

## CHASING THE ASSETS

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*“these sophisticated offshore structures are very familiar nowadays to the judiciary ... They neither impress, intimidate, nor fool anyone. The courts have lived with them for years”*

Coleridge J in *J v V* [2003] EWHC 3110 (Fam), 2004 1 FLR 1042

[1] That may be so in the Family Division of the High Court, where judges have a broad discretion in relation to the distribution of wealth between parties on divorce or dissolution of civil partnership. Offshore trust arrangements have been encountered less frequently in Scottish financial provision cases under the Family Law (Scotland) Act 1985 and when they do arise they are much more difficult to deal with.

[2] The difficulty is this. When property is held by trustees, they have title. The person or persons entitled to a beneficial interest under the trust does not hold the property. Section 9(1)(a) is the starting point in a claim for financial provision and is usually the most valuable consideration for a claimant. It requires the net value of the matrimonial or partnership property to be shared fairly. Section 10(4) of the Family Law (Scotland) Act 1984 defines matrimonial property as “all the property belonging to the parties or either of them at the relevant date...” The definition excludes property inherited or donated by third parties. Unless property falls within the definition in section 10(4), its value is not available to be shared under the principle in section 9(1)(a). Trust property may be difficult to classify as matrimonial property. If an interest in a trust is a resource, then it may be relevant to bearing the burden of caring for a child under 16, adjusting to loss of support, or avoiding serious financial hardship as a result of divorce in terms of section 9(1)(c), (d) and (e), but these principles are not often resorted to and awards tend to be low. An interest in a trust that is a resource is relevant to financial provision (section 8(2)(b)), but only to moderate, not to increase, a claim (*Latter v Latter* 1990 SLT 805, *Welsh v Welsh* 1994 SLT 828). So what do we do with these trusts?

### **Possible approaches**

[3] There are three possibilities:

1. Argue that any interest the spouse or partner has in the trust is matrimonial (or partnership) property, and/or is available as a resource.
2. Ask the court to set aside or vary the spouse's or partner's transfer into the trust. This raises difficult issues in relation to the position of trustees.
3. Ask the court to make an incidental order setting aside or varying a term of the trust. The argument has some bearing upon matrimonial partnerships.

### **Spouse or partner retaining interest in trust**

[4] For the purposes of section 9(1)(a) it is necessary to identify what "property" there is that belongs to one or both of the parties. The first point to make is that the fact of a trust does not preclude there being matrimonial property. The property itself is not matrimonial property, but an interest as beneficiary in the trust may be. In the case of a "bare trust" where the spouse or partner has a defined interest in the trust, then that interest is property. The interest may confer a right to call for the property to be transferred. More controversially there may be a right to an income stream. It is arguable that this is "property belonging" to a party. If an interest under a trust is as a result of gift or inheritance, then the exercise is academic, as that interest is incapable of forming matrimonial property in any event.

[5] The more interesting trusts are those where property held in the trust has not been inherited or donated by a third party, but the spouse or partner claims not to have a vested interest. The classic form of trust is a discretionary trust, where no-one has an immediate vested interest, but the trustees may advance capital or income to beneficiaries. In such a case the spouse or partner could legitimately say that the property held by the trustees is not his or her property and that he or she may never receive any benefit. Such a claim is worthy of close examination. There are a number of English cases where the court has been prepared to hold that a discretionary trust, even an offshore discretionary trust, should be treated as the property of one of the parties. The most celebrated case in recent years is probably *Charman v Charman* [2007] EWCA Civ 503, [2007] 1 FLR 1246 where the Court of Appeal upheld the decision of Coleridge J, who attributed the assets in a discretionary trust worth £52 million to the husband when calculating ancillary relief for the wife. The Court did add a

postscript complaining about the lack of principle in such cases and acknowledging that “London has become the divorce capital of the world for aspiring wives.”

[6] It is possible to achieve a similar result in Scotland. In *AB v CD* 2007 FamLR 53 the Lord Ordinary was satisfied that the assets of a discretionary trust should be regarded as belonging to the defender. The case is not wholly secure as a precedent as the defender chose to absent himself from the proof and the trustee did not enter the action. Nevertheless it was necessary to persuade the court of the argument. The defender had established a trust based in Jersey, and had transferred the matrimonial home at Mergie House to the trust. The house is described in the judgment as “a substantial 16<sup>th</sup> century country house”. He had also established a company during the marriage to develop certain inventions. The shares of this company were held in the trust. The assets of the trust were worth over £2,000,000 on the relevant date. But to whom did the value belong? There were a number of special features:

- The trust had been established by the husband. The assets transferred to the trust were his assets. His purpose at the time had been to protect assets from his creditors.
- The correspondence file recovered from the husband’s solicitors showed that the husband was giving instructions to solicitors and surveyors in relation to the assets of the trust, on matters such as loans, and sale of property.
- The trustees made payments to the husband and acted in accordance with his directions. There was no evidence that they exercised any independent discretion.

In these circumstances the court was prepared to hold that the trust in this case was “no more than a means of managing assets for the benefit of the first defender...” The Lord Ordinary accepted that the trust was the first defender’s “piggy bank”.

[7] Whether a trust is a “piggy bank” for one of the parties, or the party who is a potential beneficiary genuinely has no interest that could be characterised as matrimonial property will be a question of fact in each case. Experience of litigation has produced examples where a party has set up a trust and given himself a life interest, with a reversionary interest falling to children. If the party is a trustee, and the trustee has a power of appointment, so they may appoint the whole fund to the spouse, then it may be difficult to resist the conclusion that the net value of the matrimonial property to be attributed to him includes the

whole value of the trust, particularly if the trustees have meantime exercised lending powers and had lent the whole fund to the spouse.

[8] These arguments must however be viewed with some caution. There has been something of a backlash in England about the assertion that a trust is a “sham”. The law was analysed with some care by Munby J in *A v A*, [2007] EWCH 99 (Fam), [2007] 2 FLR 467. He pointed out that a sham trust is simply void and that trust cannot be treated as a sham for one purpose and not for another. Further “The court cannot grant relief merely because the husband’s arrangements appear to be artificial or even ‘dodgy’.” He warned in particular about the need for care where third party interests were involved. There is a useful definition of sham adopted from Diplock LJ in a hire purchase case, *Snook v London and West Riding Investments Ltd* [1967] 2 QB 786 at 802. He held that in so far as the term has any meaning in law, “it means acts done or documents executed by the parties to the “sham ” which are intended by them to give to third parties or to the court the appearance of creating between the parties legal rights and obligations different from the actual legal rights and obligations (if any) which the parties intend to create. ... for acts or documents to be a “sham”, with whatever legal consequences follow from this, all the parties thereto must have a common intention that the acts or documents are not to create the legal rights and obligations which they give the appearance of creating.”

[9] It remains a moot point whether a party has to go so far as to establish a sham in order to assert that the value of a trust should be attributed to their spouse or partner. In England the Court of Appeal did not find it necessary to go this far in attributing the value of the Dragon Trust to Mr Charman. Lord Brodie did not go so far in attributing the value of the Mergie Trust to the defender husband. It was sufficient to show that those trusts were treated by the trustees as “interest–in-possession” trusts for the husbands.

[10] So much for the difficult issue of trying to have the value of trust assets included in the net value of the matrimonial property. It may be an easier task to have access to trust money taken into account as a resource. Resources are statutorily defined in section 27(1) of the Family Law (Scotland) Act 1985 as “present and foreseeable resources”. Again there is a

shortage of Scottish authority, but there is English authority to suggest that where a spouse has some influence with third parties, such as trustees, it is legitimate to make orders that give some inducement to releasing funds (*Thomas v Thomas* 1995 2 FLR 668, see *A v A* [2007] EWCH 99 (Fam), [2007] 2 FLR 467).

### **Spouse or partner parting with property to trustees**

[11] What if the spouse or partner really has disposed of property? Property may have been transferred to a trust, or given to another family member. Section 18 of the Family Law (Scotland) Act 1985 allows the court to set aside, or vary, any transfer of, or transaction involving, property effected by the other person not more than five years before the date of the making of the claim. The application for an order under this section must be made not later than one year from the date of disposal of the claim.

[12] There has been a power to prevent a spouse transferring property to avoid financial provision since the introduction of financial provision (as opposed to relicts rights) in the Succession (Scotland) Act 1964. There have been attempts to defeat such anti-avoidance provisions, since they were introduced (see *eg Johnstone v Johnstone* 1967 SC 143). Section 27 of the 1964 Act allowed the Court to reduce or vary a settlement or disposition of property made by the defender within the three years before the application. The Divorce (Scotland) Act 1976 section 6 allowed either party to claim financial provision, and to seek an order reducing or varying a settlement or disposition. These measures were of limited use as the court could not set aside a gift of money (*Maclelean v Maclelean* 1976 SLT 86). The use of the words “transfer or transaction” in the 1985 Act was designed to close this gap. The language of “reduction” was abandoned, to make it clear that the sheriff, who could not ordinarily order reduction, could set aside or vary a transaction. In the 1985 Act “the court” means the Court of Session or the sheriff, as the case may require (section 27(1)). Under the pre-1985 law an order could be made if the settlement or disposition had as its primary purpose defeating the claim for financial provision. Intention was difficult to prove. The 1985 Act adopts an objective test. The court may exercise its power under section 18 if the transfer or transaction had the effect of, or is likely to have the effect of, defeating in whole or in part, the claim for financial provision, or a claim for aliment.

[13] When the power to make “anti-avoidance” orders was retained in 1985 no thought appears to have been given to how such an order would interact with the principles in section 9 of the Act. ‘Matrimonial property’ is defined by reference to what belonged to the parties on the relevant date (1985 Act, section 10(4)). If a spouse has given away property in anticipation of separation, the court may set aside the gift. Prior to the order being made that property was not matrimonial property. Is the effect of the order setting aside the disposal to add the restored property to the pool of matrimonial property? It would seem fair that this should be the result. The alternative approach would be to take the alienation of the property into consideration by the court as a special circumstance (see section 10(6)(c)) and then treat the restored property as a resource from which an order for financial provision could be met. There are two problems with this approach. The first would be if the net value of the matrimonial property, not including the restored property, was too small to allow a fair award if the restored property were to be taken into account. The second is not really a problem. It is simply that if the situation can be covered by a special circumstances argument, then an order restoring property may be unnecessary.

[14] There are no reported examples of a transaction actually being set aside, so there is no guidance from the court on how the power in section 18 to set aside transactions should be used. Section 18 is generally of more use to prevent a transaction before it has occurred. The court may interdict a spouse or partner from effecting a transfer or transaction that is likely to have the effect of defeating a claim for financial provision. Interdicts should be clear and specific. A person must know what he or she is prohibited from doing. Some of the interdicts under section 18 repeat the terms of the section and prevent a party “effecting a transfer or transaction that is likely to have the effect of defeating a claim for financial provision”. It may not be clear at the time of the transaction whether or not it will have such an effect. The interdicted party may be needlessly restrained, for fear of breaching the interdict. The party who has secured the interdict may not be adequately protected. If interdict is to be sought there should be precision about the transaction to be prohibited.

[15] There is protection for third parties. The court cannot grant an order setting aside or varying a transfer or transaction if this would prejudice any rights of a third party who has acquired the property in good faith for value, or derives title to the property from any person

who has done so. Once there is a transaction in good faith for value, then no section 18 order may be made. There is authority relating to the 1976 Act to the effect that it is for the third party to aver themselves within the proviso, and presumably to prove that they have acquired in good faith for value (*Leslie v Leslie* 1987 SLT 232). It is not clear whether value means full value, although a transaction at undervalue may not be in good faith. If there is a conclusion, or crave, for an order setting aside or varying a transfer or transaction, the third party affected must be given an opportunity to be heard (*Harris v Harris* 1988 SLT 101, see now RC 49.8(1)(j), OCR 33.7(1)(j) and OCR 33A.7(1)(h)).

[16] Intimation to third parties puts them on notice and allows them to apply by minute to be sisted as parties (RC 49.16, OCR 13.1). They are not parties unless they are sisted. There are however cases where it would be wise for the pursuer to join trustees or others holding property as defenders. This is where an interim order or protective diligence is necessary. In *AB v CD* the trustees were joined as defenders in order to seek inhibition. In *M v M* 2009 SLT 608 (OH); 2009 SLT 750 (IH) trustees were joined as defenders in order to seek interim interdict. In cases where it is too late to prevent a partner or spouse from passing on property, then it may be essential to prevent the person to whom the property has been transferred from disposing of the property pending the determination of the claim. It is possible to secure interdict against third parties in an action for divorce, if there is a claim for a transaction to be set aside under section 18. This was established in *M v M*. In that case the husband had transferred over £3,000,000 to trustees to purchase an estate to be held in trust for his children. The children were the offspring of extra-marital relationships. The wife claimed to have been unaware of the existence of the trust, or the children, until after separation. The trustees resisted interdict on the ground that the wife had no title to sue them and that interdict against them was not competent. The matter was settled in the Inner House. The Court held that interdict was competent against third parties in terms of section 18(2) or at common law.

[17] Inhibition and arrestment on the dependence must now be sought under the Debtors (Scotland) Act 1987, as amended by the Bankruptcy and Diligence (Scotland) Act 2007. It is no longer possible to secure inhibition and arrestment under section 19 of the Family Law (Scotland) Act 1985. The 1987 Act, as amended, allows diligence on the dependence to be

granted in respect of a “future or contingent debt” (section 15C). This is designed to cover claims for financial provision on divorce, but there are no reported decisions, as yet, on how the change in legislation affects actions between spouses, partners, and third parties involved in a claim under section 18 of the 1985 Act. Warrant for arrestment on the dependence is only competent where there is a claim for payment of a sum of money and inhibition is competent only where there is a claim for such a sum, or for specific implement of an obligation to convey heritable property to the creditor or grant in the creditors favour a real right in security or some other right over such property. Would it be sufficient to seek an order that the holder of property transfer the property to the other spouse or partner?

[18] Intimation to trustees or trustees being joined as defenders may be fraught with difficulty in relation to expenses. It is a moot point whether trustees should respond by seeking to be sisted as parties or lodging defences. There is English authority to suggest that in disputes between rival claimants to a trust fund the trustees should remain neutral and offer to submit to the court’s directions. This arose where a firm of solicitors sued a former partner for dishonesty and sought to have trusts he had set up for the benefit of himself and his family declared void (*Alsop Wilkinson v Neary* [1996] 1 WLR 1220). A Scottish trustee may be similarly encouraged to take a watching brief only, as he or she may be personally liable for expenses in a competition with a successful pursuer, who may be entitled to the fund in its entirety (*Cameron v Gibson* 2006 SLT 1088). On the other hand the pursuer takes a risk if he or she seeks protective orders at the outset. If the claim cannot thereafter be justified, he or she risks being found liable for the trustees expenses.

[19] A final word about partnerships. Can an interim order under section 18 be granted to prevent termination of a partnership pending decree of divorce? If spouses or civil partners are conducting a business as partners, then dissolution of the partnership may be to the prejudice of one of the parties. For example where husband and wife are nominally partners, then termination of the partnership by the husband may mean that the wife receives a nominal sum from a judicial factor for her interest in the partnership while the husband continues the business from other premises. Alternatively it may mean that the wife becomes entitled to a large sum under the partnership agreement, while the husband’s claim for transfer of her interest in the partnership as part of financial provision is defeated. Either party may have an

interest in keeping the partnership going pending resolution of financial matters. The sheriff court view is that interdict against dissolution is not available as notice to terminate the partnership is not a transaction involving property” (*Robertson v Robertson* 2009 FamLR 13). That view may not be shared by the Inner House, which is inclined to a more protean view of section 18. The court may “make the order applied for or such other order as it thinks fit”. Such other order could include suspension of a notice to terminate a partnership (see Commentary by Carolyn MacBride, 2009 FamLR 17).

### **Variation of trusts**

[20] A further possibility, where there is a trust, is to seek to set aside or vary the trust itself under section 14(2)(h) of the Family Law (Scotland) Act 1985. This can only be done if the trust can be characterised as an antenuptial or postnuptial marriage settlement. This, again, is a provision carried forward from the Succession (Scotland) Act 1964, section 26 and the Divorce (Scotland) Act 1976, section 5. It is again a provision that fits with the broad discretionary basis for financial provision that existed prior to the 1985 Act, but which is perhaps harder to bring into play within the more rigid structure that we now have.

[21] There are English examples of variation of trusts. *C v C (Ancillary Relief: Nuptial Settlement)* [2004] Fam 141 sets out a useful analysis of the law. The classic definition of a post-nuptial settlement is that it provides for the financial benefit of one or both of the spouses as spouses and with reference to the married state (*Prinsep v Prinsep* [1929] P 225 at 232). A disposition that makes some form of continuing provision for both or either of the parties to a marriage was considered by the House of Lords to be variable under the equivalent English provisions in *Brooks v Brooks* [1996] AC 375. *Brooks* is an interesting case, as the House of Lords affirmed a decision in the lower courts that a company pension fund fell within the definition of a post-nuptial marriage settlement.

[22] The variation of trust provisions do have potential in the Scottish context, albeit the settlement must be brought within the definition of matrimonial property for the purposes of section 9(1)(a) of the 1985 Act, or will require to be treated as resource giving scope for variation to satisfy the principles in sections 9(1)(c), (d) or (e), or used more generally to

satisfy an order justified by the principles, in terms of section 8(2)). Rights of third parties cannot be prejudiced (section 15(3)). Sadly the only post-1985 attempt to secure an order for variation of trust failed. This was in *Robertson v Robertson* 2003 SLT 208, where there was an attempt to argue that a partnership agreement between husband and wife fell within the broad definition of “marriage settlement” accepted by the House of Lords in *Brooks v Brooks*. The Temporary Lord Ordinary held that the partnership contact was a business arrangement, not a marriage settlement. This may be a decision worth re-visiting in the future, if on the facts it could be argued that the purpose of a particular agreement is to make provision for one or both spouses.

### **Conclusion**

[23] The Family Law (Scotland) Act 1985 has been with us for over twenty years, but we have not as yet explored all aspects of the legislation. On one view the Act provides a clear framework that gives predictability, allows sensible negotiation, resolution of cases and limits expenses. Another perspective is that it is too rigid to allow a fair outcome in complex cases. There is however still some scope for creative application of the law, in pursuit of a just result.

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