Business and Tax Consequences of Marital Dissolution*

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Abstract

We study how divorce affects private firms owned by separating couples, using administrative data that link spouses' business ownership to their individual tax returns and firm balance sheets. Our matched event-study design compares owners who divorce with similar owners who divorce later. Divorce is followed by large and persistent reductions in the firm's total assets, capital, employment, profits, and corporate tax liabilities. At the same time, the focal owner's personal income and tax payments rise, potentially reflecting value being drawn out of the business to finance a payout to the departing spouse. To test whether this financial adjustment drives the contraction, we compare divorce events that differ in how much of the firm the departing spouse can claim. The decline is largest among couples most exposed to the division of business wealth and much smaller when the claim is weak. We then exploit British Columbia's 2013 Family Law Act that expanded property-division rights to common-law couples. The reform led to a decline in divorce among common-law couples, and a subsequent increase in their firms' size, profits, and tax liabilities. Taken together, our results suggests that divorce contracts real business activities, and that family property law alters both the incentives and financial consequences of separation, with implications for aggregate economy and tax revenue.

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1 Introduction

Divorce is one of the most consequential economic events in family life. It terminates the pooling of income and risk within the household and forces the division of wealth accumulated during the relationship. An extensive literature examines its effects on household resources, labor supply, and children (Gray, 1998; Gruber, 2004; Voena, 2015; Frimmel, Halla and Winter-Ebmer, 2024; Johnston, Jones and Pope, 2025). However, much less is known about what happens beyond the household when the separating couple owns a private business. This gap matters because privately-held, small firms account for roughly half of total employment and sales in the United States and Canada, and at least a quarter of business owners go through a divorce in their life. When marital assets include claims on a business, resolving these claims may alter its ownership and require financial adjustments, with aggregate implications for investment, employment, and fiscal policy.

The direction of these consequences is theoretically ambiguous. Under frictionless bargaining, a division of the firm may not affect productivity. A settlement could efficiently reallocate ownership to the spouse best qualified to the firm (Grossman and Hart, 1986; Hart and Moore, 1990) or dissolve an ongoing conflict (Becker, Landes and Michael, 1977). In practice, however, private businesses are often cash constrained and closely tied to their owners' personal finances, so satisfying a property claim requires borrowing or liquidation that can alter firm performance. Identifying these effects is challenging because divorce is not random and observing households and firms together requires administrative data that link detailed ownership information of individuals with their balance sheets.

In this paper, we study how divorce affects firm performance and tax liabilities using Canadian administrative data from 2001 to 2019 that link individual tax and marital records to the universe of firm ownership and balance sheet data. To identify the effects of divorce on firm outcomes and to isolate a key mechanism, we use two empirical designs. First, we use an event-study design where we compare business owners (and their firms) who go through a divorce with a matched set of control owners (and their firms) who go through a divorce at a much later time. To ensure that treated and control owners are comparable, we match them on their relevant characteristics, such as business' sector, province, firm and individual characteristics. This approach allows us to examine how divorce affects the key outcomes without making causal statements. Second, since divorce is endogenous, we use a difference-in-differences design based on the 2013 Family Law Act in British Columbia that exogenously shifts the probability of divorce among common-law partners, which would subsequently affect their business outcomes.

Broadly, we categorize three main channels through which divorce affects firm outcomes. The first channel is related to losing a valuable partner who helped run the business. The second channel is the division of the business' value accumulated during marriage and the subsequent financial costs associated with cash payouts to the departing spouse. The last channel is the combination of all other changes after divorce that increase the emotional and time costs of the operating spouse who continues to run the business, such as changes in family structure, home location, and child custody.

To isolate a key mechanism, we separately examine three different types of divorce events in our event-study analyses. The first type is where both spouses own the same firm and go through a divorce. In this case, the departing spouse can claim cash payouts for selling his or her ownership stakes, so there will be an automatic division of the business' assets upon divorce. The second type is where only one member of the married couple owns the firm, but the other spouse has no ownership in the firm (or any other firm). In this case, the other spouse can still claim an equal split of the business' value accumulated during marriage, but the magnitude of the split depends on how much the business grew after marriage. The third type is where common-law couples go through a divorce and only one of them owns the firm, while the other spouse has no ownership in the firm (or any other firm). Since most common-law partners are not required to split the business' value upon divorce in our sample of provinces and time periods, we use this case to test how much the asset-division channel matters for post-divorce firm outcomes. For all divorce types, we apply the same matching strategy and event-study design to estimate what happens to business owners and their firms after divorce relative to control owners and firms.

Our event-study results show that divorce is followed by a persistent contraction in jointly owned private firms. Over the five years after divorce, the focal (operating) owner's share rises by 16.5 percentage points as the former spouse's share falls by nearly the same amount. This reallocation is accompanied by a 20 percent decline in total assets, a 13 percent decline in capital, and a 17 percent decline in employment. The contraction in firm size carries through to the firm's profitability and tax base, with profits falling by 15 percent, and corporate taxes by about 10 percent. At the same time, the focal owner's personal income and personal taxes rise without a detectable increase in wages. This pattern is consistent with a financial reallocation associated with divorce, rather than a decline in the owner's labor income.

To understand the mechanism behind this contraction, we examine an ownership-division and liquidity channel. A former spouse's claim on the firm's value may require the owner who retains the business to draw resources from it to settle that claim. This channel pre-

dicts larger contractions when the spouse's claim is stronger. We compare couples who jointly owned the same firm with couples in which only the focal owner held shares, and among the latter, married and common-law couples. After divorce, firm size and performance deteriorate most in jointly owned firms, less in sole-owner marriages, and little in sole-owner common-law relationships. This gradient is consistent with a larger financial adjustment when the departing spouse has a stronger claim on the firm's value. We then examine whether the adjustment varies with pre-divorce retained earnings, a proxy for internal financial resources. Firms with fewer internal resources experience larger reductions in capital, whereas firms with greater resources preserve capital but reduce retained earnings, suggesting that financial capacity affects how firms absorb the cost of separation.

We also test two alternative channels – the loss of a valuable business partner and owner's inattention – but neither fits the pattern. If the contraction reflected the loss of a spouse who contributed labor or management, it should be smaller in larger, professionally managed firms. Instead, larger firms experience similar contractions in size and performance. Likewise, if it reflected the owner's inattention, one would expect the negative effects to fade in the longer run, as owners adjust and refocus on the business. However, the effects persist through the fourth year after divorce. These patterns reinforce the evidence for ownership division and liquidity as the primary channel through which divorce affects firm outcomes.

There are two main threats to identification based on our event-study design. The first threat is reverse causality: owners whose business is failing may be induced to go through a divorce, so the divorce is actually the result of the failing business rather than the cause. We show parallel pre-trends on the main outcomes which would alleviate concerns regarding this potential reverse-causality issue. The second threat is a concurrent shock that would differentially affect treated and control groups. For example, there could be a negative health shock that leads to a divorce event and drives poor firm performance. To address this concern, we exploit different types of divorce events described earlier assuming that a concurrent shock would be equally likely to happen across different types of divorce events. Since we do not find much impact on firm outcomes after a divorce event where only one of the spouses owns the firm, it is difficult to see how a negative shock would only occur in a divorce event when both spouses jointly owned the firm, while such a shock would not occur and drive negative firm outcomes in the other types of divorce events. Still, identifying the causal effects of divorce on firms outcomes and isolating a specific channel are challenging based on the event-study design alone.

To identify the ownership-division and liquidity as the key channel through which divorce affects firm outcomes, we use a difference-in-differences design based on the 2013 Family Law

Act in British Columbia, which mandated common-law couples who have lived together for at least two consecutive years to split assets upon divorce. In particular, we exploit this reform to test whether the asset-splitting requirement affected the probability of divorce among common-law partners and subsequently how it affected their business outcomes. To identify the effects of the reform, we compare the outcomes of common-law couples in British Columbia who had been in a relationship for at least two consecutive years before 2013 with those of common-law couples in control provinces (mainly Ontario and Quebec). We find that the reform significantly reduced the probability of divorce among common-law partners in British Columbia relative to common-law partners in control provinces. Subsequently, we find significant and large increases in firm size (e.g., total assets, capital, and employment) and performance (profits and profit margins). Our IV-estimates on firm outcomes are consistent with our event-study estimates and quantitatively comparable: divorce leads to decreases in firm size and performance, followed by increases in owners' tax burdens in the short to medium run.[1]

Related literature. This paper contributes to three strands of literature. First, we contribute to the literature on how family law and property rights affect household behavior. An extensive body of work shows that the legal framework governing divorce, such as unilateral divorce and asset-splitting rules, alters intra-household bargaining. By shifting spouse's outside options, these legal regimes dictate the allocation of household labor supply, savings, and domestic welfare (Chiappori, Fortin and Lacroix, 2002; Stevenson and Wolfers, 2006; Voena, 2015). While this work focuses on the distribution of resources within the family, we show that family law also governs productive capital. When household wealth is held in an operating private firm, the property regime acts as a friction. The legal threat of asset division not only reallocate passive savings, but forces the extraction of capital, altering firm's ownership structure and investment incentives.

Second, we contribute to the literature on the economic consequences of divorce. Existing research documents the disruptions borne by separating family members, showing that marital dissolution changes adults' labor market behavior (Johnson and Skinner, 1986; Canessa et al., 2026) and imposes lasting adverse effects on children's education, earnings, and other adult outcomes (Gruber, 2004; Frimmel, Halla and Winter-Ebmer, 2024; Johnston, Jones and Pope, 2025). We expand the scope of the literature by identifying a novel transmission channel through which family shocks propagate into the broader economy. When a business is subject to marital asset division, the requirement to satisfy a splitting claim acts as a

[1]These results are currently under review for vetting. An updated draft incorporating these results based on the reform will become available in late September.

forced liquidity event for the firm. Divorce may therefore affect people and economic activity outside the separating household if it changes the firm's financial resources, employment, or performance.

Finally, our paper is also related to the literature on shocks to owners and financial resources in closely held firms. Studies in this literature have shown that transitions in corporate control or the loss of an owner's human capital, e.g., retirement or death, lead to declines in firm performance (Smith et al., 2019; Sauvagnat and Schivardi, 2024). Related work also highlights the vulnerability of private firms to their owners' personal balance sheets, showing that exogenous wealth shocks or succession taxes force an extraction of firm liquidity that depresses investment and employment (Tsoutsoura, 2015; Ring, 2023). We study a shock that bridges these channels. Unlike an owner's death or retirement, divorce creates a property claim on the business even when the focal owner retains operational control. We examine whether the financial adjustment required to resolve this claim affects firm performance, testing the liquidity mechanism against alternatives like managerial inattention or the loss of a firm partner. In doing so, we see family property law as a non-tax redistributive policy, demonstrating how settlements meant to protect vulnerable spouses can distort firm productivity and carry broader fiscal consequences.

This paper is organized as follows. Section 2 describes institutional details regarding family property laws for business owners and provincial reforms that changed how property is divided among common-law partners in Canada. Section 3 describes our data, sample restrictions, and variable definitions. Section 4 describes our empirical designs and identification challenges. Section 5 shows the results and their economic interpretations, and Section 6 explores potential mechanisms behind our findings. Section 7 concludes.

2 Institutional Background

This section describes the institutional details regarding family property laws, in particular for business owners, in Canada and provincial reforms that changed how the property is divided among common-law partners upon divorce.

2.1 Family Property Laws for Business Owners in Canada

2.1.1 For Married Couples

In Canada, family property laws, governed provincially, consider a business established, acquired or grown during a marriage as a shared family asset. Upon divorce, a married partner is therefore entitled to an equal share of the business' value accumulated during the marriage, regardless of his or her ownership stake. For example, suppose a married couple started and grew a business together, and one of the spouse has 20 percent ownership stakes in the business while the other spouse has 80 percent stakes. If they get divorced, the spouse with the lower ownership rate can still claim an equal split of the business' value. Note that the pre-marriage baseline value of the business is usually excluded from this calculation.

The equal split of the business for a married couple holds true even if one of the spouses does not have any ownership stake in the business. In that case, the operating spouse (with the majority ownership stakes) typically keeps 100 percent control of the company and pays a monetary compensation or trades other types of assets (e.g., business properties or family home) to satisfy the other spouse's share. An independent corporate evaluator is usually required to inspect and determine the fair market value of the business.

2.1.2 Financial and Tax Implications of Divorce

Given that an operating spouse has to provide a cash payout to the other spouse upon divorce, raising capital for this payment, usually installed over several years, can gradually drain corporate cash flow or force the sale of the firm's assets over time. Furthermore, both spouses' tax burdens would increase from cash settlements. For the operating spouse who has to liquidate a part of the company's assets, his or her personal income would increase upon the sale of the assets. Subsequently, personal tax burdens would also rise. At the same time, corporate tax liabilities may decrease as firm size and taxable income shrink. Therefore, in the short to medium run, personal taxes would rise while corporate tax burdens would decrease for the operating spouse in order to raise cash for the payout.[2] The other spouse's personal tax burdens would increase as well after receiving cash payments. If the other spouse sells his or her shares to the operating spouse, he or she also has to pay capital gains taxes. Overall, both spouses' personal tax burdens would increase in the medium run after divorce. If the negative financial burden for the business leads to a worse firm performance,

[2]It is also possible for the operating spouse to pay the other spouse by selling non-business assets (e.g., family home). In this case, there are no direct impacts on the firm side, although there could be still indirect impacts through the financial burdens of divorce.

however, the firm's corporate tax liabilities may continue to decrease in the long run. Thus, the fiscal externality of divorce for business partners remains unclear in the long run.

2.1.3 Corporate Divorce: Butterfly Transactions in Family-Owner Businesses

In the case where both spouses have ownership stakes in the business and go through a divorce, they can minimize their tax burdens through a butterfly transaction, a form of corporate reorganization where the company's assets are divided among its shareholders on a tax-deferred basis. Specifically, a butterfly transaction makes use of Section 85 of the Income Tax Act and prevents a capital gains realization on the disposition of assets by allowing the taxpayer to transfer property to a taxable Canadian corporation on a tax-deferred basis.

There are two types of butterfly transactions. In a single-wing butterfly transaction (more common), a operating spouse continues with the business and takes 100 percent ownership while the other spouse receives a portion of the corporation's assets. In this case, the departing spouse would incorporate a new firm (e.g., holding company) and transfer its shares from the original firm without realizing any gains. The shares held by the original firm in the new holding company are subsequently redeemed by the new firm, while the original firm concurrently repurchases its shares held by the new firm for cancellation. In this way, the departing spouse can exit the original firm and is compensated for his or her shares, while the operating spouse continues to run the business. Both spouses would eventually pay taxes upon selling their assets and shares if the departing spouse wants a cash payout. In a double-wing butterfly transaction, each spouse receives a portion of the firm's assets and the company ceases to exist. In this case, both spouses would set up their own holding companies to transfer their shares from the original firm and are able to defer paying taxes until they realize their gains. Note that either type of butterfly transactions is a tax-deferral vehicle, rather than a tax-avoidance one, and it is used only when the departing spouse agrees not to get a cash payout upfront. Furthermore, setting up holding companies through butterfly transactions to defer taxes is costly and needs to be planned in advance.

2.1.4 Pre-nuptial Arrangements

Pre-arranged marital contracts, known as pre-nuptial agreements, can override statutory rules and the court can order unequal splits of the business' value after divorce. Therefore, not all divorces among married couples would result in equal splits of the business' assets. How such events would affect the division of the firm's assets is context-specific and needs to be examined empirically.

2.2 For Common-Law Couples

Family property laws for married couples after divorce do not directly apply for common-law couples in Canada, and differ across provinces. By definition, a common-law partner is in a conjugal relationship for at least one year with a person who is not a married spouse. In many provinces and territories, such as Ontario, Quebec, and Nova Scotia, common-law partners do not have automatic right to an equal split of the business' value accumulated during the relationship.

In four provinces, on the other hand, common-law partners are considered as married spouses after living together for at least 2 years (in British Columbia and Saskatchewan) or 3 years (in Alberta and Manitoba). Therefore, common-law partners who meet the cohabitation threshold have the right for an equal division of the business' assets after divorce in these provinces after the reforms described below.

2.3 Policy Changes for Common-Law Couples

The four provinces had not always recognized common-law partners as married couples. In Saskatchewan, the Family Property Act in 2002 was implemented to explicitly include common-law partners as married spouses. In Manitoba, an equal split of family property (including the business) for qualifying common-law partners started on 2004 when the Common-Law Partners Property and Related Amendments Act came into effect. In British Columbia, the Family Law Act in 2013 was established to allow an equal split of the business' value accumulated during the relationship for common-law couples. Finally, in Alberta, the Family Property Act in 2020 allowed an equal split of the business' value for eligible common-law partners. Given our data availability and sample, we exploit the reform in British Columbia as our key empirical strategy since we have enough sample size and pre-reform periods to test for parallel pre-trends. We describe the details in Section 5.

3 Data, Sample Restrictions, and Variable Definitions

For our empirical analyses, we use the following datasets from 2001 to 2019, all merged at the individual level using the unique identifier: (1) individual tax returns data (T1PMF) to identify individual income and tax information, (2) ownership data on incorporated businesses (T2S50), and (3) firm-level balance sheet data (NALMF) to identify corporate income and tax information. We focus on individual owners with at least 20 percent ownership in a

given firm and year to focus on major shareholders with meaningful stakes in the company (Jakobsen et al., 2024). We drop a small fraction of individuals who have gaps in their tax records or who die during our sample period to avoid misclassifying death events as divorce events. Furthermore, we focus on individual owners who have a single business, which account for the majority of owners in our setting, to make our results on firm outcomes easier to interpret, although we find similar results including multiple-business owners. In our setting, major shareholders have 60.5 percent ownership rates on average and account for almost all shareholders, while those with a single business have 47.8 percent ownership and account for 73 percent of individual shareholders on average (Moon and Wu, 2026).

We define a business owner as having a spouse if the individual has a spouse identifier in the tax return. In the data, there is a variable that defines the individual's marital status, which we use to distinguish between married couples and common-law couples among individual owners with a spouse. Then, we define a divorce (or separation for common-law couples) event when the individual's spouse ID changes from the previous year or becomes missing if the spouse ID was not missing from the year before. Again, since we already dropped individuals who ever die during our sample period, we avoid misclassifying a death event as a divorce event. As we explain in the next section, we focus on divorce events when both spouses had been in the relationship for at least two years before the event.

The main outcome variables are measures of owner-level and firm-level outcomes. The owner-level outcomes include measures of income, such as their pre-tax personal income and deferred corporate income (defined as changes in retained earnings plus corporate taxes paid) as well as their wage earnings and personal taxes (at both federal and provincial levels). For firm-level outcomes, we examine firms' total assets, capital stock, the number of employees, taxable income, and corporate taxes paid. For performance measures, we look at firms' profits, defined as total revenue minus total expenses, and profit margins, defined as profits divided by total revenue (Bonney, Pistaferri and Voena, 2025). We drop individuals below age 20 and financial firms (NAICS 52) from our analyis sample.

4 Empirical Design

This section describe our empirical strategies to identify the effects of divorce on firm and individual outcomes. We exploit two empirical designs that complement each other. First, we use an event-study design where we compare business owners (and their firms) who divorce with control owners (and their firms) who divorce at a later time. This approach allows us to see how divorce affects the key outcomes descriptively without making strict

causal statements. Since divorce is endogenous, we need a reform that exogenously shifts the probability of divorce among business owners, which would subsequently affect their outcomes. We use the 2013 Family Law Act in British Columbia as a quasi-experimental variation and describe how we use it to identify the key channel through which divorce affects firm and individual outcomes.

4.1 Event-Study Design

We use an event-study design where we compare treated business owners (and their firms) who go through a divorce at a given year with a set of control owners who go through a divorce at least 5 years later. We focus on major owners (with at least 20 percent ownership) who hold a single business for at least two consecutive years before the event. We define owners as "treated" if they go through a divorce in a given year after being in a relationship for at least two consecutive years before the event and as "control" if they go through a divorce at least 5 years later. In this way, control owners are not yet treated during the event window, avoiding comparisons with later treated units within the event time (Borusyak, Jaravel and Spiess, 2024).[3] To ensure that treated and control owners are comparable, we match them on various measures of income, taxes, firm characteristics, sector, gender, age, and marital status in the year before the event. To have enough control owners who divorce at a later time, we restrict the first divorce event for treated owners to be no later than 2013, which is before the 2013 Family Law Act that we exploit as the second empirical design.

Importantly, we examine three different types of divorce events separately. The first type is where both spouses own at least 20 percent in the same firm and go through a divorce. The second type is where only one of the married couple owns at least 20 percent in the firm, but the other spouse has no ownership in the firm (or any other firm). The third type is where common-law couples go through a divorce and only one of them has at least 20 percent stakes in the firm, while the other spouse has no ownership in the firm (or any other firm). For all divorce types, we apply the same matching strategy and event-study design to estimate what happens to business owners and their firms after divorce relative to control owners and firms.

To examine post-divorce outcomes at the firm level, we estimate the following event-study

[3]Our results are robust to using alternative sample restrictions and redefining control owners (who divorce at least 9 years later), and including major shareholders with more than one firm.

specification:

$$y_{jt} = \sum_{k=-4}^{4} \alpha_k \mathbb{1}(t = k) \times Treated_j + \omega_j + \tau_{t \times c} + \phi_{t \times p} + \psi_{t \times s} + \mu_{jt} \tag{1}$$

where y_{jt} is an outcome variable for firm j whose owner goes through a divorce in year t, $\mathbb{1}(t = k)$ equals 1 if event time $t = k$, and $Treated_j$ is a treatment group indicator, ω_j are firm-by-cohort fixed effects, $\tau_{t \times c}$ are event-time-by-cohort fixed effects, $\phi_{t \times p}$ are event-time-by-province fixed effects, and $\psi_{t \times s}$ are event-time-by-sector (2-digit) fixed effects. The standard errors are clustered at the firm level.

To examine post-divorce outcomes at the owner level, we estimate the following event-study specification:

$$y_{it} = \sum_{k=-4}^{4} \beta_k \mathbb{1}(t = k) \times Treated_i + \omega_i + \tau_{t \times c} + \phi_{t \times p} + \psi_{t \times s} + \mu_{it} \tag{2}$$

where y_{it} is an outcome variable for owner i in year t, $\mathbb{1}(t = k)$ equals 1 if event time $t = k$, and $Treated_i$ is a treatment group indicator, ω_i are individual-by-cohort fixed effects, $\tau_{t \times c}$ are event-time-by-cohort fixed effects, $\phi_{t \times p}$ are event-time-by-province fixed effects, and $\psi_{t \times s}$ are event-time-by-sector (2-digit) fixed effects. The standard errors are clustered at the owner level.

4.2 Key Threats to Identification

To interpret α_k and β_k in Equations (1) and (2) as causal impacts of divorce on firm-level and owner-level outcomes, we need to assume that selection into a divorce is independent of μ_{it}, conditional on the observables that are used in the matching process. This may be a strong assumption in practice, and a priori, the sign of the bias is not obvious. We see two key threats to our identification.

The first threat is reverse causality. For example, owners whose business is failing may be induced to go through a divorce, so the divorce is actually the result of the failing business rather than the cause. We show parallel pre-trends on the main outcomes which would alleviate concerns regarding this potential reverse-causality issue.

The second threat is a concurrent shock that would differentially affect treated and control groups. For example, there could be a negative shock (e.g., bad health) that leads to a divorce event as well as negative impacts on the firm. This is a major concern even if

parallel pre-trends hold. To address this concern, we leverage different types of divorce events described earlier assuming that a concurrent shock should be equally likely to happen across all types of divorce events. For example, suppose that we find negative impacts of divorce on firm-related outcomes (e.g., assets, investment, and performance) after a divorce event where married couples jointly own the same firm prior to the event. Even if the pre-trends are parallel relative to the control group, a valid concern is that there could be a negative shock coinciding with the divorce event, which subsequently drives the negative firm outcomes. However, suppose we do not observe any impacts of divorce on firm outcomes after a divorce event where only one of the couple owns the firm. In that case, one would have to make an argument for why such a negative shock would not occur in the latter type of divorce and subsequently drive firm outcomes. To the extent that our assumption holds, we can compare results across different types of divorce events to alleviate concerns regarding the concurrent shock.

4.3 Identifying Key Channels Behind Divorce

Importantly, we use different types of divorce events to identify the key mechanism through which divorce affects firm outcomes. Even if we can identify the reduced-form effects of divorce on firm outcomes, understanding how divorce affects firm outcomes is important and policy relevant. Broadly, we categorize three main channels through which divorce may affect firm outcomes.

The first channel is losing a valuable partner who helped run the business. To test this mechanism, we use heterogeneity analyses based on initial firm size, assuming that the impacts of losing a valuable partner through divorce are smaller for larger firms that are also likely professionally managed.

The second channel is the division of business' value and the subsequent financial burdens. This channel is most salient when a married couple jointly owns a business and has to split the value of their business upon divorce. Therefore, we use a divorce event where only one of the common-law spouses owns the business (mostly in Ontario, Quebec or British Columbia before 2013), and therefore faces no legal obligations for splitting assets. If we do not see any impacts on firms after divorce in such cases, then we can make stronger claims that splitting the business' value is the primary channel through which divorce affects the outcomes of interest. Furthermore, focusing on a divorce event where only one of the married spouses owns the business, we can also test how much the division of assets affects firm outcomes. Even though the married couple has to equally split the business' value, the baseline value

of the firm will not be split with the departing spouse who did not have any ownership in the firm before. Therefore, this type of divorce events would serve as a middle case in which the division of assets is going to be smaller (assuming the business was established before the marriage) and therefore, its subsequent impacts on the firm are smaller as well.

The last channel is the combination of all other changes associated with divorce that increased emotional and time costs of the operating spouse, such as changes in family structure, home location, and child custody. We label this as "inattention channel" because the spouse who continues to operate the firm has reduced attention to focus on running the business. If we assume that such emotional costs would dissipate over time, then this channel would not drive long-run outcomes. However, since it is difficult to observe these costs in the data, we cannot completely rule out this last channel potentially having some impacts on firm outcomes. Therefore, to isolate the second channel (division of assets and subsequent financial burdens) from the others, we exploit the 2013 reform in British Columbia, which changed the requirement for splitting assets among common-law partners upon divorce.

4.4 Difference-in-Differences Design Using 2013 Reform in B.C.

To further test whether the division of the business' value is the key channel through which divorce affects firm outcomes, we use the 2013 Family Law Act in British Columbia, which mandated common-law couples who had lived together for at least 2 consecutive years to split assets after divorce. In particular, we exploit this reform to test whether the asset-splitting requirement affected the probability of divorce among common-law partners and subsequently how it affected their business outcomes.

To identify the effects of the reform, we compare the outcomes of common-law couples in British Columbia who had been in relationship for at least 2 consecutive years before 2013 with those of common-law couples in control provinces (mainly Ontario and Quebec). Since the reform changed how the family property (e.g., business) is divided upon divorce, the difference-in-differences design allows us to identify whether the business-splitting is the key channel through which divorce affects firm outcomes. We use a two-step procedure using the reform as an instrument. First, we estimate whether the reform changed the probability of divorce among common-law partners in British Columbia relative to their counterparts in control provinces (Ontario and Quebec). Then we estimate the reduced-form effects of the reform on the key firm-level and owner-level outcomes using the same difference-in-differences design. If the reform affects the probability of divorce among common-law partners, then we can rescale the reduced-form estimates by the first-stage estimate to identify how the

division of the business' value through divorce affects the subsequent firm-level outcomes. This is because the reform precisely changed how the property is divided among common-law partners, so if the divorce were to have any impacts on firm outcomes, it has to be through the asset-splitting mechanism.

5 Results and Economic Interpretations

This section reports estimation results from Section 4 and discusses the interpretation of the results. We first document changes in firm outcomes following divorce, then examine owner-level outcomes. We next assess the robustness of these patterns and examine potential mechanisms.

5.1 Changes in Ownership and Firm Outcomes

Panel (a) of Figure 1 plots the event-study estimates of Equation (1) for the focal owner's and former spouse's ownership shares. Both series are stable during the four years before divorce. In the year of divorce, the focal owner's share rises by 5.7 percentage points and continues to increase, reaching 23.2 percentage points by the fourth year after divorce. This is equivalent to a 45 percent increase relative to the focal owner's pre-divorce mean. The former spouse's share falls by 6.8 percentage points in the year of divorce and by 22.1 percentage points by the fourth year after divorce, a 46 percent decline relative to its pre-divorce mean. Columns (1) and (2) of Panel A of Table 2 summarize the average effects from the year of divorce through four years afterward. The focal owner's share rises by 16.5 percentage points, while the former spouse's share falls by 16.6 percentage points. These nearly one-for-one changes are consistent with ownership being consolidated in the focal owner after divorce.

Panels (b) through (d) of Figure 1 show that this ownership consolidation is accompanied by a contraction in firm size and operations. Total assets fall by approximately 10 percent in the year of divorce and by 20 to 25 percent in subsequent years. Capital and employment also decline. Capital falls by about 4 percent in the year of divorce and by 12 to 18 percent thereafter, while employment falls by about 9 percent initially and by 17 to 22 percent in the following years. Columns (3) through (5) of Panel A of Table 2 imply average declines of 20 percent in total assets, 13 percent in tangible capital, and 17 percent in employment. The changes following divorce therefore extend beyond the reallocation of registered ownership to the firm's productive inputs.

So far the changes show that firms become smaller after divorce, but they do not indicate

whether the contraction is simply proportional to firm scale or also reflects weaker operating performance. In Panels (a) and (b) of Figure 2, we examine profits and profit margins. We measure profits as total revenue minus total expenses, adding back salary paid to the focal owner (Bonney, Pistaferri and Voena, 2025). Profit margin is defined as profits divided by total revenue. Profits fall by approximately 6,900 CAD in the year of divorce and by about 14,000 to 18,000 CAD in the following years. Column (1) of Panel B of Table 2 shows an average decline of approximately 13,800 CAD, or 15 percent of the pre-divorce mean. The profit margin also falls, by approximately 4 percentage points in the year of divorce and, in Column (2), by 6.6 percentage points on average over the year of divorce and the following four years. Taken together, divorce events among married couples who jointly owned the same firm are associated with large contractions of firm size and weaker firm performance, which persist over time.

Panels (c) and (d) of Figure 2 show that the contraction also reduces the firm's tax base. Taxable income falls by approximately 3,500 CAD in the year of divorce and by 4,200 to 5,400 CAD in the following years. Corporate taxes follow the same path, falling by approximately 900 CAD in the year of divorce and by 1,000 to 1,400 CAD thereafter. Columns (3) and (4) of Panel B of Table 2 show average declines of approximately 4,600 CAD in taxable income and 1,100 CAD in corporate taxes, each about 10 percent of its pre-divorce mean. This could reflect the firm becoming smaller and less profitable after divorce, which reduces its taxable income and, in turn, its corporate tax payments.

5.2 Changes in Owner Outcomes

Having documented how divorce affects the firm, we now examine how it affects the owner directly. Figure 3 plots the event study estimates of Equation (2). Panel (a) shows that personal income rises by approximately 6,300 CAD in the year of divorce, reaches about 10,000 CAD in each of the following two years, and declines modestly to around its level in the year of divorce by the fourth year afterward. Panel (b) shows negative point estimates for deferred corporate income during most of the post-divorce period, although these estimates are not statistically significant.

Columns (1) and (2) of Panel C of Table 2 show that personal income rises by approximately 8,300 CAD, or 12 percent of its pre-divorce mean, while deferred corporate income declines by approximately 1,100 CAD and is not statistically distinguishable from zero. Taken together, these two components imply an increase in total income of approximately 7,200 CAD, or 8 percent of its pre-divorce mean. To assess whether wages account for the

increase in personal income, Panel (c) of Figure 3 and Column (3) of Panel C report the corresponding estimate. Wages rise by approximately 1,600 CAD on average; however, the estimate cannot be distinguished from zero. The increase in personal income therefore does not appear to be driven by a detectable increase in wages. Panel (d) of Figure 3 shows that personal taxes rise immediately after divorce and remain higher throughout the post-divorce period. Column (4) of Panel C of Table 2 shows an average increase of approximately 1,900 CAD, or 16 percent of the pre-divorce mean. Note that the combined (personal and corporate) taxes increased in the medium run on average, as the increase in personal taxes is larger than the reduction in corporate taxes. The long-run revenue impacts after divorce remain ambiguous if the firm continues to shrink in size and taxable income over time.

Overall, these results show that the reduction in firm activity does not translate into lower contemporaneous income for the focal owner. Instead, personal income and tax payments increase after divorce. One explanation lies in how the settlement is financed. As discussed in Section 2, divorce events among married couples are associated with large financial burdens for the operating spouse who has to make cash payments to the departing spouse. The cash payout, typically installed over several years, results in the operating spouse liquidating a part of the company's assets (e.g., capital that can be sold for cash) if the firm does not have a lot of retained earnings. Therefore, both personal income and taxes would increase in the short to medium run as the operating spouse is liquidating the company's assets to make cash payments. At the firm level, by contrast, taxable income and corporate taxes each fall by about 10 percent as the firm contracts, so the corporation remits less tax at the same time as its owner pays more. The fact that the two tax bases move in opposite directions suggests the settlement shifts income out of the corporation and onto the owner's personal return.

5.3 Robustness Checks

We conduct two checks on the sensitivity of our estimates to the length of the event window and to the construction of the control group. First, we restrict the control group to owners whose separations occur at least nine years after the treated owner's separation, rather than five years later, and extend the event window through eight years after separation. This specification ensures that control owners remain untreated throughout the longer window, although it reduces the available sample at longer horizons. The estimates show similar patterns to the baseline specification. Ownership becomes consolidated in the focal owner, while assets, capital, employment, and profits decline after separation. The effects remained persistent throughout the event window. Second, we also estimate the event study using

owners who do not separate during the sample period ("never-treated") as the control group. This alternative comparison group yields qualitatively similar post-separation changes in ownership and firm outcomes.

6 Mechanism

Our main results show that divorce is followed by ownership consolidation and a decline in firm scale and profitability, but they do not tell us through what channels this happens. We therefore examine three potential mechanisms: the loss of the spouse as a valuable business partner, the financial adjustment associated with dividing business assets, and the disruption of the owner's attention.

6.1 Three Key Channels

Losing a Valuable Partner. One explanation for the decline in firm outcomes is that the spouse may have been involved in the firm's management or day-to-day operations, or perhaps have supplied firm-specific capital or knowledge. In that case, separation could reduce firm performance by removing a valuable worker or manager. If this is the primary channel, the effects should be smaller among larger firms, which are more likely to be professionally managed and less dependent on the contribution of one spouse.

Figure 4 compares the baseline estimates with estimates for firms that employed at least five workers in the year before separation. Since most firms in our analysis sample are small private businesses in our sample, both the median and mean firm size is around one employee. So firms with at least five employees represent top 25 percent of firms in the size distribution. It reports effects on a proportional scale. Level estimates are divided by the pre-separation mean, while log estimates approximate proportional changes. Navy circles show the baseline estimates for all firms, and orange triangles show the estimates for larger firms. The ownership reallocation is similar across the two samples. In both cases, the focal owner's share rises by roughly 32 percent of its pre-separation mean, while the former spouse's share falls by a similar amount. Firm outcomes also do not exhibit a smaller contraction among larger firms. Total assets and capital decline by at least as much as in the baseline sample, while the declines in employment, profits, and profit margins are not statistically different.

These results suggest that the loss of the spouse's involvement in the business is unlikely to be the primary explanation for the negative firm performance. Larger firms are more

likely to be professionally managed, with responsibilities distributed across more workers, yet they experience broadly similar declines after separation.

Ownership Division and Liquidity. A channel through which separation may affect firms is the division of business wealth. How much of the firm has to be given up depends on what the departing spouse can claim, which gives us three types of events, ordered by the size of that claim. When both spouses hold shares ("co-owned"), the departing spouse has an equity stake that must be transferred and, in addition, a claim on the value accumulated during the relationship. When only the focal owner holds shares ("sole-owned"), there is no stake to transfer, but a legally married spouse can claim a portion of the value accumulated during the marriage. When the firm is sole-owned and the couple is in a common-law relationship, neither applies, because common-law partners generally had weaker rights to property division. If the division of business wealth is what drives our main results, effects should be largest for co-owned couples, followed by for sole-owned married couples, and smallest for sole-owned common-law couples.

Figure 5 reports average post-separation effects for three types of divorce events. Black circles represent our baseline results (discussed in Section 5) among married couples who jointly owned the same firm. Navy triangles represent estimates for "sole-owned" common-law partners, while orange diamonds represent estimates for "sole-owned" married couples. The focal owner's share changes little in the latter two groups, declining by around 1 percent of its pre-separation mean. This differs from the main jointly owned-firm sample, in which the focal owner absorbs a substantial share previously held by the former spouse. In the absence of a direct reallocation of shares, firm and owner outcomes differ only a bit by marital type among sole-owned couples.

Turning to the firm's balance sheet outcomes, total assets fall by approximately 20 percent among co-owned couples, by 7 percent among sole-owned married owners, and by 1 percent among sole-owned common-law owners, where the estimate is not statistically distinguishable from zero. Employment declines by approximately 17, 7, and 2 percent across the same three groups, and again the common-law estimate cannot be distinguished from zero. The contraction in firm size therefore scales with what the departing spouse can claim.

Profits and profit margins decline substantially among co-owned couples, by approximately 15 and 13 percent of their respective pre-separation means. Among the two sole-owned groups both estimates are small, neither is distinguishable from zero, and their confidence intervals overlap almost entirely, so these two outcomes cannot speak to marital type. Profitability therefore deteriorates only where the departing spouse held an equity stake.

On personal financial adjustments, personal income rises by approximately 12 percent among co-owned couples and 4 percent among sole-owned married owners, while personal taxes rise by approximately 16 and 8 percent. For sole-owned common-law owners both are close to zero. Value leaving the firm therefore reappears on the owner's personal tax return, and in the same order, which is consistent with a financial adjustment associated with property division.

We next examine whether the margin of adjustment differs with firms' internal financial resources. We divide firms into tertiles based on pre-separation retained earnings, using this measure to proxy firm's internal financial buffer. The results indicate that the margin of adjustment differs across firms. Firms with low pre-separation retained earnings experience a larger decline in capital, consistent with having to liquidate their physical capital stock when internal resources are limited. On the contrary, firms with higher retained earnings experience a smaller reduction in capital and a decline in retained earnings after separation. This pattern is consistent with greater internal resources allowing firms to absorb more of the adjustment without reducing physical capital. Despite these different adjustments, profits decline by similar amounts in both groups. This suggests that firms with different levels of internal financial buffer adjust along different margins, but both experience a comparable decline in profitability following separation.

Taken together, the heterogeneity analyses across three types of divorce events show that the effects of divorce are concentrated in the baseline case where married couples jointly owned the same firm and are forced to split the business' value (based on the pre-event ownership rate). Focusing on sole-owned couples, either common-law or married, we find much smaller to null effects on firm size and subsequent performance measures since the division of assets is smaller or not required. These results highlight the importance of the asset-splitting as the key channel through which divorce affects firm outcomes.

Inattention. Separation may also affect firms by distracting owners from business decisions during an emotionally and administratively demanding period. If this disruption is the main channel, its effects should be temporary and should be smaller in larger, more professionally managed firms, where day-to-day operations are less dependent on the owner. As shown in Figure 1 and 2, the declines in assets, capital, employment, and profits persist for several years after separation rather than returning to their pre-separation levels. Moreover, Figure 4 shows that larger firms experience contractions of a similar magnitude to those in the baseline sample. These patterns suggest that inattention alone is unlikely to account for the sustained decline in firm outcomes. Separation may still disrupt owners' attention in the

short run, but the persistence of the effects points to a more lasting adjustment in the firm.

Summary. Overall, the evidence points most strongly to the ownership division and liquidity as an important source of the post-separation contraction in firm outcomes. Among firms in which the spouse holds no shares before separation, legally married owners experience larger declines in assets and employment, as well as larger increase in personal income and taxes relative to common-law owners. The results by retained earnings as a proxy for immediate internal financial resource in the company further suggest that firms with different levels of buffers adjust along different margins after separation. By contrast, the persistence of the effects and their similar magnitude among larger, more professionally managed firms make the loss of a valuable partner or temporary inattention incomplete explanations for the overall lasting decline. These comparisons do not establish that property division accounts for all of the effect of separation, but they are consistent with it imposing a persistent financial adjustment on the firm.

6.2 Using 2013 BC Reform to Isolate the Key Channel

As explained in Section 4, we use the 2013 Family Law Act in British Columbia to isolate the division of the business' assets as the key channel behind how divorce affects firm outcomes. We find that the reform significantly reduced the probability of divorce among common-law partners in British Columbia relative to common-law partners in control provinces. Subsequently, we find significant and large increases in firm size (e.g., total assets, capital, and employment) and performance (profits and profit margins). Once we rescale these reduced-form estimates on the key outcomes by the first-stage estimates on divorce rates, our IV-estimates on firm outcomes are consistent with our event-study estimates and quantitatively comparable: divorce leads to decreases in firm size and performance, followed by increases in owners' tax burdens in the short to medium run.[4]

7 Conclusion

This paper studies how divorce affects private firms owned by separating couples. Using Canadian administrative data that link marital status, individual tax returns, firm ownership, and balance sheets, we find that divorce is associated with a persistent contraction in

[4]These results are currently under review for vetting. An updated draft incorporating these results based on the reform will become available in late September.

jointly owned firms. Ownership becomes consolidated in the focal owner, while firms reduce assets, capital, employment, profits, and corporate tax payments. At the same time, the focal owner's personal income and tax payments rise without a corresponding increase in wages. The evidence points to the financial adjustment associated with dividing business wealth as an important source of the decline in firm performance. The declines are largest when the former spouse has the strongest potential claim on the business and much smaller where that claim is limited.

Our findings have two policy implications. First, family-property rules are usually evaluated in terms of how they allocate resources and insure spouses upon divorce. Our results identify an additional consequence when household wealth is embedded in an illiquid operating business. Settling a spouse's claim may reduce the firm's capital, employment, and profitability, so the effects can extend beyond the separating household.

Second, the broader effects of family-property law depend on both behavioral and fiscal responses. The 2013 British Columbia reform shows that extending property-division rights can alter separation decisions. Our main results show that divorce also changes the composition of tax payments. Corporate tax payments decline as firms contract, while the focal owner's personal tax payments rise. Combined payments increase in the medium run, although the longer-run revenue effect remains uncertain and hinges on firm dynamics over longer horizons. Evaluating family-property rules therefore requires considering their distributional consequences for spouses alongside their effects on separation rate, business activity, and fiscal revenues.

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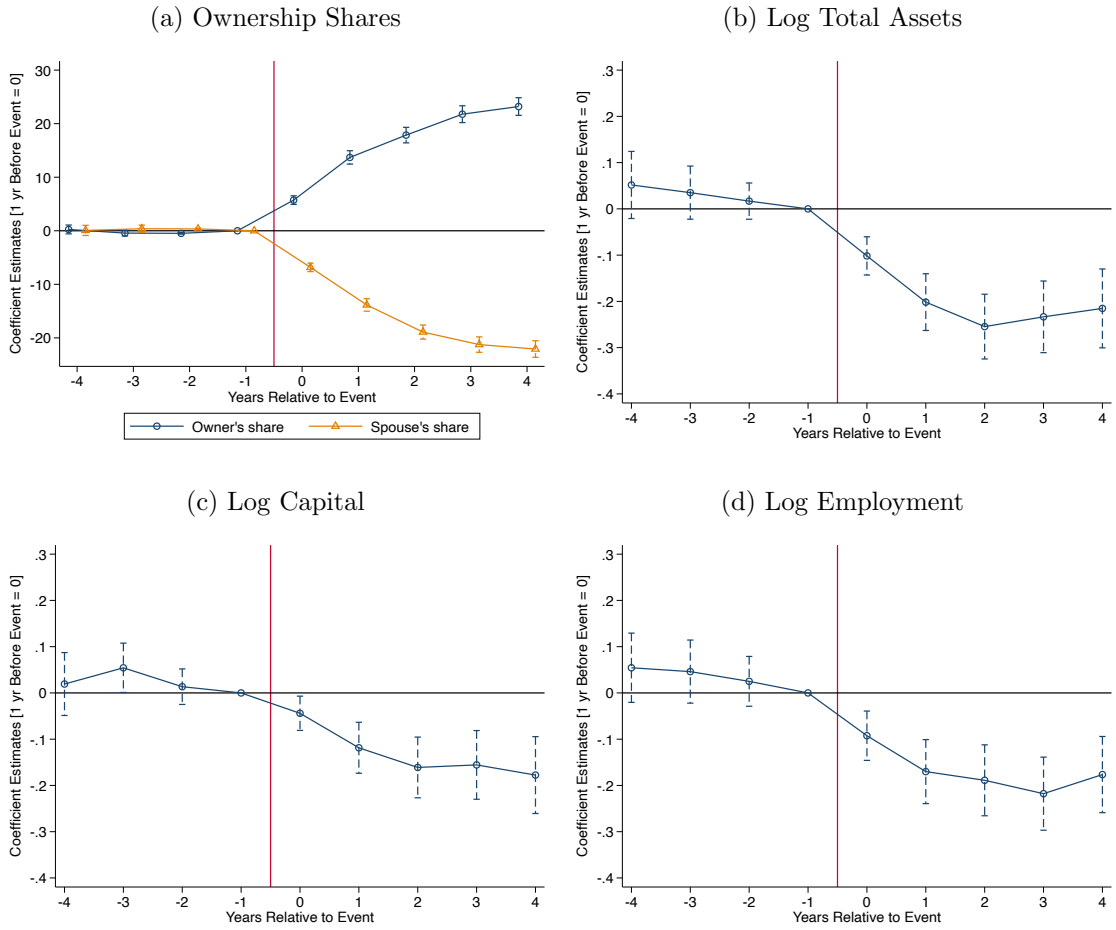
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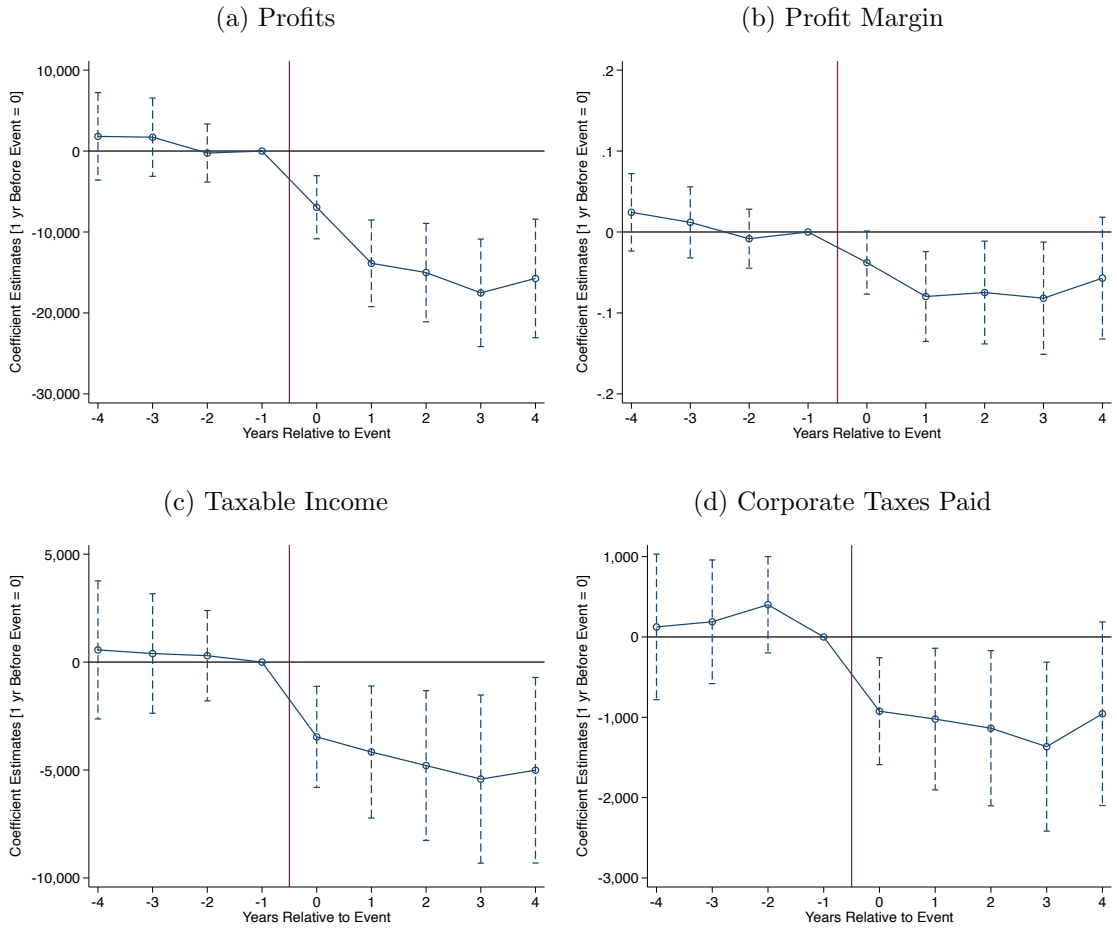
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Figure 1: Ownership and Firm Size



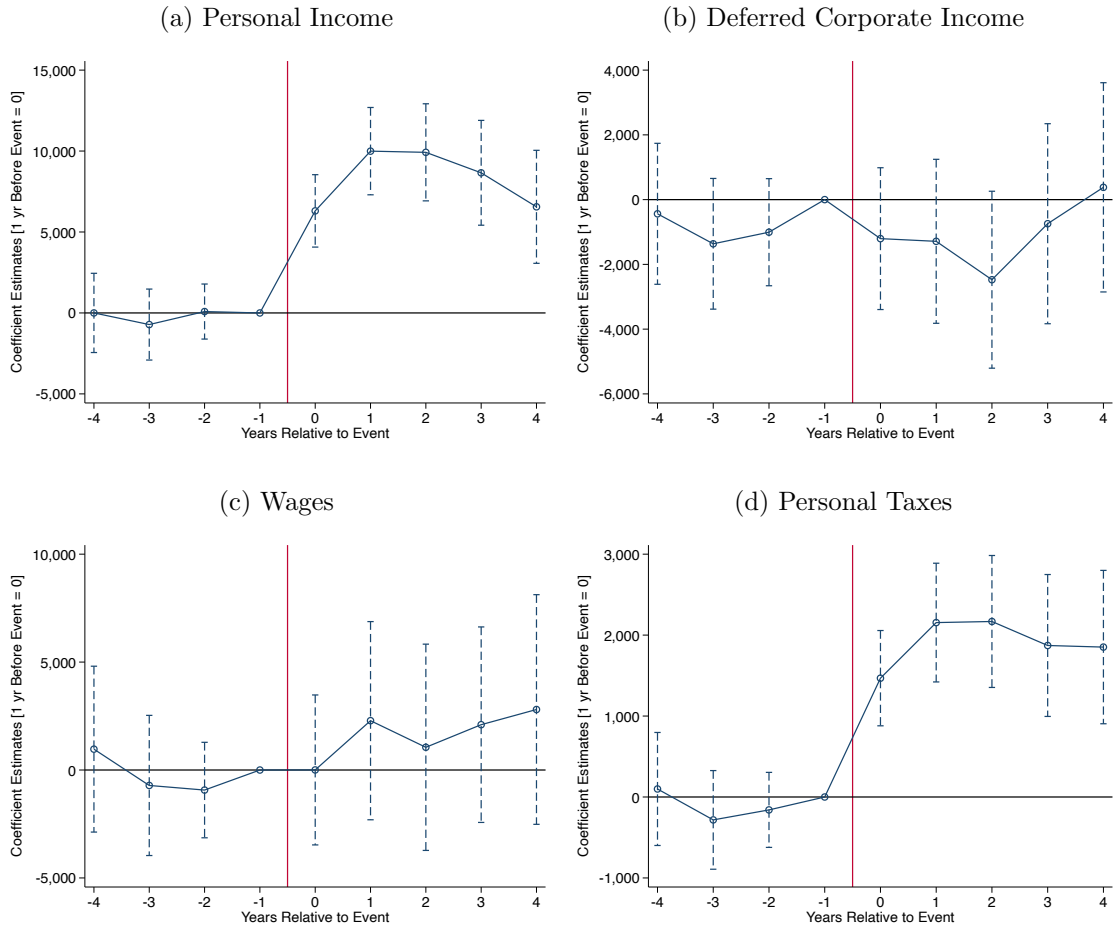
Notes: Panels (a) to (d) plot coefficients from the stacked event-study specification in Equation (1). The sample consists of firms in which the focal owner and spouse each held at least 20 percent of shares before divorce. Treated firms are matched to control firms whose owners divorce at least five years later. Event time zero is the year of divorce, and the omitted reference period is one year before divorce. The vertical line marks the divorce event. Whiskers show 95 percent confidence intervals based on standard errors clustered by firm. Panel (a) plots the focal owner's and the former spouse's ownership shares, both measured in percentage points. Total assets, tangible capital, and employment are in logs.

Figure 2: Firm Performance and Corporate Taxes



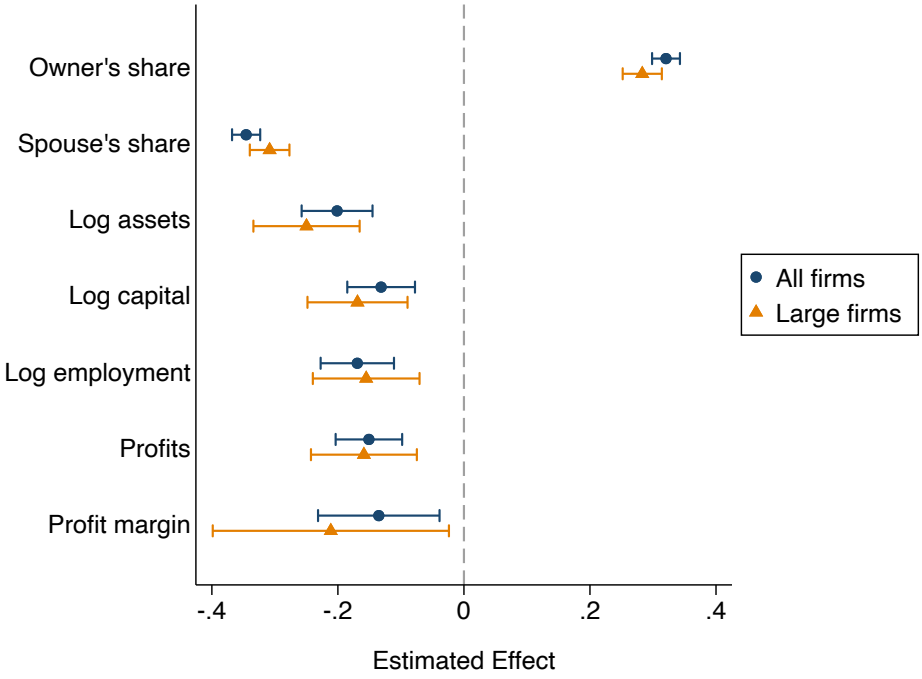
Notes: Panels (a) to (d) plot coefficients from the stacked event-study specification in Equation (1). The sample consists of firms in which the focal owner and spouse each held at least 20 percent of shares before divorce. Treated firms are matched to control firms whose owners divorce at least five years later. Event time zero is the year of divorce, and the omitted reference period is one year before divorce. The vertical line marks the divorce event. Whiskers show 95 percent confidence intervals based on standard errors clustered by firm. Profits equal total revenue less total expenses plus salary paid to the focal owner and are in Canadian dollars. Profit margin is profits divided by total revenues. Taxable income and corporate taxes are reported in Canadian dollars.

Figure 3: Owner Income and Taxes



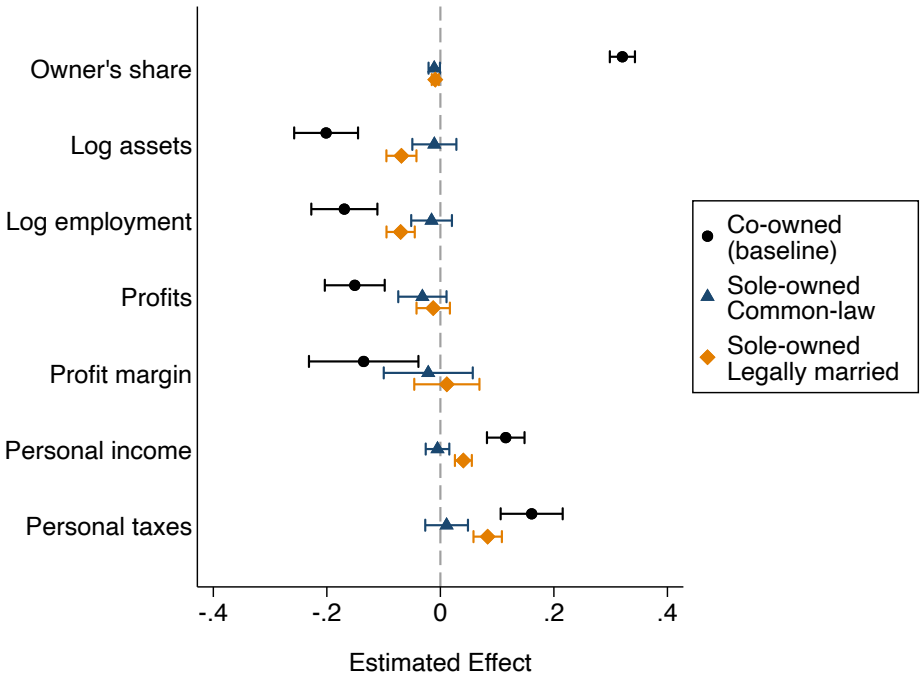
Notes: Panels (a) to (d) plot coefficients from the stacked event-study specification in Equation (2). Treated owners are matched to control owners who divorce at least five years later. Event time zero is the year of divorce, and the omitted reference period is one year before divorce. The vertical line marks the divorce event. Whiskers show 95 percent confidence intervals based on standard errors clustered by owner. All outcomes are measured in Canadian dollars. Personal income is pre-tax income reported on the individual tax return, deferred corporate income equals the annual change in retained earnings plus current corporate taxes, and wages are employment earnings reported on T4 slips.

Figure 4: Heterogeneous Effects by Firm Size



Notes: The figure reports average event-study estimates from the year of divorce through the fourth year afterward. Navy circles show estimates for all firms in the baseline sample, which were jointly owned by legally married couples before divorce. Orange triangles show the corresponding estimates for firms with at least five employees one year before divorce. To place outcomes on a common scale, estimates for outcomes measured in levels are divided by the relevant sample's pre-divorce mean. Coefficients from log specifications are interpreted as approximate proportional changes. Whiskers show 95 percent confidence intervals based on standard errors clustered by firm.

Figure 5: Heterogeneous Effects by Marital Type



Notes: The figure reports average event-study estimates from the year of divorce through the fourth year afterward, estimated separately on each sample. Black circles show estimates for the baseline sample, in which both spouses held at least 20 percent of the firm before divorce, regardless of marital type. Navy triangles and orange diamonds show estimates for common-law and legally married couples respectively, in the sample where the focal owner holds shares and the spouse holds no shares before divorce. To place outcomes on a common scale, estimates for outcomes measured in levels are divided by the relevant sample's pre-divorce mean. Coefficients from log specifications are interpreted as approximate proportional changes. Whiskers show 95 percent confidence intervals based on standard errors clustered by firm for firm outcomes and by focal owner for owner outcomes.

Table 1: Descriptive Statistics on Matched Owners

	Control (1)	Treated (2)	Total (3)
Age	49.25	49.18	49.21
	(10.53)	(10.34)	(10.44)
Total income	83,569	85,196	84,383
	(61,320)	(66,031)	(63,715)
Deferred corporate income	13,672	13,261	13,466
	(30,679)	(29,964)	(30,320)
Personal income	69,898	71,935	70,916
	(45,957)	(50,305)	(48,184)
Wages	47,148	46,303	46,726
	(70,081)	(60,070)	(65,260)
Personal taxes	11,220	11,830	11,525
	(12,326)	(13,354)	(12,853)

Notes: This table reports means and standard deviations of owner-level characteristics measured in the year before the event, for the matched sample used in our main specification. Treated owners are those who divorce in a given year. Control owners are matched owners who divorce at least five years later. The sample is restricted to male owners who hold at least 20 percent of a single business and whose spouse also holds at least 20 percent of that business. Personal income is pre-tax income reported on the individual tax return, and deferred corporate income is the annual change in retained earnings plus current corporate income taxes. Total income is the sum of the two. All monetary values are in Canadian dollars. Standard deviations are in parentheses.

Table 2: Average Effects of Divorce on Firm and Owner Outcomes

Panel A. Firm ownership and size					
	Owner's share	Spouse's share	Log assets	Log capital	Log emp.
	(1)	(2)	(3)	(4)	(5)
Treated#Post	16.451	−16.586	−0.201	−0.131	−0.169
	(0.579)	(0.547)	(0.029)	(0.027)	(0.030)
Observations	33,240	33,240	32,520	29,780	20,660
Pre-event mean	51.30	47.99	11.43	10.76	0.78

Panel B. Firm performance and corporate taxes				
	Profits	Profit Margin	Taxable income	Corporate taxes
	(1)	(2)	(3)	(4)
Treated#Post	−13.815	−0.066	−4.571	−1.081
	(2.467)	(0.024)	(1.421)	(0.386)
Observations	33,050	32,570	33,050	33,050
Pre-event mean	91.61	0.49	45.30	11.19

Panel C. Owner income and taxes				
	Personal income	Deferred corp. income	Wages	Personal taxes
	(1)	(2)	(3)	(4)
Treated#Post	8.286	−1.066	1.649	1.903
	(1.215)	(1.031)	(1.976)	(0.330)
Observations	64,810	64,810	64,810	64,810
Pre-event mean	71.94	13.26	46.30	11.83

Notes: The estimated coefficients are averages of the event-study estimates from the year of divorce through the fourth year afterward. The sample consists of firms in which the focal owner and spouse each held at least 20 percent of shares before divorce. Treated firms and owners are matched to controls whose owners divorce at least five years later. Panels A and B report firm-level estimates from Equation (1), and Panel C reports focal-owner estimates from Equation (2). Ownership shares are measured in percentage points. All monetary outcomes are measured in thousands of Canadian dollars. Assets, tangible capital, and employment are in logs, while taxable income is measured in dollars. Profits equal total revenue less total expenses plus salary paid to the focal owner, and profit margin equals profits divided by total revenues. Deferred corporate income equals the annual change in retained earnings plus current corporate taxes. The pre-event mean is calculated for treated observations one year before divorce. Standard errors, in parentheses, are clustered by firm in Panels A and B and by owner in Panel C.