CONTRACTING OUT RULES FOR FAMILY INCOME SHARING ARRANGEMENTS: PROVIDING CERTAINTY AND PROTECTING THE VULNERABLE

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Despite equal division of assets at the end of a relationship, residual economic disparity often remains. This is especially common when one partner has left the workforce to care for children. Addressing such divergent economic prospects at the end of long-term relationships has been a perennial policy challenge. In 2019, the Law Commission completed its review of the Property (Relationships) Act 1976 (PRA). The Commission recommended replacing the current economic disparity compensation and maintenance regimes with an income pooling mechanism: Family Income Sharing Arrangements (FISAs). It also recommended that couples be able to contract out of FISAs. This article explores the rationale for changing the current regime and the conceptual underpinnings of the proposed FISA regime, using human capital as a framework. The article proposes a detailed policy regime for FISA contracting out. The proposed rules consider the needs of couples with children, where a partner has left the labour force, or where lived reality has not met the couple’s ex ante expectations. The resulting rules meet the policy goal of allowing couples to contract out of FISAs, but only where their contract causes no hardship. Additional disclosure is also recommended for contracting out of the other provisions of the PRA, with greater deference recommended for such private arrangements as a result.

I INTRODUCTION

Earning capacity is a function of a person’s human capital. Human capital is defined as the monetary value of a person’s knowledge, skills, and abilities. In practical terms, it is most often assessed through qualifications and career building. Family finances in New Zealand are dominated

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by two types of assets: capital tied up in housing, and human capital. Along with the other countries of the Organisation for Economic Cooperation and Development (OECD), New Zealand has a high level of human capital, a result of the dramatic expansion of higher education since the 1970s:¹

Figure 1:

![Diagram of Human and Physical Capital Stocks](image)

The current regime for dividing family property on separation is set out in the Property (Relationships) Act 1976 (PRA), which, in its current incarnation, was the result of a reform implemented in 2001. The PRA divides relationship property equally.

When there is a mismatch in human capital at the end of the relationship, this can lead to inequitable financial prospects. There are two mechanisms in the current law to address this problem: these are s 15 and s 15A of the PRA. These sections deal with economic disadvantage and the maintenance regime under the Family Proceedings Act 1980. As explained at section III below, these provisions are not proving effective to deliver substantial equality, and so require major change.

In its 2019 report on the PRA, the Law Commission made proposals to change the treatment of human capital by implementing a limited form of human capital pooling. Earnings are pooled for up to five years from the end of certain qualifying relationships. This scheme is called FISA: Family Income Sharing Arrangements. The proposals include the possibility for the couple to contract out of FISAs.

¹ Ministry for Culture and Heritage “University enrolments, 1900–2010” <www.teara.govt.nz>; for Figure 1 see Thi Van Trinh Le “Estimating the Monetary Value of the Stock of Human Capital for New Zealand” (PhD Thesis, University of Canterbury, 2006) at Table 4.8 Human and physical capital stocks.
This article analyses the policy scaffolding of the FISA proposal using a human capital lens and goes on to examine how contracting out applies to relationship property. Recommendations are then made for a bespoke contracting out regime to address the issues unique to the FISA scheme.

II CURRENT CLASSIFICATION AND POOLING RULES

A Context and History of Law Commission Report

New Zealand’s relationship property regime dates from 1976, with a major reform in 2001. The 1976 PRA introduced equal sharing of the family home and other "matrimonial property". The 2001 reforms included de facto relationships for the first time and changed the terminology from "matrimonial property" to "relationship property". Part of the policy of the 1976 PRA was that couples could decide to opt out.2 The opt-out provisions are now found in pt 6 of the PRA. While the majority of the provisions relevant to couples are in the PRA, maintenance is found in the Family Proceedings Act 1980 and the Child Support Act 1991.

The Law Commission was asked to review the regime in 2016. It then released an issues paper in 2017, along with a study paper which described the social context.3 These were followed by a preferred approach paper in 2018,4 and a final report in 2019.5

The Law Commission recommended that succession laws also be reviewed. The Government accepted that recommendation, and so full Government consideration of the final report is waiting for that review to conclude.

B Income and Capital Distribution in Relationships: The Policy Problem

To apply an aquatic metaphor to relationships, assets can be conceptualised as "levels", and income can be conceptualised as "flows". The current regime is focused on levels. With some exceptions, most notably the family home and chattels, the increase in the level of assets during the relationship is the relationship property that is shared equally. This is described as sharing the fruits of the relationship.6

The family home and chattels are shared equally under the current regime. Under the proposed regime, the family chattels would continue to be shared equally. However, where one partner had

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6 At [3.15].
owned the home before the relationship began, the family home rule would change so that only the increase in value would be shared. This model is sometimes referred to as "community of surplus".\(^7\) This aligns the family home to the "increase in levels" approach. There are exceptions to these rules which I do not expand on in this article.

Leaving aside the maintenance provisions of the Family Proceedings Act 1980 and s 15 and s 15A of the PRA, the remainder of the regime is not particularly concerned with "flows" of money, that is, income.

To an economist, an ongoing flow of money is an asset with a definable net present value. A share in a publicly traded firm, for example, can be priced as an entitlement to share in the future profit stream of that firm.

In \(Z v Z\) (No 2), decided under the Matrimonial Property Act 1976, it was expected that the husband’s future income would be $300,000 per year, while the wife’s income would be $7,000 per year.\(^8\) The Court accepted that property had a wider meaning as the Act was "social legislation",\(^9\) but it did not accept the wife’s argument that enhanced earning capacity could be matrimonial property that was subject to equal sharing.\(^10\) The Court held that, although an unjust result would follow, "expanding the definition of property to include a husband’s increased earning capacity would be a radical departure from the conventional concept which Parliament chose to endorse".\(^11\) The only exception to this is where the earning capacity is captured by a legal interest which can fall within the definition of property; it applied in this case to the husband’s interest in an accounting partnership.\(^12\)

\(Z v Z\) (No 2) was decided before the 2001 reforms. Since this judgment, the purposes of the PRA have changed to include "the principle that a just division of relationship property has regard to the economic advantages or disadvantages to the spouses or partners arising from their [relationship]".\(^13\) Specific provisions have also been added to allow claims to be made to address such advantages or

\(^{7}\) Report of the Working Group on Matrimonial Property and Family Protection (Department of Justice, 1988) at 15.

\(^{8}\) Z v Z (No 2) [1997] 2 NZLR 258 (CA) at 276.

\(^{9}\) At 263.

\(^{10}\) At 264.

\(^{11}\) At 264.

\(^{12}\) At 265.

\(^{13}\) Property (Relationships) Act 1976, 1N(c).
disadvantages.\textsuperscript{14} Atkin has argued that these changes justify re-examining the finding that increased earning capacity cannot be relationship property.\textsuperscript{15}

Such an argument runs counter to the legislative history of the PRA. One of the two select committee reports that led to the 2001 amendments to the PRA addressed the "economic disadvantage suffered by the non-career spouse" and saw three options to redress it: (1) allow for unequal sharing of matrimonial property; (2) treat human capital as matrimonial property; or (3) address the issue through spousal maintenance.\textsuperscript{16} The report records that one member of the committee favoured approach (2), of treating human capital as matrimonial property, but this was not the majority view.\textsuperscript{17} Instead, the Committee liaised with the Minister and was assured that a supplementary order paper would be introduced which would follow approach (3), by enhancing the maintenance provisions of the Family Proceedings Act to address the issue. After a change of Minister and the merger of the reform proposals for de facto relationships and marriages, the final shape of the reform was approach (1).\textsuperscript{18} This was effected through the introduction of ss 15 and 15A of the Act, discussed in the next section of this article.

The Law Commission's 2019 FISA proposals cleave most closely to approach (3), as FISA is based on earnings over time. This is discussed further at section \textsuperscript{V} The FISA Proposals below.

\section*{III CURRENT ECONOMIC DISPARITY AND MAINTENANCE PROVISIONS}

As set out in the preceding section, s 15 of the current PRA resulted from a process that considered three options to address prospective disparities at the end of a relationship: treating earning capacity as capital; adjusting ongoing maintenance; or (as selected) adjusting the pool of relationship property to account for a disparity in future earnings.

As Peart and Henaghan put it, "by including a compensation provision for economic disparity, [the 2001 amendments sought] to include earning capacity as human capital to be shared."\textsuperscript{19} This quote helps to illustrate the fact that the three approaches are economically equivalent, although the details of how the mechanism is explained and implemented can have crucial implications.

\textsuperscript{14} Sections 15 and 15A.
\textsuperscript{15} Bill Atkin "What Kind of Property Is Relationship Property" (2016) 47 VUWLR 345 at 357.
\textsuperscript{16} Matrimonial Property Amendment Bill (109–2) (select committee report) at xiv.
\textsuperscript{17} The Labour members in the minority used the term "career capital", at xx.
\textsuperscript{18} Margaret Wilson "Policy and law in the development of relationship property legislation in New Zealand" (2017) 15 Otago LR 89 at 97.
\textsuperscript{19} Nicola Peart and Mark Henaghan "Children's Interests in Division of Property on Relationship Breakdown" in Jessica Palmer and others (eds) \textit{Law and Policy in Modern Family Finance: Property Division in the 21st Century} (Intersentia, Cambridge, 2017) 65 at 90.
Under the introduced s 15, compensation through unequal division of relationship property is available where after the relationship:

… the income and living standards of one spouse or partner (party B) are likely to be significantly higher than the other spouse or partner (party A) because of the effects of the division of functions within the [relationship].

Section 15A deals with situations where, in similar circumstances to those covered by s 15, the value of separate property has increased. In this case, compensation can be awarded from the separate property. This is similar to s 15 and this article does not focus on it further.

The paradigmatic situation in the minds of the legislature can be seen from the Hon Margaret Wilson’s introduction speech for the Bill:20

I have received details of many case studies illustrating the serious injustices that can occur under the current law. Many of them also demonstrate a recurrent pattern. Women are left, after long-term relationships, some of which have lasted as long as 35 years or 40 years, with very few assets and few employable skills.

After 20 years, s 15 has failed to deliver justice in the situations that the Minister described. Section 15 is "unpredictable, inefficient, and expensive to enforce".21 In Scott v Williams, the leading case on s 15, Arnold J held that s 15 "has not lived up to expectations",22 and Elias CJ concurred that it "cannot be accounted to have been successful in meeting its purpose".23

The main problems with s 15 have been the linked issues of quantum and causation. Quantum asks how much should be awarded to compensate for the expected disparity, which in turn raises the causation question: how much of the disparity, if any, was caused by the division of functions within the relationship? For example, if a nurse and a surgeon marry, at the end of their marriage, little of their disparity in future earnings will be "because of the effects of the division of functions" in their relationship.24 Instead, it will primarily be because surgeons have extraordinary earning power, while nurses do not, and this is persistent over time despite any division of functions.

For a relationship structured along 'traditional lines' where the parties started with comparable economic advantages, as in Scott v Williams, there is now an assumption that all of the disparity that

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23 At [351].
follows from the relationship results from the division of functions. However, as both working and family lives become more diverse, this will provide an answer for a shrinking subset of the separating population.

The economic disparity provisions are supplemented by the maintenance regime under the Family Proceedings Act 1980 which makes one partner liable to meet the "reasonable needs" of the other partner where their ability to meet those needs is adversely affected by circumstances within the relationship. Those circumstances include care of children, any need for re-training before entering the workforce, and the "division of functions" within the relationship. The recipient partner must "assume responsibility for [their] own needs within reasonable time". Maintenance takes into account means that are derived from dividing the relationship property.

Maintenance awards are:

based on needs rather than earning disparities and obscure drafting leaves us guessing as to what needs will be met by maintenance payments and how long maintenance liability will linger.

Reviewing the combined effect of the Property (Relationships) Act and the Family Proceedings Act, Peart and Henaghan conclude that:

… there is an inevitable tension between family obligations and property entitlements. The PRA tips the balance firmly towards property.

This imbalance is exacerbated by the fragmented approach to the consequences of a relationship breakdown.

The Child Support Act 1991 sits outside these two statutes and has a complex inter-relationship with them. For example, an occupation order under the Property (Relationships) Act may affect child support entitlements. Surveying the overall legislative picture, Peart and Henaghan conclude that each statute has its own principles. There is no coherent and consistent set of principles to govern the consequences of a relationship breakdown.

25 Scott v Williams at [204] per Glazebrook J, [345] per Elias CJ, and [293] and [323] per Arnold J.
28 Section 64A.
30 Peart and Henaghan, above n 19, at 90.
31 At 90–91.
IV THEORY AND POLICY OF POOLING HUMAN CAPITAL

Whether effected through maintenance, unequal sharing, or explicit valuation of "career capital", the rationale for pooling and dividing human capital is that its accumulation is gendered and shaped by family roles:32

… the common pattern remains for women and men as parents to make differential life-course investments, with fathers’ primary investment being in the marketplace of career or self-employed business, while women's life investments are more diversified, and include a major orientation towards the care of children. … [I]f the relationship breaks down, then she loses out in her investment in her partner's earning capacity if her role is not compensated in some way through a property settlement and/or maintenance.

The Law Commission confirms that contemporary data validate that women continue to disproportionately shoulder the burden of child raising, with corresponding costs for their careers.33 This establishes the need for an effective legislative mechanism to address human capital inequities, through a form of human capital pooling. I use “human capital pooling” here as a generic term which captures the three main policy alternatives: compensation through the division of property of the relationship or the other partner; valuation and division of "career capital"; or maintenance.

The Law Commission warns against conflating “meeting needs” and compensation for disparity caused by the division of functions.34 However, its advancement of FISAs does precisely that, as such “financial reconciliation orders” are a "hybrid of compensating loss and meeting needs”.35

To simplify somewhat, where causation is clear-cut, a s 15 award using Arnold J’s Scott v Williams methodology is calculated by taking the actual discrepancy between the future incomes of the parties, assigning a present value to it (which requires choosing a duration and contingency factors), and then awarding half the resulting figure as compensation.36 This approach aligns unequal division of relationship property very closely with the career capital approach: An award under a "career capital” approach would be calculated (assuming a zero starting position) by looking at the differences in net present value of the projected income stream of each spouse.

34 At [18.78].
35 At [19.5].
The situation with maintenance is somewhat different. Maintenance historically stems from a husband’s moral duty to provide for his wife’s needs. Maintenance orders cease to have effect if the disadvantaged partner commences a new relationship. Given that a party must have shown by this point that their own ability to meet their reasonable needs was caused by the division of functions within the prior relationship or other related causes, such as the care of children of that relationship, the fact that maintenance ceases on re-partnering may seem to be an offensive infringement of individual autonomy. However, if the justification for providing the disadvantaged partner with a share of ongoing earnings is that they had an expectation to continue sharing in the fruits of the previous relationship, the logical conclusion is that when they are in a new and equivalent relationship, they no longer have a loss to be compensated for. After all, their partner’s income is relationship property that they will share in, at least when their relationship becomes a qualifying relationship.

The endowment effect, or “prospect theory”, is an important factor to consider in policy design. A system which creates an automatic entitlement, which may then be challenged by the paying party, puts the recipient in a position of defending an entitlement that they already have. By contrast, if the recipient must prove their entitlement, as with maintenance and s 15 orders, they bargain from nothing. The endowment effect holds that people are relatively more motivated to retain what they already have than to acquire the same thing from a zero base. Accordingly, "only the grant of clearer legal rights to a given share in the resources can level the playing field for private settlement.”

Notably, this is achieved in Canada by the wide acceptance of entitlements calculated using published guidelines.

V THE FISA PROPOSALS

The Law Commission’s final report on the PRA recommends abolishing maintenance and the economic disparity provisions and replacing them with a hybrid regime of financial reconciliation orders known as FISAs: Family Income Sharing Arrangements. It also recommends that couples be able to contract out of the FISA regime. The policy implementation details described in the report have not reached the stage of legal drafting, and so, some uncertainties remain. This section will

37 Atkin and Henaghan, above n 29, at 180.
38 Family Proceedings Act 1980, s 70A.
describe the shape of the FISA policy, with a focus on those aspects that are relevant to issues around contracting out.

FISAs represent nearly a full swing of the pendulum from "discretion" to "rules". The current provisions for economic disparity and maintenance are hard to access and are plagued with expense and complexity. The complexity results from the need to prove that the disparity, or need for maintenance, was caused by the division of functions within the relationship. FISAs are instead designed to largely be activated by objectively ascertainable and non-controversial factual criteria. Instead of requiring that the applicant prove causation, two broad rubrics are introduced that act as proxies for causation: that the partners had a child together, or that the relationship had a minimum ten-year duration. There is also a wider category that:

   during the relationship:

(i) Partner A stopped, reduced or did not ever undertake paid work, took a lesser paying job or declined a promotion or other career advancement opportunity in order to make contributions to the relationship; or

(ii) Partner B was enabled to undertake training, education and/or other career sustaining or advancing opportunities due to the contributions of Partner A to the relationship.

While this category may seem to reintroduce a requirement for causation, the Law Commission anticipates that, because of the reverse onus, usually the mere presence of the events will suffice – for example, the fact that the higher-earning partner undertook training during the relationship.

The duration of a FISA will be a maximum of five years, determined as half the duration of the relationship. The amount payable will be calculated as if each party’s pre-separation income for the final three years of the relationship continues unchanged, at a rate that means the income would be equalised in the first year, and then diminishes from that point. Either party will be able to seek a departure from the formula assessment if applying the formula would give rise to serious injustice, which the Court would assess using a non-exclusive list of statutory criteria.

Policymakers must choose between targeting individualised justice, at the cost of the remedy being more expensive and less accessible; and maximising the overall efficiency of the system by

43 At [10.85].
44 At [R53].
45 At [10.103].
46 At [10.64].
47 At [10.117].
choosing accessible rules-based implementation, accepting that injustice for some is the cost of greater accessibility for all. The FISA regime will bring post-relationship human capital sharing within the reach of many more couples than the current proposals.

Prima facie, it is unjust to require a payment from one party to the other unless compensation is earned. That is, where the paying party must bear responsibility for the prospective difference in living standards because such difference was caused by the division of functions in the relationship, which the paying party consented to at least tacitly. Where FISA will create liability without the payment being "earned", that is a failure to provide justice to the individual. However, as Miles argues:

… substantive economic equality is proving too difficult to operationalise by way of judicial discretion. Some new mechanism is needed.

Inevitably, the nettle of average, rather than individualised, justice must be grasped.

The premise of the FISA scheme is that the injustice that results from providing entitlement in a limited number of cases where there is not true causation is to be weighed in the balance against the greater average justice delivered by the greater efficiency and lower cost of a strict rules-based regime.

The Law Commission proposes that couples be able to contract out of the FISA regime, which is addressed in the next section.

VI CONTRACTING OUT

A Theory and International Perspective

Should partners be able to make their own agreements as an alternative to the default relationship property regime? There is an inescapable tension between upholding the right to autonomy and the need to protect the vulnerable.

And what of love? The great poets assure us that love begins with a temporary madness. While it would not be wise for jurists to try and measure such a notoriously variable and deeply subjective phenomenon, love has profound relevance to agreements to contract out of the Act. The Law Commission cites the Law Commission for England and Wales' observation that "people in love may have a firm belief that the relationship will never end." For the legislative scheme to require a level of cynicism and self-interest that is fundamentally at odds with building a strong relationship is wrong-

48 Miles, above n 40, at 290.

49 Law Commission, Review of the Property (Relationships) Act 1976, above n 5, at [R57].

headed as it will systematically confer advantages on the more cynical party. More formally, Scherpe quotes the American Law Institute:\textsuperscript{51}

These distinctive expectations that persons planning to marry usually have about one another can disarm their capacity for self-protective judgement, or their inclination to exercise it, as compared to parties negotiating commercial agreements.

The ability of the partners to contract out of the matrimonial property regime in New Zealand, and later the relationship property regime, has been present since the regime’s inception. That the 1976 regime allowed ‘opting out’ was an important element of its social acceptance.\textsuperscript{52} The continuing need for contracting out was accepted by the 1988 Working Group,\textsuperscript{53} and was not seriously challenged in the 2001 reform process or the Law Commission’s recent review process.\textsuperscript{54}

Jens Scherpe notes that the extent to which regimes embrace contracting out is closely linked to their underlying rules.\textsuperscript{55} For example, the Netherlands has an immediate full community of property system, which means that marriage has unusually radical consequences, but contracting out of the system is common as a result.\textsuperscript{56}

Internationally, Scherpe describes that a common pattern is discernible when courts scrutinise contracting out agreements: a “protection of autonomy” stage; and then a “protection from autonomy” stage.\textsuperscript{57} The protection of autonomy stage is directed at the formal and procedural aspects. The enquiry usually has advice, disclosure, and time requirements.\textsuperscript{58} At the end of this enquiry we can say that the agreement was entered into "willingly, consciously, and with sufficient information about its consequences".\textsuperscript{59} After that, the substantive protection from autonomy enquiry begins.


\textsuperscript{52} Law Commission Dividing Relationship Property – Time for Change?, above n 3, at [30.11].

\textsuperscript{53} Department of Justice, above n 7, at 37.


\textsuperscript{55} Scherpe, above n 51, at 363.

\textsuperscript{56} At 363.

\textsuperscript{57} At 388.

\textsuperscript{58} At 388.

\textsuperscript{59} At 388.
B New Zealand’s Initial Requirements: Procedure and Disclosures

In the New Zealand regime, the protection of autonomy provisions are found in s 21D of the Act, which provide that agreements may stipulate how property is divided and which property is joint and which is separate property.

The primary procedural requirements are found in s 21F which provides that each party must receive independent advice about the effect and implications of the agreement from the lawyer who witnesses its execution. Section 21G provides that these requirements are cumulative to other legal and equitable avenues for setting aside agreements. This means that even if procedural requirements have been met, the court can set an agreement aside on generic contract law grounds, such as undue influence.60

Boyd v van Houten61 in which one party did not know the relationship was at an end, implies that in extreme cases withholding material matters can invalidate an agreement. The lack of an explicit disclosure requirement is a notable omission from the New Zealand provisions when compared with the principles applying to agreements between spouses propagated by the Commission on European Family Law (CEFL).62 In New Zealand, even when one partner is unwilling to provide full disclosure, this does not prevent the requirements of s 21F being met.63

The result of the initial protection of autonomy checks can be ascertained as soon as the contracting agreement has been made. The second stage, protection from autonomy, is an evaluation at the time that one partner seeks to rely on the agreement of whether it is appropriate for it to be upheld and applied by the Court.

C New Zealand Substantive Requirements: the "Serious Injustice" Question

Any contract entered into near the start of a relationship, or at any stage where there is still a mutual commitment to a future shared life, is an agreement "about an uncertain future".64 Because, in New Zealand, a de facto relationship that precedes a marriage is included as part of the same relationship for relationship property reasons, few contracting out agreements are genuinely made prior to the relationship. However, they may well be made around events that have property

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60 David Neild "Using Duress, Undue Influence and Unconscionable Bargain to Set Aside Relationship Property Agreements" (2014) 8 NZFLJ 10.
64 Scherpe, above n 51, at 388.
consequences, such as a marriage. As an agreement may be made at any time prior to or during the relationship,\textsuperscript{65} whether a qualifying relationship has commenced is generally not significant. Although, as discussed at Boyd above, the quantum of accrued entitlements at the time an agreement is entered into may be relevant.

The central question at this stage of the enquiry is whether giving effect to the agreement would give rise to serious injustice. Before the 2001 reforms, this threshold was merely "injustice".\textsuperscript{56} The 'serious injustice' threshold is the same level set in the CEFL's Principles of European Family Law Regarding the Property, Maintenance and Succession Rights of Couples in De Facto Unions, principle 5.9.\textsuperscript{67} It is one step below the corresponding principle for spouses where the threshold is "exceptional hardship".\textsuperscript{68} This is because the CEFL principles for de facto relationships do not have procedural requirements, such as external legal advice,\textsuperscript{69} while the principles for agreements between spouses do require such advice.\textsuperscript{70}

In considering "serious injustice", section 21J (4) of the Act requires the courts to have regard to:

(a) the provisions of the agreement:
(b) the length of time since the agreement was made:
(c) whether the agreement was unfair or unreasonable in the light of all the circumstances at the time it was made:
(d) whether the agreement has become unfair or unreasonable in the light of any changes in circumstances since it was made (whether or not those changes were foreseen by the parties):
(e) the fact that the parties wished to achieve certainty as to the status, ownership, and division of property by entering into the agreement:
(f) any other matters that the court considers relevant.

The leading case is Harrison v Harrison,\textsuperscript{71} which emphasised the greater value that Parliament had placed on certainty by adding subs (4)(e) and changing the threshold from "injustice" to "serious

\textsuperscript{65} Property (Relationships) Act 1976, s 21.
\textsuperscript{67} Maarit Jänterä-Jareborg and others Principles of European Family Law Regarding Property, Maintenance and Succession Rights of Couples in De Facto Unions (Intersentia, Cambridge, 2019).
\textsuperscript{68} Boele-Woelki and others, above n 62, at 348.
\textsuperscript{70} Boele-Woelki and others, above n 62, at 347.
\textsuperscript{71} Harrison v Harrison [2005] 2 NZLR 349 (CA).
injustice” in the 2001 amendment. The Court approvingly cited Wood v Wood for the proposition that parties are free to agree quite different arrangements from the default under the PRA; the intention was not for all to be consigned to the “same Procrustean bed”. The Court held that refusal to reconcile unless the agreement was entered into was not illegitimate pressure.

Courts cannot set aside a contracting out agreement in part. That is, if an agreement is mostly appropriate for the partners’ circumstances and just, but had one provision that would cause serious injustice, a court cannot set aside that one provision only. This has some benefits, in that a court cannot unpick a bargain struck between the parties that traded off various components of the regime. However, a court having the power to strike out unjust provisions while otherwise upholding the agreement, may increase the likelihood that property is divided substantially according to the contracted scheme. The Law Commission has proposed that courts will, in future, have the power to set aside agreements in part.

Fisher argues that agreements are most likely to be upheld if they follow the principles of the “fruits of the relationship” model, and only reserve “externally sourced assets” from sharing. By contrast, if they spurn the concept of community property altogether and attempt to reserve all the assets legally owned by a party as that party’s separate property, they are likely to be set aside unless there is significant value also going to the other party. Such an agreement, preserving separate legal title, would be completely acceptable as a marital agreement in a typical civil law system; but the context would be very different there as the regimes are not ‘deferred’ community systems and so the agreements also regulate title inside marriage.

VII THE FISA REGIME: CONTRACTING OUT
A On or After Separation

The Law Commission’s proposals contemplate the partners making an agreement that would substitute for the FISA on separation or after separation. These agreements are settlement agreements.
agreements and safeguards are proposed to protect people from bad bargains.\textsuperscript{79} These settlement agreements can also be set aside if they would cause serious injustice.\textsuperscript{80}

\textbf{B At a Date Prior to Separation}

FISA is designed to replace both s 15 compensation for relationship-caused economic disparity under the PRA and maintenance under the Family Proceedings Act 1980. There is "significant uncertainty" about whether s 15 is able to be contracted out of,\textsuperscript{81} but it seems that it is usually regarded as within the scope of s 21D.\textsuperscript{82}

Maintenance, conversely, cannot be contracted out of.\textsuperscript{83} Child support, which also cannot be contracted out of,\textsuperscript{84} sits to one side. However, pt 3 of the Child Support Act 1991 provides for voluntary agreements for either domestic maintenance or child support.\textsuperscript{85} If an agreement is submitted to the Inland Revenue Department and accepted by it, the agreement determines the rate payable and can be administered by Inland Revenue.\textsuperscript{86} However, such voluntary agreements can be terminated unilaterally,\textsuperscript{87} so they serve more as administrative mechanisms to effect payment than true contracting out agreements.

The FISA regime was conceived relatively late in the Law Commission's review of the PRA. In its issues paper, only the broad outlines were provided and contracting out was not mentioned. At the Preferred Approach Paper stage, the Law Commission clearly set out that partners should be able to "contract out of the FISA provisions before or during a relationship under section 21".\textsuperscript{88} However, little reasoning was provided.

\textsuperscript{79} At [10.127].
\textsuperscript{80} At [10.128].
\textsuperscript{81} Law Commission \textit{Dividing Relationship Property – Time for Change?}, above n 3, at [30.54].
\textsuperscript{83} Law Commission \textit{Review of the Property (Relationships) Act 1976}, above n 5, at [10.135].
\textsuperscript{84} At [10.135].
\textsuperscript{85} Child Support Act 1991, s 47.
\textsuperscript{86} Section 58.
\textsuperscript{87} Section 64.
The Commission noted that:89

A contracting out agreement that deals with an entitlement to a FISA may be vulnerable to a challenge on the ground that giving effect to the agreement would cause serious injustice, if the partners' circumstances have changed since the agreement was made (section 21J). We are satisfied that section 21J provides an appropriate safeguard given the inevitable uncertainty in seeking to predict the future.

The Commission reported that the correct response to that was to encourage partners to:90

… revisit their agreement throughout the relationship and at key life events, such as when the partners start planning or having children together, when the relationship passes the 10 year mark, and when the partners are contemplating decisions that would significantly affect one partner’s earning capacity (such as the partners moving countries in order for one partner to take up a new job).

As observed earlier, s 15 claims have been characterised by high degrees of evidential complexity as they require an evaluation of the future earnings of each party. Such evaluation naturally becomes more complex as the interval being predicted gets longer. With respect to the Commission, it strains credibility that partners will have the inclination or capacity to undertake such a prospective analysis at each major life juncture and will then reflect their updated analysis each time in an updated s 21 agreement at a cost of thousands of dollars.

Scherpe surveys the rules on maintenance in a range of jurisdictions and concludes that in default regimes, after a relationship ends “there appears to be general agreement that the 'needs' of a spouse ought to be covered [by the other partner].”91 Relationship-caused economic disparity is often addressed through a generous interpretation of "needs".92 Turning to contracting out rules, Scherpe describes the core of obligations as those that cannot be contracted out of, and concludes that:93

maintenance obligations because of needs arising from ongoing child care, or old age and infirmity are deemed to be closest to the core and thus, in practice, are almost impossible to contract out of.

Consistently with these observations, as noted above, maintenance cannot be contracted out of in New Zealand.

In Australia, contracting out agreements, called "financial agreements", can address maintenance.94 The second stage "protection from autonomy” evaluation includes the ground that "a

89 At [5.110].
90 At [5.111].
91 Scherpe, above n 51, at 381.
92 At 381.
93 At 390.
94 Family Law Act 1975 (Cth), s 90E.
subsequent material change of circumstances affecting a child’s welfare such that the child or the caretaking parent would suffer hardship if the agreement is not set aside”.95

The waters are muddied in New Zealand by the courts’ view that the needs of children are “plainly” to be met via the Child Support Act 1991, not via adult maintenance,96 and so “the purpose of adult maintenance is not to boost the children’s financial well-being”.97 The Law Commission, however, reports that the “inadequacies of the child support regime” mean that children still add to financial need.98

Children are a source of radical uncertainty in any relationship. The demands that children make on their parents vary dramatically both between children, and over time for the same child. Before parenthood, people are notoriously unable to anticipate what the reality of parenting will be like.

The Law Society is of the view that FISAs should not be able to be contracted out of, because:99

… women in that paradigm rarely appreciate or anticipate the economic effects of bringing up children within a relationship, or ceasing work to support a travelling spouse, or the economic position of each party some years in the future.

Reviewing the same issues, retired High Court judge John Priestley concludes that “there were strong public policy grounds which prohibited a married person being able to contract out of spousal or child maintenance obligations. A FISA, however, is a new animal!”100

Priestley goes on to say that contracting out of FISAs should be permitted, but that the “only justification for curtailing the right to contract out” is the interests of children, in which case contracting out should be void as a matter of public policy.

In Austria, “anticipatory contracts concerning possible divorce maintenance” are permissible. Key concepts are the "clausula rebus sic stantibus (fundamental change of circumstances clause)", and

97 Caldwell, above n 96, at 409.
99 At [5.21].
that a contract that did not allow for maintenance in the event of poverty would be unenforceable.\textsuperscript{101} This offers a potential model for how to resolve the quandary that FISAs will replace both maintenance, based on needs, and \textsection{15}.

Defining the bottom lines for FISA contracting out is essentially a social policy design question. The 1972 Royal Commission on Social Security provides the definitive statement of values and goals for income support.\textsuperscript{102} Continuity of income is noted to be an aspirational goal of income support, but not one that the state should necessarily provide.\textsuperscript{103} The targeted standard is belonging, requiring a "standard of living much like the rest of the community", allowing "a sense of participation in and belonging to the community".\textsuperscript{104} Beneath that lies the stratum of subsistence, which is poverty alleviation.\textsuperscript{105} The most relevant contemporary definition of poverty in New Zealand is calculated as 50 per cent of median household income.\textsuperscript{106} As this is a private scheme, there is no justification for allowing contracts for provision below the "belonging" standard. Accordingly, to avoid social dislocation given the reality of socioeconomic spatial segregation, income within a couple's geographical community needs to be considered.\textsuperscript{107} Median family income within a community is suitable for use as a comparator. This information is available as part of Statistics New Zealand's SA2 dataset, which provides such aggregate measures for areas with the population levels of Wellington's Mount Victoria suburb.\textsuperscript{108}

\begin{footnotesize}

\textsuperscript{102} The Royal Commission on Social Security in New Zealand Social Security in New Zealand (Government Printer, 1972) at 62.

\textsuperscript{103} At 64.

\textsuperscript{104} At 65; and Jo Barnes and Paul Harris "Still Kicking? The Royal Commission on Social Policy, 20 Years On" (2011) 37 Social Policy Journal of New Zealand 1 at 2.

\textsuperscript{105} The Royal Commission on Social Security in New Zealand, above n 102, at 63.


\end{footnotesize}
C Recommended FISA Contracting Out Regime

These recommendations use "child of the relationship" consistently with the current RPA, and "child of the partners" to mean a child where both partners are legal parents of the child (biologically or by adoption). The latter term aligns with the Law Commission's phrase "where the partners have a child together".109

The FISA scheme's design is based on the premise that each partner's future income can be adequately estimated as the average of the previous three years' income. This average figure is referred to as the "deemed income" in these proposals. The "adjusted deemed income" is the income that results from adding or subtracting any FISA amounts from the deemed income.

While the Law Commission proposals contemplate a broad definition of income,110 taxable income is a practical proxy measure. There is room for doubt about whether the desired wide definition of income will eventuate, given the countervailing desire for administrative efficiency and the desire for administration by Inland Revenue.111 For simplicity, these recommendations are based on taxable income.

I recommend that the s 21F procedural requirements for all new contracting out agreements should have the additional requirement that each partner make financial disclosure by statutory declaration. This should include information about trusts if the partner is able to obtain it after reasonable enquiries, if the partner has any right or interest in that trust (including a discretionary interest). This information should be available to partners in the future as a result of the Trusts Act 2019 creating a presumption of proactive disclosure.112

I recommend that the procedural requirements for a contracting out agreement that seeks to vary the default FISA rules should include:

(a) An estimate in the agreement for each partner of taxable income for each year following the agreement until that party turns 75, expressed in real (i.e. inflation-neutral) terms. This will be utilised as a baseline when evaluating the substance of the agreement.

(b) A default that the agreement will not apply if either partner's aggregate income during the relationship falls below 75 per cent of the estimated level or exceeds twice the estimated level (the "income deviation default"). The agreement may vary this default.

(c) A default that the agreement will not apply if there is a child of the partners (the "no children default"). The agreement may specifically address children of the partners.


110 At [10.91].

111 Atkin and Henaghan, above n 29, at 190.

112 Trusts Act 2019, s 51.
(d) A default that the agreement will not apply if either party spends more than two years substantially out of the full-time labour force before age sixty, unless the agreement specifically anticipates time spent out of the labour force (the "out of labour force default"). This is intended to be an objective way of assessing care contributions to the relationship, as well as issues like physical and mental health.

The "income deviation default", "no children default", and "out of labour force" default provisions are collectively called the "scope defaults". These defaults will be privileged at the second "protection from autonomy" stage, so that parties are incentivised not to change them.

As set out at section IV, above, the CEFL principles set the higher threshold of "exceptional hardship" for setting aside a marital agreement rather than "serious injustice" for a de facto agreement. This is because there are disclosure and advice requirements for marital agreements under the CEFL spousal contract principles.

Accordingly, I recommend that where the new disclosure requirement recommended for s 21F has been fulfilled at the time the agreement was made, the threshold for setting aside an agreement in s 21J be raised from serious injustice to exceptional hardship. For agreements pre-dating the amendments which did not feature such disclosure, the threshold would remain at serious injustice.

For reasons further elaborated in the next section, I recommend that a cumulative provision be added to allow FISA clauses (collectively "clauses") to be struck out from the main contracting out agreement in the following circumstances:

(a) where the clauses would lead to exceptional hardship; or
(b) where the clauses would leave one partner below the poverty threshold; or
(c) where there is a child of the partners, and the clauses would give a partner an adjusted deemed income below 200 per cent of the poverty threshold, and giving effect to the clauses would lead to injustice; or
(d) where the "out of labour force" default has been changed by the clauses, and the clauses would give a partner an adjusted deemed income below 200 per cent of the poverty threshold, and giving effect to the clauses would lead to injustice; or
(e) where the "income deviation default" has been changed by the clauses and giving effect to the clauses would lead to injustice.

Supporting that, a definition of "poverty threshold" would be added to this part meaning, with respect to a partner, the partner's deemed income, as adjusted by the effect of any FISA contracting out agreement, is below 50 per cent of the median household income in the SA2 area in which the partners were living together as a couple (or if no common residence, that partner's SA2 area during the relationship).

I also recommend that where the FISA clauses do not apply because the circumstances fall outside either a "default scope" or variation, courts should have discretion to nonetheless apply the clauses if
it would be just to do so. An example might be if a partner had intentionally and strategically exited the labour market to avoid the FISA clauses in their contracting out agreement.

**D Discussion of Recommendations**

The foregoing recommendations attempt to square the circle of protecting the vulnerable while providing certainty to those contracting out of the FISA arrangements that the Law Commission has proposed. These two aims can be reconciled, but at the cost of an expensive contracting out process. The contracting out process I have recommended is expensive both at the "protection of autonomy" stage, where formal disclosure is added, and at the "protection from autonomy" stage where certainty can only be purchased through generous provision.

This reflects that across many family law regimes there is a theme that:

… the parties are (more or less) free to decide that their relationship is one where they do not share everything, that they are free to maintain separate property and retain it when the relationship ends. However, another common theme is that nevertheless the marital relationship (and others, where applicable) brings with it responsibilities which cannot be contracted out of. Entering into the relationship, and living in it, brings with it certain responsibilities for the [partner] that continue even after the relationship ends. Mostly, these responsibilities relate to what are often called ‘relationship-generated’ disadvantages, and the remedies are of a compensatory nature and/or intended to cover a former spouse’s needs, at least for a certain period. This appears to be what most jurisdictions deem to be the inalienable core of their relationship law which is not at the disposition of the parties.

The recommendations at the procedural stage are designed to ensure that the partners are only bound to their agreement if the future that eventuates is one that they have foreseen adequately. These "scope" provisions are designed to ensure that ascertaining whether an agreement can be applied at the time of separation is a matter of review against what a, ex post, readily available objective facts: the number of children, time out of the labour force, and recent taxable income. The *ex-ante* uncertainties about these issues are gendered, in that women are the child-bearing partner and are more likely to compromise their career to provide care in the home.

Without more, these provisions would quickly be drafted around with FISA contracting out clauses containing words such as "[t]his agreement is intended to bind the parties whether they have children or not." This tendency for lawyers to bypass the scope constraints through broad pro forma language is what drives the variable level of review set out in the "protection from autonomy" provisions.

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113 Scherpe, above n 51, at 391–392.
At the "protection from autonomy" stage, the recommendations start from the strict position of agreements only being able to be set aside for "exceptional hardship", consistently with the CEFL Principles on Property Relations between Spouses,\textsuperscript{114} which apply because disclosure has been made.

However, this exceptional hardship threshold applies only if both parties end up with an income of at least half the median income for their area. The median household income varies dramatically between SA2 units. This test is intended to ensure that if the parties start in Remuera, each party is at least provided with a standard of living sufficient to subsist in Onehunga. That is, while they may be unable to each sustain a grand standard of living, each must remain comfortable. This may not be possible, but then the default FISA rules will apply which are designed to avoid causing hardship to either party.\textsuperscript{115}

If there is a child of the partners, then the evaluation of the protection from autonomy provisions means that the "no children default" has been varied; otherwise the agreement would not be in force. The clauses apply only if both parties maintain incomes of twice the poverty threshold, which is the median household income, or else if the provisions do not cause injustice. This rule does mean that if children are involved, only the wealthy can attain the certainty of avoiding scrutiny under the relatively low 'injustice' threshold that applied prior to the 2001 reforms. That is the price of protecting the vulnerable.

A similar rule applies with the "out of labour force" default. The age of 60 set as the delimiter is arbitrary and could equally well be aligned with eligibility for New Zealand Superannuation.

The purpose of lowering the threshold when the "income deviation default" has been changed is simply to provide a strong incentive not to change it, so that parties are only bound in circumstances that they have foreseen. As income is measured on a cumulative basis over a longer relationship, year-by-year variations will become less important.

My aim is that these recommendations provide confidence that the parties cannot contract for a regime that will not fulfil unmet 'reasonable needs' that are caused by a relationship, especially in the presence of children. Although contracting out will be expensive to do, it should provide certainty, provided that the contract is sufficiently generous in its provision. For additional robustness, agreements could refer to the statutory income floor levels, rather than having to make private estimates.

\textsuperscript{114} Boele-Woelki and others, above n 62, at 348.

\textsuperscript{115} Law Commission Review of the Property (Relationships) Act 1976, above n 5, at [10.95].
The higher exceptional hardship bar for setting aside agreements which have been made after full disclosure provides an additional fillip to couple autonomy. As said of the Scottish system:116

The very limited scope for challenge … may be regarded as both the Scottish system’s greatest strength and also potential weakness. While parties can be fairly confident that what they agree will be upheld, they should also be fully aware that they have little legal scope for reconsideration or regret.

VIII CONCLUSION

That FISAs will be adopted by the Government is far from a foregone conclusion. However, if they are adopted, there will be strong political pressure to allow couples to opt out of this new requirement.

Designing a FISA contracting out regime is a challenging undertaking, as the agreements are contracts for an uncertain future. In this future, disparities are caused by unpredictable family factors and the consequences fall most heavily on women. FISAs will replace maintenance which has provided a private safety net for need and which cannot be contracted out of. As a result, it is sensible for the FISA contracting out regime to give greater scrutiny to agreements that do not guarantee an income that is above a certain floor level.

I have recommended that FISA contracting out be permitted, but under a burdensome regime. If the strict procedural requirements are met, and the contracted provision is sufficiently generous, then agreements should be hard to set aside. In cases where it is not possible or not desired to be as generous with provision, then agreements should be more vulnerable to being set aside.

This proposal may be criticised as offering autonomy only to the rich. That is a fair criticism, but that is the price of protecting the vulnerable in this important area of social policy.