

CASE NOTE

CLAYTON v CLAYTON: ADDRESSING THE ELEPHANT IN THE ROOM

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I INTRODUCTION

Mrs Clayton’s counsel, Deborah Chambers QC, began her submissions in the Supreme Court by arguing: “Mrs Clayton’s case is that the [Property (Relationships) Act 1976] is sufficient in its subject, scope and purpose, to address the elephant in this courtroom, the often devastating effect of relationship breakdown on women and children.”¹

Which assets are available to a woman at the conclusion of a long-term relationship is of vital importance to her economic freedom and independence. This is particularly true where a woman has compromised her own income to support a partner or raise children. The statutory framework aims to recognise domestic contributions on an equal playing field with paid work.² However, that aim can be thwarted when the pool of assets available to be divided is artificially small due to the use of trusts.

The Supreme Court’s decisions in *Clayton v Clayton* are of particular relevance to this issue because of the novel approach taken to trust property. The Court held that a bundle of powers under a trust deed amounting to de facto control was “property” under s 2 of the Property Relationships Act.³ The Court also held that a trust settled during a marriage is prima facie a nuptial trust under s 182 of the Family Proceedings Act 1980.⁴

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¹ *Clayton v Clayton* [2015] NZSC Trans 21 at 12 [*Transcript*].

² The scheme of the Property (Relationships) Act 1976 is premised on this idea.

³ *Clayton v Clayton* [2016] NZSC 29, [2016] 1 NZLR 551 at [69] [*Vaughan Road Property Trust*].

⁴ *Clayton v Clayton* [2016] NZSC 30, [2016] 1 NZLR 590 [*Claymark Trust*].

The Court discussed other issues of importance, including developing the jurisprudence on sham and illusory trusts.⁵ This case note will focus on the impact that the Supreme Court's decision has had and will have on relationship property law. This is important as relationship property has been an area of law that acutely impacts on women's economic rights. The *Clayton* decisions gave Mrs Clayton access to assets hidden by the economically and legally privileged party (Mr Clayton) in a decision that provided a much-needed step towards a more equal recognition of the traditional economic disadvantages faced by women.

II STATUTORY CONTEXT: THE PROPERTY (RELATIONSHIPS) ACT 1976

The Property (Relationships) Act (the PRA) is premised on couples who have a shared life together sharing the economic fruits of their partnership. At the end of their relationship, those fruits are divided equally.

The principles of the PRA are that men and women have equal status and their equality should be maintained and enhanced; that all forms of contribution are treated as equal; that a just division has regard to economic advantages or disadvantages to spouses arising from their marriage and that relationship property questions are to be resolved as inexpensively, simply and speedily as is consistent with justice.⁶

This statutory framework also expressly recognises that where, traditionally, a woman has undertaken childcare and other domestic work at the expense of paid work the law should value those contributions equally with paid work. It does this by applying a prima facie equal division of relationship property (50/50) regardless of whether one partner was in paid employment or making contributions in other ways such as in the home.⁷

Of crucial importance therefore, is what constitutes "relationship property", as defined in the PRA,⁸ as that represents the pool available for division accessible by the Court. If the property is "separate property", or "trust property", it is not available for division.⁹

⁵ See *Vaughan Road Property Trust*, above n 3, at [108].

⁶ Section 1N.

⁷ Section 11.

⁸ Section 8.

⁹ Sections 9 and 10.

The increasing use of trusts as a means of safeguarding assets from claims by creditors and spouses had the effect of placing large amounts of relationship property beyond the reach of the courts, often to the detriment of one of the spouses or partners. The social purposes of a joint relationship property law were thereby lost. This was recognised nearly 30 years ago in the Ministry of Justice *Report of the Working Group on Matrimonial Property and Family Protection*.¹⁰

Trusts are often used for “business purposes” — segregating and protecting assets from other business ventures and creditors.¹¹ This was the overt purpose for which Mr Clayton used his trusts.¹² Often the partner who is in control of the couple’s wealth and assets is the one who understands how the trust structures work, and where the real value is. That excludes the less financially literate partner from knowing the value of potential shared wealth that exists. The Court in *Clayton* was alive to these issues and, as will be discussed, took a novel approach to trust assets in the context of the PRA.

III THE SUPREME COURT DECISIONS

The Supreme Court dealt with issues relating to two separate trusts in two separate decisions: the *Vaughan Road Property Trust* decision,¹³ and the *Claymark Trust* decision.¹⁴ The decisions were released together. They were also, unusually, released after the parties had reached a settlement on 21 December 2015, due to the importance of the issues raised.¹⁵

A *The facts*

Mr and Mrs Clayton had a long marriage of 17 years during which they had two daughters.¹⁶ At the outset of their marriage Mr Clayton was a small business owner in the timber industry in Rotorua.¹⁷ By the end of their relationship their combined assets were, Mrs Clayton alleged, worth well in excess of \$29 million.¹⁸

¹⁰ Ministry of Justice *Report of the Working Group on Matrimonial Property and Family Protection* (October 1988) at 28–31.

¹¹ See *Claymark Trust*, above n 4, at [24].

¹² *Vaughan Road Property Trust*, above n 3, at [11].

¹³ *Vaughan Road Property Trust*, above n 3.

¹⁴ *Claymark Trust*, above n 4.

¹⁵ *Vaughan Road Property Trust*, above n 3, at [3].

¹⁶ At [6].

¹⁷ At [8].

¹⁸ *Transcript*, above n 1, at 24.

They had a relatively traditional relationship. Mrs Clayton assisted Mr Clayton in his business ventures. She was the main childcare provider. She also did some book keeping and accounting work for the Claymark Trust.¹⁹

Mr Clayton had structured their assets into a number of discretionary trusts. There were four trusts established during the marriage and four trusts established post separation. The “web of companies and trusts”²⁰ was ostensibly for “business reasons”.²¹ Two trusts set up during the marriage were the subject of litigation; the Vaughan Road Property Trust (VRPT) and the Claymark Trust (Claymark Trust). The VRPT assets included the land that the Claymark businesses operated. The Claymark Trust owned other business assets.

B Litigation history

The Family Court Judge, Judge Munro, set aside the s 21 PRA agreement that stipulated that, should they separate, the maximum Mrs Clayton could receive on division of their shared assets was capped at \$30,000.²² That agreement was set aside under s 21J of the PRA, which empowers the court “to set aside such agreements if satisfied that giving effect to it would cause serious injustice.”²³ Judge Munro also considered that the VRPT was an illusory trust and held that the majority of its assets were relationship property.²⁴

Justice Rodney Hansen in the High Court upheld the setting aside of the s 21 agreement and, for different reasons, considered that the VRPT was an illusory trust.²⁵

The Court of Appeal took the case in a different direction; the Court rejected the submission that the Trust was illusory.²⁶ It found, however, that the power of appointment that Mr Clayton held as Principal Family Member under the VRPT deed was “property” under s 2 of the PRA and that the value of the relationship property was the value of the assets of the trust.

19 *Claymark Trust*, above n 4, at [76].

20 At [79].

21 At [40].

22 *Vaughan Road Property Trust*, above n 3, at [7].

23 At [9].

24 *MAC v MAC FC Rotorua* FAM 2007-063-652, 2 December 2011 at [85].

25 *Clayton v Clayton* [2013] NZHC 301, [2013] 3 NZLR 236 at [91].

26 *Clayton v Clayton* [2015] NZCA 30, [2015] 3 NZLR 293 at [85].

C The Vaughan Road Property Trust decision

The VRPT was a trust settled 13 years into the Claytons' marriage. The VRPT held, among other assets, land used for the Claymark timber business and operated as a banker, taking loans for the businesses.²⁷ Mr Clayton was the settlor and sole Trustee as well as being one of the discretionary beneficiaries in his capacity as the Principal Family Member along with his daughters and Mrs Clayton. His powers were “both broad and free from the normal obligations imposed on fiduciaries in family trust deeds”.²⁸ In essence Mr Clayton retained total control over the assets of the trust.

Mrs Clayton sought to gain access to the trust assets for the purpose of her relationship property claim, and broadly argued that this was possible because either the VRPT was void ab initio as it was a sham or illusory, or the powers that Mr Clayton exercised amounted to control over the assets in the trust and that they should be valued as property under the PRA.

In summary, the Supreme Court held that: the bundle of rights and powers that Mr Clayton held under the trust deed did amount to property for the purpose of the PRA;²⁹ the value of the property rights was the value of the assets in the VRPT;³⁰ and the trust was not a sham.³¹ The Court declined to make a finding on whether the trust was illusory.³²

The most important finding by the Supreme Court was on the scope of “property” as defined in s 2 of the PRA. Property is defined broadly in the PRA to include “any interest in real or personal property ... and any other right or interest”.³³

The Court considered that the purposes of the PRA, including the principles of equality between spouses, were important: “of particular note in the present context is the purpose [at s 1M of the PRA] of recognising the equal contributions of both spouses to a marriage partnership”.³⁴

27 *Vaughan Road Property Trust*, above n 3, at [11].

28 At [14].

29 At [131].

30 At [131].

31 At [132].

32 At [133].

33 Property (Relationships) Act 1976, s 2.

34 *Vaughan Road Property Trust*, above n 3, at [15].

The Court accepted the submission for Mrs Clayton that “the property definition in s 2 of the PRA must be interpreted in a manner that reflects the statutory context”, holding:³⁵

We see the reference to “any other right or interest” when interpreted in the context of social legislation, as the PRA is, as broadening traditional concepts of property and as potentially inclusive of rights and interests that may not, in other contexts, be regarded as property rights or property interests.

The Court then considered the rights and powers held by Mr Clayton and whether they came within the definition of property. The test that the Court applied was adopted from a Privy Council decision, *Tasarruf Mevduati Sigorta Fonu v Merrill Lynch Bank and Trust Co (Cayman) Ltd*, that considered powers of revocation in a trust deed were “tantamount to ownership” over assets in a receivership context.³⁶

The Supreme Court said that *if* the VRPT had given Mr Clayton, as the Principal Family Member, the power of appointment to make himself sole beneficiary, the effect of that power would be analogous to the revocation of the trust and therefore tantamount to ownership of the assets.³⁷ However, the Court disagreed with the Court of Appeal that this was the correct interpretation of the trust deed, as in fact Mr Clayton did not have the power to remove the final beneficiaries of the trust, his two daughters.³⁸ The power of appointment alone was therefore not tantamount to ownership in the same way that the power of revocation was in the Privy Council decision of *Tasarruf Mevduati*.³⁹

However, the Court did consider that when viewed together Mr Clayton’s powers and entitlements under the VRPT deed gave him such a *degree of control* over the assets of the VRPT that it was appropriate to classify those powers as rights and interests under s 2 of the PRA. In particular, Mr Clayton was settlor, sole Trustee and Principal Family Member with the ability to transfer the power of appointment and to change any provision relating to the management and

35 At [38].

36 *Tasarruf Mevduati Sigorta Fonu v Merrill Lynch Bank and Trust Co (Cayman) Ltd* [2011] UKPC 17, [2012] 1 WLR 1721 [TMSF].

37 *Vaughan Road Property Trust*, above n 3, at [44].

38 At [46].

39 TMSF, above n 36, at [48].

administration of the trust.⁴⁰ The trust deed was to be interpreted in his favour, he could apply any part of the capital to himself, he could appoint a vesting day at any day of his choosing and effect a final distribution to himself (at the exclusion of the final beneficiaries, his daughters) and there was a very broad resettlement power.⁴¹ Further, the trust deed expressly allowed Mr Clayton to exercise powers in his own favour without traditional fiduciary constraint.⁴² These powers effectively amount to a general power of appointment in relation to the assets of the VRPT.⁴³ The powers, taking into account the statutory context, are properly classified as rights that give Mr Clayton interests in the assets of the VRPT and are therefore “property”.⁴⁴

The Court held that as the powers were acquired during the relationship they were relationship property.⁴⁵ Importantly, although not applicable in the *Vaughan Road Property Trust* decision, the Court did note that if some of the trust assets themselves were separate property (for example, if they were acquired prior to the relationship) it may be possible to use s 13 of the PRA, in relation to extraordinary circumstances, to adjust the presumption of equal sharing.⁴⁶

The Court valued the property interest as being the value of the trust assets.⁴⁷ The powers of control over the assets were tantamount to ownership, by analogy with the powers of appointment cases, making this approach to valuation consistent.⁴⁸ The reality was that Mr Clayton could, without any impropriety, allocate the entire trust corpus to himself, and why would he not thereby attribute market value to the assets?⁴⁹

40 At [14] and [51]–[55].

41 See [51]–[55].

42 At [57].

43 At [68].

44 At [80].

45 At [86].

46 At [89]. Although Mr Clayton maintained that some of the assets in the VRPT were separate property, the Family Court Judge had made a global allowance of \$500,000 for the value of the separate property, which Mrs Clayton did not challenge on appeal. Therefore, the Supreme Court did not consider it necessary to enquire further into the classification of assets in the trust.

47 At [107].

48 At [104].

49 Following *Walker v Walker* [2007] NZCA 30, [2007] NZFLR 722 at [60].

The Court then went on to discuss the submissions in relation to whether the VRPT was a sham or an illusory trust. The Court agreed with the lower courts that the VRPT was not a sham, as there was manifest subjective intent by Mr Clayton to create a trust.⁵⁰ The Court declined to make a finding on whether the VRPT was an illusory trust.⁵¹ These interesting issues are not discussed further here.⁵²

The *Vaughan Road Property Trust* decision is important for the broad inclusive approach taken to “property” for the purposes of the PRA. The Court found that the bundle of rights enjoyed by Mr Clayton did amount to property under the Act, and were acquired during the relationship.⁵³ They were therefore relationship property to be shared equally between the parties. The value of the rights was the value of the assets in the trust.

It is interesting to consider why the Court used this remedy in preference to the Family Court and High Court remedial route of declaring the trust to be illusory and a sham. One obvious benefit so to speak is that this “remedy” is only available in relationship property contexts, as was made clear by the attention paid to the social nature of the PRA. If the Court were to have followed the sham/illusory trust remedy path the implications for validity of trusts would have been far wider, and could potentially have undermined beneficiaries’ rights substantively. It is also important to recall the unusual facts of this case — the powers that Mr Clayton held without fiduciary restraint over the assets of the trust were not, one would like to hope, a typical example of family trust drafting. In that sense the ratio of this decision could be seen as quite narrow.

D The Claymark Trust decision

The second decision released by the Supreme Court relates to the Claymark Trust which was another trust established during the marriage and connected to the timber business. The primary legal issue was the scope and application of s 182 of the Family Proceedings Act 1980 (the FPA). That section provides a historic discretion to courts to make orders where property is settled for the benefit of the parties or their children during the marriage (and now civil

⁵⁰ *Vaughan Road Property Trust*, above n 3, at [117].

⁵¹ At [127].

⁵² See also, Jessica Palmer and Nicola Peart “Clayton v Clayton: a step too far?” (2015) 8 NZFLJ 114.

⁵³ At [80], [86] and in conclusion [98(a)].

union) and the premise of the settlement is fundamentally undermined by the end of the relationship.⁵⁴ The section only applies to couples who have been married or in a civil union (not long term de facto relationships) and is not intended to subvert any s 21 agreements.⁵⁵

Mrs Clayton argued that she should be entitled to compensation from the assets of the trust as it was a nuptial trust premised on the continuation of the marriage and from which she had had an ongoing expectation of benefiting.⁵⁶

The Court agreed, finding that the Claymark Trust was a nuptial settlement.⁵⁷ Two points are worth expanding on: the Court's discussion of the two-stage methodology around s 182 decisions and the expanded view of what, on the facts, can constitute a nuptial settlement.

The Supreme Court held that the lower courts had erred in not overtly adopting a two-stage approach in applying s 182.⁵⁸ The proper approach is first, to determine whether there has been a nuptial settlement and, second, to determine how the Court's discretion ought to be exercised. Stage one requires construction of the settlement documentation with a "generous approach" to finding a nuptial settlement.⁵⁹ Stage two is a discretionary assessment that will require individual consideration but the exercise of the discretion is not predicated on showing need. Rather, it is to remedy a change in the fundamental premise of the settlement.⁶⁰

The remedy that the Court would have granted, but for settlement, would have been to split the trust equally into two separate trusts to benefit Mrs Clayton equally.⁶¹

The second important point arising from the judgment is a broader approach to stage one — what constitutes a "nuptial settlement". The Supreme Court referred to the Court of Appeal's decision of *Ward v Ward*, which the Supreme Court said decided that:⁶²

54 *Claymark Trust*, above n 4, at [4]–[6]. The section's origins date back to s 5 of the Matrimonial Causes Act 1859 (UK) 22 & 23 Vict c 61.

55 Family Proceedings Act 1980, s 182(6).

56 At [21] recording her submission in the Family Court below.

57 *Claymark Trust*, above n 4, at [42] per Glazebrook J and at [133] per Elias CJ in a concurring judgment.

58 At [30].

59 At [88].

60 At [90].

61 At [83].

62 *Ward v Ward* [2009] NZCA 139, [2009] 3 NZLR 336 at [27].

to come within the term “settlement” as used in s 182 of the FPA, any arrangement must be one which ... makes some form of continuing provision for either or both of the parties to a marriage in their capacity as spouses, with or without provision for their children.

It was also made clear that discretionary family trusts can be settlements for the purposes of s 182.⁶³

The Supreme Court in the *Claymark Trust* decision went on to say that:⁶⁴

... the requirement that the settlement be for both or either of the parties “in their capacity as spouses” as meaning only that there must be a connection or proximity between the settlement and the marriage. Where there is a family trust (whether discretionary or otherwise) set up during the currency of a marriage with either or both parties to the marriage as beneficiaries, there will almost inevitably be that connection.

The *Claymark Trust* was in part a business vehicle.⁶⁵ Importantly, the Supreme Court rejected a submission that the *Claymark Trust* could not be a nuptial settlement because it was set up for business reasons:⁶⁶

For a start, one of the purposes of the Trust was said to be to take assets out of the circle of bank guarantees related to the business. It seems to us that the separation of property from the risks associated with business assets must have the purpose of protecting assets for the family.

The nature of the assets is not determinative of whether it is a nuptial settlement.⁶⁷ This broadens the understanding of what a nuptial settlement is and prevents the argument that a trust is not so classified simply because it is used to control or segregate business assets.

IV CONCLUSION

The Court will not look through trusts, or ‘trust bust’ in a relationship property context without legal foundation. The legal avenues through which trust assets can be accessed presently include:⁶⁸

63 At [28]–[31].

64 *Claymark Trust*, above n 4, at [34] (footnotes omitted).

65 At [79].

66 At [40] (footnotes omitted).

67 At [87].

68 See also Kate Davenport and Tammy McLeod *Webinar Clayton – implications for Practitioners* (NZLS

- i) a s 44C claim under the PRA;
- ii) an equitable claim such as constructive trust in narrow circumstances;
- iii) an argument that the trust deed (set up during the relationship) grants such a degree of control over the trust assets to a partner in the relationship that those rights are tantamount to an interest in the assets and are therefore property under s 2 of the PRA; or
- iv) an argument that the trust was a nuptial settlement that created an expectation of ongoing benefit during the marriage which needs to be resettled following divorce under s 182 of the Family Proceedings Act 1980.

This case note has discussed the latter two avenues, which have been established and expanded on by the Supreme Court in its Clayton decisions.

The Supreme Court Clayton decisions have been discussed for their impact within relationship property law only. These decisions give further important support and legal redress to women seeking economic equality and independence at the conclusion of long-term relationships. The cases also have wider implications — raising questions about the rights of beneficiaries who potentially lose their beneficial interests, about the legitimate use or otherwise of trusts in business and/or family contexts and about the implications of trust rights as property in other areas of the law such as insolvency.