Valuation Considerations for Premarital Agreements

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Premarital, or "antenuptial," agreements are often developed in a marital setting to establish financial terms regarding the division of assets upon divorce. Such agreements often arise in circumstances when a couple (1) brings children from a prior marriage, (2) has inheritance considerations, or (3) is dealing with a family-owned business. Required financial disclosure obligations of parties considering a premarital agreement vary by jurisdiction. The potentially complex nature of such obligations, and the complexity involved in developing such agreements, requires experienced legal counsel, and often the services of qualified valuation analysts, in order to produce a legally enforceable document.

Introduction

With the divorce rate in many parts of the country over 65 percent when individuals with multiple marriages are included, many people are re-examining the value of a premarital agreement in their personal and business planning. These agreements are also sometimes called "prenuptial" or "antenuptial" agreements. A premarital agreement is particularly helpful when there are children from a prior marriage, when inheritance is a mutual goal for both parties, or when ownership of a family business is involved.

The popular belief is that these agreements are not legally enforceable except when a spouse dies. Nothing could be further from the truth. In most states, these agreements, if properly drafted and negotiated, are legally enforceable in the context of a divorce, too.

In summary, generally there are four requirements under law for a premarital agreement to be valid:

1. It has to be in writing.
2. It has to be read and understood by each spouse.
3. Certain states require each spouse to have his or her own lawyer.
4. There has to be a "fair and reasonable" or a "full and fair" disclosure of each spouse's assets.

It is also a good idea to start the process of addressing a premarital agreement early in the planning stages. It does not need to take a long time to conclude.

Most couples will want to get these legal formalities finalized well before the more traditional aspects of the wedding and marriage begin. Also, the process of negotiating the premarital agreement is sometimes very helpful in allowing the individuals to focus on what is important in their relationship. After the agreement is signed, many couples feel the process was very constructive, and in fact, strengthened their relationship and helped increase confidence in their future spouse.

This discussion will focus primarily on the financial disclosure obligation required in premarital agreements. The disclosure obligation is not a cut-and-dried issue. Instead, the disclosure obligation has been the subject of litigation in numerous state courts.

Furthermore, state laws vary significantly regarding the disclosure obligation. For example, some states permit a spouse to make a voluntary waiver

of a full disclosure of assets. However, other states do not allow waivers.

Also, certain states require a "fair and reasonable" disclosure of assets while other states require a more stringent "full and fair" disclosure of assets. These seemingly slight but legally significant alterations in state statutes can make a world of difference when negotiating a premarital agreement between parties.

The Uniform Premarital Agreement Act

For simplicity and uniformity, the National Conference of Commissioners on Uniform State Laws promulgated the Uniform Premarital Agreement Act ("UPAA") in 1983. Currently, some form of the UPAA has been adopted by 26 states and the District of Columbia. The exact language of the disclosure obligation under the UPAA is provided under Section 6(a)(2) of the Act.

The relevant part of Section 6 provides as follows:

> Section 6. Enforcement.
>
> (a) A premarital agreement is not enforceable if the party against whom enforcement is sought proves that:
>
> (1) that party did not execute the agreement voluntarily; **or**
>
> (2) the agreement was unconscionable when it was executed **and**, before execution of the agreement, that party:
>
> (i) was not provided a *fair and reasonable disclosure* of the property or financial obligations of the other party;
>
> (ii) did not voluntarily and expressly waive, in writing, any right to disclosure of the property or financial obligations of the other party beyond the disclosure provided; and
>
> (iii) did not have, or reasonably could not have had, an adequate knowledge of the property or financial obligations of the other party. [Emphasis added]

Under the UPAA, a spouse must fairly and reasonably disclose his or her property holdings and financial obligations if the spouse wishes to be able to enforce an agreement against the other spouse, unless there is a voluntary and express waiver of the other spouse's disclosure rights. If there is not a fair and reasonable disclosure, however, actual knowledge by the other spouse at the time of the agreement would still permit enforcement on these grounds. Further, if disclosure is defective, the agreement must be unconscionable, as well, to preclude enforcement on these grounds.

While certain states have chosen to adopt some form of the UPAA, almost half of the states have chosen to *not* adopt the Act. Instead, those states have chosen to rely on common law or have crafted their own premarital agreement laws and disclosure obligations which the state believes fits the needs of its jurisdiction.

Further, even the states that have adopted the UPAA have modified the original Act to meet the needs of the particular state. Accordingly, uniformity among the states has not been achieved.

Disclosure Obligations by Jurisdictions

Exhibit 1 identifies the jurisdictions that have chosen to adopt the UPAA (26 states and the District of Columbia), and it also indicates whether the state has chosen to modify the disclosure obligations for premarital agreements under its particular UPAA statute.

For those jurisdictions that have chosen not to adopt the UPAA (24 states), the exhibit indicates the jurisdiction's disclosure obligation for premarital agreements as well as the applicable law setting forth the standard.

While a majority of jurisdictions require a "fair and reasonable" disclosure of each party's assets as contemplated by the UPAA, a number of jurisdictions, as indicated in the exhibit, have chosen to adopt the more stringent standard of "full and fair" disclosure in premarital agreements.

"Full and Fair" Disclosure

A number of states have chosen to adopt a "full and fair" disclosure standard as opposed to the "fair and reasonable" standard promulgated under the UPAA. While the concept of "full and fair" disclosure is interpreted differently by state courts, it generally requires that each party be given a clear idea of the nature, extent, and value of all the other party's assets.

The standard of "full and fair" disclosure will give the other party the ability to make an informed decision as to everything that may be relinquished or foregone as a result of entering into the premarital agreement.

Exhibit 1
Adoption of the Uniform Premarital Agreement Act ("UPAA")

States	Adoption of UPAA	Disclosure Requirements	Citation
Alabama	No	Alabama requires a person seeking enforcement to show that the entire transaction was fair, just and equitable **or** that the agreement was freely and voluntarily entered into with knowledge of the opposing side's interest in the estate and its approximate value.	*Barnhill v. Barnhill*, 386 So.2d 749 (Ala. App. 1980)
Alaska	No	Alaska generally follows the UPAA by requiring fair and reasonable disclosure of the property or financial obligations of the other party.	*Brooks v. Brooks*, 733 P.2d 1044 (Alas. 1987)
Arizona	Yes	Same as UPAA.	Arizona Revised Statutes § 25-202
Arkansas	Yes	Arkansas follows the UPAA, however, the state requires that if there was no financial disclosure, the party who did not get the disclosure must have *consulted with an attorney* before waiving the right to the disclosure.	Arkansas Code § 9-11-406
California	Yes	California requires that the party must have been provided "fair, reasonable and *full* disclosure of the property or financial obligations of the other party." This varies from the UPAA in that the UPAA requires only "fair and reasonable disclosure."	California Family Code § 1615
Colorado	No	In Colorado, a party has adequate financial disclosure under its statute if the party received a reasonably accurate description and good-faith estimate of value of the property, liabilities, and income of the other party **or** has adequate knowledge of the information.	Colorado Revised Statutes § 14-2-309
Connecticut	Yes	Connecticut does not allow for the waiver of the right to disclosure of the other party's financial information. Further, Connecticut requires that for a premarital agreement to be enforceable, the party must have been afforded a reasonable opportunity to consult with independent counsel.	Connecticut General Statutes § 46b-36g
Delaware	Yes	Same as UPAA.	13 Delaware Code § 326
District of Columbia	Yes	Same as UPAA.	District of Columbia Official Code § 46-506
Florida	Yes	Same as UPAA.	Florida Statutes § 61.079(7)

Exhibit 1 (cont.)
Adoption of the UPAA

States	Adoption of UPAA	Disclosure Requirements	Citation
Georgia	No	Georgia requires a full and fair disclosure of all material facts prior to a premarital agreement.	*Bilge v. Bilge*, 283 Ga. 65 (2008); *Scherer v. Scherer*, 249 Ga. 635 (1982)
Hawaii	Yes	Same as UPAA.	Hawaii Revised Statutes § 572D-6
Idaho	Yes	Same as UPAA.	Idaho Code § 32-925
Illinois	Yes	Same as UPAA.	750 Illinois Compiled Statutes § 10/7
Indiana	Yes	Indiana's enforcement statute only states that a premarital agreement is not enforceable if the agreement was unconscionable when the agreement was executed.	Indiana Code § 31-11-3-8
Iowa	Yes	Under the Iowa statute, unconscionability alone is adequate for a premarital agreement to be held unenforceable.	Iowa Code § 596.8
Kansas	Yes	Same as UPAA.	Kansas Statutes Annotated § 23-807
Kentucky	No	In Kentucky, a premarital agreement requires each party to fully disclose, in good faith, the amount of property each party holds.	*Daniels v. Banister*, 146 Ky. 48 (1911)
Louisiana	No	In Louisiana, very little case law exists delineating the disclosure obligations for premarital agreements. However, the case law that does exist provides that premarital agreements will be approved so long as they are not contrary to public policy.	*McAlpine v. McAlpine*, 679 So.2d 85 (La. 1996)
Maine	Yes	Same as UPAA.	19-A Maine Revised Statutes Annotated §608
Maryland	No	In Maryland, each party must have a full, frank, and truthful disclosure of the other party's assets, **or** adequate knowledge of a frank, full, and truthful disclosure of the other party's assets.	*Cannon v. Cannon*, 384 Md. 537 (2005); *Hartz v. Hartz*, 248 Md. 47 (1967)
Massachusetts	No	Massachusetts notes full and fair disclosure of each party's financial circumstances is a significant aspect of the premarital agreement.	*Dematteo v. Dematteo*, 436 Mass. 18, 762 N.E.2d 797 (2002)
Michigan	No	In Michigan, the premarital agreement must be fair, equitable and reasonable, and must be entered into voluntarily, and with full disclosure.	*Rinvelt v. Rinvelt*, 190 Mich. App. 372, 475 N.W.2d 478 (1991)

Exhibit 1 (cont.)
Adoption of the UPAA

States	Adoption of UPAA	Disclosure Requirements	Citation
Minnesota	No	For premarital agreements to be enforceable in Minnesota, there must be a full and fair disclosure of the earnings and property of each party.	Minn. Stat. Ann. § 519.11
Mississippi	No	In Mississippi, case law requires each party to a premarital agreement to disclose his or her financial assets.	*Smith v. Smith*, 656 So. 2d 1143 (Miss. 1995)
Missouri	No	In Missouri, a premarital agreement must be entered into in good faith with full disclosure.	*Ferry v. Ferry*, 586 S.W.2d 782 (Mo. Ct. App. 1979)
Montana	Yes	Same as UPAA.	Montana Code Annotated § 40-2-608
Nebraska	Yes	Same as UPAA.	Nebraska Revised Statutes § 42-1006
Nevada	Yes	Under the Nevada statute, unconscionability alone is adequate for a premarital agreement to be held unenforceable.	Nevada Revised Statutes § 123A.080
New Hampshire	No	In New Hampshire, fairness is the ultimate measure in enforcing a premarital agreement. Further, a premarital agreement is presumed valid unless it is proved that there was nondisclosure of a material fact.	*In re Estate of Hollett*, 150 N.H. 39, 834 A.2d 348 (2003); N.H. Rev. Stat. Ann. § 460:2-a
New Jersey	Yes	New Jersey requires a "full and fair disclosure of the earnings, property and financial obligations of the other party." Further, New Jersey requires that there be a statement of assets attached to the premarital agreement.	NJ Rev Stat §§ 37:2-33 & 37:2-38
New Mexico	Yes	Same as UPAA.	New Mexico Statutes § 40-3A-7
New York	No	The case law in New York provides limited guidance on the disclosure obligations of each party to a premarital agreement. However, certain cases have held that a full disclosure is not required.	*Hoffman v. Hoffman*, 474 N.Y.S.2d 621 (App. Div. 1984); *Panossian v. Panossian*, 569 N.Y.S.2d 182 (App. Div. 1991)
North Carolina	Yes	Same as UPAA.	North Carolina General Statutes Annotated § 52B-7
North Dakota	Yes	Same as UPAA.	North Dakota Statutes § 14-03.1-06
Ohio	No	Ohio case law requires a full disclosure or full knowledge, and understanding, of the value and extent of each prospective spouse's property.	*Gross v. Gross*, 11 Ohio St. 3d 99, 464 N.E.2d 500 (1984)

Exhibit 1 (cont.)
Adoption of the UPAA

States	Adoption of UPAA	Disclosure Requirements	Citation
Oklahoma	No	In enforcing a premarital agreement in Oklahoma, a court will consider whether the agreement afforded a fair and reasonable provision for a spouse and whether it provided full, fair and frank disclosure of the other spouse's worth.	*Starcevich v. Starcevich*, 2014 OK CIV APP 100
Oregon	Yes	Same as UPAA.	Oregon Revised Statutes § 108.725
Pennsylvania	No	In Pennsylvania, a premarital agreement will not be enforced unless there was full disclosure.	*Simeone v. Simeone*, 380 Pa. Super. 37 (1988), aff'd, 525 Pa. 392 (1990)
Rhode Island	Yes	Same as UPAA.	Rhode Island General Laws § 15-17-6
South Carolina	No	In South Carolina, a premarital agreement will be presumed fair if there was a full financial disclosure made by each spouse.	South Carolina Code of Laws § 20-3-630
South Dakota	Yes	Same as UPAA.	South Dakota Codified Laws § 25-2-21
Tennessee	No	Tennessee requires each prospective spouse to make a full disclosure of the nature, extent and value of property in the premarital agreement.	*Wilson v. Moore*, 929 S.W.2d 367 (Tenn. Ct. App. 1996)
Texas	Yes	Same as UPAA.	Texas Family Code § 4.006
Utah	Yes	The Utah statute contemplates that "fair and reasonable" disclosure may not be possible at times and thus adds the phrase "insofar as was possible" to the disclosure section of the statute.	Utah Code § 30-8-6
Vermont	No	For premarital agreements in Vermont, each party must provide a fair and reasonable disclosure of each party's financial status.	*Bassler v. Bassler*, 156 Vt. 353 (1991)
Virginia	Yes	Same as UPAA.	Virginia Code § 20-151
Washington	No	In Washington, a premarital agreement will be presumed fair if it provides a fair and reasonable disclosure of each party's assets.	*In re Marriage of Matson*, 107 Wash.2d 479 (1986).
West Virginia	No	West Virginia does not require the parties to a premarital agreement to execute a detailed, written disclosure of one another's assets.	*Pajak v. Pajak*, 182 W. Va. 28 (1989)
Wisconsin	No	In Wisconsin, a premarital agreement will be deemed fair if each prospective spouse made a fair and reasonable disclosure to the other of his or her financial status.	*Button v. Button*, 131 Wis.2d 84 (1986)

Exhibit 1 (cont.)
Adoption of the UPAA

States	Adoption of UPAA	Disclosure Requirements	Citation
Wyoming	No	In Wyoming, case law suggests that prospective spouses do not need to fully disclose to one another the nature, extent and value of one another's property. Instead, there simply must be a fair disclosure of each other's assets.	*Laird v. Laird*, 597 P.2d 463 (Wyo. 1979)

A "full and fair" disclosure will normally require each party to disclose his or her assets, income, liabilities, and the respective value of each. The premarital agreement should indicate whether the value reflects fair market value, fair value, book value, cash value or some other type of professional value estimation.

As a starting point to determine these values, each party to the agreement should consider making available to one another their federal income tax returns for the three years prior to the date of the premarital agreement.

Due to the complexity in determining the value of particular assets (specifically interests in closely held business organizations), a professional familiar with these types of valuations should be engaged. As we will discuss in the next section, a number of complexities are involved when calculating the value of an asset for premarital agreement purposes.

Determining Value

When determining the value of premarital assets, the most frequent standard used is "fair market value." This term is often confused with "fair value." Presented below is a brief overview of how each value is determined.

As we will discuss, the calculations are complex and may require a financial expert to determine the appropriate valuation in connection with the premarital agreement.

The term "fair market value" is frequently defined as "the price at which the property would change hands between a willing buyer and a willing seller when the former is not under any compulsion to buy and the latter is not under any compulsion to sell, both parties having reasonable knowledge of relevant facts."[1]

Internal Revenue Service Revenue Ruling 59-60, which has been commonly accepted as setting forth the criteria to consider in determining the "fair market value" of a closely held corporation for federal gift and estate tax purposes, lists the following factors as fundamental in a "fair market value" analysis:

> (a) The nature of the business and the history of the enterprise from its inception.
>
> (b) The economic outlook in general and the condition and outlook of the specific industry in particular.
>
> (c) The book value of the stock and the financial condition of the business.
>
> (d) The earning capacity of the company.
>
> (e) The dividend-paying capacity.
>
> (f) Whether or not the enterprise has goodwill or other intangible value.
>
> (g) Sales of the stock and the size of the block of stock to be valued.
>
> (h) The market price of stocks of corporations engaged in the same or a similar line of business having their stocks actively traded in a free and open market, either on an exchange or over-the-counter.

On the contrary, "fair value" does not have a generally accepted definition. The Financial Accounting Standards Board has defined "fair value" as the "price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date."[2]

Further, courts have determined that "fair value" considers only "the proportionate interest in a going concern."[3]

It is also important to note that when appraising the "fair market value" of a noncontrolling ownership interest in a closely held business, the application of certain discounts may be warranted to reflect the potential impact on value attributable to the lack of control and/or lack of marketability inherent in the subject ownership interest.

Thus, it may be appropriate for a valuation analyst to apply discounts when determining the "fair market value" of interests in a closely held business for "full and fair" disclosure purposes. The application of discounts is just another added complexity in determining the valuation of a party's assets required for a "full and fair" disclosure under a premarital agreement.

Retaining an Expert

Before entering into a premarital agreement, it is crucial that each party retain experts to assure compliance with the premarital agreement laws of the parties' jurisdiction. An estate planning or family law attorney is needed to determine the disclosure obligations and other necessary requirements needed for a premarital agreement in the particular jurisdiction.

As specified above, the requirements for premarital agreements vary significantly by state. Accordingly, it is important that each party is comfortable with their attorney's proficiency with the premarital agreement obligations in the particular jurisdiction. For example, the retained attorney should know whether the jurisdiction requires a "fair and reasonable" or a "full and fair" disclosure of assets, as this requirement is essential in determining each party's disclosure obligations under the premarital agreement and its validity.

Once the disclosure obligations of the particular jurisdiction have been identified, a valuation analyst should be retained by each party to determine the value of each party's assets for the premarital agreement. A number of factors may be considered by the analyst before arriving at the value of a particular asset.

For example, the analyst will determine whether to use fair market value, fair value, book value, cash value, or some other estimation in calculating the value of an asset for the agreement.

Particular assets require different standards of values to be used which in turn require different factors that must be analyzed by a valuation analyst. As noted above, interests in closely held businesses require the consideration of a whole host of components before an expert can arrive at a value.

To ensure enforcement of a premarital agreement, the support of a valuation analyst is essential to satisfy the "full and fair" or "fair and reasonable" disclosure obligation under the particular jurisdiction's premarital agreement law whenever assets or liabilities without clear cash values are involved.

Unfortunately, some individuals fail to begin the premarital agreement process sufficiently early, allowing inadequate time for thorough asset valuation. While delay of the wedding to allow such valuation is always preferable in these circumstances, the parties may desire to instead stipulate as to the values of certain assets or liabilities in the interests of scheduling.

In such cases, the parties should be advised of the risk that such stipulations—while contractually appearing to satisfy legal requirements—bring no guarantee that a court will not later set aside the premarital agreement on the grounds that the requisite disclosure was not made such that a party would know exactly what he or she was giving up in an objective financial sense.

Conclusion

In summary, the premarital agreement financial disclosure obligations of each jurisdiction vary greatly. These obligations are confusing, complex, and subject to interpretation.

Absent legal counsel that there will be a risk that the premarital agreement may not be enforceable, when unique assets are involved, it is essential to retain a qualified valuation analyst to satisfy the applicable financial disclosure standard in order to ensure the enforceability of the premarital agreement.

Notes:

1. United States v. Cartwright, 411 U.S. 546, 551 (1973); Treas. Reg. § 20.2031; Rev. Rul. 59-60, 1959-1 C.B. 237 (1959).
2.. ASC Topic 820, Fair Value Measurement.
3. See Brown v. Allied Corrugated Box Co., 154 Cal. Rptr. 170, 178 (Cal. App. 2d Dist. 1979); Pueblo Bancorporation v. Lindoe, Inc., 63 P.3d 353, 364 (Colo. 2003).

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