation?**

Again, if it is agreed that the business is going to be passed to the children in due course, then a very different approach may be adopted both by the courts and by your spouse.

## **Farms on divorce**

## **What makes farming divorces different?**

Farm businesses are usually more difficult to deal with but otherwise they are no different to any other business. They can be a little more complicated because:

- Many members of a family can share ownership so extracting capital can be difficult.
- The ownership is often complicated by farming tenancies, corporate ownership and/or trust ownership
- The value of the land and property can often be substantial compared to the income of the business.
- The lifestyle that the farm gives its owners is often the major benefit of the business
- Farms are often inherited, making them non-matrimonial assets that will not be subject to the sharing principle (i.e. will not usually be divided equally)
- There is often a lack of liquidity, so raising cash to buy alternative houses can be difficult

## **What should I do first?**

Firstly, it is important to gather all the information you have about the farm, including a map, details of who owns the plot and information of any mortgages. If you have valuations already include those. Otherwise, do not get a valuation done at this point. Give an estimate as to what the land and the properties might be worth.

## **Do I need a divorce lawyer in connection with the farm?**

It is very important to get the correct legal advice as farms are specialised businesses. It is cheaper to reach an agreement before going through the courts however with a farm involved this negotiation needs greater experience and skill.

## **How does the court approach farming divorces?**

If a farm has been inherited, it will usually firstly be a question of trying to raise capital to meet the housing needs of both spouses. For example, if a farmer has inherited a farm from his family, the basic requirement when divorcing is to supply his wife with a suitable home for herself and possibly the children. It may be necessary to sell off part of the farm in order to do this, or to borrow against it. But that may damage the core activity of the farm and a court might be reluctant to do that.

Courts are reluctant to damage the livelihoods of other third parties and so if the farm is owned through the wider family, then this will need very careful thought.

With farms it can be difficult when paying maintenance out of the farm income. The lifestyle sustained by a farm may seem higher than the income it actually produces. When that income is shared, there may be a dramatic fall in the standard of living of the person receiving the maintenance.

## **Will the farm have to be sold on divorce?**

It is usually a question of raising capital for housing purposes, perhaps by selling off a part of the farm, maybe some outbuildings, or by borrowing against the property. It is uncommon for a court to order that an entire farm has to be sold.

Occasionally, the court does order a farm to be sold, particularly if it is not viable as a business. The farmer is therefore caught between two difficult lines of fire – he does not want to exaggerate the value of the business and its income stream, while on the other hand he does not want to play down its viability to such an extent that the court thinks there is no point in continuing it.

### **Will the farm have to be valued?**

It is usual in farming cases to have the farm valued, however it may be that if there are other valuations prepared in the recent past then they will suffice. A new valuation will normally be prepared by a single joint expert.

It is advisable to deal with this evaluation through lawyers to ensure the scope and detail is correct. This avoids having to potentially have another valuation done at further expense.

### **What about if the farm is owned in trust?**

This depends on the type of trust involved.

The courts will generally respect “a dynastic trust”. However, if the trust is “nuptial” (i.e. it relates to the specific marriage) then the court has the right to vary the trust – and its powers are very wide; it can sack the trustees and put in new trustees, sell assets and make whatever distributions it thinks are appropriate.

It is less easy for the courts to deal directly with trusts if they are on a discretionary basis. This does not mean that the courts will ignore them. They will be treated as a “financial resource” and the court will look at the history of distributions – of capital and of income. The courts can make orders which assume that the beneficiary will continue to get those benefits in the future.

### **What should I consider next?**

After gathering together all the information you have on the farm, you need to contact a specialist divorce lawyer for advice. A commercial lawyer or a farming lawyer are not going to give you the advice you need. Ensure that your solicitor has experience in dealing with farming divorces.

For a fixed fee it is possible to have a one-off meeting. This will allow you to take advice but stay in control while you assess your best route forward. You need to be clear what you want from the meeting.