

## Dealing with Trusts in Property Settlement Disputes

Allegations are sometimes made within property proceedings that a trust is a sham trust. A popular argument raised within property settlement proceedings is that a party to the proceedings has the control or influence over the trust which, if proven, would lead to a finding that the property of the trust ought to be included as property available for distribution between the parties in a matrimonial or de facto property settlement. The rationale is that if the husband or wife is the trustee of a discretionary trust, he or she may use that power to appoint themselves as a beneficiary of the trust and therefore create an interest in the trust property.

Claims against discretionary trusts were recently considered in the High Court case of *Spry v Kennon* [2008]. Prior to *Spry v Kennon*, the Court's position with respect to trust property was dependent on establishing alter ego/puppet scenarios. That is, a trust established by either spouse over which he or she exercises control and that trust in turn owns or controls property. In circumstances like this, the Courts have described these types of trusts as the 'alter ego' or the 'puppet' of that party.

"*Spry v Kennon* changed this position considerably," says Antonious Abdelshahied, Lawyer, **Michael Sing Lawyers Pty Ltd**.

In this High Court case, the parties were married in 1978, separated in 2001, and divorced in 2003. A trust was created in 1968. In 1983 the trust deed was executed in which the Husband released and abandoned any beneficial interest in the trust he may have had as settlor (creator of the trust) and otherwise as, on the face of the clause, a beneficiary.

At the same time, the Husband appointed the Wife as trustee in the event of his death or resignation. In 1998, three years prior to separation, a deed was executed by the Husband excluding the Wife and himself from any 'interest, rights and possibilities in the capital of the fund.'

Shortly after separation, the Husband created a number of other trusts for the benefit of his children, and transferred assets to them. Those transfers were later found to be transactions to defeat an anticipated order under the *Family Law Act 1975* ("the Act").

The asset pool was valued at around \$9.8 million, of which approximately \$4.5 million was property held by the trust. The trial judge ordered that the 1998 deed be set aside and the Husband pay to the Wife \$2.1 million. The difficulty for the Husband was that he only had \$1.7 million of property in his own name.

On Appeal, the Full Court of the Family Court found that "*once it is accepted the effects of the 1983 deed can be reversed, this is a case like many others where assets are held in a discretionary trust and the Husband has "control" as trustee and is capable of having the capital and income distributed to him as a beneficiary*".

The High Court, by a 4-1 majority, dismissed the appeals and upheld the trial judge's order for the Husband to pay the Wife \$2.1 million. The Husband was also ordered to pay the Wife's costs. Essentially, the Husband argued that the assets of the trust were not part of the asset pool to be considered in making property orders.

French CJ held that the property of the trust, as well as the beneficiaries' right to due administration of the trust, is property for the purposes of property settlement proceedings.

Gummow, Hayne and Keifel JJ held that the property was the right to due administration of the trust and that where due administration of the trust included the powers to distribute the entirety of the trust property to either spouse as beneficiary, then the value of that right constituted the value of the trust property.

Further, if the purpose to remove as trustee or beneficiaries' spouses in a property settlement matter has the effect of removing that property from the purposes of property settlement, and therefore to defeat an order, then it follows that the Court can set aside those dispositions (amendments) pursuant to s106B of the Act.

The effect of the High Court decision is that the Family Law Courts can now deal with trust arrangements in a far more robust way than was previously possible. The use of a trust structure, particularly one which is in reality a device used to accumulate family assets, is now even less likely to put such property beyond the jurisdiction of the Family Court.

"It is virtually impossible to protect an existing discretionary trust from a family law claim," warned Mr Abdelshahied.

However, there a couple of ways of dealing with potential future claims for newly formed trusts and they include:

- ✓ When drafting the terms of the discretionary trust deed, the terms would need to ensure that:
  - the class of beneficiaries effectively have no control over the trust; and
  - the power of appointment/removal of trustees would need to be independent of the class of beneficiaries; and
  - the trustees themselves would need to be unrelated (in both a business and family sense) to the beneficiaries; and
  - neither spouse could be named as a residuary or default beneficiary, with some charitable organisation being the only remaining option.
- ✓ The use of the trust (both on the face of the deed and in practice) would need to be more than a vehicle for accumulation of 'family' assets.
- ✓ The advantage of drafting the deed in this way is that it *might* protect against a finding of property, but the primary disadvantage is that the income and capital of the trust becomes so remote that the original purpose of the trust might be thwarted – leaving the Courts in a position to 'exclude' the trust property from family law property settlement.

In family law, a transfer intended to defeat an existing or anticipated family law claim may be set aside by virtue of Section 106B of the *Family Law Act*. Given the reasoning and decision in the High Court for *Spry*, the Court focused on the 1983 deed executed by the Husband. It could not have possibly been in anticipation of a family law claim, bearing in mind that it was some 19 years prior to separation.

"The conclusion is that re-settlement of a trust to exclude a spouse is unlikely to be effective; even when the parties are not even contemplating separation," warned Mr Abdelshahied.



If you have an issue involving family law, please contact the **Michael Sing Lawyers Pty Ltd** family law team in Brisbane on (07) 3229 6099 or the Gold Coast on (07) 5597 8888 to arrange a consultation.

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