



/guide



Your questions answered

WHAT HAPPENS TO A BUSINESS DURING DIVORCE?

This purpose of this Stowe guide is to give a simple overview of how ownership of a business affects divorce.

Is a business considered marital property?

Yes. It's a common misconception that the Courts will disregard business interests when considering a financial settlement. Like property, shares, savings and pensions, business assets are included in the matrimonial pot and subject to being divided on divorce, irrespective of which party founded or runs the business.

Whilst the Courts prefer not to interfere with the smooth running of a business or change its ownership, the business will be considered during proceedings both in terms of its overall value and the income that it produces.

While each case is different, it is necessary to establish some key facts:

- How the business is owned and by whom
- The nature of the business
- What it is worth and what is the most appropriate method of calculating that sum
- What income it has historically provided and what can it provide in the future
- Whether there are any surplus funds in the business which could be extracted to meet either party's claim and if so, what is the most tax efficient way of doing so?

How the business is owned

The most common types of business are:

Sole trader

A single person owns, operates, and controls the business for their personal benefit, frequently using a distinct trading name. Staff may be employed. All assets are personally owned, and all liabilities are personal. The business is liable to pay tax and national insurance.

Partnerships

A partnership involves two or more individuals who agree to share in the profits or losses of the business as well as having joint responsibility for the risks, costs, benefits, and obligations of running it. Each partner pays tax and national insurance on their share of the profits.

Partnerships can be either unincorporated entities, meaning that partners are personally responsible for the losses or debts that the business undertakes, or incorporated e.g. a Limited Liability Partnership (LLP), meaning that the partner's liability is limited to the amount of money they invest in the business.

Limited company

A limited company is operated by its' directors on behalf of the shareholders and is a wholly separate legal entity with its' own legal rights and obligations. This means the company is responsible for everything it does, and its finances are totally separate to the personal affairs of its owner(s).

How is a business valued during divorce?

Business owners must provide an estimate of the business value, supported by company accounts. There is no 'one size fits all' approach to company valuation. A range of factors are used to calculate business value, most commonly including:

- Total business assets
- Annual turnover and profits for previous years
- Expected profits
- Business debts

How different business structures are most often valued

The valuation approach is different for each of the three main business structures.

Sole trader / limited company through which the proprietor's services are sold

Typically, there is unlikely to be any premium receivable on sale of these types of businesses to a third party as without the proprietor there would simply be no business to sell. In other words, there is no goodwill to consider on sale as the business operates solely to provide an income stream and the overall value is determined by the value of its' net assets at any given date.

Property or investment-based business

Businesses of this nature are operated predominantly to take advantage of capital growth of the assets owned, rather than as an income stream to the owners. The value therefore lies in assets less liabilities, in other words the business 'break up' value.

For any business, a valuation on this basis will represent the minimum sum.

Trading business

Typically, businesses that sell goods and are trading in nature are valued by reference to profits and establishing their value can be complex.

Adjustments are often made for factors such as debt, surplus assets, or minority shareholder discount, dependent on individual circumstances. A valuation will also be considered on an asset basis (as referred to above) and the greater figure will generally be adopted as the value of the business.

The calculations used to reach maintainable earnings will also be relevant for consideration of the income that the business can provide to its directors/ shareholders and are consequently also relevant for consideration of spousal and child maintenance.

Capital Gains Tax

The potential incidence of Capital Gains Tax should always be considered in calculation of the (net of CGT) value of the parties' interests in a business.

What if there's a disagreement over the value of a business?

A Court will often direct that an independent expert, such as a qualified accountant often known as a Single Joint Expert ('SJE'), be instructed jointly by both parties. The SJE will establish overall business value and the income it can provide, assisting the Court to determine the extent to which it can be included in the financial settlement.

The extent of work an independent SJE can do to assess the value of a business may be limited which is why we have an in-house specialist forensic accountant at Stowe Family Law.

What happens when both spouses own shares?

The Courts prefer to achieve full separation in terms of ownership of business interests. In cases where both parties own shares but only one party actively runs the business a possible outcome is a share transfer, whereby ownership of shares moves from one party to the other.

Business ownership and divorce proceedings

The value of a business and the income it produces can be a contentious issue during divorce proceedings.

However, there is nothing to be gained from falsely trying to argue that a business has a lower value. Manipulation or misrepresentation of figures is a false economy and is often exposed, potentially leading to consequences such as reopening of the proceedings.

Need more information?

Call our Client Care Team on **0330 838 7456** to speak with one of our specialist family lawyers or visit www.stowefamilylaw.co.uk



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