How A Prenuptial Agreement Can Help Protect Your Business Interests

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Leadership Strategy

We explore how divorce impacts your business and financial well-being.

If you had asked your intended spouse for a prenuptial agreementa decade or so ago, you might have gotten a defiant scowl or the cold shoulder. But over the past several years, prenuptial agreements have become more commonplace, as couples increasingly recognize the wisdom of having a legally binding contract outlining, for example, who owns what prior to the marriage, and how marital assets would be distributed in the event of divorce.

No one wants a divorce – and certainly not a contentious or expensive one – but having a prenup can be particularly valuable in the case where one or both parties own a business. Say you started a business five years ago, maybe before you even met your spouse-to-be. Do you want that business to become marital property, subject to distribution by the courts in the event of divorce? Or would you prefer to create a plan with your partner now that determines what will happen to the company and who has rights to which assets?

Here are five things a prenup enables you to do to protect your business:

Establish the value of the business as of the date of marriage. While additional value gained during the marriage may be subject to division, you can, as the titled owner, protect the premarital value of the business as your separate property so that it will not be subject to any type of distribution upon divorce.

Determine what will happen with the appreciation or depreciation of the business from the date of marriage. Will your spouse share in the profits and losses? Considerations weighing into this determination should include the level of direct or indirect contributions the nontitled spouse will be making to the company and whether he or she has invested capital in the business.

Regarding the nontitled spouse's contributions, set clear expectations for what his or her role in the company will be (if any), and make sure if he or she works in the business that it is with fair compensation. Often during divorce, a spouse will claim that he or she acted in a certain capacity but was not fairly compensated and therefore deserves a larger percentage of the business. But if he or she was drawing a market-appropriate salary, then his or her entitlement to a greater share is either eliminated or minimized. Likewise, you should agree to how you will value your spouse's indirect contribution if, for example, he or she stays home to raise the children so that you can run and grow your business.

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In terms of capital, determine what the source(s) of capital may be for the company in the event it's required. Will these funds come out of marital property? If so, will the entire business then become marital property, or will the marital estate get a credit back for the capital that was contributed?

Specify how you will value the business. Coming to an agreement as to how your business would be valued at the time of divorce could save you the expense and disruption of an intrusive third-party valuation process. This type of process makes demands on your employees, accountant and others associated with the business as people come on-site to evaluate your financial records, practices and procedures.

Specify a percentage of the business your spouse would be entitled to in the event of divorce. Assigning a percentage that your spouse would be entitled to ofthe value in the business could prevent the company from being subject to the same distribution guidelines as other marital assets. For example, if you have agreed that he or she will receive 10% of the value of your interest in the company, then that is the percentage he or she will receive upon divorce, even if other marital assets are being divided 50/50.

Provide details of how your income will be handled. If you as titled owner are not taking a market-appropriate salary for your work in the business, opting instead to keep those funds in the business, then you are limiting your capacity for creating marital property—savings, for example—that could be shared with your spouse upon divorce. A prenup gives you the opportunity to address what this will mean were divorce to take place. As with the other related issues, you want to make sure there will be a fair distribution of assets.

While no one wants to think that their marriage might end in divorce, couples are discovering that having a prenup in place can give them peace of mind, especially when there are business and personal factors at stake. Marriage requires partners to deal with the pragmatic as well as the romantic, so talking about business and financial matters should be a natural part of premarital discussions. A prenup gives you the opportunity to put a plan in place that, hopefully, you will never need.

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