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Pre-marital calculation? It's a question of time

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Adele Pledger
SENIOR ASSOCIATE | UK

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BLOG

So, you have owned a business for a few years…you get married…your business grows and prospers…sadly the marriage breaks down and you are getting divorced.

Arguably, the pre-marital element of the business is non-matrimonial and not available for 'sharing' (unless required to meet your ex-spouse's 'needs').

But how do you value that pre-marital element?

In Jones v Jones [2011] EWCA Civ 41 the Court of Appeal adopted the following calculation: take the value of the business at the date of the marriage (in that case, £2million), adjust that to reflect (1) the latent potential, or 'springboard' effect (which the Court used to arbitrarily increase the value at the date of the marriage to £4million); and (2) passive economic growth throughout the marriage (the Court used what they considered was the most appropriate index in that case to inflate the non-matrimonial element from £4million to £9million).

More recently, Mr Justice Mostyn adopted a different approach in the case of WM v HM [2017] EWFC 25 which, he says, "more fairly and realistically reflects the true potential of [the] company at the start of the marriage". Mr Justice Mostyn considered the exercise of finding a fair figure for the historic value of an asset to be an 'evaluation' rather than an exercise of 'discretion'.

Mr Justice Mostyn considered the following two time based retrospective analyses, working backwards from the current value of the business:

(1) A linear time apportionment, which assumes that the value of the business increased in equal proportions over the course of its existence. You can plot on a graph a straight line from £0 at the business' inception, through to the current value today, and then you work out the value as at the date of the marriage (or arguably the date of cohabitation if seamless into marriage) by assessing the proportion of the business' life that had passed at the ate of the marriage. Essentially, if you have for example a 40 year old business, and a 30 year marriage, 10 years (so 25%) of the business is 'pre-marital', and so if the business is worth £10million at the date of the divorce, under this methodology £2.5million would be pre-marital.

(2) Apply a discount rate at the 'natural value of money' (which Mostyn J took as 5% following Locke's theory in 1722) back from the current value to the date of the marriage. This assumes a notional value at the inception of the business, and results in a curved graph (see the orange line on the graph below*).

Mr Justice Mostyn considered the linear approach to be most fair, and that is the valuation technique he adopted in WM v HM (although as you will see from the graph below it did not make a great deal of different on the figures involved in WM v HM due to the timing of the marriage).

In any event, both the linear apportionment and discounting methods will no doubt be argued in future cases, and are particularly useful when it is very difficult, if not impossible, to work out the actual historic valuation of the business at the date of the marriage (as occurred in Jones v Jones).

Authors

Adele Pledger

SENIOR ASSOCIATE | LONDON

Divorce and family

+44 20 7597 6447

adele.pledger@withersworldwide.com