



Is Your Business Safe From a Divorce?

What you need to know about shareholder, partnership, and buy-sell agreements.

BY TAYLOR IMEL

Texas is a good place to do business. No corporate or individual income tax and a simplified regulatory system have made Texas a haven for small-business owners and entrepreneurs. According to the U.S. Small Business Administration, Texas small businesses employed roughly 4.7 million people in 2015, or 45.6% of the private workforce in the state. Often, the ownership interests of these small businesses account for the largest asset of a Texas family both in terms of value and the income generated from the same—which is why they are some of the most highly contested issues in a divorce suit.

Is a business owner's interest in his or her company protected from the warring spouse? The answer is complicated. More often than not, the actual interest in the company or partnership is protected from disposition to the other spouse by the various entity agreements. But, are the provisions in these entity agreements

sufficient in the event of a divorce, particularly the valuation of the community estate's interest in the corresponding entity?

The law is unclear on this matter. Texas appellate courts are split on the controlling nature of such agreements, and the Texas Supreme Court has yet to weigh in on the issue.¹ However, despite the apparent conflict, each appellate decision seems to indicate that entity agreements containing buy-sell provisions specifically providing for valuation of the partner/shareholder's interest in the event of a divorce may in fact be binding on the non-owner spouse, provided that the triggering event has occurred and the provisions regarding valuation have been followed by each shareholder/partner on a consistent basis.

But divorce provisions in such agreements often have not been drafted correctly to bind the non-owner spouse to the agreement. Most fail to define when

the divorce provisions are actually triggered (i.e., upon the filing of a divorce), and many include inappropriate standards of value that are either outdated or are designed to deprive the non-owner spouse of a fair value. While no Texas court has to date clearly outlined the requirements for binding a non-owner spouse to a buy-sell agreement in the event of a divorce, extraordinary care should be taken when incorporating divorce provisions in such agreements to best ensure their enforceability and to prevent costly litigation.

Divorce is a reality for nearly half of all families in the U.S. For a small-business owner, the divorce process can severely disrupt the ongoing nature of the business. Formal valuations and forensic analysis of the financials of a closely held company or partnership during a divorce are invasive, time-consuming, and expensive. Given the split nature of the appellate courts in Texas, it is essential that divorce provisions are not an afterthought in the drafting of buy-sell and other entity agreements. Consulting with a family law practitioner adept at reviewing and crafting such provisions could potentially save tens of thousands of dollars in future legal fees and greatly reduce the overall instability and disruption to a business during a divorce. **TBJ**

NOTE

1. See, e.g., *Finn v. Finn*, 658 S.W.2d 735, 742 (Tex. App.—Dallas 1983, pet. denied) (finding that the buy-sell provisions in the partnership's agreement were binding on the non-owner spouse as to division of corporate goodwill); *Keith v. Keith*, 763 S.W.2d 950 (Tex. App.—Fort Worth 1989, no writ) (holding that the buy-sell provisions of a partnership agreement that were silent as to divorce were not controlling on the non-owner spouse); *Von Hohn v. Von Hohn*, 260 S.W.3d 631 (Tex. App.—Tyler 2008, no pet.) (same); *Mandell v. Mandell*, 310 S.W.3d 531 (Tex. App.—Fort Worth 2010, pet. denied) (holding that specific divorce buy-sell provisions in a stock purchase agreement were binding on the shareholder's spouse).



TAYLOR IMEL

practices family law at KoonsFuller in Houston, where she focuses on complex property division and highly contentious custody cases, both at the trial court and appellate levels. She is certified in family law by the Texas Board of Legal Specialization.