



PUMP COURT

CHAMBERS

**FINANCIAL MISCONDUCT**

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## THE QUESTION

How do you counter questionable conduct:

e.g. one party running down a small family company, starting a new similar company and bagging the goodwill?

# SCENARIO

## Albert and Beatrice

25 year marriage. Adult children.

Marital assets: FMH £1m, other liquid assets £1m.

Albert trained as an apprentice cobbler. He set up his business 'Feet R Us Ltd' with his first shop in Hammersmith pre marriage.

By 2014 he had 10 shops. Beatrice worked in the business in a number of roles, most recently as a regional manager.

# SCENARIO

## Albert and Beatrice

In 2014 Albert discussed a possible sale of the business but it did not come to anything. Beatrice says there was a formal offer tabled of £2m but Albert refused to sell at that price.

In 2018 the parties separated. Albert wound down Feet R Us and closed all the shops. He transferred the goodwill and stock to a new internet trading company Shoes 4U Ltd.

He claims to have done this because High Street trading had become unprofitable and on-line trading was the way forward.

## SCENARIO

### Albert and Beatrice

Beatrice places a value of £2m on Feet R Us and says that Albert deliberately wound it up to defeat her claim.

The SJE says it is difficult to value Feet R Us in hindsight. The company did appear to have been profitable. The offer of £2m in 2014 was a relevant factor but market conditions had changed significantly since then.

She values Shoes 4U at £0.5m (mainly stock) but as it is an internet start up she says its future is uncertain.

## FINANCIAL MISCONDUCT - GENERAL

A court is only going to find conduct that is 'inequitable to disregard' in a very limited number of circumstances.

Financial misconduct which has the effect of dissipating the marital asset base will be one such situation.

A party who fritters away or otherwise dissipates assets runs the risk of an 'add back' of the notional value thereby lost.

As per Cairns LJ in *Martin v Martin* [1976] Fam 335: "a spouse cannot be allowed to fritter away the assets by extravagant living or reckless speculation and then to claim as great a share of what was left as he would have been entitled to had he behaved reasonably"

## FINANCIAL MISCONDUCT – ADD BACK

The term ‘add back’ derives from *Norris v Norris* [2002] EWHC 2996 (Fam), [2003] 1 FLR 1142 – Bennett J added back £250,000 of overspend to H’s assets.

In *Vaughan v Vaughan* [2007] EWCA Civ 1085, [2008] 1 FLR 1108 the Husband, by his own admission, gambled away and wasted over £80,000. DJ at first instance refused to ‘add back’ these sums. CJ estimated dissipated money as between £100,000 and £175,000.

CA held it was appropriate to reattribute a sum to the Husband in view of his dissipation. Court adopted the CJ’s minimum figure of £100,000.

## **FINANCIAL MISCONDUCT – ADD BACK**

*Vaughan v Vaughan*

Per Wilson LJ: “... a notional reattribution has to be conducted very cautiously, by reference only to clear evidence of dissipation (in which there is a wanton element) and that fiction does not extend to treatment of the sums reattributed to a spouse as cash which he can deploy in meeting his needs, for example in the purchase of accommodation.”

## FINANCIAL MISCONDUCT – ADD BACK

Further examples where ‘add back’ arguments raised:

*F v F (Financial Remedies: Premarital Wealth)* [2012] EWHC 438 (Fam), [2012] 2 FLR 1212.

Husband had made substantial lifetime gifts to 4 children from previous marriage. Macur J held it was entirely reasonable for him to do so at a time when he was making provision for his younger children and his wife. The gifts did not adversely impact upon the high standard of marital lifestyle.

*“For the avoidance of doubt I make clear that the wife has not discharged the burden of proving any alienation of matrimonial funds by the husband with the intention of defeating or reducing her claim, nor of wanton and reckless behaviour to found any ‘add back’ argument, quasi or otherwise”.*

## FINANCIAL MISCONDUCT – ADD BACK

Further examples where ‘add back’ arguments raised:

*AC v DC (No 2)* [2012] EWHC 2420 (Fam), [2013] 2 FLR 1499  
Sir Hugh Bennett ordered an ‘add back’ of £4.55m, finding clear evidence of dissipation (including a wanton element) by or on behalf of the Husband.

*MAP v MFP (Financial Remedies: Add-Back)* [2015] EWHC 627 (Fam), [2016] 1 FLR 70 per Moor J.

Parties were married 40 years and established a successful property maintenance company. In FR proceedings the Wife alleged the Husband was spending £6,000 a week on drugs (cocaine) and further large sums on prostitution.

## **FINANCIAL MISCONDUCT – ADD BACK**

*MAP v MFP (Financial Remedies: Add-Back)*

The Wife claimed a wanton dissipation of assets which necessitated an 'add back' of £1.5m. Moor J held that whilst the Husband's spending, particularly on drugs and prostitution, was morally culpable it was not deliberate or wanton dissipation within the meaning formulated in the authorities. It would therefore be wrong to add it back. He had not overspent to reduce the Wife's claim. It was down to his flawed character. A spouse had, as it were, to take his or her partner as he or she found them.

## FINANCIAL MISCONDUCT – ADD BACK

*MAP v MFP (Financial Remedies: Add-Back)*

The Wife had been a 5% shareholder in the company. When she discovered the Husband was using prostitutes, she was suspended from the company and eventually dismissed for gross misconduct. She had never received details of the allegations against her. As a result of this she lost her entitlement to entrepreneur's relief in the sum of £271,000.

Moor J held that this sum should be 'added back' into the schedules. This had been a deliberate and wanton act. The Husband could have found a way round this problem, but he chose dismissal. The Wife should not be penalised for this.

## **FINANCIAL MISCONDUCT – EVIDENTIAL HURDLES**

Evidential hurdles can provide the most significant bar in these cases to persuading the court to ‘add back’ sums.

In very many cases, in my experience, ‘add back’ arguments are raised but they rarely succeed. This is because of the difficulty of showing ‘clear evidence of dissipation in which there was a wanton element’

On many occasions our clients believe the evidence to be stronger than it actually is!

# FINANCIAL MISCONDUCT – EVIDENTIAL HURDLES

<https://www.youtube.com/watch?v=2Gkiw7zpULo>



## FINANCIAL MISCONDUCT – EVIDENTIAL HURDLES

Highlights importance of proper objective analysis of strength of case.

*BJ v MJ (Financial Remedy: Overseas Trusts)* [2011] EWHC 2708 (Fam), [2012] 1 FLR 667.

The Husband had made gifts to the parties' son of £140,030 and the Wife sought an 'add back' of this amount.

Mostyn J cited his own observations in *N v F (Financial Orders: Pre-Acquired Wealth)* [2011] 2 FLR 533:

## FINANCIAL MISCONDUCT – EVIDENTIAL HURDLES

”In this country we have separate property. If a party disposes of assets with the intention of defeating the other party’s claim then such a transaction can be reversed under s.37 of the MCA 1973. Similarly, where there is ‘clear evidence of dissipation (in which there is a wanton element)’ then the dissipated sums can be added back or re-attributed (see *Vaughan v Vaughan*...). But short of this a party can do what he wants with his money. What is not acceptable is a faint criticism falling short of either of these standards. If a party seeks a set aside or a re-attribution then she must nail her colours to the mast”.

He added: “Although intellectually pure, the problem with this technique is that it does not re-create any actual money. It is in truth a process of penalisation. In my judgment it should be applied very cautiously indeed and only where the dissipation is demonstrably

## **FINANCIAL MISCONDUCT – UNPROVEN ALLEGATION**

*MF v SF (Financial Remedy: Financial Conduct)* [2015] EWHC 1273 (Fam), [2016] 2 FLR 622

Husband had been high earner but was made redundant. Wife alleged broad ranging conspiracy between the Husband and the company which involved falsely pretending to make the Husband redundant and falsely asserting the Husband owed the company £1m. Parties spent almost £1m in legal fees.

Moylan J found assets to be £2.2m. The formal starting point should have been an equal division of these assets but the Wife's case had been advanced on a speculative and unfounded basis. It would not be fair to ignore the consequences of that conduct when exercising the Court's discretion. Accordingly adjustment made in Husband's favour so division £1.3m to Husband and £0.9m to Wife.

## FINANCIAL MISCONDUCT – SCENARIO

Feet R Us Limited / Shoes 4U Limited:

- Can Beatrice prove firm £2m offer and that this represents value of company now had Albert continued trading?
- Can Beatrice prove decision to wind up Feet R Us represented dissipation of assets with wanton element?
- Can she disprove Albert's response that market conditions had changed necessitating the move from retail units to online?
- Even if Beatrice surmounts evidential hurdles, what impact would this have on fair distribution given Albert's needs?
- Will sum ultimately spent on litigation prove to be proportionate?

## VALUATION PROBLEMS

Feet R US – difficult to value in hindsight.

Shoes 4U Limited – internet start up, value speculative.

*Hart v Hart* [2017] EWCA Civ 1306, [2018] 1 FLR 1283

Per Moylan LJ: In situations where the parties' wealth comprised matrimonial and non-matrimonial property, the court did not have to undertake a detailed evidential enquiry and was not required to undertake a formulaic approach. It could adopt a broader approach.

## VALUATION PROBLEMS

Feet R US – difficult to value in hindsight.

Shoes 4U Limited – internet start up, value speculative.

*Martin v Martin* [2018] EWCA Civ 2866

Per Moylan LJ: Valuations of private companies could be fragile and had to be treated with caution. In practice the broad choices were (a) ‘fix’ a value, (b) order the asset to be sold; or (c) divide the asset in specie.

*Miller & McFarlane* per Lord Nicholls “valuations are often a matter of opinion on which experts differ. A thorough investigation into these differences can be extremely expensive and of doubtful utility”.

## VALUATION PROBLEMS

*H v H* [2008] 2 FLR 2092 Per Moylan J:

”I understand, of course, that the application of the sharing principle can be said to raise powerful forces in support of detailed accounting. Why, a party might ask, should my ‘share’ be fixed by reference other than to the real values of the assets? However, this is to misinterpret the exercise in which the court is engaged. The court is engaged in a broad analysis in the application of its jurisdiction under the Matrimonial Causes Act, not a detailed accounting exercise.”

## VALUATION PROBLEMS

*Martin v Martin* Per Moylan LJ:

“... even when the court is able to fix a value this does not mean that that value has the same weight as the value of other assets such as, say, the matrimonial home. The court has to assess the weight which can be placed on the value even when using a fixed value for the purposes of determining what award to make. This applies both to the amount and to the structure of the award... I would also add that the assessment of the weight which can be placed on a valuation is not a mathematical exercise but a broad evaluative exercise to be undertaken by the judge.”

## VALUATION PROBLEMS

*Martin v Martin* Per Moylan LJ:

“I would also had that this is not, as Mostyn J suggested, to take realisation difficulties into account twice. Nor, as submitted by Mr Pointer, will perceived risk always be reflected in the valuation. The need for this approach derives from the fact that, as said by Lewison LJ, there is a ‘difference in quality’ between a value attributed to a private company and other assets. This is a relevant factor when the court is determining how to distribute the assets between the parties to achieve a fair outcome.”

If an expert has given a bracket, it might be reasonable to assume that a figure in the middle is likely to give a sufficient *indicative value* for the purposes of a financial remedy application.

## VALUATION PROBLEMS

In practice the broad choices are (a) 'fix' a value, (b) order the asset to be sold; or (c) divide the asset in specie.

*Versteegh v Versteegh* [2018] EWCA Civ 1050, [2018] 2 FLR 1417  
Judge at first instance held he was unable to determine the value or future liquidity of the Husband's company so he made a Wells v Wells order.

Moylan LJ: It was undoubtedly far more satisfactory for all concerned if a court could, with sufficient confidence, settle of a valuation of a business on the balance of probabilities. However, considerable unfairness could be caused to one or both parties if the approach was to be in a sharing case that there was an absolute requirement on the court to settle on a valuation.

## VALUATION PROBLEMS

Despite very real practical problems, CA upheld decision to grant the Wife a minority interest in the Husband's company.

One such problem became apparent after extensive argument at first instance. Judge had wanted to award preference shares but in the end only ordinary shares were awarded.

It was very hard to know what else could be done given that valuations of shares in private companies are amongst the most fragile that can be obtained, especially given their want of exposure to the real market!



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