# The perils of prenuptial financial agreements

## Effectiveness and professional negligence

Wade, John

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# The Perils of Prenuptial Financial Agreements in Australia: Effectiveness and Professional Negligence

**By Professor John Wade**
**Bond University**

Legal practitioners in Australia who draft financial agreements **before** (s 90B; 90UB) or **during** a marriage or relationship (s 90C; 90UC) have a *high risk* of being guilty of professional negligence. Vigilance, protocols and expertise only *reduce* the risk; it is never eliminated. That is why a number of experienced and smart family lawyers in Australia will never draft pre-nuptial (s 90B; 90UB) or "during relationship" agreements. They send their clients to more naïve or risk-taking lawyers. In each case, the professional negligence and ineffective agreements lie dormant and hidden like hand grenades. The agreements will explode over say the 30 years which follow signing – either upon the separation of the signatory spouses, or the death of one, or a dramatic change of circumstances for better or worse of one of the spouses.

That is, it is very likely given normal patterns of marital life, that the majority of such financial agreements (pre-nuptial or during relationship) will be subsequently re-examined by critical eyes searching for loopholes.

Will the vast majority of such re-examined financial agreements be actually or potentially "nonbinding"; and will lawyers be blamed? Yes. The following chart sets out a *cumulative* list of what a binding prenuptial or during relationship agreement legally "requires", or *may* be required by the time the agreement is re-examined!, and matches each actual or potential requirement with the contrary standard pattern of human behaviour. These "standard patterns" are only derived anecdotally by the author from conversations and conferences with family lawyers around Australia. It is unlikely that many lawyers will formally admit in a formal survey (other than by their professional insurers)to the host of "errors", or at least risks, contained in their ticking and closed prenup cabinets?

The author acknowledges that every proposition set out below leads to debate about wandering precedents and "common practice". Some lawyers argue with unconvincing enthusiasm that their own drafting and protocols surrounding prenups are risk-free or bulletproof. Their speeches have a hollow ring in the current sea of uncertainty, and the revised defensive practices of some specialist family law firms.

| "Legal and/or Avoiding Professional Negligence Requirements" | Reality? |
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| 1. The terms of a pre-nuptial agreement should arguably (and arguably is risk enough?) reflect what orders would be made under s 79 of the *FLA* in order to avoid the easy implication of duress, or mental instability; or misunderstanding; superficial legal advice, or "unconscionable conduct" (*FLA*, s 90K(1)(e)). Additionally, due process protection of the weaker spouse should multiply in time and expense in direct proportion to the substantive unfairness of the agreement ( beware a pro forma list of recitals). See now *Thorne* v *Kennedy* [2017] HCA 49, where multiple pressures to sign a one-sided agreement held to be "undue influence". Additionally, agreements "in the broad s.79 range" are arguably a prerequisite to the court power in s.90 G(1A) to "remedy" technical and other defects. | 1. In the vast majority of agreements, one spouse contracts to be paid far less than (s)he would receive under s 79 of the *FLA*. Moreover, the "stronger" spouse is not expressly advised in writing that failure to provide "within the broad *FLA* range", possibly/probably destabilises the agreement in the variety of ways listed. Moreover, the stronger spouse does not insist upon proportionally more rigorous documented and expensive advice for the weaker spouse. ( ie insist on a greater degree of "informed" consent). |
| 2. The terms of a pre-nuptial agreement should provide staggered increases of payments based at least on the duration of the relationship in order to reflect ranges under s 79 of *FLA.* For example, gradually increasing amounts of cash for the first three years reflecting the "short marriage" cases, then gradually increasing percentages for the next two years etc. | 2. Few do; at least because the drafting of such a "time formula" is so complex, expensive and time consuming. |
| 3. Clients must make carefully documented full disclosure of assets (*FLA*, s 90K(1); plus independent valuation of major assets is highly recommended. | 3. Many clients are in too much haste; and want to avoid expense. |

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| 4. The drafting and final signatures of a pre-nuptial agreement should take place at least two months before cohabitation or a wedding – to reduce error; reduce the implication of duress and uninformed consent. | 4. The majority are not prepared and signed "early". ( eg *Thorne* v *Kennedy*: "sign or the forthcoming wedding in eleven days is off.") |
| 5. As a relationship survives, the pre-nuptial or "during relationship" agreement should have a sunset clause (say every five years), so that new financial arrangements can be made which more closely reflect the range under s 79 of the *FLA*. | 5. Few do. Such a clause would give the standardly exploited partner multiple opportunities to negotiate for more money; with a brilliant fallback position of "oh well, I will just rely on s 79 of the *FLA* if we ever separate". Alternatively, if negotiations fail during the specified period, one spouse could consciously decide to separate before that period expired - a dramatic fallback position every five years? |
| 6. Financial agreements can be set aside under the express terms of *FLA* when "normal" life events occur, such as birth of a child; serious illness of a child; change of caregiving of a child; unemployment or serious illness of a caregiver of a child(s 90K; 90 UM – "material change" re child). | 6. Drafters attempt to negate the effect of these standard life events by inserting a clause saying that the parties foresee all these events, in the hope that the agreement will prevail over them all. Clearly such clauses are ineffective and do not trump the legislation. |
| 7. Clients who sign such standardly one-sided agreements must be emotionally stable and give "informed consent". | 7. Many are not. Moreover, *their own lawyers* write copious self-serving and protective notes on the file to provide neat evidence that their own client was unstable, hurried, under pressure and signed despite clearly being advised not to do so!! This evidentiary time bomb is of course kept secret, and the other spouse has no idea that he has signed an ineffective agreement! |
| 8. If a lawyer's independent statement is challenged by *either* spouse, the Family Court will investigate what advice was actually given and heard in BOTH lawyers' offices years before. That is, the written certificates of advice of BOTH lawyers about "advantages" and | 8. Many lawyers read through the draft agreement with the client in less than an hour; sign the bland statement of advantages and disadvantages; and keep no abundant notes or videos of the specific advantages and disadvantages discussed; partly to |

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| "disadvantages" are not conclusive that such advice was accurately given! (*Hoult* [2011] Fam CA 1023; *Parker and Parker* [2012] FamCAFC 33; contra Benjamin J in *Wallace and Stelzer* (2011) FamCA 54). Therefore before spouses sign, both lawyers must witness the hand over to each other *and* to their own clients, a copy of a particular letter or video of advice given, in simple language, which explains the effect of the agreement and the advantages and disadvantages of entering the agreement for their own client. Thereby, both have evidence that the *other* lawyer has actually communicated a correct and considered (as compared to a routine) advice. If *Hoult* and *Parker* are followed, they will indeed halt pre-nups and mid-nups. No doubt subsequent case law will attempt to modify this clumsy consequence. | reduce client costs; and certainly do not *witness* the mutual hand over of more comprehensive copies of letters or videos of advice to each spouse and to the other lawyer—let alone *before* the client signs.<br>( Compare failure of both lawyers in *Neal v Jacovou* [2011] NSWSC 87 to check the fast advice given by one of them under a state TFM contractual release). |
| 9. It is likely that creeping case law will develop duties of each lawyer, not only to her/his *own* client, but also to the **other** client eg *Noll & Noll & Anor* [2011] Fam CA 872. (Compare the duty of a will drafter not only to the "client" testator, but also to beneficiaries). These duties may develop under the umbrella of avoiding "false or misleading" behaviour as required by state or federal consumer protection legislation. A lawyer would be wise to say little or nothing in the presence of the "other" spouse; specify that all correspondence is to be shown **only** to her his own client; and scrupulously ensure that any statement in the agreement (eg "I gave independent and comprehensive legal advice just before the agreement was signed") is true! | 9. Lawyers are not aware of the dormant duty to the "other side"; and in the ebb and flow of conversations, letters and drafting, often state "half truths" (eg this is "final"; "watertight"; "I have given the necessary advice" etc). |

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| 10. Before 4 January 2010, perhaps 95% of pre nuptial agreements in Australia were not binding because of one or more "technical" errors under convoluted old s 90G. The list of technical requirements under s 90G has been retrospectively reduced. However traps remain; (and the *Hoult* and *Parker* direction have multiplied the traps). For example, every time a draft financial agreement is amended in *any minute way*, each lawyer must give fresh advice just **before** each client finally signs (eg s 90G (i); 90UJ(i)); eg *Parker and Parker* [2010] Fam CA 664; [2012] Fam CAFC33). It is common for agreements to be amended multiple times, even to correct spelling errors. | 10. Many lawyers do not know or comply with even the reduced list of procedural "traps" which have survived in s 90G and s 90UJ. |
| 11. Due to residual procedural errors still possible under s 90G, each lawyer should require either: (a) all signings to take place in one room in front of all parties and lawyers; or (b) each lawyer to swap separate written warranties (immediately after signing) that all requirements in his/her control under s 90G(1) have been performed by him/her. | 11. Many agreements are not signed in a rugby scrum, but are posted from one signatory site to another; or signed in separate rooms<br>AND few lawyers would request performance warranties; or be willing to give such warranties which double the plaintiffs in a future professional negligence claim. |
| 12. *"Limping" and belatedly binding agreements.* A further procedural sting has remained in the tail of s 90 G(1) (ca). This subsection *requires* that a copy of *each* signed statement of advice be provided to the other spouse or his/her legal practitioner, with *no time limit* on this double handover.( eg *Hoult* [2011]FamCA 1023) So the agreement may be non-binding for say 20 years ( or forever) unless and until (a) both handovers occur; (b) to living, sane, non-dementia and accessible partners; or (c) to lawyers who happens to still be employed by the recipient spouses | 12. See above. Most lawyers are not aware of this sting in the tail; and do not use rugby scrums; or witness and record instant handovers of statements of advice; or give written warranties of compliance; or handover comprehensive letters of advice (see 8 above). |

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| ( very unlikely); and (d) of copies of both statements which still exist; and (e) with credible evidence that both handovers occurred! Again, presumably subsequent case law will attempt to patch up this awkward literal interpretation with vague phrases like "reasonable time". | |
| 13. As the allegations about either procedural error; or duress; or haste will arise say 5-30 years later when all memories are faded and reconstructed, it is essential that each lawyer writes a lengthy record of events relating to capacity and "technical compliance"<br>AND somehow stores that written record in at least one secure safe, similar to a safe for wills. The file must never be "thrown out". | 13. In reality, the majority of lawyers neither make such copious records; or store them safely; or charge clients appropriate fees if they do so. |
| 14. Many clients who want these agreements are from other cultures and English is not their primary language. It is essential that translators be hired; **and** that copies of the agreements be signed both in English and in certified primary language versions. | 14. The expense of all of this, and the reality that the stronger party often does not want the weaker party to "understand", means this rarely occurs. |
| 15. To avoid inevitable professional negligence accusations years later, each lawyer must provide his/her own client with a carefully drafted letter and/or video setting out a list of situations when the financial agreement will **not** be binding (*including all of the comments in this list!*). Clients should not be sold a product based on false representations or impressions of "*finality*". The client should sign and return a copy of such letter of advice to provide long term evidence of understanding that (s)he is buying a leaky product. *Hoult* and *Parker* also lead to the argument that such a letter or video | 15. On this requirement, lawyers are necessarily damned. The protective letter of advice **must** be given by each lawyer to reduce the number of professional negligence categories and accusations. However, those who draft such letters know that they are either too simple; or too legalistic to be accurate **and** understood. Moreover every list of exceptions is necessarily incomplete; and that a generic clause "there are other emerging exceptions" scares clients away! |

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| of exceptions is now essential ( not optional) to "binding"(ness), as s.90G(1) mandates advice "about the effect [and therefore non-effect] of the agreement on the rights [and therefore non-rights] of [the client]" | |
| 16. To avoid professional negligence, it is essential that each lawyer explain in writing the complex proposition that the agreement is not final post-death. That is, the survivor can attempt an amendment or "second bite" of finances under state TFM legislation. | 16. In many cases, this large "hole" in finality is neither explained in writing, or understood by clients. |
| 17. In NSW, it is possible for the clients to agree to undertake a Supreme Court application to overcome the major post death exception to finality (s95 *Succession Act* 2006 (NSW)). Lawyers should strongly advise such an immediate step in writing, and structure the financial agreement with extra periodic payments as incentives to do so; and make it clear that the severable financial agreement survives even if the *Succession Act* release is unsuccessful; and pay for extensive legal advice (definitely more than one interview) for BOTH parties; and ensure that the release payments are "generously " within the current and predicted TFM ranges. | 17. In reality in NSW, few clients "bother" to go through the expensive procedure under s 31 of *Family Provision Act* 1982 (NSW), though an executor can attempt to do so after one partner's death (eg *Neal v Jacovou* [2011] NSWSC 87). Moreover, lawyers usually do not do one or more of the following: record their recommendations in writing; together with staggered payments to provide incentives to complete Supreme Court approval; nor do they expressly sever the TFM release terms from the financial agreement; or pay for extensive independent TFM legal advice; or make generous post death provision ( usually the opposite). |
| 18. Theoretically, if spouses want to **vary** or "terminate" a financial agreement, they should do so by preparing and signing a new formal financial agreement with its attendant expense and formality (s 90J; 90UL). | 18. Most clients do not bother. They "vary" the formal agreement by casual conversations and inconsistent behaviour; thereby triggering uncertainty about the status of the formal agreement under the common law of estoppel, waiver, implied variation of contact and promissory estoppel (s 90KA; 90UN). |

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| 19. Technical and other defects in financial agreements which render them "non-binding" under s90G can be "fixed" in limited and expensive circumstances under s90G(1A). However, those are limited, uncertain and untested circumstances, which will save very few lawyers or clients (*Senior and Anderson* [2011] FamCA 802) | . 19. Most specialist family lawyers are aware that s90G(1A) offers rare salvation. Less aware lawyers (and their clients) may discover this "just and equitable" rescue section in times of trouble, though usually in vain. ( In *Wallace and Stelzer* [2011] FamCA 54, Benjamin J assisted the parties with the exercise -- "even if the agreement is not binding or is set aside, these are the just and equitable orders I would have made") |

If the above analysis is correct,

(1) Why are any lawyers in Australia willing to draft pre-nuptial (s 90B) financial agreements?
(2) How can lawyers and clients be effectively "warned" about the risks attached to pre-nuptial financial agreements?
(3) Should lawyers be advised to send letters to all clients AND their partners for whom they drew up pre-nuptial agreements under s90B, advising them their agreement is increasingly unlikely to be binding, and not to rely on it? And send copies of such correspondence to their professional insurers?

**Post Nuptial (s 90D; s90UD) Agreements**

The avalanche of warnings set out above in relation to prenups (s 90B; s90UB) and midnups (s 90C; s90UC), do not apply to the same extent to "postnuptial" financial agreements under s 90D or s90UD of the FLA. These are agreements entered into after the breakdown of a de facto relationship, or after divorce of a married couple.

This is because even though there are almost certainly technical errors in many s90D and s90UD postnup financial agreements, which thereby render them "non-binding", this usually does not matter. Why? Because before the error is discovered, the agreement is usually fully performed; and because such post separation agreements are not negotiated in the haze of romance; and because the terms of such s90D agreements are usually "in the range" of s79 orders, and so the desire to renege is less prevalent. (Contra Parker [2012] FamCAFC33 where the allegedly unfair agreement under s90C was signed after an initial separation).

Nevertheless, lawyers as risk managers understand the normal incidence of post-settlement blues. Therefore, the increasing potential for even s90D and s90UD agreements to be non-binding prior to full performance, unless expensive and intrusive signing protocols are followed exactly, will undoubtedly mean that informed lawyers will

abandon postnup s90D and s90UD agreements  for a time, and use consent orders instead to formalise financial settlements.

**APPENDIX**

## "Termination" Terminology and Financial Agreements under the *Family Law Act*

Financial Agreements in Australia at present can be:

1. **"Not binding"** for **technical** defects at the time of entry (s 90G); or at the time of entry one party engaged in "unconscionable" conduct (s 90K (1)(e); 90UM).
2. **"Set aside"** only by a **court order** for a limited list of post entry events (s 90K; 90UM).
3. **"Rescinded"** or **"varied"** by one of the **parties** if it is "void, voidable or unenforceable" under normal common law and equitable principles which apply to contracts. (s.90KA; 90UN). However, the parties' decision to rescind can be **overruled** or **confirmed** by the Family Court (s 90KA; 90UN).
4. **"Terminated"** (s 90J; 90UL) by another consensual financial agreement with equivalent degree of **formality** and statements (s 90J; 90UL).