

## **USING BUSINESS VALUATION EXPERTS TO YOUR BEST ADVANTAGE IN DIVORCE**

In 2010 we saw a number of high profile celebrity divorces and break ups occupying the tabloids and evening news. Tiger Woods and Elin Nordegren's divorce was just the beginning. As the year closed we saw Sandra Bullock's marriage crash and burn. Even Hollywood's starlets like Elizabeth Hurley, Eva Longoria and Scarlett Johansson couldn't avoid the hazards of matrimonial failure. In some instances these divorces may have ended inauspiciously due to a prenuptial agreement or the ability of the parties to cut ties financially without disrupting their lifestyle.

For attorneys representing clients in a divorce the breakdown of this economic partnership may require a forensic accountant and business valuation expert. But how does the matrimonial practitioner use this resource to better serve their client? Here are four things to consider, along with cases that illustrate the issues.

### ***Always Use a Qualified Business Valuation Expert.***

In *Brooks v. Brooks*, the husband owned minority interests in his family's limited liability companies (LLCs), which held commercial property. At trial, the wife presented the companies' financial statements and a real estate expert, who appraised the LLC's underlying property at \$61 million. Notably, the expert testified that his appraisal was only the first step in a fair market valuation (FMV), which required assessing the companies' outstanding debt and closely held stock.

At the close of the wife's case, the husband decided *not* to call his BV expert, saying there was "no valuation testimony" to rebut. Instead, he presented only the

operative buy-sell agreements plus his tax returns, which essentially showed a book value of \$400,000 for his LLC interests.

The court asked the wife if she wanted to call the husband's expert to testify regarding the LLCs, including the effect of non-marketability and minority shares, but she declined. Thus the court was faced with the buy-sell and book values, on one side, and the broad real estate appraisals and financials on the other.

Finding the former "simply would not do justice," the court took the appraised value of each property and multiplied it by the husband's share in the LLC, less the mortgage debt on each property plus the value of cash-on-hand.

The husband appealed, claiming the trial court improperly equated the FMV of the properties with that of his LLC interests, thereby ignoring three "critical" features: lack of marketability, lack of control, and the effect of the restrictive buy-sells. The wife argued that since he'd neglected to present valuation evidence at trial, he couldn't complain about its omission—but the appellate court disagreed.

The husband had "vigorously objected" to the wife's real estate appraisals at trial, and her own expert conceded a lack of expertise to value the husband's interests. The wife also rejected the chance to call the husband's BV expert. At the same time, the trial court failed "to follow some reasonable path" in ascertaining FMV, which required assessing the marketability and minority aspects of the husband's interests as well as any contractual restrictions, and the appellate court remanded the case for a new trial on valuation.

### ***Use Your Expert to Facilitate Proper Discovery and Disclosure.***

In *Hissa v. Hissa*, the husband's expert valued his orthopedic practice at approximately \$320,000. By contrast, the wife's expert valued it at \$650,000, based in part on a comparison to industry averages. Both experts relied on the applicable FMV standard, and both agreed that accounts receivable (AR) were an important element. However, the husband failed to provide the wife's expert with the same information concerning AR that he'd given his own expert, forcing the wife's expert to estimate their value. The husband also provided flawed tax and financial information to *both* experts, and as a result, the trial court found his evidence *less* convincing than the wife's, and adopted her expert's value.

The husband appealed, alleging the trial court erred by crediting the wife's expert over his own. But, "the [trial] court determined that [the husband's] failure to be forthcoming about his business expenses led it to discredit the information he provided his own expert," the appellate court found, "particularly given his expert's valuation of the medical practice at nearly one-half of what [the wife's expert] determined the value to be," and it affirmed the latter's value.

### ***Use the Expert to Educate the Court.***

In *re Marriage of Armour*, the vast majority of the parties' wealth was tied up in the husband's 50,000 shares of stock in his employer, which were subject to the company's right of redemption at a below market price. Like many jurisdictions,

California family courts prefer an in-kind division of marital assets unless economic circumstances warrant another method.

Here, the wife's valuation expert analyzed the consequences of an in-kind division: Assuming the husband retained his stock for a reasonable time until retirement, his 50% share would produce a present value of \$36 to \$40 million, but the wife's share would net only \$18 million at the forced redemption price.

Despite this evidence, the trial court ordered a simple in-kind division and the wife appealed. Based on the wife's valuation evidence, the appellate court found this "disregarded economic realities" and ordered a division that ensured an equal result for both parties.

***Use Your Expert to Rebut the Other Side.***

In *Gupta v. Gupta*, the husband owned three medical practices and an imaging center in rural Texas. At trial, his expert valued the practices at \$359,000 and the imaging center at zero, due to its significant debt service and operating losses. By contrast, the wife's expert valued all the businesses at \$780,000, excluding goodwill and a marketability discount.

In addition, the wife's expert submitted a separate report to rebut the husband's expert, highlighting his errors regarding valuation of revenue, AR, equipment, depreciation, and his misuse of historical financial statements. As a result, the trial court accepted the wife's expert value, and the husband appealed, claiming the wife's expert failed to visit the practices, interview his staff, or view the equipment. She also

misclassified his practice, comparing it to “specialty medical practices” rather than a “general physician office,” and failed to factor the debts and losses of the imaging center. His rebuttal was too late, however, and the appellate court upheld the wife’s expert evidence in full.

## **Conclusion**

The valuation of a business is often a difficult issue; but it is crucial for attorneys to understand the role of the business valuation expert in marital dissolution so that they can effectively counsel their clients in achieving their goals in asset distribution and financial support. To learn more how our business valuation and forensic accounting team can assist you please call our offices at 516-829-4936 (New York), 203-357-1500 (Connecticut), 973-226-4500 (New Jersey) or visit our website at [www.msgcpa.com](http://www.msgcpa.com).