COMPANY VALUATIONS
Diving into the unknown

HANDOUT
Talk for White Paper
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1 Hare Court

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Introduction

1. The presence of a company within our financial remedy cases is becoming almost standard fare. Many more people develop products or provide services through them than they did in the past, and sometimes with considerable success resulting in great wealth.

2. Keeping or receiving a fair share of the value generated within such a company is now a central issue for us and it can be broken down into two broad categories. Those cases where:
   a. the business was started during a marriage, and where the value has accrued during that time (i.e. where it is all matrimonial); and
   b. those cases, which are much harder, where one party brought the business to the marriage, so only an element is matrimonial.

3. But once one has arrived at a value how is that divided between the spouses? Should cash be paid out to the departing spouse or should they get shares or a bit of both? Should the company be sold?

4. These are all very difficult questions to answer and there are few general rules. It will depend on the specific facts of each case and which judge you get.

5. In short, this is one of the hardest areas in which to advise within financial remedy work.

How to approach valuation

6. But first, let's take a step back and look quickly at the process of obtaining a valuation of a company.

7. The received wisdom is that one must have a single joint expert (an SJE). But that is an over-simplification of the rules.

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8. FPR 25.11 supplies the court's power to direct that evidence is to be given by an SJE and PD 25D para 2.1 stipulates that **wherever possible** expert evidence should be obtained from an SJE instructed by both parties.

9. But in *JG v The Lord Chancellor & Ors* [2014] 2 FLR 1218 Black LJ held that the power in rule 25.11(1) does not extend to forcing a party who was not seeking to instruct an expert himself to join in the instruction of an expert which another party has invited the court to approve. If one party does not seek expert evidence on a particular matter then he cannot be forced to join in the instruction of an SJE on that matter.

10. But assuming one does join in with the other side and seek a SJE valuation there is then the possibility of seeking a further report from your own expert if you are dissatisfied with the SJE's valuation pursuant to the case of *Daniels v Walker*.

11. Often, neither party likes it and both seek permission for a report from their own expert.

12. Some judges in the High Court anticipate this and will in certain cases permit sole experts from the start. In short, it reduces the number of experts from 3 to 2, saves costs and quickens the whole process.

Approximate value

13. We must not forget that the court is only looking for approximate value, when it comes to businesses. Why? Because it is an art and not a science. In short, it is never possible, or very rarely indeed, to come up with a definitive value as what the expert is being asked is to guess what someone would pay for it.

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14. Moylan J (as he was then) said in *H v H* [2008] EWHC 935 (Fam) at para. 104 the following:

> 104. … I have already made plain during this judgment my objection to treating the valuation exercise as though it is an exact science which, to adopt again the words of Lord Nicholls, justifies a thorough investigation when such an investigation is not only extremely expensive but also of doubtful utility.

15. Moylan LJ makes the same point towards the end of the case of *Hart v Hart*. And, as we will see, Mostyn J largely agrees.

16. It is against this backdrop that we must operate.

How to approach valuation of a company generated during the marriage?

17. Going back to my two types of cases above (valuations of business generated during the marriage and those brought to a marriage), the former is more straightforward but the latter is rather more complex.

How to approach valuation of a company brought to the marriage?

18. The issue of how to deal with the valuation of the company brought to the marriage is much more difficult.

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19. Essentially, until recently (and for many judges it still will be) the holy grail has been working out:
A: the value of the company now
B: the value of the company at the date of the marriage / cohabitation
and performing the following calculation:

A-B/2 = result

20. Although that appears to be simple, in practice it is highly complex, can lead to unfair outcomes.

21. The real issue is how you value, or evaluated, "B": i.e. the value of the company when it was brought to the marriage.

22. You may remember that Wilson J struggled with this in the case of *Jones v Jones* and came up with a methodology involving "springboards", indexation as well as passive and active growth.

***WM v HM* (Mostyn J) – May 2017**

23. Mostyn J dealt with this issue in his case of *WM v HM*. Following the 29 year partnership / marriage, Mostyn J was asked to determine whether there should be a departure from equality on grounds of what H said were:
a. the pre-marital assets: "great value" he had brought into the relationship in 1986; and
b. special contribution: made by H which were said to outweigh those made by W.

24. In order to make things simpler and fairer (in that case) Mostyn J developed a linear approach to historic valuation of a business. He also, on the facts of that case, rejected special contribution.

25. Let's look at what Mostyn says on the valuation issues.

Computation

26. H started the business X Group plc in 1978 and it had "gone from strength to strength". It was valued at the final hearing by Mostyn J at £221m on the basis of what a "notional or hypothetical purchaser" would pay. That is "A" in the formula.

What was the value of the business at the date of the marriage/cohabitation?

27. However, in accordance with his previous long line of cases (e.g. *N v F*) it was necessary to determine the value of the business at the date the parties commenced cohabitation in April 1986. This is "B" in the formula.

"The Scottish Case"

28. In *WM v HM* Mostyn J set out that he had recently considered "the same issue" in a judgment "incapable of camouflage" simply cited as “The Scottish Case”; a case in which I acted for the wife.

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29. At para. 11 of *WM v HM* Mostyn J quoted passages of that judgment firstly on the application of the 'sharing' principle’ and secondly on the ‘approach to an historic valuation of a business’.

The sharing principle

"38. I am firmly of the view that the correct approach to give effect to the sharing principle is to try to calculate the scale of the matrimonial property and then normally to share that equally leaving the non-matrimonial property untouched. This is logically pure, morally sound, easy to understand, and limits individual judicial caprice."…

"I continue to oppose the school of thought that plucks a random percentage out of the air where the pool of assets is a mixture of matrimonial and non-matrimonial property".

Approach to historical valuation of a business

30. Mostyn J agreed with what Moylan J said in *SK v WL* [2010] EWHC 3768 (Fam) that the use of hindsight in an historic valuation was "not merely legitimate" but also "realistic and right".

31. He said that the approach in *Jones v Jones* [2011] EWCA Civ 41 provided a valuable guideline, but it did not supply a tramline (i.e. a predetermined destination). The exercise of "finding a fair figure for the historic value of an asset" was not one of "discretion" but was "an evaluation" (see para. 12 of *WM v HM*).

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32. In *WM v HM* Mostyn J said:

17. In this case the SJE has valued the company in July 1986 as between £188,000 and £414,000. His approach eschewed any hint of retrospective analysis. He identified (in May 2016, when he wrote his main report) a 540% increase in the FTSE All-Share Sector relevant to this business. That would be about 700% now.

Thus, using a strict *Jones* technique he would give a non-matrimonial value of the company of £1.5m - £3.3m.

18. **I do not consider that this low bracket begins to reflect fairly the true present value of what the husband brought into the marriage through XG.**

A linear time [straight-line method] apportionment would suggest that just over 20% (20.12% to be exact) of the present value had been accumulated at the time of the marriage. In numeric terms this is £44.5m.

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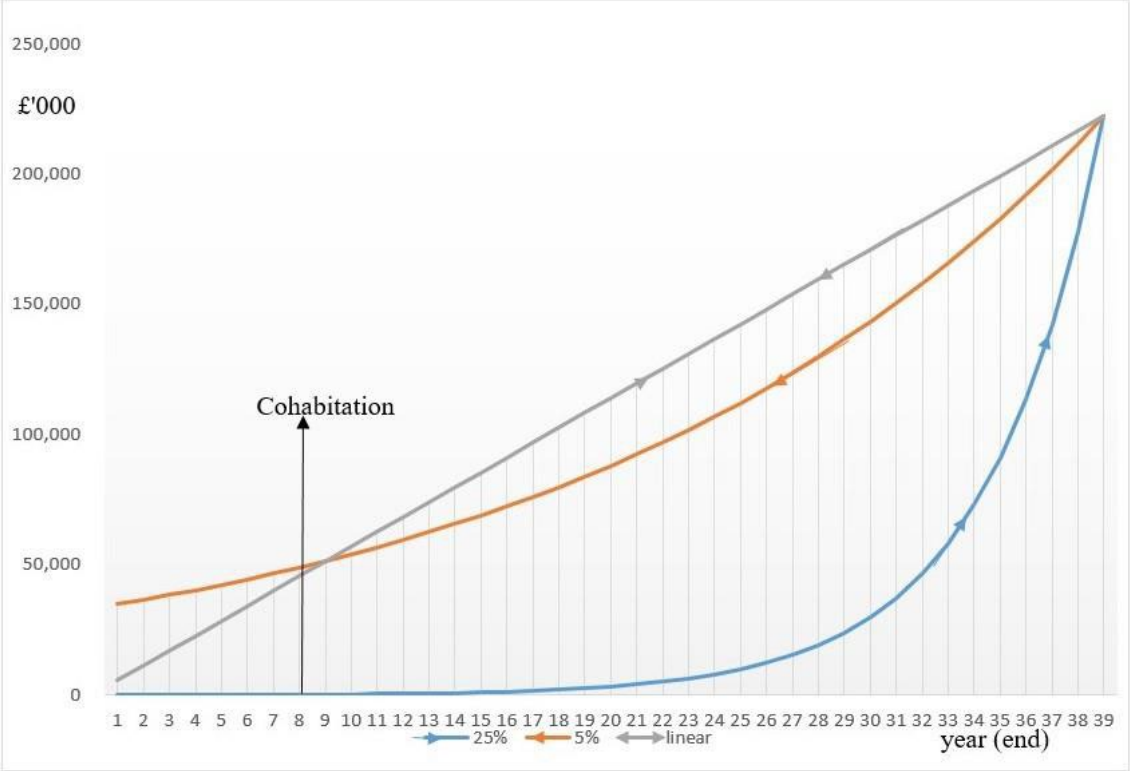
33. The graph.



The straight-line method is not the only way of looking at the matter. **An alternative is to take a discount rate of say 5% and work backwards from the current value.** 5% has long been thought to be the "natural value of money". Locke thought so in 1722 when writing about interest on an unsecured debt. Using this technique, £221m in year 39 shrinks to £49m in year 8. **This approach would suggest that the business had a notional present day value of £33m** at the end of the first year, which may be another way of expressing the idea, used by the House of Lords in *Miller v Miller* [2006] UKHL 24, [2006] 2 AC 618 of attributing a sizeable value to a good idea at the very start. The objection of the wife's legal team is to echo Lady Justice Arden. It does not reflect reality, they say. They have produced a graph which plots in separate lines the increase in turnover and post-tax profit. For each line the business had barely got off the ground in 1985. It made a loss in that year on a turnover of £2m. Compare that, they say, to turnover of £63m and profit of £13.4m in 2015. Their lines have an exponential shape. If one were to start with say £46,000 of value and to increase that every year by 25% you would end up with £221m. The graph would look the same as Mr Pointer's….

34. Mostyn said at para. 16 of *WM v HM* that the "artificial assumption of a straight-line growth up to eventual sale provide[s] a useful basis for analysing the issue which if commonly adopted would have the beneficial side effect of eliminating arid, abstruse and expensive black-letter accountancy valuations of a company many years earlier at the start of the marriage".

35. Mostyn goes on to justify his straight line approach in *WM v HM* by saying that "it much more fairly and realistically reflects the true potential of this company at the start of the marriage". The matrimonial element of XG was therefore c.£176.6m and the non-matrimonial element c.£44.5m.

***Hart v Hart*: the retreat from scientific approach**

36. But no sooner than Mostyn had handed down his Judgment in *WM v HM*, Moylan LJ decided the case of *Hart v Hart* in which we see a retreat from this scientific approach.

37. The facts of that case are not relevant. The judge at first instance, HHJ Wildblood QC, tried to adhere to the Mostynian formulaic approach (in line with his long line of cases) to arrive at a value of the matrimonial assets. The wife in *Hart* did not like his decision and appealed.

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38. What was this case about? See para. 1 of *Hart*:

> 1. This case concerns the approach which the court should take to non-matrimonial property when determining a financial remedy claim by application of the sharing principle. I emphasise that, what I say in this judgment, is confined to this principle. It raises both evidential and legal issues. How is such property to be assessed? What degree of assessment is required? Is the approach formulaic or does the court have a broader discretion?

39. On appeal, Moylan LJ said at para. 14:

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> 14. The central factual issue considered by the judge was the relevance of the husband's pre-marital wealth to the determination of the wife's claim. In considering this issue it is clear that, although **the judge** referred to every case as being different and as being decided on its own facts, he **felt constrained, as he said at the outset of his judgment, to seek to apply the "formulaic approach" taken in *Jones v Jones*** [2011] 1 FLR 1723. This led him into a long exploration of the extent of the husband's pre-marital wealth and its value; the manner in which this wealth had developed during the marriage; and the extent to which there had been "mingling". He did this because he wanted, if possible, to obtain a "baseline figure" to use for the purposes of a mathematical calculation as had occurred in *Jones*…

40. But Wildblood made it very clear in his judgment that it was not possible for him to carry out the "formulaic approach with any degree of precision".

41. This was because there was no reliable evidence of the husband's worth when the parties cohabited and any attempt at quantifying it was guesswork. There had also been extensive mingling since.

42. On the appeal, counsel for Mrs Hart referred to the "two-step approach" set out by Mostyn J in *N v F* as being the right one, namely to "identify the scale of the non-matrimonial property to be excluded, leaving the matrimonial property alone to be divided in accordance with the equal sharing principle".

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43. At paragraph 68 Moylan LJ said:

68. Put in simple terms, the court ultimately has to decide, as part of the discretionary exercise, how to weigh or reflect the existence of non-matrimonial property when determining the award. **A key question** which has emerged, and which is engaged in the current case, **is whether this [*how to take into account non-matrimonial property*] should be undertaken in a formulaic manner or whether the court can adopt a broader approach**.

Moylan v Mostyn

44. Therefore, who was right? Mostyn or Moylan? Moylan goes on to say:

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84. **In my view, the court is not *required* to adopt a formulaic approach either when determining whether the parties' wealth comprises both matrimonial and non-matrimonial property or when the court is deciding what award to make.** This is not necessary in order to achieve "an acceptable degree of consistency", Lord Nicholls in *Miller* (paragraph 6), or to achieve a fair outcome. Indeed, I consider that the present case demonstrates the difficulties which can arise if a court strives to adopt a formulaic approach in circumstances where that is not likely to be easily achieved because of the nature of the financial history.

45. Moylan goes on to say this about Mostyn J:

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87. **In addition, with due respect to Mostyn J's extensive experience in this field, I am not sure there are different schools. In my view, the differences which he identifies are examples of the same principle being applied, but applied in a different manner depending on the circumstances of the case.** One application may be more specific than the other but this will typically reflect the "degree of particularity or generality appropriate in the case": *Miller* (paragraph 27). **The outcome will be the same, namely**, when justified, **an unequal division of the parties' property.**

46. Moylan LJ goes on to say:

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96. … **In arriving at this determination, the court does not have to apply any particular mathematical or other specific methodology. The court has a discretion as to how to arrive at a fair division and can simply apply a broad assessment of the division which would affect "overall fairness".** This accords with what Lord Nicholls said in *Miller* and, in my view, with the decision in *Jones*.

47. So, for Moylan, it was an art not a science and discretion, not precision, dominates.

48. Therefore, at this point we had a real difference of approach between Mostyn and Moylan. But Moylan was in the Court of Appeal and he ended his judgment with the following:

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97. Finally, I would repeat that **fairness has a broad horizon**. **I recognise, of course, the need for clear guidance and principles** when the court is given a discretion as wide as that contained in section 25 of the 1973 Act. Such clarity not only assists judges when determining financial claims but also enables those seeking to resolve the consequences of their separation and divorce, as it has been described, "to bargain in the shadow of the law": *Matrimonial Property, Needs and Agreements* 2014 (Law Com No 343) paragraph 3.6. **However, this should not lead to the imposition of constraints which are not needed to achieve, and which deprive the court of the flexibility required to achieve, a fair outcome.**

49. *WM v HM* was appealed and was reported as *Martin v Martin* [2019] 2 FLR 291.

50. In short, Moylan agreed with Mostyn about his approach to valuation. From para. 2 of the head note:

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(2) **The judge had been entitled to adopt a straight-line apportionment approach when determining what part of the current value of the company had to be characterised as non-marital property. Whether property was matrimonial or not had to be determined in a partly evaluative and partly discretionary manner.** The judge had clearly expressed his reasons for using the straight-line approach in his judgment. The approach had resonated with fairness, as it had taken an overarching review of the weight to be attributed to the husband's contributions to the business throughout its existence. **The exercise on which the court was engaged was not restricted to a single route to determining how the wealth was to be characterised for the purposes of the application of the sharing principle. The judge had not relied on the 1986 valuation given by the expert or the turnover/profit graph produced by the wife, because those approaches had not provided a fair assessment of the part of the current value of the company which had to be characterised as non-marital**….

A retreat from broad discretion?

51. But has there been a retreat from this very broad and undiscernible discretion?

52. To some degree, yes. Moylan has had to row back from his ultra-discretion approach in *Hart* to a more principled one as set out in the recent case of *XW v XH* [2019] EWCA Civ 2262.

XW v XH

53. This was heard by Baker J (as he was then) at the end of 2017. It was appealed to the Court of Appeal who handed down Judgment just before last Christmas (2019).

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54. The facts of this case can be stated in short form:
    a. The parties were c.50;
    b. 7 year marriage;
    c. A young child who has special needs, looked after mainly by W;
    d. W had access to trust assets of her own;
    e. The total assets were c.£530m;

f. H was the CEO of a company set up some years before the marriage; and
g. That company was sold in 2015/16 generating £370m which, by the time of the hearing (at first instance) had grown to almost £500m.

55. The main issue was, yet again, the value of the business at the time H brought it to the marriage and what, therefore, comprised non-matrimonial property that should not be shared. But, more importantly, it was about "latent value" or "springboard": i.e. value that existed within the business at the time of the marriage but which cannot easily be discerned from the company accounts at that time.

56. However, the SJE accountant in *XW v XH* did not apply any "springboard".

57. Barker J decided that:

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> [237] … **the fair outcome is one that departs from the sharing principle and leaves the husband with a significantly greater proportion of the assets.** I reach that conclusion for the following reasons.
>
> [238] First, the parties have to a very substantial extent **kept their financial affairs completely separate** during the marriage…
>
> [239] Secondly, **the assets which grew so substantially in value during the latter years of the marriage were the husband's business assets.** The case-law remains unclear as to whether such assets should be regarded as matrimonial or non-matrimonial. In the sense that the growth in value occurred during the marriage, they could be said to be matrimonial. On the other hand, the assets remained at all times in the hands of the husband. They were never pooled. In that sense, they can properly be described as non-matrimonial. Ultimately, the label does not matter. What is relevant, in my judgment, is that they were the husband's business assets…

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> [240] Thirdly, **I am satisfied that there was a latent potential in the company not reflected in the conventional valuation conducted by Mr Kay. The ultimate phenomenal success of the company was due in part to developments and decisions taken in the business during the marriage, but it was also attributable to developments and decisions taken before the marriage** – the creation of the company, the putting together of the team, the earlier activities of the company in its field, including the original product models, and the development of a marketing strategy. To a not inconsiderable extent, the later success was built on those earlier foundations. Mr Kay thought that this was not a significant factor in determining the value of the company at the date of the marriage because the subsequent growth in the business did not occur for several years after the marriage. In my judgment, however, the latent potential was there at all material times – it just remained latent for rather longer until the opportunities for growth arose.

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[241] How should this latent potential be taken into account? To my mind, with great respect to both Holman J and Mostyn J, I consider that neither the approach in *Robertson v Robertson* [2016] EWHC 613 (Fam), [2017] 1 FLR 1174 (treating 50% of the value of the business at the date of sale as having been created prior to the marriage) nor the approach in *WM v HM (Financial Remedies: Sharing Principle: Special Contribution)* [2017] EWFC 25, [2018] 1 FLR 313 (excluding the proportion of value in the business that was created before the marriage on a linear apportionment basis) is appropriate in this case. As Arden LJ noted in *Jones v Jones* [2011] EWCA Civ 41, [2012] Fam 1, [2011] 3 WLR 582, [2011] 1 FLR 1723, the court must try to look as far as it can at the reality of what actually happened rather than proceed on an artificial assumption of a straight-line growth from the date of foundation of the business up to the eventual sale. To insist on a linear or arithmetical approach would be to fall into the error identified by Moylan LJ in *Hart v Hart* [2017] EWCA Civ 1306, [2018] 2 WLR 509, [2018] 1 FLR 1283 of imposing 'constraints which are not needed to achieve, and which deprive the court of the flexibility required to achieve, a fair outcome.' **In this case, adopting Moylan LJ's approach, I conclude that the evidence does not establish a clear dividing line between matrimonial and non-matrimonial property and it is neither proportionate nor feasible to seek to determine a clear line. Instead, I propose to undertake a broad evidential assessment before deciding how the wealth should be divided. My assessment is that there was a significant, though unquantifiable, latent potential in the company at the date of the marriage which is not reflected in the formal valuation. The fact that there was such a latent potential in the company must therefore be taken into account when determining the extent to which there should be a departure from the sharing principle.**

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[242] Fourthly, and finally**, I am satisfied in this case that the husband's contribution to the growth in the value of the business assets during the marriage comes within the concept of special contribution**….

…

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[245] In all the circumstances, I have concluded that a fair outcome would be to award the wife a lump sum equivalent to 25% of the difference between the husband's share of the proceeds of sale of the company in 2016 and the value of the husband's shares at the date of the marriage as assessed by Mr Kay, but increased to take account of passive growth applying the MSCI World Technology share index as proposed on behalf of the wife.

58. Therefore, W got £152m (including her own assets) and H £378m.

The Court of Appeal decision in *XW v XH*

59. At paragraphs 82-90 Moylan LJ sets out the legal context and the tension between necessary discretion and a principled and discernible pathway to the outcome.

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60. In his first retreat from his position in *Hart*, Moylan says:

> 86. in respect of financial remedy cases, the need for the judgment to explain with sufficient clarity how the award has been calculated. Without this, there would clearly be scope for a party to argue that the judgment is not sufficiently reasoned. As I have said very recently, and since the hearing of this appeal: "Every financial remedy judgment should clearly set out how the award has been calculated", *Moher v Moher* [2019] EWCA Civ 1482, at [114(ii)].

Latent value

61. How did Moylan deal with the issue of latent value: i.e. the value of the business at the date of the marriage, He said this:

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> 114. **What is being undertaken is a *retrospective* analysis to determine, by making (to repeat) "fair overall allowance" or by giving the weight the court considers just, what part of the *current* value of the asset should be treated as marital property for the purposes of the application of the sharing principle.** This is not to attribute value to what Wilson LJ called "the subsequent activity of the diver or gymnast" (*Jones*, at [42]) because that is the product of marital endeavour. However, **because the analysis is undertaken with the benefit of hindsight, a court is not bound to adopt the mathematical route adopted in *Jones* based on a prospective valuation as at the date of the marriage (i.e. one that ignores later, known, events).** It is well-recognised, but worth repeating, that although the court in *Jones* started with this valuation, the figure was then doubled because the judge had found that there was, what was called, "a springboard in place (which was) not reflected in the valuation", at [41]. The doubling of the valuation by Wilson LJ was, as he acknowledged, "highly arbitrary", at [43].

62. And in a further retreat from his position in *Hart*, Moylan goes on to say:

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> 115. In addition, having regard to the judgment below in this case, I think **I need to make clear that, when I said in *Hart*, at [94], that the court can "undertake a broad evidential assessment" when there is a "complicated continuum" and "leave the specific determination of how the parties' wealth should be divided to the next stage", I did not mean that the court need not identify *at* the next stage, namely quantification of the award, how this factor impacted on the award. The "court does not have to apply any particular mathematical or other specific methodology", *Hart*, at [96], because, as I said in *Martin*, at [112], there is no "single route to determining what assets are marital".** However, as I also said in *Hart*, at [96], "the court will have to decide … what award of such lesser percentage than 50% makes fair allowance for the parties' wealth in part comprising or reflecting the product of non-marital endeavour". This can be a broad assessment, but when this is the *only* factor justifying a departure from equal sharing, the percentage division will inevitably make plain the court's decision (because, for example, by awarding the applicant 30% of the current wealth, it will be apparent that the court's broad assessment was that 40% of the wealth was not to be treated as matrimonial property). I return to this latter issue below.

63. Moylan's main criticism of Baker J's Judgment was that:

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126. I first propose to consider the overall basis of the judge's award. As referred to above, **the judge gave four reasons for departing from the sharing principle. His judgment does not seek to differentiate how each of these impacted on his award. Rather, he decided to give them a cumulative effect reflected in his decision to award the wife a lump sum equivalent to 25% of the growth in the value of the husband's shares based on the value given by the accountant with indexation. Does this approach, in this case, satisfy the need for a judgment to provide sufficient clarity as to how the award has been calculated? Or, as Ms Stone submitted, is the judgment flawed because it does not set out how each factor, in particular in respect of latent potential, "affected his overall calculation of" the award?**

64. In short, he said yes, it was flawed and did not differentiate how each factor impacted on his award. He said that:

130… in most cases the court will be able to, and should, make clear at some stage what part of the value of the asset or assets the court has determined is non-matrimonial.

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65. And then:

158. (ii) Latent Potential Value:

Again for the reasons given above, I consider that the judge was entitled to find that part of the proceeds of sale of the shares was non-marital property to which the sharing principle did not apply. He was also entitled to determine what proportion was not marital property other than by applying the expert's valuation increased by indexation. It was open to him to undertake, as he said, "a broad evidential assessment" and to conclude that there was significant value not reflected in the formal valuation, at [241]. **However, because the judge did not set out his determination of the extent of the marital property in this case, this court is unable to separate out this aspect of his decision for the purposes of deciding whether or not to uphold it.**

Outcome

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66. Moylan simply said:

163. I consider that we are in a position to undertake the "broad assessment", as explained in *Hart*, required in this case to determine the "fair allowance" (referred to above). It is clear that, as in *Robertson*, the Company had its roots in a business started some years before the marriage, as reflected in the graph in the judgment, at [200]. I would also note that the graph of the Company's progress in terms of turnover appears to be similar in shape, a J, to that of the company in *WM v HM*, at [18]. **Applying the judge's determination that the ultimate success of the Company was attributable to "a not inconsiderable extent" to its pre-marriage "foundations" and that they remained a "significant" factor, I consider that it would be fair to both parties to treat 60% of the wealth derived from the shares, of just under £490 million, as matrimonial property and 40% as non-matrimonial. This gives a figure of £293 million for the former and £195 million for the latter. If the former was shared equally between the parties, the wife's share would be £146.5 million.**

67. Once that was added to her own resources the W got £182.45m (34.5%) and the H £347.55m (65.5%), as opposed to 28.75% and 71.25% per Barker J's decision.

Special contribution

68. *XW v XH* also dealt with the concept of "special contribution".

69. H argued that he had made an exceptional contribution (pursuant to the MCA 1973) which could be found within the current value of the company and, because of that, he should be awarded a greater share of the assets regardless of any other factors.

70. Barker agreed, but this was overturned by Moylan LJ on appeal. Moylan was very plain that Baker had simply got this wrong.

> 159. (iii) Special Contribution:
>
> The judge failed to undertake the required assessment, namely to consider whether there was such a *disparity* in the parties' respective contributions to the welfare of the family that it would be inequitable to disregard. His finding in this respect must, therefore, be set aside.

71. It is all about disparity in contribution, per *Work v Gray*.

Implementation

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72. Also see what Moylan J says about the cost associated with investigating all of this at para. 90.

> 90. It may be, for example, that the external contribution can immediately be seen to be sufficiently insignificant in the context of the case that it warrants no further enquiry… **If**, on the other hand, **the enquiry would require an account to be undertaken of the marriage and/or some other expensive investigation and/or would be of "doubtful utility", the court could be expected to decide that such an enquiry was neither proportionate nor required to enable the court to achieve a fair outcome…**

Sharing value

73. When one finally arrives at a valuation for a company one then has to decide how that value (or the matrimonial element) should be divided and the departing spouse's share made available to her or him.

74. Should the departing spouse have their share all in cash or partly cash and shares? If in cash, how is the cash to be generated? By way of dividend or, exceptionally, a sale?

75. The answer to those questions will depend on the value of the business compared with the other assets in the case and whether any off-setting can or should be done. That may be possible where the net value of the business is small in the context of the other assets. But where it is the dominant asset is can become very problematic.

Dividend Tax in addition to CGT

76. Normally, the SJE provides a gross value for the business and a net value after CGT and costs of sale have been taken into account.

77. But do not forget that there may be further tax on extracting value or cash from the business. There are real problems and potential pitfalls here.

78. In *WM v HM* the husband had (by the end of the trial) accepted that "a very large dividend" of £80m (gross) could be paid so as to enable W to be paid a lump sum.

79. See the assets schedule in *WH v HM* at para. 27:

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XG	
Value	221,125,000
79.88% marital	176,634,650
less costs of sale	(4,239,232)
less dividend tax on £80m	(30,480,000)
less CGT	(17,369,653)
Net:	124,545,765

80. In the notes to this schedule in Mostyn J's judgment he says the following:

81. This problem of double taxation does not concern Mostyn J in the slightest. See what he says at para. 26 of *WH v HM*:

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> 26. The second consequence is that in calculating the net assets the latent tax has to be assessed on the basis that a very large dividend is paid in order to give the husband the means to pay the wife a substantial lump sum, while at the same time allowing him to continue working in and on the business. The dividend tax rate of 38.1% is higher than the capital gains tax rate of 20%. **This means that the overall net value of the assets is slightly less that it would have been on a notional immediate sale, and that the value of the wife's share is correspondingly less. I am not disconcerted by this in the slightest. If somewhat more tax is paid, or taken to be paid, because I have decided that it is fair that the husband should be allowed to continue with this business, then that is a consequence that the wife will have to bear.**

Wells v Wells

82. So when the court comes to deciding how a departing spouse's award is made up what are the guidelines?

83. Well, as we know, the case for an equal sharing of the liquid and illiquid assets comes from the case of *Wells v Wells*, even though in that case such a division was not brought about, because the husband wished to keep his shareholding (as is often the case).

84. But look at what Thorpe LJ in the Court of Appeal said in *Wells v Wells*:

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> **[24] Having read the skeleton arguments and the judgment we were at once struck by the security of the result that the wife had achieved in contrast to the risks confronting the husband's economy. The family's standard of living has throughout been dependent upon the fortunes of the husband's business. Had the marriage survived the family would undoubtedly have shared adversity as it had shared prosperity.** The years of marriage comprise the years of the husband's commercial vitality between his late 30s and his mid-50s. The harvest of those years is represented by the concrete assets totalling £1,823,000. But the future years look hazardous. It seems unlikely that the husband will restore the pattern of prosperity and savings from income in the years ahead. After all, if it is reasonable for him also to seek to retire at 60, he has only 5 years in which to recover the profitability without which Soundtracs will not be easily realisable for significant value**. In principle it seems to us that the separation of the family does not terminate the sharing of the results of the company's performance. That is easily achieved in any case in which the wife's dependency is met by continuing periodical payments. It is less easy to achieve in a clean-break case. In that situation, however, sharing is achieved by a fair division of both the copper-bottomed assets and the illiquid and risk-laden assets. After all, the wife was already a shareholder in Soundtracs and a substantial increase in her shareholding would at least have enabled her to participate in future prosperity by dividend receipts or capital receipts on sale or a cessation of trade.** An increase in her share of the illiquid and risk-laden asset would have allowed a reduction in the *Duxbury* fund, if not in the housing fund. If profitability were not recovered then both parties would share the experience of a marked reduction in standards of living.

85. And therein lies the problem.

Discount for getting cash now?

86. But where one party does get cash and the other shares, should a discount from 50% be applied to the share being taken away by the spouse with the cash? As the other will be left with all the risk laden assets?

87. In *Chai v Khoo* Bodey J discounted W's share of what he called "the kitty" from 50% to 40% to take into account that Ms Chai was getting cash and Dr Khoo was keeping the businesses. But he did this after also allowing for a "blockage" discount to the value of the business in the first place (as recommended by the SJE), because of the problems Dr Khoo would have in selling his shares in Laura Ashley all at once.

88. In *WH v HM* Motsyn J fundamentally disagreed with this approach. He said at para. 29:

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> "I am aware that in *Chai v Peng & Ors* Bodey J divided the "kitty" 60:40 in favour of the husband because the wife's award would be largely cash or easily realisable assets: see para 140. I do not adopt that approach. A valuation of an asset is the estimate of what it will sell for now. If it is perceived as being hard to realise then its value will be discounted to reflect that difficulty**. It does seem to me to use discounted figures and then to move away from equality is to take into account realisation difficulties twice. Whatever the asset the only difference between it and its cash proceeds is, as Thorpe LJ once memorably said, the sound of the auctioneer's hammer**."

89. But the Bodey approach was recently been followed by Roberts J in an unreported case.

90. And then in *Martin v Martin* [2019] 2 FLR 291 (which was *WM v HM* on appeal, Moylan LJ said, from the Headnote (para. 1):

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> (1) … The judge had failed to consider whether his proposed award had achieved a fair division of both the copper-bottomed assets, and the illiquid and risk laden assets. **He had erred in basing his conclusion that there had been no difference between the valuation of the company and its cash proceeds on sale**, on the auctioneer's hammer analogy. That reference was inapt to the circumstances of the case; there was a difference of substance between the value ascribed to the company and other assets including the cash to be extracted from the company by way of dividend.

91. What Mostyn J said in *WM v HM* about that was as follows:

> **[29]** I am aware that in *Chai v Peng and Others* Bodey J divided the 'kitty' 60:40 in favour of the husband because the wife's award would be largely cash or easily realisable assets: at para [140]. I do not adopt that approach. **A valuation of an asset is the estimate of what it will sell for now. If it is perceived as being hard to realise then its value will be discounted to reflect that difficulty. It does seem to me to use discounted figures and then to move away from equality is to take into account realisation difficulties twice. Whatever the asset the only difference between it and its cash proceeds is, as Thorpe LJ once memorably said, the sound of the auctioneer's hammer.**

Departing spouse's award partly in shares

92. The quote from *Wells* above would appear to be excellent authority for leaving a departing spouse with a substantive shareholding in a company. But the problem with that is twofold:
    a. it offends the clean break principle;
    b. often necessitates complex Shareholders' Agreements and policing arrangements;
    c. the departing spouse's minority shareholding is open to devaluation by the remaining spouse; and
    d. normally neither party wishes for it to happen (as was the case in *Wells*).

93. Mostyn J recognised the clean break point in the case of *WM v HM*. At para. 24 Mostyn J records that in that case it was the husband's intention to sell the business by his 75th birthday and on that basis he decided that:

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> 24. … Therefore, but for this divorce I proceed on the footing that it was the husband's intention to cash out at that time – seven years from now. Of course, the divorce alters everything. However, it is my judgment that it is reasonable for the husband to be able to continue with his life's work if most of the wife's award can be provided now either by transfers of real property or in cash. **Generally speaking, a *Wells* sharing arrangement should be a matter of last resort, as it is antithetical to the clean break. It is strongly counterintuitive, in circumstances where one is dissolving the marital bond and severing as many financial ties as possible, that one**

should be thinking about inserting the wife as a shareholder into the husband's company. Its inaptness was well illustrated when Mr Marks QC put it to the wife that a form of *Wells* sharing would have happened had the marriage continued, to which her pithy response was "but it hasn't continued". However, *Wells* sharing is not so objectionable if it only applies to a minority element of the claimant's award.

94. As a result, Mostyn J decided that most of the wife's award (c.£53m or c.74%) was provided in liquid assets and cash with only c.26% (c.£19m) needed to be transferred to her in shares. This was not overturned by the Court of Appeal.

95. Mostyn J says the following at para. 25:

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25. Therefore, it is **my central finding that if most of the wife's award can be provided to her now, or soon, it is not unreasonable to proceed on the basis that the business will not be sold until the husband chooses to sell it. This finding has two consequences so far as the wife's award is concerned. First, and obviously, and as I have already mentioned, it means that a minority part of the wife's award will be expressed as an enlarged shareholding in XG. For reasons I will explain the wife's shareholding will be enlarged from 1% to 17.5%. This is about 26% of her overall award, which is a not unreasonable proportion.**

Should the company be sold?

96. What about a more radical way to solve the problem of a lack of liquidity or a *Wells v Wells* imbalance? Sell the company and take the golden goose to market.

97. You will remember what Coleridge J said at the end of his case of *N v N*, that :

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"However, **I think it must now be taken that those old taboos against selling the goose that lays the golden egg have largely been laid to rest; some would say not before time. Nowadays the goose may well have to go to market for sale**, but if it is necessary to sell her it is essential that her condition be such that her egg laying abilities are damaged as little as possible in the process. Otherwise there is a danger that the full value of the goose will not be achieved and the underlying basis of any order will turn out to be flawed."

98. Roberts J followed this route in the case that Nigel Dyer and I did last year. She gave the husband time to pay out the W's award, but in default a sale of the company was ordered from which the wife would get an equal share, not a discounted sum because she was getting cash (see above).

99. So what it the right way of approaching the matter? Personally, I think that given the right facts, and probably only in a case where the business was wholly generated during the marriage:
    a. the outcome should be *Wells* compliant; and
    b. if a spouse (normally the husband) owns or has run the business cannot find the liquidity to pay the other out within a reasonable timeframe, it should be sold.

Conclusion

100. So what are the bullet points to take away:

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1. It is not as hard you may think to get in your own expert in a case, just possibly at the outset, but via a *Daniels v Walker* application.
2. But beware about the current trend for indicative valuations and the move away from precision.
3. Outside of Court 50 there has been a move away from a formulaic approach to dealing with the valuation of companies (and assets) brought to a marriage in favour of a broader more impressionistic approach, but after *XW v XH* that should be in retreat.
4. Beware of the fiscal implications of extracting value from a business: i.e. you need to take into account both CGT upon a sale and DIV tax.
5. Lastly, there is a very real trend of all judges doing whatever they can to reduce the value of the business: whether by robustly evaluating its value when it was brought to the marriage; discounting it for other reasons suggested by the SJE and/or taking a valuation at the lower end of their range, and then discounting the other spouse's share of the kitty for *Wells* reasons. All in an effort to reduce the cash payment to the other spouse so as to bring about a proper clean break and avoid a sale.

101. This is a very fast changing area of the law. It is highly case specific and full of potential pitfalls or opportunities, depending who you are acting for.

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102. Good luck!

Nicholas Yates QC

10 June 2020