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— Franks & Zalev - This Week in Family Law

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Material Change . . . But from When??? And Using Without Prejudice Correspondence

***Proust v. Proust*, 2026 CarswellBC 1912 (C.A.)**

Ladies and gentlemen, we give you section 17(4.1) of the *Divorce Act*, RSC 1985, c 3 (2nd Supp) (the "*Divorce Act*"):

> **Factors for spousal support order**
>
> (4.1) Before the court makes a variation order in respect of a spousal support order, the court shall satisfy itself that a change in the condition, means, needs or other circumstances of either former spouse has occurred **since the making of the spousal support order** or the last variation order made in respect of that order, and, in making the variation order, the court shall take that change into consideration. [**emphasis** added]

Seems pretty clear. To vary spousal support, the party seeking the change must show a "material change" since the making of the spousal support order.

But look what happens when we get some hard facts.

This case was about a provision in a Separation Agreement that allowed the parties to apply to vary spousal support on a material change in their financial circumstances. Nothing out of the ordinary so far.

After a lengthy marriage, in which the Appellant (Husband) was the income earner and the Respondent (Wife) was a stay-at-home parent, the parties separated in 2021.

By the summer of 2023, the parties had negotiated a settlement on most of the financial issues. For spousal support, they agreed the Husband would pay the Wife $18,500 a month based on the 2022 and 2023 incomes of the parties. However, as there remained some outstanding issues to be negotiated, the Separation Agreement was not actually signed at that time. Rather, discussions between counsel continued for the next several months.

In November 2023, before signing and formalizing the separation agreement, the parties met and discussed other outstanding financial issues. In *without prejudice* correspondence (this part will be interesting later) delivered on November 29, 2023, the Husband's counsel informed the Wife's counsel that the Husband's projected 2024 income was $267,000 and that he could not afford to pay $18,500 in monthly spousal support. The Husband accordingly sought to renegotiate his spousal support payments from $18,500 to $10,000 per month.

While the parties did not then change the amount of support in the Separation Agreement, the Wife did agree to reduce the financial threshold for a material change in the Husband's income.

The parties signed the Separation Agreement in December 2023, with stated "effective date" of July 1, 2023. One of the recitals in the Separation Agreement stated:

> The parties, through discussions with their counsel, settled all of the financial issues arising from the breakdown of their marriage, with an effective date of July 1, 2023. The parties are entering into this agreement to formalize the terms of that settlement.

In August 2024, the Husband brought an application to reduce his spousal support to $7,328 from April 2024 due to the drop in his income.

The issue on the Application was whether a material change in the Husband's income had occurred that the parties had not reasonably anticipated when they signed the Separation Agreement.

The question then arose — a material change from when? What date was the comparator? What was the baseline from which to judge a material change?

The chambers judge chose December 2023, the date the Separation Agreement was signed — not July 2023, the stated "effective date" of the Separation Agreement. According to the chambers judge, as the Husband had *specifically* communicated the expected reduction in his income in November 2023, the parties had specifically contemplated the income reduction that had in fact occurred when the Separation Agreement was signed.

No material change.

The Husband appealed. The major point on appeal was whether the chambers judge had erred by measuring the Husband's claimed change in circumstances from the time the Separation Agreement was signed rather than from the "effective date" of the settlement.

The Court of Appeal was of the view that the chambers judge erred by failing to assess the change in financial circumstances *from the effective date of the agreement*. It did not matter that some financial issues remained outstanding in late 2023, because none of those issues related to spousal support. And there was "no basis for treating the discussions between counsel in November 2023 about spousal support as being within the contemplation of the parties as of the agreement's effective date in July 2023."

Furthermore, according to the Court of Appeal, spousal support is not to be assessed on "speculative future events," including uncertain changes in a party's income. Rather, future events contemplated at the time of an Order, *but still speculative or uncertain*, should be addressed by a subsequent review: *Eldridge v. Eldridge* (2024), 96 R.F.L. (8th) 269 (B.C. C.A.) at para. 61.

Here, as found by the Court of Appeal, the determinative point was the wording of the Separation Agreement itself: it specified July 1, 2023 as the "effective date" and, as such, the contractual baseline from which a claimed material change had to be measured. In focussing on the date the Agreement was signed rather than the stated "effective date", the chambers judge erred in principle. When assessed from July 2023, it was clear that there had been a material change — the Separation Agreement did not contemplate such a significant reduction in the Husband's income.

One more interesting point.

Remember that the November 2023 *without prejudice* correspondence the Husband's lawyer wrote to the Wife's lawyer about the Husband's anticipated drop in income — before the Separation Agreement was signed? Sure you do. Well, the chambers judge admitted that *without prejudice* letter into evidence as relevant to the Husband's knowledge at the time the Separation Agreement was signed.

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The Husband appealed the admission of that letter because it had been written on a without prejudice basis. He argued that the chambers judge erred in admitting the letter into evidence. The chambers judge had reasoned as follows in admitting the letter:

> [36] In bringing this application [the Husband] has put the parties' actual contemplation regarding their future financial circumstances squarely in issue. As a result, I find that the November 2023 without prejudice correspondence from his counsel is admissible as it is helpful in determining the parties' actual expectations regarding their financial circumstances at the time the Settlement Agreement was made.

On this issue, the Court of Appeal sided with the chambers judge:

> [56] This Court has held that the test for establishing an exception to **settlement privilege** should not be set too low because the policy behind settlement privilege is a compelling one. **However, an exception applies where documents are relevant and necessary in the circumstances**: *Dos Santos v. Sun Life Assurance Co. of Canada*, 2005 BCCA 4 at paras. 19-20. The privilege may not apply if it obscures from the court the true state of affairs between the parties: *Fisher v. Airfoam Industries Ltd. (Quad-Lock Building Systems)*, 2025 BCSC 758 at para. 26.
>
> [57] Here, the chambers judge correctly found that the [Husband] put in issue his state of knowledge at the time he entered into the separation agreement. The necessary implication from the [Husband's] application to vary spousal support on the basis of a material change in his financial circumstances is that the change was either unknown or had not been contemplated at the time of the agreement. The [Husband's] knowledge of his 2024 income, as evidenced by the without prejudice correspondence, was relevant and necessary, given that his application turned on the parties' actual contemplation regarding their future financial circumstances. [**emphasis** added]

We take no issue with the letter being admitted. However, we might feel differently if the letter in question was *actually* subject to settlement privilege, which does not appear to be the case. This was, rather, an ordinary without prejudice letter. Settlement privilege, on the other hand, is a "class privilege" (like solicitor-client privilege and litigation privilege) and not subject to case-by-case exceptions: *Middelkamp v. Fraser Valley Real Estate Board*, 1992 CarswellBC 267 (C.A.); *Brown v. Cape Breton*, 2011 CarswellNS 186 (C.A.); *Sable Offshore Energy Inc. v. Ameron International Corp.*, 2013 CarswellNS 428 (S.C.C.); *Bellatrix Exploration Ltd. v. Penn West Petroleum Ltd.*, 2013 CarswellAlta 76 (C.A.); *Union Carbide Canada Inc. v. Bombardier Inc.*, 2014 CarswellQue 3600 (S.C.C.).

But in any case, no harm — no foul.

However, with respect to correspondence that is marked "without prejudice", it is worth keeping in mind that such documents may be admissible, if exclusion would otherwise obscure from the court the true state of affairs between the parties.

Debt Repayment Is Not a Magic Income Eraser

***Roe v. Roe* (2026), 24 R.F.L. (9th) 275 (Alta. K.B.) — Kubik J.**

Can a payor use corporate earnings, use it to rapidly pay down or accelerate debt repayment — improving the company's balance sheet in the process — and then ask the court to treat those funds as "unavailable" for child support purposes? It sounds sort of obvious when we ask it that way — but it seemingly still needs be said. That is what makes *Roe v. Roe* useful.

In self-employment cases, simply labelling something a "necessary business expense" does not automatically answer whether the funds used for the stated purpose were genuinely unavailable for child support. The real question is what the money was actually used for. Debt repayment, capital investment, inventory surcharge, retained earnings, shareholder benefit, and required dealer contribution are not interchangeable concepts and are not all created equal. If counsel do not unpack them, available income can be materially understated.

The parties had four children and separated in October 2018. Their December 2019 Divorce and Property Agreement set the husband's child support based on an agreed income of $100,000, but it also expressly contemplated annual disclosure

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and recalculation under s. 18 of the *Federal Child Support Guidelines*, SOR/97-175, because the husband earned income through privately held corporations. The husband owned and controlled the relevant corporations after the wife relinquished her shareholdings to him. Because the husband earned income through those corporations, the real dispute was not what appeared on his tax return, but how much of the corporations' pre-tax earnings should be considered "available" for child support.

The husband's Line 15000 income ranged from $80,000 to $95,000, but once corporate pre-tax income and corporate-paid personal expenses were considered, the income picture changed dramatically. The husband's own expert calculated the husband's income to be in a range between $91,000 and $275,000, while the wife's expert calculated between $195,000 and $329,000. That is exactly why Line 15000 is said to be only the *beginning* of the analysis.

Justice Kubik properly considered the income issue through s. 18 of the *Guidelines*, which allows the court, where a spouse is a shareholder, director, or officer of a corporation to include all or part of the corporation's pre-tax income in guideline income where Line 15000 income does not fairly reflect all money available for child support. The exercise is discretionary, and it requires balancing the children's right to fair support against the *legitimate* capital and expense needs of the corporation. And that is an important balance. While a court need not accept corporate accounting choices at face value, it should also not automatically second guess business decisions or look to place the largest shovel in the company store: *Kowalewich* v. *Kowalewich v. Kowalewich* (2001), 19 R.F.L. (5th) 330 (B.C. C.A.); *Quinton v. Kehler*, 2020 CarswellBC 2246 (C.A.).

To determine the husband's income for support purposes, Justice Kubik analyzed the corporate payment in issue in three different buckets: mandatory dealer investments, accelerated debt repayment, and rebate income. This structure is worth keeping in mind because each category turned on a different question about whether the corporate funds were actually available for child support.

Accelerated Debt Repayment

The debt repayment issue illustrates how s. 18 is supposed to work. After separation, the husband accelerated the repayment on the mortgage on a rental property and on various corporate debts. He argued that the principal portion of those repayments should not be included in his Guideline income, but he provided no business (or any) rationale for that position. The wife's position was that, but for the accelerated payments, the money would have been available for child support.

The court accepted the wife's expert evidence that, under generally accepted accounting principles ("GAAP"), debt repayment is not an expense category. While GAAP did not decide the support result, it did stop the debt repayment from being ushered through as an "expense." The legal question then became whether the corporate cash nevertheless had to remain in the business or whether it was used reasonably/justifiably.

The husband bore the onus of establishing that the accelerated debt repayment was reasonably necessary for the management and ongoing financial health and viability of the business. He did not. In fact, the evidence before the court showed the opposite: the corporations were financially viable, with increased equity and working capital as a result of the accelerated debt repayment. The court therefore included the funds used for accelerated debt repayments in the husband's Guideline income for support purposes.

That is the practical lesson. Paying down debt may be prudent. It may even be financially wise (depending on the interest rate.) It may even be commercially rational. It may be exactly what a careful business owner would do. But prudence is not the test. The question is whether the repayment was genuinely required for the business, or whether it was a use of available corporate cash that had the effect of lowering support income while increasing the payor's corporate equity. That is a very important distinction. Furthermore, were it financially wise to do so, it does behoove the owner to explain why the payments were only accelerated after separation.

Post-separation, a payor cannot rearrange their corporate affairs in an effort to build equity and capital reduce support. One cannot build assets on the back of one's support obligations. *N. (M.) v. C. (T.)* (2012), 22 R.F.L. (7th) 247 (B.C. Prov. Ct.); *Hausmann v. Klukas* (2009), 64 R.F.L. (6th) 54 (B.C. C.A.); *Birnie v. Birnie* (2018), 7 R.F.L. (8th) 188 (Sask. Q.B.).

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However, in keeping with the need to *balance*, ordinary-course repayment of principal is not automatically income either. As we discussed in the June 14, 2021 (2021-23) edition of *TWFL*, *A.R.J. v. Z.S.H.* (2021), 53 R.F.L. (8th) 368 (B.C. S.C.) involved roughly $50,000 per year in principal payments made by one of the husband's companies toward long-term debt. In that case, the court declined to include those principal repayments in the husband's income for support purposes because they were made in the ordinary course, there was no evidence of acceleration or income manipulation, and the payments were necessary to sustain the companies as viable enterprises. A corporate decision to pay down its mortgages for properties used for business purposes, in an ordinary, long-established manner, in accordance with its mortgage covenants is eminently reasonable. It is entirely appropriate (and usually *required*) that corporate income be directed to mortgage payments and not available for support purposes where there is no suggestion of manipulation: *McKenzie v. McKenzie* (2014), 51 R.F.L. (7th) 84 (B.C. C.A.); *A.R.J. v. Z.S.H.* (2021), 53 R.F.L. (8th) 368 (B.C. S.C.); *Neeteson v. Neeteson* (2007), 45 R.F.L. (6th) 164 (Ont. S.C.J.); *Tether v. Tether* (2009), 62 R.F.L. (6th) 197 (Sask. Q.B.).

But *Roe* sits on the other side of that line: if the repayment is accelerated post-separation, and if the payor cannot explain why the acceleration was necessary, the court is entitled to ask whether the money was truly unavailable or was simply redeployed into corporate equity.

Not Every Corporate Asset Represents Available Income — Mandatory Dealer Investment

With respect to the mandatory dealer investments, one of the husband's companies operated a Home Hardware store and paid surcharges on inventory that funded special shares and five-year notes under its dealer arrangement. Those amounts were not "expenses" in the ordinary sense; they actually created corporate assets. But the expenditure was mandatory, could not be cashed in or otherwise accessed in the relevant years except under the Dealer Agreement, and were necessary to manage the business. Justice Kubik therefore treated them as corporate value that was not actually available for support in those years and excluded them from the husband's guideline income. Notably, this was also an "expense" that was not new.

In contrast, the accelerated debt repayment was included because it was a post-separation construct, not shown to be necessary, and that actually improved the corporation's financial position. The required dealer investments were excluded because they were mandatory, inaccessible in the relevant period, and necessary to the business.

Rebate Income

One of the husband's companies also received $70,193 in rebate income issued by way of preferred shares. The court treated that amount as income returned to the company under the Dealer Agreement, not as proceeds from the sale of a capital asset. It included the amount because the rebate reflected funds available for child support and there was no evidence that inclusion would impair the corporation's financial viability. Notably, the shares also seem to have been the flip-side of the mandatory dealer investment.

When acting for recipients, the takeaway from *Roe* is not "add back all debt repayment." That would be too easy — it is an incorrect oversimplification. The practical move is to force the payor to explain the transaction in business terms and support it with evidence. What debt was repaid? Was repayment scheduled or accelerated? Who decided to accelerate it? Was there a covenant, refinancing requirement, looming default, supplier pressure, a tax-driven rationale, or operational necessity? What happened to retained earnings, working capital, shareholder equity, and cash flow before and after the repayments? And what happened before separation? If the answer is simply, "we thought it was good business," that may not be enough when child support is in play.

That starts with disclosure. Do not stop at tax returns. Do not stop at "the accountant says this is an expense." Ask for the documents you need to understand what the financial statements actually show. If you do not know what to ask for, get help from an expert.

That is where cases like Justice Kiteley's decision in *Meade v. Meade* (2002), 31 R.F.L. (5th) 88 (Ont. S.C.J.) come in. As her Honour explained at paragraph 81 of that decision, a self-employed person has a *positive obligation* to produce not merely

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adequate but *comprehensive* financial records — a package from which the recipient can understand the income picture and the appropriate amount of child support can be determined. Where disclosure falls short, the resulting adverse inferences should favour the recipient, not the payor whose inadequate records made the analysis unnecessarily difficult and expensive.

The lesson for payor counsel is just as direct. If your client wants to exclude corporate funds used to repay debt or other obligations, the *evidence* has to explain why the repayment was necessary.

In *Roe*, the husband bore the burden of proving that the pre-tax corporate earnings were not available for support purposes and/or were required to manage the business and ensure its ongoing viability. On the debt repayment issue, he failed because he produced no evidence showing that the accelerated repayments were necessary.

Although *Roe* is an Alberta decision, the income point travels across the country. Lawyers across Canada encounter this issue regularly with incorporated professionals, trades, franchise operators, consultants, and small-business owners. The lesson is not that debt repayment equals income. That is too simple. The lesson is to scrutinize the debt, test the claimed business necessity, insist on the supporting evidence, and draft annual disclosure and recalculation clauses that allow that analysis to occur when support is revisited.

A debt repayment may be a legitimate business necessity. It may also be a way of converting available corporate cash into shareholder equity while claiming there is no income available for support. *Roe* is useful because it insists on evidence to distinguish one from the other. The label — business expense, debt repayment, capital investment, retained earnings — does not answer the s. 18 question. Only evidence can do that.

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