The Issues of Valuing and Dividing a Business Started Before a Break-Up

The recent New Jersey case of Fox v. Fox settled the matters of whether a business started before marriage should be divided equally, and when its valuation and distribution should be determined. One of the most

important factors involved whether the owner or the "non-owner" spouse must establish the pre-marital value of the business.

The Details

In 2001, two years after Edward Fox broke up with his girlfriend, Catherine, he started a small part-time bowling equipment business, EBN Services, Inc. Edward and Catherine reconciled in 2003 and married in July 2004. Before their marriage, the business wasn't profitable.

During their marriage, Edward and Catherine shared the childcare and household duties. Around the time of the marriage, Edward quit his job and pursued EBN full time. By 2008, EBN had over $770,000 in gross sales and a net loss of around $20,000. Edward testified that Catherine never worked for EBN in any significant manner; she was a hairdresser and later worked part-time.

He asserted that Catherine's income remained higher than his own until around their separation in May 2012. EBN flourished after the separation. Edward said he could devote more time to the business because Catherine cared for their kids.

Nearly two-and-a-half years later, Edward filed for divorce in 2015; the delay was due to financial reasons. The couple hired an accountant who assessed the business's fair market value at $183,000 in 2015 and, using a less involved method, between $43,000 and $56,000 in June 2012. The accountant didn't value the company as of 2004.

The trial court decided Edward started his company in 2001, about three years before the couple married. The court assumed EBN lacked value in 2004 because it wasn't profitable then, and awarded Catherine half of the $183,000 2015 business value.

In his appeal, Edward contended that EBN should not have been divided equally because Catherine didn't contribute to the company's growth during or after the marriage; he also felt the court abused its discretion. He argued if EBN is subject to equitable distribution, it should be divided according to its 2012 value, the year of separation, instead of 2015, when he filed for divorce.

New Jersey Appellate Division Decision

The court refuted the prior decision that because a business is unprofitable, it lacks value, stating, "An unprofitable business may still have a positive fair market value. For instance, a business can have valuable tangible assets or inventory, as well as intangible assets, such as goodwill and customer lists."

The Appellate Division upheld the trial court decisions to divide the business fifty-fifty and to keep the valuation date of 2015 instead of 2012, noting that the value increased during the marriage.

"While the increase was directly tied to Edward's efforts, Catherine indirectly contributed to the increase by enabling Edward to devote time and resources to EBN….Catherine provided financial stability and flexibility so that Edward could pursue EBN, a risky business venture. As the trial court found, based on adequate support in the record, "[I]t was his marriage to [Catherine], and her financial and non-financial contributions to the household and child-rearing, that allowed plaintiff to devote his full-time efforts to building EBN…"

Regarding the increase in value after the 2012 separation, the court concluded, "…the fact that the company grew significantly post-separation but pre-complaint is relevant to the ultimate allocation decision, not the question whether EBN was subject to distribution in the first place…."

On the issue of who shared the most risk in the marriage, the court found that "While he [Edward] was pursuing EBN, Catherine lacked the benefit of a spouse's regular income and stable employment. In other words, Catherine shared in the risk with Edward when he pursued EBN. Most of EBN's appreciation occurred after the separation, but we find that the trial court properly considered this fact when it distributed EBN…We shall not disturb the trial court's finding that '[Catherine] made an equal, non-financial contribution to the appreciation in value of [EBN] even after the parties separated….'"

The court remanded or sent back the pre-marital business valuation to the trial court for decision, and assigned Edward the burden of proof.