

**RISK MANAGEMENT IN FAMILY CASES -**

**PRE-NUPTIAL AGREEMENTS**

**[1] Risk:**

* **the potential of gaining or losing something of value - *Wikipedia***
* **a situation involving exposure to danger – *Oxford dictionary***
* **the possibility of something bad happening – *Cambridge dictionary***

Not perhaps the issues that immediately leap to mind when contemplating a wedding.

**[2] Pre-nuptial agreements**

[2.1] A pre-nuptial agreement is essentially an exercise in managing risk, the risk that the marriage might fail and that the financial consequences of failure may be unacceptable. The odd thing about pre-nuptial agreements in contemporary Scots law is that we have a well-defined set of principles for financial provision in the event of divorce, that are designed to ensure fairness, and a pre-nuptial agreement is, by definition, an attempt to impose something else. What is more, the impetus usually comes from the party with the assets, who is seeking to prevent the other party participating in those assets to the extent the law may in the future regard as fair.

[2.2] The Scottish position on pre-nuptial agreements derives from law that pre-dates the Family Law (Scotland) Act 1985. In *Thomson v Thomson* 1981 S.C. 344 Lord Cameron, in the First Division of the Court of Session, explained:

“parties to a marriage contract being of full age are entitled to make such terms as they think fit, including the right to discharge any claim to legal rights on the part of one spouse on the dissolution of the marriage, whether caused by death, divorce, or any other cause.”

In *Elder v Elder* 1985 SLT 471 Lord Mackay of Clashfern held that *Thomson* was binding authority to the effect that the right to claim a periodical allowance under the Divorce (Scotland) Act 1976 could be validly discharged. This decision has been cited in support of the same proposition under the Family Law (Scotland) Act 1985.

[2.3] On the other hand, section 16 of the Family Law (Scotland) Act 1985 allows the court to set aside an agreement on financial provision, or any term of it, where the agreement was not fair and reasonable at the time it was entered into. This provision was applied to a pre-nuptial agreement by Sheriff Principal Dunlop in *Kibble v Kibble* 2010 S.L.T. (Sh Ct) 5. It therefore requires to be kept in mind as a counter-balancing consideration in relation to the benefit of a pre-nuptial agreement. To be fair *Kibble* is the only reported modern Scottish case on pre-nuptial agreements. It does not therefore give us much to go on, but it is worth thinking about these agreements, on the basis that they are likely to be open to future challenge under section 16.

**[3] Drafting the agreement**

[3.1] For any agreement, the drafting is important. If the terms are not clear, then they may be open to challenge. There is a strong argument for keeping matters as simple and straightforward as possible. The general position is that the court will do its best to give effect to a contract since contracts are intended to have legal effect. For example LP Clyde in *R and J Dempster Ltd v Motherwell Bridge & Eng. Co. Ltd.* 1964 SC 308/327 said:

“… when a court of law is asked to construe a commercial arrangement couched in terms which are *prima facie* obligatory … the court will prefer a construction which gives the contract binding effect. For the essence of commerce is making bargains, and unenforceable arrangements are the exception and not the rule.”

Lord Woolman *Dundee CC and others v D Geddes (Contractors) Ltd* [2014] CSOH 164 both confirmed and qualified this proposition:

“The court always strives to adopt a construction that gives effect to a term of a contract, *…* There are, however, limits beyond which it cannot go. It cannot rewrite the parties’ contract.”

[3.2] Even when there is apparent conflict between two provisions the court would only hold the contract void for uncertainty as a last resort (Lord Macfadyen in *Ideal Services Scotland Ltd v Premier Glass Packaging Ltd* 1999 SLT 134 at 137E - F). Matters were put rather pithily in the English case of *Brown v Gould* [1972] 1 Ch 53, the court will not hold an instrument void for uncertainty “unless it is utterly impossible to put a meaning upon it. The duty of the court is to put a fair meaning on the terms used, and not, as was said in one case, to repose on the easy pillow of saying that the whole is void for uncertainty”. There is therefore reassurance that the court will seek to give effect to a poorly drafted agreement, but it would obviously be preferable not to have to invoke this line of authority.

[3.3] In my experience the most common substantive error in framing an agreement is to overlook the point that it is the parties who are committed to fulfilling the obligations under the agreement. If one or both of the parties are involved in a limited company, the company is generally a third party, and is not going to be bound by an agreement between spouses or cohabitants. It may be of no use to provide in a minute of agreement, whether separation, pre-nuptial or cohabitation, that a company will do something, if the company is not a party to the agreement. For example, if an essential element of the arrangement is that property is transferred by a company, then careful thought is required as to what happens if the company does not do so. Is the agreement to be abrogated? Is one of the parties going to undertake an obligation or make a payment in lieu? How is the situation to be managed? This may be an error that arises more regularly in separation agreements, than in pre-nuptial agreements. In the latter parties are looking into the future when an artificial person such as a company may no longer exist and it is to be hoped this has been appreciated when preparing the agreement.

[3.4] A pre-nuptial agreement is, like insurance, designed to be put in a drawer in the hope it is not required. It may however be pulled out and dusted down 10, 20, 30 or more years hence. This does distinguish it from a separation agreement. It raises issues of how closely it should follow the current law? Should it be time limited and cease to apply after a particular period, or in particular circumstances? Are children taken into account? And how should the agreement be safeguarded?

**[4] The criteria of fairness and reasonableness**

[4.1] If pre-nuptial agreements are going to be subject to the same considerations as other agreements on financial provision, then we can look at the section 16 case law generally, and see how pre-nuptial agreements measure up. The leading Court of Session authority is *Gillon v Gillon (No 3)* 1995 SLT 678, where the Outer House judge before whom the case finally landed, Lord Weir, set out a series of propositions in relation to exercise of the power to set aside agreements relating to financial provision. He said:

“(1) It is necessary to examine the agreement from the point of view of both fairness and reasonableness.

(2) Such examination must relate to all the relevant circumstances leading up to and prevailing at the time of the execution of the agreement, including amongst other things the nature and quality of any legal advice given to either party.

(3) Evidence that some unfair advantage was taken by one party of the other by reason of circumstances prevailing at the time of negotiations may have a cogent bearing on the determination of the issue.

(4) The court should not be unduly ready to overturn agreements validly entered into. (5) The fact that it transpires that an agreement has led to an unequal and possibly a very unequal division of assets does not by itself necessarily give rise to any inference of unfairness and unreasonableness.”

[4.2] Is this analysis helpful? The wife in *Gillon* had accepted no aliment and given up her claim to the husband’s assets, including his pension, but in return had obtained the right to purchase the husband’s interest in the matrimonial home at an advantageous price. She had not had the husband’s pension valued before she surrendered her claim. She did not have the outcome she would have secured had she gone on to claim financial provision under the Family Law (Scotland) Act 1985, but she had secured what she had wanted to achieve, namely the house and the benefit of certainty. Lord Weir refused to set aside the agreement.

[4.3] These considerations are echoed in a very recent decision of the Sheriff Appeal Court in *Bradley v Bradley* ([2017] SAC (Civ) 29, issued on 21 September 2017. The appeal sheriffs were unimpressed by a submission based on the “ethos” of the Family Law (Scotland) Act 1985 in favour of a clean break and keen to stress that the ethos also included encouraging parties to settle their differences by agreement. The husband in that case was protesting about an agreement to pay half his monthly pension income to the wife until the death of one of them. He had not wanted to hand over a lump sum to her and he had wanted to buy a house. The wife had kept the matrimonial home, but had raised a loan of £120,000 to pay a capital sum to him, which allowed him to buy the house he wanted. The sheriff had been swayed by the sole factor of lack of legal advice to the husband in relation to periodical allowances under the Family Law (Scotland) Act 1985. She set aside the monthly payment, imposing in its place a different arrangement involving a pension-sharing order. The Sheriff Appeal Court allowed the wife’s appeal. The husband had got what he wanted and could not now complain. Appeal Sheriff Ross set out that what amounted to unfairness or unreasonableness in any case depended on the facts and circumstances. He made the useful comment that it would rarely be sufficient to focus on a single aspect.

[4.4] There is therefore no “magic bullet” to attack an agreement. It all depends on the facts. This is all very well but it does not assist much in dealing with the exercise of assessment of risk. The best we can do is point to the sort of factors that are capable of influencing the court one way or the other.

**[5] The starting point - What is the agreement designed to protect?**

[5.1] Anxiety about section 16 can divert attention from the most important issue, namely what is the pre-nuptial agreement designed to protect? The first question to ask in drafting, or advising on such an agreement is, “What is the loss, or ‘bad thing’ that is feared?” The task of the drafter should be focussed on the purpose of the agreement. If the purpose is clear and is inherently reasonable, then this represents a good starting point. If a proposed, or challenged, agreement goes further than it needs to for its purpose, then that may be the first indicator that it is not fair or not reasonable.

[5.2] I must confess that this is not an argument that has featured in any judgment, but then it is an argument that is by its nature more likely to be relevant to pre-nuptial agreements than separation agreements, and we do not yet have a developed case law on pre-nuptial agreements. It must however be good practice to start with a clear idea of what the agreement is designed to achieve. And it must be a legitimate point to raise if advising the potential recipient of such an agreement, if the agreement goes further than it needs to do, to achieve the expressed objective. And as an aside, drafting a heavy-handed agreement for a couple not yet married is not necessarily the most constructive contribution to their future happiness.

[5.3] One of the most common issues is that one of the parties has an asset, is aware that there could be a change in form of that asset, and wishes to protect any resulting asset from sharing. For example, a fisherman will know that his vessel will probably require to be renewed in the course of the marriage and wants to avoid the risk that the value of any new vessel could be shared with his wife. Or a wife may have shares in a family company. If she retained them they would not be matrimonial property, but were there to be a company reorganisation in the course of which she exchanged her shares for shares in a new holding company, the full value of the new shares could be exposed to sharing. In consequence we are regularly asked to draft pre-nuptial agreements providing that if a particular asset owned on marriage is sold, and the proceeds are invested in a replacement, the value of that replacement will not be shared in the course of financial provision on divorce. These sorts of agreements are in effect, agreements on “special circumstances”. They provide conclusively for how it will be taken into account that property on divorce derives from property on marriage.

[5.4] Pre-nuptial agreements are often motivated by a desire to protect others who may be affected were there a requirement to share the value of the property. It may be a concern about breaking up a commercial or agricultural enterprise if there is a future marital breakdown. There are cases where a couple marry later in life and want to ring fence property for their children from earlier relationships. Agreements of this kind should be relatively easy to justify and if necessary to defend.

[5.5] In contrast a total renunciation and discharge of financial provision may well go too far, in a case where one party may patently be left in a difficult financial provision. A case where there must be particular anxieties is the young girl who marries the son of a wealthy man, where the father insists on a pre-nuptial agreement, on the basis that he is not prepared to leave his wealth to the boy, if his new wife would participate on divorce. The Family Law (Scotland) Act 1985 excludes inherited wealth from matrimonial property, but inherited wealth that changes form is available for sharing (subject to special circumstances) and inherited wealth may be a resource and as such available to satisfy an award, including an award under section 9(1)(b), (c), (d) and (e). This sort of case must raise doubts about initial fairness and reasonableness as between the intending spouses.

**[6] Offsetting risk**

[6.1] There are then factors that emerge from the case law that would tend to demonstrate that an agreement should or should not be set aside. The following issues emerge from the case law, albeit this is case law relating to separation agreements

[6.2] *Is there mutuality?*

[6.2.1] In both *Gillon* and *Bradley* the court was swayed by the consideration that the spouse complaining about the agreement had actually achieved an outcome that at the time they had thought valuable. The agreements in those cases were not therefore one-sided. An agreement that has something for both parties is much more likely to be considered fair and reasonable. It will be a relevant consideration when drafting an agreement to ask what is in this for the other party. This is somewhat different when engaged in a hypothetical exercise in the context of a pre-nuptial agreement, but it is possible to apply a similar principle.

[6.2.2] If one intending spouse is protecting a company, and the other has a (real) business interest that is also to be protected, even if less valuable, there is an element of mutuality. If one is renouncing claims, but the agreement makes provision of a house and payments to cover adjustment to loss of support, then the agreement contains advance benefit and assurance about some aspects of financial provision. Even if one is making more of a sacrifice than the other, if it can be said that his or her interests have been taken into account and appropriate protection provided, then the agreement will be easier to defend.

[6.2.3] There must be an element of concern about an intending spouse who agrees to renounce all claims to prove they love the other for himself/herself, not his/her money. The recipient of this devotion who accepts the sacrifice, without considering whether it is fair, may be setting up an agreement that fails to meet the test of section 16. He or she may be thought to have taken unfair advantage of the other intending spouse.

[6.3] *Has there been disclosure?*

[6.3.1] Great store is laid on full disclosure of assets in separation agreements relating to financial provision. Solicitors do not generally resolve financial provision cases without information on assets and resources. The issue of disclosure is also relevant to a claim under section 16, as was remarked by Lord Penrose in *Gillon v Gillon (No 1)* 1994 SLT 978. The issues raised by section 16 are however distinct form what might in the end be awarded by way of financial provision, as was confirmed by the Inner House who agreed that a preliminary proof on the issues raised by section 16 was competent in *Gillon v Gillon (No 2)* 1994 SC 162. Failure to make full disclosure may result in a separation agreement being set aside, as in *McKay v McKay* 2006 SLT (Sh Ct) 149, where the husband failed to disclose a pension policy, albeit he apparently did this on legal advice. The sheriff set aside the resulting minute of agreement, and her decision was sustained by the sheriff principal. Failure to make full disclosure played a part in persuading the sheriff to set aside an agreement in *MacDonald v MacDonald* 2009 Fam LR 131, although in that case there was also an unacceptable degree of coercion, in the form of the husband repeatedly contacting the wife and shouting and swearing at her. Again this was a decision sustained by the sheriff principal.

[6.3.2] Failure to take account of assets need not be culpable. In *Worth v Worth* 1994 SLT (Sh Ct) 54 Sheriff Thomson set aside a minute of agreement discharging financial claims, which overlooked the parties’ pensions. The parties had simply not appreciated the significance of the pensions, had reached an agreement between themselves, without the benefit of advice, and had asked a solicitor to put this into “legal form”. Sheriff Macnair, in *Clarkson v Clarkson* 2008 SLT (Sh Ct) 2, set aside an agreement that had proceeded on the basis of a misapprehension about the value of the husband’s shares in his own business. While the forensic accountants disagreed over the value, neither was aware that VAT had mistakenly been included in turnover. HMRC insisted on immediate repayment. In consequence the company was liquidated.

[6.3.3] Disclosure may be less relevant in a pre-nuptial agreement, as the financial provision to be made will be in the future, when the relevant assets may be quite different. There is something almost laughable about schedules where one spouse lists multimillion pound shareholdings and the other puts down their CD collection and Volkswagen. These schedules do however give the context for determining whether the agreement is unfair or unreasonable, given that section 16 requires the test to be applied “at the time the agreement is entered into.” This can, of course, be played both ways. On the one hand it may highlight that there is a serious imbalance of resources. On the other it permits an argument that the imbalance was fully known at the material time.

[6.4] *Has there been (good) legal advice*

[6.4.1] There is no getting around the issue of legal advice. As we seen from *Bradley,* the absence or otherwise of legal advice may not be determinative, but it will be material. Interestingly Lord Weir did not refer to legal advice *per se.* In his opinion he refers to the *“*nature and quality of any legal advice given to either party”. Bad legal advice may result in an agreement being set aside. This may be a little unfair on the other party, but in principle he or she may not be permitted to take advantage of the fact that their intending spouse was poorly advised. Lord Penrose in *Gillon v Gillon (No 1)* remarked that it would often be the case that a party who is advantaged by incompetent legal advice received by another party will be fully aware of the position. Bad advice is however not conclusive. In *Turner v Turner* 2009 Fam LR 124 Sheriff McCulloch held, contrary to a wife’s protestations, that parties’ solicitors had reached agreement and the fact that the wife may well have received poor quality or inadequate legal advice at the time and her interests may not have been fully protected, did not mean that the agreement was unfair or unreasonable. The issue had to be looked at “broadly and having regard to the factors and circumstances prevailing at the time…”

[6.4.2] A person cannot, or course, be forced to take legal advice, as emerges from the cautionary tale of *Inglis v Inglis* 1999 SLT (Sh Ct) 59. In that case both parties approached an Edinburgh solicitor, one Mr K MacAskill. He distinguished himself by keeping a note of their attendance and that the wife made it clear she did not wish to pursue a claim against her husband’s pension. After the meeting he wrote to her in very clear terms explaining that she had a potential claim for a capital sum based on her husband’s (unvalued) pension and advising her that if she had any doubts she should take independent legal advice. He raised this again with her in another letter. Nevertheless, she signed the agreement. Sheriff Farrell’s comment was,

“where a mature, intelligent adult in her sane senses, in receipt of the clearest warnings regarding the course of action which she proposes to follow, elects … to enter an agreement which, quite foreseeably, thereafter produced the financial disadvantage which it did in this case, then I see no basis for holding the agreement not to be fair and reasonable at the time it was entered into.”

The pursuer had renounced her claim in order to achieve the husband’s departure from the matrimonial home, so this was not merely a question of legal advice, but the clear warning issued by Mr MacAskill was relevant.

[6.5] *Are both parties in a fit state to make rational decisions?*

[6.5.1] This is where we move into the small print of section 16 cases. Aside from cases such as *MacDonald v MacDonald* 2009 FamLR 131 where there was an unacceptable level of coercion, there are only a limited number of successful applications for setting aside of agreements, but one such was *Short v Short* 1994 GWD 21-1300, which again involved Sheriff Farrell. The wife there had discharged all claims other than aliment pending sale of the matrimonial home, but she was suffering from a depressive illness to such a degree that it amounted to a nervous breakdown. She had not been in a fit state to make rational decisions on important matters. And the legal advice offered to her had been “poor”. She was awarded a capital sum. There was a similar result in *MacDonald v MacDonald* 2002 GWD 22-721, reported only in relation to the effect of failure to seek leave to appeal. The wife in that case had been seriously unwell and in no fit state to make decisions. However, a moderate depressive illness that affects concentration and memory may not, of itself, be decisive, particularly where a party has received good legal advice and is fully aware of the consequences of his or her actions (see *Anderson v Anderson* 2015 SC GLA 65).

[6.5.2] While the same principle could apply to pre-nuptial agreements, the reason for lack of rationality may be quite different. When a preliminary proof was first allowed in *Gillon v Gillon (No 1)* Lord Penrose said that it would be appropriate to look at all the circumstances prior to and at the time the agreement was entered into and relevant to its negotiation and execution to see whether there was some unfair or unconscionable advantage taken of some factor or some relationship between the parties. This involves the court considering whether the agreement was not truly entered into by one party or the other as a free agent.

[6.5.3] It would be interesting to argue that one side was blinded by love, but the argument might have to be much more practical. If the wedding announcement has been made, the dress purchased and the reception and honeymoon booked, then it may be extremely difficult to reject a pre-nuptial agreement. Timing may be highly significant. Every effort should be made to deal with an agreement well in advance of the wedding. That said, in my experience negotiations have a habit of extending to fill the time available and it may be possible to say that the issue of a pre-nuptial agreement was broached well in advance, with plenty of opportunity to delay or cancel the wedding. The argument may not be attractive. It will all depend on the circumstances.

**[7] Cross-border issues**

[7.1] Not all jurisdictions have the same approach to pre-nuptial agreements. In particular the English have had a significantly different approach. Pre-nuptial agreements that provided for the contingency of separation were historically viewed as contrary to public policy. It is still not possible to oust the jurisdiction of the court to make ancillary financial provision on dissolution of a marriage. This was explored by the UK Supreme Court in *Radmacher v Granatino* [2011] 1 AC 534. The Court came to the conclusion that pre-nuptial agreements should be given weight in affording ancillary relief. To carry full weight the parties must enter into an agreement of their own free will, without undue influence or pressure and informed of its implications. These considerations are not dissimilar to the test under section 16, but they relate to whether and how the agreement should be implemented, not the very different issue of whether it should be set aside. The English court may still grant ancillary relief to address issues of need and ‘compensation’ for economic advantage and disadvantage, notwithstanding a pre-nuptial agreement.

[7.2] If the parties are eventually divorced in England, then English law will apply. There are potential steps that can, at the moment, be taken to try and have Scots law applied. The first may be to insert a “choice of court” agreement. This is not binding in relation to divorce, but is binding on the issue of “maintenance” as Council Regulation (EU) no 4/2009 (the Maintenance Regulation) is binding between England and Scotland by virtue of the Civil Jurisdiction and Judgments (Maintenance) Regulations 2011 (SI 2011/1484). If the parties agree that maintenance shall be determined by the Scottish courts, then the Scottish courts will have exclusive jurisdiction under article 4 (provided the relevant connecting factors and other conditions are present). Maintenance covers all awards designed to enable a spouse to provide for himself or herself, or taking into consideration the needs and resources of each of the spouses, even if payable in the form of a lump sum or constituted as a transfer of property order (*Van den Boogaard v Laumen* [1997] QB 759). A choice of court agreement on maintenance will therefore generally cover financial provision, unless it relates solely to separation of property.

[7.3] It is not possible to choose the court for divorce, and the conflict of court provisions in Domicile and Matrimonial Proceedings Act 1973 say (in broad terms) that the court for the place the parties last lived together take priority (schedules 1 and 3, paragraph 8 in each schedule). There is no reported decision on how to deal with a case where priority for divorce is in a place that cannot deal with financial provision. It would however represent an effective deterrent to a spouse trying to raise an English action in order to seek more than was provided for in a pre-nuptial agreement if the English court did not have jurisdiction. It may also be possible to seek agreement not to raise divorce proceedings outwith Scotland, if a Scottish court has jurisdiction. This would give rise to interesting arguments about personal bar (or the English equivalent), but there are no guarantees as to success.

[7.4] The cross-border issues give rise to the potential for confusion, complexity and expense. Further, the choice of court argument turns on an EU Regulation, applied cross-border, and who knows what will happen to such measures post-Brexit.

**[8] Cohabitation agreements**

[8.1] The Family Law (Scotland) Act 2006 introduced certain rights for cohabitants. It is clearly possible to contract out of some rights. Section 26 sets out a presumption of a right to an equal share in household goods acquired (other than by gift or succession) during the period of cohabitation. The presumption is rebuttable and an agreement could be used to rebut the presumption. Section 27 provides for money derived from an allowance for joint household expenses or for similar purposes or for property acquired out of such money. Such money and property is to be treated as belonging to each cohabitant in equal shares, but this time there is express provision for agreements to the contrary.

[8.2] The most significant right is however probably that in section 28 which allows a cohabitant to claim financial provision. Given the Scots respect for agreements then it should be possible to exclude a claim for financial provision. In such a case there is no equivalent to section 16 allowing the agreement to be set aside if not fair and reasonable at the time it is entered into. It may only be reduced on the common law bases for challenging contracts, that is fraud, force and fear or facility and circumvention. The same would presumably apply to a discharge of a right to claim provision on death under section 29. The message to cohabitants is that if you contract in these areas, you are likely to be stuck with the terms of your agreement.

**[9] Conclusions**

Do pre-nuptial agreements or equivalent agreements for cohabitants exclude the possibility of something bad happening? Well it all depends. They may limit risk, but like all legal tools must be handled in an informed and intelligent manner, or they will themselves become a source of danger and result in loss in the form of expensive proceedings.