

Collaborative Family Law

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Happy New Year to all! We are again beginning the year with a series of newsletters highlighting the various professional roles of the collaborative team and the type of assistance each can bring to people undergoing separation. We begin with the Financial Edition, with articles by two of our members, Tanya Sterling and Chris Ounsted.

Having the answer isn't always the best solution.

Usually one person knows the finances better than the other. Maybe one person handled getting the mail and paying the bills, while the other person coordinated social activities and household needs. When this is the case, there is often an imbalance in knowledge around the finances and the partner who was less involved in the financial affairs may have been in the dark about what the financial story was. Now what?

In order to try to save money and be as upfront as possible, the one who is more financially savvy in the relationship might prepare a nice outlined summary of what they have, and come up with an option or two. Great idea right? So you would think. Although it is counter-intuitive, my experience shows that this is the worst place to start. When looking to resolve differences, it's important to fully understand the options before jumping to solutions.

Part of the collaborative process is about coming up with solutions using an interest-based approach that works for both of you, leaving you with a legally binding agreement that is tax-effective and fully informed. Before signing on the dotted line, not only should you receive legal advice around what those options might be, there more than likely are some hidden tax considerations, available loopholes and some fancy stick handling that a financial professional can bring you up to speed on. This alone saves considerably more time and money in the long-run than if they were overlooked. In looking over past agreements, I see many people who lost out on opportunities because they didn't take the time to talk to a financial expert in the area to get their 2 cents.

Coming up with solutions before looking at all the possible options leads to 'positional thinking'. Positional thinking is when one holds on to a fixed idea, or position, of what they want and continue to argue for it, regardless of any underlying interests. It seems silly, but when it comes down to things that are important to us, it's often hard to see the forest through the trees. Once an idea is in mind, it becomes very difficult to move from there. Interestingly enough, one of the first things people say when they come to see me is "Give me the numbers!", which is instinctively the first place many people want to go, but can't go but this is not the most efficient or effective way to resolve the conflict. This is often what happens in adversarial legal situations. I cringe when we are instructed to look into financial pieces that will cost more in professional fees than it's worth, yet nobody seems to care, they just want to win. In my

opinion, that doesn't help anyone, except those whose pockets are being lined.

When someone shows up with a calculation saying, "I have the answer, but he/she won't listen to me, you have to tell my partner this is the solution.", it usually means we need to spend more time (a.k.a. money) back peddling from the finish line. I understand this is frustrating, because if someone has taken the time and effort to come up with solutions, they expect to be pretty much at the finish line and really just looking for that snapshot at the crossing line to see the final result. Often these solutions have already been presented to the other partner, so both now already have an expectation in mind or, as is often the case, the numbers have been tossed around and disagreed upon so much that there is no longer any trust or goodwill in the relationship around finances. As a result, more work needs to be done to dig further than may have otherwise been required if a financial neutral had helped them from the beginning and worked together to come up with options.

What does save time is preparing a summary of all of your assets and liabilities both at the time of separation and the current date, if some time has passed – with related supporting documentation, copies of your last three personal tax returns as well as corporate returns and financial statements. Having this information in hand helps the professionals with the information gathering, which is often the phase in the process that eats the most time – but probably not where you want or need to be spending your money. Having a financial neutral help to sort through the information means the cost is shared and you can be creative about solutions, instead of shifting the arguments you had at home, to arguments to be had between the professionals at a much higher cost. If you come to the starting gate with these pieces in hand, you will make it to the finish line faster and with less conflict than if you start the process with 'the answer' already in hand.

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Business Valuations

The Value of Business Valuations

Business valuations are typically required when either or both separating spouses are shareholders in a corporation. These business valuations will often form a critical piece to the settlement process to assist in the allocation of family assets. A business valuator is considered an Expert Witness and as such, is not to be an advocate for any party but to act as a neutral professional. Being a neutral professional is crucial as the valuation assignment requires a degree of professional judgement that is based on experience and relating that experience and knowledge to the specific circumstances of the assignments. In simple terms, business valuations are an art, not a science.

The cost of a business valuation expert can vary from hundreds of dollars to thousands of dollars depending on the extent of work that is needed. Every assignment is different and will require different needs. Some assignments can be as simple as a few phone calls and a quick review of information while others will require significant analysis with a written report. However, based on my experience, the cost of a business valuation engagement associated with the Collaborative Family Separation Professional is, on average, less than other valuation engagements associated with a separation or divorce.

The Process

The process of performing a valuation always begins with the parties signing an engagement letter. An engagement letter will outline, among other items, the role of the business valuator, the scope of the engagement (for example, if a written report is required), the information that may be requested and the fees that are estimated to be charged.

A business valuation begins with obtaining key financial information regarding the business such as corporate financial statements and tax returns as prepared by the corporate accountant. Discussions with the business operator are important to the process to determine such information as the background of the business, critical success factors and the future expectations.

The Approaches

Valuing a company is generally based on three approaches and these are the asset based approach, the income based approach and the market approach.

The **asset based approach** assumes the company's fair market value is the fair market value of the company's net assets, that is, its tangible assets less its liabilities. Tangible assets include such items as equipment, machines, property

bank accounts, receivables and inventory. This approach is common when the company owns a significant amount of tangible assets such as property. It is also common when the company would be considered to not own any commercial goodwill. There is commentary on commercial goodwill later.

The **income based approach** assumes the value is based on the company's future earning capacity. This approach is common with a business that generates income from something it produces or services that are being provided. In very simple terms, this approach is calculated by multiplying an expected annual earnings range by a range of "Multiples" to determine the fair market value. Multiples are determined by reviewing factors such as general economic conditions, industry conditions and the degree of risk involved. It is assumed that the income based approach will provide a higher valuation conclusion than the asset based approach.

The **market approach** assumes that the fair market value would be calculated by comparing the company to recent transactions of the business or similar businesses. This approach would be used when there is enough information from similar businesses that have been sold. An example of this would be a franchise. When franchises are being bought and sold there is often critical financial markers that will identify that business' value. For example, if the sales are \$xxx then the value is \$xxx. This is also referred to as a "Rule of Thumb". A common rule of thumb would be that the fair market value of the business is based a percentage of the sales or revenue. A significant amount of caution must be exercised to ensure the comparable transaction or the Rule of Thumb is relevant to the specific situation. As mentioned before, every situation is different.

Goodwill – Whose value is it anyways?

In valuation terms there are two types of goodwill, personal and commercial.

Personal goodwill relates to a specific person and if that person leaves the business, so does the goodwill. An example would be a medical professional operating through a corporation. The business has no goodwill value if the medical professional stops working. Therefore, personal goodwill has no value in the valuation context as it is not transferrable to another owner.

Commercial goodwill is generally defined as value that is not attributable to a tangible asset. It is therefore considered an intangible asset. Some different sources of goodwill are based on brand recognition, customer loyalty, etc.

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Commercial goodwill is calculated by determining the difference of between the value of the business by using the income based or market based approaches and the asset based approach.

Fair Market Value – Timing is everything

An important consideration in the business valuation context is timing. What valuation date is being used? Valuations are based on facts and assumptions at a specific point-in-time. Situations and circumstances can significantly change and so will the calculations and ultimately the conclusions. Consideration must also be given to the availability of financial information at a specific date. Valuers often use a valuation date that coincides with the company's year-end date. At the year-end date, the company's accountant will perform certain analysis and make annual adjustments that may affect the company's value.

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Are you separating and wondering where to start? The mental health professionals who work as coaches with our collaborative team offer a service which assists separating couples to choose the best process option for them in achieving a separation agreement. Please see the "Getting Started" section of the website for further information about this service. A referral is not required. To make an appointment, you may call the coach corresponding to the month in which you are making the call.