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Premature Distributions, Waste and Addbacks

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Blanchfield Nicholls

Since establishment in 2007 Blanchfield Nicholls has evolved into one of Sydney's most trusted family advisory firms. Blanchfield Nicholls has been consistently recognised as one of leading family law firms in Sydney from 2015 – 2023 inclusive by the independently researched and peer nominated Doyles Guide.

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Introduction

1. In property settlement proceedings under s79 or s90SM of the *Family Law Act* ("*FLA*"), the Court is required to determine whether it is just and equitable to alter the parties' interests in property following marriage or de facto relationship breakdown, and in considering what order, if any, should be made, have regard to the asset pool, the parties' contributions and future needs factors. The consideration of whether it is just and equitable to make a property settlement order begins with "*identifying, according to ordinary common law and equitable principles, the existing legal and equitable interests of the parties in property*"[1].

2. In practice, it is not that uncommon for there to have been a premature distribution of assets, particularly in cases where there is a lengthy period of time between separation and final hearing, or complaints made by a party that assets have been "wasted" by the other, or that assets should be "added back" to the pool.

3. The Full Court in *Omacini & Omacini*[2] identified three clear categories in which the court was willing to notionally add-back property:

    1. **Premature distribution of funds:** where there has been a premature distribution of matrimonial assets;
    2. **Legal fees:** where the parties have expended money on legal fees;
    3. **Wastage:** In the circumstances outlined *In the Marriage of Kowaliw*[3] ('*Kowaliw*') - where one party has "*embarked upon a course of conduct designed to reduce or minimise the effective value or worth of matrimonial assets*" or has "*acted recklessly, negligently or wantonly with matrimonial assets*" with the effect of reducing their value.

4. Whilst these categories are not exclusive[4], they represent the majority of matters in which add-backs have been discerned.

[1] Standford & Stanford [2012] HCA 52 at [37]
[2] (2005) 191 FLR 317 at [30].
[3] (1981) 23 Fam LR 396.
[4] *Layton & Layton* [2014] FamCAFC 126 at [37].

Addbacks

5. The authorities are clear that it is ultimately a matter for the trial judge's discretion whether to notionally add back property to the asset pool[5] . Further, the Full Court has confirmed in *C v C* [1998] FamCA143 at [46] that:

> "*whilst not seeking to place a fetter upon the exercise of discretion of a trial judge in individual cases, it seems to us that the concept of adding monies reasonably disposed of back into the pool ought to be* ***the exception rather than the rule****. The parties are entitled to reasonably conduct their affairs post separation in a manner that is consistent with properly getting on with their lives*".

6. The Full Court in *Omacini* confirmed that an addback does not necessarily occur whenever "*a party has expended money realised from the disposition of assets that existed as at the date of separation*", the Full Court describing such a proposition as "*unduly simplistic*". It will be necessary within the context of the matter to consider the reasonableness of the expenditure. For example, reasonable expenditure incurred for living expenses will not be added back[6]. In *M v M* [1998] FamCA 42 the Full Court held at [2.11]:

> *There seems to be no appropriate basis for notionally adding back monies that existed at separation but which have subsequently been spent on meeting reasonably incurred living expenses. Neither the Family Law Act nor the case law require that parties go into a state of suspended economic animation once their marriage breaks down pending the resolution of their financial arrangements. Parties are entitled to continue to provide for their own support. Whether any expenditure so incurred is reasonable or extravagant is a matter that can be determined by the trial judge*."

7. The Full Court in *Trevi & Trevi* [2018] FamCAFC 173 again confirmed the fundamental precept that addbacks are exceptional and that generally the Family Court must take the property of a party to the marriage as it finds it at trial. Further, and [30] "*two fundamental premises emerge from Omacini and the authorities preceding it. First, "adding back" is a discretionary exercise. When the discretion is exercised in favour of adding back, it reflects a decision that,* ***exceptionally****, in the particular circumstances*

[5] *Chorn & Hopkins* [2004] FamCA 633 at [56].
[6] *M v M* [1998] FamCA 42 at [2.11].

of a case, justice and equity requires it. The second premise is its corollary: in cases that are not "exceptional" justice and equity can be achieved, not by adding back, but by the exercise of a different discretion – usually by taking up the same as a relevant s 75(2) factor. Indeed, it has been said that the latter is "a course which is, perhaps, technically more correct" than adding back to the list of existing interests in property.

8. In *Kouper & Kouper*[7] Murphy J confirmed the ultimate manner in which dissipation of matrimonial property was dealt with was a matter for the judge's discretion. However, in reviewing the earlier authorities his Honour summarised the approach to add-backs as being a five-question approach:

> 1. *Is it contended that property (including money), that would otherwise be available for distribution between the parties if a section 79 order is made, has been dissipated with a consequential loss to the property otherwise potentially divisible between the parties at the date of trial?;*
> 2. *If so, is it alleged that the dissipation of property was in respect of things other than what, in the particular circumstances of this particular marriage, can be classified as "reasonable living expenses"?;*
> 3. *If it is asserted that any loss to the divisible property results from dissipation of property other than in respect of such expenses, why is it asserted that the result should be a sharing of that loss by the parties other than equally?*
> 4. *If it is contended that this be the result, why should there be an add back (which brings to account, dollar for dollar, such past expenditure in current dollars) as distinct, for example, from there being an adjustment being made pursuant to s 75(2)(o)?; and*
> 5. *How should either any "add back", or adjustment pursuant to s 75(2)(o), be quantified?*
>
> …
>
> *The task is not to examine conduct for the purposes of fitting it within a particular description, or to reward the prudent and punish the imprudent. Rather, task is to examine and make findings about the particular circumstances surrounding expenditure and to determine, within that context, the manner in which overall justice and equity indicates the diminution in the pool ought to be treated*".

[7] (no. 3) [2009] FamCA 1080.

9. Further, the Full Court in *Trevi & Trevi* [2018] FamCAFC 17 explained that:

> *Adding back does not seek to create property interests that do not exist. Rather, doing so emphasises that satisfying the respective requirements of ss 79(2) and (4) of the Act to do justice and equity can require an "accounting" or "balance sheet" exercise for the purposes of s 79(2) and (4), so as to include the value of the dissipated property or expended sums within the total value of the parties' existing interests in property, and to credit the value of same against the assessed entitlement of the dissipating or spending party.*

Premature distribution of funds

10. *Townsend v Townsend* [1994] FamCA 144 is perhaps the most referenced case on the issue of premature distribution of funds. The husband in this case, after separation, sold a taxi license for $148,000 and retained the profit from the sale and ultimately spent the funds. The Court found that the proceeds were a matrimonial asset to which the wife had a legitimate interest in and therefore it would be unjust to treat such conduct as a matter merely under s 75(2)(o). Nicholson CJ held at [81]:

> *"In my view, what occurred in this case, as I said during the course of argument, was, in fact, a premature distribution of a proportion of the matrimonial assets. What the husband did was to distribute to himself an asset in which the wife had a legitimate interest. In such circumstances I consider that it would be unjust in the extreme to simply treat such conduct by the husband as a matter to which regard should be had under s.75(2)(o). It seems to me that the husband has had the benefit of that money. Had he retained, for example, the taxi licence instead of selling it, that would have been brought into account as an item of property which would have been dealt with in the same way as the remaining items of property in this case. Accordingly, I am of the view that the correct way in which to deal with the husband's receipt of those monies is to bring them into the pool of assets on a notional basis and make a distribution accordingly."*

11. In the more recent case of *Baggin & Hallion* [2021] FedCFamC1F 80, Baumann J exercised discretion in deciding to notionally addback savings of $215,630 that the husband had at separation in circumstances where it was found his income was sufficiently adequate for him to enjoy a lifestyle of his choice, without the need to spend that additional sum of savings. Baumann J considered the disposition as *Townsend*-

like and this was also done in the context of his Honour not adding back either parties' legal fees. His Honour held at [58]:

> "*Certainly his income, post separation alone, was more than adequate for him to enjoy a lifestyle of his choice with some expenditure on luxury discretionary items (some of which the wife identified in the evidence on alleged "wastage"). Again, because I have decided not to include any allowance for paid legal expenses, I see it as just and equitable to include the husband's savings at separation."*

Non-Disclosure

12. In the case of non-disclosure, the value of the asset may be added back to the pool, at the trial judge's discretion[8]. The Full Court held that once it was established that a party had been deliberate in its non-disclosure, the Court should not be unduly cautious about making findings in favour of the innocent party. This is to be taken with a grain of salt however, as the Court's power to make an order going beyond the identified property only arises once sufficient evidence[9] has supported a finding that a party has not made full disclosure of his or her assets.

13. The Court may instead however approach the asset pool to take into account non-disclosure by making an adjustment in favour of the other party pursuant to s 75(2)(o) of the *Family Law Act*[10].

Wastage

14. Marriage (and in more recent times de facto relationships) have been determined as an economic partnership, for most couples[11]. The reported decisions in respect of property settlements under s 79 are unanimous that both parties should share the economic fruits of a marriage, although not necessarily equally[12]. Similarly financial losses by the parties during the marriage, caused by joint or several liability should be something shared between the parties, although not necessarily equally. Generally, you take the good with the bad. The exception to this being wastage, as outlined in *Kowaliw*[13] where one party has:

[8] *Weir and Weir* (1993) FLC 92.
[9] S 140 *Evidence Act 1995* (Cth).
[10] *Gould and Gould* (2007) FLC 93.
[11] *In the Marriage of Kowaliw* (1981) FLC 91-92.
[12] Ibid.
[13] Ibid.

1. "*embarked upon a course of conduct designed to reduce or minimise the effective value or worth of matrimonial assets*", or

2. "*acted recklessly, negligently, or wantonly with matrimonial assets, the overall effect of which has reduced or minimised their value*".

15. In these circumstances the Court may add-back the value of the wasted assets to the pool, or make an adjustment pursuant to s 75(2)(o).

16. The husband's actions in *Kowaliw* involved allowing a prospective purchaser of the matrimonial home (who did not eventually purchase it) to live there without paying rent for a period of about 12 months. The trial judge Baker J. found that these actions were "*commercially inept and economically reckless*" and the husband alone should be entirely responsible for the consequential loss of rental income, maintenance levies and mortgage instalments which should have been paid.

17. In the recent case of *Halstron & Halstron* [2021] FamCA 437 the Court dealt with, amongst other matters, losses on the parties' share portfolio as a result of the wife's freezing of the CommSec trading account through which the husband traded shares during the marriage, primarily through the parties' self-managed superannuation fund. The wife had complete access to the CommSec account, including the ability to log into it, monitor the husband's transactions, and buy shares herself if she wanted to do so. The wife froze the account in October 2017. The husband repeatedly asked the wife to unfreeze it, including via correspondence from his solicitors but she refused to do so. As a result of the wife's failure to reactivate the account the parties have incurred substantial losses on their share portfolio, which the husband estimated to be over $1 million. This $1 million loss is said to have arisen in circumstances where in March 2018 the husband sought to have the wife reactivate the CommSec account in order that he could sell 5,156,353 shares in QQ Pty Ltd on a tax effective basis. There was evidence that at this time the share price for QQ Pty Ltd was approximately 31 cents per share. The husband submitted that if the QQ Pty Ltd shares had been able to be sold at this time the parties would have received some $1.598 million, but the wife refused to permit this. At the time of the hearing in February 2020 the QQ Pty Ltd share price was approximately 10 cents, meaning that the value of the parties' shareholding had fallen to about $515,000. The husband argued that had the wife unlocked the account in late March 2018, as he had sought, there would have been an additional $1 million available for division between the parties, something which the wife

ultimately admitted in cross examination. The Court did not "add back" the $1 million however the wife's conduct and subsequent loss were dealt with via s 75(2)(o).

18. In the 2022 matter of Potter & Lloyd[14] the evidence of potential addbacks were less than satisfactory. Regarding the amount of rental income received by the de facto wife post-separation the de facto husband stated "*it is my assumption that* [the respondent's] *rent monies substantially exceed* [her] *expenses*", because he "*simply* [does] *not know how* [the respondent] *financially survives*". Campton J stated that it would be unsafe to guess as to the quantum of the benefits retained by the de facto wife from the rents and hence inappropriate to notionally add back the value asserted by the de facto husband.

19. In that same case, the de facto wife argued that the de facto husband had caused substantial losses due to his renovation on the property that was occupied by both parties. The de facto wife constructed the impact of the work done on the property as a 'negative contribution'. However, Judge Campton stated that the following circumstances should be decided through the lens of *Kowaliw* and it's guideline on waste. It was found that the renovations were a joint endeavour, by the parties for the benefit of each them. The respondent de facto wife directed, encouraged, and observed the works for a number of years and sourced monies for the funding. Thus, it was not found that the de facto husband acted in a 'negligent, reckless or wanton manner'. Upon also relying on *Browne & Green* [1999] FamCA 1483; (1999), there should be good and substantial reasons for departing from the principle that where there are economic losses incurred in a relationship, those losses should be shared, absent any negligence, recklessness, or deliberate dissipation of assets by one party.

<u>Gambling</u>

20. Monies spent on gambling are usually argued as wasted funds, and sought to be added back to the pool. *De Angelis and De Angelis* [1999] FamCA 1609 is one of the leading authorities on gambling in this context.

21. In *Hamilton & Thomas* [2008] FamCAFC 8 some of the grounds of appeal concerned findings made by the trial judge about gambling and how those findings were dealt with pursuant to section 75(2)(o). The Full Court of the Family Court of Australia held:

[14] (No 2) [2022] FedCFamC1F 284.

34. *In De Angelis and De Angelis [1999] FamCA 1609; (2003) FLC 93-133; (1999) 30 Fam LR 304, Lindenmayer and Finn JJ observed:*

> *76. We agree that gambling is for some people a form of entertainment and that a party can be no more criticised for spending money on it than the other party can be criticised for spending money on sporting or other forms of entertainment...*

35. Whilst their Honours then went on to say "however every case must depend on its' own particular circumstances", in our view, the circumstances of this case are apposite to the first observation, namely that for this family the gambling undertaken was no more than their normal form of entertainment and that the amounts involved were not so disproportionate as to, in our view, justify the trial judge in making any adjustment to the entitlements to the pool of assets of either of the parties.

36. Over the course of the marriage of some 4 and a half years, the Wife's losses at $100 a week would have totalled approximately $23,000. Offset as against those losses were the Husband's losses of an unidentified amount. The losses had to be viewed in light of two key findings, firstly that these parties' had non-superannuation assets of over $800,000 and superannuation assets of a further $500,000, and further the finding at paragraph 131 that "it was part of their lifestyle to attend at clubs on a regular and frequent basis".

37. In our view there was nothing so disproportionate in relation to the losses incurred by the parties' in the lifestyle that they chose, that would make it appropriate for there to be an adjustment of the available capital upon the breakdown of the marriage. More is required than simply the existence of gambling losses. There needs in our view to be some element of wastage that is disproportionate to the positive contributions being made by each of the parties.

[emphasis added]

22. In the case of *Giang & Trom*[15] the husband's gambling expenditure and related loans totalling $155,627 was viewed as a significant sum by contrast to the remainder of the property pool which was $649,000. The Court looked to the context of the family's financial circumstances including the respective wages of both parties, the personal

[15] [2021] FedCFamC2F 149.

loans taken out by the husband during the relationship, and the related mortgage debt, and came to the conclusion that the husband had committed wastage within the *Kowaliw* sense and as such the property pool should be adjusted pursuant to s 75(2)(o) of the *FLA*. The Court held that even absent Kowaliw and in any event, the justice of this particular case required the gambling expenditure to be taken into account in the wife's favour pursuant to section 75(2)(o) because the found gambling expenditure represented such a significant sum when compared to the value of the family home and related mortgage debt (both present and historically) and the financial circumstances of this family. A percentage adjustment was made in the wife's favour.

23. The party alleging the waste has the onus of proof on the balance of probabilities: see *D and D* [2005] FamCA 356 at [160].

Legal Fees

24. The general rule in relation to costs in all family law matters is set out in s 117 of the *Family Law Act*, that in the first instance at least, each party shall bear his or her own costs.

25. Therefore legal fees "*occupy a particular position in the consideration of addbacks by reason of s 117(1) of the Act… If a party is paying legal fees from joint assets, it means the other party is contributing to those legal fees which is not the starting point created by s 117(1).*"[16]

26. The Full Court in DJM v JLM (1998) 23 FamLR 396 held at [11.6]:

> *"s. 117 provides that each party to proceedings under the Family Law Act shall bear their own costs unless the Court otherwise orders. Failing to add back monies expended by parties on costs frequently has the effect of defeating the policy of s.117 by permitting the pool of available assets for distribution between the parties to be diminished by any monies that either of the parties have managed to spend on their costs up to the date of trial. We are of the view that the normal approach ought be to add costs already paid back into the pool. Whilst there may be cases where that approach is inappropriate, the reasons why it is not taken ought normally be spelt out. We see no reason advanced in this case as to why the costs paid should have been kept out of the pool."*

[16] Oamara & Williams [2021] FamCAFC 117

27. The Full Court in *Chorn & Hopkins* outlined four principles to guide the trial judge in their discretion:

> *56. In summary, we consider that the above mentioned decisions of the Full Court establish that, while 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 the funds.*
>
> *57. If the funds used existed at separation, and are such that both parties can be seen as having an interest in them (on account, for example, of contributions), then such funds should be added back as a notional asset of the party, who has had the benefit of them.*
>
> *58. If funds used to pay legal fees have been generated by a party postseparation 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 added back as a notional asset; nor would any borrowing undertaken by a party post-separation to pay legal 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 postseparation income or acquisitions.*
>
> *59. Outstanding legal fees themselves are generally not taken into account as a liability.*
>
> *60. If, in the exercise of discretion, it is determined that legal fees already paid should be taken into account as a 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.*

Status of addbacks post Stanford

28. In Stanford, the High Court held that the consideration of whether it is just and equitable to make a property settlement order begins with "*identifying, according to ordinary common law and equitable principles, the* ***existing*** *legal and equitable interests of the parties in property*".[17]

[17] Standford & Stanford [2012] HCA 52 at [37]

29. This was followed by the obiter statement of Bryant CJ and Thackray J in Bevan & Bevan [2013] FamCAFC 116 at [79]:

> *We observe that "notional property", which is sometimes "added back" to a list of assets to account for the unilateral disposal of assets, is unlikely to constitute "property of the parties to the marriage or either of them", and thus is not amenable to alteration under s 79. It is important to deal with such disposals carefully, recognising the assets no longer exist, but that the disposal of them forms part of the history of the marriage – and potentially an important part. As the question does not arise here, we need say nothing more on this topic, save to note that s 79(4) and in particular s 75(2)(o) gives ample scope to ensure a just and equitable outcome when dealing with the unilateral disposal of property.*

30. Stanford and Bevan prompted widespread commentary by practitioners and academics on whether addbacks are still appropriate, with some arguing addbacks are a thing of the past.

31. The legal position on addbacks was cleared up by the Full Court in *Vass & Vass* [2015] FamCAFC 51 at 138-139:

> *138. There is no error committed per se in adjusting the parties' actual property interests by a calculation involving notionally adding back into the pool sums which have been dissipated by the parties. We reject any suggestion that the decision of Bevan & Bevan [2013] FamCAFC 116; (2013) FLC 93-545 – or, more particularly, the decision of the High Court in Stanford & Stanford [2012] HCA 52; (2012) 247 CLR 108 - is authority for any necessary contrary solution. Some statements made by the High Court may lead to the conclusion that references to "notional property" as have been referred to in decisions of this court and at first instance may need to be reconsidered.*
>
> *139. The decisions referred to seek to remind the Court that, however the exercise of discretion might seek to deal with property that is said to be the subject of "add back", proper consideration must be given to existing interests in property, and the question posed by s 79(2) as a separate inquiry from any*

adjustment to property interests by reference to s 79(4) if a consideration of s 79(2) reveals that it is just and equitable to alter existing interests in property.

32. The Full Court in *Calder & Calder* [2016] FamCAFC 36 confirmed it was permissible for a trial judge to add-back notional property, holding at [135] "*if there was any doubt that the position mioght have changed as a result of what was said in Stanford v Stanford or Bevan & Bevan… that doubt has been removed by what was said by this court in Vass & Vass*.

33. Addbacks are alive and well!

Practical tips

Prevention and protection strategies

34. How do you prevent dissipation of assets? How do we protect and preserve the asset pool?

35. If you have any concerns that a party is taking steps to dissipate assets, consider filing an application for urgent injunctive relief. Such an application would of course need to be supported by evidence, and your client will usually need to give an undertaking as to damages.

36. Is an ex-parte application appropriate?

37. If real estate is involved, think about whether your client has a caveatable interest? If so, lodge a caveat if it is appropriate to do so.

Evidence

38. It is important to note the factual matrix of each case. We as practitioners need to be mindful of what assertions can be supported by evidence, and what arguments can be run. Clients at times make generalised statements about gambling or other asserted wastage. But the question is – what evidence do we have to support those assertions and is there an arguable case?

39. Be clear on what evidence there is to support or resist the add back, or argue section 75(2)(o).

40. Gather all relevant material, request disclosure and issue subpoenas.

41. Costs Notices are important. We are required to identify the source of funds used to pay legal costs. Request further disclosure from the other side if source of funds is not obvious.

Other tips

42. Time is often not your friend. Cases where there is a long gap between separation and final hearing are usually the ones where arguments about addbacks are going to be made.

43. Section 106B Applications may also be appropriate, to set aside the transaction or instrument.

44. Consider running arguments in the alternative ie addback and the section 75(2)(o).