Prenuptial Agreements and Postnuptial Agreements -

Two Forensic Accounting Issues - Let the Lawyer Beware

Prior to marriage or during a marriage, the two future spouses or married spouses may choose to execute a prenuptial agreement, a post nuptial ag reeme nt or neither of these two agreements.

A **prenuptial agreement** is an agreement made before marriage, usually to resolve issues of support and property division if the marriage ends in divorce or by the death of a spouse.

A **postnuptial agreement** is an agreement entered into during marriage to define each spouse 's property rights in the event of death or divorce. The term commonly refers to an agreement between spouses during the marriage at a time when separa tion or divorce is not immine nt.

**Marital property** is property that is acquired during the marriage and that is subject to distribution or division at the time of marital dissolution. Generally, it is property, except gifts and inheritances, acquired after the date of marriage and before a spouse files for divorce. A prenuptial agreement or a post nuptial agreeme nt ca n a lte r t he general treatment of designa ted assets and liabilities at divorce.

Notwithstanding the social interpretation that prenuptial agreements and postnuptial agreements are unromantic, these agreements attempt to deal with the financial issues in the marriage. Marriage is, among, hope fully, many other thing s, an eco nomic partnership between the spouses. In the writing and execution of prenuptial agreements and postnu ptial agreements, a myriad of legal issues are involved. Both parties need to be represented by family law attorneys. A sizable number of financial, accounting, and tax issues are also involved. Both parties need to be represented by acco untants who are well versed in those non-legal iss ues .

T his article discusses two such non-lega l issues that should be addressed before either a prenuptial agreement or a postnuptial agreement is signed. Issue number one is identifying and accounting for all the assets and liabilities to be designated as either separate to each party or earmarked according to the agreement of the partie s. Issue number two is determining the fair market value of all assets and liabilities either as of the incep tion of the marriage in the case of prenuptial agreements or at a designated time during the marriage in the case of a postnuptial agreement.

## Identifying and Listing Assets and Liabilities

All assets and liabil ities for which each propertied spouse (or future propertied spouse) is respons ible must be delineated. The details are to be listed as of a certain date. For those

assets where the propertied spouse (or future propertied spouse) is a partia l owner, the percentage of ownership should be established.

**ASSETS**

I - Cash on hand - Count the cash, if signi ficant, and sign off on the amount.

1. - Bank accounts - Named owner(s), name of financial institution, account number, and balance of each account
2. - Securities accounts - Named owner(s), name of financial ins titution, account number, and balance of each account
3. - Collectibles - Itemized description, quantity of each identifiable item, and original cost
4. - Loans receivable - Named creditor(s), name of debtor(s), terms including interest rate, payment frequency, and repayment schedule
5. - Real estate - For each parcel: Title holder(s), date of purchase, and original cost
6. - Other valuable personal possessions - Detailed listin g, owner(s), dates of purchase, original cost
7. - Equity in private ly owned businesses - List of equity owners and their percentage ownership, future spouse's date of acquisition, and acquisition cost
8. - Educational degrees and licenses - Narrative of educational history and career history IO - Pat e nts, trademarks, literary works, and other intellectual property - Details of each item such as acquisition costs and the acquisition process

11 - Celebrity goodwill - Brief narrative as to history of development of this asset

# LIABILITIES

Pre pare a detailed list of all relevant liabilities, such as unpaid bills, unsecured loans, mortgag es, contingent liabilities (pending litigation , loan guaranties, etc.) The details will include date the party became indebted, payment terms, and all other pertinent details.

## Calculating the Inception Fair Market Value of Assets and Liabilities

The fair market value of each asset and liability as of a certain beginning date for purposes of the prenuptial or postnuptial agreement forms the base for future calculations of marital value. These values will enable an expert at a future date, if necessary, to assist attorneys in establis hing the value of the components of the marital estate. That is, the "down-the-road" values of the components of the marital estate will be affected by the beginnin g values as originally established by the expert pursuant to the prenuptial or postnuptialagreement.

# ASSETS

1. - Cash on hand - The fair market value equals the actual counted amount.
2. - Bank accounts - The fair market value equals the actual balances in the accounts.
3. - Securities accounts - In most cases, the financial institutions will provide the market value of publicly traded securities. In those cases where the fair market value of one or more securities or investments is not readily available, the forensic accountant in his/her role of professional valuation expert will be available to estimate that value.
4. - Co llectibles - Specific appraisers may need to be hired to estimate the value of each collectible. In some cases, reference books or Internet data are available.
5. - Loa ns receivable - The forensic accountant as valuation expert should be engaged to estimate the value of these asse ts. T he expe rt must utilize app ropr iate methodology, which includes, among other things, comparing the stated interest rates to comparable market interest rates as well as asce1t aining the extent of bad debts or doubtful collectibility.
6. - Real estate - Real estate appraisers should be engaged to estimate the value of each parcel of real estate.
7. - Other valuable personal possessions - Other appraisers, such as fine arts appraisers, may be needed. The forensic accounta nt may be needed to estimate the value if specific appraisers cannot be located.
8. - Equity in privately owned businesses - The forensic accountant, as business valuator, must be engage d to estima te the fair market value of these assets . The methodology to be utilize d will vary fro m entity to entity depending upon the industry, the availability of data, the accuracy of data, and the availa bili ty of market comparable data. Sometimes the expert will discover hidden assets, including other businesses, during the performance of analytical procedures as part of the methodology in estimating the fair market value of a privately owned business.
9. - Educat ional degrees and lice nses - In New York State, enhanced earning capacity is

sti ll a marital asset. The forensic accountant will provide a viab le estimate of fair market value.

1. - Patents, trademarks, literary works, and other intellectual property - These intangible assets present valuation cha llenges . It is important to engage the services of a valuator, such as the writer of this article, who has specific experience estimating the value of intellec tual property. Some of the most challengi ng assig nments will be to value these asse ts.
2. - Celebrity goodwill - This asset was defined by Justice David B. Saxe in the Mann v. Mann case in 1995 . " As applied to an individual, it is frequently understood to mean the good reputation of the individual in that business or profession so that future business will probably continue to be generated by that indi vidual." Once it is es tab lished that the individual is a celebrity, it is important to address the value at the outse t. The valuation methodology will vary from case to case. Several of our fi rm' s professionals are equipped to estimate the fair market value of this asset.

# LIABILITIES

The fair market value of the liabilities must be determined. The fair market value of current liab ilities , those that will be paid in full generally within twelve months, will be their book value adjusted for accuracy. Regarding long-term debt, it would be a mistake to accept the book value as the fai r market value. Adjustments need to be made to book value of long-term loans based upon the loans' actual interest rates in comparison with

current market interest rates. The forensic accountant as valuator will utilize market data and analytical procedures in order to make the appropriate adjustments and render an opinion as to the fair market value of each liability.

As has been briefly narrated, identifying each of the assets and liabilities in a particular case and establishing their individual fair market value should not be undertaken without the assistance of accounting experts who are trained and experienced in identifying, locating, and valuing all varieties of assets and liabilities, both tangible and intangible.