

BANKRUPTCY AND THE FAMILY HOME: THE IMPACT OF RECENT DEVELOPMENTS

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This article explores the effect of recent legal developments on the division of the family home in the context of bankruptcy of a spouse or de facto partner. While the traditional approach to division has been to determine the bankrupt's beneficial interest in the home (which vests in the trustee in bankruptcy), amendments to the Family Law Act 1975 (Cth) ('FLA') in 2005 now give family law courts jurisdiction to determine this issue, where there are FLA property proceedings on foot, using a structured statutory discretion under s 79 of the FLA. The authors examine the possible approaches that are now open to courts following these amendments. They argue that decisions of courts exercising both FLA and traditional bankruptcy jurisdiction suggest confusion about the appropriate principles to apply and that this has produced uncertain and sometimes questionable case outcomes. The authors call for further legislative reform that achieves greater clarity of principle and leads to the achievement of more just and equitable outcomes.

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I THE ISSUE

In Australia, the owner-occupied home remains something of a cultural icon — the ‘Great Australian Dream’ — having ongoing psychological and emotional, as well as financial, significance.¹ Home ownership, while increasingly difficult to achieve, ‘is the most common and most desired form of housing in Australia’.² The family home is the asset most commonly divided on spousal and de facto partner relationship breakdown,³ and more broadly, its fate is likely to be an issue of crucial importance when financial adversity strikes.

In this article, we explore the issue of how the family home is divided when a spouse (used throughout to include a de facto partner) becomes bankrupt with unsecured liabilities that are at least partly paid through sale or buy-out by the non-bankrupt spouse of the bankrupt spouse’s interest in the family home.⁴ The Federal Court of Australia (‘Federal Court’) and, from

¹ Shelley Mallett, ‘Understanding Home: A Critical Review of the Literature’ (2004) 52 *Sociological Review* 62, 66, 84.

² Australian Association of Social Workers, *Position Statement on Housing Affordability* (Australian Association of Social Workers, 2015) 3.

³ Lixia Qu et al, *Post-Separation Parenting, Property and Relationship Dynamics after Five Years*, (Commissioned Report, Australian Institute of Family Studies, 2014) 93–4. Among the 7439 separated parents surveyed in 2013 by the Australian Institute of Family Studies, ‘[t]he most common type of asset [described as having been divided after separation] was the family home (62 per cent), followed by cash savings (33 per cent), father’s superannuation (30 per cent) and mother’s superannuation (27 per cent). A minority of parents reported investment properties (14 per cent), other investments such as shares (15 per cent) and businesses (10 per cent)’: at 94.

⁴ While our focus is on bankruptcy, we also discuss the broader *Family Law Act 1975* (Cth) (‘*FLA*’) position on unsecured debts, which forms an integral part of family property law. We

2000, the Federal Circuit (previously Magistrates) Court of Australia ('Federal Circuit Court') (collectively referred to in this article as 'generalist federal courts') have traditionally had jurisdiction in disputes involving beneficial ownership of the family home in a bankruptcy context.⁵ But following amendments to the *Family Law Act 1975* (Cth) ('FLA') in 2005,⁶ it is now the Family Court of Australia ('Family Court'), the Family Court of Western Australia ('Family Court of WA') and the Federal Circuit Court (collectively referred to in this article as the 'family law courts' when exercising *FLA* jurisdiction, which includes altering the interests in the property⁷ of parties to a marriage or a de facto relationship) that effectively have jurisdiction where a party to *FLA* property proceedings is or becomes bankrupt.⁸ The jurisdiction of the Family Court and the Federal Circuit Court was further extended from 1 March 2009 (with the exception of Western Australia), to include financial disputes on breakdown of de facto relationships,⁹ adding to its pre-existing jurisdiction regarding financial disputes arising out of marital relationships.¹⁰

In our research on the fate of the family home in the context of bankruptcy of a spouse, we noticed that since 2010 there have not been many substantive contested cases dealing with bankruptcy and the family home that have gone to final judgment, whether in the family law courts or generalist federal courts (which continue to retain jurisdiction when there are no *FLA* proceedings on foot). Prior to 2010 and after the passage of the *Bankruptcy and Family Law Legislation Amendment Act 2005* (Cth) ('2005 Bankruptcy Amendments'), the high watermark in terms of case law activity in the Full Court of the Family

leave to one side the enforcement of *FLA* financial agreements in this context, but for a recent example see *Grainger v Bloomfield* [2015] FamCAFC 221 (18 November 2015).

⁵ Since 1988, the Family Court has had additional jurisdiction in (among other things) bankruptcy matters transferred to it by the Federal Court with the consent of the parties: *Family Court of Australia (Additional Jurisdiction and Exercise of Powers) Act 1988* (Cth) pt V.

⁶ *Bankruptcy and Family Law Legislation Amendment Act 2005* (Cth) sch 5 ('2005 Bankruptcy Amendments'), supplemented by the *Family Law Amendment Act 2005* (Cth) ('2005 Family Law Amendments').

⁷ 'Property' is a term without straightforward definition in family law or under the general law; in both contexts, it is not a word of fixed meaning. Notably, however, the definition of 'property' has been broader in family law compared to the general law: see *Kennon v Spry* (2008) 238 CLR 366, 387 [54], 390–1 [64] (French CJ).

⁸ See *FLA* ss 75(2)(ha), 79(1)(b), 79(10)–(10A), 79(11)–(16); *Bankruptcy Act 1966* (Cth) s 35.

⁹ *FLA* pt VIIIAB.

¹⁰ *Ibid* pt VIII.

Court was two cases decided in 2009 by the differently constituted benches of the Court, and adopting divergent approaches: *Trustee of the Property of Lemnos v Lemnos* ('*Lemnos*')¹¹ and *Federal Commissioner of Taxation v Worsnop* ('*Worsnop*').¹² In this period, we noticed that the volume of decided cases dealing with this issue in federal courts exercising jurisdiction under the *Bankruptcy Act 1966* (Cth) continued much as it had before, until slowing down in 2010 and thereafter.¹³

We sought to determine specific and dominant trends, outcomes and approaches to this issue by courts post-*Worsnop*¹⁴ and *Lemnos*.¹⁵ In the course of trying to do so, we also became interested in *why* there were not more cases being decided by the family law courts, given the presence of the 2005 *Bankruptcy Amendments* which we had thought would be likely to lead to more rather than fewer cases, at least in the family law courts. Are there procedural, doctrinal, institutional or strategic reasons behind trustees' (as representatives of unsecured creditors) or non-bankrupt spouses' reasons for not going ahead with litigation? Does it have something to do with the family law courts now having jurisdiction in some of these cases, and with trustee perceptions of how those courts would approach and decide cases (including the deterrent effect of family law cases where judges have been critical of the amount of fees claimed by trustees)¹⁶ and/or uncertainty generated by the amendments themselves,¹⁷ or more specifically by *Lemnos*¹⁸ and *Worsnop*?¹⁹

¹¹ (2009) 41 Fam LR 120 (Coleman, Thackray and Ryan JJ).

¹² (2009) 40 Fam LR 552 (Bryant CJ, Warnick and Cronin JJ).

¹³ See, eg, Lisa Sarmas, 'Trusts, Third Parties and the Family Home: Six Years since *Cummins* and Confusion Still Reigns' (2012) 36 *Melbourne University Law Review* 216, 237–43. See also below Part III(B). On the cases pre-2010 see Alison Umbers, 'Issues for Trustees in Bankruptcy in Proceedings under s 79 of the *Family Law Act*: 10 Years after *BFLAA*' (Paper presented at the Insolvency Law and Family Law Practice Groups, Monash University Law Chambers, Melbourne, 5 September 2014).

¹⁴ (2009) 40 Fam LR 552.

¹⁵ (2009) 41 Fam LR 120.

¹⁶ See, eg, *West v West* (2007) 38 Fam LR 431, 444–7 [65]–[77] (O'Sullivan FM).

¹⁷ See Umbers, above n 13, 15 [65].

¹⁸ (2009) 41 Fam LR 120.

¹⁹ (2009) 40 Fam LR 552. It may be that settling for less in the midst of such uncertainty is preferable to the risk involved in setting a precedent that may ultimately work against the interests of trustees in the long run. On this issue see, eg, Robert H Mnookin and Lewis Kornhauser, 'Bargaining in the Shadow of the Law: The Case of Divorce' (1979) 88 *Yale Law Journal* 950.

Or, perhaps the *2005 Bankruptcy Amendments* struck the right balance between the interests of trustees and non-bankrupt spouses, thereby promoting settlement of these matters rather than litigation? Perhaps the early cases represent a ‘blip’ effect; a testing of the new provisions? We know that the decline in litigation was not due to a lack of bankruptcies — which have declined since 2010 but remain significant in number (17 202 in 2015–16 compared to 22 163 in 2011–12, as recorded by the Australian Financial Security Authority).²⁰ In terms of the paucity of cases decided by generalist federal courts post-2010, it is likely that the slowdown in the case law would at least be partly due to the fact that cases involving the trustee’s claim to an interest in the family home which occurred in a relationship breakdown context and which would have been heard by them before the *2005 Bankruptcy Amendments* are now being heard by family law courts exercising *FLA* jurisdiction. However, the apparent rarity of cases in the family law courts is more difficult to explain.²¹

We also wondered what sorts of settlements were being reached between trustees and non-bankrupt spouses, in cases where there is no adjudicated outcome. Perhaps the goals of the *2005 Bankruptcy Amendments* — in essence, to resolve uncertainty and achieve a better balancing of interests between unsecured creditors and non-bankrupt parties — are being achieved?

II THE 2005 BANKRUPTCY AMENDMENTS

A *The Amendments and their Legislative Intention*

The *2005 Bankruptcy Amendments* have particular significance for non-bankrupt spouses and the trustee in bankruptcy in circumstances where there are *FLA* property proceedings on foot.

²⁰ Australian Financial Security Authority, *Annual Statistics* <<https://www.afsa.gov.au/resources/statistics/provisional-bankruptcy-and-personal-insolvency-statistics/annual-statistics/annual-statistics>>.

²¹ It is to be noted that the *Bankruptcy Legislation Amendment Act 2010* (Cth) sch 4 pt 1 increased the minimum debt to support a Bankruptcy Notice and Creditor’s Petition from \$2000 to \$5000. It is difficult to tell whether this change may have contributed to the slight decrease in the number of bankruptcies; however, as noted in the text above, despite the slight decline, the overall number of bankruptcies is still considerable and it is unlikely that the decline is a significant factor contributing to the rarity of cases.

The legislative intention in enacting the reforms was to improve the interaction between bankruptcy law and family law, as part of the federal government's response to the recommendations of the Joint Taskforce Report on the Use of Bankruptcy and Family Law Schemes to Avoid Payment of Tax.²² Problems in this area were longstanding.²³ In 1992, the Attorney-General's Family Law Council had described the non-interaction of bankruptcy and family law as follows:

It is well recognised that bankruptcy and family law conflict in such a way that when both systems apply simultaneously to a given situation the claims of the non-bankrupt spouse and family and that of the bankrupt's unsecured creditors are in competition. To date that conflict has remained largely unresolved because each piece of legislation, and the policy behind the legislation, favours or gives some sort of protection to the rights of the parties to whom that legislation relates without due regard to the needs and rights of others.²⁴

Consistent with this, the federal government sought to address 'inconsistencies between family law and bankruptcy law which create uncertainty for all involved and can cause hardship for either or both creditors and non-bankrupt spouses.'²⁵ The Revised Explanatory Memorandum to the *2005 Bankruptcy Amendments* notes that the amendments seek to clarify 'the rights of the bankruptcy trustee and the non-bankrupt spouse ... [by enabling] concurrent bankruptcy and family law proceedings to be brought together to ensure all the issues are dealt with at the same time.'²⁶ The Memorandum further explains that:

From a bankruptcy perspective, trustees can find themselves in an uncertain position when having to resolve or reconcile competing claims ... The special interest of the non-bankrupt spouse in the marital property created through

²² Supplementary Explanatory Memorandum, Family Law Amendment Bill 2005 (Cth) 2.

²³ See generally Jacqueline Campbell, 'Separate Lives but Joint Debts: The Implications from a Family Lawyer's Perspective of the Interaction between the *Bankruptcy Act* and the *Family Law Act*' (1996) 10 *Australian Journal of Family Law* 198.

²⁴ Family Law Council, 'The Interaction of Bankruptcy and Family Law' (Report to the Minister for Justice, Family Law Council, June 1992) [1.02].

²⁵ Revised Explanatory Memorandum, Bankruptcy and Family Law Legislation Amendment Bill 2005 (Cth) 2 [10]. See also Campbell, above n 23.

²⁶ Revised Explanatory Memorandum, Bankruptcy and Family Law Legislation Amendment Bill 2005 (Cth) 2 [14].

both financial and non-financial contributions, which may be recognised by the Family Court in exercising its discretion to alter property interests, is not expressly recognised under the *Bankruptcy Act* ... Different outcomes result depending upon the order in which events occur (those events including separation, bankruptcy and distribution of property by the trustee in bankruptcy).²⁷

As we discuss below, in bankruptcy matters dealt with by generalist federal courts (where there are no *FLA* property proceedings on foot), the effect of applying the *Bankruptcy Act 1966* (Cth) provisions is that the trustee will be allocated the bankrupt spouse's share of the proprietary interest in the family home using relevant property and trusts principles.²⁸ Prior to the *2005 Bankruptcy Amendments*, when a bankruptcy occurred after a *FLA* property order was made, the non-bankrupt spouse would be subject to the doctrine of relation back, with the effect that (depending on the time period that had elapsed between the bankruptcy and the making of the *FLA* property order) the *FLA* property order is treated as not having been made and any interest in property of the bankrupt that may have been altered in favour of the non-bankrupt spouse is clawed back.²⁹ Where bankruptcy occurred before *FLA* proceedings, the practical effect would be that, in the court's view, there was no property of the bankrupt spouse for orders in favour of the non-bankrupt spouse to attach to.³⁰ When the bankrupt's property had vested in the trustee, 'a non-bankrupt spouse could only hope to recover a share in that property in the event of a surplus after the creditors had been paid.'³¹

²⁷ *Ibid* 2 [11]–[14].

²⁸ This approach has not been affected by the *2005 Bankruptcy Amendments* as the *Amendments* apply to proceedings before the family law courts only. It is to be noted that property that the bankrupt holds on trust is not 'property divisible among creditors': *Bankruptcy Act 1966* (Cth) s 116(2)(a). On the relevant property and trusts principles used in non-family law courts see below Part III(B).

²⁹ *Bankruptcy Act 1966* (Cth) s 122(1). See also Kerry Wells, 'Third Party Creditors and the Non-Debtor Spouse: New Developments' (1996) 10 *Australian Journal of Family Law* 127, 127–9.

³⁰ *Re Chemaïsse v Federal Commissioner of Taxation* [1990] 13 Fam LR 724, 732–4. See also Anthony Dickey, 'A Question of Priorities: Wives or Unsecured Creditors?' (1992) 6 *Australian Journal of Family Law* 229; Wells, above n 29; Patrick Parkinson, 'Property Rights and Third Party Creditors — The Scope and Limitations of Equitable Doctrines' (1997) 11 *Australian Journal of Family Law* 100; Deena Shiff and Peter Waters, 'Bankruptcy and Family Law: First Come, First Served?' (1985) 8 *University of New South Wales Law Journal* 40, 49.

³¹ Umbers, above n 13, 2 [4].

Since the passage of the *2005 Bankruptcy Amendments*, the *FLA* makes clear that the trustee in bankruptcy of a ‘party’ to *FLA* property proceedings³² (or a creditor of a non-bankrupt party to *FLA* property proceedings)³³ may become a party to those proceedings, thereby providing a process enabling concurrent debt, bankruptcy and family law issues to be considered at the same time by the family law courts. As the Federal Circuit Court always had jurisdiction and could hear cases under the *FLA* and the *Bankruptcy Act 1966* (Cth) together, and the Family Court had some additional bankruptcy jurisdiction, the real change was in the wording of s 79. Specifically, s 79(11) provides that ‘the court must join the bankruptcy trustee as a party to the proceedings’ if:

- (b) either ...
 - (i) when the application was made, the party was a bankrupt;
 - (ii) after the application was made but before it is finally determined, the party became a bankrupt; and
- (c) the bankruptcy trustee applies to the court to be joined as a party to the proceedings; and
- (d) the court is satisfied that the interests of the bankrupt’s creditors may be affected by the making of an order under this section in the proceedings ...

Significantly, the *2005 Bankruptcy Amendments* also give the family law courts jurisdiction to alter interests in property of a party that has vested in the trustee in bankruptcy.³⁴ Under s 79(1) (and s 90SM(1) for de facto partners) the court may make property orders as it ‘considers appropriate’:

- (b) in the case of proceedings with respect to the vested bankruptcy property in relation to a bankrupt party to the marriage—altering the interests of the bankruptcy trustee in the vested bankruptcy property;

³² *FLA* s 79(11).

³³ *Ibid* s 79(10). Section 79(10A) of the *FLA* indicates that a creditor with debts provable in the bankruptcy is not entitled to become a party to proceedings to the extent to which the debt is a provable debt.

³⁴ *FLA* ss 79(10), (11). See also Denis Farrar, ‘Bankruptcy and Family Law’ (Paper presented at the 36th Australian Legal Convention of the Law Council of Australia, Perth, 17–19 September 2009).

including:

- (c) an order for a settlement of property in substitution for any interest in the property; and
- (d) an order requiring:
 - (i) either or both of the parties to the marriage; or
 - (ii) the relevant bankruptcy trustee (if any);
 to make, for the benefit of either or both of the parties to the marriage or a child of the marriage, such settlement or transfer of property as the court determines.

It is interesting to note that the drafting of s 79(1)(d) indicates that in such cases, *FLA* property orders can be made for the *benefit* of the *parties to the marriage or a child* of the marriage. Section 79(1)(d) does not mention the making of an order for the benefit of the trustee.

Also relevant is the definition of ‘matrimonial cause’ in s 4(1), which stipulates the jurisdiction of courts deciding cases under the *FLA*, and refers to proceedings between:

- (i) a party to a marriage; and
- (ii) the bankruptcy trustee of a bankrupt party to the marriage; with respect to any vested bankruptcy property in relation to the bankrupt party ...

As a result of the terms of s 79(1)(b) and the definition of ‘matrimonial cause’, in our view the court has power to alter interests in vested bankruptcy property in *favour* of the non-bankrupt spouse but *not* in favour of the trustee.³⁵ In other words, the power to alter interests under ss 79 or 90SM of the *FLA* does not extend to a power to enlarge the trustee’s interest.³⁶ The

³⁵ The question was left open by the majority in *Lemnos* (2009) 41 Fam LR 120, 165–6 [247] (Thackray and Ryan JJ).

³⁶ While it is arguable that the court may alter interests in property of the trustee or non-bankrupt spouse in favour of the *bankrupt* (as the bankrupt is ‘a party to the marriage’), ‘should an order be made against the non-bankrupt spouse or the Trustee in Bankruptcy for property to be transferred to, or settled upon the bankrupt spouse before he is discharged from his bankruptcy, any such property immediately becomes “after-acquired property” and would vest in the trustee as a result: *Redmond v Stolz* [No 3] [2015] FamCA 692 (21 August 2015) [172]–[175] (Forrest J). Given that the property would vest in the trustee, it is arguable that such an order would not be for the *benefit* of the bankrupt (unless it gets the bankrupt out of bankruptcy) and should not therefore be made. Doubt also surrounds the question of

competition is for priority in relation to the insolvent spouse's pre-bankruptcy property between the trustee and the non-bankrupt spouse.

Given this, the identification of the non-bankrupt spouse's pre-bankruptcy legal and equitable interests in property is logically a prerequisite in all cases involving bankruptcy including those that fall within the jurisdiction of the *FLA*, in order to ensure that the trustee's claim is confined to the bankrupt's legal and equitable interest at the point of bankruptcy. In contrast, our analysis of cases in Part III indicates that findings as to the spouses' respective proprietary interests are commonly not being made by family law courts exercising jurisdiction under s 79.

In addition, the *2005 Bankruptcy Amendments* inserted s 75(2)(ha) into the *FLA*, adding to the range of factors to be considered in *FLA* property proceedings: 'the effect of any proposed order on the ability of a creditor of a party to recover the creditor's debt, so far as that effect is relevant'. Our analysis of cases in Part III makes clear that 'creditor' in s 75(2)(ha) has been understood by courts to include the trustee, and that courts have at times taken into account the interests of the trustee under this provision by withholding or reducing an adjustment they would otherwise have made in favour of a non-bankrupt spouse. Some doubt, however, surrounds the interpretation of this provision and whether 'creditor' in s 75(2)(ha) includes the trustee.³⁷ If it does not, then it would seem that in at least two ways (namely, the application of s 75(2)(ha) and the non-identification of the parties' existing legal and equitable interests in property), courts may be engaging in an interpretation of the *2005 Bankruptcy Amendments* that does not accord with the legislation itself and which is more likely to operate in the interests of trustees than non-bankrupt spouses.

A further significant development occurred in 2012, with the High Court's decision in *Stanford v Stanford* ('*Stanford*').³⁸ In *Stanford*, the High Court majority emphasised the legislative requirement that the court must not make a *FLA* order altering existing legal and equitable interests in property 'unless it is satisfied that, in all the circumstances, it is just and equitable to make the

whether the bankrupt would have standing to seek orders in such circumstances: see *Trent v Rowley* [2014] FamCA 447 (25 June 2014).

³⁷ Television Education Network, 'Bankruptcy and Insolvency in Family Law Matters: The Tricky Bits Explained', *Webinar*, 23 February 2016, 33 (Jacky Campbell).

³⁸ (2012) 247 CLR 108.

order' under s 79(2)³⁹ and the requirement of a principled exercise of discretion under s 79 without a predetermined view as to outcome (that is, there is no assumption that existing interests in property should be altered).⁴⁰

These aspects of *Stanford* have encouraged varying approaches by differently constituted benches of the Full Court of the Family Court in relation to specific *FLA* property issues,⁴¹ but so far the Court has not considered *Stanford's* impact in the bankruptcy context. While it has been suggested that *Stanford* has the capacity to strengthen the position of trustees,⁴² in our view, the emphasis in *Stanford* on the requirement that the court first identify the spouses' existing legal and equitable interests in property may in fact have a protective effect for the non-bankrupt spouse. The identification of such interests (rather than just relying on bare legal title as the starting point) brings into focus and makes clear whether particular orders altering those interests under s 79 would amount to an enlargement of the trustee's interest (contrary to what is permissible under s 79(1)(b) and the s 4 definition of 'matrimonial cause') and to an encroachment on the proprietary interests of the non-bankrupt spouse. However, as we discuss below, following the decision in *Stanford*,⁴³ family law courts are not commonly first identifying the parties' respective legal and equitable interests in property when making property orders in the bankruptcy context.

³⁹ Ibid 120 [37] (French CJ, Hayne, Kiefel and Bell JJ).

⁴⁰ Ibid 121 [40].

⁴¹ For example, in relation to, respectively, add backs in *Bevan v Bevan* (2013) 279 FLR 1 and the abandonment of the doctrine of special skill in *Hoffman v Hoffman* (2014) 1 Fam LR 568; but cf *Vass v Vass* (2015) 53 Fam LR 373. So far, however, the Court has not considered *Stanford's* impact in the bankruptcy context. See also Belinda Fehlberg et al, *Australian Family Law: The Contemporary Context* (Oxford University Press, 2nd ed, 2015) ch 13.

⁴² Jacqueline Campbell and Evelyn Young, 'Stanford, Bankruptcy and Unsecured Liabilities — Options and Opportunities' (2015) 24(2) *Australian Family Lawyer* 31, 31–2, 48–9; Paul Glass, 'Family Law and Bankruptcy: Is the Marriage Any Happier Post-*Stanford*?' (Paper presented at the Insolvency Law and Family Law Practice Groups, Monash University Law Chambers, Melbourne, 5 September 2014) 7–8.

⁴³ (2012) 247 CLR 108.

B A Range of Possible Approaches Available to Family Law Courts
after the 2005 Bankruptcy Amendments

The *procedural* effect of the 2005 *Bankruptcy Amendments* is to make clear that the family law courts have jurisdiction to alter property interests when there are concurrent bankruptcy and family law property proceedings on foot. The amendments may, however, also involve a change in the *substantive* legal principles to be applied when the jurisdiction of family law courts is invoked in such matters. This is due to the fact that the non-bankrupt spouse now has a right to seek orders under s 79 against vested bankruptcy property, in addition to any other rights they had under the *Bankruptcy Act 1966* (Cth) or the general law.

When considering what order (if any) should be made under s 79(1) of the *FLA*, family law courts must be satisfied that it is ‘just and equitable’ to make *an* order and, if relevant, *the* order,⁴⁴ taking into account the usual s 79(4) factors including each spouse’s financial and non-financial contributions to their property,⁴⁵ and to the welfare of their family and a range of additional factors mainly directed at economic disparity between the parties,⁴⁶ but also including, as noted earlier, the effect of any proposed order on the ability of a creditor of a party to recover the creditor’s debt (s 75(2)(ha)).⁴⁷ As these *FLA* provisions clearly permit a consideration of factors that go beyond the existing proprietary interests of the parties, and s 75(2)(ha) is but one of a range of other considerations to be taken into account, the 2005 *Bankruptcy Amendments* signal a substantive change in the balance between the interests of non-bankrupt/non-debtor spouses and unsecured creditors, although the balance to be struck is not clear.

It is our contention that there is a range of possible approaches available to family law courts after the 2005 *Bankruptcy Amendments*, given that these provisions, which afford such courts a broad discretion, do not directly address or resolve the substantive question of the relative priority to be given to the competing interests of the trustee and the non-bankrupt spouse. The

⁴⁴ *FLA* s 79(2).

⁴⁵ *Ibid* ss 79(4)(a)–(b).

⁴⁶ *Ibid* ss 79(4)(c)–(g), 75(2) (by virtue of s 79(4)(e)).

⁴⁷ Note that the effect on the general application of s 79 on s 79(2) and its interpretation in *Stanford* (2012) 247 CLR 108 is considered below.

lacuna in the legislative provisions arguably leaves open a number of possible approaches including those discussed below.⁴⁸

1 'Section 79 Approach'

The court could first identify the spouses' pre-bankruptcy legal and equitable interests in property (consistent with the terms of s 79(1)(b) and the definition of 'matrimonial cause' in s 4 of the *FLA*, and with *Stanford*,⁴⁹ including their interests under relevant resulting and constructive trust principles). The court could then consider the factors under s 79 of the *FLA* (that is, the spouses' respective contributions and the additional considerations including under s 75(2), which has as its main focus the economic disparity between the spouses — but where bankruptcy has occurred, the court's concern will be the economic position of the non-bankrupt spouse). The court could *then* make an order (if any) altering the interests of the parties (the 'parties' being the

⁴⁸ Other possible approaches include that suggested by Justice Brereton, who argued in 2005 that, having decided what order would have been made but for the bankruptcy, the court should then treat it as if it were a provable debt in the bankruptcy, so that it abates *pro rata* with the liabilities that have been proven in the bankruptcy: Justice Paul L G Brereton, 'Recent Developments in Family Law: Bankruptcy, Third Parties and Other Matters' (Speech delivered at the NSW Young Lawyers Committee Meeting, Sydney, 21 September 2005) 5; Judge Grant T Riethmuller, 'Family Law and Bankruptcy: An Alternative Conceptualisation' (2014) 28 *Australian Journal of Family Law* 290, 290, in which Judge Riethmuller observed in relation to the approach advocated by Justice Brereton that '[w]hile a simple and elegant approach, it must be recognised that it does not result in a real consideration of the totality of [s 79], which was questionable at that time, and simply cannot be sustained following *Stanford*'. Judge Riethmuller argues in favour of an 'analogous with equity' approach, at 291:

That is, recognising that orders adjusting the property interests of an insolvent spouse in favour of a solvent spouse have the same prioritising effect (as between the solvent spouse and the unsecured creditors) as granting the solvent spouse a proprietary remedy. Once this effect is recognised, considerations analogous to those relevant in equity should be identified as being of particular relevance within the rubric of s 79 ...

See also Patrick Parkinson, 'Family Property Law and the Three Fundamental Propositions in *Stanford v Stanford*' (2013) 23(2) *Australian Family Lawyer* 4. Parkinson's analysis of *Stanford* similarly argues that 'there could be much benefit to the future development of family property law in contextualising the statutory jurisdiction within a broader jurisprudence concerning doctrinal rationales for the alteration of legal title or for the imposition of equitable obligations upon legal owners of property': at 10. Both Judge Riethmuller's and Parkinson's approaches are broadly consistent with our approach throughout the article, although s 79's genesis in equity's shortcomings in the area of matrimonial property law for economically vulnerable parties, particularly women, also makes us wary of the limits of equity's utility in this context: see below n 54.

⁴⁹ (2012) 247 CLR 108.

non-bankrupt spouse and the trustee). Such an order could only be made altering interests in favour of the non-bankrupt spouse, as in our view, the legislation does not permit an enlargement of the trustee's initial proprietary interest in what was the pre-bankruptcy property of the bankrupt. Under this approach, the proprietary interest of the non-bankrupt spouse and that spouse's allocation under s 79 is insulated from the trustee.

This approach, which focuses on what the non-bankrupt spouse would have received under s 79 regardless of the bankruptcy of their spouse, is consistent with the legislative positioning of the provisions implemented by the 2005 *Bankruptcy Amendments* as part of s 79 of the *FLA*,⁵⁰ which was originally introduced to overcome the shortcomings of the law of resulting and constructive trusts in property disputes between separating spouses.⁵¹ However, as the *FLA* provisions currently stand, it could be argued that this approach may not sufficiently take into account s 75(2)(ha), which directs the court to consider 'the effect of any proposed [property] order on the ability of a creditor of a party to recover [the debt owed to them]' (assuming, for the purposes of this discussion, that 'creditor' in s 75(2)(ha) includes the trustee and that therefore the interests of the trustee can in fact be considered here).⁵²

As discussed earlier, under the provisions as they currently stand, we do not think it is appropriate for a court to reduce the adjusted share of a non-bankrupt spouse under s 75(2)(ha) when making the s 79 assessment. However, this is not the approach that courts have so far taken in this context.⁵³ If we are wrong and the legislation *does* permit an adjustment in favour of the trustee under s 75(2)(ha), then the question becomes, in what circumstances should such an adjustment be made?

In determining when, if at all, the non-bankrupt spouse should be made to pay for any of the debts incurred by the bankrupt, it may be instructive to consider the approach taken by the Full Court of the Federal Court in

⁵⁰ In support of this interpretation see *Lemnos v Lemnos* (2007) 38 Fam LR 594, 603–4 [60] (Le Poer Trench J), quoting Tom Altobelli.

⁵¹ Our point here is that s 79 of the *FLA* was enacted to ensure that factors not sufficiently (or not at all) considered under the law of trusts (such as homemaker contributions and the economic disparity between the parties), would be considered under the *FLA*. See, eg, John Dewar, 'Contributions Outside Marriage' (Paper presented at the 10th National Family Law Conference, Melbourne, 17–20 March 2002). See also the detailed discussion in the judgment of Carmody J in *Moore v Moore* [2008] FamCA 32 (25 January 2008) [146]–[235].

⁵² For discussion, see above Part II(A).

⁵³ See below Part III(A).

Parsons v McBain ('*Parsons*')⁵⁴ to the question of whether a spouse's equitable interest in the matrimonial home under a constructive trust would be defeated by the trustee in bankruptcy. In that case, the Court said:

the interest may be defeated by, or may be made to defer to, later claims 'by conduct, by representations, by misstatements of a character which would operate and enure to forfeit and to take away the pre-existing equitable title ... something tangible and distinct having grave and strong effect to accomplish the purpose' ...⁵⁵

Examples might include a non-bankrupt spouse who knows and consents to her husband's non-payment of primary taxation (including penalties),⁵⁶ or who knows and consents to expenditure that leads to the bankruptcy (for example, agreeing to a child of the parties attending a private school, the fees for which are paid using the bankrupt spouse's credit card). The Court in *Parsons* also made the following important points:

The equitable interest will not be defeated merely because the legal title has passed to a trustee in bankruptcy, for he stands in the shoes of the bankrupt ... What is the position here? There is nothing in the conduct of [the non-bankrupt spouse], as regards her acquisition of her interest in the matrimonial home, or the manner in which she dealt with that interest, which could lead a court to deny her full beneficial entitlement to her. That is, [the non-bankrupt spouse has] done nothing that would cause a court to prefer the interests of unsecured creditors of the bankrupt estates of [the bankrupt spouse] ... over [her] own equitable interests. That being so, neither [ss] 120 nor 121 [of the *Bankruptcy Act 1966* (Cth)] can have application to the transfer by the bankrupt to his wife, of the legal interest in property in which the wife holds the beneficial interest.⁵⁷

⁵⁴ (2001) 109 FCR 120, 126. *Parsons* includes a helpful discussion of much of the extensive jurisprudence on trusts law relating to insolvency.

⁵⁵ *Ibid* 126 [16] (citations omitted).

⁵⁶ In this regard we would not make the distinction between primary taxation liabilities and penalties: *Johnson v Johnson* (1999) 26 Fam LR 475, 478 [20.4]–[20.7] (Ellis, Kay and Dessau JJ), cited in *Lemnos* (2009) 41 Fam LR 120, 165 [244] (Thackray and Ryan JJ).

⁵⁷ *Parsons* (2001) 109 FCR 120, 126 [16]–[17].

This approach, assuming that trustee's interests are relevant, is consistent with s 75(2)(ha) of the *FLA*. It is, we would argue, also principled;⁵⁸ there would appear to be no legitimate reason to distinguish between those factors that are relevant to deferring or defeating the non-bankrupt spouse's interest under a constructive trust and the legitimate considerations relevant to deferring or defeating a non-bankrupt spouse's interest based on relevant s 79 factors (including s 75(2)(ha)). It is an approach consistent with the view that there can be no justification in visiting liability on a person who has not chosen to take on a liability or to enjoy an alleged resulting benefit:

to equate the claims and needs of the bankrupt's family to the position of unsecured creditors is simply illogical. Unsecured creditors chose to become creditors, and they could have protected themselves against the consequences of being unsecured (eg through retention of title clauses, effective credit control and administration etc). It might be somewhat harder to convincingly assert that a bankrupt's child chose to be in a situation where they might lose the home they live in, and that they could somehow have protected themselves.⁵⁹

The interests of 'worthy' unsecured creditors who are unable to take security (such as taxpayers, judgment creditors and employees) are more appropriately addressed by other mechanisms such as tax avoidance reform, public compensation schemes and reform of bankruptcy and insolvency laws respectively.

2 'Non-Bankrupt Spouse Shares the Debt Approach'

On the basis of established *FLA* jurisprudence regarding the treatment of unsecured debts where there is no bankruptcy on foot, the court might first deduct all debts of the spouses from the property pool before the court considers what alteration, if any, to make under s 79 to the net pool. Under this approach, the interest of the non-bankrupt spouse is available to the unsecured creditors of the bankrupt.

This is basically the starting point adopted by family law courts in relation to unsecured debts outside the bankruptcy context since before the 2005

⁵⁸ See also Patrick Parkinson, 'Constitutional Law and the Limits of Discretion in Family Property Law' (2016) 44 *Federal Law Review* (forthcoming).

⁵⁹ *Lemnos v Lemnos* (2007) 38 Fam LR 594, 603-4 [60] (Le Poer Trench J), quoting Tom Altobelli.

Bankruptcy Amendments were enacted (applying *Re Marriage of Biltoft*)⁶⁰ and is an approach still evident in the case law. Its development has been accompanied by the elaboration of several ways of modifying the approach,⁶¹ including that the debtor should be seen as having wasted assets in the sense described in *Kowaliw v Kowaliw*.⁶²

In *Lemnos*⁶³ and *Worsnop*,⁶⁴ the trustee and the unsecured creditors respectively argued that the Court should not have made s 79 orders at all because the liabilities of the spouses exceeded their combined assets. The Court in *Lemnos* did not accept this argument, making it clear that after the 2005 *Bankruptcy Amendments*, vested bankruptcy property is to be treated as part of the assets available for division under s 79.⁶⁵ Questions do, however, continue to arise regarding the extent to which the general approach of deducting unsecured liabilities from the property pool continues to operate and to influence courts in *FLA* bankruptcy cases.⁶⁶

More broadly, while the starting point of deducting liabilities from assets reflects the accepted legal approach in the case of secured liabilities, it is an

⁶⁰ *Re Marriage of Biltoft* (1995) 19 Fam LR 82. See also Dickey, above n 30; Wells, above n 29, 128; Parkinson, 'Property Rights and Third Party Creditors', above n 30; Campbell, 'Separate Lives but Joint Debts', above n 23; Jacqueline Campbell, 'When Family Law Meets Bankruptcy' (Paper presented at the Law Institute of Victoria, Melbourne, 17 February 2015) 7–14.

⁶¹ Fehlberg et al, above n 41, 553–62.

⁶² (1981) FLC ¶91-092. Baker J said, at 76 644:

'As a statement of general principle, I am firmly of the view that financial losses incurred by parties or either of them in the course of a marriage whether such losses result from a joint or several liability, should be shared by them (although not necessarily equally) except in the following circumstances:

- (a) where one of the parties has embarked upon a course of conduct designed to reduce or minimise the effective value or worth of matrimonial assets, or
- (b) 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.'

This passage has received widespread support — for example, in *Lemnos* the appeal was allowed by the Full Court on the basis that the trial judge had wrongly applied the 'waste' principle. The Court considered that the husband's actions were not wasteful, but rather were designed to increase the matrimonial assets: (2009) 41 Fam LR 120, 144 [123]–[124] (Coleman J), 164 [243] (Thackray and Ryan JJ).

⁶³ (2009) 41 Fam LR 120.

⁶⁴ (2009) 40 Fam LR 552.

⁶⁵ (2009) 41 Fam LR 120, 138 [96] (Coleman J), 159 [202] (Thackray and Ryan JJ).

⁶⁶ See below Part III(A).

approach that is highly questionable in the case of unsecured debts. This is because it, in effect, gives priority to the interests of unsecured creditors over the interests of the non-debtor spouse, yet has no clear legislative basis in the *FLA* and is contrary to the position that would operate in property and trusts law.⁶⁷ In practical terms, the longstanding readiness of family law courts to adopt as a starting point the sharing of the burden of unsecured debts arguably suggests a 'partnership' view of marriage, yet the same starting point was not correspondingly evident over many years in relation to cases involving the division of very high assets.⁶⁸ In practical terms, the adoption of a starting point of deducting all liabilities from the asset pool may also be reflective of the family law courts' reluctance, at least in cases involving modest assets, to engage in detailed analysis that will extend the time and cost to parties for what might be thought to be negligible overall gain in outcomes. In our view, however, this is no reason for adopting the wrong starting point. This approach is also not consistent with the legislative framework of the *FLA*, which requires the interests of creditors to be considered *alongside* other s 79 factors, not in *priority* to them.⁶⁹

3 'Property and Trusts Approach'

The court could first identify the spouses' pre-bankruptcy legal and equitable interests in property, including their interests under relevant resulting and constructive trust principles. This is consistent with *Stanford*⁷⁰ and with the traditional bankruptcy and property law principle that it is only the *bankrupt's property* (whether legal or equitable) that can be claimed by the trustee in bankruptcy to satisfy the bankrupt's unsecured debts.⁷¹ The next step would be to consider whether there should be an alteration under s 79 of the *FLA* of

⁶⁷ Dickey, above n 30.

⁶⁸ In the context of such cases, the doctrine of special skills (which involved treating high earning, entrepreneurial husbands as having made a more valuable contribution to the marriage than their homemaker wives, despite the significant contributions and sacrifices made by them over the course of the marriage to support the husband's activities) evolved in earnest after *Re Marriage of Ferraro* (1992) 16 Fam LR 1 has been applied, expanded upon and not applied by differently constituted Full Courts since then, and post-*Stanford* was rejected by the Full Court in *Hoffman v Hoffman* (2014) 51 Fam LR 568 as an approach that pre-disposed the outcome.

⁶⁹ See *FLA* s 75(2)(ha).

⁷⁰ (2012) 247 CLR 108.

⁷¹ See especially *Parsons* (2001) 109 FCR 120.

existing proprietary interests in favour of the non-bankrupt spouse. An adjustment in favour of the trustee would not be permissible as it would be inconsistent with traditional bankruptcy and property law principles (just noted) as well as the terms of s 79(1)(b) and the definition of ‘matrimonial cause’ in s 4 of the *FLA*, as discussed above. As this approach focuses on existing proprietary interests and the satisfaction of the trustee’s claim under traditional bankruptcy principles, it is likely that the court would simply declare and confirm the parties’ existing proprietary interests, and less likely that it would then go on to make a s 79 adjustment to those interests. This is also consistent with the tenor of the High Court’s decision in *Stanford*, where the Court emphasised both the importance of first identifying the proprietary interests of the spouses and then only making an adjustment to those interests if it is ‘just and equitable’ to do so under s 79(2) of the *FLA*.⁷² In the context of the bankruptcy of one of the spouses, it is likely that the court would consider the context of unpaid debts of the bankrupt as a factor militating against the making of an adjustment that would reduce the assets allocated to the trustee to satisfy those debts.

The key difference between this and our first approach outlined in Part II(B)(1) (the ‘Section 79 Approach’) is really one of emphasis. Under this approach the court is more likely to confirm the non-bankrupt spouse’s proprietary interests without making an adjustment in their favour under s 79. Under our first approach, the court focuses on what the non-bankrupt spouse would have received under s 79 regardless of the bankruptcy (or not) of their spouse, and is therefore more likely to make an adjustment under s 79 in favour of the non-bankrupt spouse. What both approaches share is the assumption that, at the very least (except possibly in the case of ‘wrongdoing’, mentioned earlier), the non-bankrupt spouse’s property is insulated from the debts of the bankrupt, in accordance with the legislation and traditional bankruptcy and property law principles.

4 ‘Combination Exercising Broad Discretion Approach’

The court could combine one or more of the above approaches, and use a broad discretion depending on specific circumstances.

This approach is unpredictable in its operation and outcomes, due to the use of a broad discretion in dealing with the interests of the trustee and

⁷² (2012) 247 CLR 108, 120–2 [35]–[42] (French CJ, Hayne, Kiefel and Bell JJ).

unsecured creditors, as well as with other potentially relevant factors. It involves the combination of a broad discretion with an emphasis on one or a number of the approaches identified above. For example, the court may decide that it will make a s 79 adjustment on the basis of the ‘contribution’ of the non-bankrupt spouse to the parties’ property and to the welfare of their family from the vested bankruptcy property, but will not make any further adjustment that would, but for those debts, have been made under s 75(2) to address economic disparity between the spouses.⁷³ At least some applications of this approach are arguably in keeping with the tenor of the High Court’s approach in *Stanford*, which underlined: (1) the breadth of matters relevant to the court satisfying itself that it is ‘just and equitable’ to make an order under s 79;⁷⁴ and (2) that if discretion is exercised under s 79 it must be ‘principled’ in accordance with s 79, rather than assuming any particular outcome.⁷⁵

Obviously, the method chosen by the court will affect (sometimes dramatically) the respective outcomes for the non-bankrupt spouse and the unsecured creditors. In the next section of the article, we examine the case law thus far.

III THE CASE LAW

In this Part of the article we look at the case law since *Worsnop*⁷⁶ and *Lemnos*⁷⁷ were decided in 2009, and examine the substantive outcomes of cases involving the trustee and non-bankrupt spouses.⁷⁸ In balancing the rights of the trustee and the non-bankrupt spouse, do family law courts exercising *FLA* jurisdiction apply different criteria to that of generalist federal courts? What

⁷³ *FLA* s 75(2).

⁷⁴ (2012) 247 CLR 108, 120–2 [35]–[42] (French CJ, Hayne, Kiefel and Bell JJ).

⁷⁵ *Ibid* 122 [41].

⁷⁶ (2009) 40 Fam LR 552.

⁷⁷ (2009) 41 Fam LR 120.

⁷⁸ For this part of the article, we accessed the Family Court, Full Court of the Family Court, Federal Circuit Court and Federal Magistrates Court of Australia (‘Federal Magistrates Court’) Family Law sections of AustLII, using the search terms ‘Lemnos’, ‘Worsnop’, ‘bankrupt’, ‘bankruptcy’ and ‘bankruptcy and family and home’. We also accessed the Federal Court, Full Court of the Federal Court, Federal Circuit Court and Federal Magistrates Court sections of the AustLII website, using the search terms ‘Trustees of the Property of Cummins’ and ‘Calverley v Green’. The last date for all searches was 16 December 2015.

criteria do the latter apply? Do the approaches adopted by courts relate to any of the four approaches we have suggested?

In summary, we have found it very difficult to answer these questions due to a lack of coherent case law on the issue. As we now discuss, differently constituted benches of the Full Court of the Family Court have taken divergent approaches in *Lemnos*⁷⁹ and *Worsnop*.⁸⁰ Since those decisions, case law in the family law courts appears to reflect the fourth approach just outlined (that is, the ‘Combination Exercising Broad Discretion Approach’), although there are also elements of the second approach (‘Non-Bankrupt Spouse Shares the Debt Approach’). The inconsistency between *Worsnop* and *Lemnos* remains unresolved, and ultimately both the approach to be taken and the likely outcomes in this area remain unclear.⁸¹

As is to be expected, generalist federal courts⁸² (which retain jurisdiction when there are no family law property proceedings on foot, and which do not have s 79 of the *FLA* available to them), tend to adopt the third approach (‘Property and Trusts Approach’) — but without any possibility at all of a s 79 adjustment.⁸³ However, as we will discuss, the trusts principles applied in this approach are far from consistent and have become particularly confused since the High Court’s decision in *Trustees of the Property of Cummins v Cummins* (‘*Cummins*’).⁸⁴

A FLA Cases

1 *Worsnop and Lemnos*

As already noted, the only two (substantive) cases decided by the Full Court of the Family Court under the *2005 Bankruptcy Amendments* are *Worsnop*⁸⁵

⁷⁹ (2009) 41 Fam LR 120.

⁸⁰ (2009) 40 Fam LR 552.

⁸¹ See Riethmuller, above n 48.

⁸² And some state courts (if called upon to determine the beneficial interests of spouses when one of them is bankrupt in matters pertaining to state jurisdiction, for example, when a caveat or injunction against the family home is the subject of the proceedings).

⁸³ See below Part III(B).

⁸⁴ (2006) 227 CLR 278.

⁸⁵ (2009) 40 Fam LR 552.

and *Lemnos*,⁸⁶ both decided in 2009. Key differences between the cases were that in *Lemnos*,⁸⁷ the husband was bankrupt and the legal interest in the family home had vested in the trustee as it had been purchased by the husband in his sole name, while in *Worsnop*,⁸⁸ the husband was not bankrupt and the family home was in the name of the wife, the husband having transferred his 'half share' to her about five years before the parties separated. In both cases there was no discussion of equitable ownership; rather, it appears to have been assumed in *Lemnos* that the whole of the property had vested in the trustee,⁸⁹ and assumed in *Worsnop* that the husband had a half share in the home, apparently on the basis of his joint legal ownership prior to the transfer of title into the wife's name and evidence at trial suggesting this was done to protect the property from claims of potential creditors.⁹⁰ Both cases involved a competition between the Australian Taxation Office ('ATO') (pursuing money owed by the husband) and a wife following marriage breakdown, with the key asset at stake being the family home. In both cases, liability had arisen due to the husband's conduct regarding completion of his taxation returns and the wife had no awareness, nor reason to be aware, of the husband's conduct. The key significance of these cases is that while involving similar facts, they are irreconcilable in both their reasoning and outcomes, and so read together offer little guidance and would therefore seem likely to discourage litigation.

Worsnop did not involve a bankruptcy, but it did involve applying s 79 of the *FLA* after the *2005 Bankruptcy Amendments* came into force, due to the intervention of the Federal Commissioner of Taxation as a creditor of the husband.⁹¹ The Full Court of the Family Court dismissed the Commissioner's appeal against property orders for equal division between the wife and the Commissioner of the net proceeds of sale of the former matrimonial home, which was the parties' only significant asset, in circumstances where the husband's tax liability was \$12 031 124 and the value of the former matrimonial home was \$4 750 000. The trial judge found that 'the husband engage[d]

⁸⁶ (2009) 41 Fam LR 120.

⁸⁷ *Ibid.*

⁸⁸ (2009) 40 Fam LR 552.

⁸⁹ This is evident from the first instance judgment in *Lemnos v Lemnos* (2008) 38 Fam LR 584, 600 [39] (Le Poer Trench J) and this point was not discussed on appeal.

⁹⁰ (2009) 40 Fam LR 552, 556 [17], 572 [92].

⁹¹ *Ibid.*

in reckless financial conduct but the wife truly was the “innocent” victim of his dealings’.⁹² The Full Court concluded that the first instance decision of Rose J came within the parameters of a reasonable exercise of discretion.⁹³ Following assessment of the husband and wife’s contributions as equal, Rose J had carefully weighed up the interests of the wife and the Commissioner, and this, combined with the fact that he had not made a s 75(2) adjustment in the wife’s favour (which, given her primary care of the spouses’ four children, would have given her an additional estimated \$500 000) and had not added back into the asset pool for division the husband’s legal fees and other monies (together amounting to approximately an additional \$700 000), appeared significant to the Full Court’s decision not to disturb the trial judge’s order for equal division.⁹⁴ Of the approaches outlined earlier, the Court’s approach in *Worsnop* is closest to our fourth approach (‘Combination Exercising Broad Discretion Approach’). The Court did not simply deduct the whole debt from the pool (‘Non-Bankrupt Spouse Shares the Debt Approach’), nor did it determine the wife’s equitable interest in the home using a trusts analysis (‘Property and Trusts Approach’). The approach of the Court was also not in accord with our first approach (‘Section 79 Approach’), as the Court in effect reduced what the wife would otherwise have received in the absence of the Commissioner’s claim (that is, no s 75(2) adjustment and no add back of the husband’s legal fees and other monies) to take some account of the interests of the Commissioner, but without any indication that the wife’s allocation should be compromised for the sorts of reasons explained by the Federal Court in *Parsons*.⁹⁵

In *Lemnos*,⁹⁶ decided a month after *Worsnop*⁹⁷ by a differently constituted Full Court of the Family Court, the husband was bankrupted due to his substantial liability to the ATO. The Full Court allowed the ATO’s appeal against the judgment of Le Poer Trench J at first instance. Similar to *Worsnop*, Le Poer Trench J found that the liability to the ATO had arisen due to the husband’s ‘reckless and negligent’ conduct regarding completion of his

⁹² *Worsnop v Worsnop* [No 2] (2007) 39 Fam LR 202, 227 [220] (Rose J).

⁹³ *Worsnop* (2009) 40 Fam LR 552, 570 [84].

⁹⁴ *Ibid* 571 [88]–[89].

⁹⁵ (2001) 109 FCR 120, 126–7 [17]–[18].

⁹⁶ (2009) 41 Fam LR 120.

⁹⁷ (2009) 40 Fam LR 552.

taxation returns and that the wife had no awareness or reason to be aware of the husband's conduct.⁹⁸ On this basis, applying s 79 of the *FLA*, Le Poer Trench J allocated 50 per cent of the assets (purchased in the husband's name) to the wife on the basis of her contributions, making no further adjustment in favour of her (apart from the transfer of a car of modest value) or the ATO on the basis of s 75(2).⁹⁹ In taking this approach, Le Poer Trench J considered the significant economic disparity between the parties (arising from the wife's role as a homemaker and primary carer to the couple's four children over the 30 year marriage while the husband worked as a successful property lawyer) and sought to balance this against the interests of the ATO.¹⁰⁰ This was a similar approach to *Worsnop*¹⁰¹ in that the wife's s 75(2) adjustment (to take account of the economic disparity) was being waived in the interest of creditors, ostensibly pursuant to s 75(2)(ha) of the *FLA*. Nevertheless, in *Lemnos* the ATO successfully appealed; all members of the Full Court considered that the outcome was outside the range of reasonable discretion (specifically, that it was too generous to the wife) and that this 'may well have been the result of his Honour having given disproportionate weight to the wife's lack of complicity in the husband's indiscretions and having given inadequate weight to the fact that the wife had benefited from those indiscretions.'¹⁰² The view therefore seemed to be that the wife should 'take the good with the bad' and share in losses over which she had no control, on the basis that she had the benefit of the funds that resulted from the husband's misconduct.¹⁰³

As the matter was remitted for retrial, the Full Court's view of the appropriate balance to be struck between the competing interests of the wife and the ATO was not clear. However, of our four suggested approaches, the first instance decision in *Lemnos*¹⁰⁴ appears similar to the Full Court's reasoning in *Worsnop*¹⁰⁵ (similar to our 'Combination Exercising Broad Discretion

⁹⁸ *Lemnos v Lemnos* (2007) 38 Fam LR 594, 610 [88].

⁹⁹ *Ibid* 611 [98]–[99].

¹⁰⁰ See *ibid* 607–8 [67]–[68], 610 [91].

¹⁰¹ (2009) 40 Fam LR 552.

¹⁰² (2009) 41 Fam LR 120, 175 [292] (Thackray and Ryan JJ); see also at 155 [175]–[177] (Coleman J).

¹⁰³ *Ibid* 165 [244]–[245] (Thackray and Ryan JJ), quoting *Johnson v Johnson [No 1]* (1999) 26 Fam LR 475, 478 [20.6].

¹⁰⁴ (2007) 38 Fam LR 594.

¹⁰⁵ (2009) 40 Fam LR 552.

Approach'), while the Full Court's reasoning in *Lemnos*¹⁰⁶ appears closest to our 'Non-Bankrupt Spouse Shares the Debt Approach'. However, as the wife's equitable interest in the property was not determined, the extent to which this is the case was unclear. There was no re-hearing in *Lemnos* so it appears the matter settled, perhaps influenced by the decision in *Worsnop* and the difficulty in predicting the outcome given the disparate Full Court approaches that were evident in the two cases.

2 First Instance Decisions of the Family Law Courts

There have been a handful of relevant first instance cases decided by the family law courts following *Worsnop* and *Lemnos*.¹⁰⁷ In these cases, the approach most commonly followed appears closest to our 'Combination Exercising Broad Discretion Approach'.

One example is the Family Court of Western Australia's 2011 first instance decision of Thackray CJ in *A v A*.¹⁰⁸ In this case, the spouses married in 1996 but were in an 'on-again, off-again' relationship between 1986 and 2004 due to the 'cycle of violence' perpetrated by the husband on the wife.¹⁰⁹ The violence comprised the husband's assaults on the wife every few months (for which he had received a conviction),¹¹⁰ verbal abuse and property damage. Indeed, Thackray CJ observed that 'the transcript [of the wife's giving of evidence concerning her husband's violence] is unlikely to reveal the full extent of the quiet menace evident in the husband's strongly controlled presentation'.¹¹¹ The key asset in dispute was the parties' jointly owned family home, valued at \$500 000, in which Thackray CJ treated each party as having a half share without consideration of their equitable interests. After separation, but before trial, the wife became bankrupt on her own petition, owing \$85 000 on a litigation loan she had taken to fund her representation in the proceedings.

¹⁰⁶ (2009) 41 Fam LR 120.

¹⁰⁷ *A v A* [2011] FCWA 98 (14 November 2011); *Roberts v Pedrana* [2013] FamCA 224 (9 April 2013); *Redmond v Stolz [No 3]* [2015] FamCA 692 (21 August 2015); *Zang v Juong* [2014] FamCA 582 (23 July 2014); *Morrison v Jepson* [2014] FCCA 1937 (26 August 2014); *Simon v Simon* [2013] FCCA 432 (5 June 2013); *Pander v Popa* [2013] FCCA 2177 (19 December 2013); *Bendell v Bendell* [2014] FCCA 1386 (3 July 2014).

¹⁰⁸ [2011] FCWA 98 (14 November 2011).

¹⁰⁹ *Ibid* [4], [109].

¹¹⁰ *Ibid* [97]–[107].

¹¹¹ *Ibid* [108].

The trustee did not intervene and the wife was self-represented, 'aware that her assets have vested in her trustee and the trustee will be entitled to the fruits of her claim, albeit she would be entitled to any surplus in her bankrupt estate.'¹¹² Thackray CJ concluded that the parties' contributions would have been of roughly equivalent value had it not been for the husband's violence, which on the basis of *Kennon v Kennon*,¹¹³ made her contribution during the marriage far more difficult than it would otherwise have been. While the s 75(2) factors were not considered to favour either party, Thackray CJ made clear that he was obliged to consider s 75(2)(ha), and the final orders reflected a balancing of all interests.¹¹⁴ The outcome in this case was that the Court ordered that the parties' home be sold. Assuming it was sold for \$500 000, and after repayment of certain of the parties' liabilities (including secured debts), there would be \$252 601 available for distribution (less the costs of sale) of which the wife would receive the first \$60 000, 'as well as retaining her superannuation of \$40 000 and other modest assets, and remain responsible for the debts proven in her bankruptcy.'¹¹⁵ The balance would then be equally divided between the husband and the wife (subject to any orders for costs). It would appear that in *A v A*,¹¹⁶ the better outcome to the wife resulted solely due to the husband's significant family violence rather than any intention to benefit the trustee.

While the prevailing approach appears closest to the 'Combination Exercising Broad Discretion Approach', divergent approaches are also evident, sometimes on similar facts. For example, in *Bendell v Bendell*,¹¹⁷ the husband's bankruptcy arose as a result of a guarantee that he executed without the wife's knowledge during their marriage to fund a business conducted by the couple. The spouses' main asset was the matrimonial home, purchased by them as tenants in common and in which there was equity of \$224 000. Judge Turner did not determine the spouses' respective shares in the existing equity; rather, he took the approach of subtracting the husband's liability under the guarantee from the spouses' total equity and altered the spouses' interests in the

¹¹² Ibid [13].

¹¹³ (1997) 22 Fam LR 1, 24 (Fogarty and Lindenmayer JJ).

¹¹⁴ *A v A* [2011] FCWA 98 (14 November 2011) [91].

¹¹⁵ Ibid [119] (Thackray CJ).

¹¹⁶ [2011] FCWA 98 (14 November 2011).

¹¹⁷ [2014] FCCA 1386 (3 July 2014).

amount left in the pool.¹¹⁸ This approach resembles our ‘Non-Bankrupt Spouse Shares the Debt Approach’ and appears inconsistent with the terms of s 79(1)(b) and the definition of ‘matrimonial cause’ in s 4 (as discussed above).

We also noticed that in some cases judges exercised creativity and flexibility in their attempts to tailor orders that balanced the interests of non-bankrupt spouses and unsecured creditors, and achieved a just and equitable outcome. One example is *Morrison v Jepson*,¹¹⁹ in which Judge Scarlett ordered that the matrimonial home valued at \$800 000 not be sold (thus delaying payment to the trustees of the \$135 000 they claimed to satisfy the outstanding amount owed under the husband’s bankruptcy) for four years, when the youngest child of the marriage would turn 18.¹²⁰ This order took account of the wife and children’s housing needs, the wife’s ‘somewhat dire’¹²¹ financial position having been left in Australia by the husband who had phoned to tell her that he had re-partnered overseas, the circumstance that ‘[a] large portion of the sum sought by the trustees consists of costs incurred by the trustees’¹²² after the husband petitioned for bankruptcy, and the judge’s observation that

There is no evidence that the [w]ife contributed in any way to the debts incurred by the [h]usband which led to his bankruptcy, quite the reverse, in fact, as she has given evidence that she used money she obtained from her father to pay her husband’s credit card debt in the sum of \$15 000.¹²³

Once again, however, there were no findings regarding the husband and wife’s respective legal and equitable interests in the matrimonial home, and so we cannot determine what really happened on a doctrinal level. In contrast, in *Zang v Juong*,¹²⁴ the interests of unsecured creditors were more overtly prioritised by Watts J when formulating orders in circumstances where the debt that led to the husband’s bankruptcy was accrued during the marriage

¹¹⁸ Ibid [18], [24]–[29].

¹¹⁹ [2014] FCCA 1937 (26 August 2014).

¹²⁰ Ibid [102]–[103].

¹²¹ Ibid [32].

¹²² Ibid [58].

¹²³ Ibid.

¹²⁴ [2014] FamCA 582 (23 July 2014).

and arose out of the spouses' joint commercial activities, and the wife had also attempted to dispose of the proceeds of sale of a property purchased by the spouses to a third party prior to *FLA* proceedings (a transaction set aside under s 106B of the *FLA*).¹²⁵ Once again, however, their legal and equitable interests in that property were not stated or determined.

In summary, our overall impression was that judges exercising *FLA* property jurisdiction in first instance cases involving bankruptcy debts which would result in sale of the family home are apparently striving in a variety of ways to balance the interests of the trustee against the interests of the non-bankrupt spouse. These ways include: in most cases, expressly considering the interests of the trustee in the s 75(2) context under s 75(2)(ha); reducing (or not making) a s 75(2) adjustment in the non-bankrupt spouse's favour in order to balance her interests with those of the trustee (similar to *Worsnop*);¹²⁶ and exercising creativity and flexibility in other ways by tailoring outcomes that reflected consideration of the bankrupt spouse's, the non-bankrupt spouse's and the trustee's respective levels of financial responsibility in the particular circumstances of the case.

However, approaches and results are also unpredictable and it does not appear that, in most cases, outcomes for non-bankrupt spouses are more favourable than would be achieved through adhering to existing legal and equitable interests in property (in fact, they may well be less favourable) — a sobering thought given that it was deficiencies in the law of trusts that prompted legislation in the area of family property law from the 1970s.¹²⁷ We

¹²⁵ *Ibid* [106], [196]–[198].

¹²⁶ (2009) 40 Fam LR 552. See, eg, *Simon v Simon* [2013] FCCA 432 (5 June 2013) [85] where Jarrett J commented that the 15 per cent adjustment to the wife on the basis of s 75(2) of the *FLA*:

would have been larger but for the fact that the debts of the unsecured creditors are debts that have been incurred in the course of this family's day-to-day business and which would otherwise have been taken into account for their full value but for the bankruptcy. Those matters are, in my view, relevant considerations pursuant to s 75(2)(ha) of the Act.

See also *Redmond v Stolz* [No 3] [2015] FamCA 692 (21 August 2015), where Forrest J assessed the wife's contributions as 75 per cent and made no further adjustment in favour of the wife or trustee under s 75(2) on the basis that the husband's bankruptcy had occurred after separation as a result of his unilateral actions (non-payment of school fees) and that the wife had been put to considerable cost and trouble in having to defend proceedings brought by the husband over four years, leading to a vexatious proceedings order under *FLA* s 102QB(2).

¹²⁷ See *Moore v Moore* [2008] FamCA 32 (25 January 2008) [159]–[179] (Carmody J).

found no evidence that *Stanford*¹²⁸ was being utilised to the advantage of the interests of trustees or non-bankrupt spouses. Courts were usually not making findings regarding the legal and equitable interests of spouses in property, which in cases involving trustees and non-bankrupt spouses is a prerequisite for the exercise of jurisdiction under s 79 of the *FLA*, given the terms of ss 79(1)(b) and 4(1) ('matrimonial cause').¹²⁹ This approach is perhaps the result of the overarching influence of the general approach taken in relation to unsecured debts of subtracting the spouses' debts from their assets at the outset, which does not differentiate between the spouses' interests unless an exception is established. In the end, however, because key findings were not being made regarding existing interests, whether or not s 79 adjustments were being made in favour of trustees from non-vested property was also unclear.

B *Trusts Analysis: Cummins and Non-FLA Cases after the 2005 Bankruptcy Amendments*

In this section of the article, we consider the approach taken to the division of the family home in the bankruptcy context by courts that are not exercising jurisdiction under the *FLA*.¹³⁰ In this context (still the most likely province for bankruptcies involving non-separated spouses), courts tend to adopt the 'Property and Trusts Approach' — but without any possibility of an adjustment under s 79 of the *FLA* given that the parties are not engaging in *FLA* property proceedings. However, the specific trusts principles applied by courts are not necessarily consistent or clear, particularly since the High Court's decision in *Cummins*.¹³¹

In *Cummins*, the High Court held that a bankrupt husband, who had contributed less than 25 per cent to the purchase price of a home, had a joint beneficial interest in that home under a resulting trust.¹³² This entitled his

¹²⁸ (2012) 247 CLR 108.

¹²⁹ An exception is *Redmond v Stolz* [No 3] [2015] FamCA 692 (21 August 2015) [172] (Forrest J).

¹³⁰ Note that our analysis does not include cases dealing with trusts between parents and children: see, eg, *Gleeson v Charan* [2011] FMCA 729 (21 September 2011); *Gillespie v Aravanis; Re Gillespie* [2014] FCA 630 (17 June 2014).

¹³¹ (2006) 227 CLR 278.

¹³² *Ibid* 301 [66]–[67].

trustee in bankruptcy to a half interest in the home as against the non-bankrupt spouse. The basis of the decision was twofold: first, that any presumption of resulting trust arising from contribution to purchase price was rebutted on the evidence;¹³³ and second, that there is a presumption of joint ownership of the family home as between husband and wife, regardless of the quantum of contribution to the purchase price.¹³⁴ As Sarmas has shown, the second basis of the High Court's judgment (presumption of joint ownership) has led to confusion and uncertainty in subsequent case law as it departs from traditional resulting trusts principles (such as the presumption of resulting trust based on contribution to the purchase price and the presumption of advancement of a wife by her husband) and may be in conflict with them.¹³⁵

Thus, in subsequent case law since *Cummins*,¹³⁶ courts have taken a somewhat mixed and arguably confused approach to the application of trusts principles in the determination of third party claims against the family home.¹³⁷ Sarmas notes that following *Cummins*, first instance federal courts and New South Wales state courts (both first instance and appellate) tended to apply the presumption of joint ownership almost mechanically, thereby declaring that the trustee is entitled to a half interest in the family home, regardless of the contribution by the non-bankrupt spouse.¹³⁸ More recently, the presumption of joint ownership has tended to be downplayed by these courts in favour of more traditional resulting and constructive trust principles. Interestingly, this more recent approach has generally resulted in the trustee receiving less than half the interest in the family home.¹³⁹

¹³³ Ibid 298–301 [57]–[67].

¹³⁴ Ibid 301–3 [68]–[72].

¹³⁵ Sarmas, above n 13. Sarmas also observes that when courts apply the presumption of joint ownership in place of traditional trusts principles, it tends to lead to worse outcomes for non-bankrupt wives than under traditional resulting trust principles: at 244–6.

¹³⁶ (2006) 227 CLR 278.

¹³⁷ Sarmas, above n 13, 237–43.

¹³⁸ Ibid.

¹³⁹ See, eg, *Lo Pilato v Stankovic* [2012] FMCA 736 (31 August 2012) where the Court held that there was a *Baumgartner* constructive trust (*Baumgartner v Baumgartner* (1987) 164 CLR 137) in favour of the wife over the family home giving her a 68 per cent share and the trustee of the bankrupt husband a 32 per cent share; *Sutherland v Byrne-Smith* [2011] FMCA 632 (22 December 2011) where constructive trust principles were applied to give the de facto wife a 60 per cent share of the family home and the trustee of her de facto partner 40 per cent;

On the other hand, federal appellate courts and state courts (other than in New South Wales) have generally ignored the *Cummins* presumption of joint ownership from the beginning, and have generally continued to apply traditional resulting trust principles.¹⁴⁰

Thus, while it is clear that courts not exercising *FLA* jurisdiction are using trusts law to determine third party claims to the family home (including claims by the trustee), the somewhat confusing state of affairs in relation to the correct trusts principles to be applied has led to uncertainty for both courts and, no doubt, for trustees and non-bankrupt spouses when conducting their negotiations and determining their litigation strategies.

Substantively, it would appear that when courts apply the *Cummins* presumption of joint ownership, the trustee tends to get a 50 per cent share of the family home; however, when the traditional principles are applied, the trustee generally tends to get less than 50 per cent.¹⁴¹

IV SETTLEMENTS OUTSIDE OF ADJUDICATED OUTCOMES

It also seems that there are a number of factors that currently encourage trustees and non-bankrupt spouses to settle without judicial adjudication.

First, anecdotal evidence gleaned from our conversations with professionals working in the area (judges, family lawyers and insolvency practitioners) indicates that bankruptcy practitioners are alive to current uncertainty surrounding the principles and practices that will be applied in bankruptcy matters by courts exercising family law jurisdiction, as well as judicial criticism of the amount of fees claimed by trustees, thereby making them less

Official Trustee in Bankruptcy v Brown [2011] FMCA 88 (20 May 2011) where the Court applied a resulting trust analysis under *Calverley v Green* (1984) 155 CLR 242 to give the de facto wife an approximate two-thirds interest in the family home as against the official trustee of her de facto husband. An exception to this later trend is the first instance Federal Court decision in *Deputy Federal Commissioner of Taxation v Vasiliades* [2015] FCA 412 (5 May 2015), which involved a claim by the ATO to recover more than \$30 million in tax debt from Mr Vasiliades. As part of this claim the ATO also sought a declaration that Mrs Vasiliades, who had held legal title to the family home, now held half the net proceeds of sale of that home on resulting trust for Mr Vasiliades. The Court invoked the *Cummins* (2006) 227 CLR 278 inference of equal ownership of the family home to grant the declaration sought by the ATO, holding that the couple, who had financed the home through joint borrowings, intended that it be held for the benefit of both of them.

¹⁴⁰ Sarmas, above n 13, 240–2.

¹⁴¹ See *ibid* 237–43 and the cases referred to therein.

confident about pursuing a robust litigation strategy. Furthermore, trustees are not able to initiate *FLA* s 79 proceedings, making it more likely that they are 'on the back foot' in the litigation process in the sense that they cannot initiate cases where they have a strong chance of success.

In cases where the non-bankrupt spouse has not initiated proceedings, uncertainty as to principles and practices may also provide an incentive for the trustee to attempt to settle matters quickly if the trustee perceives a risk that family law proceedings are imminent. If the bankruptcy matter can be dealt with before family law proceedings are initiated, then there may be a perception that it would be more difficult for the non-bankrupt spouse to claw back any property that is already vested in the trustee in those proceedings, and once the trustee has distributed the bankrupt's property to unsecured creditors, the 'window' for the non-bankrupt spouse to obtain *FLA* orders is lost.

Another important factor that may contribute to trustees' reluctance to litigate is the greater perceived difficulty in recovering costs under *FLA* s 117 (especially given judicial criticism of trustee's fees noted earlier, and the fact that parties to *FLA* proceedings usually bear their own costs) as compared with Federal Court proceedings. This may provide a greater incentive for the trustee, in particular, to seek to settle the matter in order to avoid the risk that it may have to cover its own costs if proceedings go ahead and the usual outcome occurs that a costs order is not obtained (or even worse, that a costs order is made against it).¹⁴²

A further factor is the recent reduction in funding of the ATO and, a few years ago, the Australian Financial Security Authority (whose responsibilities include the administration and regulation of the personal insolvency system).¹⁴³ As a significant creditor in bankruptcy matters, the ATO has traditionally played an important role in funding the trustee's litigation strategy in bankruptcy cases. Recent reduction of funding to the ATO may have impact-

¹⁴² See Leslie Glick, Peter Fary and Catherine Gobbo, 'Impact of Bankruptcy on Proceedings for Property Adjustment under the *Family Law Act 1975* (Cth)' (Paper presented at the Victorian Bar Bankruptcy and Family Law Seminar, Melbourne, 3 March 2016).

¹⁴³ See, eg, Kate Kachor, 'Govt Slashes ASIC, ATO Funding', *Financial Observer*, 13 May 2014 <<http://www.financialobserver.com.au/articles/govt-slashes-asic-ato-funding>>; Australian Financial Security Authority, *Introduction to AFSA*, Australian Government <<https://www.afsa.gov.au/about-us/introduction-to-us>>.

ed on its willingness and ability to provide funds to the trustee to pursue its interests through the courts.

At a practical level, it appears that trustees are highly commercial, practical and risk-averse. They prefer to settle and do not have the emotional investment in litigating that we may expect to see in parties to *FLA* disputes. As they are not able to initiate *FLA* s 79 proceedings, they are likely to be involved in matters that are in their interests to settle: that is, applications made by non-bankrupt spouses with stronger cases to argue.

What sorts of settlements are being reached outside of adjudicated outcomes? Anecdotal evidence suggests that this would be an area well worth further investigation. From what we have heard so far, a 50:50 split of equity in the family home is not unusual, although this will depend on the circumstances — for example, if there are dependent children it is possible that a trustee will agree to the non-bankrupt spouse retaining a greater share.

Anecdotal evidence also suggests that where a 50:50 approach is taken, it is reflective of the range of factors discussed in the previous section: overall, the outcomes of and uncertainty in the case law point to the commercial wisdom of a 50:50 division of home equity.

This raises questions regarding the approach taken where there are other assets. Anecdotally, it seems that often there are few other assets, especially as the bankrupt's superannuation savings do not vest in the trustee. *Lemnos*,¹⁴⁴ *Worsnop*,¹⁴⁵ *A v A*,¹⁴⁶ *Morrison v Jepson*,¹⁴⁷ *Zang v Juong*,¹⁴⁸ *Simon v Simon*¹⁴⁹ and *Redmond v Stolz [No 3]*¹⁵⁰ suggest that this is the case — in each instance the family home was the main asset. However, the cases we have identified reflect our key interest in disputes involving the family home and there would be value in research that explored the fate of other assets further.

¹⁴⁴ (2009) 41 Fam LR 120.

¹⁴⁵ (2009) 40 Fam LR 552.

¹⁴⁶ [2011] FCWA 98 (14 November 2001).

¹⁴⁷ [2014] FCCA 1937 (26 August 2014).

¹⁴⁸ [2014] FamCA 582 (23 July 2014).

¹⁴⁹ [2013] FCCA 432 (5 June 2013).

¹⁵⁰ [2015] FamCA 692 (21 August 2015).

V EVALUATION OF CURRENT LAW AND PRACTICE REGARDING
BANKRUPTCY AND THE FAMILY HOME

It would appear that there is a lack of clarity in the approach to this issue by both family law courts and generalist federal courts in the family home context. As far as family law courts are concerned, the *2005 Bankruptcy Amendments* provide little guidance as to the substantive principles to be applied, leaving a range of possible approaches open to the courts, as identified above. Unsurprisingly, then, family law courts have not taken a consistent approach in the few decided cases. The gap in legislative detail would suggest that family law courts see themselves as having a broad discretion when considering the claims of creditors during *FLA* property proceedings, and that failure to identify the spouses' legal and equitable interests in their property (perhaps influenced by the approach outside of the bankruptcy context of deducting unsecured liabilities from the pool and the existence of the broad s 79 discretion to alter existing interests), is often evident in the cases, with the result that it is not possible to know whether s 79(1)(b) of the *FLA* — which restricts courts to altering the trustee's interests in vested bankruptcy property — is in fact being complied with. In addition, the exercise of discretion has led to a range of approaches, including making an alteration using s 79 principles and treating the debt as that of the husband,¹⁵¹ requiring the non-bankrupt spouse to share in the debt,¹⁵² and taking the debt into account under s 75(2) and/or in the shaping of orders using a broad discretion.¹⁵³ What is clear is that there is little certainty as to what approach will be applied in a given case.

While the exercise of a broad discretion may be partly justified by the lack of substantive detail in the *2005 Bankruptcy Amendments*, the 'Section 79 Approach' that we have identified (which involves making the *FLA* s 79 assessment and then deducting amounts due to unsecured creditors from the bankrupt's share subject to any culpability of the non-bankrupt spouse, in the terms set out in *Parsons*)¹⁵⁴ is, in our view, consistent with the legislation and

¹⁵¹ *Morrison v Jepson* [2014] FCCA 1937 (26 August 2014).

¹⁵² *Lemnos* (2009) 41 Fam LR 120; *Bendell v Bendell* [2014] FCCA 1386 (3 July 2014).

¹⁵³ *Worsnop* (2009) 40 Fam LR 552; *A v A* [2011] FCWA 98 (14 November 2001); *Redmond v Stolz [No 3]* [2015] FamCA 692 (21 August 2015); *Zang v Juong* [2014] FamCA 582 (23 July 2014); *Simon v Simon* [2013] FCCA 432 (5 June 2013).

¹⁵⁴ (2001) 109 FCR 120.

is, in any case, the preferred approach from a policy perspective. As far as other courts are concerned, it is clear that the ‘Property and Trusts Approach’ is used to determine the property available to the bankrupt’s creditors. However, the specific trusts principles to be applied are the subject of some confusion by courts, particularly since the decision in *Cummins*.¹⁵⁵ In terms of existing legal principle, in the absence of *FLA* s 79 orders, it would appear to be correct that the trustee can claim the bankrupt spouse’s share of the beneficial interest in the property. However, the lack of clarity as to the relevant principles to be applied to determine the beneficial interest is troubling. Moreover, this approach is problematic from the point of view of policy, in that there is no scope whatsoever to consider the future needs of the non-bankrupt spouse in the allocation of beneficial interests (as there is under the *FLA*). Furthermore, the undervaluing of non-financial contributions by courts in the quantification of the spouses’ respective beneficial interests has been well documented.¹⁵⁶

VI CONCLUSION

In the end, the key question is the extent to which an appropriate balance is being reached when the interests of trustees are pitted against the interests of the non-bankrupt spouse in claims involving the ‘Great Australian Dream’ — the family home. From what we can gather so far, the current state of the law is both unsettled and largely unsatisfactory. The lack of legislative detail in the *2005 Bankruptcy Amendments*, and the divergent interpretations of family law courts as to their effect represent a lost opportunity to achieve clarity and an appropriate balance in this area. The continued confusion as to appropriate trusts principles to be applied in generalist federal courts, particularly following *Cummins*,¹⁵⁷ only compounds the problem.

In our view, this area is clearly in need of further legislative reform — at least in terms of making clear the approach to be followed by courts determining cases involving trustees and non-bankrupt spouses. In the meantime, we would recommend that family law courts hearing *FLA* property cases

¹⁵⁵ (2006) 227 CLR 278.

¹⁵⁶ See, eg, Marcia Neave, ‘The New Unconscionability Principle — Property Disputes between De Facto Partners’ (1991) 5 *Australian Journal of Family Law* 185; Helen Carr and Simone Wong, ‘Feminist Approaches to Property Law Research’ (2014) 3 *Property Law Review* 247.

¹⁵⁷ (2006) 227 CLR 278.

involving trustees (and also cases involving unsecured creditors outside the bankruptcy context) take the approach of: (1) identifying existing interests in property; (2) if s 79 discretion is exercised, altering the property interests in favour of the non-bankrupt spouse under s 79, taking into account the respective contributions and the additional considerations including under s 75(2) as they relate to the spouses; and (3) *then* considering the position of the trustee or unsecured creditors in the context of s 75(2)(ha),¹⁵⁸ and only in circumstances where there is culpability of the non-bankrupt/non-debtor spouse in relation to the incurring of the liability in the terms set out in *Parsons*.¹⁵⁹ Importantly, any adjustment made in favour of the trustee on the basis of s 75(2)(ha) cannot amount to an overall enlargement of the trustee's initial vested proprietary interest. This approach is consistent with our 'Section 79 Approach'.

In suggesting this, we acknowledge that at the level of everyday practice of family law, the approach we propose is likely to go against the grain for family law practitioners, due to the longstanding notion that the partnership of marriage provides a sensible and convenient basis for automatic debt-sharing on relationship breakdown. In response, we would argue that our approach is consistent with legal and equitable principle, the legislative terms and purpose of the *FLA* and *2005 Bankruptcy Amendments*, *Stanford*,¹⁶⁰ and the achievement of just and equitable outcomes.

¹⁵⁸ As noted above, if 'creditor' is given a narrow meaning in *FLA* s 75(2)(ha) then the interests of the trustee cannot be considered under this provision.

¹⁵⁹ (2001) 109 FCR 120, 126.

¹⁶⁰ (2012) 247 CLR 108.