

ESTATE PLANNING & LPR ADMINISTRATION ISSUES

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WILLS AND ESTATES UPDATE

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1 General Overview

This paper focuses on discreet issues regarding the administration of an estate. The legal personal representative or representatives of an estate will therefore find this paper of most relevance.

The information, however, can be used in the estate planning context as the issues of how the estate is ultimately administered have a significant, and too often overlooked, impact on the preparation of estate plans and the drafting of clients' wills.

There are eight discreet topics considered herein. They are:

1. Executors / Executrixes and Administrators vs Trustees
2. Informal Wills
3. Liability of the legal personal representative or representatives;
4. Stamp duty issues for beneficiaries;
5. Tax issues in estate administration;
6. GST issues in estate administration; and
7. in some detail, Testamentary trusts.

By their nature – being discreet issues, albeit with relevance to each other – it is convenient to consider them separately.

2 Executors / Executrix's and Administrators vs Trustees

Given that this paper focuses on the administrative issues for the legal personal representative, but that a large part of it will focus on testamentary trusts, it is appropriate to consider the similarities and differences between an executor or executrix or administrator, on the one hand, and a trustee, on the other hand, in the administration of estates and management of assets thereafter.

In doing so this paper the term *legal personal representative* refers to an executor / executrix or administrator carrying out their functions up to the end of the administration of a deceased's estate. Once an executor / executrix or administrator becomes – for an asset of the deceased or a newly acquired asset – the trustee of a testamentary trust, their new role is referred to as a *trustee*.

2.1 Differentiating as between an 'executor' and a 'trustee'

Although both legal personal representatives and trustees are in a fiduciary relation (in particular, the duty to due administration) with respect to a beneficiary, the duties of an executor differ from the duties of a trustee of a trust created under a will. A legal personal representative is appointed by a deceased to execute, manage, administer, direct and dispose of a deceased's will. A legal personal representatives is required to get in the assets of the deceased, pay expense, and distribute the residuary estate in accordance with the will (or intestacy or order of the court): see *Re Chirnside* [1956] VLR 295.

A legal personal representatives only has a power to act in relation to a deceased's property after a grant of probate is obtained: *The Daily Pty Ltd v White* (1964) 63 WN (NSW) 262. That is, a legal personal representative's duties and powers are based on the principle that a legal personal representative is required to wind-up the deceased's estate. In contrast, a trustee has an on-going role, dependent on the term and duration in the trust deed.

With respect to a residuary estate, a change in character from a legal personal representative to a trustee occurs when an estate has been fully administered – that is, when all of the debts and liabilities have been discharged and the residuary is ascertained. Further, a legal personal representative (if property is retained after executorial duties are performed – see below) can become a trustee with respect to different assets of the estate at different times – acting in both the capacity of trustee and executor: see *Porteous v Rinehart* (1998) 19 WAR 495 at 503.

The duties of a legal personal representative are more circumscribed than those of other trustees. *Hansen v Young* [2004] 1 NZLR 37 is authority for the proposition that the primary responsibilities of legal personal representatives are those that relate to:

- the collection of the testator's debts;
- the identification of assets of the deceased;
- the payment of funeral and testamentary expenses; and
- the discharge of legacies provided under the will.

Lindley LJ in *Re Chapman* [1895] All ER 1104 observed that the role of an executor is:

[S]imply to call to the testator's unsecured debts and to convert into money so much of his personal estate as was necessary to enable him to then pay his funeral and testamentary expenses and his debts and pecuniary legacies and to handover to trustees whatever personal estate was not wanted for those purposes.

Isaacs J in *Union Bank of Australia v Harrison, Jones & Devlin Ltd* (1910) 11 CLR 492 at 515-516 observed that:

'Death, while removing the individual, leaves the property, debts, and claims of the deceased still remaining. His nomination of an executor is a request to represent him for certain purposes including the payment of debts, and do what he can no longer do for himself. Wentworth ... says that the office of executors is 'to execute the mind, will, and intent of their testator' ... And for this reason that 'the main and principal part of an executor's office, and that which concerns the soul of a testator ... is the payment of his debts: now who knows not that the very making of an executor is the continuing of such a person who is to pay all debts'.

Isaacs J at 515 further observed that a legal personal representative is ‘... *the minister and dispenser and distributor of the testator’s property ...*’.

In contrast, the essential duties of a trustee of a trust which is created under a will is to obtain control of the trust property. It was observed in *Hansen v Young* [2004] 1 NZLR 37 that the responsibility of trustees of trusts that are created under a will include:

- gather in funds due to the trust estate;
- preserve trust property, secure it from risk and loss; and
- conform to, and carry out the terms of the trust.

2.2 Similarities as between legal personal representatives and trustees

There are some similarities as between legal personal representatives and trustees. Specifically:

- both legal personal representatives and trustees owe a fiduciary duty of due administration to the beneficiaries: see *Johnson v Trotter* [2006] NSWSC 67;
- in the event of misapplication of trust property, then the equitable entitlement to trace subsists: see *Foskett v McKeown* [2001] 1 AC 102;
- trustee legislation include ‘legal personal representative’ within the definition of ‘trustee’: see for example section 5 of the *Trustee Act 1925* (NSW). As a result, the courts have a statutory (and inherent) power to remove trustees and executors: see for example *Gibbs v Gibbs* [2004] WASC 132. However, it should be noted that except in Victoria, the respective trustee provisions do not allow a court to appoint a new executor: see for example s 6(12) of the *Trustee Act 1925* (NSW).
- In most jurisdictions probate and administration legislation allows commissions to personal legal representatives and trustees of testamentary trusts: see s 86 of *Probate and Administration Act 1898* (NSW). Although not specifically provided for in NSW, commissions may be provided to NSW trustees under the ‘expediency’ jurisdiction.

2.3 Distinctions as between legal personal representatives and trustees

The powers and duties of legal personal representatives and trustees differ: see *Vacuum Oil Co Pty Ltd v Wiltshire* (1945) 72 CLR 319 at 324-325. Specifically:

- A legal personal representative is obliged to wind-up a deceased's estate, whereas a trustee has an on-going role. As a result, executors have a broader power of sale than trustees: see for example s 153 of the *Conveyancing Act 1919* (NSW). However, a trustee has a broader power to carry on a business than a legal personal representative has.
- Both the legal and equitable interests in the estate is held by the legal personal representative. In contrast, only the legal interest vests in a trustee.

However, a legal personal representative still has fiduciary duties. Whilst both legal and beneficial interests are held by legal personal representatives, the full beneficial ownership is not held by the legal personal representatives, and they are still bound by fiduciary duties owed to beneficiaries of the estate: *Hosken v Danahar* [1911] VLR 214. Whilst beneficiaries of unadministered estates do not have an equitable interest in the estate, they have no right to caveat any property held subject to the estate: *Meynert v Leafdale Pty Ltd* [2005] WASC 102 at [32] – [39]. However, beneficiaries do have a right to secure proper administration of the estate: *Commissioner of Stamp Duties (QLD) v Livingstone* [1965] AC 694 and *Official Receiver in Bankruptcy v Schultz* (1990) 170 CLR 306.

Further, a legal personal representative who retains property after its executorial duties are performed will become a trustee with respect to the property: *McCaughey v Commissioner of Stamp Duties* (1946) 46 SR (NSW) 192. At that time, the equitable interest of the beneficiaries become vested, quantifiable and identifiable: *Probert v Commissioner of State Taxation* (1998) 72 SASR 48.

- In disposing trust property, trustees are required to act unanimously. However, individual executors can bind an estate, and can do so without concurrence of any other legal personal representatives: see *Johnson v Trotter* [2006] NSWSC 67 at [21], *Attenborough v Solomon* [1913] AC 76 and *Exception Holdings Pty Ltd (in liq) v Albarran* (2005) 223 ALR 487 at [20] – [26].

- During administration, executors cannot retire or appoint successor trustees. In contrast, appointment and removal of trustees is provided for in statute. However, an executor who holds an estate upon trust (i.e. after administration) may use the statutory powers: *Re Cockburn's Will Trusts* [1957] 1 Ch 438 and *Estate of Graham* [1910] VLR 466.

Further, in some jurisdictions, there are distinctions with respect to limitation of actions as between executors and trustees.

3 Informal Wills

In relatively recent Supreme Court decisions¹ in New South Wales and Queensland Supreme Court it has been made clear that it is not only formal, printed, signed and witnessed documents that can constitute a valid will. The wide variety of circumstances in which a deceased can express himself or herself, exacerbated in these times of apps, personal computers and tablets, an executor or their advisers must be vigilant to ensure they are fully comprised of the testator's or testatrix's wishes and testamentary dispositions.

The Courts will try to give effect to a deceased's testamentary intention if they can. The cases here considered bear out what Mahoney JA said 20 years ago,² *'There are, in the history of this branch of the law, many cases in which the intention of the deceased has not been able to be given effect. That is an evil which should be remedied as far as may be.'*

As practitioners it is incumbent on us to ensure those testamentary intentions, wherever they be located, are made known to the Courts. This includes the various modern devices on which intentions may be recorded. The cases, which will be considered in turn, are a timely reminder to us of that obligation.

3.1 Yazbek's Case – Microsoft Word³

Justice Slattery summarized the issue in Yazbek's Case at [1]:

The late Daniel Yazbek ("Daniel") was a creative and entrepreneurial restaurateur with a flair for Japanese cuisine. Daniel was born on 1 December 1970, the sixth child of a family of eight siblings. He died at the age of 39 on 18 or 19 September 2010. In these proceedings the plaintiff, Acob Yazbek ("Alan"), one of Daniel's brothers, propounds an informal testamentary document as Daniel's will. The defendants, Ghosn Yazbek ("Ghosn"), Daniel's father, and Mouna Yazbek ("Mouna"), Daniel's mother, resist this relief. They say Daniel died intestate.

The legal issue was whether the "Will.doc" or a printed out paper copy of it satisfied the requirements of s 8 of the *Succession Act* 2006 (NSW) (the "**Succession Act**") sufficient for the Court to declare either to be Daniel's last will.⁴ That section provides:

¹ In New South Wales the decisions of *Ian Yazbek v Ghosn Yazbek & Anor* [2012] NSWSC 594 ("**Yazbek's Case**"), *Costa v The Public Trustee of NSW* [2008] NSWCA 223 ("**Costa's Case**"), *Newman v Brinkgreve*;

² *Re Estate of Masters (decd)*; *Hill v Plummer* (1994) 33 NSWLR 446 at 462.

³ As this case also sets out the framework of s 8 of the *Succession Act* it is longer than the analysis of other NSW decisions in this paper.

8 When may the Court dispense with the requirements for execution, alteration or revocation of wills?

- (1) This section applies to a document, or part of a document, that:
 - (a) purports to state the testamentary intentions of a deceased person, and
 - (b) has not been executed in accordance with this Part.
- (2) The document, or part of the document, forms:
 - (a) the deceased person's will—if the Court is satisfied that the person intended it to form his or her will, or
 - (b) an alteration to the deceased person's will—if the Court is satisfied that the person intended it to form an alteration to his or her will, or
 - (c) a full or partial revocation of the deceased person's will—if the Court is satisfied that the person intended it to be a full or partial revocation of his or her will.
- (3) In making a decision under subsection (2), the Court may, in addition to the document or part, have regard to:
 - (a) any evidence relating to the manner in which the document or part was executed, and
 - (b) any evidence of the testamentary intentions of the deceased person, including evidence of statements made by the deceased person.
- (4) Subsection (3) does not limit the matters that the Court may have regard to in making a decision under subsection (2).
- (5) This section applies to a document whether it came into existence within or outside the State.

⁴ Other parties alleged Daniel had printed the "Will.doc", signed it and later destroyed it, thereby revoking that document (printed or not) as a testamentary document. This issue

His Honour found that “Daniel” prepared a Microsoft Word document, entitled “Will.doc” on his computer between 11 and 14 July 2009, just before he left for an overseas holiday, and 14 months before his death. The Police found Daniel’s death to be suicide and, in doing so, searched various electronic devices including a laptop computer. It contained the “Will.doc”. The “Will.doc” contained well wishes to Daniel’s family and friends, descriptions of how some (but not all) of Daniel’s property should be distributed and his name typed at the conclusion of the document. It was edited over a 3 day period of editing and last accessed on 1 September 2010, 8 or 9 days before Daniel’s death.

Justice Slattery held the “Will.doc” was Daniel’s will. A [77] and [78]⁵ his Honour noted there is no substantive difference between s 8 of the Succession Act and its predecessor (s 18A of the *Probate and Administration Act 1898 (NSW)*), and that the requirements of execution under that predecessor provision are clear:

1. there must be a document – by s 3 of the Succession Act and s 21 of the *Interpretation Act 1987 (NSW)* a word document in soft copy is a “document”;⁶
2. which purports to state the deceased’s testamentary intentions – his Honour held the “Will.doc” did so because it dealt with a large part of the estate, was saved under the name “Will.doc”, referred to Daniel’s life in the past tense and because of the structure of the “poignant messages” to his family in the document; and
3. which the deceased intended to form his will – his Honour held Daniel so intended as he named the document “Will”, told people he had a will & had said it was at least on his computer, it immediately preceded overseas travel, Daniel typed his name after the salutation and he opened it without amending shortly before his death. These considerations outweighed countervailing considerations.

⁵ Quoted with approval by Hallen J in *Bolger & Anor v McDermott & Anor* [2013] NSWSC 919 at [103] (considered below).

⁶ Justice Slattery also noted *Re Trethewey* [2002] VSC 83 per Beach J and *Mahlo v Hehir* [2011] QSC 243 per McMurdo J to the same effect under the Victorian and Queensland equivalent legislation.

Another important aspect of *Yazbek's Case* was the approach approved in rejecting the defendants' argument for revocation. At [127] Slattery J held you do not look in detail to the law of revocation, but instead you look to the test asked by s 8 of the Succession Act. That is, you merely apply s 8 at the relevant time rather than applying it earlier and looking for evidence of revocation. This may be obiter, however, as even if that law was applied his Honour would still have found no revocation occurred.

What is clear – especially when *Yazbek's Case* is contrasted with decisions such as *NSW Trustee and Guardian v Pittman – Estate of Koltai* [2010] NSWSC 501 and *Bell v Crewes* [2011] NSWSC 1159 – is that the Court will discern whether the deceased intended the informal document to operate as a will. For instance in *Bell v Crewes* the fact that the document provided for a signature, and it was not signed, weighed heavily in finding the printed document was not a will. In assessing an informal will, therefore, indications that the deceased intended it to be a will should be the focus of your attention.

3.2 Costa's Case – Suicide Note

Before committing suicide Robert Costa left a hand-written document that was found in his bedroom. It was written in the form of a poem and was addressed to his parents. Included in the poem were the words, '*I think I'm dying*' and '*I want you to have my house*'. The deceased's house was his only valuable asset. The deceased's parents sought the grant of probate. The issue was whether the deceased had the intention for the document to constitute a will. At first instance Windeyer J dismissed the claim, holding that there was no such intention. His Honour held⁷ at [19]:

After careful consideration I consider that the document propounded is in the nature of a suicide note expressing wishes and requests and not a document intended to operate as a testamentary instrument. Its form and wording lead to that conclusion. It follows that I am not satisfied the requirements of s 18A are made out.

⁷ At first instance see *Costa v The Public Trustee in the Estate of Robert Costa aka Way Geary Coaster* [2007] NSWSC 1271.

The parents successfully appealed that decision. The Court of Appeal⁸ held that inferences may be drawn in applying the test of s 18A of the *Probate and Administration Act* 1898 (NSW) (now s 8 of the Succession Act) and in this case the correct inference was that the deceased intended the poem to constitute his will. The facts underlying that inference were to be applied as follows:⁹

I would give less weight than the primary judge apparently did to the precatory wording of the document, the deceased's knowledge of the requirements of a valid will, the lack of a signature and the form of the document.

I would give more weight to the consideration that the document was written on a solemn unique occasion, as a last message to his parents, the persons apparently closest to him. I would give more weight to the consideration that, if the document was no more than an emotional expression of wishes, the house would to the deceased's knowledge be disposed of under his will to an ex-acquaintance with whom the deceased's relationship had broken down and with whom the deceased had lost contact. I do not think it likely that the deceased was, by this document, intending to do no more than to indicate an ineffectual emotional wish for something that would not happen.

Costa's Case shows not only the nature of the inquiry – establishing facts from which an inference of the deceased's intention, which is largely undiscoverable, can be determined – but also the various ways in which the testamentary intention can be found. Here being a suicide note delivered in poem.

3.3 Newman's Case – Surrounding Circumstances will assist

⁸ Hodgson, Ipp and Basten JJA.

⁹ See Hodgson JA at [27] to [29] on which point Ipp JA (at [52]) and Basten JA (at [114]) agreed.

In Newman's Case the deceased was a patient in hospital in 2011 when he wrote, on the back of some clinical notes, a purported alteration to his 2004 will. It was held to be a valid amendment to his will. Newman's Case makes clear that the circumstances surrounding the document will be important in assessing the document under s 8 of the Succession Act. In upholding the 2011 document Hallen J relied on the fact that the deceased was in hospital, initiated the 2011 document himself, crafted it carefully to avoid errors, made earlier comments on relationships consistent with the outcome of the 2011 document, had experience in executing wills and referred to the document as a will, sought witnesses, dated and signed the document, said his '*mind is strong and I know what I'm doing*' and that the deceased requested the document be placed with his medical records.

3.4 Bolger's Case – Stop gap wills

Bolger's Case is an example of informal documents being rejected as the deceased's will. It does not set out new grounds in relation to informal wills but reference is made to Bolger's Case, however, for 2 reasons: it contrasts with the outcome of the other 3 cases here considered and it reaffirms (at [111] and [112]) the ability of a 'stop gap' will to operate. A 'stop gap' will intended to be interim in operation but taking effect on the testator's death before the further contemplated will can be completed.

The case was a bitter dispute between family members.¹⁰ The deceased had executed a professionally drawn will and codicil to it (both on 18 September 2008), but had also, subsequently, prepared a typed document and a handwritten document (both on 30 June 2009). The typed document was a typed version of the handwritten documents. The 30 June 2009 documents were not executed. Although his Honour had concerns about the manner in which the 30 June 2009 documents came to be (see at [113]), he ultimately held those documents were not the deceased's and he did not intend them to revoke his earlier will.

3.5 Re Yu's Case – iPhone 'Notes'

¹⁰ Justice Hallen's comments at [1] to [4] show how bitter.

Though *Re Yu's Case* was an *ex tempore* decision of some 10 paragraphs only it remains instructive. Shortly before his suicide the deceased created a series of records on his iPhone, in the "Notes" program. Some of the notes were messages the deceased intended to be read after his death, including a purported will. It was titled '*This is the last Will and Testament ...*' in which the deceased named an executor and provided for his property to be gifted away. The named executor applied to the court seeking that the iPhone record be proved as a will.

3.5.1 Requirements of a will

The iPhone record did not meet the formal requirements of a will required by section 10 *Succession Act 1981* (Qld) (the "***Qld Act***"), namely that it:

- be in writing
- be signed by the will-maker (or someone else in the presence of an at the direction of the will-maker), and
- have two independent persons who are present at the same time to witness the will-maker's signature.

A will which does not meet the formal requirements (sometimes referred to as an informal will) may be proved as a valid will provided that certain conditions are met (see s 18 of the Qld Act).

First condition: there must be a document in existence.

The definition of document is found in section 36 *Acts Interpretation Act 1954* (Qld) and is in broad terms. Basically, it includes any paper of material on which there is writing or marks, and '*any disk, tape or other article or material from which sounds, images, writing or marks are capable of being produced or reproduced (with or without the aid of another article or device).*'

Justice Peter Lyons considered *Yazbek's Case* (see above). With reference to that case, and the cases cited in it, the judge was satisfied the record on the iPhone was of a similar nature to the Word document and therefore, it met the definition of document.

Second condition: whether the document purports to state the testamentary intentions of the deceased. That is, the document must deal with the distribution of the deceased's property on their death.

Justice Lyons considered it relevant that the document:

- dealt with the whole of the deceased's property;
- was created by the deceased when was contemplating his imminent death (which was evidenced by the fact that the deceased had also created numerous final messages in the Notes app around the same time);
- appointed an executor as well as nominated a substitute executor; and
- the document authorised the executor to deal with the deceased's affairs in the event of his death.

Consequentially his Honour gained the general impression that the document set out the testamentary intentions of the deceased.

Third condition:the deceased must have intended the document to form his will.

The document must be more than a mere letter or memorandum of wishes. The deceased must intend it to be a legally binding document by which their property is disposed on their death. Justice Lyons was satisfied that the deceased held the requisite intention based on the terms of the document alone. It does not appear from his Honour's judgment that he considered any external evidence as to the deceased's intention. For instance, evidence that the deceased told someone he had created a will and it could be located on his electronic device (as occurred in *Yazbek's Case*). Indeed, the decision does not make plain how the executor became aware of the notes on the deceased iPhone.

His Honour considered the relevant matters to be:

- the document commenced with the words '*This is the last will and testament ...*';
- the deceased formally identified himself and his address;
- the document clearly appointed an executor;

- the deceased typed his name at the end of the document in a place where a signature would appear on a paper document and then typed the date followed by his address again; and
- the document was created shortly after a number of final messages were created.

As the three conditions were satisfied, the application was successful and the court issued a grant of probate of the iPhone document to the executor named in it.

3.6 Conclusion re Informal Wills

While the circumstances of some of these cases makes for very interesting reading, a will should always, where possible, meet the formal requirements set out above. The types of application referred to above involves cost, delay and uncertainty as to the outcome. A will that meets the formal requirements is far more likely to result in the will being administered in an efficient way.

However, the cases make clear that practitioners must confirm the deceased's testamentary intentions, which may not be limited to formal will executed in accordance with the legislation. Thinking outside the square may be required of us.

4 Liability of the Legal Personal Representative(s)

The liability of a legal personal representative in a Commonwealth tax context is dealt with in more detail at 6.2 below. Here the liability of a legal personal representative generally is considered.

4.1 Probate Legislation

Section 91 of the *Probate and Administration Act 1898* (NSW) provides an indemnity to legal personal representatives, but it is limited to circumstances where the grant of probate is invalid, or otherwise affected, and that issue causes the liability of the executor.

4.2 Indemnity Generally

In certain circumstances trustees – and for many purposes legal person representatives are considered to be trustees of an estate are trustees – are indemnified from the trust's (or estate's) assets. However, that right of indemnity is a right to resort to and apply trust funds for the discharge of liabilities incurred in the *authorised conduct of the trust*: *Octavo Investments Pty Ltd v Knight* (1979) 144 CLR 360 at 371.

While it is true that case law establishes the indemnity applies in circumstances where the trustee was wrong, it is important to note that those cases apply where a third party – as opposed to the beneficiaries – sues the trustees. For instance:

- In *Re Raybould* [1900] 1 Ch 199 the trustee was carrying on a colliery business as part of the trust estate and, in the course of operations, he caused the subsidence of a neighbour's land and consequent injury to the buildings; it was held that the trustee's personal liability in damages could be recovered from the trust assets.
- In *Bennett v Wundham* (1862) 45 ER 1183 the trustees of a settled estate employed woodcutters to cut down some trees on the settled estate and during the carrying out of the work, a bough fell and injured a passer-y who recovered heavy damages against the trustee. It was held that the trustee was entitled to indemnity out of the trust estate.
- In *Gastios Holdings Pty Ltd v Nick Kritharas Holdings Pty Ltd (in liq)* [2002] ATPR 41-864 the NSW Court of Appeal held that the trustee of a trading trust, found to have contravened the *Trade Practices Act 1974* (Cth) in the course of the trust business, was entitled to be indemnified.

Again, they were not beneficiaries suing the trustee. This is significant as the trustee – or in the case of a deceased estate, a legal personal representative – seeking indemnity from the estate when being sued by the beneficiaries would be self-defeating. The beneficiary's claim is for the effect the trustee's actions had on the estate. To indemnify such a claim from the estate would render the beneficiary's claim practically meaningless: see *Cherry v Boulthée* (1839) 41 ER 171. In that case it was held that a trustee that owes the trust cannot benefit from the right of indemnity until the debt owed is satisfied. That is, where the trustee has some obligation to the trust estate the right of indemnity is postponed behind the trustee's obligation. If the trustee is held to have breached the trust, and therefore is liable to the beneficiaries, the right of indemnity would be postponed to that claim.

Further, the question of authorisation is crucial. If the trustee's activities were not authorised by the trust instrument – or relevantly, the will – prima facie no right of indemnity can arise, and if they were authorised prima facie a right of indemnity does arise: *R W G Management Ltd v Commissioner for Corporate Affairs* [1985] VR 385 at 396-7.

There can be specific examples where different rules apply. For instance, Geddes, Rowland & Studdert in *Wills, Probate and Administration Law in New South Wales*, LBC1996 Sydney at 404,[48.11] state:

The remedies for devastavit by a personal representative are not the same as the remedies for breach of trust.

Somewhat unhelpfully the authors cite no authority in support of that proposition. However, it means that the restrictions on indemnity for breach of trust may not be directly applicable for devastavit (allowing assets of the estate to waste).

4.3 Indemnity clause in the will

There is a clear distinction between the liability of an executor to beneficiaries compared to creditors; since beneficiaries are bound by the terms of the will protection may be afforded, for instance an exclusion clause: *Armitage v Nurse* [1988] Ch. 241.

If a will contains an exclusion clause the legal personal representative will stand to benefit from that clause.

The starting point is that an exclusion clause concerning a trustee will be read no more broadly than its language requires on a fair reading: *Walker v Stone* [2001] 2 WLR 623 at 657 per Sir Christopher Slade.

Further, the exclusion is not available where the trustee has acted with mala fides or dishonestly: *Armitage v Nurse* [1998] Ch 241 at 252 per Millet LJ.

Finally, the context in which the clause appears, that is the whole document and setting, is relevant to its construction: *Darlington Futures Ltd v Delco Australia Pty Ltd* (1986) 161 CLR 500 at 510 per Mason, Wilson, Brennan, Deane and Dawson JJ.

4.4 If beneficiaries instigated the breach

Section 86 of the *Trustee Act 1925* (NSW) allows indemnity to trustees if the beneficiaries have directed the conduct that is a breach. It provides:

- (1) Where a trustee commits a breach of trust at the instigation or request or with the written consent of a beneficiary, the Court may, if it thinks fit, make such order as to the Court seems just for impounding all or any part of the interest of the beneficiary in the trust estate by way of indemnity to the trustee or person claiming through the trustee.
- (2) The provisions of subsection (1) shall be deemed to empower the Court to impound all or any part of the interest of any beneficiary who receives any pecuniary benefit from the breach of trust.
- (3) This section applies notwithstanding that the beneficiary may be a married woman entitled for her separate use and restrained from anticipation.
- (4) This section applies to breaches of trust committed as well before as after the commencement of this Act, but shall not prejudice any question in any suit or other proceeding instituted before and pending at the commencement of this Act.

Consideration should often be given to this provision.

4.5 Relief for Breach

Section 85 of the *Trustee Act 1925* (NSW) gives the court power to relieve a trustee of the consequences of any breach of trust they have committed. It provides:

- (1) Where a trustee is or may be personally liable for any breach of trust, the Court may relieve the trustee either wholly or partly from personal liability for the breach.

- (2) The relief may not be given unless it appears to the Court that the trustee has acted honestly and reasonably, and ought fairly to be excused for the breach of trust and for omitting to obtain the direction of the Court in the matter in which the trustee committed the breach.
- (3) (Repealed)
- (4) This section applies whether the transaction alleged to be a breach of trust occurred before or after the commencement of this Act.

Consideration should also often be given to this provision.

5 Stamp Duty Issues for Beneficiaries

Section 63 of the *Duties Act 1997* (NSW) ('the Duties Act') provides that:

- (1) Duty of \$50 is chargeable in respect of:
 - (a) a transfer of dutiable property by the legal personal representative of a deceased person to a beneficiary, being:
 - (i) a transfer made under and in conformity with the trusts contained in the will of the deceased person or arising on an intestacy, or
 - (ii) a transfer of property the subject of a trust for sale contained in the will of the deceased person, or
 - (iii) an appropriation of the property of the deceased person (as referred to in section 46 of the *Trustee Act 1925*) in or towards satisfaction of the beneficiary's entitlement under the trusts contained in the will of the deceased person or arising on intestacy, and
 - (b) a consent by a legal personal representative of a deceased person to a transmission application by a beneficiary, and
 - (c) a transmission application to a devisee who is also the sole legal personal representative.
- (2) If a transfer of dutiable property is made by a legal personal representative of a deceased person to a beneficiary under an agreement (whether or not in writing) between the beneficiary and one or more other beneficiaries to vary the trusts contained in a will of the deceased person or arising on intestacy, the dutiable value of the dutiable property is to be reduced by the portion of the dutiable value that is referable to the dutiable property to which the beneficiary had an entitlement arising under the trusts contained in the will or arising on intestacy.
- (3) Section 25 does not apply to a dutiable transaction to which subsection (2) applies.

The Chief Commissioner of State Revenue for New South Wales gives the following example of an appropriate under 46 of the *Trustee Act 1925* (NSW):

Two beneficiaries (A and B) are equally entitled to the residue of a deceased estate which comprises:

- The family home value at \$500,000
- Shares value at \$500,000

Each beneficiary is entitled to half of the family home and half of the shares. The trustee appropriates the family home and the shares so that the family home will be transferred 100% to A and the shares will be transferred 100% to B.

Concessional duty of \$50 will be chargeable on the transfer of the family home to A.

This only applies where a trustee invokes their power under the Trustee Act 1925 to appropriate the property of the estate in or towards satisfaction of the beneficiary's entitlement under the estate. The \$50 duty concession does not apply where the beneficiaries agree to vary the trusts contained in the will, or arising on intestacy.

It can be seen, then, there is a critical difference between the legal personal representative choosing to appropriate in accordance with their power under s 46 of the *Trustee Act* 1925 (NSW) and that of the beneficiaries entering into a *Deed of Family Arrangement*.

It should also be noted that stamp duty on transfers of shares in private companies was abolished on and from 1 July 2016.

6 Tax Issues in Estate Administration

As this paper focuses on the legal personal representative or representatives the tax issues that arise in an estate's administration will be considered from that vantage point. That is, the tax issues for the legal personal representative in undertaking the estate administration, rather than the tax liabilities of the beneficiaries on assets passing to them from the estate, will be the paper's concern.

6.1 Deceased's Tax Liability Arises at Death

Even though taxpayers only have to pay tax when it is due for payment, often as a result of an assessment, their tax liability arises at year end; that is, before the income tax return is filed: s 4-10(1) of the *Income Tax Assessment Act 1997* (Cth) (the '1997 Act'). But the obligation to pay depends on either the issue of a notice of assessment or the date specified in the relevant ATO *Legislative Instrument*¹¹ for lodgment of tax returns. When income tax is "due and payable", it becomes a debt due to the Commonwealth: s 208 of the *Income Tax Assessment Act 1936* (Cth) (the '1936 Act') and s 255-5(1)(a) of Schedule 1 to the *Taxation Administration Act 1953* (Cth) (the 'TAA').

If income tax is imposed on income derived at year-end, as is the case with s 4-10 of the 1997 Act, a deceased person's liability arises at the time of death. This is despite the fact that there has been no assessment for that year: *Commr of Stamps (WA) v West Australian Trustee, Executor and Agency Co Ltd* (1925) 36 CLR 98. The assessment process is only a timing mechanism for payment and the basis for an objection or appeal.

6.2 Statutory Vicarious Liability

Division 260-E of Schedule 1 to the TAA sets out a special tax obligation and collection regime for legal personal representatives for outstanding tax-related liabilities of the deceased at the time of their death. The regime does not apply to tax liabilities that arise after death, which are the legal personal representative's separate responsibility.

The term "tax-related liability" is defined to be '*a pecuniary liability to the Commonwealth arising directly under a taxation law – including a liability the amount of which is not yet due and payable*': s 255-1 of Schedule 1 to the TAA. Once it is due and payable, it becomes a debt due to the Commonwealth and is payable to the Commissioner of Taxation: s 255-5(2).

¹¹ See the *Legislative Instruments Act 2003* (Cth).

The term “outstanding tax-related liability” of an entity at a particular time is defined in s 995-1 of the 1997 Act to be a tax related liability of an entity:

- (a) that has arisen at or before that time (whether or not it is due and payable at that time); and
- (b) an amount of which has not been paid before that time.

Subsection 260-140(2) of Schedule 1 to the TAA applies if a deceased had a tax liability at death – an outstanding tax related liability – and there has been either a grant of probate of the deceased’s will or of letters of administration of the deceased’s estate. It provides that the Commissioner of Taxation may, for the liability, deal with the legal personal representative as if the deceased person were still alive and the legal personal representative were that deceased person.

The relative onerous tax liabilities to which the legal personal representative or representatives are then subject are:

- to provide any returns and other information that the deceased person was liable to provide, or would have been liable to provide if they were still alive: s 260-140(3)(a);
- to provide any additional returns or other information relating to the liability that the Commissioner of Taxation requires: s 260-140(3)(b);
- to discharge, in the legal personal representative’s capacity, the liability and any penalty imposed for the liability under a taxation law (including any general interest charge) that the deceased person would be liable for if they were still alive: s 260-140(3)(c).

The Commissioner of Taxation’s practice is set out in *Practice Statement Law Administration* PS LA 2006/11 at [32.3.8]:

A trustee is required to lodge with the Commissioner returns of all indirect taxes, as well as returns of all income, profits or gains of a capital nature or of any other nature prescribed by legislation derived by the deceased person in respect of the period to the date of death in which no return was lodged by the deceased person [s 260-140(3)]. Non salary and wage final returns should be accompanied by a full and true estimate of assets and liabilities valued at the date of death. This same information may be requested by the Commissioner in regard to salary and wage returns.

If the amount of the liability requires an assessment under a taxation law, but the assessment has not been made, and the legal personal representative fails to provide a return or other information the Commissioner of Taxation may assess that amount. If he does so, the assessment has the same effect as if it were made under that taxation law: s 260-140(4) of Schedule 1 to the TAA.

A legal personal representative has the same objection and appeal rights as if they were the deceased person: ss 260-140(4) and (5) of Schedule 1 to the TAA.

6.2.1 Indemnity Claim Against the Estate

Aside from a trustee's right under the general law to be indemnified – for which case law and relevant trustee legislation¹² provides – a legal personal representative has a statutory right under s 265-40 of Schedule 1 to the TAA to retain or deduct an amount from the deceased estate to compensate for any amount paid to the Commissioner of Taxation for the deceased's tax-related liability. The same rights also exist under s 254(1)(f) of the 1936 Act.

If a legal personal representative makes a payment for a deceased person's tax liability up to the date of death, the payment will be a charge against the deceased's estate. Although the account of a deceased estate may separate the tax liabilities of the deceased for the period up to death and those arising after the date of death, the payment to the Commissioner comes from the one general estate.

6.2.2 Contribution Between Multiple Legal Personal Representatives

¹² *Trustee Act 1958* (Vic), s 36(2); *Trustee Act 1925* (NSW), s 59(4); *Trustee Act 1925* (ACT), s 59(4); *Trustee Act 1973* (Qld), s 72; *Trustee Act 1936* (SA), s 35(2); *Trustee Act 1962* (WA), s 71; *Trustee Act 1898* (Tas), s 27(2); and *Trustee Act 1980* (NT), s 26. These Acts include a legal personal representative within their definition of trustee (via the definition of trust estate). By the definition of 'trust' in the *Trustee Act 1925* (NSW) s 5 the term includes 'the duties incident to the office of legal representative of a deceased person'.

If there are multiple legal personal representatives they are jointly and severally liable for any obligation under s 260-140 of Schedule 1 to the TAA. If one of them has made payment to the Commissioner of Taxation, that representative has a statutory claim for contribution against the others: s 265-145 of Schedule 1 to the TAA.

6.2.3 Liabilities After Assets Distributed

If a legal personal representative has caused the distribution or diminution of the assets of a deceased estate, leaving it unable to pay its tax debts of which they were aware, the legal personal representative will be personally liable to the Commissioner of Taxation to the extent of the distribution or diminution: s 254(1) of the 1936 Act.

This most often arises after audit where fraud or tax schemes are involved.

The Commissioner of Taxation's approach is set out in *Practice Statement Law Administration* PS LA 2006/11 at [32.2.11] to [32.4.2].

6.2.4 Beneficiaries' Liability if No Assets Left to Pay Tax

The converse of the issue raised in 6.2.3 is whether a beneficiary, who has received a distribution from a deceased's estate that is later found to owe taxes but is insolvent, has a liability to make good that tax liability from their own assets up to the amount of the distribution. It seems not based on the Commissioner of Taxation's approach set out in *Practice Statement Law Administration* PS LA 2006/11 at [32.4.3].

This approach may be questionable, however, if the recipient beneficiary knew of the tax liability at the time of the distribution.

6.3 Where No Administration Starts

If a deceased has a tax liability at year end and no legal personal representative has been appointed within six months after the date of death, the Commissioner of Taxation can make a claim for the taxes by making a determination of the amount of outstanding tax-related liabilities that the deceased had at the time of death, publishing the claim and then seizing the deceased's assets to the value of the claim plus recovery costs: s 260-0145 and 260-150 of Schedule 1 to the TAA.

The Commissioner of Taxation can also seek to be appointed as trustee under the applicable state law.

Anyone who has a claim against or an interest in an administered estate, or who later applies for probate or for letters of administration, and is dissatisfied with the Commissioner of Taxation's claim, has objection and appeal rights: s 260-145(5) of Schedule 1 to the TAA.

6.4 Insolvent Estates or Bankrupt Deceased's

If a deceased is bankrupt at the time of death, the bankruptcy process continues after death and the Official Trustee effectively administers the deceased's estate. Section 63 of the *Bankruptcy Act 1966* (Cth) provides that the bankruptcy proceedings continue '*so far as they are capable of being continued, as if [the bankrupt] were alive.*'

If a deceased dies insolvent, the creditors of a debt not less than \$2,000 may bring a petition for the administration of the estate under Part XI: s 244 of the *Bankruptcy Act 1966* (Cth). This is often used by secured creditors. Service of the petition is usually on the deceased's legal personal representative: s 244(9) and (10) of the *Bankruptcy Act 1966* (Cth). Part XI also deals with the situation where a debtor dies after the presentation of a creditor's petition: s 245 of the *Bankruptcy Act 1966* (Cth). In both cases, the legal personal representative must make out a statement of the deceased's affairs and their administration of the deceased's estate: s 246 of the *Bankruptcy Act 1966* (Cth).

A legal personal representative may present a petition for an order for the administration of the estate under Part XI of the *Bankruptcy Act 1966* (Cth), accompanied by a state in duplicate of the deceased person's affairs and their administration of the estate.

7 GST Issues for Deceased Estates

The following GST rules apply on the death of a person who was registered for GST and for the legal personal representative after death.

7.1 Effect of death on registration

On the death of an individual who was registered for GST, the registration is canceled: s 25-55(2) of the *A New Tax System (Goods and Services Tax) Act 1999* (Cth) (the ‘**GST Act**). The deceased’s current period terminates on the day before the date of death: s 27-40(1) of the GST Act.

7.2 Effect of death on installment period

An installment period of a deceased registered for GST, who was an installment GST payer, does not terminate on death but there is no obligation to make any GST installment for the period starting after the date of death: s 162-85 of the GST Act.

7.3 Deceased’s input credits

If the legal personal representative or a beneficiary of the deceased estate does not continue to carry on the enterprise of the deceased and is not registered for GST, the legal personal representative will be liable for an increasing cancellation of registration adjustment for the input tax credits claimed by the deceased: s 138-5 of the GST Act.

7.4 Legal personal representative or beneficiary carrying on the enterprise

If the legal personal representative or a beneficiary of the deceased estate continue to carry on the enterprise of the deceased and are registered for GST, the legal personal representative is not liable for an increasing cancellation of registration adjustment for the input tax credits the deceased claimed: s 137-17 of the GST Act. The legislation assumes that their GST registration is made immediately after the deceased’s death.

7.5 In specie distributions to a beneficiary

If a deceased estate distributes enterprise assets to a beneficiary who does not carry on an enterprise, the GST input tax credits claimed by the deceased or the legal personal representative are cancelled and clawed back. This occurs by the legal personal representative calculating and making a GST increasing adjustment: s 139-5 of the GST Act.

The clawback does not apply if the legal personal representative or a beneficiary carries on or intends to carry on the enterprise carried on by the deceased: s 139-5(3) of the GST Act. For example, if an executor / executrix of a deceased who carried on the deceased's business distributes the trust assets to a beneficiary who carries on the same business.

8 Testamentary Trusts

A ‘testamentary trust’ is an ‘express trust’¹³, created under the terms of a will, or a codicil¹⁴ of a will. Testamentary trusts have the same attributes as other trusts. That is, they are a relationship as between a trustee and beneficiary¹⁵ with respect to trust property. Further, and for the purposes of both trusts created inter vivos and those created under testamentary instruments, the following elements must be present in order for a trust estate to subsist:¹⁶

- first – there needs to be at least one trustee, who holds a legal (or equitable) interest in the trust property. The trustee has an obligation to deal with the trust property in terms of the trust;
- second – there must be property capable to be held on trust (*Port of Brisbane Corporation v ANZ Securities Ltd* [2003] 2 Qd R 661). Further, there must be certainty as to the property held subject to a trust (*Herdegen v Federal Commissioner of Taxation* (1988) 84 ALR 271);
- third – there must be a beneficiary for whom the trust assets are held; and
- fourth – the trustee must be under a personal obligation to deal with the trust property for the benefit of the beneficiaries.

Testamentary trusts are also known as ‘executory trusts’. Gummow J in *Herdegen v Federal Commissioner of Taxation* (1988) 84 ALR 271 observed at 280 that the term ‘executory trust’:

¹³ There are three categories of trusts, being express trusts, resulting trusts and constructive trusts. An express trust is a trust created by express intention. A resulting trust is a trust created by implied intention. A constructive trust is a trust that is imposed to prevent person(s) from succeeding in making an unconscionable assertion of ownership over property.

¹⁴ A codicil is a ‘... document supplementary to a will made earlier which is executed by a testator with the intention of adding to, altering, revoking, explaining or confirming a will, provision or part of a will. As a subsidiary testamentary instrument, a codicil must be executed with the same formalities as a will and when so executed, becomes part of the will and must be provided with the will ...’ (see *Butterworths Concise Australian Legal Dictionary*).

¹⁵ Charitable trusts do not vest beneficial estates or interests in any persons, as they are established to promote a purpose, or purposes, and not for the direct benefit of persons as individuals or members of a class of individuals (see *Attorney-General for New South Wales v Perpetual Trustee Company (Limited)* (1940) 63 CLR 209 at 222-223).

¹⁶ See paragraph 104 and following of *Jacobs’ Law of Trusts in Australia*.

... is used usually to describe situations where there is (a) an agreement or covenant for the subsequent execution of a trust instrument or (b) a direction or declaration (usually in a will) giving instructions or short leads from which the trustee is to prepare a formal written statement ...

Lord Cairns in *Mortimer Sackville-West v Viscount Holmesdale* (1870) LR 4 HL 543:

[T]he second codicil to the will of the testatrix ... creates what is commonly described as an 'executory trust', that is to say, not a trust which remains to be executed, for in this sense all trusts are 'executory' at their creation, but a trust which is to be executed by the preparation of a complete and formal settlement, carrying into effect, through the operation of an apt and detailed legal phraseology, the general intention compendiously indicated by the testatrix. The codicil is, in fact, equivalent to directions or instructions for a settlement.

Broadly speaking, a testamentary trust displays the following characteristics:

- first – testamentary trusts are established under a testamentary instrument;
- second – testamentary trusts are funded by either:
 - the assets of a deceased estate; or
 - payments to the estate in consequence of death, such as superannuation death benefits or insurance proceeds paid to a deceased estate, rather than being paid to nominated beneficiaries under a will; and
- third – testamentary trusts are typically administered by the executor of the estate, or another person appointed as the trustee under the terms of the will. The testamentary trust is subject to the terms of the will.

8.1 Why establish testamentary trusts?

The main taxation benefit of a testamentary trust is the income tax concessions for minors, who are taxed as adults with the benefit of the tax free threshold under Division 6AA of the 1936 Act. Section 102AG of the 1936 Act provides for 'excepted trust income', being a category of income derived by minors.

‘Excepted assessable income’ includes Income derived by a minor from property of a deceased estate or which is transferred to a minor from a deceased estate (see paragraph 102AE(2)(c) of the 1936 Act).

‘Excepted trust income’ includes:

- paragraph 102AE(2)(c) of the 1936 Act – ‘... *assessable income of a trust estate that resulted from ... a will, codicil or an order of a court that varied or modified the provisions of a will or codicil ...*’; and
- paragraph 102AE(2)(d) of the 1936 Act - ‘... *is derived by the trustee of the trust estate from the investment of any property ... that devolved for the benefit of the beneficiary from the estate of a deceased person ...*’

That is, the essential requirement for minors to be eligible for the concessionally taxed income is that the income is ‘... *assessable income of a trust estate that resulted from ... a will...*’. That is, it is essential to ensure that the trust under which the minor benefits is established under the testamentary instruments, and not subsequently declared or settled without the appropriate intentions / actions of the testator.

Further, it should be noted that a distribution to minor beneficiaries under the terms of a testamentary trust creates a legal entitlement in favour of the minor beneficiary. As a result, the distribution must either be physically paid to the minor beneficiary, or a loan account in favour of the minor beneficiary will be created, which will ultimately be payable to the minor either at demand, or when the testamentary trust vests.

As a result, and in the event that the testator wishes for the residuary estate be divided (ultimately) equally, and ‘equalisation clause’ may be required in the will. Such clauses allow for an allocation of ‘non-will benefits’ (e.g. insurance or superannuation proceeds) to be allocated to the other (non-minor) beneficiaries.

The purpose of the establishment of the testamentary trust will dictate whether it is 'discretionary' or 'fixed' in nature (or a combination of both), and as a result, the associated benefits which attach to the structure. A testamentary trust may be drafted so as to be (for example) on one hand:¹⁷

- *a restricted trust* – being established to protect particular vulnerable beneficiaries; and on the other
- *a discretionary testamentary trust* - under which there may be a wide range of potential beneficiaries under the terms of the trust.

Another example of a testamentary trust is a trust established with respect to certain property whereby (for example) a beneficiary has a life interest (i.e. an income beneficiary), with the remainder going to other beneficiaries (i.e. capital beneficiaries).

Macdonald¹⁸ provides for the following reasons for establishing a testamentary trust:

- tax benefits on distributing income to minor children, grandchildren (see above);
- tax benefits on distributing income to lower taxed beneficiaries (see below);
- protection of assets from ex-spouses;
- protection of assets from creditors;
- protection of assets from being wasted by spendthrift beneficiaries;
- protection of assets from being wasted by addicted beneficiaries; and
- a combination of all of the above.

Further, the terms of a testamentary trust may allow for the streaming of particular distributions to particular beneficiaries (e.g. franking credits, the 50% CGT discount, et cetera).

¹⁷ Perkins M and Monahan. Estate Planning – A Practice Guide for Estate and Financial Service Professionals. LexisNexis – Butterworths, Sydney, 2005 p 111.

¹⁸ Arlene Macdonald. *Testamentary Trusts: Not Just 'Another' Trust?*. 14th National Intensive Retreat, 17-19 August 2006.

Further, and as noted by Macdonald,¹⁹ as a testamentary trust does not come in effect until the death of the testator, the terms of a testamentary trust may be varied at any time before the testator's death. Further, the property to be dealt with under the terms of the testamentary trust may change from time to time by the testator, until the testator's death.

The use and advantages of discretionary trusts in both tax planning and asset protection contexts have been well documented. In the usual form of discretionary trust, the trustee is given a 'discretion' to choose the share or amount of income which any one or more particular beneficiary (typically chosen from a specified class) of the trust is to receive. For example a trust deed may provide that '*... the trustee may distribute the trust income to the children of the Testator, and any members of the Testator's family according to the trustee's unfettered discretion*'.

It may be appropriate to vest a 'discretion' in the trustee when, for example, the needs of the beneficiaries may vary from time to time. From a tax planning prospective, such flexibility may enable the trustee to distribute the trust income in such a way (i.e. to those beneficiaries and in those amounts) so as to minimise the overall tax liability on the total trust income or on the total income of the family group for an income year.

Furthermore, as the beneficiaries of a discretionary trust are 'mere objects', then they have no rights to the assets held subject to the trust. As a result, the creditors of a beneficiary cannot prima facie attack the assets held subject to a discretionary trust.

Discretionary trusts are favoured because of the advantages attaching to their use. These include:

- when the trust property is held by the trustee, the assets are protected from claims by creditors of the beneficiaries and the beneficiaries are protected from claims by creditors of the trust. By comparison, in the case of a 'fixed trust' the (for example) unit holders have an item of property which may be attacked by the unit holder's creditors – being the unit in the unit trust;
- trust income and capital can be distributed to beneficiaries in a tax effective way, the trustee having the discretion to accumulate trust income in the trust or to distribute it to beneficiaries; and

¹⁹ *ibid*

- the ability to transfer the use, enjoyment and benefit of (for example) the trust's assets free of transaction costs.

The tax disadvantages with the discretionary trust structure include that:

- losses are trapped within them (i.e. cannot be distributed);
- beneficiaries of a discretionary trust cannot claim a tax deduction for interest referable to borrowings which they might use to 'invest' in a discretionary trust.²⁰ This is because, as a result of a trustee's discretion to allocate income – a beneficiary in a discretionary trust has no expectation of receiving distributions of income. Rather, a beneficiary only has a right to be considered. If the Testamentary Trust is to be geared, then it would be necessary to do this in the trust – i.e. the trustee borrows and not the beneficiaries.

An issue to consider in the testamentary trust concept is how both the advantage, and the assets held subject to a testamentary trust remain with, and pass to the testator's family group. This may be achieved by:

- Ensuring that only those who are in the testator's family may benefit under the terms of the testamentary trust. In particular, it should be ensured that the capital default beneficiaries are those in the testator's family;
- Ensuring that the control (e.g. a position of 'appointor') passes to the testator's family groups. As the position of appointor is personal, it may need to be ensured that the position passes under the will of those that will take the position is consistent with the testator's will; and
- Have an open beneficiary clause.

8.2 Formalities for establishing a testamentary trust

²⁰ A vexed issue (and not in the scope of this paper) is whether further settlements can be made on a testamentary trust after it has come into effect.

As testamentary trusts are created under the terms of testamentary instrument(s), the formal requirements for establishing a trust under a will are the same as the requirements for the creation of a valid will, or codicil. As a result s 6 of the Succession Act, which contains those requirements, need to be satisfied. Section 6 of the Succession Act provides:

- (1) A will is not valid unless:
 - (a) it is in writing and signed by the testator or by some other person in the presence of and at the direction of the testator, and
 - (b) the signature is made or acknowledged by the testator in the presence of 2 or more witnesses present at the same time, and
 - (c) at least 2 of those witnesses attest and sign the will in the presence of the testator (but not necessarily in the presence of each other).
- (2) The signature of the testator or of the other person signing in the presence and at the direction of the testator must be made with the intention of executing the will, but it is not essential that the signature be at the foot of the will.
- (3) It is not essential for a will to have an attestation clause.
- (4) If a testator purports to make an appointment by his or her will in the exercise of a power of appointment by will, the appointment is not valid unless the will is executed in accordance with this section.
- (5) If a power is conferred on a person to make an appointment by a will that is to be executed in some particular way or with some particular solemnity, the person may exercise the power by a will that is executed in accordance with this section, but is not executed in the particular way or with the particular solemnity.
- (6) This section does not apply to a will made by an order under section 18 (Court may authorise a will to be made, altered or revoked for a person without testamentary capacity).

That is, in order for a testamentary instrument (and therefore a testamentary trust under a testamentary instrument) to be valid:

- the testamentary instrument must be in writing;
- the testamentary instrument should be signed by the testator or by some other person in the presence of and at the direction of the testator;

- the testator's signature is made (or acknowledged) in front of at least two (2) witnesses; and
- at least two of the witnesses attest and sign the will in front of the testator.

Section 6 of the Succession Act, like section 23C of the *Conveyancing Act 1919* (NSW)²¹ is intended to prevent fraud.

As with other express trusts, in order to validly create a testamentary trust, there must be certainty with respect to:

- the intention to create the trust;
- the subject matter of the trust (i.e. the trust property); and
- the object(s) (i.e. the beneficiaries) of the trust.

Whilst all three of the certainties are often subject to dispute, the two most disputed aspects of testamentary trusts (and indeed testamentary instruments) include the capacity of a testator to make a will, and whether the testator was under undue influence when creating the trust instrument. It should be noted that as long as a testator has testamentary capacity, the testator (subject to illegality) may have a 'capricious' will - Young J in *Gregory v Hudson* (1974) 41 NSWLR 573:

There is nothing to stop a person making the most capricious will. A person could make a will which said that he gave all his property to X to be held on trust, the terms of which were that X was to arrange for a 0055 telephone number and was to pay the whole of the testator's estate to the hundredth person who rang that number, or for the first born child at a certain hospital in 1998. There is nothing to stop the testator directing that his executor convert the whole of the money into bank notes and proceeding to the corner of George and King Streets at 8 o'clock on a designated night and throwing the money away.

²¹ Section 23C of the *Conveyancing Act 1919* (NSW), which is modelled on the Statute of Frauds 1677 (Eng) has the objective of preventing hidden oral transactions in certain type of property, which defrauded those truly entitled to them (see *Vandervell v Inland Revenue Commissioners* [1967] 2 AC 291 at 311). This objective was accomplished by requiring the relevant transactions to be executed in writing or at least evidenced in writing.

Further, there may be situations where the testamentary instruments show intention by the testator to establish a testamentary trust, but the precise terms of the trust are not provided. If the testamentary instrument provides that a trust is to be established, then a person taking a gift must hold the gift upon the trusts provided for, or upon trust for whom the law provides. It was observed in *Morice v Bishop of Durham* (1805) 32 ER 974 at 953 that:

If he ... [the testator] ... says, he gives in trust, and stops there, meaning to make a codicil, or an addition to his Will, or, where he gives upon trusts, which fail, or are ineffectually expressed, in all those cases the Court has said, if upon the face of the Will there is declaration plain, that the person, to whom the property is given, is to take it in trust; and, though the trust is not declared, or is ineffectually declared, or becomes incapable of taking effect, the party shall be trustee; if not for those who were to take by the Will, for those, who take under the disposition of the law.

Similarly, in *Briggs v Penny* (1851) 42 ER 371 at 375, Lord Truro LC observed that:

It is not necessary to exclude the legatee from a beneficial interest that there should be a valid or effectual; trust; it is only necessary that it should clearly appear that a trust was intended ... Once establish that a trust was intended, and the legatee cannot take beneficially. If a testator gives upon trust, though he never adds a syllable to denote the objects of that trust, or though he declares a trust in such a way as not to exhaust the property, or though he declares it imperfectly, or though the trusts are illegal, still in all these cases, as is well known, the legatee is excluded, and the next-of-kin take.

For completeness, it should be noted that the rule against delegation of will-making power has been brought into line with the rule in equity regarding certainty of objects via section 44 of the Succession Act, which provides that:

A power or trust to dispose of property, created by will, is not void on the ground that it is a delegation of the testator's power to make a will, if the same person or trust would be valid if made by the testator by instrument during his or her lifetime.

8.3 Importance of the terms of the testamentary trust

As well as establishing a testamentary trust, the testamentary instruments will also provide for the terms of the testamentary trust. As with trusts established inter vivos, the powers, duties, trusts and discretions that a trustee of a testamentary trust has is contained in the trust instrument – being the testamentary instruments. Indeed, Lord Westbury LC in *Wilkins v Hogg* (1861) 31 LJ Ch 41 at 43 observed that:

The testatrix was at liberty to say ‘Your duty shall require no more of you than this’. The Court could not extend the office, or invest it with greater obligation.

As a result, both the rights and obligations of trustees of testamentary trusts, as well as beneficiaries will be provided for (primarily) in the testamentary instruments.

As a result, the usual tensions arise with respect to whether the powers and trusts under the trust are wide, and the potential resulting tensions that arise as between trustees (who control the trust estate) and beneficiaries. This may be an issue (for example) if there is property held subject to a testamentary trust by a sole trustee, for the benefit of more than one (adult) beneficiary.

Further, the flexibility of the use of the trust fund (for example, power of investment, amalgamation of trust fund et cetera) may be drafted narrowly for the purposes of protecting the trust fund, but may become an issue when dealing with the trust fund some time after the establishment of the testamentary trust.

8.4 More than one testamentary trust?

A common issue that arises in the context of succession planning, particularly in the context of establishing testamentary trust(s) by a testator with a number of (adult) children, is whether one or more testamentary trusts should be established under a will.

For example, should one child be the trustee and appointor to hold the trust fund for the benefit of all of the children, should a testamentary trust be established for each of the testator(s) children, or a mixture of both?

This will depend on the individual circumstances of the family group, and will depend on circumstances outlined above.

8.5 The position of appointor

As with other trusts (e.g. *inter vivos* discretionary trusts), a method of ensuring control of a trust is maintained is by providing for an ‘appointor’, who may have rights with respect to (for example) the appointment and removal of trustees (i.e. overall control of a trust).

The considerations with respect to appointors of testamentary trusts are the same as those for *inter vivos* trusts.

It should be noted that the position of Appointor is a personal position, and is not an item of ‘property’. In *Re Burton; Wily v Burton* - BC9405738, Davies J in the context of bankruptcy law, observed that ‘... *the power which Mr Burton holds as Appointor is not ‘property’ which vests in his trustee in bankruptcy nor a power ‘as might have been exercised by the bankrupt for his own benefit’.* As a result, the position of appointor, because it is not an item of property but rather is a personal appointment, it was held that the position does not pass to a trustee in bankruptcy.

Similarly, in the context of succession laws, the position of appointor passes to a deceased’s personal legal representative, and does not enter into a deceased appointor’s estate. For example, section 40 of the *Probate and Administration Act 1898* (NSW) provides that the existence of ‘property’²² within the jurisdiction (i.e. NSW) is essential to grant probate and letters of administration: ‘*The Court shall have jurisdiction to grant probate of the will or administration of the estate of any deceased person leaving property, whether real or personal, in New South Wales.*’ The only exception to this rule is a grant of administration to permit an application to be made under the Succession Act (formerly the *Family Provision Act 1982* (NSW)): see section 41A of the *Wills, Probate and Administration Act 1898* (NSW).

²² It should be noted that the term ‘property’ is not defined in the *Wills, Probate and Administration Act 1898* (NSW). Rather, the terms ‘real estate’ and ‘personal property’ are defined in section 3 of the *Wills, Probate and Administration Act 1898* (NSW) as follows:

Real estate extends to messuages, lands, rents, and hereditaments, of freehold or any other tenure, and whether corporeal, incorporeal or personal, and to any undivided share thereof, and to any estate, right, or interest (other than a chattel interest) therein, and in part 2 includes lands held under building leases or any lease for twenty-one years and upwards.

Personal estate, except in part 2 as hereinbefore mentioned, extends to leasehold estates and other chattels real, and also to moneys, shares of government and other funds, securities for money (not being real estates), debts, choses in action, rights, credits, goods, and all other property whatsoever, which, prior to the coming into operation of the Real Estates of Intestates Distribution Act of 1862, commonly known as “Dr. Lang’s Act,” by law devolved upon the executor or administrator, and to any share or interest therein.

As a result, a position of appointor created under a testamentary trust, unless otherwise provided for, will pass to the appointor's personal legal representative and not the appointor's estate. The position of appointor will not be dealt with by (and for example) the *Probate and Administration Act 1898* (NSW).

8.6 Secret Trusts

'Secret trusts' are a type of trust that may arise under a will. Secret trusts have been described as follows:²³

Secret trusts arise where a testator leaves property to X after communicating with X that X is to hold the property on trust. ... Since a will is open for public inspection on the testator's death, a secret trust allows a testator to provide for an object he or she wishes to be kept secret.

However, it should be noted that 'secret trusts' may arise in wills under the terms of wills. In addition to the requirements required to establish an 'express trust',²⁴ secret trusts require the following three elements (see *Blackwell v Blackwell* [1929] AC 318):

- the testator's intention that the property is to be used according to its specifications;
- communication of intention to the intended trustee(s); and
- acquiescence on behalf of the trustee(s).

It should be noted that secret trusts arise in a will, but do not operate because of a will. Secret trusts arise outside of a will, and the beneficiary obtains its interest because of the trust and not the will: *Ledgerwood v Perpetual Trustee Co Ltd* (1997) 41 NSWLR 532.

8.7 Varying the terms of a testamentary trust

²³ G. E. Dal Pont and DRC Chalmers. *Equity and Trusts in Australia*. Law Book Co, Sydney, 2007 para18.45.

²⁴ That is, the 'three certainties' – being the certainty of intention to create a trust; certainty with respect to trust property; and certainty of objects / beneficiaries.

An issue is whether the terms of a testamentary trust may be changed. Whether a testamentary trust may be changed to appoint new beneficiaries has been a vexed point. The issue is whether such an amendment causes a resettlement to occur, or indeed if there is a delegation of trust power. It seems that the better view is that varying the terms of a testamentary trust to include a new 'class' of beneficiary will cause a resettlement to occur.

As with *inter vivos trust* estates, the first issue to determine when seeking to vary the terms of a testamentary trust is determining whether the trust instrument has a variation clause.

If the will does not contain a power of variation, then either the inherent jurisdiction of the court must be sought, or the terms of the *Trustee Act 1925* (NSW) must be relied upon.

In *Chapman v Chapman* [1954] AC 429, Lord Simmons explained four instances in which the court may exercise its inherent jurisdiction, which include:

- to change the nature of an infants' property holdings from personalty or realty, and vice-versa;
- to pay maintenance out of income where there is a direction to accumulate income;
- to effect a compromise on behalf of some infant beneficiaries; and
- to direct that, in the event of an emergency, a transaction unauthorized by the trust instrument should be carried out by way of salvage of the trust property.

Further, regard should be given to the court's statutory power to amend the terms of a trust. Relevantly, section 81 of the *Trustee Act 1925* (NSW) provides that:

- (1) Where in the management or administration of any property vested in trustees, any sale, lease, mortgage, surrender, release, or disposition, or any purchase, investment, acquisition, expenditure, or transaction, is in the opinion of the Court expedient, but the same cannot be effected by reason of the absence of any power for that purpose vested in the trustees by the instrument, if any, creating the trust, or by law, the Court:

- (a) may by order confer upon the trustees, either generally or in any particular instance, the necessary power for the purpose, on such terms, and subject to such provisions and conditions, including adjustment of the respective rights of the beneficiaries, as the Court may think fit, and
 - (b) may direct in what manner any money authorised to be expended, and the costs of any transaction, are to be paid or borne as between capital and income.
- (2) The provisions of subsection (1) shall be deemed to empower the Court, where it is satisfied that an alteration whether by extension or otherwise of the trusts or powers conferred on the trustees by the trust instrument, if any, creating the trust, or by law is expedient, to authorise the trustees to do or abstain from doing any act or thing which if done or omitted by them without the authorisation of the Court or the consent of the beneficiaries would be a breach of trust, and in particular the Court may authorise the trustees:
- (a) to sell trust property, notwithstanding that the terms or consideration for the sale may not be within any statutory powers of the trustees, or within the terms of the instrument, if any, creating the trust, or may be forbidden by that instrument,
 - (b) to postpone the sale of trust property,
 - (c) to carry on any business forming part of the trust property during any period for which a sale may be postponed,
 - (d) to employ capital money subject to the trust in any business which the trustees are authorised by the instrument, if any, creating the trust or by law to carry on.
- (3) The Court may from time to time rescind or vary any order made under this section, or may make any new or further order.
- (4) The powers of the Court under this section shall be in addition to the powers of the Court under its general administrative jurisdiction and under this or any other Act.
- (5) This section applies to trusts created either before or after the commencement of this Act.

It should be noted that the power to vary trusts is narrower in New South Wales than in Queensland, Victoria, South Australia, Tasmania and Western Australia. The other States have provisions which specifically empower the courts to vary trusts.

Further, the New South Wales provisions only allow a court to vary if to do so, would be advantageous to the beneficiaries of the trust as a whole: *Riddle v Riddle* (1952) 85 CLR 202 at 220.