



NICHOLES

Family Lawyers

BINDING FINANCIAL AGREEMENTS AND THIRD PARTY CREDITORS

Parties to a marriage have been able to enter into Binding Financial Agreements ('BFA') since December 2000. The Family Law Act ('FLA') provides that BFAs may be entered into by parties contemplating marriage, during a marriage both before and after separation and after a divorce. The issue of parties entering into a BFA during a marriage prior to separation recently raised considerable media coverage following the Family Court of Australia's unreported decision in ASIC v Rich¹. This decision highlighted a loophole in the FLA which allowed the parties to enter into an agreement to defeat the claims of third party creditors. Following the Family Court decision the Commonwealth Government has amended the FLA to remove the loophole.

Background

Mr Rich was a joint managing director of One.Tel Limited until his resignation from that position on 17 May 2001. One.Tel Limited was placed into administration on 29 May 2001.

Two days later Mr Rich entered into a BFA . The parties were not contemplating separation at this time. Pursuant to the agreement Mr Rich transferred approximately \$5 million in assets to his wife. These assets include Mr Rich's interest in the family home at 2 Queens Avenue, Vaucluse. Mr Rich also agreed to pay \$1000 per week to his wife to enable her to meet the outgoings, expenses and maintenance of the matrimonial home, and for the provision of food and the expenses of their joint life together. In order to secure this payment Mr Rich agreed to a charge over his remaining share of the sale proceeds of "Craigend" at Darling Point. Mr Rich acknowledged that the furnishings of the home, including valuable artworks and a Porsche motor vehicle are the sole property of Mrs Rich.

The recitals to the agreement stated that Mr Rich's financial affairs had taken a significant turn for the worse and his financial future was under a cloud. The wife was concerned that her professional career, as a lawyer, and public company director may be significantly compromised as a result of the adverse change in the husband's circumstances. They further state that in the event the parties were to separate the wife would be entitled to a significant award by way of property settlement and maintenance.

The Decision

ASIC² commenced proceedings against Mr and Mrs Rich in the Family Court of Australia in August 2002 seeking an order setting aside the BFA. In their responses to the application commenced by ASIC in the Family Court, Mr and Mrs Rich each sought to have the application dismissed. Mr

¹ ASIC v Rich and Rich (15 October 2003) unreported decision of His Honour Justice O'Ryan, Family Court of Australia.

² See Press release issued by ASIC dated 4 November 2003.

Rich contended that the Family Court did not have jurisdiction to hear ASIC's application.

On 15 October 2003, Justice O'Ryan held that the Family Court did not have jurisdiction to make the orders sought by ASIC. The primary reason was that the definition of "matrimonial cause" did not authorise the Court to consider the issue on behalf of a third party creditor independent of existing proceedings before the Court. In other words, because neither Mr nor Mrs Rich had proceedings on foot before the Court ASIC had no standing to file an application in respect of the agreement.

In his judgment Justice O'Ryan said: *"In my view ... there is prima facie evidence that the husband and wife entered into the agreement in order to reduce the extent and value of the husband's assets. ... Prime facie the evidence supports the contention by Senior Counsel for ASIC that the agreement was entered into because of a concern about claims on the husband's property by third parties as a result of the collapse of One.Tel Limited. It was therefore entered into to defeat the interests of third parties."*

Justice O'Ryan was critical of the legal reasons provided in the recitals for the transfer of assets to Mrs Rich. He noted that the effect of the agreement was to increase the wife's total assets from approximately \$13,000,000 to \$16,500,000 and to decrease the husband's total net assets from approximately \$9,455,000 to approximately \$3,900,000. In effect the husband was left with approximately 17.3% of the total assets. He stated *"Prior to the agreement the wife had assets of a greater value than the value of the husband's assets and it is for this, and other reasons, that I find the legal advice recited in the agreement incredulous"*.

Reforms to the FLA

The Government has since legislated to remove this loophole from the FLA. The definition of 'matrimonial cause' now includes third party proceedings to set aside a BFA. A third party is defined as including a creditor or government body acting in the interests of a creditor. The definition of creditor includes a person who could reasonably be foreseen by the court as being reasonably likely to become a creditor of either of the parties to the BFA.

A BFA may be set aside if either party entered into the agreement for the purpose of, or including the purposes of defrauding or defeating a creditor or creditors of the party, or with reckless disregard of the interests of a creditor or creditors of the party.

Care must be taken in entering into a BFA that it does not have the actual or anticipated effect of defrauding or defeating a creditor of either party to the agreement.

Contact Points:

Sally Nicholes – Partner

Family Law

Phone: 03 96704122

sally@nicholeslaw.com.au

Georgette Antonas – Solicitor

Family Law

Phone: 03 9205 2121

georgette_antonas@middletons.com.au