

NIIFA welcomes a new member:

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NIIFA 10th

ANNIVERSARY

NIIFA are proud to celebrate our 10 year anniversary. Thank you to all our clients.

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WORTH MORE DEAD THAN ALIVE

TO DISCOUNT OR NOT TO DISCOUNT? A suggested approach to minority discounts.

“INNOCENT” WIVES Where criminal and family lawyers meet.

WORTH MORE DEAD THAN ALIVE

Common commercial sense can sometimes have no place in the assessment of damages in fatal accident dependency claims.

Consider a family business that is run as a partnership between parents and two children. The father is the driving force behind it and his wife and children play a nominal role but each receives a substantial share of the profits for tax-planning reasons.

Suppose that the husband is killed in an accident so that his children have to take over from him. If they are so successful in doing so that the profits actually increase, how should the widow's and the children's damages be assessed under Section 3 of the Fatal Accidents Act 1976?

An accountant's answer might be that there could be no loss in circumstances in which the family was as least as well off after the deceased's death as before. However, in *Welsh Ambulance Services NHS Trust & Anor v Jennifer Mary Williams [2008] EWCA Civ 81* it was held that, in just these circumstances, that the financial benefit that the children brought to the family by taking over the business was irrelevant to the assessment of the dependency under s.3 of the Act. The reason for this was simply because as a matter of law a dependant could not by his or her own conduct after the death affect the value of the dependency at the time of the death.

The question for forensic accountants in such cases may not be to compare the performance of the family business before and after the deceased's death. Instead an assessment has to be made as to the cost of replacing the services of the deceased. That may not be his or her market rate of remuneration. In the *Welsh Ambulance* case, the deceased was described to be a "Wealth creator" and his wife was awarded just over £1.7 million plus interest.



TO DISCOUNT OR NOT TO DISCOUNT, THAT IS THE QUESTION

A new suggested approach to the vexed question of minority discounts.

There are few better ways to test the mettle of a forensic accountant than to cross examine him or her about the appropriate discount to be applied to the shareholding of a minority interest in a private company.

The fact is that there is very little published information about the level of minority discounts in any given set of circumstances. For that reason this is one of the relatively few areas in which the court is seeking from the expert accountant a pure opinion. The challenge for the expert is obviously to ensure that it is his or her evidence that is preferred. Credible and clear reasoning is therefore crucial.

Ironically one of the few published tables in this area is that quoted by the Family Law Bar Association's "At a glance" guide for family lawyers. It is prefaced with the warning "this table gives a very crude guide to the general value of private company shareholdings. It is inappropriate for formal use in evidence or in court proceedings; for such valuations expert valuers should be consulted".

Despite that warning, members of NIFA are aware that a number of respected forensic accountants use the table as a point of reference, albeit not a definitive one.

The table is reproduced below for illustration only and sets out the factors (after taking account of the appropriate discount) which could be applied to the pro-rata value of shareholdings for different sizes of company.

Size of shareholding	Post tax profit (£'000)				
	under 100	100-200	200-500	500-1000	over 1000
under 10%	25%	30%	35%	40%	40%
10% to 25%	30%	40%	45%	50%	50%
25.1% to 49.9%	35%	45%	50%	60%	65%
50%	40%	50%	60%	70%	75%
50.1% to 74.9%	45%	55%	65%	75%	85%
75% and over	55%	65%	80%	90%	100%

NIFA does not endorse this table and considers that the weight which it gives to the profitability level is inconsistent with general practice. Any table is only a guide because the level of discount needs to be reviewed in the light of the facts of each case. Matters are further complicated because there are always two questions that need to be considered in relation to minority discounts. The first is what the discount should be and the second is to what extent it should apply.

These two questions are distinct and each should be considered separately. All too often attempts are made to answer them together and this can result in confusion and unpersuasive evidence.

The question as to what the discount should be is to a certain extent, judgemental, but in any given case, should not be considered without having regard to provisions in the company's constitution. In essence the greater the protection that is afforded to minority interests in the Articles of Association, any shareholders' agreement, or otherwise, the lower should be the rate of discount.

Such protection may be contained in provisions in the Articles of Association that set a cap on directors' remuneration, offer pre-emption rights, or protect minorities from a dilution of their interests. A Company's Articles of Association may even prescribe a method as to how minority shareholdings are to be valued.

Once the level of discount has been established, the second question can be addressed, namely to what extent should that discount be applied? The answer will depend on the circumstances applicable to the valuation.

Of relevance in that regard will be such matters as:

- i. The extent to which the company could be said to be a quasi-partnership;
- ii. The imminence or likelihood of a sale of the company as a whole; and
- iii. The relative holdings of other shareholders. In that context a minority discount is likely to be more applicable in the case of a company with 50 shareholders, each of whom has a 2% stake, than in the case of a shareholder with a 2% stake in a company in which there are two other shareholders who each have a 49% stake. Clearly, in the latter case, there is an argument that the 2% shareholding is worth more than a pro-rata valuation would suggest and therefore the application of a premium to it would be more appropriate than a discount.

“INNOCENT” WIVES

The interaction of the Matrimonial Causes Act 1973 with the Proceeds of Crime Act 2002 has the unhappy consequence of bringing family lawyers into the unfamiliar world of the criminal law and criminal lawyers into the unfamiliar world of divorce. No wonder the area is fraught with difficulty.

It is now clear that the non-criminal spouse (usually the wife and I will assume it is the wife for the purpose of this article) is unlikely to be treated on a *White v White* basis. The presumption of equality as a starting point will not apply. Rather, if the wife is to be awarded anything, it will be her reasonable needs that will be relevant.

It has also been established¹ that the court has no jurisdiction to confiscate assets from a wife unless she is herself subject to the confiscation proceedings. In other words, if she has a beneficial interest in an asset she will be able to keep it **even if it is tainted** and was acquired with the proceeds of crime.

¹ Gibson v Revenue and Customs Prosecutions Office [2008] 2 FLR 1672

“INNOCENT” WIVES continued

Subject to these basic principles the divorce court has a very wide discretion which it will exercise on the basis of the facts of any given case. Often these facts rely to some extent on accounting evidence so it is perhaps unsurprising that, as forensic accountants we are seeing more and more instructions in this area and are being asked to consider such matters as:

What assets have been acquired from the proceeds of crime?

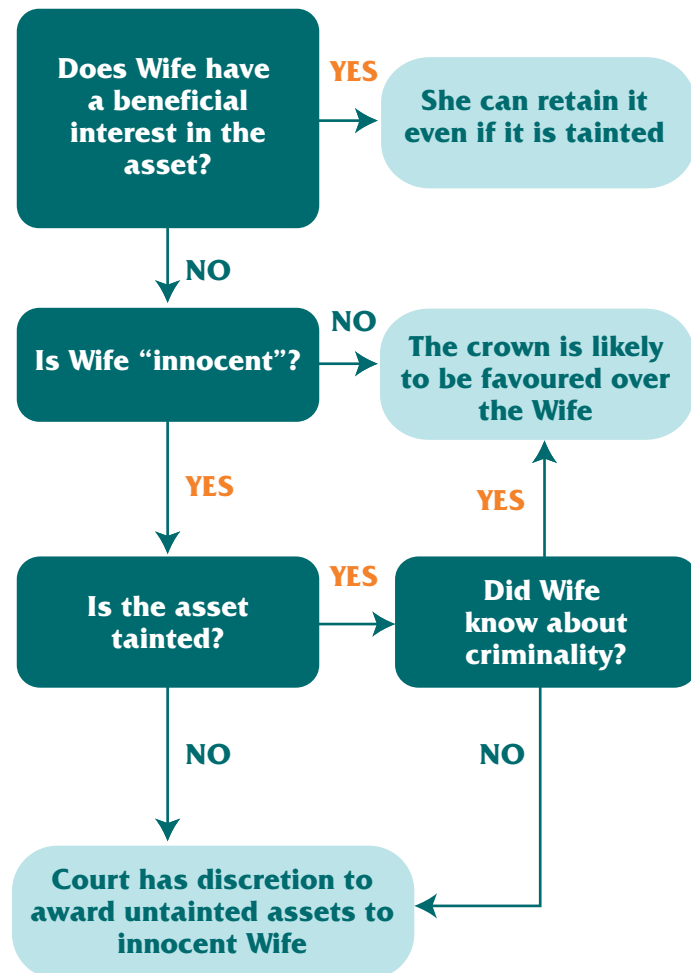
What accounting evidence is there to support or refute a claim that the wife has a beneficial interest in a particular property?

To what extent have the proceeds of crime funded the wife’s lifestyle?

Is there any accounting evidence to suggest that the wife was not as innocent as she suggests and to what extent was she involved in the business or family finances?

Is there any benefit in valuing the husband’s business from the perspective of the divorce?

As a rule of thumb, we have developed a rough and ready decision tree for matrimonial proceedings that can sometimes be used to help clarify what are usually the key questions. It is set out opposite.



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