What Commercial Lawyers Need to Know about Family Law Property

Michael A Fellows [1]
Barrister-at-law, mediator, arbitrator

1.0 Introduction

1.1 This paper is divided into 3 parts:

[a] A short discussion of the legislative provisions of the *Family Law Act* ("the Act"); together with a comment concerning 'binding financial agreements'.

[b] The mechanisms by which commercial structures and agreements are put at risk once a marriage has broken down. [2]

[c] A short discussion about avoiding litigation and being settlement minded once a family law dispute has arisen.

1.2 The median duration of a marriage is a little more than 12 years. The peak periods for the incidence of divorce are in the age brackets between 39 and 54 years of age; [3] a bracket when people typically reach their peak earning capacity and begin the acquisition of real assets. In 2001 there were 48,935 divorces; 121,752 marriages. A crude statistic - at least 40% of all marriages end in divorce.

1.3 Statistics are not readily available for *de facto* relationships.

1.4 Commercial lawyers ought always be aware that the "happy family" present at the time family trust and corporate structures are created may not remain so happy.

---

[1] Sir George Kneipp Chambers, 53-61 Wills Street, Townsville
[2] where I refer to "marriage" and "husband" and "wife" in this paper I intend to encompass *de facto* relationships and the partners of those relationships - the *Family Law Act* extends the jurisdiction of the family law courts to such relationships and treats them as the same as a marital relationship
[3] 38.2% of all divorces - the data in this paragraph does not include *de facto* relationships - see http://www.abs.gov.au/ausstats/abs@.nsf/Products/9637C5730D66B951CA257AC500113161?opendocument

2.0 The provisions of the Act

2.1 For present purposes the primary section is s. 79 which says:

[a] The court "may make such order as it considers appropriate" to alter the interests of the parties to a marriage to the property that they or either of them own;

[b] But no order can be made unless it is "just and equitable" to make the order.

2.2 It is not possible to summarise more than 30 years of jurisprudence concerning s. 79 in this short paper; other than to highlight several key matters:

[a] Except in special cases the court indentifies and values the property that exists as at the date of trial rather than the date of separation or some other time;

[b] The court is not confined to what is sometimes called "matrimonial property" – all of the property of the parties whether acquired before, during or after the relationship – is subject to identification and valuation;

[c] In assessing the property division to make, section 79 allows a court to look "backwards" at the contributions that have been made during the course of the relationship and "forwards" to the future needs of one or both of the parties;

[d] The court looks at both the financial and non-financial contributions that have been made during the relationship; and though there is no legal assumption that contributions have been equal [4] in a relationship of say 10 years duration or more it can be difficult to mount an argument that contributions have not been equal. So for example the following observation of the Full Court in *Re McLay* [5] illustrates what occurs:

> *The reference to "normal range" in Ferraro and in her Honour's judgment is not a return to a presumption of equality as a starting point or any other presumption or starting point but is a practical recognition of the circumstance that in many marriages each party contributes in ways which might be described as the normal way in our society and that in any qualitative evaluation of those matters the likely outcome is one of equality. This is repeatedly recognised in the day-to-day experience of this*

[4] see the decision of the High Court in *Mallett* (1984) 156 CLR 605

[5] (1996) 20 Fam LR 239

court over many years in dealing with a very large number of s 79 cases. In many cases any assessment of the facts readily makes it clear that an outcome of equality within pars (a) to (c) is most likely and that a lengthy trial in which those facts are examined in detail will produce no different result. It will only mean significant extra costs to the parties and an unproductive use of the time of the Court.

[e] The previous statement may require modification in cases where one of the parties makes an overwhelming financial contribution but there have been repeated judicial warnings against under-valuing the role of the home-maker and so favouring the partner who earns significant income or brings in substantial property. [6]

[f] When considering future needs particular attention tends to be given to the relative earning capacity of the parties – in the Full Court's decision in *Clauson* [7] this passage appears:

It has long been recognised that in most cases the most valuable 'asset' that a party can take out of the marriage is a substantial, reliable, income-earning capacity.

2.3 The expression 'just and equitable' is not and has not been capable of exhaustive definition. There are no fixed rules. [8] It follows that the discretion to alter property interests is wide though not so wide as to permit an exercise of 'palm tree justice.' [9]

2.4 As a result it is not possible for family lawyers to give precise advice – we can say what the law is; but predicting its application in individual cases can be difficult. That may be frustrating for clients – but especially for businessmen or women who separate from their marital partners – they can seek from their lawyers a degree of 'commercial' certainty that cannot be delivered.

2.5 A mechanism for avoiding uncertainty is to make use of 'binding financial agreements'. Part VIIIA of the *Family Law Act* allows a couple to enter into a binding financial agreement before or during a marriage; and after a marriage has broken down. [10] These agreements can govern how some or all of the property of the parties is to be dealt with during and/or after the marriage. Properly made, these agreements can oust the jurisdiction of the family courts; and they can be an effective protective tool for those persons who are already wealthy at the time of a marriage or for those entering into a second (or third!) marriage.

---

[6] *Ferraro* (1993) FLC 92-335; *Figgins* (2002) FLC 93-122

[7] (1995) 18 Fam LR 693 at 710

[8] *Mallet* at 608; *Stanford* [2012] HCA 52 at [36]

[9] *Stanford* at [38]

[10] Part VIIIB of the Act has similar provisions concerning *de facto* relationships.

2.6 Recent jurisprudence has been complicated and caused not a little angst amongst the profession. The technical requirements for making a proper agreement have been the source of much litigation. The courts have required quite strict compliance with the legislation before the ouster of jurisdiction is accepted. There have been some serious professional negligence claims against law firms. [11] A consequence is that many firms have withdrawn from this line of work; but it can be profitable work for those firms willing to assist their more wealthy clients. Anecdotal evidence suggests that fees well in excess of $50,000 can be earned in complex matters. My practical recommendation is that, if asked to draft a binding financial agreement, it would be prudent for there to be a close liaison between the commercial and family lawyers in a firm; and with the client's accountant. It is very much a team effort; and needs to be a careful one.

3.0 The way in which commercial agreements and arrangements are at risk.

3.1 It is important to bear in mind that one of the chief purposes of the *Family Law Act* is to ensure that upon breakdown of a marriage there is a fair division of property and an allocation of financial responsibility between former partners.

3.2 This part of my paper will be divided into two sections:

[a] A discussion of the jurisprudence which has developed as a mechanism for assisting the court to achieve the purposes of the Act; and

[b] A discussion of various sections of the Act that supplement or enlarge the general power of the court under s. 79.

3.3 <u>Jurisprudential developments</u>

3.4 The Family Court and Federal Circuit Court of Australia are creatures of statute and do not, ordinarily, have jurisdiction beyond that conferred by statute.

3.5 The consent of the parties cannot confer an extended jurisdiction. [12]

3.6 A difficulty in family law property matters can be that a range of commercial agreements or structures control or influence the outcome of the case – typically these will include corporate or trust structures, partnership agreements, and mortgages or other forms of security.

---

[11] Queensland law firms should, in particular, consult the various guidelines issued by Lexon Insurance Pty Ltd.
[12] *Ridley v Whipp* (1916) 22 CLR 381

3.7 In earlier years lawyers relied upon the cross-vesting legislation as a mechanism for seeking relief from the consequences of commercial agreements or structures. Following the constitutional collapse of the cross-vesting legislation [13] that path was closed.

3.8 As a result greater attention has focussed upon the concept of accrued jurisdiction following cases concerning the Federal Court of Australia. [14] The family courts accept that they have accrued jurisdiction to determine the non-federal aspects of a justiciable controversy of which the family law claim forms a part where those non-federal aspects are "attached" and "not severable." [15]

3.9 The most usual examples where the accrued jurisdiction is invoked are those involving family tax planning or financial planning arrangements. Typically, a wife may allege that the husband's property includes a beneficial interest in the property owned by his parents - and rely upon the remedial constructive trust as the legal mechanism to advance that claim. Or a husband might wish to challenge a debt (and associated security) alleged to be owed by the wife to her parents (or an associated company). A guarantee might be challenged by alleging duress or unconscionable conduct. [16] In these typical examples a parent (or other relative) of the married couple (or one of them), along with, if necessary their attached corporate and/or trust structures will end up as respondents to the family court proceedings. [17]

3.10 So it follows that the commercial arrangements made within a family or by a family member with a third party can be subject to challenge in the family courts, rather than in the civil courts. Thus far, such a challenge is made on the basis of ordinary principles of law or equity.

3.11 But such legal or equitable challenges may fail. A debt to a third party or related family member may remain.

3.12 The family courts have long recognised that the exercise of discretion allows the court either to discount or ignore a debt or to direct that one or other of the parties to the marriage assume responsibility for a debt and indemnify the other in respect of it.

3.13 As to the first matter where there are undocumented or insufficiently documented transactions alleged to create debts by a spouse to some

---

[13] *re Wakim; ex parte McNally* (1999) 163 ALR 270

[14] *Philip Morris Inc v Adam P Brown* (1981) 148 CLR 457; *Fencott v Muller* (1983) 46 ALR 41; *Stack v Coast Securities* (1983) 49 ALR 193

[15] *Marriage of Warby* (2001) 28 FamLR 443

[16] as in the typical *Amadio* claim - see *Commercial Bank of Australia Ltd v Amadio*

[17] as was the factual circumstance in *Warby*

other family member, it can be common for the family courts to ignore or discount the debt.

3.14 So long as the debt/liability is unsecured there is no requirement upon the family courts to protect the interests of unsecured creditors; nor is there a rule of priority between creditor and spouse. [18] In *Commissioner for Taxation & Worsop* [19] for example, the husband owed in excess of $12,000,000 for unpaid tax, interest and penalties; the wife being ignorant of and innocent in respect of the husband's tax evasion. The matrimonial home was worth $4,750,000. Notwithstanding the intervention of the ATO in the proceedings the trial judge concluded that on sale of the house the ATO could receive only half the proceeds; the wife to receive the balance. The decision was approved on appeal.

3.15 It follows that so long as the debt to a third party or relative is unsecured the creditor cannot be certain that property otherwise available for execution (that is property in the title of the debtor) will be so available.

3.16 My recommendation is that, even in the friendliest of interfamily borrowing/lending careful thought be given to

[a] Properly documenting the transaction; and

[b] Taking of security for the debt/liability created – at least where the sum of money is significant.

3.17 Sometimes the problem can be that assets are "locked up" in a company or trust. Provided the facts are clear enough so as to show that the marital partner exercises full control of the entity and can apply the assets of that entity as she or he wishes for their own benefit the family courts have always been prepared to go behind the corporate or trust veils and declare that the entity in question is the "alter ego" of that marital partner so that the assets of the company or trust are treated as the assets of that partner. [20]

3.18 <u>Legislative assistance to challenge commercial structure/agreements</u>

3.19 Section 106B(1) of the Act provides:

In proceedings under this Act, the court may set aside or restrain the making of an instrument or disposition by or on behalf of or by direction or in the interest of, a party which is made or proposed to be

---

[18] *Biltoft* (1995) FLC 92-614; *Aldous* (1996) FLC 92-715

[19] (2009) FLC 93-392

[20] *Ascot Investments Pty Ltd v Harper* (1981) 148 CLR 337; *Kennon v Spry* [2008] HCA 56 per French CJ at [68].

made to defeat an existing or anticipated order in those proceedings or which, irrespective of intention, is likely to defeat any such order. [21]

3.20 "Disposition" is defined [22] as including a "gift" and especially as

The issue, grant, creation, transfer or cancellation of or a variation of the rights attaching to an interest in a company or a trust.

3.21 Sub-section (3) provides that

The court must have regard to the interests of and shall make any order proper for the protection of a bona fide purchaser or other person interested.

3.22 Section 106B can be a powerful tool where proceedings in the family courts have already commenced. Any transaction made once proceedings have commenced is at risk if the transaction occurs without the consent and/or knowledge of the other party - that is especially where the obligation of disclosure of financial information (in the family courts) is extensive - the family courts take a "no excuses" approach to disclosure.

3.23 It is important however to bear in mind the words "anticipated". It is not uncommon for a spouse, aware the relationship is breaking down or at risk, to begin a process of transferring or removing assets; or such activity occurs in the period after separation but before proceedings have commenced.

3.24 The words "anticipated" have been interpreted as imposing an objective test not the subjective test of whether anyone actually thought an order would be made. [23] The question is whether a reasonable person in the respondent's position would have considered that there was a real chance, as distinct from a remote possibility, that such a situation would occur. [24]

3.25 The forensic issue in each of these cases is one of examining the circumstances of the relationship and the temporal connection between those circumstances and the making of the transaction in question. So for example in *Kennon v Spry* [25] the husband, 3 years before the date of separation and without the knowledge of the wife, used his power as trustee to remove both himself and the wife as beneficiaries of the trust capital of the family trust. After separation

[21] the underlining is my emphasis
[22] s. 106B(5)
[23] this proposition arose as a result of a sequence in decisions in the period 1980 - 1982
[24] see *Marriage of D* (1984) 10 Fam LR 73
[25] (2008) 40 Fam LR 1

from his wife he then disposed of the assets of the trust by creating 4 trusts in favour of their adult children. The trial judge used s. 106B to set aside all these transactions - that decision was ultimately approved in the High Court. But in *Marriage of Toohey* [26] the transaction occurred 6 years before separation and survived challenge.

3.26 S. 106B can have a limited use – that arises because it is necessary to show that the agreement under attack "is made or proposed to be made to defeat an existing or anticipated order ...". It follows that a temporal connection – as referred to in the previous paragraph – is an essential element to the success of the challenge.

3.27 Nevertheless where a lawyer is asked to draft or advise upon a commercial agreement, amendment of a trust deed, transfer of assets etc and knows (or suspects) that it is in the context of marital disharmony or separation, considerable caution is required. It would be *prima facie* negligent not to advise the client as to the consequences of s. 106B.

3.28 A far broader power to attack commercial agreements or structures comes from Part VIIIA of the Act.

3.29 I set out the major provisions in full.

s. 90AC

This Part overrides other laws, trusts deeds etc.

(1) This Part has effect despite anything to the contrary in any of the following (whether made before or after the commencement of this Part):

(a) any other law (whether written or unwritten) of the Commonwealth, a State or Territory;

(b) anything in a trust deed or other instrument.

(2) Without limiting subsection (1), nothing done in compliance with this Part by a third party in relation to a marriage is to be treated as resulting in a contravention of a law or instrument referred to in subsection (1).

s.90AD

Extended meaning of Matrimonial Cause and Property.

---

[26] (1991) 14 Fam LR 843

*(1) For the purposes of this Part, a debt owed by a party to a marriage is to be treated as property for the purposes of paragraph (ca) of the definition of **matrimonial cause** in section 4.*

*(2) For the purposes of paragraph 114(1)(e), **property** includes a debt owed by a party to a marriage.*

s. 90AE

Court may make an order under section 79 binding a third party

(1) In proceedings under section 79, the court may make any of the following orders:

(a) an order directed to a creditor of the parties to the marriage to substitute one party for both parties in relation to the debt owed to the creditor;

(b) an order directed to a creditor of one party to a marriage to substitute the other party, or both parties, to the marriage for that party in relation to the debt owed to the creditor;

(c) an order directed to a creditor of the parties to the marriage that the parties be liable for a different proportion of the debt owed to the creditor than the proportion the parties are liable to before the order is made;

(d) an order directed to a director of a company or to a company to register a transfer of shares from one party to the marriage to the other party.

(2) In proceedings under section 79, the court may make any other order that:

(a) directs a third party to do a thing in relation to the property of a party to the marriage; or

(b) alters the rights, liabilities or property interests of a third party in relation to the marriage.

(3) The court may only make an order under subsection (1) or (2) if:

(a) the making of the order is reasonably necessary, or reasonably appropriate and adapted, to effect a division of property between the parties to the marriage; and

(b) if the order concerns a debt of a party to the marriage--it is not foreseeable at the time that the order is made that to make the order would result in the debt not being paid in full;

and

(c) *the third party has been accorded procedural fairness in relation to the making of the order; and*

(d) *the court is satisfied that, in all the circumstances, it is just and equitable to make the order; and*

(e) *the court is satisfied that the order takes into account the matters mentioned in subsection (4).*

(4) *The matters are as follows:*

(a) *the taxation effect (if any) of the order on the parties to the marriage*

(b) *the taxation effect (if any) of the order on the third party;*

(c) *the social security effect (if any) of the order on the parties to the marriage;*

(d) *the third party's administrative costs in relation to the order;*

(e) *if the order concerns a debt of a party to the marriage--the capacity of a party to the marriage to repay the debt after the order is made;*

(f) *the economic, legal or other capacity of the third party to comply with the order;*

(g) *if, as a result of the third party being accorded procedural fairness in relation to the making of the order, the third party raises any other matters--those matters;*

(h) *any other matter that the court considers relevant.*

3.30 Section 90AF contains a power to make orders or injunctions under the alternative s. 114 of the Act – s. 90AF has the same wording as s. 90AE so I will not repeat that.

3.31 Two cases illustrate the potential reach of Part VIIIAA.

3.32 In *Allan v Allan and others* [27] the wife's complaint was that the husband was not servicing mortgage debts so that she was at risk of matrimonial property being sold by financiers. She sought orders against the husband and a company that was trustee of the husband's family trust so as to enable her to gain control of the trust so that she

[27] (2009) 41 Fam LR 565; [2009] FamCA 553

could, if necessary, sell the properties owned by the trust (and so reduce the debts). Moreover, within the trust were antiques and collectables said to be worth $20,000,000. Thus her aim was to use those assets so as to reduce debt rather than sell real property. The evidence suggested that the husband's tactic had been to have real property sold rather than the collectables.

3.33 So as to enable the wife to protect her position His Honour made orders substituting the wife as the controller of the trustee company and permitting her to enter into such sales of property and assets as she chose.

3.34 *AC and others v VC and another* [28] involved a discretionary trust of which the husband, wife and their three (adult) children were specified beneficiaries who were entitled to share the capital of the trust upon the vesting day. The husband's mother was the person who controlled the trust via a company of which she was the sole shareholder. Though a beneficiary as to income the husband's mother was not entitled to a share of capital upon the vesting day. The value of the net assets of the husband and wife was about $5,300,000; of which about $2,500,000 was the value of the husband and wife's interest in the trust.

3.35 The trust had been established during the marriage - but its vesting day was in June 2064.

3.36 The husband's mother was utilising up to $3,000 a month from the trust for her living expenses. Based upon her life expectancy and the past pattern of drawing upon the trust this meant her future drawdown from the trust might amount to about $338,000.

3.37 The husband's sister was also a general beneficiary but the evidence was that the assets in the trust had been accumulated over the life of the marriage largely with the input of the husband and no input from the sister. She had not, to the date of trial received any benefit from the trust.

3.38 The trial judge made orders that included:

[a] An order that the trustee bring forward the vesting date of the trust to the date of judgment in June 2010;

[b] Thereafter the trustee was to set aside for the husband's mother the sum of $338,000;

[c] Then the trustee was to distribute the capital of the trust equally to the husband the wife, and the 3 children.

---

[28] (2013) FLC 93-540

3.39 On appeal the Full Court of the Family Court affirmed that the powers in Part VIIIAA were sufficient to make orders requiring the vesting day of the trust to be brought forward. The judgement was set aside because, in natural justice terms, the husband's mother had not been given an adequate opportunity to be heard concerning the sum set aside for her benefit.

3.40 The use of trusts for the purposes of estate planning and as tools for risk and tax minimisation is commonplace and proper. Usually they are created in quite non-controversial ways at a time when the relationship between husband and wife is happy.

3.41 *Allan v Allan* shows that once controversy erupts between husband and wife then the court may put the "innocent" or "responsible" partner in charge of the trust; *AC and others* demonstrates how broad a power exists to create mechanisms by which one (or both) of the partners can enjoy the assets of the marriage now rather than those assets being "locked up" for an essentially indefinite period.

3.42 It must follow that commercial advisers need to be cautious in the advice given to clients concerning the "sanctity" of corporate or trust structures.

4.0 The benefits of early resolution of disputes

4.1 The jurisdiction of the family courts to make orders for the just and equitable distribution of the property of marital partners is broad; and the legislative and jurisprudential methods of assisting to achieve that purpose are extensive. Both the law and practice emphasise openness, fairness, and equity.

4.2 Except in special factual circumstances (and in my career I would struggle to think of even half a dozen that I have been involved in) there will <u>always</u> be a property settlement order.

4.3 Commercial lawyers should encourage their business and commercial clients to enter promptly into settlement negotiations – if only for the usual reasons associated with the costs, delays and stresses of litigation and the diversion of resources from the conduct of business to the conduct of litigation. But there are some more particular considerations requiring attention so far as family property settlements are concerned.

4.4 Section 72 of the Act provides that a partner in relationship is obliged to maintain the other:

[a] to the extent that he/she is able to do so;

[b] if and only if the other party is unable to support her/himself adequately.

4.5 In the immediate aftermath of a separation, especially those where one partner has been the 'stay-at-home' partner, spousal maintenance orders are common – and they are payable from post-tax income.

4.6 A typical example which arises in the case of family businesses is that income has been split for taxation purposes but after separation the partner in control of the business stops the pay packet or drawings of the other partner. There is only one rule – don't do it – unless special facts exist a spouse maintenance order is guaranteed to follow.

4.7 Usually a spouse maintenance order remains in place until a property settlement is made. The best means of bringing a spouse maintenance obligation to an end or modifying the amount of the liability is to make a property settlement order as soon as possible – delay simply extends the obligation.

4.8 The cost of litigation in the family court can be very high once disclosure of significant financial information and the valuation of business entities is required. In one of my current cases the cost of the forensic valuation of the business enterprise is already $180,000 and will top out at something of the order of $220,000. See paragraph 4.14 below for another example of legal fees.

4.9 The family court has developed jurisprudence that can even up the balance of legal power – to level the playing field

4.10 So where most of the assets (or a significant income) is in the hands of one of the parties (the husband typically) orders can be made [29] whereby:

[a] The husband pays to the wife a lump sum sufficient to cover her anticipated legal fees for the trial or for a fixed period; or

[b] The husband is obliged to pay to the wife's solicitors an amount equivalent to the amount he is paying to his own solicitors – a "dollar-for-dollar" order.

4.11 It follows that the usual imbalance of power or resources, which is a feature of so much civil litigation, is not such a factor in family property litigation. If you are paying the other side's legal fees (or at risk of doing so) then, like spousal maintenance, the best mechanism for avoiding or limiting the obligation is to reach a property settlement as soon as possible.

---

[29] typically called "Hogan Orders" after the case of that name

4.12 In other respects there is no advantage for the "wealthy" partner from delay in resolution of the case. The usual rule is that assets are valued at the date of trial. Unless special factors are in play, the other partner is entitled to share in the increase in value in assets that may have occurred during the period from separation to trial.

4.13 On the other hand where losses or a decline in value in assets have occurred in the period after separation those losses will not necessarily be shared if it can be demonstrated that the loss has arisen as a result of the deliberate or "reckless, negligent or wanton" conduct of one of the parties. [30] Where assets are sold or investment decisions made in the period following separation the prudence of those decisions can be examined.

4.14 As well, recent jurisprudence makes it clear that where it is certain that a party is entitled to at least an identifiable percentage of the pool of property he or she is not obliged to wait until the conclusion of the final trial in order to be awarded at least a proportion of her/his entitlement. In *Strahan* [31] the assets were at least $60,000,000 comprising properties and businesses in Australia and overseas. The husband had conceded in his preliminary court documents that the wife was entitled to 30% of the assets. The wife asserted that the husband's assets were worth considerably more; his income from one enterprise alone was about $300,000 per week. By the time of the interim hearing the wife's expenditure on legal fees, valuations and forensic valuations had reached $10,500,000 and she had exhausted the funds available to her.

4.15 The Full Court, on an appeal, awarded the wife $5,000,000 as an "interim property settlement" making it clear that the power to make a property settlement order could be exercised in stages as the case progressed rather than confined to being exercised at the time of final trial.

5.0 Conclusion.

5.1 Sound commercial practice requires effective risk management.

5.2 I am sometimes tempted to inform my clients that the best form of risk management is to put the effort into making the relationship work – from one perspective it is cheaper and 'easier' than the consequences of a separation.

5.3 But if the relationship is at an end – encourage clients to settle early, efficiently and fairly. Little or no advantage is gained from delay or the non-disclosure of documents or information.

---

[30] *Kowaliw and Kowaliw* (1981) FLC 91-092

[31] (2009) 42 Fam LR 203

5.4 Be especially cautious when a client, recently separated, seeks assistance to enter into new commercial or financial relationships.

M.A. Fellows
6/8/13