

Since divorce is a fact of life, it's better to be prepared

My favorite line from the 80's TV show, *The 'A' Team*, was Hannibal's exclamation, "I love it when a plan comes together!" I think I used to watch the whole half hour just to hear those eight words. They capture the entrepreneur's dream.

Most businesses are pretty conscientious about updating their strategic plans and insuring against risks whenever possible. However, the non-business-related risk of divorce can smack headlong into the best laid plans. Each of us can hope that we will never be confronted by divorce, but, only 50% of Americans are so lucky. The rest *will* face this unpleasant experience at some point - so there are things we need to understand. For simplicity sake, I assume throughout that *he* is the business owner and *she* the dependent spouse.

Divorce is accomplished through legal means but is, in essence, a financial transaction. Each state is responsible for regulating its own process. In Pennsylvania, property settlements are structured to achieve 'equitable distribution.' Note that equitable is *not* equal. Because the definition of 'equitable' is case specific, and the divorce rules vary from state to state, don't try to check with family or friends to see how *your* divorce should unfold. Instead, seek the advice of an attorney and appropriate financial professionals.

Business appraiser, Victor Haas, has reported to me that most husbands think, "She wasn't involved. She doesn't deserve any of my business....." Under case law, that thinking is irrelevant. The court isn't interested in damaging or carving up your business, but they are interested in determining its financial value. The way the rules work, whatever portion of your business was achieved while married *is* part of the 'marital estate.' Its value will be included in the calculation of your marital net worth. As family law attorney, Jennifer Brandt, counsels her clients, "What happened in the marriage stays in the marriage."

There could be an exception if a pre-nuptial agreement is in place. Such agreements are generally used by the wealthy for mature businesses, and by family firms or partnerships established before the marriage. Should you be contemplating an engagement, the time to discuss a pre-nup is early on. Waiting

until close to your wedding date is counterproductive. Actually, this conversation could provide a powerful springboard for the financial conversations all couples benefit from having – long *before* they ‘tie the knot!’

Both Jennifer Brandt and Victor Haas agree that perhaps the biggest risk a business owner faces in a divorce proceeding is the definition of income. Many business owners and their spouses have become happily accustomed to ‘having their cake and eating it, too.’ What does this mean? The owner probably draws a salary (his cake.) But in addition (and eating it, too,) he and the family enjoy perks such as channeling personal expenses through the business, bonuses, profits re-invested into the business, and other creative ploys resulting in a *real* family income way above the designated salary.

The court is very interested in true income because it forms the basis for child support and spousal support payments. It may also impact who gets what with respect to equitable property settlement decisions. Count on it! The court will carefully scrutinize the cost of your lifestyle – irrespective of reported salaries.

Watch out dependent spouses! ‘He’ may have treated you like a financial dummy, but the court assumes you are savvy. If you signed all those tax returns showing almost no income - while enjoying the good life - the IRS innocent spouse rule probably won’t save you now. ‘Ratting’ on him in hopes of helping yourself to a bigger piece of the cake is also likely to backfire. You may simply serve up more ammunition to the court. Remember that the court is free to report findings to the IRS if tax fraud might be an issue.

How can you protect yourself? First of all, hire competent advisors and be totally honest with your attorney and financial professional. Secondly – if you’re not already doing so - begin keeping clear, concise records of all of your expenses and business dealings. Financial mysteries do not help divorcing couples. Perhaps the old adage, “Do unto others as you would have them do unto you” is supremely apt for navigating divorce with the least possible cost – legally, emotionally, and financially.

Joslyn G. Ewart is an educator, financial analyst, and business owner. E-mail her at joslyn@entrustfinancial.com. Her business column appears on a regular basis in Main Line Life.