ENLARGING THE ASSET POOL – ADDING BACK NOTIONAL ASSETS[1]

The Honourable Justice Judy Ryan

Introduction

It is well known that the preferred approach to the determination of proceedings for the adjustment of matrimonial property involves a four step process, the first of which requires that the court identifies and evaluates the matrimonial assets. ***Ferraro and Ferraro (1993) FLC 92-335.*** The question of "what is property" is central to the courts exercise of jurisdiction under section 79. By section 4 of the *Family Law Act* property is given a wide definition and is described as *"property, in relation to the parties to a marriage or either of them, means property which those parties are, or that party is, as the case may be, entitled, whether in possession or reversion."* In early cases such as ***In the marriage of Slattery (1976) 1 FLR 11,395*** property was ascribed a narrow meaning and attempts were made to limit its application to corporeal property. This trend ended with the Full Court's decision in ***Duff (1977) FLC 90-917***. In *Duff* property is described as being a term which is *"indicative and descriptive of every possible interest which the party can have."* The words *"in possession or reversion"* are words of extension not limitation. *Duff* is consistent with the High Court's pre *Family Law Act* approach in ***Saunders and Saunders (1967) 116 CLR 366*** which underpins subsequent jurisprudence on this topic. Generally, the court identifies the matrimonial property as at the date of hearing and orders adjustments determined by the outcome of the findings made pursuant to sections 79(4), 75(2) and 79(2).

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1 A paper given to the Hunter Valley Family Law Practitioners Conference 22-23 September 2006 . I am grateful to my Deputy Associate Dian Neligan and her predecessor Paloma Sessions for their research on this topic.

By the early 1980's we see the Family Court grappling with the problem of depletion of the asset pool by a spouse's unilateral disposition of matrimonial property prior to trial. That is property which clearly fell within the courts property jurisdiction and which, but for its disposition, would have been included in the asset pool for distribution. Case law, which would not have been possible if the narrow definition of property remained in vogue, developed a line of authority enabling courts to include notional property, even where that property no longer existed at trial. These cases generally commence with Baker J's description of "wastage" described in ***Kowaliw (1981) FLC 91-092.*** Closely aligned and no less difficult are those cases concerned with the alleged disposition of property but where there exists good reason to believe it is secreted and not lost. Starting with *Kowaliw* a line of authority developed which enables a court to take these losses into account. Building on *Kowaliw*, more recently the cases have gone further than merely taking the losses into account, by notionally adding back the value of the losses or assets to the pool of property. It is this category of case that this paper addresses.

Kowaliw sets the scene for dealing with assets disposed of prior to hearing

In *Kowaliw* the husband allowed prospective purchasers of the matrimonial home to occupy the home rent free for 12 months. This, the wife submitted, amounted to twelve months lost income which she claimed should be taken into account. Baker J took the position that for most couples, marriage is an economic partnership. As a statement of general principle Baker J found that financial loss incurred by the parties in the course of the marriage, whether or not a joint liability, should be shared between them except in the following circumstances:

- *"where one of the parties embarked upon a course of conduct designed to reduce or minimise the effective value or worth of matrimonial assets, or*

- *where one of the parties has acted recklessly, negligently or wantonly with matrimonial assets, the overall effect of which has reduced or minimised their value".*[2]

If the losses had been suffered by the parties in the course of the pursuit of the objectives of the marriage, for example gaining income and/or assets, then such losses should be shared by the parties, although not necessarily equally. Relevantly Baker J held this issue should be considered under s 75(2)(o).

In ***Townsend v Townsend (1995) FLC 92-569*** the Full Court took a more robust approach than previously seen and determined that the wasted property should be notionally added back to the pool of assets. Simply put, after separation the husband sold the parties most valuable asset, a taxi which sold for $148,000.00. The husband had had the sole benefit of the money from the taxi and none of the sale proceeds remained. The court found that selling the taxi was a premature distribution of marital property and thus it would be unjust in the extreme to merely treat such conduct by the husband as a matter under s 75(2). The taxi, if it was retained, would have been brought into account as any other item of marital property. The Full Court determined the taxi should be brought, *"into the pool of assets on a notional basis and make a distribution accordingly."*[3] Anthony Dickey QC raises some of the problems of the notional add back approach in *Townsend* in his article, *"A new concept in property proceedings: notional property"*[4]. Dickey points out that in notionally adding back the money, their Honours infer that the money should be accounted for not in a general way [the *Kowaliw* approach] but on a dollar for dollar basis. What particularly concerns Dickey is that their Honours offered no guidance as to when this approach should be taken. Dickey points out that the concept of notionally adding back assets is not novel, citing as an example the *Family Provision Act 1982 (NSW)*. However the *Family Provision Act 1982 (NSW)* contains provisions as to when money should be notionally added back, whereas the *Family Law Act 1975* specifies no such provisions. Hence the necessity for appellate direction. Dickey

2 at 76,644

3 at 510

suggests that the notional add back approach should be used when formerly owned property has been unreasonably disposed of after separation, but acknowledges that there is no authority confirming this reasoning. His approach does not accord with subsequent developments.

Kowaliw has received widespread appellate support. In ***Brown v Green (1999) FLC 92-873*** the Full Court considered whether the quarantining of losses from the parties' failed business as a loss absorbed by the husband was manifestly unjust. The trial judge determined that the husband should bear full responsibility for the losses incurred by the business because the husband alone initiated the venture and had control over it. There was no suggestion of recklessness on his part nor a course of conduct designed to reduce the asset pool. Essentially this case involved a promising business venture which went sour. The Full Court considered whether *Kowaliw* espoused a rule of general application or is merely a guideline. The Full Court agreed with the trial judge that the principle in *Kowaliw* does not form a fixed code, but should be used as a guideline. The Full Court cited with approval comments made by Nicholson CJ and Fogarty J in *Townsend* that *Kowaliw* should not be used to define the parameters of considerations to be applied in all cases involving waste. On the back of ***Norbis v Norbis (1986) 161 CLR 134***, the appellate court found that the trial judge had not explained to their satisfaction why she considered that the circumstances of this case warranted departure from the *Kowaliw* principle. In placing the full burden of the loss on the husband, the trial judge had made orders which were manifestly unjust.

In ***Bell and Bell [2000] FamCA 1301*** the Full Court makes it clear that notional adjustments are not limited to wasted assets but may also include *"identified items of property that have been bona fide disposed of"*. Also that *"It may also be appropriate, depending on the circumstances, to notionally include in the pool of assets items of property in respect of which no or no reasonable explanation has been given for the assertion that they no longer exist or never existed: Mezzacappa and Mezzacappa*

4 (1996) 70 ALJ 805

(supra). In other words, it is also possible, in appropriate cases, to have regard to, and notionally include in the list of assets, what is called unascertained property the value of which is capable of some identification and quantification. In this case, the trial Judge notionally included in the pool of assets items that were capable of identification and quantification. However, he also found that there were other assets the identity of which was not known but for which an adjustment should be made in favour of the wife. There is no doubt that such a finding is open to a trial Judge."

The Full Court has been reluctant to notionally add back assets where monies that existed at separation have been spent on reasonably incurred living expenses. Parties are entitled to continue to provide for their own support. In ***WBM v RCM [1998] FamCA 42***, the Full Court held: "*It is well settled that save in exceptional circumstances a trial Judge should deal with the property as at the date of the hearing and make adjustments taking into account the various matters set out under s.79. (Wells v Wells (1977) FLC 90-285; Wardman v Hudson (1978) FLC 90-466; In the Marriage of Geyl 7 Fam LR 219). However, the particular justice of the case may make it appropriate to notionally add back assets which have been demonstrated to have been dissipated either during the marriage or post-separation. Normally it is necessary to demonstrate an appropriate basis for doing so, for example by wastage such as gambling or extravagant living. (Kowaliw v Kowaliw (1981) FLC 91-092; Fane-Thompson v Fane-Thompson (1981) FLC 91-053; Winnel v Winnel (1984) FLC 91-580; Townsend v Townsend (1995) FLC 92-569; Doherty v Doherty (1996) FLC 92-652."*

In ***GVC v HPC [1998] FamCA 143*** the Full Court held where the monies have been shown to have been reasonably disposed of, the notional add back approach should be the exception and not the rule.

More recently the Full Court has considered add backs in three decisions. The first, ***Chorn and Hopkins (2004) FLC 93-204, NHC v RCH (2004) 32 Fam LR 518*** is a case

concerning notionally adding back paid legal fees into the asset pool**.** In an exhaustive review of key authorities the Full Court first summarises ***Farnell and Farnell (1996) FLC 92-619***. In *Farnell* the trial judge correctly included as a notional asset money withdrawn from the joint account and applied towards legal fees. In ***Line v Line (1997) FLC 92-729*** the Full Court held it is appropriate to add-back funds spent on legal fees as a notional asset in instances where joint funds are used. ***C v C (1998) 23 Fam LR 491*** emphasises the discretionary nature of the treatment of legal fees in property proceedings. In ***DJM v JLM (1998) FLC 92-816*** the legal fees in question had been paid from funds which the court had ordered the husband release to the wife. It was held to be appropriate that the paid fees should be added back. ***Finlayson [2002] FamCA 898*** confirmed that it is appropriate to notionally add back paid legal costs, where it is found that this amounted to a premature distribution of matrimonial assets. It also confirmed that, where funds are borrowed to pay legal fees, and the liability is still outstanding, neither the payment of fees nor the liability should be taken into account.

Writing *ex judicially* Justice Boland[5] said *"The principles which emerge from the Full Courts* [in Chorn and Hopkins] *review of previous decisions can be summarised as follows:*

- *Monies reasonably disposed by a party in the conduct of their post-separation lives should not usually be added back.*
- *The treatment of funds used to pay legal costs remains ultimately a matter for the discretion of the trial judge.*
- *In determining how to exercise that discretion, regard should be had to the source of funds.*
- *If the funds used existed at separation and are such that both parties can be seen as having an interest in them (on account of contributions) then such funds should be added back as a notional asset of the party, who has had the benefit of them.*

5 9th Australian Family Lawyers' Conference, Sabah 11-13 June 2005 *"Trends in the Full Court: Recent cases"*

- *If the funds used to pay legal fees have been generated by a party post-separation from his or her own endeavours or received in his or her own right (for example, by way of gift or inheritance), they would generally not be notionally added back as a notional asset; nor would any borrowing undertaken by a party post-separation for payment of fees be taken into account as a liability in the calculation of the net property of the parties.*
- *Funds generated from assets or businesses to which the other party had made a significant contribution or has an actual legal entitlement may need to be looked at differently from other post-separation income or acquisitions.*
- *Outstanding legal fees themselves are generally not taken into account as a liability.*
- *If in the exercise of discretion it is determined that legal fees already paid should be taken into account as notional asset, then normally any liability associated with the acquisition of the monies used to pay the legal fees should also be taken into account."*

The key factors which appear to have general application are the emphasis on the source of the funds. That is were the funds received through one parties efforts alone or in his or her own right, whether the funds disposed of came from assets in which both parties had an interest and whether the funds were acquired pre or post separation. This case is not concerned with the issue of notionally adding back assets or income lost unreasonably or wasted. The Full Courts decision in *Chorn and Hopkins* has been subject to critical comment. In the unreported judgment of ***K v K***[6] (delivered 30 August 2005), Justice O'Ryan discusses the approach taken by the Full Court in *Chorn v Hopkins*. In his judgment he rejected a submission, explicitly reliant on *Chorn v Hopkins* that costs paid by a party from post separation income ought not to be notionally added back into the asset pool. In deciding against the contention Justice O'Ryan referred to the well known principle that the identification and evaluation of available assets at stage one of s 79

6 SY3773 of 2004

proceedings does not differentiate between pre and post-separation assets. ***Carter and Carter (1981) FLC 91-061.*** His Honour observed that in ***Farmer and Bramley (2000) FLC 93-060*** Justice Finn stated at 87,948 *"57. Secondly, if it was to be determined that a majority of the community considered that one spouse should, as a general rule, have no entitlement to share in property either by good fortune or good management acquired after separation by the other spouse, then the Act would need to be amended to make this clear. As the Act currently stands, the jurisdiction conferred by s 79(1) to alter the interests of spouses in property extends without limitation to all the property which either spouse is entitled "whether in possession or reversion" (s 4)."* Essentially his Honour's view is that although the dichotomy of pre or post separation asset and income acquisition may be relevant during the second or third stage of the preferred approach, the question of the source of funds [including payment of legal fees] should not be confused with a court's obligation to identify the asset pool at step one.

In a paper *"Property by any other name – the treatment of paid and unpaid legal fees in family law"* [7] – Paul Doolan submits that Justice O'Ryan's approach is correct. Concerning *Chorn and Hopkins* Doolan says *"…while endeavouring to provide a comprehensive survey of the case law and guidance for trial judges on the treatment of paid and unpaid legal costs, the Full Court's decision appears to create uncertainty in one potentially crucial aspect where none existed. It is submitted that Chorn v Hopkins opens the door to a treatment of income and assets generated by post-separation endeavours, that sits uneasily with the general principle that the court should divide property based upon the available net asset pool at date of trial versus that at date of separation."* Doolan submits that *Chorn and Hopkins* does not account, for example, for funds drawn from an exceptionally high salary which one party has built up over the course of the marriage, often aided by contributions from the other spouse. He argues this may lead to an injustice to one of the parties, in that the spouse earning the high salary may use this to pay legal fees without risking these fees being notionally added into the

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pool. Justice O'Ryan describes other situations which he believes will cause an injustice including that if saved funds earned post separation would be included as property.

For so long as *Chorn and Hopkins* remains binding authority, Doolan suggests practitioners should ensure:

- *parties should maintain accurate records of the source utilised for the payment of legal fees. The court cannot speculate on such matters and can only make findings based on evidence. Evidence will need to be adduced, by annexure to affidavit or tender of documents as exhibits, proving the source of funds for paid legal costs.*
- *as far as possible, legal fees should be paid from post separation income. If fees are paid in this manner, then on the ration of Chorn v Hopkins, the submission can legitimately be made that monies so paid should not be added back into the pool of property. That submission may not be available where that income is derived from a business or asset built up during the marriage.*
- *lawyers should insist on strict compliance with r 19.04(5)* [this rule does not operate in the Federal Magistrates Court] *that requires disclosure of the source of funds in a notification of costs.*
- *subpoenas and/or a notice to produce should be issued, seeking corroborating documents on the question of source of funds.*

It will be interesting to see if this issue is reconsidered by the Full Court. Until it is, *Chorn and Hopkins* is authorative.

Omacini and Omacini (2005) FLC 93-218 deals with a series of transactions which the husband argued were erroneously notionally included in the asset pool. The appeal judgment demonstrates the risks of double counting when notionally including assets. The parties were married for about twenty five years, finally separating during 2000. At the date of the trial, the husband was 51 years old, and unemployed. The wife was 48,

and the proprietor of a real estate business. In April 1994 the wife purchased a rundown real estate business with another partner, whom she bought out later that year. At some stage the husband became a director in this business. In July 2001, without the husband's consent the wife withdrew from the real estate business and formed a company with a new business partner. Together the wife and her partner purchased two adjacent shops from where her real estate business operated. At hearing it was the wife's position that the value of her business should be included at $114,077, its value at separation. The parties full financial position is not set out in detail in the appeal judgment. It is noted however that, having started married life with no assets, the parties acquired nett assets in excess of $3 million. At trial, the wife sought to have $502,012 added back as monies lost by the husband, or as monies he had received that should be brought into the asset pool. These included the husband's withdrawals from two joint accounts [$226,089], the sale of shares [$31,904] and share dividends received [$1,800]. There were also share investments [$15,000] and bonds [$4,306], the proceeds of a property and an investment [$165,935] and the depreciation of a truck [$8,000]. The final portion was made up from a payment the wife made to reduce a joint debt apparently incurred by the husband [$30,779]. The wife also claimed the loss of rent at another of the parties properties which, because of improvements the husband made to the property, the trial judge did not include.

It was the wife's position that, since the parties final separation, the husband had invested foolishly for which he alone should bear responsibility. She was also concerned that since separation the husband had elected not to take paid work. Essentially it was the wife's position that, as all of her income had been taken into account, so should that of the husband. In relation to share investments, on which he made a loss, the husband asserted that these reflected the risks inherent in trading and were neither wasteful nor reckless. The trial judge concluded that the husband should bear responsibility for these losses, as they mostly occurred after separation, and contrary to the wife's wishes. The trial judge added back the money the husband 'wasted' on the sale of a BMW which he sold at a loss. As for money received from BHP shares and the sale proceeds of one of the properties, these were considered to be joint assets. As joint assets currently held by one

party, they were to be added back into the asset pool *"in the usual way."* Concerning an investment unit the trial judge found that it was acquired after separation, with the husband making the major contribution. As the increase in the value of the wife's business post-separation was not brought into account, the trial judge decided against including the profit on the husband's investment unit in the asset pool. Depreciation of the husband's truck was also disregarded. The husband's share losses were brought into account in defining the pool. However, the money the wife paid toward the joint debt incurred by the husband was not added back. It was agreed that the legal fees paid by both parties as well as the valuation fees paid by the wife should be added back.

The Full Court detailed three categories of cases which have emerged, where it is appropriate to notionally add back to the pool of assets. Relevantly the Full Court does not suggest that the category of cases is closed. The three categories identified are:

- *Where the parties have expended money on legal fees [DJM and JLM (1998) FLC 92-816];*
- *Where there has been a premature distribution of matrimonial assets [Townsend and Townsend (1995) FLC 92-569]; and*
- *Where one of the parties has embarked upon a course of conduct designed to reduce the worth of the matrimonial assets, or where one of the parties acted "recklessly, negligently or wantonly" in a way that the value of the matrimonial assets are reduced [As outlined by Baker J in Kowaliw and Kowaliw (1981) FLC 91-092 at 76,644].*

Applying these principles to the trial judge's decision, the Full Court considered there were a number of errors. Their Honour's were critical of the trial judges approach to the adding back of the shares and the property proceeds as though they *"should be included in the usual way, as being joint assets of the parties now realised, but held by one party"*. The Full Court was concerned the trial judge had not closely examined the reasonableness of the husband's post separation expenditure. Whilst the trial judge

recognised the husband had received a redundancy package she overlooked the fact that presently the redundancy was frozen. Because of the husband's inability to access these funds it was reasonable that he use other assets in order to meet his expenses. The husband deposited the proceeds of the sale of a property into his bank account, from which he purchased a car and caravan, as well as paid his legal fees. The expenditure from the bank account, as well as the car, caravan and legal fees were all listed in the pool of assets, essentially leading to these being accounted for twice. A similar error occurred with the sale of BHP shares, which were deposited into an account and also used to pay legal fees. The Full Court held that the trial judge erred in failing to quantify the asset pool as at the date of trial, and did not adequately quantify the parties contributions to the pool. Instead she relied upon *"a complex mixture of add backs, the exclusion of some assets and the inclusion of others and notional valuations"*. Essentially the approach adopted was fraught with difficulties and as a result a retrial was ordered.

During the course of the proceedings in ***SMB and MFB [2006] FamCA 46*** the wife made a number of successful applications for costs and interim spousal maintenance. In total she received approximately $102,000 on the basis that, at trial, the court would categorise the precise nature of these payments. At trial the entire amount was added back as property, as opposed to maintenance, and the parties paid legal fees were excluded from the asset pool. The primary issue at first instance was the value of the asset pool. Both parties argued that the other had exclusively used capital immediately prior to, or upon separation, and that consequently there should be substantial add-backs. The husband contended that $233,000 should be added back against the wife, being for a number of purchases, bank account withdrawals and funds removed from the husband's credit card. This included the ordered $102,000 as well as additional spousal maintenance. The husband conceded the wife should have $60,000 as a notional allowance for spousal maintenance, an amount already deducted from the sum sought to be notionally added back. For her part, the wife sought that $363,775 be added back against the husband, being for dividends removed from family companies; proceeds of the sale of an apartment; paid legal fees and additional funds removed from companies.

At first instance the wife's arguments met with little success. In relation to the family companies, the corporate structure was treated as the husbands business, and as a result, in drawing against this the trial judge determined the husband was drawing against post-separation income, for which he was not obliged to account. The trial judge determined that, as part of the husband's drawings were used to pay the wife, adding these amounts back was effectively adding back the husband's post-separation income. The husband used other company drawings to purchase a home unit in which he resided. Because the wife remained in the matrimonial home it was held this could not be impugned as unreasonable. Concerning the add backs sought against the wife, the trial judge considered that it was not unreasonable for the wife to look to the husband to provide financial support for her and the children, at least pending final determination of the property proceedings. Subsequently, any drawings of or payments to the wife needed to be set-off against the wife and children's reasonable needs post-separation, measured against the husbands ability to meet those needs. Because the wife had access to assets by way of credit, drawings against superannuation, proceeds of the sale of shares and the surgery, as well as maintenance, and also having the use and benefit of the matrimonial home for which the husband had paid the mortgage repayments, the trial judge categorised the $102,000 as property which he added back into the asset pool.

The wife submitted that the parties paid legal fees should be brought into account and debited against each parties entitlement. Concerning the husband's legal fees, the trial judge held that as his payments were sourced from his post separation income it was inappropriate to add these back in. In order to pay her legal fees the wife raised a $40,000 loan which was secured against the matrimonial home. His Honour took into the account the total amount the wife had available to her post-separation and that a substantial part of that sum had been applied to legal costs. He determined that to bring her legal fees into account as add backs debited to the wife amounted to double-dipping.

On appeal the Full Court examined the process by which the trial judge came to the conclusion that the $102,000 was property, and found him to be in error. Their Honours

held the trial judge failed to give sufficient weight to the wife's evidence concerning her expenses, and the need to support herself and the parties two children, including their school fees. In concluding that the wife had access to $45,000 per year, which the trial judge determined was an ample amount for her support, he fell into error. Even if the trial judge was correct in categorising the $102,000 as property on the basis that it drawn from capital rather than from the husband's income, it is not axiomatic that as property this amount would automatically be added-back. Central to the Full Court's decision is their concern that the trial judge did not closely examine the wife's income or her expenditure. Relevantly, the appeals court was satisfied there was no evidence that the wife misapplied her funds. The Full Court cited with approval the principles discussed in both *Chorn and Hopkins* and *WBM v RCM [1998] FamCA 42*, and concluded that it is generally appropriate to notionally add back monies to the asset pool where assets have been dissipated either during the marriage or post separation when this involved wastage or extravagant living. Adding back assets required by the parties to meet their reasonable day to day living expenses is generally inappropriate. Their Honours cited with approval the Full Court's decision in *GVC v HPC [1998] FamCA 143*, quoted below. The Full Court decided against notionally adding the $102,000 back into the asset pool. In relation to legal costs, as the amount paid by the wife came out of money she received from the husband, the Full Court considered this amount should be added back, as should the husband's legal fees. One of the reasons for adding back the husbands paid legal fees stems from the trial judge treating the tax liability on dividends and directors fees allocated to the husband as a joint matrimonial liability.

In spousal maintenance and child support cases one sees different outcomes to the "what is reasonable" question. Context is important, and depending upon a families overall circumstances, expenditure may be classified as reasonable in one set of circumstances yet unreasonable in another. ***Vautin v Vautin (1998) FLC 92-827, Rosatti v Rosatti (1998) FLC 92-804.*** In the arena of notional add backs, one must anticipate differing outcomes to consideration of reasonable living expenses depending on the parties particular circumstances.

If the notional add back argument fails all is not lost

In contrast to the notional add back approach in *Townsend* there are numerous decisions where wasted assets and any consequences are considered under s 75(2)(o). In ***Antmann (1980) FLC 90-908*** the husband had, during separation, closed the doors of the family business resulting in the loss of business income and the ruining of stock. In relation to the business their Honours found that up to the date of closure the business was trading satisfactorily and it was as a result of the husband's actions that debts were incurred and the stock deteriorated. Counsel for the wife argued that the wife should be compensated for what was called his, "negative contribution". Their Honours found that there could be no such concept under s 79(4)(a) and (b). Their Honours noted that if the wife had stepped up and began to run the business herself, that would be relevant as evidence of an increased burden on her, but that there was no room for a negative contribution when a party's passive act causes loss. The wastage of matrimonial assets should be considered as a factor under s 75(2)(o), in cases where there is evidence that the wife has lost as a result of the husband's actions.

In *Kowaliw* Baker J considered the decision in *Antmann*. Baker J went on to say that if *Antmann* is to be taken literally and the court is precluded from considering negative contributions under s 79(4), then evidence of wantonness and recklessness may be taken into account under s 75(2)(o). The notion of negative contribution was finally put to rest in ***Kennon (1997) FLC 92-757*** a well known case concerning domestic violence.

In ***De Angelis v De Angelis (2003) FLC 93-133*** the Full Court considered the treatment of gambling losses where gambling is identified as a "condition" and also whether losses should be dealt with as any other form of entertainment, for example the husband's golf. The trial judge found that the wife had gambled away $90,000 in marital property to which each party had contributed, and dealt with this loss under s 75(2). At trial and on appeal the wife claimed that her gambling losses were not "negligent, reckless or

wanton" as required by *Kowaliw* to constitute waste, but rather due to her condition caused by her husband's treatment of her. The Full Court agreed with the trial judge's decision in not excusing the wife's gambling losses because of her apparent condition. The Full Court found that while for some people gambling is a form of entertainment and should attract no more comment than say, golf, the family's circumstances are relevant. In the circumstance of this case, specifically given the limited assets of the parties, the wife's losses were reckless, and a relevant s 75(2)(o) consideration which counted in the husband's favour as waste occasioned by the wife. The Full Court ordered the wife to pay the husband an amount constituting half of money which was the parties' joint money that she has gambled away. This amounted to fifty per cent of $84,220 or $42,110.

A case which draws the issues of waste and notional add backs together is ***G and G [2001] FamCA 1138.*** In this case, after separation the husband invested $1.8 million in wine, which investment at trial had a value of $1,220,739. The effect of the investment was to reduce the asset pool by $579,261. Counsel for the wife argued that at least the difference between the two amounts ought to have been added back to the asset pool under the *Townsend* principle. The Full Court noted particular features of the transaction as follows: The investment was made after separation, after the parties had each sought advice on property settlement and on the advice of a financial adviser. The husband was aware that in the short term there would be a significant decrease in the value of the investment and was investing for the long term. His expectation and that of his advisor was that the short-term losses would be significantly outweighed by longer term gains. The trial judge concluded that the investment was appropriate, that is not reckless or irresponsible and not tantamount to waste. Thereafter no further adjustment was made as a consequence of the loss. The Full Court determined this case was not about waste, essentially because the money was not lost and would be returned with a significant profit in the long term. Their Honours concluded that whether or not the removal of $580,000 from the asset pool was a deliberate plan or an unintended consequence of the investment was irrelevant. To deny the wife the right to share in nearly $580,000 which she would have done but for the wine investment, whilst at the

same time denying her the opportunity to participate in the investment cannot be said to be just and equitable.

The Full Court remitted the matter for re-hearing. However, before doing so, their Honours held there were a number of ways the economic consequences of the wine transaction could have been taken into account in order to achieve a just and equitable result. *"They could have been taken into account in a number of ways, for example: according to the Townsend guidelines; or upon a consideration of the s 75(2) factors. Alternatively it was open to his Honour to adjourn the proceedings pursuant to s 79(5)."* Presumably this would have been to a date when the wine had at least recouped its original investment or its anticipated increased value.

A miscellany of other case studies

In ***SL & EHL [2005] FamCA 132*** after thirty five years of marriage the parties separated with assets worth about $8 million. One major issue concerned the treatment of payments and other benefits the husband was making to his present wife. It was argued by the wife that interests in two apartments owned by the husband and his present wife, and well as her superannuation and distributions received from the parties family trust should be notionally added back. The husband contended that there was no case for add backs largely because payments made to his present wife were from income generated by the husband post-separation, albeit to a considerable degree from assets established during his first marriage.

Warnick J held that at law the property and benefits received by the husband's present wife belonged to her. His Honour was concerned about potential injustice to the husband if the court notionally added back to the matrimonial pool amounts paid to his present wife and property held in her name which advances the husband may not have been able to recover. If notionally added back it was difficult to resolve how taxation saved through

trust distributions to the present wife would be taken into account. Importantly, his Honour held the court could not ignore contributions the present wife may have made to the assets sought to be notionally added back. The court decided that the use of funds by the husband post-separation was something to which regard ought to be had in assessing contributions, rather than evaluating the asset pool. Unless the husband's expenditure was recoverable as his property, his Honour held that to add it back into the asset pool was an inappropriate way treat this expenditure.

The parties were beneficiaries to a discretionary trust to which a charity was also a beneficiary. From time to time the husband caused money to be distributed to the charity, which the charity always loaned back to the trust, interest free. No drawings of significance had been made on the account. The wife submitted one of several approaches should be taken in relation to the charity/trust transactions, as well as claiming that the trust property be notionally added back. The three approaches are:

- That the loan liability to the charity is disregarded as it would seemingly not be called upon before the husband's death;
- That the liability be brought to account at its present value, assuming it is not payable until the husbands death, or
- That the loan monies be added back to the asset pool, on the basis that they represented use of monies by the husband for his own purposes.

On all counts the wife failed. His Honour considered when regard was had to pre-separation distributions it would unjust and inequitable to proceed as the wife suggested. The loan arrangement was one which provided considerable financial benefit to the husband, and it was considered that it would be unfair to add in the loan monies without giving any credit for the advantage. There were no add backs of note factored into the asset pool.

HDM & MM & SJM [2006] FamCA 47 is another recent Full Court decision. The parties commenced cohabitation upon their marriage in 1977, and separated in 2001. They were divorced in 2003. At the time of trial the husband had remarried. He was a partner in a firm of chartered accountants. The wife worked primarily as a homemaker and she also ran a small design business from home. This was the husbands appeal against orders in relation to property and spousal maintenance. The trial judge determined the parties and assets were valued at $1.6 million, of which the wife received 75% and the husband 25%. Also the wife was awarded spousal maintenance for two years of $1100 per week, reducing to $750 per week thereafter. On appeal the husband sought that the value of the asset pool be reduced to $1.2 million, the wife's division of assets be reduced to 70% and that her spousal maintenance cease after two years. One of the issues on appeal concerned the sum of $239,000, being the net distribution the husband received from his accounting partnership shortly before separation which the trial judge included in the asset pool. The trial judge rejected the husband's contention this amount was income earned during the 2003 financial year and thus post separation earnings. The trial judge found that this sum comprised dividends from the proceeding financial year during which the parties had separated and thus also cohabited.

On appeal the Full Court applied the *Omacini* principles. Their Honours held that the husband had not *"acted recklessly, negligently or wantonly"* nor in a way that would see the joint matrimonial assets being deliberately reduced. The husband submitted that, as a considerable portion of the distribution was used in the purchase of a new home for he and his new partner, and as this property had been included in the matrimonial asset pool, to add back the entire $239,000 sum was double dipping. The Full Court agreed and held that the portion of funds used in the acquisition of the husband's new home should not be notionally added in.

The Full Court observed that, because of his profession, the husband was in a position to provide the court with better particulars than he proffered in relation to expenditure of these funds. As a result, there was room for the trial judge to be sceptical and treat the

sum *"more boldly than the husband might have wished"*. In the end however, it was deemed that the lack of disclosure on the husband's behalf did not amount to a deliberate attempt to deceive, and by the end of the trial the fate of the undisclosed funds had been revealed. Their Honours concluded that the husband should be given credit for income tax and the acquiring of the property out of the distribution, either by increasing the matrimonial liabilities or reducing the extent of the add back. Either way, the pool of assets was to be reduced by a total of $141,476, reducing the net asset pool to $1,493,292.

At trial the husband had invited the court to include a $160,000 taxation debt amongst the liabilities of the parties, on the grounds that it related to income which had been contributed to the make up of the asset pool, and the support of the wife. Given the husband's large salary, and his habit of paying his taxation liability from his following year's income, as well as the fact that much of his post-tax salary was going to support his new wife and his mortgage with her, the trial Judge did not consider it appropriate that this be added back against the wife. This was particularly so as the debt related to a period well after the parties separated. Their Honours agreed with this approach and held that it would be inappropriate for the wife to be responsible for *"tax referable to monies utilised by the husband in the acquisition or support or conservation or improvement of assets belonging to his present wife"*. On this point, their Honours held that there was no error in exercise of discretion by the trial judge.

In ***D and D [2003] FamCA 227*** **t**he parties married in December 1995 and separated in December 2000. In January 1998 the husband was injured at work. One year after separation the husband received $440,000 damages, about $300,000 of which had been dissipated by the hearing. The wife sought to include the entire verdict in the pool, whilst the husband sought to only include the remaining $140,000.

The first instalment of the damages claim ($382,261.97) was deposited into an account held by the husband's brother in law. In that same month, the husband alleges he began gambling a casino. A few months later the husband received an additional $46,000, which he contends he spent on living expenses and gambling. All told, the husband claimed that between January and June in one year he lost between $180,000 and $200,000 at Star City. From that time, the husband said his brother in law transferred $137,000 of the settlement funds into his own account to hold for the husband and gave $30,000 to their father. With that money, their father advanced the husband about $350 per week for living expenses. At the date of hearing the husband claimed to have $140,000 of his compensation money remaining. He provided details of his current expenditure and prior gambling. Other than the funds given to his father the husband was unable to account for the balance. The trial judge found that the husband's actions were designed to defeat any claim the wife had to his settlement monies, and these actions were assisted by the brother in law. The evidence in relation to the husband giving his father $30,000 was also rejected.

Her Honour considered whether, owing to the husbands lack of full and frank disclosure, the full value of the settlement monies should be put into the asset pool. Certainly her Honour accepted that the husband had attempted to disguise the settlement, and that his disclosure had been neither full nor frank. She also accepted however that some discount should be given to the settlement amount to account for the husbands gambling addiction ($78,000), and his day to day living expenses ($20,000). Justice Boland also took into account legal expenses the husband paid from the funds ($34,950), and noted that, unless a deduction was made for these, including the sum and the settlement monies would lead to double counting. Ultimately a figure of $295,000 was to be added back into the pool.

The next issue her Honour addressed was whether or not the sum to be included in the list of assets and liabilities should be increased because of the manner in which the husband applied the funds. It seemed that on its face, the gambling would reasonable be regarded as "negligent, wanton or reckless". However Justice Boland gave weight to the fact that,

prior to receiving the money the husband had a serious accident, underwent surgery and lost his job. Her Honour found that he was bored and depressed, which state of mind contributed to his gambling. Thus her Honour was not persuaded that all the funds lost should be added back into the asset pool. However, while persuaded against adding back the entire settlement fund, the fact that the husband had sole use of these funds, and the manner in which he used them were taken into account as s 75 (2) factors.

Conclusion

The principles which arise from these cases are the following:

- The principle in *Kowaliw* is not a fixed code.
- *Kowaliw* is a useful guideline for dealing with cases involving lost assets or income.
- In cases involving waste there must be a proper reason for adopting a non *Kowaliw* approach.
- If the losses occurred in the course of the pursuit of the objectives of the marriage then such losses should be shared by the parties, although not necessarily equally.
- The economic consequences of waste must be dealt with in a just and equitable manner.
- The economic consequences (loss) may be treated as a premature distribution of the asset pool and notionally added back as the asset of the party who had its sole benefit.
- Taking the premature distribution into account in a general way pursuant to s 75(2)(o) and applying the cumulative outcome of the s 79(4) and s 75(2) findings to the smaller depleted asset pool may offend s 79(2) notions of justice and equity.

- Where the asset pool had been seriously depleted it may be that only by giving the premature distribution its full dollar value that justice can be given.
- The premature distribution concept is not restricted to post separation transactions.
- Where the monies have been shown to have been reasonably disposed of the notional add back approach should be the exception and not the rule.
- Notional adjustments are not limited to wasted assets but may also include property that has been bona fide disposed of.
- The source of the funds is relevant.
- Notionally included assets may include unascertained assets, even if the precise value is not known.
- Even if does not involve waste, the economic consequences of a significant reduction in the asset pool must be considered.

Catch word summaries - Family Court first instance

C & C [2004] FamCA 911

PROPERTY - Family Law Act - Parties marriage of 13 years duration. Parties reached agreement that the child of the marriage live with the mother and have substantial contact with the father. Parties initial contributions approximately equal. Husband received $80,000 advance from his father. Characterisation of the advance in dispute. In 2000 the husband received a repayment of his superannuation entitlement including an invalidity component of $175,500 gross. Dispute over add backs to the parties list of assets and liabilities CHILD SUPPORT - Family Law Act - Query whether appropriate to make a departure from the statutory assessment of child support on the basis of the agreement of the parties for the child to attend Newington College.

L & L [2005] FamCA 166

PROPERTY settlement – add backs of capital distributed to asset list in lieu of examination of post separation expenditure - child support departure – parenting orders re details of father's contact.

H & H [2005] FamCA 1076

Property settlement – discussion of appellate authorities concerning 'add-backs', exclusions or modifications to the composition of the parties' assets and liabilities for s 79 purposes – discussion of appellate guidelines related to composition of the parties' net assets - findings as to various submissions about 'add backs' to the assets list and about various liabilities alleged.

S & S [2005] FamCA 1181

PROPERTY SETTLEMENT – Family Trust – wife seeks to set aside pursuant to s 106B trust variation instruments which exclude the husband from the capital of the fund and dispositions of shares worth $500,000 and trust property worth $4.7million by the husband – alternatively wife seeks to notionally add back shares and trust property to the pool – alternatively wife seeks to treat trust assets as a financial resource of the husband taken into account under s 75(2) – husband is appointer and trustee of the trust – assets of the trust can be treated as the property of the husband or his financial resource – Part VIIIAA cannot be applied as the requirements of s 90AE have not been satisfied – trust variations may be set aside pursuant to s 106B – alternatively Townsend principles applicable to the husband's distribution of assets – husband's contributions outweigh the wife's due to his substantial initial contribution – no s 75(2) adjustment, wife's care of the youngest child offset by her greater income and earning capacity – total pool $9.8million –order 52%/48% division in favour of the husband – orders do not cause a breach of trust or fraud on power – set aside the disposition of trust property and the variation to the trust instrument excluding the husband from the capital of the fund.

R & R & S [2006] FamCA 32

PROPERTY SETTLEMENT – 8 year marriage – husband received a $240,000 lump sum compensation payment for a work injury – wife the primary caregiver of the 4 children of

the marriage – husband wasted money gambling – husband failed to make mortgage and loan repayments post-separation – notionally add back moneys spent by the husband post-separation – assess contributions 52.5%/47.5% in favour of the husband – s75(2) factors: wife's care of the children, husband's ability to obtain work, lack of support provided by the husband for the children – 70/30% distribution in favour of the wife.

Federal Magistrates Court decisions

AB & GB [No 2] [2005] FMCAfam 402

FAMILY LAW – Property – contributions – damages – gambling losses – waste –add backs – discussion *Kowaliw* principle – *Kowaliw* is not a fixed code – even if it does not involve wasted economic consequences of a significant reduction in the asset pool must be considered – whether lost funds should be notionally added back applying *Townsend* principle or addressed pursuant to s.75(2)(o) – where the asset pool has been seriously depleted it may only be by giving premature distribution its full dollar value that justice can be given – premature distribution concept is not restricted to post separation transactions – future needs.

A & A [2002] FMCAfam 244

FAMILY LAW - Property - initial contribution - investment property and business sold without wife's knowledge - notional add back of part of proceeds of sale - spouse maintenance.

ST & BC [2005] FMCAfam 37

FAMILY LAW - Property - contributions - initial contribution - application of *Townsend* principles for notional add backs - valuation of company - wife claims *Kennon* adjustment - *Kennon* does not establish a principle of general application that any assault warrants adjustment in the spouse victim's favour pursuant to s 79(4)(c) - where assets are held in a family company - wife asserts taxation implications should be disregarded - *Rossati* discussed - because company must pay taxation on a distribution of its assets taxation must be taken into account - future needs.

J & J (Property – Jewellery, ill health) [2003] FMCAfam 4

FAMILY LAW - Property settlement - neither party working - husband disabled - both parties in poor health - valuation of retirement, compensation and other benefits received and in part spent by the parties - valuation of jewellery - disputed chattels - just and equitable.

AP & ENP [2002] FMCAfam 164

FAMILY LAW - Property settlement - husband Vietnam war veteran - effect of wife's psychological or emotional condition - wife suffering from untreated clinical depression - application of s 75(2) factors