

**THE FORENSIC ACCOUNTANT'S CHANGING ROLE IN
MATRIMONIAL DISPUTES**

by Rakesh Kapila

The forensic accountant has long had an active role in matrimonial disputes arising from provisions in the Matrimonial Causes Act 1973 that the Court should take account of the income, earning capacity, property and other financial resources available to both parties to a divorce.

Although a key aspect of the expert accountant's role in matrimonial disputes over the years has related to business valuations as part of the process of identifying the property and financial resources available to both parties, this article provides an overview of how the forensic accountant's role has changed in recent years and the primary aspects in relation to which useful work is now undertaken.

Recent developments

Developments over the last few years arising from case law have resulted in important changes in relation to the split of assets between the parties on divorce. In particular, the House of Lords ruling in *White v White* in 2000 resulted in a change in focus away from the wife's reasonable requirements and the husband's ability to pay to achieving fairness in divorce settlements by recognising the contribution each party has made to the marriage. On this basis, it was noted that, as a general guide, equality should be departed from only if, and to the extent that, there is good reason for doing so and Mrs Pamela White accordingly received 40% of the family assets resulting in the sale of the family business.

White v White has been followed-up by other "landmark" cases including *McFarlane v McFarlane* in 2006, the House of Lords ruling that the settlement made in Court should not just reflect the wife's needs but, for wealthy couples, compensate her for her losses.

Implications for forensic accountants

Matrimonial case law in recent years has had a significant impact on the forensic accountant's role. The emphasis in the work undertaken by expert accountants has changed as follows:

- Much work used to be focused on business valuations which were prepared on an "overview" basis in many cases and on calculating the reasonable needs of the wife on the basis of the *Duxbury* model. The approach was particularly useful given that Court settlements would not necessitate the disposal of family businesses and "needs-based" settlements had to take account of future inflation and interest rates at a time when such rates were relatively volatile.

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- Work in recent years has included a more active involvement in identifying the financial resources of the parties, a greater number of business valuations which are better informed and a critical appraisal of the ways in which funds may be secured to effect settlements which do not jeopardise the ongoing viability of the primary business owned by one or more of the parties. Forensic accountants therefore play an important role in valuing family businesses and also in finding ways of ensuring that such businesses do not always need to be disposed of in securing the resources required to implement agreed settlements.

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The present-day role of the forensic accountant

Introduction

The changing role of the forensic accountant has resulted in an increased involvement in the following areas of work as considered in greater detail below:

- assisting in the compilation of questionnaires after the disclosure of Forms E;
- valuations of businesses; and
- identifying ways in which funds can be released from businesses.

Compiling questionnaires

After the disclosure of Forms E, the Financial Statements of each of the parties, the forensic accountant may have an active involvement in assisting solicitors in compiling questionnaires for the following primary reasons:

- seeking clarification and further information in relation to data provided in the parties' Forms E or in the supporting documentation, e.g. further information in respect of pension provision or the reasons for significant receipts as ascertained from bank statements;
- obtaining further information to ensure that assets are included at realistic amounts in the parties' Forms E, e.g. updated valuations and accounts of private companies in which the parties have shares; and

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- obtaining detailed information in respect of businesses identified in the parties' Forms E with a view towards "improving" the valuation process, e.g. updated financial statements, details of "one-off" income and expenses and data on management remuneration.

There are instances in which the type of information sought by expert accountants results in early settlements without the need to incur significant costs in court attendance and protracted negotiations.

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Valuations of businesses

The forensic accountant's "traditional" role in establishing whether businesses should be valued on the basis of their earnings streams, their assets or the dividends paid by them has been "enhanced" through a detailed scrutiny of the following aspects:

- the extent to which business profitability has been affected by "one-off" income and expenses or by unusually high levels of management remuneration;
- the extent to which the net assets of businesses are mis-stated owing to the lack of updated valuations of properties or the extent to which a proportion of net assets is "surplus" to requirement through the inclusion of properties not central to the activities of the businesses concerned; and
- the shareholdings of the parties and the need to apply discounts to valuations attributed to businesses to take account of minority shareholdings, quasi-partnerships and the types of sector in which businesses are involved.

Realising funds from the business

Given the greater willingness of the courts to make settlements which result in the disposal of part or all of businesses owned by the parties, the forensic accountant's role in identifying ways in which funds may be raised can improve the prospects of businesses continuing to be run by existing owners. The expert accountant can assist on the following basis:

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- evaluating the prospects of realising funds through the disposal of minority shareholdings, the sale of "own" shares or the raising of funds against shareholdings;

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- considering the cumulative profits of businesses available for distribution and the liquidity available to effect distribution, including a consideration of the ways in which liquidity can be improved, e.g. selling “surplus” assets or raising funds through the provision of property as security; and
- identifying suitable ways of distributing available funds after taking general tax aspects into account, e.g. by way of remuneration, dividend payments or the repayment of amounts recognised in directors’ loan accounts.

Conclusion

Since there is no certainty that family businesses will automatically be protected on divorce, the early and active involvement of expert accountants could ensure that settlement is achieved cost-effectively and in ways which better suit the parties.

Rakesh Kapila is a member of the Academy of Experts and the Expert Witness Institute and is a partner at Sim Kapila, Chartered Accountants, a firm based in London W1 which specialises in forensic and investigative accountancy. E-mail: rkapila@simkapila.co.uk

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