Sharland: the end of the cheat's charter?

Business valuation is not an exact science. As Lord Nicholls of Birkenhead said in the Miller and McFarlane cases:

> "*[D]etailed accounting is expensive, often of doubtful utility and, certainly in respect of business valuations, will often be based on divergent opinions each of which may be based on sound reasoning.*"

I console myself in the knowledge that, before his retirement, Lord Nicholls did not have the pleasure of experiencing one of FAR's accounting reports – which as any reader will attest are consistently of valuable utility (and are certainly not expensive).

Any business valuation can only be as good as the information on which it relies. The accounting records – principally reflected by the annual financial statements – do not convey the whole story. In order to try and reflect the true value of a business it is important to fully understand its context, prospects and the drivers that underpin it; such as specific issues in the industry sector, competitive forces, the performance of and relationships with key suppliers and customers, product life cycles, key long term contracts, the worth and abilities of the management team, succession management ..... The list goes on.

Many of these issues cannot be objectively corroborated; whilst there is clearly a skill in asking the right questions, the valuer is reliant on the business owner relaying the true facts to him. However, as forensic accountants instructed in matrimonial matters, our valuations are most often in situations where the worth of the shareholding is in dispute, or at least not agreed. In such cases, the business owner may have what I will politely refer to as an "agenda".

In recent years, there have been matrimonial cases that have been perceived as endorsing a "cheat's charter". In its 2010 decision in *Imerman v Tchenguiz*, the Court of Appeal concluded that wives were no longer free to rummage through their husbands' financial papers to check and see whether they were lying. Later, in the Anglo-Nigerian case of *Petrodel v Prest*, the Supreme Court provided comfort for those whose wealth is tied up in complex off-shore structures. This created an environment whereby a divorcing business owner might have felt legitimised in hiding his assets.

Nevertheless, the recent case of *Sharland*, which has grabbed a lot of headlines recently, suggests that the tide is turning.

I am sure that the facts are familiar to most but in (very brief) summary, the husband (H) was a successful software entrepreneur. At a financial proceedings hearing in July 2012, he declared that there were no plans for an Initial Public Offering "on the cards for today", and a deal was brokered between H and W relating to the value of his shareholding. It later came to light that he had misled the Court, and that H had in fact been liaising with a number of investment bankers and exit plans had been in full swing when he gave his evidence.

The Supreme Court recently held that this was a fraudulent misrepresentation by H, which led W to compromise her claim for financial remedies – and the case should be returned to the family court for further directions.

As it turned out, the IPO did not proceed; it may transpire that the value ascribed to the shares at the hearing was there or thereabouts. Nevertheless, that fact alone does not negate H's lie.

There was some fear that such a ruling in favour of W would lead to an opening of the floodgates; and that a whole raft of financial settlements reached over the years will be re-appraised.

The Sharland case involved a clear instance of deliberate misrepresentation. Almost as a matter of policy, the Court held that this should prompt a reappraisal. The only exception to this general rule would be in circumstances where the fraud would not have influenced a reasonable person in agreeing consent – and the Court directed that the onus was on the deceitful H to demonstrate this. Notably, in the *Gohil* case that was heard on a parallel basis to Sharland, the Court clarified that if the misrepresentation was accident or negligent, then this might still justify the order being set aside; although in those circumstances, the burden would fall on W to demonstrate that the misrepresentation was sufficiently material.

It is difficult to conceive of a scenario whereby H would deliberately mislead the Court if the underlying misconception was immaterial to the financial appraisal. Why otherwise take the risk? Consequently, there must be a strong presumption that a fraudulent declaration will lead to the matter being reheard. Moreover, if the representation was material to valuation, then I find it hard to think of circumstances where it would have been omitted or negligently mis-stated. Might this suggest that a material mis-declaration is likely to be have been made deliberately? Only time will tell.

This, of course, could all be great news for forensic accountants. We sit by our phones, calculators poised, waiting for the call; ready to reperform valuations initially completed years ago, or perhaps asked to assess whether a misrepresentation might be material to the valuation.

However, we must be wary. Just because W made what appears with the benefit of hindsight to be a bad bargain does not necessarily justify a re-opening of the envelope.

'Hindsight' is something we perpetually grapple with when providing valuation evidence and advice. In the context of litigation, we are often asked to comment on valuation retrospectively – although there is a convention that events arising in the post-valuation period should not ordinarily be taken into account. Nevertheless, a useful comment on hindsight was contained in *Trustees Executors and*

Agency Co Ltd v Federal Comr of Taxation (Victoria) (1941) 65 CLR 33:

> *"It may be conceded that the calculation of duty on the deceased's estate is not controlled by events subsequent to the death of the deceased, but subsequent events may be taken into account as evidence of what were the facts at the date of the testator's death."*

Whilst this was an Australian case unrelated to divorce, the principle made is an interesting one. Consider the following scenarios:

- A share transaction made at an increased value in the months following the settlement;
- The reported profits of the business in the year of the settlement (or the following year) being markedly higher than had been previously "forecast".

If these issues arose as a consequence of matters that should reasonably have been foreseeable at the time of the settlement, had H provided full and honest disclosure, then under the *Sharland* principle it may be possible to re-open the valuation. We can provide assistance in this regard; providing a discrete assessment of the change in the underlying metrics, and whether that should have been reflected in the earlier valuation.

The Supreme Court has set a very clear marker regarding honest declarations in matrimonial proceedings, and this is a stern warning to any party not being entirely sincere (including when dealing with their advisers). Whilst it might not open the floodgates as feared, it should act as a strong deterrent.