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When Family Law and Business Deals Overlap

By Mary S. Pence

A Marital Asset Under Development:

The "pot" that we call "marital property" in a divorce typically includes many different types of assets. But when it comes to distribution of marital assets in a divorce case, perhaps one of the most unique and complex assets to handle involves a real estate project which is currently in the process of being developed, such as an office complex, a residential housing development or a retail establishment.

In the divorce of Sara and Brett, Brett had been a member of a family partnership which acquired title to a large tract of land in suburban Maryland prior to the parties' marriage. However, during the marriage, the parties' jointly bought out the interests of the other family members in the land and began to develop the tract, including obtaining the necessary zoning, beginning preliminary planning for construction of roads, sewers and other infrastructure, and obtaining a series of construction loans from a lender. At the time that Sara told Brett that she wanted a divorce, ground had not yet been broken for the development project.

Some of the issues which were presented by this project under development in Sara and Brett's divorce included:

(1) The illiquid nature of the asset;
(2) The conceptual and technical difficulty of valuing the asset;
(3) The disparity in views as to a fair outcome between Brett, who wanted to retain title to the asset in the divorce, and Sara, who was willing to be bought out[1]; and
(4) How to handle the non-marital portion of the value of the asset.

The Approach:

Sara's divorce attorney, as an initial matter, advised Sara to retain a consultant with experience in business deals involving this particular type of development. The combination of the skill sets of Sara's divorce counsel with extensive experience in handling high-value matrimonial cases, and the business consultant versed in deals involving this particular type of development was a powerful and advantageous one for Sara. For his part, Brett had his family's business attorney and long-term accountant to assist his divorce counsel.

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[1] Although another couple might have been willing to remain business partners while dissolving their marriage, Sara and Brett chose not to go down that path.

Counsel to both parties consulted about the valuation issues. Ultimately, in order to reduce both costs and conflict, the parties decided to jointly retain a mutually-agreed, neutral valuation expert and to equally share the costs of the expert.

Their neutral expert came up with a range of valuation numbers which also took into account the non-marital component of the asset, and the parties used this range of numbers in their settlement discussions.

Because the marital component of the value of the project dwarfed the combined values of the other marital assets, and that value was completely illiquid, the parties considered a number of creative alternatives to achieve an approximately 50-50 division of the marital assets, including: (1) a promissory note from Brett to Sara secured by the value of the property being developed; (2) a "carve-out" of several parcels of the property, title to which would be transferred into Sara's name, with Brett shouldering all the costs of development of the total tract of land, and (3) the transfer of certain other non-marital assets titled in Brett's name from Brett to Sara.

An important key to final settlement of the case was the careful drafting of the ancillary documents necessary to paper the deal, including deeds of trust and an inter-creditor agreement in addition to the basic Marital Settlement Agreement.[2]

Ultimately, the parties were able to successfully resolve the issues posed by the overlapping business deal and their divorce in one overarching settlement, and each party was able to move on feeling financial secure and comfortable with the total resolution.

[2] As its name suggests, a Marital Settlement Agreement is a comprehensive document which resolves or "settles" all of the issues incident to the parties' divorce, including issues involving the parties' children, support, division of assets, tax matters, health and life insurance questions, and other miscellaneous provisions.