

TYPES NOT MAPPED YET March 16, 2017 | TTR not mapped yet | Lacey R. Searfoss

How to protect your family-owned business from your child's spouse

For most people, a child's wedding is one of those great life moments that is filled with months of planning and excitement. However, for people who own a family-owned business, the old myth that 50 percent of marriages end in divorce might cause some anxiety and a visit to an attorney. In Missouri, as with most other states, there is a presumption under the law that marriage is an economic partnership. This economic partnership gives a child's spouse certain economic rights upon dissolution of the marriage and at a child's death.

Generally, the economic rights of a spouse are controlled by state law and vary from state to state. Owners of family-owned businesses are diligent in protecting their businesses and wealth from creditors by purchasing insurance and operating through entities such as corporations, limited liability companies and limited liability partnerships; however, they sometimes fail to protect their business from a different type of potential "creditor" — a child's spouse.

Generally, for divorce purposes, all property owned by married couples is classified in two categories: (1) marital property and (2) non-marital property (also called separate property). In most states, in a divorce, the separate property of a spouse is not subject to division by a court and remains the separate property of such spouse. Unlike separate property, courts have broad discretion in dividing the marital property between spouses.

So the distinction between the two categories of property plays an important role in protecting property from a child's spouse upon divorce. In Missouri, separate property includes: (i) property owned prior to the marriage, (ii) property acquired subsequent to the marriage by gift or inheritance, (iii) property that by agreement of spouses is separate property (a premarital agreement), and (iv) the increase in value of separate property except to the extent, if any, that marital assets, including labor, have contributed to such increase. However, Missouri takes a distinctly minority approach among the states in characterizing income from separate property as marital property. Marital property is all property of a married person that is not classified as separate property.

In addition to a property settlement at divorce, a court may award maintenance (also known as alimony) to a child's spouse. The purpose of maintenance is to provide a spouse with sufficient income for his/her reasonable needs. A court considers many factors in awarding maintenance, including the separate property of each spouse. So, although a court cannot award a spouse's separate property to the other spouse, the income from separate property may be needed to pay an award of maintenance.

In the context of the death of a married child, the distinction between marital property and separate property goes away. Rather, any property "owned" by a married child is subject to certain marital rights of the surviving spouse.

In Missouri, the principal marital right is the right to a fractional share of the deceased spouse's "estate." Generally, the surviving spouse is entitled to one-half of the estate if there are no children of the marriage; or one-third of the estate if there are children of the marriage. However, the "estate" is not necessarily the totality of a deceased child's assets. As an example, property owned by a child's revocable trust prior to marriage would not be considered as part of such child's "estate" against which a spouse would have a fractional interest.

By contrast, property titled solely in a child's individual name, that does not pass by operation of law at death (by beneficiary designation or otherwise), would be considered as part of such child's "estate." To prevent a deceased spouse from impoverishing the surviving spouse by transferring assets to others, including a revocable trust, Missouri allows certain property to be pulled into the "estate" if the surviving spouse can show the transfer was made "in fraud of the surviving spouse's marital rights."

There are many ways to prevent a child's spouse from becoming a "creditor" of a family-owned business. Below are three common ways to protect the family-owned business:

Premarital Agreement. A premarital agreement is an agreement between a child and the child's future spouse. The premarital agreement should be entered into by the parties months before the wedding date. The parties to a premarital agreement can establish how property will be retained or divided and whether either party will make maintenance payments to the other party in the event the marriage is dissolved, and establish what rights a surviving spouse will have in the estate of the deceased spouse. If a child already owns an interest in the family-owned business and works for the business, a premarital agreement probably provides the most certainty in protecting the family-owned business from a child's spouse. An important part of a premarital agreement is full financial disclosure of a child's assets, income, and liabilities to the child's future spouse, including financial details about the family-owned business.

Child's Estate Plan. A child should create a revocable trust and transfer all property owned by the child, including any interest in the family-owned business, to the revocable trust prior to contemplation of marriage. The assets (excluding income earned) of the revocable trust should remain the separate property of the child for divorce purposes and should be excluded from the child's "estate" for purposes of determining the surviving spouse's rights in the assets at the child's death. The child should be careful not to withdraw the trust-owned assets and commingle them with other assets owned by the child or the child's spouse, including adding spouse as an owner of such assets. Note that a transfer of property of a child to the child's revocable trust after the marriage or close in time to marriage may be challenged by the spouse after the child's death as a transfer intended to deprive the spouse of marital rights.

Parent's Estate Plan. Any interest in the family-owned business that a parent wants to give a child should be given to such child in a trust that will remain in existence for the lifetime of the child. As long as the trust is drafted carefully, the property held in trust will not be subject to claims of a spouse in the context of a divorce or at death because the child does not "own" the property. Although, the assets of the trust are protected, the income distributed by the trust to a child is likely to be considered marital property in a divorce proceeding and subject to division by a court.

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