



THREE IMPORTANT THINGS YOU NEED TO KNOW ABOUT TAX AND FAMILY LAW

PROPERTY SETTLEMENTS

There are many issues where tax impacts upon a family law property settlement. In my experience, the following three are some of the most important and/or overlooked problems that arise when parties are looking at finalising their property settlement:-

- 1. Tax which has not yet been realised (for example, capital gains tax on an investment property) will not be taken up as a liability by the Federal Circuit and Family Court (“the Court”) unless the sale of that investment property is required pursuant to the Orders or in the event the sale is inevitable in the very near future**

In other words, when parties are affecting a property settlement, there can be many assets which are “*impregnated*” with taxes. Retained earnings within a company, capital gains tax, tax on the winding-up of a business etc. are but a few of examples where this latent tax may exist.

It is real, but the Court will not take it up as a liability unless the tax is:

- incurred before the settlement; or
- incurred as a result of the settlement; or
- incurred as part of the settlement; or
- inevitable that it will be incurred in the very near future.

Therefore, for example, if you have substantial retained earnings in a company and you are going through a divorce, do not expect the Court to take-up the tax on the future declaration of a dividend when it hasn’t yet occurred or to take up the capital gains tax on a property you don’t intend to sell in the foreseeable future.

- 2. Ensure that Family Court Orders properly account for all incidents of tax**

Often, parties will propose Orders that split their estate in a certain percentage (for example 50 / 50). It is important that you make sure that the taxation

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You should seek legal advice or other professional advice in relation to any particular and specific matters you may have.



consequents of those Orders and where the tax falls are taken into account when negotiating any Orders with the other side or putting Orders up for approval by the Court. Technically, tax liabilities that have not yet been incurred are not regarded as “*liabilities*” but the failure to take up these tax liabilities in an Order can lead to an Order being not “*just and equitable*”.

Therefore, if you fail to take up tax in your share of the assets that you are retaining (when doing the percentage split) this may lead to the Orders not being what you intended them to be.

3. **Don't forget the relevance of tax remaining on assets you receive as part of your property settlement**

Even though the Court will not take up as a mathematical calculation the future tax that may be incurred on some asset you retain (for example, the future capital gains tax on the sale of your investment property) doesn't mean that you should ignore the consequences of that tax when dealing with your solicitor and accountant in a family law financial settlement.

If you are receiving a settlement that has assets that are heavily impregnated with taxation consequences for the future, then your accountant and family lawyer should be working closely with you to calculate notionally the nature and impact of those taxes.

Whilst those taxes would not be deducted dollar for dollar by the Court, there is good reason that an amount, by way of adjustment, could be agreed in negotiations as part of reaching a settlement in good faith. Alternatively, if argued in Court, the incident and size of such latent or impregnated taxes can still be relevant under another section of the *Family Law Act* when the Court happens to make adjustments.

In other words, a dollar for dollar amount is not deducted from the pool but, in some cases, the Court may make a small percentage adjustment in favour of the party who bears the greater future burden of taxation liabilities.

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In all financial property settlement matters you should work closely with your accountant and divorce lawyer. Good divorce lawyers need the assistance of good accountants to help advise their clients on these important issues.

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