THE LAWYER'S DAILY

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Splitting Family Debt

Till debt do us part: dividing liabilities

By **Laurence Klass**

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(November 15, 2019, 9:10 AM EST) -- When most people think of family law cases, their minds turn to the dilemma of fairly dividing the family assets (in other words, "matrimonial property"): the house, the car, the pensions, perhaps the heirloom grandfather clock in the dining room. The flip side of the coin, however, is frequently less straightforward. What is the best approach to untangling not just the assets, but the liabilities?

Given s. 81 of the *Family Law Act*, SBC 2011, Chapter 25 (FLA), there is a presumption that on separation, each spouse is equally responsible for family debt. The definition of "family debt" then becomes central to the overall liability imposed on each spouse.

Whereas the previous *Family Relations Act*, RSBC 1996, Chapter 128 (FRA) did not provide such a definition, s. 86 of the FLA spells out the starting point of what is considered a "family debt": "Family debt includes all financial obligations incurred by a spouse (a) during the period beginning when the relationship between the spouses begins and ending when the spouses separate, and (b) after the date of separation, if incurred for the purpose of maintaining family property."

While this statutory definition is non-exhaustive, the general framework is to apply a 50-50 division on debts incurred during the relationship and debts incurred after the relationship for the purpose of maintaining family property. As a result, debts incurred before the relationship are excluded and thus remain in the name of the spouse who incurred them.

The interplay between family property and family debt is an interesting one and will almost always colour the determination of each spouse's post-separation liability. Section 85 of the FLA provides a list of what constitutes "excluded property"; however, there is no corresponding statutory provision for "excluded debt." This is likely because "family property" is defined quite expansively: pursuant to s. 84(1) of the FLA, all real and personal property that is owned by at least one spouse on the separation date will presumptively qualify as family property. In contrast, family debt is bracketed by the date on which it was incurred.

On July 23, the B.C. Supreme Court released *Xu v. Hu* 2019 BCSC 1336, an interesting case discussing responsibility for debt upon the breakdown of a relationship. In this case, the ex-wife's father had gifted the couple a $6 million house nominally purchased by the father's company but held in trust for the ex-wife. It was previously found that this beneficial interest in the house was "family property," and so the ex-husband would receive his share. At the same time, some $1.2 million in tax liabilities had arisen from the sale of the house, which the ex-husband sought to avoid.

In summarizing the situation, the court put forth at para. 6: "Mr. Xu therefore seeks to enjoy the financial benefit of his wife having received the Marguerite Property from her father while avoiding any tax obligations and expenses associated [with] acquiring, maintaining and disposing of that property."

In reaching the conclusion that the ex-spouses would share equally in the tax liabilities, the court canvassed the leading case law on apportionment of family debt. It upheld the principles in *Stein v. Stein* 2008 SCC 35, which though decided under the ambit of the former FRA, continues to guide the court's determination of fairness in the division of family debt. For example, the Supreme Court of Canada stated at para. 16 of *Stein*: "… where a debt has been incurred for use within the family unit,

it is more likely appropriate to reapportion assets to account for that debt than if it were accumulated solely for use outside of the marriage."

Principles in *Stein* were affirmed in *Lightle v. Kotar*, 2014 BCCA 69, where the B.C. Court of Appeal provided at para. 58: "… there is no reason to depart from the rule, applied in relation to the other family property in this case, that the matrimonial property and debts, including the business assets and contingent liabilities as of the date of the triggering event, should be equally divided between the parties. That, in my view, is the result dictated by the principles of equality and fairness."

As noted in *Xu v. Hu*, these general themes were carried forward in other B.C. Court of Appeal cases more recently, including *Maguire v. Maguire* 2016 BCCA 431, and *Sanai v. Mahmoud* 2017 BCCA 155.

As a general proposition, the approach to dividing family debt should correspond to that of dividing family property, despite the different definitional boundaries in these two domains espoused by the FLA. There is potential for tension between the concept of "fairness" voiced by the courts and a strict textual reading of the applicable FLA provisions.

An example of this tension may arise in cases where a spouse purchases a new home for the couple using the Home Buyers' Plan (HBP), withdrawing RRSPs to do so and garnering a future obligation to repay those funds. If this spouse makes the withdrawal before the relationship begins, but the home eventually becomes the family home, how is the debt divided upon separation?

A couple may consider drawing up an agreement with respect to division of property and debt, to forestall potentially unfair consequences that may nonetheless come about due to a strict reading of s. 86 of the FLA. As always, such agreements would be further subject to the "significant unfairness" consideration in s. 93 of the FLA.

It is hoped that adequate mechanisms exist in either statutory or common law authorities that operate to prevent the unfairness of enjoying an equal share of a family asset, while carrying none of the liabilities associated with that asset. In other words, the legal framework should ensure that former spouses do not "have their cake and eat it too." (Unless they have the stomach for it!)

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