

TEAR THEM DOWN TO PIECES

THE MARRIAGE BETWEEN DIVORCE AND CORPORATE INSOLVENCY

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The Marriage Between Divorce and Corporate Insolvency



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Overview

Since its invention, the limited liability company has provided firm protection for company assets against the personal liabilities and obligations of shareholders and directors. Riding on the back of the House of Lords' decision in Salomon v Salomon [1897] AC 22, it is generally accepted that the company, as a legal entity, is separate and distinct from its members and shareholders. This feature is one of the key advantages of incorporation as opposed to other forms, such as Sole Proprietorships and Partnerships. Therefore, company assets are not available for distribution in divorce proceedings.

And yet, for all the strengths and virtues of the limited liability company, it is vulnerable at the hands of the shareholders and directors. The company is an inanimate object and often relies on the collective actions of the shareholders and directors to drive it. In this light, the dynamics of the relationship between directors and shareholders is a significant determinant of whether the company succeeds or not. This is particularly true for companies where the directors and shareholders are married couples. Good times positively impact the business. Fair times keep the company on an even keel. But tumultuous times in the personal lives of these married couples expose the company to challenges.

In essence, divorces do have ripple effects. They affect relations between children and parents, between family members, and between the principal actors (i.e., husband and wife). They can impact children and their future if care is not taken. In summary, a divorce affects joint enterprises between the man and the woman, and the company is an example of such a joint enterprise.

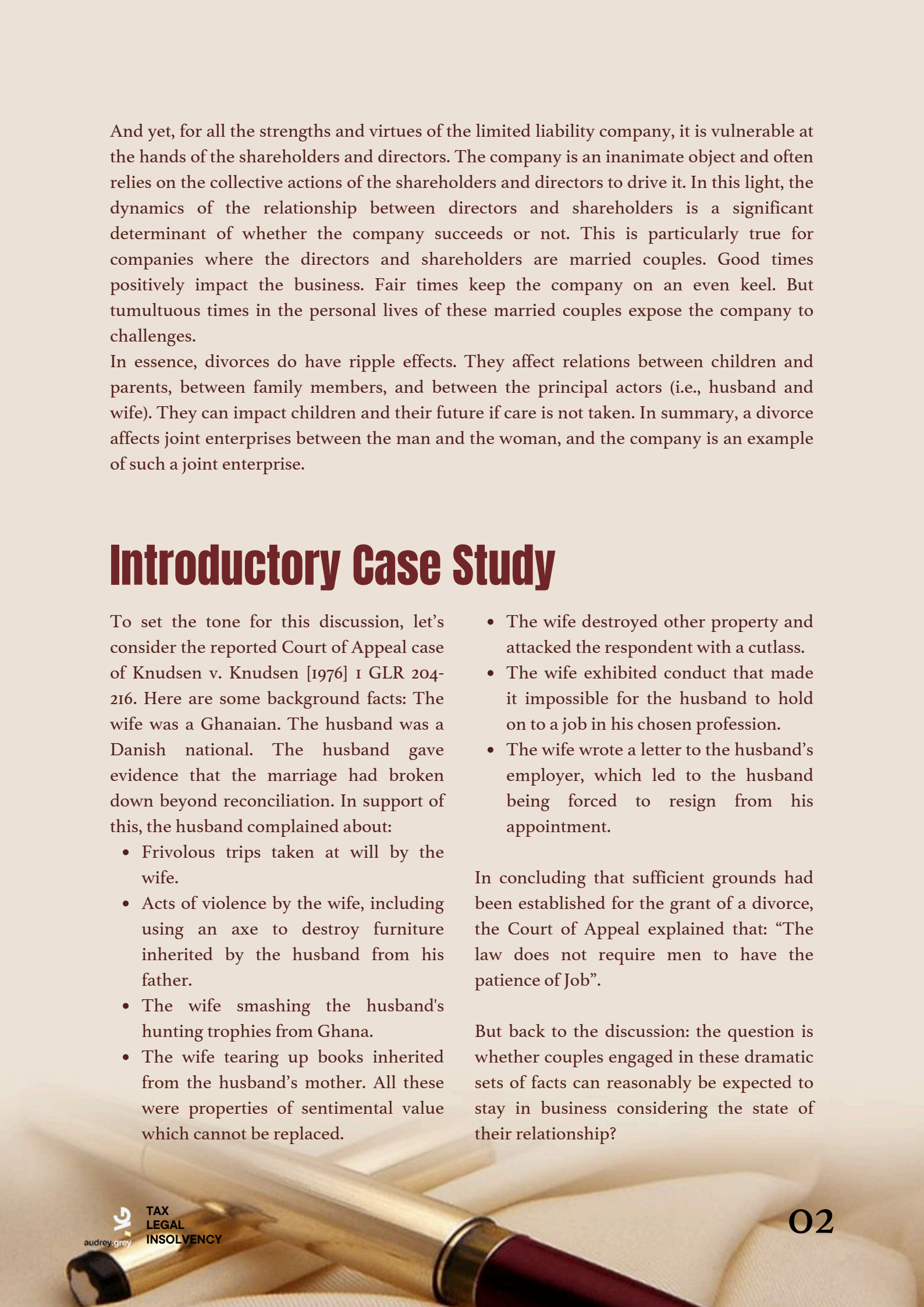
Introductory Case Study

To set the tone for this discussion, let's consider the reported Court of Appeal case of Knudsen v. Knudsen [1976] 1 GLR 204-216. Here are some background facts: The wife was a Ghanaian. The husband was a Danish national. The husband gave evidence that the marriage had broken down beyond reconciliation. In support of this, the husband complained about:

- Frivolous trips taken at will by the wife.
- Acts of violence by the wife, including using an axe to destroy furniture inherited by the husband from his father.
- The wife smashing the husband's hunting trophies from Ghana.
- The wife tearing up books inherited from the husband's mother. All these were properties of sentimental value which cannot be replaced.
- The wife destroyed other property and attacked the respondent with a cutlass.
- The wife exhibited conduct that made it impossible for the husband to hold on to a job in his chosen profession.
- The wife wrote a letter to the husband's employer, which led to the husband being forced to resign from his appointment.

In concluding that sufficient grounds had been established for the grant of a divorce, the Court of Appeal explained that: "The law does not require men to have the patience of Job".

But back to the discussion: the question is whether couples engaged in these dramatic sets of facts can reasonably be expected to stay in business considering the state of their relationship?



The Company and Married Couples

The Companies Act requires that where a minimum of two but not more than twenty people decide to come together to do business for gain or profit, they must do so through the vehicle of a company. Section 3 of the Companies Act uses the expression "company" or "association." The expression "company" or "association" may mean different things in different contexts. But generally, it connotes a gathering of like-minded people who come together to achieve either a common objective (in the case of companies limited by guarantee) or to make a profit (in the case of companies limited by shares). Section 3 of Act 992 does not impose any restrictions or limitations on who may be part of this "company" or "association." It may comprise people with similar or complementary skills, experiences, and training. It matters little whether they are married couples or not.

Marriage Propels Business Growth

A business may profit significantly from the union between husband and wife. For married couples, the fact of the marriage may be its own incentive. After all, this is the person—out of all the people they have encountered—that they chose to marry. The fruit of the marriage is a testament to the strength and benefit of the union. It is a further testament to "man and woman becoming one." Married couples think of themselves as being naturally tied to the same destination ("Till death do us part"). In the Judeo-Christian context, it is the ultimate severing of all prior ties (leaving and cleaving, forsaking all else). In some sense, it is the Olympics of responsibility and commitment.

This "oneness" of mind, purpose, spirit, and destination that comes with marriage has the potential to propel the growth of a business. Marriage, as an institution, offers an intimate platform for two people to pool their resources, skills, training, and experiences together in a way that no pay rise, employee share option scheme, or any other incentive scheme can guarantee. This union of two can make the difficult moments of business bearable.

In cases where there are children from the marriage, these children may potentially serve as a human resource, providing business continuity. In essence, marriage can be beautiful.



From a legal point of view, marriage as an institution is recognised and sanctioned under the law. As a by-product of the union of marriage, the law protects the sanctity of communications between husband and wife. Confidential communications between husband and wife are privileged. As a result, a spouse has the privilege to "refuse to disclose, and to prevent any other person from disclosing, a confidential communication" made between spouses (see Section 110 of the NRCD 323). The scope of the spousal privilege provision under the Evidence Act is wide. It applies in civil and criminal matters. It covers all "confidential information" made during the marriage. No other business partner, associate, or colleague can assert this kind of privilege. The practical effect of Section 110 of the Evidence Decree is that—as far as business goes—spouses are, or should be, the safest repository of confidential information. As long as the information is confidential, they cannot be compelled to disclose it. And even if they wanted to disclose it, the other spouse can prevent them from doing so.

Married Couples in Business

Married couples in business live in at least three parallel worlds. There is the personal world where each party to the marriage makes decisions concerning themselves. Then there is the "oneness" world where husband and wife make decisions together. Finally, there is the corporate world where they make decisions concerning the business or company. In the personal world, the husband and wife are free to acquire property in their own names for their exclusive benefit during the pendency of the marriage (see Fynn v Fynn). Within the context of marriage, properties may be jointly acquired (see Adjei v Adjei [2021] GHASC 5 (21 April 2021); and other cases such as Mensah v Mensah [2012] GHASC 8 (22 February 2012), Boafo v Boafo (2005-6) SCGLR 705, Amoakohene v Amoakohene [2020] GHASC 18 (13 May 2020)). On a daily basis, married couples move in and out of these worlds so often that the lines become blurred.

In the corporate world, married couples may be instrumental in the company acquiring properties. Couples may use inheritances or jointly acquired properties to finance business operations without necessarily being mindful of the worlds in which they are operating. While the personal and marital worlds may sometimes be blurred because determining whether a property acquired during marriage is personal or jointly acquired is a matter of fact or proof, business property is largely shielded. Even if the couple uses their money to acquire company assets, those assets do not belong to them. At best, the company is indebted to them to the extent of the amount invested in acquiring the property. The point is that the assets of the company belong to the company alone and not to the shareholders. As a result, these company assets are not available for distribution during the dissolution of a marriage.

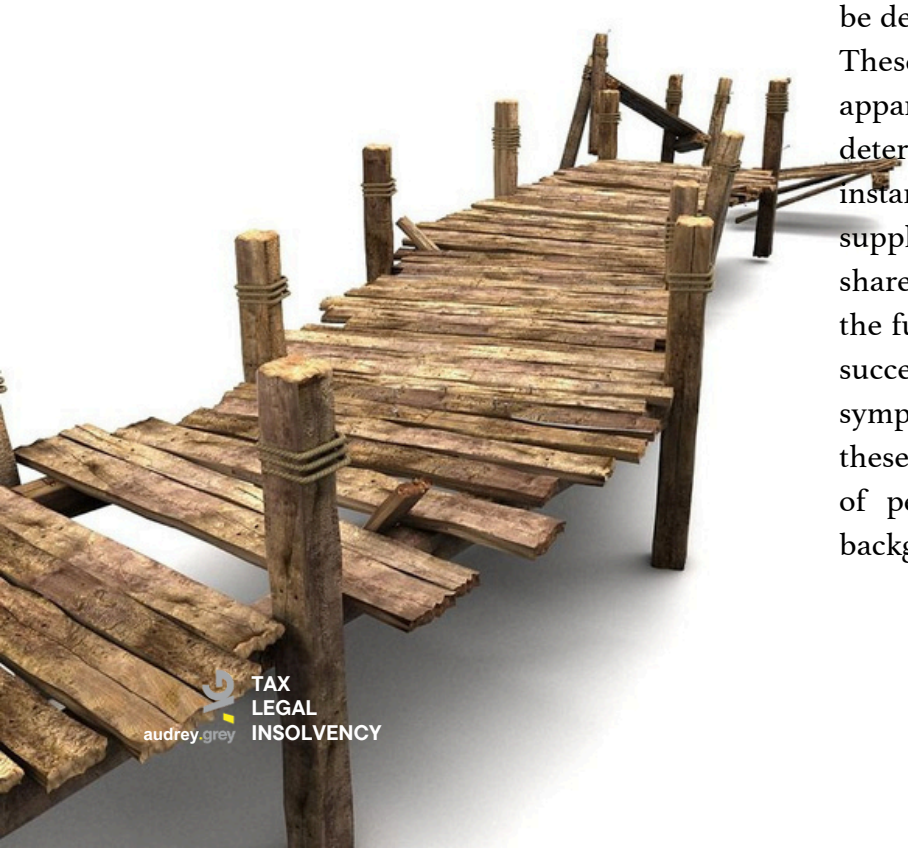
The assets of the company are not those of the couple—no matter how exalted and influential they may be in the company (see Lee v Lee's Air Farming [1960] UKPC 33).

Bad experiences

In much the same way that marriage feeds the growth and development of the business, the decline of a marriage or the onset of a divorce impacts the business negatively.

Link Between Corporate Insolvency and Divorce

Under the Corporate Insolvency and Restructuring Act, 2020 (Act 1015), a company is considered insolvent when it is unable to pay its debts as and when they fall due (commercial or cashflow insolvency) or when its liabilities exceed its assets (balance sheet insolvency). It is important to note that the Corporate Insolvency and Restructuring Act, 2020 (Act 1015), does not prescribe the events that may trigger insolvency.



The causes of a company's insolvency are tiered, multilayered, and complex. There may be apparent or symptomatic causes of a company's insolvency. These apparent or symptomatic causes include poor cash flow management, excessive debt, poor financial management, market changes, management and fraud, unexpected events, loss of key customers or contracts, and high operating costs. Aside from these apparent or symptomatic causes, there are what could be described as root causes of insolvency. These root causes are not immediately apparent but play a decisive role in the deterioration of the company. For instance, regardless of the systems and supply lines in place, a company with shareholders at cross purposes regarding the future of the company is not likely to succeed. Therefore, while there may be symptomatic signs of a failing company, these visible symptoms are only the result of personal issues playing out in the background.

Take this simple scenario: a husband and wife jointly set up a company. They are both 50 per cent shareholders. The marriage hits the rocks. Under our fault-based system, couples are required to prove that the marriage has broken down beyond reconciliation. As a result, they need to give grounds to merit the grant of the divorce. These grounds include: (a) adultery; (b) unreasonable behaviour; and (c) the parties have not lived together for at least two years immediately preceding the presentation of the petition. One allegation invites another. If the separation process is not handled efficiently, it could lead to acrimony or amplify existing acrimonies. Such an acrimonious state of affairs may impact the solvency of the company.

First, there is the likelihood of divided allegiances amongst workers or officers of the company. Secondly, where the skill sets the couple bring on board are complementary, a divorce is likely to affect the quality-of-service delivery, leading to the loss of clients and key contracts. There are anecdotal instances of a man and woman who co-owned a school. The woman petitioned for divorce on the grounds of adultery. The school was split, and some teachers went along with the woman. Neither of the two schools is viable on its own.

In some instances, the company becomes the battleground. Take banking mandates as an example. Where couples opt to give signature mandates jointly, the refusal of one person has the potential to bring operations to a standstill, with the company defaulting on its obligations. Where the signature mandate permits either party to access the funds of the company, there is a high possibility of one of the spouses seeking to transfer the funds for their personal benefit.



Strained Relations May Impair Decision Making

With couples in divorce, a major challenge that arises is decision-making. Under Ghanaian law, most decisions involving the company are made either on the basis of a simple majority (ordinary resolution) or with the consent or assent of shareholders holding 75 per cent of the shares (special resolution). In a company where the husband and wife each hold 50 per cent of the shareholding, relationship problems will result in deadlocks in decision-making. While the Companies Act allows the directors to intervene, the question that arises is—what happens if the company directors are the same husband and wife? Even if the husband and wife are not the directors, it should not be overlooked that shareholders exercise some influence over directors, and the potential for directors to take sides is likely.

These strained relations often result in a deadlock and would often require some external intervention for resolution. In the event that the parties are unable to resolve their issues and differences, one option would be the winding up of the affairs of the company.

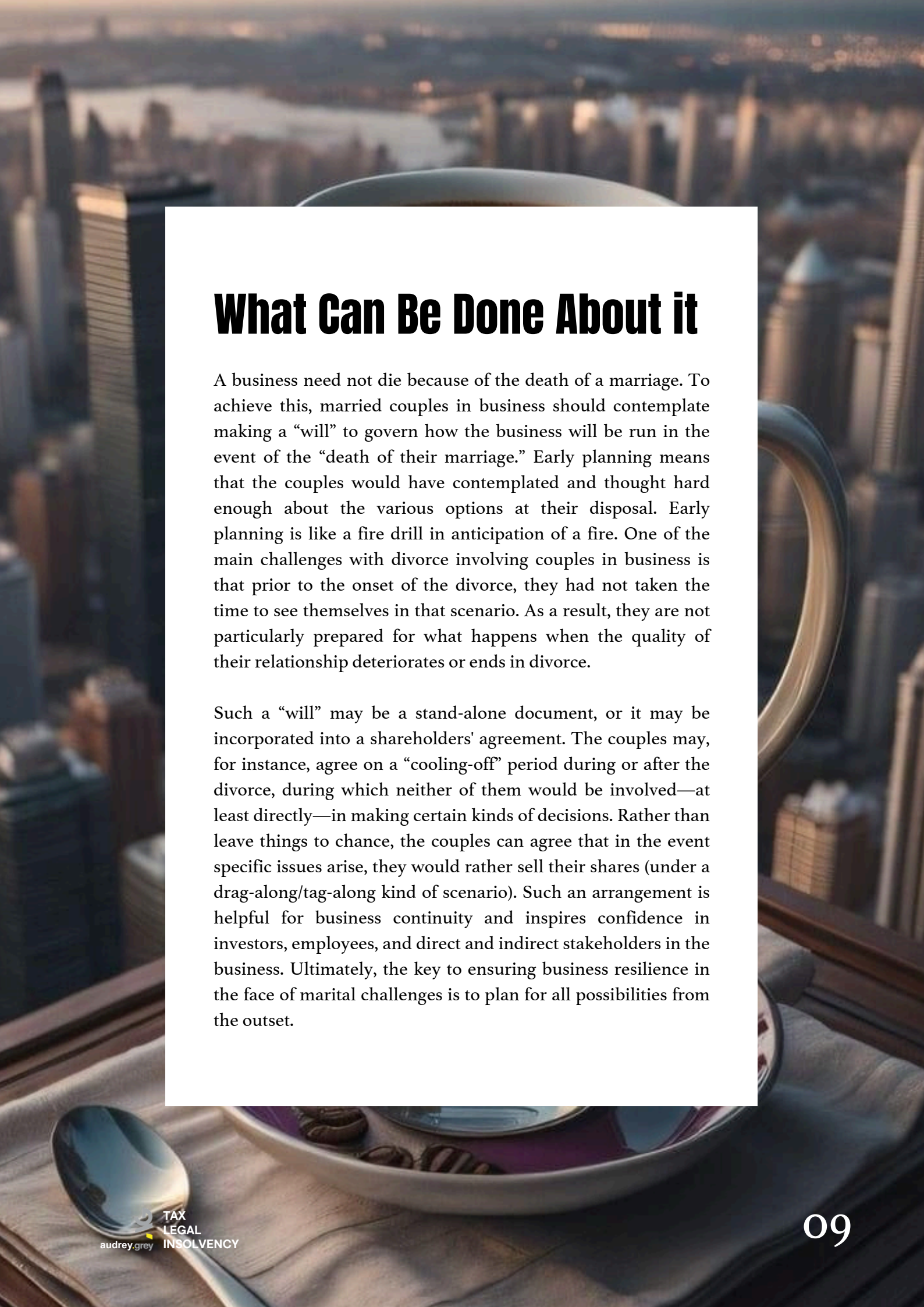


Winding up of the Affairs of the Company Due to Impact of Divorce

Under the insolvency and restructuring framework, a company may be wound up for a variety of reasons. These reasons include: (a) a company suspending business for a year within the year after the incorporation of the company; (b) the company not having any members; (c) the company being unable to pay its debts as they fall due. These grounds, as set out, may be triggered by the personal animosity and difficulties between the principal characters, who happen to be husband and wife. For instance, personal difficulties and feelings of betrayal may result in the company suspending operations within a year after its incorporation.

Another significant ground upon which the affairs of the company may be wound up is where "the Court is of the opinion that it is just and equitable that the company should be wound up." The "just and equitable" ground is wide enough to cover a variety of circumstances. In Re Kurilpa Protestant Hall Pty Ltd [1946] St R Qd 171 at 183, Macrossan CJ noted that: "The words 'just and equitable' are words of the widest significance and do not limit the jurisdiction of the court to any case. It is a question of fact, and each case must depend on its own circumstances." Similarly, in Billy v. Kuwor & Anor [1991] 1 GLR 522-532, it was held that: "Consideration of the just and equitable rule was a question of fact, and as such, each case must depend on its own circumstances. The court, therefore, had an unfettered discretion in that exercise since it was not possible to lay down a general guide to the solution of what were essentially individual cases."

Therefore, under the just and equitable grounds, a court may entertain a petition from a divorced couple arguing that, due to the tempestuous relationship between them, it is just and equitable that the company should be wound up. In Chu v Lau [2020] UKPC 24, the Privy Council explained that a winding-up order may be made "... to resolve a functional deadlock where an inability of members to co-operate in the management of the company's affairs led to an inability of the company to function at board or shareholder level."



What Can Be Done About it

A business need not die because of the death of a marriage. To achieve this, married couples in business should contemplate making a “will” to govern how the business will be run in the event of the “death of their marriage.” Early planning means that the couples would have contemplated and thought hard enough about the various options at their disposal. Early planning is like a fire drill in anticipation of a fire. One of the main challenges with divorce involving couples in business is that prior to the onset of the divorce, they had not taken the time to see themselves in that scenario. As a result, they are not particularly prepared for what happens when the quality of their relationship deteriorates or ends in divorce.

Such a “will” may be a stand-alone document, or it may be incorporated into a shareholders' agreement. The couples may, for instance, agree on a “cooling-off” period during or after the divorce, during which neither of them would be involved—at least directly—in making certain kinds of decisions. Rather than leave things to chance, the couples can agree that in the event specific issues arise, they would rather sell their shares (under a drag-along/tag-along kind of scenario). Such an arrangement is helpful for business continuity and inspires confidence in investors, employees, and direct and indirect stakeholders in the business. Ultimately, the key to ensuring business resilience in the face of marital challenges is to plan for all possibilities from the outset.

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