"FOR THE DROVER'S LIFE HAS PLEASURES THAT THE TOWNSOLK NEVER KNOW"

RURAL FARM ENTERPRISES AND ESTATE PLANNING

Professional advisers to rural farm enterprises need to consider estate planning and succession planning as part of providing effective and practical advice.

Ownership of Property

Rural farm enterprises may be conducted through a series of companies, family trusts and/or partnerships. Older rural farm enterprises may still have "Gorton style" companies, which were historically used to limit death duties, where one person (usually the parent) owns control shares and another (usually the child) owns equity shares.

The land may be owned by the company, family trust or partnership, or may be owned by the grazier/farmer either in their own name or jointly or as tenants in common with spouses or children. The farm machinery, equipment and other items such as spelling yard fences or irrigation infrastructure may be owned by a company, family trust, partnership or individuals. There may be limited records of who owns what – the best records may be tax return depreciation schedules.

Advisers should inform clients that creating a family discretionary trust or company may provide asset protection and be tax effective, and may limit the testator's exposure to family provision claims, but it may limit the client's ability to dispose of their assets as they wish.

The testator's advisors may attempt to resolve these issues when the administer the estate, but they may be expensive and may not be effective. For example, a solicitor may prepare a "statement of wishes" to the trustee of the family discretionary trust to be attached to the will. However, these are not binding and the trustee may ignore the statement. [1] The testator may arrange for the trusts to be collapsed, the joint tenancy to be severed and re-transferred, and/or the companies to be dissolved during his life time, or direct the executor to do so after he passes away, but this will incur punitive capital gains tax and stamp duty. In *Ireland v Retallack*[2], the testator's will provided

> "I DECLARE that my said executors will be entitled to manipulate the assets of my estate in order to transfer real property detailed in Schedule One from Glengowan (Moorilda) Pty Ltd to SANDRA JANE RETALLACK and any other real property from Glengowan (Moorilda) Pty Ltd to GORDON FAMILY CORPORATION."

This simple direction led the executor to incur significant costs obtaining accounting and legal advice about the tax and stamp duty consequences of different scenarios, that led Justice Pembroke to say that the estate was being treated as a milch cow.

Division of Testator's Property

Even if the testator is able to deal with the assets in the will, the testator needs to carefully consider the consequences of dealing with the assets.

There may be an informal arrangement pursuant to which the family trust or family company runs the farming business, and merely pays the outgoings on the land such as rates, water and insurance as "rent". The person taking over the farming business may need to negotiate a formal

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1 *Hartigan Nominees v Rydge* (1992) 29 NSWLR 405

2 *Ireland v Retallack* [2011] NSWSC 846

lease to secure the farming business' rights to use the land. The notional rent may no longer be reasonable if the land is bequeathed separately to a number of beneficiaries, where the interests of the owners of the land are not the same as the interests of the farming operations.

It may be that the beneficiaries wish to sell the land and realise their inheritance. It may be practically difficult for the land to be sold without the irrigation system, let alone the solar hot water system and cool-room attached to the homestead, which may technically belong to the family trust or the family company. This becomes even more complicated if there are mortgages and overdrafts to finance the farm operations.

The testator may bequeath parcels of land to different beneficiaries. There may be issues about "shared" assets used by all of the land such as water rights or farm machinery, and there may need to be easements to allow for the use of infrastructure that is fixed on one parcel.

The testator may decide to bequeath the farming operations to one or a limited number of beneficiaries, and leave shares in the land or shares in the family company to other beneficiaries. The testator and the person/s taking over the family farm may expect the other beneficiaries to become silent or passive land-owners or shareholders. The other beneficiaries may slowly simmer about the fact that the person currently running the farm operations has the homestead's rates and water paid for by the company or family trust, leases a car for their child through the company "because it's a farm ute", and fills up all of the family's cars at the petrol bowser on the farm. In relation t companies, there is a risk of claims that there is oppression of the minority or claims against the directors for breach of their fiduciary duties, and in relation to land the risk of section 66G Conveyancing Act claims.

Executor

The testator may not fully understand how the farm operations are structured. The testator's spouse or children may understand even less.

When the will is drafted, professional advisers should check with the testator if the testator has contacted the proposed executor to confirm that they are willing to do it. The professional adviser may suggest that the professional adviser confers with the testator and proposed executor so that the testator can explain how the farm operations are structured.

The testator should also be alive to the risk that appointing the person who is currently running the farming operations, or who is expected to take over the farming operations, may lead to difficult conflicts of interest.

Inter-generational Transfers

A rural family may take advantage of stamp duty and capital gains tax concessions for inter-generational transfers. It may be a condition of continuing finance – the financier requires the person currently operating the farming business to give a personal guarantee, and the person currently operating the farming business may be unwilling to do so unless they actually own the land and the machinery. An inter-generational transfer may also assist the testator and spouse access the age pension.

However, this may have unexpected consequences. In *Alexander v Jansson* [2010 NSWCA 176, the testator and his mother owned a rural property as tenants in common. His 94 year old mother had lived on the property for 73 years. Unfortunately, the testator died before his mother, and his children wanted to sell the property to obtain their inheritance, and force the mother to move. The testator's mother was compelled to bring family provision proceedings so she could remain living on the property.

Family Provision Claims and other claims

Even if the testator has engaged advisers for considered and comprehensive estate planning, this may be upset by family provision or other legal claims.

First, there may be claims by the child or children who worked on the farm. The child may have been paid less than award or nominal wages, and may not have pursued higher education or obtained trade qualifications because they were working on the farm. Their claim may be framed as a family provision claim,[3] or may also be framed as a proprietary estoppel or promissory estoppel claim on the basis that the testator made a representation that they would receive the farm, or a particular parcel, and they relied on the representation to their detriment.[4] However, it is not enough to show that the child worked on the farm. In *Vigolo v Bostin,*[5] the applicant worked on the family farm since he was 16 until he had a falling out with the deceased. However, he could not demonstrate the deceased had left him without adequate provision for his proper maintenance and advancement, because of his strong financial circumstances and the competing situations and claims on the testator's bounty of the other beneficiaries.

Alternatively, the testator may leave the farm to the child who stayed behind, but may impose difficult conditions. In *Couch v Couch* [2002] VSC 502, the will provided that the deceased's dairy farm be held on trust until the deceased's widow's death, and then to the applicant son subject to paying his brother a third of the net estate. The applicant son was concerned that the trustee would encumber or sell the farm during the widow's lifetime. Ashley J did not order that the farm be immediately transferred to the son, but ordered that the trustees could not sell the farm, could not encumber it except to raise capital for infrastructure improvements, and that the applicant son would pay a proportion of any interest on such loan.

Second, there may be claims by the child or children who left. The courts acknowledge that the testator has no obligation to treat the testator's children equally. As stated above, the child who stayed behind has often sacrificed part of his life to the rural enterprise, and has provided much of the support to the parents. In *Dobra v Brennan* [1999] WASC 98, Commissioner Martin QC said

> "Whilst Thomas had chosen his way of life as a farmer, that decision had been somewhat thrust upon him, by the difficult circumstances concerning James' ill health that had prevailed when Thomas was a boy of 15. Thomas has obtained no formal or professional qualifications, unlike his sisters. His whole livelihood and existence is based upon his capacity to derive an income from the Calingiri Properties, as he has been doing with varying success since 1970."

He noted that it was largely the son's efforts that resulted in the testator ultimately holding the valuable farming assets that he did. In *Carey v Robson* [2010] NSWCA 212, the NSW Court of Appeal noted that the son had spent all of his working life building the value of the rural farm enterprise, with little remuneration, at first with the testator and then, increasingly, by his own efforts, and the sisters had contributed little if anything to the value of the estate, and the son had largely borne the burden of looking after the testator in his illness.

In *Carey v Robson,* the testator transferred a parcel to his son during the testator's life time worth approximately $4.8 million, and the testator in his will left a parcel to his son worth approximately $4.5 million, and property and cash worth around $500,000 to each daughter. The NSW Court of Appeal noted that the testator was not obliged to treat his children equally and dismissed each daughters' claim.

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[3] McLeod v Hodge (unreported, 26 November 1984, McClelland J)

[4] *Kenneth Walter Waddell v Allan William Waddell: Estate Ronald John Waddell* [2011] NSWSC 1174*; Lewis v Lewis* [2001] NSWSC 321

[5] *Vigolo v Bostin* (2005) 221 CLR 191

Further, the courts strive to ensure that the rural farm enterprise remains viable. This issue will become more acute as the strong Australian dollar damages Australian agricultural competitiveness and many of Australia's rural properties move into drought.[6] In *Dobra v Brennan*, the properties had always been worked as one farming unit, and the lands would not be sufficient to continue a viable farming operation.

In *Salmon v Osmond*[7] two of the testator's daughters were seeking two of the parcels of property. The trial judge Ball J noted that the property was marginal and was supporting two families - the beneficiary son and his family, and the testator's widow. In addition, there was evidence that the rural farming enterprise could only be operated as an integrated whole.

Defending a case may require detailed evidence about the farm's profitability and viability. This may include balance sheets, profit and loss statements, livestock holdings, calving and weaning rates. This may also include independent information such drought and flood projections and long term trends from Australian Bureau of Agricultural and Resource Economics and Sciences (ABARES) and the Bureau of Meteorology. This may also include expert reports prepared by agricultural consultants and accountants.

However, litigants need to be advised that they will need to swear that their financial information is correct. The other parties may issue subpoenas to third parties to cross-check information that the litigant has provided to third parties is the same as the information in the litigant's affidavit. The litigant must ensure that the financial information that forms part of their affidavit is consistent with information that they have provided to their bank, information that they have provided to the Australian Tax Office, information that they have provided to an ex-spouse as part of a property settlement pursuant to the Family Law Act, or information provided to a trustee in bankruptcy. Further, they need to be advised that the information may be used against them in other contexts such as a property settlement.

In any case, in *Salmon v Osmond*, the trial judge Ball J acknowledged that the viability of the farm may need to yield to providing provision, and this was accepted by the NSW Court of Appeal at [98] per Beazley P (McColl and Gleeson JJA agreeing). Ball J said at [92]

> **"**The effect of the order I have proposed gives Michael reasonable prospects of remaining on the farm in the long term. But if that is not possible, he will have adequate assets on which he can live. As I have said, the preservation of the farm cannot be a determinative consideration.

A further twist is when an applicant applies for provision from an estate in circumstances where the applicant already has an interest in an unrelated rural farm enterprise. A family provision applicant must demonstrate need. At first blush, it may appear that the applicant has no need when they have an interest in a rural farm enterprise. However, the applicant may be asset rich and cash poor, or may be involved in a rural farm enterprise where they have little control. In *Lloyd-Mayfield v Williams* (2005) 63 NSWLR 1, the NSW Court of Appeal (Bryson J, Giles and Stein JJ concurring) confirmed that the applicant was entitled to significant provision from her father's estate to purchase a house in town notwithstanding her interest in her husband's family's property and an interest in the family discretionary trust. Bryson J described many of the debits and credits in the rural farm enterprise as "fairy gold" because they were not readily enforceable. The trial judge (White J) said that it was not unreasonable for the applicant and her husband not to sell the property to fund their retirement, because the property was being used to support a number of families in a rural farming enterprise and they intended to leave the property intact to pass on to the next generation. Bryson noted at [12]

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[6] http://www.bom.gov.au/climate/drought/#tabs=Drought-Statement

[7] *Salmon v Osmond* [2015] NSWCA 42 (trial *Peters v Salmon* [2013] NSWSC 953

> "In the present case, it is not solely in pursuit of financial advantages for themselves that the respondent and her husband participate in the Partnership and the Trust, and it cannot be expected that it will ever be; as is quite familiar in rural life, they are participating in a continuing enterprise involving the interests of several generations of closely related persons. Disrupting the arrangements would disrupt the pattern of family relationships upon which their lives and happiness are formed, and would also disrupt the interests, expectations and life plans of close relatives with whom they feel a sense of identity. "

The testator may consider that creating a discretionary trust may limit the testator's estate from family provision claims. In *Flinn v. Fearne* [1999] NSWSC 1041, Master McLaughlin did not designate a discretionary trust as notional estate where the testator was the settlor and appointed the trustees because the trustees were independent and had fiduciary duties to the beneficiaries. However, in *Kavalee v Burbidge*[8], the NSW Court of Appeal designated a Liechtenstein stiftung (similar to a discretionary trust) as notional estate because the trustee was required to act in accordance with the testator's instructions. More recently, in *Wardy v Salier*,[9] the appointor of the trust was not the testator, and the trustee was not the testator – it was a corporate trustee that always had two directors, the testator and his son. However, the corporate trustee *sole shareholder was the testator*. Therefore, a discretionary trust may be regarded notional estate for the purposes of Chapter 3 Succession Act if the testator was the trustee or controls the corporate trustee.

Estate litigation may also affect the rural farm enterprise banking facilities. The bank may require the person operating the rural farm enterprise to give personal guarantees even though the person does not have any of the estate's assets because the executor may not distribute the estate pending a family provision claim because the executor is not protected.[10] The bank's covenants may require the rural farm enterprise to notify the bank of the litigation. Estate litigation costs are personal expenses relating to the testator's personal affairs. Further, if a court orders provision, it takes effect as a codicil to the will.[11] Therefore, the cost of borrowing to finance the litigation or the provision may not be tax deductible.

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8 *Kavalee v Burbidge* (1998) 43 NSWLR 422

9 *Wardy* v *Salier* [2014] NSWSC 473

10 section 93 Succession Act 2006 (NSW)

11 section 72 Succession Act 2006 (NSW)