We all need a G v T

Business valuation and an up-to-date approach to run off

A briefing note on G v T [2020] EWHC 1613

By Michael George

3PB Barristers

This case was decided at the beginning of the pandemic. In it, Nicholas Cusworth QC grapples with the problems posed by a volatile valuation, post separation contribution and run off. Whilst this case is not hot off the press it still merits mention if you missed it first time around. The judgment reviews all the main earlier authorities on the issues raised by SJE valuations of small and medium businesses and neatly draws the themes together in a clear and well-reasoned manner.

The outcome is perhaps less important than the reasoning behind it.

As a side note the tactical decision as to whether or not to cross examine an expert is interesting and worth consideration.

This note will concentrate more on content than form.

The Facts

- Costs £1.5M
- Married 2001 separated in October / November 2017

The Issue

- H shareholder in company undertaking proprietary trading and market making
- 3 individuals own to 2/3 of the shares
- Dalliance in asset management

- Husband paid dividends based on performance income varied from £5.1M to £411K over 5-year period.

- Post separation change in business
- Binned asset management
- Marked change in staff
- Significantly increased number of staff

- Net asset valuation

The SJE and Shadow

- Shadow expert Mr Bezant FTI consulting.

- *Daniels v Walker* application
    - Questions put
    - No evidence adduced
    - Cross-examined

On value

H did not want to sell at the value placed upon it by the SJE

> *"The problem for the court is to determine from the limited evidence before it whether that obviously enhanced value to the directors actually has a corresponding value in the marketplace. In other words, whether any third party would see value in acquiring B Ltd as a going concern, at a premium based upon its past trading record."*

On liquidity

- *Wells v Wells* [2002] EWCA Civ 476
- *Versteegh v Versteegh* [2018] EWCA Civ 1050

Review the cases on problems with valuations

- *H v H [2008] 2 FLR 2092*
- *Miller v Miller; McFarlane v McFarlane: [2006] UKHL 24, [2006] 1 FLR 1186*
- *Versteegh v Versteegh* [2018] EWCA Civ 1050
- *A v A [2004] EWHC 2818 (Fam), [2006] 2 FLR 115*

- *Martin v Martin* [2018] EWCA Civ 2866
- *Hart v Hart* [2017] EWCA Civ 1306
- *Goddard-Watts v Goddard-Watts* [2016] EWHC 3000 (Fam)
- *Cooper-Hohn v Hohn* [2014] EWHC 4122 (Fam)
- *JL v SL (No.2)* [2015] EWHC 360 (Fam)
- *Timing §49 to 54*
- *Rossi v Rossi* [2006] EWHC 1482 (Fam)
- *Kan v Poon* FACV20/2013, (2014) 17 HKCFAR 414
- *SK v WL* [2010] EWHC 3768 (Fam)

See Miller v Miller ; *McFarlane v McFarlane [2006] 2 AC 618 [26]:*

> *"valuations are often a matter of opinion on which experts differ. A thorough investigation into these differences can be extremely expensive and of doubtful utility". I understand, of course, that the application of the sharing principle can be said to raise powerful forces in support of detailed accounting. Why, a party might ask, should my "share" be fixed by reference other than to the real values of the assets? However, this is to misinterpret the exercise in which the court is engaged. The court is engaged in a broad analysis in the application of its jurisdiction under the Matrimonial Causes Act, not a detailed accounting exercise. As Lord Nicholls said, detailed accounting is expensive, often of doubtful utility and, certainly in respect of business valuations, will often result in divergent opinions each of which may be based on sound reasoning. The purpose of valuations, when required, is to assist the court in testing the fairness of the proposed outcome. It is not to ensure mathematical/accounting accuracy, which is invariably no more than a chimera. Further, to seek to construct the whole edifice of an award on a business valuation which is no more than a broad, or even very broad, guide is to risk creating an edifice which is unsound and hence likely to be unfair. In my experience, valuations of shares in private companies are among the most fragile valuations which can be obtained."*

G v T Paras 39 to 48 are the core ones to read if you read nothing else.

> 39. *The Authorities*. I have also carefully considered the several recent authorities about the approach to be taken when attempting to place a value upon a private company for the purposes of a financial remedies application, when there is no evidence that the company is in the throes of sale. Those authorities now firmly take their cue from the decision of Moylan J (as he then was) in *H v H [2008] 2 FLR 2092 where he*

pointed to the fact that the fact that the vulnerability of such valuations had been specifically recognised by the House of Lords in Miller v Miller; McFarlane v McFarlane: [2006] UKHL 24, [2006] 1 FLR 1186. He said:

> 5. The experts agree that the exercise they are engaged in is an art and not a science. As Lord Nicholls said in *Miller v Miller* ; *McFarlane v McFarlane [2006] 2 AC 618 [26]: "valuations are often a matter of opinion on which experts differ. A thorough investigation into these differences can be extremely expensive and of doubtful utility". I understand, of course, that the application of the sharing principle can be said to raise powerful forces in support of detailed accounting. Why, a party might ask, should my "share" be fixed by reference other than to the real values of the assets? However, this is to misinterpret the exercise in which the court is engaged. The court is engaged in a broad analysis in the application of its jurisdiction under the Matrimonial Causes Act, not a detailed accounting exercise. As Lord Nicholls said, detailed accounting is expensive, often of doubtful utility and, certainly in respect of business valuations, will often result in divergent opinions each of which may be based on sound reasoning. The purpose of valuations, when required, is to assist the court in testing the fairness of the proposed outcome. It is not to ensure mathematical/accounting accuracy, which is invariably no more than a chimera. Further, to seek to construct the whole edifice of an award on a business valuation which is no more than a broad, or even very broad, guide is to risk creating an edifice which is unsound and hence likely to be unfair. In my experience, valuations of shares in private companies are among the most fragile valuations which can be obtained."*

40. More recently in *Versteegh v Versteegh* [2018] EWCA Civ 1050, Lewison LJ explained in a little more detail the reasons why Moylan J's rationale in the former case was a sound one. He said:

> 185. The valuation of private companies is a matter of no little difficulty. In *H v H [2008] EWHC 935 (Fam), [2008] 2 FLR 2092* Moylan J said at [5] that "valuations of shares in private companies are among the most fragile valuations which can be obtained." The reasons for this are many. In the first place there is likely to be no obvious market for a private company. Second, even where valuers use the same method of valuation they are likely to produce widely differing results. Third, the profitability of private companies may be volatile, such that a snapshot valuation at a particular date may give an unfair picture. Fourth, the

difference in quality between a value attributed to a private company on the basis of opinion evidence and a sum in hard cash is obvious. Fifth, the acid test of any valuation is exposure to the real market, which is simply not possible in the case of a private company where no one suggests that it should be sold. Moylan J is not a lone voice in this respect: see *A v A* [2004] EWHC 2818 (Fam), [2006] 2 FLR 115 at [61] – [62]; *D v D* [2007] EWHC 278 (Fam) *(both decisions of Charles J)."*

41. Subsequently, in *Martin v Martin* [2018] EWCA Civ 2866, Moylan LJ, as he now his, returned to the theme and analysed how the court should look to utilise these valuations once they have been received and determined. He said:

93. How is this to be applied in practice? As referred to by both King LJ and Lewison LJ [in *Versteegh*], the broad choices are (i) "fix" a value; (ii) order the asset to be sold; and (iii) divide the asset in specie:…The court has to assess the weight which can be placed on the value even when using a fixed value for the purposes of determining what award to make. This applies both to the amount and to the structure of the award, issues which are interconnected, so that the overall allocation of the parties' assets by application of the sharing principle also effects a fair balance of risk and illiquidity between the parties. Again, I emphasise, this is not to mandate a particular structure but to draw attention to the need to address this issue when the court is deciding how to exercise its discretionary powers so as to achieve an outcome that is fair to both parties. I would also add that the assessment of the weight which can be placed on a valuation is not a mathematical exercise but a broad evaluative exercise to be undertaken by the judge.

94. …The need for this approach derives from the fact that, as said by Lewison LJ, there is a

"difference in quality" between a value attributed to a private company and other assets. This is a relevant factor when the court is determining how to distribute the assets between the parties to achieve a fair outcome.

95. It might be said… that it would be unfair to award one party all the "upside" in the event that the valuation proves to have been an under-estimate. That, however, is intrinsic in an asset being volatile. There is potential for the value to

increase as well as decrease. If one party is not participating in that risk and is obtaining what Thorpe LJ referred to in *Wells v Wells* as a secure result, one aspect of achieving that result is that, because they don't have the burden of the risk of a decrease in value, they also don't have the benefit of an increase in value…

96. …it is all about weight and balance. Not placing undue weight on a valuation and seeking to achieve a fair balance of risk between the parties in the allocation of the assets.

42. So too in this case, I remind myself that there is no certainty at present what the economic future of the planet will hold, in the short or medium term. The husband's evidence has been that, since the last company figures were received in October 2019, the asset value of the company had first risen sharply, to the tune of more than £50m, but then fallen back to a figure now which is probably less if anything than it was in June 2019. That he had not disclosed the fact of the original rise may fairly be the subject of criticism, regardless of the precise wording of the PTR order of Holman J, but of more import is the fact that, by fixing a price for the assumed value, there is no likelihood that that creates prejudice for either party in particular.

43. It is also right that, given that the value put forward by Ms Hall is one based on the NAV of the company, the court can be certain that is accurate as at the date that it is taken. The only question is as to alternative methodology, and that renders this valuation perhaps more robust than those based on uncertain forecasts predicated upon past performance.

44. I would also stress that in this case, I am not faced with a 'bracket' for valuations provided by the experts. Ms Hall's is the only expert valuation before me. Mr Webster's brave attempt to apply her rejected methodology to more recent figures is worthy of consideration, but must inevitably come with considerably less weight. In this regard, Moylan LJ continued in *Martin* as follows:

97. I have not yet addressed one key aspect of Mr Marks' submissions, namely that a judge should adopt a conservative figure when fixing the value of shares in a private company. I am acutely aware of the importance of reducing scope for argument and "the need for clear guidance", as I mentioned in *Hart v Hart*, at [97]. However, as Lord Nicholls said in *White v White*, at p. 612 G, as "with so much

else in this field, there can be no hard and fast rule". I do not consider it appropriate to seek to limit or direct where in a bracket a judge should alight…As I have already said, it is the use which is made of such valuations which is of critical importance.

45. It follows from the above that I accept in the circumstances Ms Hall's methodology and valuations at various points in time as being the safest and most reliable available to me, and that the husband's shares in B Ltd will therefore be considered at their NAV for the purposes of determining the outcome of this case, rather than as calculated by any other method. However, the issue of determining a fair value does not end there, as there remains another matter of key importance, which is the date at which the value of the husband's shareholding should be calculated.

46. In *Hart v Hart* [2017] EWCA Civ 1306, Moylan LJ dealt with the approach which the court should take in determining what property should and should not be included as property which is subject to the sharing principle. He said:

67. The exercise on which the court is engaged, when applying the sharing principle… is …to determine whether the current assets owned by the parties …comprise the product of marital endeavour. The court must then decide how that determination should impact on the court's award…

…

84. In my view, the court is not *required* to adopt a formulaic approach either when determining whether the parties' wealth comprises both matrimonial and non-matrimonial property or when the court is deciding what award to make. This is not necessary in order to achieve "an acceptable degree of consistency", Lord Nicholls in *Miller* (paragraph 6), or to achieve a fair outcome…

85. It is, perhaps, worth reflecting that the concept of property being either matrimonial or non-matrimonial property is a legal construct. Moreover, it is a construct which is not always capable of clear identification. …When property is a combination, it can be artificial even to seek to identify a sharp division because the weight to be given to each type of contribution will not be susceptible of clear reflection in the asset's value. The exercise is more of an art than a science.

86. In my view, the guidance given by Lord Nicholls in *Miller* remains valid today and, indeed, bears increased weight in the light of the courts' experience since that case was decided. It can, as he said, be artificial to attempt to draw a "sharp dividing line". Valuations are a matter of opinion on which experts can differ significantly. Investigation can be "extremely expensive and of doubtful utility". The costs involved can quickly become disproportionate. Proportionality is critical both because it underpins the overriding objective and because, to quote Lord Nicholls again: "Fairness has a broad horizon"…

47. This was later taken up by King LJ in *Versteegh*, when she said:

90. Wilson LJ (as he then was) in giving judgment in *Jones* was by no means blind to the limitations inherent in his choice of the arithmetical route saying:

"[35]… Criticism can easily be levelled at both approaches. In different ways they are both highly arbitrary. Application of the sharing principle is inherently arbitrary; such is, I suggest, a fact which we should accept and by which we should cease to be disconcerted. "

…

93. In *Goddard-Watts v Goddard-Watts* [2016] EWHC 3000 (Fam) Moylan J took issue with the use of the word 'arbitrary' in relation to the judicial decision making process saying:

"…. Wilson LJ said in *Jones*…. "Application of the sharing principle is inherently

arbitrary". Whilst I am not entirely happy with the concept that that sum I award to reflect these factors is arbitrary, I take it that Wilson LJ meant discretionary rather than susceptible to the application of a precise formula."

94. In my judgment it is however the observation of Lord Nicholls in *Miller and McFarlane*

[2006] UKHL 24;[2006] 1FLR 1186 which continues to carry the day:

"[26] This difference in treatment of matrimonial property and non-matrimonial property might suggest that in every case a clear and precise boundary should be drawn between these two categories of property. This is not so.

[27] Accordingly, where it becomes necessary to distinguish matrimonial property from non-matrimonial property the court may do so with the degree of particularity or generality appropriate in the case. The judge will then give to the contribution made by one party's non-matrimonial property the weight he considers just. He will do so with such generality or particularity as he considers appropriate in the circumstances of the case.

48. Further, in the case of *Martin*, Moylan LJ also said this:

113. In conclusion, a judge has an obligation to ensure that the method he or she selects to determine this issue leads to an award which, to quote Lord Nicholls in *Miller; McFarlane*, at [27], the judge considers gives "to the contribution made by one party's non-matrimonial property the weight he considers just … with such generality or particularity as he considers appropriate in the circumstances of the case". This provides the same perspective as Wilson LJ's observation in *Jones v Jones* about "fair overall allowance", at [34]. This was why Holman J was entitled in *Robertson v Robertson* to reject the "accountancy" approach, not only because it seemed unfair to the husband, but because he did not consider that this fairly reflected the relevant considerations in the "overall exercise of (his) discretion", at [59]. Both of the latter cases concerned the development of trading companies and, in my view, these observations apply with particular force in such circumstances.

…

115. Finally, on this question, I mention briefly that the manner in which the court determines whether property is or is not matrimonial can probably be described as partly evaluative and partly discretionary. …the exercise is clearly at least in part evaluative because it is based on the court's assessment of the evidence as to whether the relevant asset is from a source external to the marriage or the product in part or in whole of marital endeavour. But I also consider that it can be partly discretionary for the reasons set out in paragraph 113 above.

Date for valuation

- *End June 2017 shares 12.52 June 2018 17.058 added £12.7M to the value of H shares*
- *Note separated in October/November 2017*
- *£6M question what date should be used*

- *Cooper-Hohn v Hohn* [2014] EWHC 4122 (Fam)
- *JL v SL (No.2)* [2015] EWHC 360 (Fam)
- *Rossi v Rossi* [2006] EWHC 1482 (Fam)
- *Kan v Poon* FACV20/2013, (2014) 17 HKCFAR 414

The summary of the principles provided in *Rossi v Rossi* is broader than Thorpe LJ's stricter approach [in *Cowan*] and is, in my view, preferable. It points to various factors relevant to deciding whether a post-separation accrual justifies departure from equality, including the length of the marriage and separation, the nature of the property accruing and the means or efforts by which it was acquired, and so forth.

Miller; McFarlane, at [27], the judge considers gives "to the contribution made by one party's non-matrimonial property the weight he considers just … with such generality or particularity as he considers appropriate in the circumstances of the case.

July 2021

Michael George

Barrister
3PB Barristers

0330 332 2633
michael.george@3pb.co.uk

3pb.co.uk