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Transactions to Defeat Family Law Claims:

The Monster Waiting for Estate Planners

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Transactions to Defeat Family Law Claims – the Monster Waiting for Estate Planners

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Succession and estate planning is an important tool in the armoury available to professional advisors when assisting clients to determine the best way to structure the future of their estates.

Many factors are considered by advisors and their clients, including ultimate objectives of where property is to be held, for whom the benefit is to be available, tax and duty considerations and, of course, issues of control in both the short and long term.

In this paper I will briefly summarise the provision of Section 106B of the *Family Law Act 1975* that deals with transactions to defeat claims and how it might impact on advisors: and ways to avoid this monster.

The law

The starting point must be a review of the law relating to Section 106B.

The section provides as follows:

> *"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 made to defeat any existing or anticipated order in those proceedings or which, irrespective of intention, is likely to defeat any such order."*

The section provides the Family Court with significant power to set aside and stop transactions which defeat court orders or which are likely to have that effect. In the context of bankruptcy, it has a close connections with the voidable transaction powers given to the trustees under the *Bankruptcy Act 1966* (Cth). And remember the Family Court has exclusive jurisdiction to deal with bankruptcy matters involving separated couples.

The elements required to be established before an instrument can be set aside under this section are as follows (see *Gelley & Gelley (No 2) (1992 FLC 92-291 at 79,153*):

1. There are proceedings on foot in which relief under Section 79 is sought (i.e. property settlement proceedings – and also extends to maintenance).

2. There has been a disposition.

3. The disposition was entered into by the parties to that transaction with the intent of defeating an anticipated order in the proceedings.

4. Whether an order was anticipated at the time of the transaction is determined by considering if it was "*anticipated by the reasonable disponer at the time of the disposition, properly considering all of the circumstances of the case*".

5. The effect of the transaction must be to render the party to the transaction incapable of satisfying the order made or anticipated unless the transaction is set aside.

6. The intention must be to defeat an anticipated order. In that regard, anticipation of a claim under the Family Law Act is insufficient (see Nicholson CJ in *Halabi v Artillanga (1994) FLC 92-470 at 880, 884*).

And this leads to questions that frequently arise:

7. What orders are sought or likely to be granted in favour of the spouse seeking to set aside the transaction; and

8. Could those orders have been "*anticipated by the reasonable disponer at the time of the disposition, properly considering all of the circumstances of the case"?*

As explained in a number of authorities, intention of the disponer is central when dealing with the most frequently used part of the section.

Although the authorities refer to a notion of objectivity; it is infused as a mechanism of proving that an order in proceedings under the Family Law Act was *anticipated* at the time of the disposition (*In the marriage of Pflugradt & Pflugradt (1981) FLC 91-052 at 76, 429.)*

So, an order – that the disposition would defeat – must be anticipated by the disponer at the time of the disposition. Whether such an order was anticipated at the time is said to be determined by an "*objective test*" characterised by whether it would be *"expected or foreseen as being likely or reasonably probably"* in all the circumstances of the case.

The alternate prong to this provision is to show that, "*irrespective of intention*" the transaction is "*likely to defeat any such order*".

Accordingly, the power of the Court to set aside an instrument or disposition can only be exercised where the disposition was made to defeat an anticipated order in proceedings under the Family Law Act or is "*likely to defeat any such order*".

It is generally the view that the Section 106B is one of the most powerful weapons available in the Family Court to deal with creditors who may be family members or work colleagues.

Limitations

There are various limitations on the operation of the power under Section 106B such as:

1. An application cannot stand by itself but must be ancillary to proceedings for financial relief on foot in Court or contemplated.

2. It can also include proceedings pursuant to the accrued jurisdiction of the Court that involve, for example, declarations of trusts or determining other claims of dispute or ownership as to property or creditors involving third parties.

3. The relief is purely discretionary.

4. The interests of a *bona fide* purchaser for value are protected.

5. The section only applies to instruments of disposition and so judgments in Courts do not qualify.

Options available to Court

Once the court is satisfied that the section is available for use it can do all or any of the following:

1. Mortgages or other security documents can be set aside and so converting the creditor from secured to an unsecured creditor. This leaves the creditor with rights *in personam* rather than *in rem*.

2. Part X arrangement in bankruptcy may be set aside, as may be the voluntary completion of an application for bankruptcy if there are questionable related transactions that underpin the bankruptcy and associated disposition of property.

3. A further or fresh advance on an existing credit facility may be caught as a disposition under this section (see *Commonwealth Bank of Australia v Stattz & Stattz (1988) FLC 91-942*).

4. A disclaimer by a party to an interest in a deceased's estate will qualify. The application must relate to an instrument or other disposition of a party to the marriage and not relate to an instrument between third parties.

5. While there are no time limits to a transaction, it must be linked to defeating an order and not a claim or anticipated claim.

6. For self-managed superannuation funds, changes to the provisions of trust deeds, binding death nominations, changes to members of superannuation funds, elections for an annuity and not a lump sum, changes to transition to retirement provisions may all be covered.

7. Also note that under Section 106B(2):

    (a) the Court may act independently of the power to set aside transaction that may defeat claims.

    (b) accordingly it can order that any moneys, real property or personal property dealt with by any instrument may be taken in execution or charged with the payment of sums for costs or maintenance as the Court directs.

    (c) it may also order the proceeds of sale be paid into Court to abide its orders.

    (d) the Court can rearrange the priority of debts quite independently of the transaction provisions.

Costs

Costs orders will generally follow the making of an order under this section.

AND a person acting in collusion with a spouse may be ordered to pay the costs of any other party, a bona fide purchaser or other person to include the costs incidental to any such instrument or disposition and the setting aside or restraining of the instrument or disposition.

Examples where claims have been made under this section

The case of S & S & P 2018.

This is a case that came on for hearing before the Family Court in Perth in January 2018.

It involved a claim by the husband against the wife and her mother (the second respondent) that they (the wife and mother) had entered into a transaction to defeat his anticipated entitlements as follows:

1. The wife owned shares in her mother's company given to her when she turned 21 years.

2. The wife transferred the shares back to her mother in April 1996 – about 1 month prior to her marriage.

3. After 17 years of marriage, the parties separate and proceedings are commenced some 4 years later.

4. Even though it was 21 years later, the husband sought to set aside the transaction that saw the wife transfer her shares to her mother on the basis that:

    (a) the shares had substantial value today

    (b) his future mother-in-law did not like him,

    (c) the share transfer was to defeat his anticipated entitlements and claims,

    (d) were steps taken by the mother-in-law to "quarantine" what was properly to be regarded as matrimonial property

    (e) after the Family Court proceedings finished, the shares would be transferred back to the wife – at the time of the Hearing it was understood).

The issue is whether the share transfer effected in 1996 was likely to defeat an anticipated order of the proceedings that commenced in 2017.

The husband relied on the law that an order may be anticipated even though the transaction in question was made some time before the proceedings commenced (*In the marriage of Buckeridge (No 2) 1981 FLC 91-114*).

The husband also relied on *FC & CG 2010 FLC 93-434 at 84 730* that concerned transaction some 10 years or so prior to matrimonial disharmony was set aside.

It failed and the claim against the mother in law was dismissed with the test to be applied in that case as being the objective one outlined by Elliot J *in the marriage of Pflugradt* that:

> "*… it is not a question of whether the husband expected or foresaw a subsequent property application by the wife and 'anticipated' an order being made, but whether considering all of the circumstances at the time of the disposition, such an application by her at some time, with a consequent order, was objectively to be foreseen or to be expected by him as being likely or reasonably probable.*"

Accordingly, the mother in law was released from the proceedings.

The case of G & K & J 2018.

In a different case, the parent's entities (BB Pty Ltd) and the parents personally were joined as third parties to proceedings in which the wife claimed that her husband (the son of the parents).

Part of the relief sought by her was to set aside a series of transactions involving the changing of her husband's interest in his parent's trusts, his employment contract with his parents' company and to obtain access to the assets of one of the parents' trusts.

A short chronology of the relevant events are:

	Parents born – J (1952) and B (1956)
1979	Husband (Parents' son) born
1979	Wife (their daughter-in-law) born
Early 2007	Husband and Wife cohabitation commenced
19 February 2011	Husband and Wife married
	Husband and Wife's have 2 children aged 7 & 5 years
November 2012	Parents win lotto - $27 million
	Parents establish a number of companies, investments and trusts in which their son (husband), his wife, their children, the parents and other family members are named as beneficiaries. The parents and their external accountant and financial advisor are the directors. The husband is included as a director of one company only.
	Husband employed under contract by one of his parents' companies as a project manager.
November 2012	Parents loan $750,000 to Husband and Wife to payout mortgage on their home
February 2013	Parents loan $780,000 to Husband and Wife to buy a new home
August 2014	All parties sign loan agreement acknowledging earlier advances as loans, providing for future loans up to $2m, agree security by way of mortgage with loans repayable on demand plus interest provision.
20 October 2016	Husband and Wife separate

2017	Parents advance loans to trusts controlled by them and in which husband has an interest used to buy real estate (husband lives in this property and pays "rent") and other investments managed by husband– total $1.3 million
19 December 2017	Husband commences property settlement proceedings in the Family Court
April 2018	Wife files response documents in which she seeks property settlement, the advances be deemed a gift not a loan, set aside the August 2014 loan agreement and for access to the other trusts in which Husband had an interest comprising $1.3 million
August 2018	Parents commenced Supreme Court proceedings against both husband and wife to call up the loan now at $500,000 (although $800,000 is also held in trust from the sale of an asset pending the finalisation of wife's claims). Wife sought to transfer proceedings from the Supreme Court to the Family Court and also sought to set aside a variety of transactions under section 106B which she asserted to have occurred to defeat her claim
November 2018	Finalised relief with Wife conceding that she could not succeed to set aside the transactions as they were genuinely entered into and represented valid claims and entitlements
2019	Post finalisation of matters between Husband and Wife, he has been removed as an eligible beneficiary of many of the parents' trusts, dismissed as a director of the companies and remains on an employment contract. He is now in a new relationship with issues of future estate and succession planning currently being reviewed by the parents.

Tips and tricks

Consideration of estate and succession planning and the re-structuring, review and organisation of parties' financial affairs will not ordinarily offend any of the Family Law provisions even if the objective is to make it "*family law bullet proof*" provided it is not done with the intent to defeat an order of a spouse in the Family Court.

The question then arises for the advisors what must they do to ensure that they are not seen to collude with a spouse and so offend the provision? Or offend the provision anyway "*irrespective of intention*"? And also avoid orders for penalties and costs.

Make sure you ask the question about the nature of the relationship of not only the client but also of the eligible beneficiaries/legatees/ultimate owners, especially if restructuring is contemplated.

Issues of "black sheep" in families will not overcome the difficulties that may be faced if any relationship that the black sheep has is fragile and/or separation is contemplated.

Keep good notes to protect both the client and the advisor if the re-structure is for valid reasons unrelated to concerns that may arise because of separation.

If a transaction is set aside, then tax to the ATO that has not been paid may not be recoverable, duty paid to OSR on a transaction may not be refundable, moneys paid to banks or other third party financiers may be irrecoverable and so the advisor may have to compensate the disenfranchised spouse with these costs in conjunction with the deposer if there is collusion. Potentially this could involve significant moneys because in addition to those payments, the legal and Court costs associated with undoing the transaction may also be ordered.

Therefore alarm bells should sound if clients come in to ask for your assistance with a series of transactions and restructuring of estates for specific individuals. You must ask the obvious question about the nature of the relationships as there may be not defence to "*I didn't know*".

My recommendation is that you should get to know and love a family lawyer and not hesitate to engage that person for assistance in reviewing transactions that are contemplated as part of the overall estate planning exercise: to not do so may well see the monster devour you.

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