

June 2009

Court attempts to square the circle of ongoing periodical payments versus a clean break

Judgment was handed down by Charles J. on 18 June 2009 in the latest instalment of the case of *McFarlane*. Mrs McFarlane had applied to the court for an upward variation of periodical payments both for herself and for the children. This was a year after she had been awarded periodical payments of £250,000 per annum for herself by the House of Lords together with £20,000 child maintenance for each of the three children of the family, together with school fees.

The Facts

The history of this case is well known. The parties met at university and began to cohabit at the beginning of their respective training contracts as a solicitor (in the case of the wife) and an accountant (in the case of the husband). They qualified, and married, in 1984. Until 1990, when the husband became a partner in Touche Ross, the wife had earned the same as, or sometimes more than, the husband. In 1991 the parties agreed that the wife should give up work.

The wife petitioned for divorce in 2001, and was granted Decree Absolute in 2003, following which the husband remarried. The parties had, by the time of the first hearing, agreed a broadly 50/50 division of their capital assets of around £3m. The District Judge made a joint lives order for periodical payments from the husband's then net income of about £753,000 at a rate of £250,000 for the wife and £20,000 for each of the children, together with school fees. On appeal to the High Court, Bennett J. reduced the wife's periodical payments to £180,000, and these were re-instated at £250,000 by the Court of Appeal, which imposed a term of 5 years, albeit with no prohibition on the wife applying for an extension of that term in due course. That term was subsequently removed by the House of Lords in consequence of its decision that this was "a paradigm case for an award of compensation in respect of the significant future economic disparity sustained by the wife, arising from the way the parties conducted their marriage".

At the time of the hearing before Charles J, the husband and the wife had assets broadly similar at around £3.7m (the husband) and £3.8m (the wife), although the husband had the prospect of an annuity of £66,000 per annum from his firm at 2020 which had not been valued, and was said by him not to be completely certain. The wife's annual earnings were about £22,000 net, and she predicted that, following requalification in 2011 as a Patent and Trademark Attorney, her earnings would be between £46,000 and £58,000 net. The husband had been promoted to the highest level of equity partnership at Deloitte. His net earnings for the year ended 31 May 2008 were just under £1,110,000. The husband's second wife, with whom he has a 3 year old child, is also a partner at Deloitte, and plans to give up work in 2010.

The Issues

Charles J. looked at the differences between the effects of a continuing joint lives order for periodical payments; a term order and a term order with a bar on an extension to that term. He took the view that the last of these was effectively a deferred clean break.

The wife had submitted that the principles of needs, sharing and compensation should be considered separately, and that the highest result of the three should be adopted. The judge disagreed with this approach, taking the view that the assumption that each principle could be applied separately was misconceived, and that the approach was too formulaic.

The judge said that effectively both parties agreed that there was a surplus from the husband's income once his and the wife's day to day expenses and those of the children had been deducted, and what any particular application of that surplus, when taken together with the wife's own income and her other assets, would be likely to produce for her for the rest of her life. Therefore the structure of the award needed to apply, first, the need principle in order to identify the surplus income and secondly, an application of all three principles (bearing in mind the potential for overlap) to determine how that surplus should be applied between the parties.

The Decision

The judge took £150,000 as a reasonable figure for the annual income needs of each of the parties. Interestingly, he made no deduction for any contribution to the husband's needs by his second wife, also an equity partner at Deloitte, albeit not so senior. He put the needs of the children of the first marriage at £25,000 per annum each, index linked, and for such children as there may be of the husband's second marriage at £40,000, also index linked. School and university fees totalled about £21,000 and he made an allowance of £5,000 for miscellaneous expenses.

The judge considered that it would be reasonable for the wife to have an income of £150,000 per annum for the rest of her life. He could make a term order if he considered that during that term she could save enough to provide for herself a clean break Duxbury fund. However he made it clear that he could not be certain enough that his predictions would prove accurate to bar the wife from applying to extend the term in due course.

Following that comment, it is notable that the judge then used the Duxbury tables as his guide to an appropriate lump sum for the wife to have accumulated. Given the current very low rates of interest generated by investments, it could be argued that this assumption in itself might be capable of undermining the structure of the award and render any application for an extension of a term more likely to succeed. (The Duxbury calculations currently operate by amortising lump sums on the basis of a net rate of return of 3.75%)

The judge ordered a sliding scale of percentages of the husband's annual net income to be paid to the wife (40% up to £750,000, 20% thereafter up to £1m and 10% from then on). On the parties' respective income predictions this should, he calculated, enable the wife to save between £1.2 and £1.3m without any capital growth. This, coupled with a 25% downsizing from her current

property, would provide her with an appropriate continuing income for life. For this reason, he made a term order on the periodical payments. However, this was couched with a clear warning that if the income available to the wife from the capital that she should have been able to save between now and May 2015 together with the capital released from property downsizing was not between £120,000 and £150,000 per annum then that in itself would provide a justification for the wife potentially to extend the term beyond 2015.

Ramifications

There is a clear indication here that judges should, in high income but modest capital cases be looking toward a clean break. If Charles J.'s approach is followed, then judges will be doing their best to predict the level of savings that can be achieved from periodical payments at a particular level, how those savings will combine with property downsizing, and whether this total is likely to provide a recipient with enough capital to generate an income at the level that the judge considers appropriate.

The judgement also suggests that the current approach, under which there should be exceptional circumstances for a term order to be extended, may no longer be appropriate.

Although, therefore, there is an indication (probably welcome to paying husbands) that open ended maintenance awards greatly in excess of budgets are on the wane, this development should be treated with a degree of caution. The judge's decision is hedged with provisos, and obviously there are many issues that might arise within the term of a maintenance order that could completely wreck the financial edifice build up by the judge. These could include a significant change in interest rates, a fall in property values (meaning that the payee would raise less capital from a trade down), the recipient's inability to earn at the rate anticipated and the payer's income declining.

As a side issue, Charles J.'s orders for child maintenance, making provision for the children both during gap years and for M.A. courses following their first degrees, remind us that the conventional approach of maintenance "to end of first degree" is not enshrined in statute.

Although ostensibly good news for paying parties, this decision raises a number of spectres. Certainly if this case is followed, high earners may expect to be parting with more sizeable sums from their net incomes over comparatively short periods to enable to recipient to save for a clean break reasonably quickly. What, though, if the judge's sums are proved wrong? Moreover, how will a judge in the future react if, rather than saving the excess income over needs, a recipient overspends? Is a court really likely to impose a clean break although the recipient clearly has insufficient to fund a proper level of income for the future from capital?

Once again, an attempt by a judge to give clear guidance may have resulted in yet more uncertainty. Does this judgement mean that if an award of maintenance exceeding the recipient's 'needs' is made, the surplus must be saved towards a clean break? If the clean break is to be achieved once the recipient has enough capital to provide for his or her reasonable needs, then where, in reality, has the 'compensation' or 'sharing' element of the maintenance gone?

Contact

If you have any queries or require any further information, please do not hesitate to contact:

James Freeman

Partner, Family

020 7427 6584

james.freeman@speechlys.com

Christopher Butler

Partner and Head of Family

020 7427 6618

christopher.butler@speechlys.com

John Nicholson

Partner, Family

020 7427 6548

john.nicholson@speechlys.com

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