



Précis Paper

Inheritances & Contributions in Family Law

Family law and protecting inheritance. This is our fourth session with Ian. Again it is important and will be of public interest as well. There is more to come - there is no better commentator on family law.

Discussion Includes

- Family Law approach to the treatment of inheritances
- Prospective inheritances and received inheritances
- Financial and non-financial contributions and the treatment of inheritances
- *Ascot Investments Pty Ltd v Harper* [1981] HCA 1 and third party rights
- *Kennon v Spry* [2008] HCA 56 and discretionary trusts
- Protecting inheritances from the asset pool

Précis Paper

Inheritances & Contributions in Family Law

1. In this edition of BenchTV, the Hon. Ian Coleman SC (Barrister) and Dasith Vithanage (Solicitor) discuss the treatment of inheritances in property settlements under Family Law. Mr Coleman SC is a former Family Court Judge in the Appeal Division who now privately practices from Culwulla Chambers.
2. Issues surrounding a spouse's inheritance (usually from their parent(s)) can be difficult to resolve when the Family Court divides assets in property settlement, especially since the legislative regime is silent on how they are to be approached. Accordingly, this paper will begin with a brief exposition of the general approach the Family Court will take to property settlement proceedings and then will explain where in that process inheritances might fit in.

Property Settlement

3. In light of the High Court's decision in *Stanford v Stanford* (2012) 247 CLR 108, where a court is satisfied that it is "just and equitable" to make an order (per s 79(2) of the *Family Law Act 1975* (Cth)) in relation to the property of the parties, the following steps are taken to determine a property division:
 - i. Clarify the property (both legal and equitable interests), debts and liability of the parties;
 - ii. Assess the degree to which each spouse contributed to the marriage financially and non-financially;
 - iii. Identify any special circumstances including the future needs of the parties, the costs of caring for children etc.; and
 - iv. Divide up the assets in light of the assessment of the contributions and special circumstances.
4. When considering whether a property settlement order should be made, a Court will have regard to the factors listed under ss 79(4) & 75(2) (particularly subsections (b) and (o)) of the *Family Law Act 1975* (Cth):

SECTION 79:

Alteration of property interests

- (4) *In considering what order (if any) should be made under this section in property settlement proceedings, the court shall take into account:*

- (a) *the financial contribution made directly or indirectly by or on behalf of a party to the marriage or a child of the marriage to the acquisition, conservation or improvement of any of the property of the parties to the marriage or either of them, or otherwise in relation to any of that last-mentioned property, whether or not that last-mentioned property has, since the making of the contribution, ceased to be the property of the parties to the marriage or either of them; and*
- (b) *the contribution (other than a financial contribution) made directly or indirectly by or on behalf of a party to the marriage or a child of the marriage to the acquisition, conservation or improvement of any of the property of the parties to the marriage or either of them, or otherwise in relation to any of that last-mentioned property, whether or not that last-mentioned property has, since the making of the contribution, ceased to be the property of the parties to the marriage or either of them; and*
- (c) *the contribution made by a party to the marriage to the welfare of the family constituted by the parties to the marriage and any children of the marriage, including any contribution made in the capacity of homemaker or parent; and*
- (d) *the effect of any proposed order upon the earning capacity of either party to the marriage; and*
- (e) *the matters referred to in subsection 75(2) so far as they are relevant; and*
- (f) *any other order made under this Act affecting a party to the marriage or a child of the marriage; and*
- (g) *any child support under the Child Support (Assessment) Act 1989 that a party to the marriage has provided, is to provide, or might be liable to provide in the future, for a child of the marriage.*

SECTION 75:

Matters to be taken into consideration in relation to spousal maintenance

- (2) *The matters to be so taken into account are:*
 - (b) *the income, property and financial resources of each of the parties and the physical and mental capacity of each of them for appropriate gainful employment; and...*
 - (c) *any fact or circumstance which, in the opinion of the court, the justice of the case requires to be taken into account; and...*

Distinction between Vested Inheritances and Prospective Inheritances

5. Whether an inheritance will fall within the jurisdiction of the Court in dividing the property of the parties to the marriage will largely be determined by whether the inheritance has been received or not, at the time of property settlement. In Family Law, when an inheritance has been received by a spouse it has 'vested in possession' and the spouse's entitlement to the

property is absolute. On the other hand, when a spouse is expecting an inheritance but it has not yet been received (because the testator is alive), it is termed a 'prospective inheritance'.

6. As a general rule, only where the inheritance has vested will it be treated as a contribution by the spouse who received it and become part of the property pool of the parties to the marriage to be divided on settlement.
7. The distinction is linked to the definition of property under s 4 of the *Family Law Act 1975* (Cth):

SECTION 4:

Interpretation

"property" means:

- (a) *in relation to the parties to a marriage or either of them--means property to which those parties are, or that party is, as the case may be, entitled, whether in possession or reversion; or*
- (b) *in relation to the parties to a de facto relationship or either of them--means property to which those parties are, or that party is, as the case may be, entitled, whether in possession or reversion.*

Essentially, all interests in real or personal property are property for the purposes of the Act. The relevance of this definition is that only 'property' as defined will form part of the pool to be divided on settlement and usually prospective inheritances will not be considered 'property' because of the principle of freedom of testation – more on this below.

Inheritances Vested in Possession

8. As explained above, once an inheritance vests, it is 'property' and comes within the jurisdictional reach of the court as a matrimonial cause if there are proceedings with respect to that property.
9. The basic principles for dealing with such inheritances are derived from *Kessey and Kessey* (1994) FLC 92-495, which provides that inheritances vested in possession are to be treated as contribution made by the spouse who received it.
10. There have been some inroads into this basic statement of the treatment of inheritances which have vested, particularly where the non-receiving spouse has made direct or indirect contributions to the inheritance received by the other spouse. Mr Coleman SC explains that this may arise where the parents of one of the spouses retire to a property and their child

and the child's spouse maintain the property, clean, do the washing, shopping etc. Effectively the non-receiving spouse has made a tangible contribution to the welfare of the testator and a Court may take this into account when dividing the property pool under s 75(2)(o) as a requirement of justice.

11. In *De Angelis* (2003) FLC 93-133, the contributions made by the husband to the wife's mother's property were considered by the Court in its treatment of the wife's inheritance of the property. Lindenmayer and Finn JJ, quoting the trial judge, stated that:

[t]he husband has contributed to a very substantial extent to the expectation of the inheritance of the wife's mother's home, both as to its value by his labours and contribution to the cost of renovations and maintenance and because of his contribution to which allowed the wife to care for her mother ... these contributions ought to be taken into account in adjusting the parties' division of property.

Prospective Inheritances

12. Prospective inheritances are not generally considered property under the Act because freedom of testation is considered to be an important part of the law of Australia. The effect of the principle is that there can be no assumption or presumption, either that by testamentary instrument or by intestate succession, that a party will either become entitled to an inheritance or, if and when that happens, that the inheritance will be of any value: *Commissioner of Stamp Duties v Livingston* [1965] AC 694. This is because testators may change their mind as regards to how much of their property will go to any particular person and whether it will go to any particular person at all (so long as they retain legal capacity to vary their testamentary instrument). Accordingly, prior to receiving an inheritance, prospective beneficiaries cannot be said to have any interest in property as defined under the Act.
13. However, the courts have occasionally diverged from this general approach in exceptional cases where:
 - the size of the inheritance is substantial relative to the existing property pool;
 - the likelihood of the inheritance being received is high; and
 - the time at which the inheritance is likely to be received is in the very near future.
14. In such cases, the courts may take the inheritance into account under s 75(2)(o) as a circumstance which justice requires to be considered.
15. In *De Angelis*, the matrimonial property was valued at roughly \$560,000, however, the wife in the matter was expected to receive, by way of inheritances from her mother and her aunt,

two properties with a total value of \$500,000. The wife's aunt was 90 years old and had suffered from dementia and therefore lacked the capacity to alter or revoke her existing will. The aunt had made a will, with the wife being a beneficiary under the will. Given the size of the prospective inheritance was high and the likely inheritance of the wife from her aunt, Lindenmayer and Finn JJ adjusted the overall property pool in favour of the husband, noting that it would be unjust to ignore the inheritance.

16. Another example of sufficient certainty of inheritance to justify a Court to alter interests in the property may arise where mutual wills between the parents of a spouse are bound between the wills to leave the estate to a spouse: see *White v Tulloch-White* (1995) FLC 92-640; *Milankov v Milankov* [2002] FamCA 195.
17. The timing of the inheritance may be relevant when, for example, the testator who has made provisions for one of the parties is faced with imminent death or is in a state of rapidly deteriorating health. In these circumstances, the Court may adjourn the matter (pursuant to s 79(5)(a)) until the testator has died and the actual inheritance can be identified: see *Grace* (1997) 22 Fam LR 442.

Examples

18. The following scenarios may help further clarify the approach taken by the Family Court to inheritances:

- a. Where a spouse is the primary carer of their spouse's parent, can an expected inheritance be taken into account given their non-financial contributions?

As a general rule, the difficulty again with prospective inheritances is the threshold question of whether that interest represents 'property' for the purposes of the Act. It is only in the exceptional case where there is a high probability the spouse will inherit and where the inheritance is a substantial estate that a Court might be influenced to take it into account e.g. where a spouse is an only child who is not estranged from their parents. Cases such as *Heath & Heath; Westpac Banking Corporation, Intervenor* [1983] FLC 91-362 indicate that 1 of 2 approaches are conceivable. Firstly, a Court may decide to alter interests in the existing property of the parties in favour of the non-receiving spouse pursuant to s 75(2)(o). Otherwise, where the inheritance is very substantial, the assets of the marriage are modest and the evidence indicates it will vest in the foreseeable future (e.g. a benefactor aged in their 90's with no other children), a Court may adjourn proceedings under s 79(5) until the death of the testator. This was the approach in *Grace*, where proceedings were adjourned for ultimately a decade because one spouse was a beneficiary to

a discretionary trust holding \$100M and the parties to the marriage had virtually no existing assets.

- b. Can a spouse's non-financial contributions to a testator's property be taken into account in their settlement with the receiving spouse?

This situation is very similar to the first scenario except that in situations such as this the non-receiving party will often seek relief via a series of alternate equitable claims. Often a constructive trust based on an estoppel such as that found in *Sidhu v Van Dyke* (2014) 251 CLR 505 are an effective way of crystallizing a claim. Such a claim may arise where the non-receiving party makes an assumption that they will receive an interest in property as a result of a representation, the assumption is held over a long period of time and no action is taken by the representor to rebut the representation or assumption. The claim is often considered a compromise because the non-receiving party will often receive less than if the inheritance vested and was the property of the other party.

- c. Can the Family Court compel testators or trustees to transfer inheritances in order to prevent the need for adjourned property settlement proceedings?

Ascot Investments Pty Limited v Harper [1981] HCA 1 provides that, absent a sham or alter ego scenario, third parties cannot be obliged by orders of the Family Court to do things they would otherwise not be compelled to do under the general law. In *Ascot Investments*, Family Court orders that the shareholders of a company accept a share transfer in favour of one of the parties to a marriage which the shareholders and directors of the company did not wish to accept were not upheld by the High Court. In addition, sham transactions may be set aside pursuant to s 106B or in the application of equitable principles. Further, where an alter ego (the classic example of which involves someone who is not the trustee of a discretionary trust and who may or may not be a beneficiary is seen to be the only person who receives anything out of the trust) is identified by a court, interests in the property pool will be adjusted proportionally against the party using the alter ego.

- d. Is there property for the purposes of the Act if between the parties to a marriage they control a discretionary trust which is vested with an inheritance and one of the spouses is a beneficiary?

The Court in *Kennon v Spry* (2008) 238 CLR 366 determined that where, between the parties, there is the legal capacity to control the distributions and also the capacity to receive the distributions, then the trust property is 'property' under the

Act. The Court then ordered the husband (who controlled the trust) to transfer monies to the wife (a beneficiary), in effect creating 'property'.

- e. Can a spouse remove assets into a family company to frustrate a maintenance order levied against them if they do not have de jure control over the company?

No. Section 106B creates the power to set aside such a disposition which is made with the intention of defeating a Court order or where objective, circumstantial evidence suggests that the disposition is likely to defeat a claim (such as the timing of a disposition made when it was evident that the marriage was going to breakdown):

SECTION 106B:

Transactions to defeat claims

(1) 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 an existing or anticipated order in those proceedings or which, irrespective of intention, is likely to defeat any such order.

Furthermore, as was relevant in cases such as *Harris v Harris* [2010] FamCAFC 221, Mr Coleman SC suggests that provisions of the *Corporations Act 2001* (Cth) may be useful in piercing the corporate veil, particularly the phoenixing provisions.

Implications

- 19. Protecting inheritances from the asset pool is a fast developing area of Family Law. This is particularly the case with respect to prospective inheritances because as the Court explained in *Tulloch*: there is no absolute rule in dealing with prospective inheritances, and it will largely depend on the circumstances of each individual case whether inheritances will factor into a property settlement.
- 20. At the moment, testamentary trusts are probably the simplest and most effective means of quarantining inheritances. For example, trusts where the trustees are siblings (provided that there is no reason to think that the siblings will ever fall out) and where the beneficiaries are the siblings and their children, are common. Such a trust would fall outside the ambit of *Kennon* where the siblings must act jointly to distribute the trust funds, as it cannot be said that either controls the trust. Although such trusts can be effective, Mr Coleman SC notes that clients should be advised to attain expert accounting and revenue advice given trusts inevitably involve the transferal of assets and there are stamp duty and CGT implications.

21. Another option for parents to try and prevent their hard-earned wealth from ending up where they do not want it may be via the superannuation system, although that is a whole topic for another presentation!!

BIOGRAPHY

The Hon. Ian Coleman SC

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The Honourable Ian Coleman was admitted as a lawyer in 1974, called to the NSW Bar in 1975 and appointed as a Senior Counsel in 2013. He was appointed to the trial division of the Family Court of Australia in 1991, Judge advocate of the Australian Defence Force in 1992, Commissioner of the Australian Law Reform Commission in 1993, appointed to the Appeal Division of the Family Court in 1999 and was a Judge in the Family Court of Australia in 2009-2013. He is currently an Adjunct Professor at the Western Sydney University, School of Law.

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Sidhu v Van Dyke (2014) 251 CLR 505

Stanford v Stanford (2012) 247 CLR 108

White v Tulloch-White (1995) FLC 92-640

Legislation

Family Law Act 1975 (Cth)

Succession Act 2006 (NSW)