



Valuation Issues Surrounding Professional Practices at Divorce, by Steve McDonough, Esq.

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When a divorcing spouse owns a business, several factors must be examined as part of the distribution of the marital estate. The type of business entity in question will obviously play a major role in how the business asset will be valued. One type of business that provides special challenges to an appraiser and the attorneys on the case is a professional practice, such as a medical practice or law firm.

A professional practice is considered by the court (at least here in Massachusetts) as subject to division as part of the marital estate during the divorce process. *See Goldman v. Goldman, 28 Mass. App. Ct. 603, 613 (1990).*

Although the confidential relationship between professionals and their clients must be protected, the amount of fees paid and accounts receivables due to the professional practice are not protected. For example, a 1994 case found a lawyer in trouble for failing to disclose the value of a large number of potentially fee-producing cases in his own small law practice during his own divorce.

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Discovery

It is important to collect information about a professional practice similar to any other owned business during a divorce case, thus counsel for the non-business owning spouse will want to obtain items such as:

- Financial Statements for the business;
- Tax returns;
- List of assets owned by the practice, including equipment, accounts receivable, work in progress, automobiles, investments, and the value of goodwill the business has cultivated;
- Financial Records, including bank statements;
- Information about real estate owned by the practice;
- Information on life insurance policies insuring the lives of the principals or the practice;
- Copies of all partnership agreements or other corporate documents;
- Buy-Sell agreements between partners, if any.

Once the different assets belonging to the business are identified, they must be valued. Tangible assets are normally valued at fair market value, while accounts receivables are discounted based upon their collectability. Any unbilled time must also be added to the balance sheet. Patient or client files can also have a value, mainly to determine the number of ongoing clients.

Goodwill Hunting

Perhaps the most vexing issue relates to the determination of whether goodwill is present in the practice, and then how to establish its value if it in fact exists.

Goodwill is the probability that clients will return to the same practice for future business. Valuing goodwill is not a simple task, and factors ranging from the

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professional's earning capacity and reputation in the community to the length of time the business has operated must be weighed. Additionally, there are even different types of goodwill.

Enterprise goodwill relates to the intangible value in the form of profit that would be available to a prospective buyer. This should be contrasted with *personal goodwill*, which is the total of numerous personal attributes, such as character, age, education, and performance that later develop into a professional reputation. Personal goodwill is specific to an individual, so it cannot be transferred to a potential purchaser.

An expert business appraiser should examine these factors in detail, a number of theories and formulas are employed to determine the value of goodwill. Professional business evaluations can quickly get expensive. There are many variables and subjective factors that can lead to disagreements and competing experts making the valuation of a professional practice a complicated part of property division during a Massachusetts divorce.

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