THIRTEEN WENTWORTH SELBORNE

Selected Issues in Estate Administration

NSW Law Society
Wills and Estates Law Accredited Specialists

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1. Distributions from deceased estates and testamentary trusts

1.1 CGT assets acquired on or after 20 September 1985 typically give rise to taxable capital gains or capital losses pursuant to parts 3-1 and 3-3 of the *Income Tax Assessment Act 1997 (Cth)*(**the 1997 Act**).

1.2 In order for there to be a "capital gain" or "capital loss" in relation to a CGT asset, then a "CGT event" must happen. A concession applies to CGT events that occur as a result of the death of an individual.

1.3 Section 128-10 of the 1997 Act provides that any capital gain or capital loss from a CGT event as a result of the "owner" passing away is disregarded.

1.4 Pursuant to subsection 128-15(3) of the 1997 Act, any "*… capital gain or capital loss a legal personal representative makes if the asset passes to a beneficiary in your estate is disregarded …*".

1.5 The circumstances in which an asset will "pass" to a beneficiary are contained in section 128-20 of the 1997 Act.

1.6 As a result, the *prima facie* position is that a capital gain or capital loss which arises from distribution of a CGT asset that was held by the deceased, by the executor (or administrator) of a deceased estate to a beneficiary is disregarded.

1.7 An asset is treated as passing to a beneficiary at the time the beneficiary becomes "absolutely enticed" to is as against the executor (Taxation Determination TD 2004/3).

1.8 As a result, if an estate has been fully administered but legal ownership of an asset has not been transferred to the beneficiary who is entitled to the asset, a sale of the asset by the executor will give rise to a capital gain in the hands of the beneficiary, rather than in the hands of the executor.

1.9 The Commissioner considers that it is not possible for two beneficiaries of trust to be absolutely entitled to the asset of trust (see Draft Taxation Ruling TR 2005/D25 and footnote 3 Taxation Ruling TR2006/4).

1.10 In order for the distribution of a CGT asset (from an estate) to a beneficiary to not be subject to the capital gains tax provisions pursuant to subsection 128-15(3) of the 1997 Act, the CGT asset must "pass" to the beneficiary.

1.11 In the context of capital gains tax, the question is whether an asset has "passed to" a beneficiary of a deceased estate, as provided for in section 129-20 of the 1997 Act. From a New South Wales stamp duty perspective, the question is whether section 63 of the Duties Act is complied with.

1.12 Section 128-10 of the 1997 Act provides that: " *When you die, a capital gain or capital loss from CGT event that results for a CGT asset you own just before dying is disregarded."* Subsection 128-15(1) of the 1997 Act provides that:

> *This section sets out what happens if a CGT asset you own just before dying:*
>
> *(a) devolves to your legal personal representative; or*
> *(b) passes to a beneficiary in your estate.*

1.13 Subsection 128-15(2) of the 1997 Act provides that:

> *The legal personal representative, or beneficiary, is taken to have acquired the asset on the day you died.*

1.14 Subsection 128-15(3) of the 1997 Act provides that: "*Any capital gain or capital loss the legal personal representative makes if the asset passes to a beneficiary in your estate is disregarded."*

1.15 Essential for the operation of subsection 128-15(3) of the 1997 Act is the ***asset passing*** to a beneficiary. Section 128-20 of the 1997 Act provides for when an asset passes to a beneficiary. Subsection 128-20(1) of the 1997 Act provides that:

> *A CGT asset passes to a beneficiary in your estate if the beneficiary becomes the owner of the asset:*
>
> *(a) under your Will, or that Will as varied by a Court Order; or*
>
> *(b) by operation of an intestacy law, or such a law as varied by a Court Order; or*
>
> *(c) because it is appropriated to the beneficiary by your legal personal representative in satisfaction of a pecuniary legacy or some other interest or share in your estate; or*
>
> *(d) under a deed of arrangement if:*
>
> *(i) the beneficiary entered into the deed to settle a claim to participate in the distribution of your estate; and*
>
> *(ii) any consideration given by the beneficiary for the asset consisted only of the variation or waiver of a claim to one or more other CGT assets that formed part of your estate.*

(It does not matter whether the asset is transmitted directly to the beneficiary or is transferred to the beneficiary by your legal personal representative)

1.16 That is, section 128-20 of the 1997 Act provides for a broad definition of *"passing"* of assets under a will in the CGT Event, CGT rules ensure that distributions of assets in accordance with the court order varying the will as a result of a challenge will be entitled to the CGT exemption. Similarly, a distribution in accordance with a Court order varying the Will will also be entitled to the CGT exemption.

1.17 For completeness, it should be noted that the concessions with respect to deceased estates in the context of NSW duties is contained in section 63 of the Duties Act 1997 (NSW), which provides that:

63 Deceased estates

(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

(c) a transmission application by a devisee who is also the sole legal personal representative, and

(d) a declaration by an executor of a will under section 11 of the Trustee Act 1925 if the Chief Commissioner is satisfied that the declaration is consistent with the entitlements of beneficiaries under the trusts contained in the will.

(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.

(2A) *A transmission application made by a beneficiary under a will, with the consent of the legal personal representative of a deceased person, is taken, for the purposes of this section, to be a transfer of dutiable property by the legal personal representative to the beneficiary.*

(3) *Section 25 does not apply to a dutiable transaction to which subsection (2) applies.*

(4) *If the duty chargeable in respect of a transfer or transmission application referred to in subsection (1) would, but for that subsection, be less than $50, the duty chargeable is that lesser amount.*

(5) *This section is subject to section 273, which provides for a minimum duty of $10.*

2. Substituted CGT assets

(a) Substituted assets generally

2.1 The benefit of Division 128 of the 1997 Act that arises upon death is limited to assets that form part of the estate of the deceased. The concession does not apply to CGT assets acquired by the estate after the death of the testator.

2.2 As a result (and for example) if an executor disposes of a CGT asset that was held by the deceased immeditaley before death, and acquires a substitute asset, then the first disposition will be a CGT event, and any and the subsequent distribution of the substituted assets to the beneficiaries will be treated as a further CGT event.

2.3 This is because section 128-10 of the 1997 Act looks at the CGT asset that "you own" (the "you" being the deceased), with subsection 128-15(3) of the 1997 Act also looking to that same CGT asset (i.e. the CGT asset that "you", the deceased, owned).

2.4 In such a situation, the executor would be deemed to have received the market value capital proceeds from the CGT event (as at the time of the CGT event) with respect to the CGT asset that has been distributed.

(b) An executor acquiring an asset to satisfy a legacy

2.5 The Commissioner takes a different approach if "after acquired" property (by an executor) is acquired to satisfy a general legacy. The Commissioner does not treat the subsequent distribution as being taxable.

2.6 In Taxation determination TD 93/36, entitled *Income tax: capital gains: what are the capital gains tax consequences where a legal personal representative (LPR) purchases an asset to satisfy a general legacy?*, the Commissioner considers that if after paying the deceased's deaths and testamentary expenses, the executor purchases an asset to satisfy a general legacy, this is not treated as a taxable capital gain to the executor.

2.7 In particular, the Commissioner considers that no CGT event arises on the transfer of the CGT asset to the beneficiary, as the beneficiary would be *"absolutely entitled"* to the asset from the date of purchase so that the transfer may be disregarded pursuant to section 106-5 of the 1997 Act.

2.8 The Commissioner opines as follows:

1. A person may provide in his or her will that property of a general description be left to a specified beneficiary. If the deceased did not own an asset of that description at the time of death, the LPR (after paying the debts and other expenses of the estate) may purchase an asset to satisfy that general legacy.

2. The beneficiary for whom the asset is acquired by the LPR is absolutely entitled to that asset as against the LPR. Accordingly, the acts of the LPR are taken to be the acts of the beneficiary (section 106-50 of the Income Tax Assessment Act 1997 (ITAA 1997)).[F1]. The beneficiary is taken to have acquired the asset at the time it was acquired by the LPR. Costs incurred by the LPR which can be included in the cost base of the asset are included in the cost base to the beneficiary of the asset.

3. No CGT event happens when legal ownership of the asset is transferred from the LPR to the beneficiary because section 106-50 effectively treats the beneficiary as having transferred the asset to themselves. That is, section 106-50 treats the transfer to the beneficiary as an act done by the beneficiary'.

Example:

Jane's will leaves a general legacy of 1,000 shares in XYZ Ltd to Bill. As Jane does not own any shares in XYZ Ltd at the time of her death, her executor purchases the shares on 23 April 2008 for $2,500.

Bill is deemed to acquire the shares on 23 April 2008 for an acquisition consideration of $2,500.

2.9 That is, the Commissioner does not consider that subsection 128-15(3) of the 1997 Act applies, but that the beneficiary was always "absolutely entitled" to the asset, as against the legal personal representative, pursuant to section 106-50 of the 1997 Act.

3. Distributions from testamentary trusts

3.1 It is uncertain whether the CGT exemption in subsection 128-15(3) of the 1997 Act applies to the transfer of an asset from a testamentary trust to a beneficiary.

3.2 The Commissioner has contended that because the trustee of a testamentary trust (who may have also been an executor) has ceased to be an executor, Division 128 of the 1997 Act no longer applies. This is because Division 128 of the 1997 Act only applies in relation to "legal personal representatives", and a legal personal representative is defined in subsection 995-1 of the 1997 Act as:

> ***Legal personal representative*** *means:*
>
> *(a) an executor or administrator of an estate of an individual who has died; or*
>
> *(b) a trustee of an estate of an individual who is under a legal disability; or*
>
> *(c) a person who holds a general power of attorney that was granted by another person.*

3.3 Given the definition of "legal personal representative", and in particular, that it does not include a "trustee", the transfer of an asset to a beneficiary, whether in the exercise of power of a power (e.g. a power of appointment or a power of advancement), may be subject to a CGT event.

3.4 However, the contrary argument is that a testamentary trust is subject to the concessions contained in Division 128 of the 1997 Act (and in particular, subsection 128-15(3) of the 1997 Act).

3.5 In ATO Practice Statement Law Administration PS LA 2003/12, entitled *Capital gains tax treatment of the trustee of a testamentary trust* (**"the Statement"**), the Commissioner at ([2]) contends that he will follow in the administrative practice of treating the trustee of a testamentary trust in the same way as an executor is treated for the purpose of Division 128 of the 1997 Act.

3.6 In the Statement, the Commissioner says that the Statement "*… outlines our administrative practice of treating the trustee of a testamentary trust in the same way as a legal personal representative for capital gains tax purposes* …". At [2] of the Statement, the Commissioner says:

> *2. What is the effect of the practice for the trustee of a testamentary trust?*
>
> *Broadly stated, the ATO's practice is to not recognise any taxing point in relation to assets owned by a deceased person until they cease to be owned by the beneficiaries named in the will (unless there is an earlier disposal by the legal personal representative or testamentary trustee to a third party or CGT event K3 applies).*

3.7 In particular, the Commissioner says in the Statement that subsection 128-15(3) of the 1997 Act will apply so that any capital gain or capital loss that arises where an asset owned by a deceased person passes to the ultimate beneficiary of a trust created under the deceased's will is disregarded.

3.8 The Commissioner considers that this long-standing practice promotes the policy of a provision.

3.9 The Commissioner has confirmed this treatment in Taxation Ruling TR 2006/14, entitled *Income tax: capital gains tax: consequences of creating life and remainder interests in property and of later events affecting those interests*, subject to certain qualifications, being:

3.9.1 The concessional treatment only applies to a CGT asset that the deceased held as at death. If the trustee of the testamentary trust acquires assets (to be held on trust) after death, then those CGT assets will not, when transferred to a beneficiary, benefit from the exemption of Division 128 of the 1997 Act. In such a situation, the testamentary trust is treated as though there are two trusts, one to which Division 128 applies, and the second to which Division 128 of the 1997 Act does not apply. With respect to the "non-Division 128" trust, the distribution of the "after acquired assets" by the trustee may be subject to CGT events E5, CGT event E6 or CGT event E7. In this regard, the Commissioner takes the view that if there are two or more capital beneficiaries, then they cannot be "absolutely entitled" to a trust asset as against the trustee, unless the relevant CGT asset(s) are *"fungible"* (see footnote 3 to Taxation Ruling TR 2006/14 and Draft Taxation Ruling TR 2004/D25).

3.9.2 If CGT Event E5 does not happen, then CGT Event E7 happens when the trustee disposes of the asset to the beneficiary. Under both CGT event E5 and CGT event E7, the trustee makes a capital gain and capital loss equal to the difference between the market value of the asset and the date of the CGT event and the cost base of the asset.

The difference between the two CGT Events is the timing.

CGT Event E5 happens when the trustee becomes absolutely entitled to the asset, which may be ***before*** the trustee distributes the asset.

CGT Event E7 occurs when the trustee ***distributes*** the asset.

The timing difference may affect either, or both:

(a) the quantum of the gain or loss the trustee makes; and

(b) the year of income in which it occurs.

3.9.3 If an income beneficiary receives an asset in full or partial satisfaction of the beneficiary's right to receive income, then CGT Event E6 may happen. As in the case of CGT Event E7, the trustee makes a capital gain and capital loss equal to the difference between the market value of the assets and its cost base. The trustee makes the gain at the time of ***disposing*** the assets.

3.10 As a result, if the trustee of a testamentary trust holds CGT assets that the deceased owned immeditaley before death, and also acquires CGT assets after the death of the deceased, then there may be different tax implications upon the distribution of the CGT assets, and as a result, the trustee is required to split the trust asset into two classes into:

3.10.1 those that were originally part of the deceased estate (which will not give rise to CGT); and

3.10.2 those acquired after death.

4. Effect of a family provision order CGT and stamp duty

(a) Capital gains tax implications of a family provision order

4.1 Paragraph 128-20(1)(a) of the 1997 Act provides that '*A CGT asset passes to a beneficiary in your estate if the beneficiary becomes the owner of the asset … under your will, or that will as varied by a court order…*'.

4.2 Because section 72 of the Succession Act *2006* (NSW) (**'the Succession Act'**) (and see also section 14 of the *Family Provision Act 1982* (NSW) (**'the Family Provision Act'**) with respect to deaths that occurred before 1 March 2009) provides that a family provision order has the effect of varying the will of the deceased, paragraph 128-10(1)(a) of the 1997 Act has the effect of having assets which pass pursuant to a family provision order to be a transfer pursuant to the deceased's will.

(b) Stamp duty implications of a family provision order

4.3 Deaths that occur before 1 March 2009, the Family Provision Act applies. Chapter 3 of the Succession Act applies with respect to deaths after 1 March 2009 (see clause 11(2) of Schedule 1 of the Succession Act).

(c) Effect of a family provision order

4.4 Section 14 of the Family Provision Act, and section 72 of the Succession Act provides that the effect of a family provision order is that the order is a codicil to the deceased's will. As a result, if a family provision order is made with respect to a deceased's estate (i.e. with respect to assets beneficially owned by the deceased as at the time of death and which passes to the LPR – see *Easterbrook v Young* (1977) 136 CLR 308 – and not out of the deceased's 'notional estate') is made, then as the order is deemed to be a codicil to the deceased's will, section 63 of the Duties Act will prima facie apply to subject any transfer of NSW dutiable property no nominal duty.

(d) Effect of a notional estate order

4.5 However, if an order is made from the 'notional estate' of a deceased person pursuant to section 15 of the Family Provision Act, or section 66 (and 69) of the Succession Act, specific exemptions in the respective Acts apply.

4.6 With respect to an order pursuant to section 15 of the Family Provision Act, section 34 of the Family Provision Act provides than an '*… instrument executed pursuant to an order made under section 15, being an instrument relating to property in the notional estate of a deceased person, is not liable to duty under the Duties Act 1997*'.

4.7 Similarly, subsection 66(3) of the Succession Act provides that with respect to 'notional estate' orders made pursuant to the Succession Act provides that:

The execution of an instrument relating to property in the notional estate of a deceased person pursuant to an order under this section is not liable to duty under the Duties Act 1997.

4.8 Regard should also be given to the Chief Commissioner's comments in Revenue Ruling No SD 032, entitled *Family Provision Act 1982 – Duty Concessions*,[1] which dealt with the interaction between the Family provision Act and the (repealed) *Stamp Duties Act 1920* (NSW). In that ruling, the Chief Commissioner observed that:

> *The approach from an assessment point of view does not, however, need any detail to be supplied due to the terms of Section 34. That Section specifically states that an instrument executed pursuant to an order under Section 15, insofar as the instrument relates to property in the "notional estate" of a deceased person, is not liable to stamp duty under the Stamp Duties Act, 1920.*

(e) Deeds of arrangement to vary the terms of a will

4.9 Paragraph 128-20(1)(d) of the 1997 Act provides that "… *A CGT asset **passes** to a beneficiary in your estate if the beneficiary becomes the owner of the asset … under a deed of arrangement if:*

> *(i) the beneficiary entered into the deed to settle a claim to participate in the distribution of your estate; and*
>
> *(ii) any consideration given by the beneficiary for the asset consisted only of the variation or waiver of a claim to one or more other CGT assets that formed part of your estate.*

4.10 The Commissioner in Taxation Ruling TR 2006/14, entitled *Income tax: capital gains tax: consequences of creating life and remainder interests in property and of later events affecting those interests* observed with respect to paragraph 128-20(1)(d) of the 1997 Act that:

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[1] Paragraph 17 of Revenue Ruling No. DUT 1 entitled *Commencement of the Duties Act 1997* acknowledges that the former SD rulings (i.e. those that relate to the (repealed) *Stamp Duties Act 1920* (NSW) '*… may continue to be of guidance in interpreting the provisions of the Duties Act*'.

34. Assets may pass to them as a beneficiary in the estate under paragraph 128-20(1)(d). If this occurs, there will be no consequences for the life and remainder interests as the intended owners of those interests are treated as if they had not been bequeathed them.

35. A deed of arrangement will be effective for the purposes of paragraph 128-20(1)(d) provided that it is entered into:

* *to settle a claim to participate in the estate; and*

* *any consideration given by the beneficiary consisted only of the variation or waiver of a claim to an asset or assets that formed part of the estate.*

36. For the purposes of paragraph 128-20(1)(d) a deed of arrangement must be entered into prior to the administration of the estate being completed unless the beneficiary can demonstrate that a court would, at the time the deed was entered into, have entertained their application for family provision, or an extension of time in which to make such an application. (Paragraphs 209 to 223 of this Ruling further explain this requirement. Importantly, determining whether a Court would entertain applications such as these depends on the succession laws in each State.)

37. A taxpayer is not required to commence legal proceedings in order to establish, for the purposes of paragraph 128-20(1)(d), that they have a claim to participate in the distribution of the assets of the estate. A claim may be established by a potential beneficiary communicating to the trustee their dissatisfaction with the will.

5. Trust restructures

5.1 Trust '**cloning**' and trust '**splitting**' are mechanisms for family succession planning. Ostensibly they are quite straightforward. However, there are significant tax and trust law traps for the unwary.

5.2 Broadly speaking:

(a) '**splitting**' means maintaining the one trust relationship but appointing separate trustees for different assets of that one trust. The trust obligations are undertaken according to the trust relationship provided for in the trust deed establishing the trust;

(b) '**cloning**' involves the establishment of a new trust relationship in respect of assets held by the trustee. That trust relationship may come about by settling the asset on the new trustee or bringing into existence a new trust relationship and transferring the asset to the trustee of that new trust relationship.

5.3 Although trust cloning has been a popular mechanism for the purposes of succession planning in the context of discretionary trusts given the (perceived) availability of exemptions from capital gains tax (more particularly, exemptions from CGT events E1 and

E2)in the past, as a result to amendments to those provisions (such that certain concessions are no longer available), splitting has been the preferred method of ensuring the effective passing of control of trusts between generations.

Splitting – NSW Duty

5.4 Splitting in the way described above rather than cloning is very often driven by stamp duty outcomes. It delivers imperfect separation of control and financial exposure for family members on the basis of the replacement of a trustee, addition of a trustee or retirement of a trustee.

5.5 In New South Wales subsection 54(3) of the *Duties Act* provides:

> *(3) Duty of $50 is chargeable in respect of a transfer of dutiable trust property to a person (other than to a licensed trustee company, a special trustee, a trustee of a self managed superannuation fund or a trustee of a special disability trust) as a consequence of the retirement of a trustee or the appointment of a new trustee if the Chief Commissioner is satisfied that, as the case may be:*
>
> *(a) none of the continuing trustees remaining after the retirement of a trustee is or can become a beneficiary under the trust, and*
>
> *(b) none of the trustees of the trust after the appointment of a new trustee is or can become a beneficiary under the trust, and*
>
> *(c) the transfer is not part of a scheme to avoid duty that involves conferring an interest, in relation to the dutiable trust property, on a new trustee or any other person(whether or not as a beneficiary) so as to cause any person to cease holding the whole or any part of a beneficial interest (or potential beneficial interest) in that property.*
>
> *If the Chief Commissioner is not so satisfied, the transfer is chargeable with the same duty as a transfer to a beneficiary under and in conformity with the trusts subject to which the property is held, unless subsection (3A) applies.*

5.6 Subsection 54(3) of the Duties Act contemplates nominal or no duty if the transfer of dutiable property is to give effect to the retirement of a trustee or the appointment of a new trustee. The provisions require there to be no conferring of an interest in the trust property on the new trustee or any other person to the detriment of the beneficial interest or potential beneficial interest of any other person.

Is there a Resettlement?

5.7 The question that often arises in the context of splitting is whether transfer of assets to another trustee, but subject to the precise terms of the trust instrument, bring into existence a different trust relationship? The argument that this is a new trust derives out of the rationale that a trust is a personal relationship in regard to property subject of the trust instrument between the trustee, the settlor and the beneficiaries. It follows in this argument that, if there is a new trustee, there must be a new trust relationship. This approach emphasises the relationship between the parties as the hallmark of a trust. The alternative view is that the true character of a trust relationship is to be found in the nature of the beneficial entitlements and the identity of the trustee is irrelevant. The writer prefers this latter approach – an appointment of a new trustee in respect of particular assets of the trust but adhering to the terms and conditions is not a new trust relationship but a continuation of the old relationship. Whether or not there is a resettlement turns on the question whether there is an alteration to the substratum of the trust sufficient to constitute it a new trust relationship. The observations of Megarry J in *Re Ball's Settlement*[2] are telling in this regard:

> *'If an arrangement changes the whole substratum of the trust then it may well be that it cannot be regarded merely as varying that trust. But if an arrangement, while leaving the substratum, effects the purpose of the original trust by other means, it may still be possible to regard that arrangement as merely varying the original trusts, even though that means employed are wholly different and even though the form is completely changed.'*

5.8 The question is whether the changes, which have been made, constitute 'a new charter of future rights and obligations' as observed by the High Court in *Davidson v. Chimside.*[3]

5.9 In *Roome v. Edwards (Inspector of Taxes)*[4] it was observed that:

> *'There are a number of obvious indicia which may help to show whether a settlement, or a settlement separate from another settlement exists. One might expect to find separate and defined property, separate trusts and separate trustees. One might also expect to find a separate disposition bring the separate settlement into existence. These indicia may be helpful, but they are not decisive.'*

5.10 The fact that a trustee newly appointed to the trust property declares that it holds the property subject to the terms of the original trust should not in the usual case be a resettlement ie. In Lord Wilberforce's words 'a settlement separate from another settlement'. This was the outcome in Farrar's Case[5] where a declaration was found to be a mere acknowledgment of a pre-existing trust in a New South Wales stamp duty context.

5.11 In New South Wales, the *Trustee Act 1925* (NSW) allows for the appointment of separate trustees prima facie contemplates that the trust property will be held on separate and distinct trusts. Subsections 6(1), 6(5) and 6(8) *Trustee Act 1925* (NSW) provide:

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[2] (1968) WLR 899 at 905.

[3] [1908] HCA 65.

[4] [1982] AC 279 at 292-293 per Lord Wilberforce.

[5] *Farrar v. Commissioner of Stamp Duties* (NSW) (1975) 5 ATR 364.

'(1) A new trustee may by registered deed be appointed in place of a trustee, either original or substituted and whether appointed by the Court or otherwise.

…

(5) The appointment may be made for the whole or any part of the trust property, and on the appointment:

(a) two or more trustees may be appointed concurrently;

(b) the number of trustees may be increased, but not beyond four;

(c) a separate set of trustees may be appointed for any distinct part of the trust property, that is to say, for any part for the time being held on trusts distinct from those relating to any other part or parts, notwithstanding that no new trustees or trustee are or is to be appointed for other parts, provided that the number of trustees in any separate set shall not exceed four;

(d) any existing trustee may be appointed or remain one of the separate set of trustees.

…

(8) Every new trustee appointed under this section as well before as after all the trust property becomes by law or by conveyance or otherwise vested in the new trustee, shall have the same powers, authorities and discretions, and may in all respects act as if the new trustee had been originally appointed a trustee by the instrument, if any, creating the trust.'

5.12 The references to '*held on trust distinct from those relating to any other part*' raise concerns about whether the trust deed has to specifically provide for separate and distinct trusts before there can be separate trustees appointed in respect of separate trust assets.

5.13 Subsection 6(13) of the *Trustee Act* (NSW) provides:

'Except as otherwise provided in subsection (12), this section applies only if and as far as a contrary intention is not expressed in the instrument, if any, creating the trust, and shall have effect subject to the terms of that instrument and to the provisions therein contained.'

Varying the Deed to Allow Separate Trustees

5.14 A further issue is whether the power of amendment be used to allow for appointment of separate trustees where no such power existed or does the amendment amount to a resettlement. Common sense suggests, no (unless there is something in the deed which provides that a single trustee was an absolute requirement or that separation of assets and trustees was prohibited by the deed).

5.15 Based on the views of Brightman J in *Hart v. Briscoe,*[6] Lord Wilberforce in *Roome v. Edwards*[7] and Mahoney J in *Kearns v. Hill*[8] the use of a power of amendment set out in the trust deed (and without any relevant imbedded limitations being breached) to allow the appointment of separate trustees to the trust assets is unlikely to be a resettlement so that a new trust estate comes into existence.

Appointment of Separate Appointor - the CGT Events

5.16 When the original trustee disposes of a CGT asset to the additional trustee there is a change in legal title i.e. a change of ownership for the purposes of subsection 104-10(2) of the 1997 Act. However, the change of ownership does not occur if it happens '*merely because of a change of trustee*'.

5.17 CGT event E1 will not happen if no trust is created by declaration or settlement.[9] All of the reasoning above has been to the effect that there will be no declaration of trust by merely appointing a new trustee or no resettlement. CGT event E2 is not relevant because there is no other existing trust to which the CGT assets are transferred.

5.18 CGT event E3 is not relevant. CGT event E4 could be relevant in the context of a unit trust or hybrid trust. CGT event E5 operates on the basis of a beneficiary becoming absolutely entitled as against the trustee. In the splitting approach no beneficiary becomes absolutely entitled to a CGT asset of the trust. CGT events E6, E7 and E8 are not relevant to a splitting.

5.19 Subject to there being no resettlement triggering a CGT event E1 there should be no relevant CGT event arising on a splitting.

The Tax Return

5.20 One of the minor irritants of trust splitting is the need to have the trustees lodge an income tax return and BAS. The question also arises as to whether or not the trustees need separately to be registered for GST (if that is relevant in the circumstances).

5.21 Subsection 161(1) of the 1936 Act requires every '*person'* to lodge a return of income when required to do so by the Commissioner. A '*person'* is defined to include '*a person in the capacity of trustee of a trust estate*'. This appears to require/allow each trustee to lodge a return of income in respect of the income derived from assets it holds in relation to the trust.

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[6] [1978] 1 All ER 791.

[7] [1982] AC 279.

[8] (1990) 21 NSWLR 107.

[9] Subsection 104-55(1).

5.22 Notwithstanding this possibility nothing will happen without a tax file number. Can each of the trustees acquire its own individual tax file number?

5.23 Section 202B of the 1936 Act provides that a '*person'* may apply to the Commissioner for issue of a tax file number. Based on the definition of '*person'* each trustee appears to be entitled to apply. If the Commissioner is satisfied that the person's identity has been established the Commissioner '*shall issue*' a tax file number to the applicant subject only to:

(c) the Commissioner being satisfied that the person already has a tax file number;
(d) there not being an interim notice.[10]

5.24 It would appear that it is mandatory for the Commissioner to issue a tax file number if satisfied as to the applicant's identity. The exceptions should not apply. The legislation would appear to allow the separate trustee to obtain its own tax file number in respect of its role as trustee of the trust.

5.25 Are the trustees required to be separately registered for GST? An '*entity*' includes a '*trust*'.[11] The trustee of a trust is taken to be an entity consisting of the person who is the trustee, or the persons who are the trustees, at any given time.[12] An entity carrying on an enterprise that meets the registration turnover is required to be registered.[13]

5.26 It would appear that the split trustees cannot be split for GST purposes. This would appear to be in contrast to the position for income tax. It poses a considerable difficulty for complying with the lodgement requirements in respect of BAS. From a practical perspective the Commissioner is likely not to complain if the trustees individually register.

6. Resettlements and amendments to trust deeds

6.1 Whether an amendment causes a resettlement is an issue that confronts practitioners often. The concept of "resettlement" of trusts has been discussed at [5] above.

6.2 The relevant CGT events when considering whether there is a resettlement are CGT event E1 (section 104-55 of the 1997 Act) and CGT event E2 (section 104-60 of the 1997 Act). Subsection 104-55(1) of the 1997 Act provides that "*CGT event E1 happens if you create a trust over a CGT asset by declaration or settlement*". Subsection 104-60(1) of the 1997 Act provides that "*CGT event E2 happens if you transfer a CGT asset to an existing trust*".

6.3 The Full Federal Court in *Clark & Anor v Federal Commissioner of Taxation* (2011) ATC ¶20-236) considered that there would be a "continuity" in a trust relationship if there was a degree of continuity with respect to trust property, constituent documents and Identity of beneficial interest. Further, to establish continuity one

10 section 202BA 1936 Act.

11 paragraph 184-1(1)(g) GST Act.

12 subsection 184-1(2) GST Act.

13 section23-5 GST Act.

must establish degree of continuity of property and continuity of trust obligations in relation to the property. Indeed, at [15] it was observed that "… so long as any amendments of trust obligations relating to such trust property is made in accordance with any power confers…" then not a resettlement.

6.4 That is, if any amendments are made within the scope of the power, then arguably there is a continuity of trust relationship (and no resettlement).

Amendments that change entitlements of takers-in-default.

6.5 The "Default Beneficiary" has a vested (in interest but not in possession), defeasible and contingent interest in the capital of the Trust Fund (see for example Campbell J (as his Honour then was) in *Stein v Sybmore* [2006] NSWSC 1004 (**"Stein's Case"**) and Hartigan Nominees Pty Ltd v Rydge (1992) 29 NSWLR 405 at 426-7 per Mahoney JA (with whom Kirby P agreed).

5.6 Campbell J in Stein's Case at [12] considered the following terms of a trust deed:

> *Clause 6 set out the trusts of capital:*
>
> > *"On the Vesting Day the Trustee shall stand possessed of the capital of the Trust Fund UPON TRUST for all or such one or more of the Primary Beneficiaries as the Trustee may by Deed or by oral declaration and recorded in the Minutes of the Trustee determine and if more than one in such shares as the Trustee may by Deed or by declaration declare but if on the Vesting Day the Trustee has not made such a declaration then for the Residuary Beneficiaries and if more than one in equal shares PROVIDED THAT in the event of any of the Residuary Beneficiaries dying before that Vesting Day and leaving issue surviving them then such issue shall upon attaining the age of twenty one years have the share to which the said deceased person would have been entitled if he had been alive on the Vesting Day and if more than one per stirpes amongst such issue equally but if on the Vesting Day there be no Residuary Beneficiaries or issue of the Residuary Beneficiaries then living for the Secondary Beneficiaries and if more than one in equal shares."*

6.7 At [26] in Stein's Case, his Honour observed of the "Residuary Beneficiaries":

> *In similar fashion, Clause 6 of the Trust Deed gives Tanya and Ian as Residuary Beneficiaries a* ***vested but defeasible interest in the capital of the Trust****. The interest of, say, Tanya in the capital is a* ***contingent interest, because it is contingent on her surviving until the Vesting Day. It is defeasible because if the Trustee appoints the property to someone else****, under the power of appointment contained in Clause 6 or 7, it will no longer flow to her as a taker in default of appointment.* ***Even so, such a***

defeasible contingent interest in the capital is a right of property, which is vested in interest but not in possession. [emphasis added]

6.7 That is, a default beneficiary has an interest which is a right of property which is:

6.7.1 vested in interest, but not vested in possession;

6.7.2 defeasible (that is, subject to the power of appointment); and

6.7.3 contingent (i.e. contingent on surviving the vesting of a trust estate).

6.8 Given that the interest is property, any such interest is also a “CGT asset”, which is defined in paragraph 108-5(1)(a) of the 1997 Act as “*… any kind of property…*”.

6.9 When considering changes to “default beneficiary” entitlement, the section 104-90 of the 1997 Act must be considered (i.e. CGT event E8) being a disposal by a beneficiary of a capital interest. In particular, subsection 104-90(1) of the 1997 Act provides that:

> ***CGT event E8*** *happens if:*
>
> *(a) you are the beneficiary under a trust (except a unit trust or a trust to which Division 128 applies); and*
>
> *(b) you did not give any money or property to acquire the CGT asset that is your interest in the trust capital and you did not acquire it by assignment; and*
>
> *(c) you dispose of the interest, or part of it (but not to the trustee).*

6.10 That is (and amongst other things), in order for CGT event E8 to happen:

6.10.1 there must be an “*… interest in the trust capital …*”; and

6.10.2 “*… you dispose of the interest …*”.

6.11 The term “dispose of” for the purposes of subsection 104-90(1) of the 1997 Act is defined in subsection 995-1(1) of the 1997 Act, by providing that “*… you dispose of a CGT asset (in its capacity as a CGT asset) in the circumstances specified in section 104-10 …*”.

6.12 Section 104-10 of the 1997 Act provides for when CGT event A1 happens, being “*… if you dispose of a CGT asset …*” (subsection 104-10(1) of the 1997 Act).

6.13 Subsection 104-10(2) of the 1997 Act is most relevant for the definition of “dispose of” a CGT asset as contained in subsection 995-1(1) of the 1997 Act, and it provides that:

> *You* ***dispose of*** *a CGT asset if a change of ownership occurs from you to another entity, whether because of some act or event or by operation of law. However, a change of ownership does not occur if you stop being the legal owner of the asset but continue to be its beneficial owner.*

6.14 That is, the concept of “disposing of” a CGT asset is there being a “change of ownership”. In order for there to be any such “change in ownership”, one must have “ownership in the first place (which is “changed”).

6.16 Whilst a default beneficiary has an "interest" which is property, I do not consider that the interest is "*.. in the trust capital …*". This position was accepted by the Commissioner of Taxation in Taxation Determination TD 2009/19, entitled *Income Tax: Does a taker in default of trust capital have an 'interest in trust capital' for the purposes of CGT event E8 in section 104-90 of the Income Tax Assessment Act 1997?*. Further, it seems that a default beneficiary does not have "ownership" of that capital.

6.17 The High Court in *CPT Custodian Pty Ltd v Commissioner of State Revenue of the State of Victoria* (2005) 224 CLR 98, considered that unit holder(s) of unit trusts were not "owners" of the property held subject to the trusts for the purposes of the Victorian land tax provisions. The relevant statutory provisions considered defined "owner" to include "*… every person entitled to any land for any estate of freehold in possession …*".

6.18 Without more (and although not free from doubt), "ownership" in the context of the definition of "dispose of" as contained in subsection 104-10(2) of the 1997 Act (in relation to a CGT asset) requires there to be possession (or at least a right to possession) of the relevant CGT asset (see for example *Palette Shoe Pty Ltd v Krohn* (1937) 58 CLR 1, but see for example *Austin v Sheldon* [1974] 2 NSWLR 661 where a person beneficially entitled under a contract for sale of land was considered an owner for the purposes of receiving compensation for resumption of land.

6.19 As a result, any change in a default beneficiary's interest will prima facie not cause CGT event E8 (or CGT event A1) to happen.

6.20 CGT event C2 happens if there is a cancellation, surrender or similar ending to a CGT (section 104-25 of the 1997 Act). In particular, the CGT event relates to "intangible" CGT assets. Subsection 104-25(1) of the 1997 Act provides that:

> ***CGT event C2*** *happens if your ownership of an intangible CGT asset ends by the asset:*
>
> *(a) being redeemed or cancelled; or*
> *(b) being released, discharged or satisfied; or*
> *(c) expiring; or*
> *(d) being abandoned, surrendered or forfeited; or*
> *(e) if the asset is an option – being exercised; or*
> (f) *if the asset is a convertible interest – being converted.*

6.21 If a default beneficiary's interest is an (intangible) CGT asset, then upon a change of a default beneficiaries interest – such as no longer being a "default beneficiary" - CGT event C2 may happen.

6.22 Any capital gain or capital loss is determined by comparing the "capital proceeds" with the "cost base". If a default beneficiary has not paid any amounts to be a "default beneficiary", then they will not have any "capital proceeds" referable to the default interest.

6.23 Further, if no amount is received by a default beneficiary upon a change occurring, then the market value substitution rule contained in subsection 116-30(1) of the 1997 Act may apply, to deem the default beneficiary to have received the "market value" for the CGT asset that is subject to the event. It should be noted that the exception to the market value substitution provisions of subsection 116-30(1) of the 1997 Act, as contained in subsection 116-30(3) of the 1997 Act may not apply, as the CGT event C2 may not be an "expiry" of a default beneficiary's interest.

6.24 However, subsection 116-30(3A) of the 1997 Act provides that in determining the market value for a CGT asset that is subject to CGT event C2 (where no proceeds are received), that market value is worked out as if the CGT event had not occurred. However, the interts that a default beneficiary may have (or the value thereof) may be minimal.

6.25 Note that the Commissioner, in Taxation Determination TD 2001/26, entitled Income Tax: What are the capital gains tax consequences for a beneficiary of a discretionary trust who renounces their interest in the trust? ("Ruling")

6.26 At [1] of the Ruling, the Commissioner considers that an interest of a beneficiary in a discretionary trust has a CGT asset. At [2] of the Ruling, the Commissioner considers that CGT event C2 happening for a beneficiary that has no interest in the assets or the income of a trust will generally give rise to no capital gain or capital loss, as the market value of their interest would generally be nil.

6.27 However, in relation to a taker in default, the Commissioner at [4] of the Ruling considers as follows:

> *If a beneficiary of a discretionary trust has an interest in either the assets or the income of the trust before or after the exercise of any discretion by the trustee as to the allocation of those assets or income (for example a beneficiary with a default interest) they can also renounce their interest in the trust. In these circumstances, however, a capital gain is more likely to be made by the beneficiary from the renunciation of an interest acquired on or after 20 September 1985 because its cost base is likely to be nil and the interest at the time of the renunciation may have some significant value. Whether the default beneficiary's interest has any substantial value or not will need to be determined on a case by case basis depending in each case on the terms of the particular trust and its purpose, the past history of distributions made by the trustee in favour of the default beneficiary and all the other circumstances of the particular case.*

7. Control of superannuation

7.1.1 Essential in considering control of superannuation after death include (among other things):

- 7.1.2 the terms of any binding death benefit nomination; and
- 7.1.3 determining who the "legal personal representative" of the deceased (after death) of the incapacitated person (before death but after incapacity) is.

Ioppolo & Anor v Conti & Anor [2015] WASCA 45

7.2 In *Ioppolo & Anor v Conti & Anor* [2015] WASCA 45, the Western Australian Court of Appeal (Martin CJ, Buss JA and Beech J) confirmed that upon the death of a member of a self-managed superannuation fund, the *Superannuation Industry (Supervision) Act 1993 (Cth)* (**SIS Act**) permitted, but did not require the executor of the deceased member's estate to be appointed as a trustee of the SMSF. Of concern was section 17A of the SIS Act, which provides that:

> *Subsection 17A(1) of the SIS Act contains the "basic conditions" that need to be satisfied for funds other than single member funds, in order to be a self-managed super fund. Subsection 17A(2) of the SIS Act contains for the "basic conditions" for single member funds so as to meet the definition of a "self-managed superannuation fund".*

7.3 Subsection 17A(1) of the SIS Act provides:

> *(1) Subject to this section, a superannuation fund, other than a fund with only one member, is a **self managed superannuation fund** if and only if it satisfies the following conditions:*
>
> *(a) it has fewer than 5 members;*
>
> *(b) if the trustees of the fund are individuals--each individual trustee of the fund is a member of the fund;*
>
> *(c) if the trustee of the fund is a body corporate--each director of the body corporate is a member of the fund;*
>
> *(d) each member of the fund:*
>
> *(i) is a trustee of the fund; or*
> *(ii) if the trustee of the fund is a body corporate--is a director of the body corporate;*
>
> *(e) no member of the fund is an employee of another member of the fund, unless the members concerned are relatives;*
>
> *(f) no trustee of the fund receives any remuneration from the fund or from any person for any duties or services performed by the trustee in relation to the fund;*
>
> *(g) if the trustee of the fund is a body corporate--no director of the body corporate receives any remuneration from the fund or from any person (including the body corporate) for any*

duties or services performed by the director in relation to the fund.

7.4 Subsection 17A(2) of the SIS Act provides:

> *(2) Subject to this section, a superannuation fund with only one member is a* ***self managed superannuation fund*** *if and only if:*
>
> *(a) if the trustee of the fund is a body corporate:*
>
> *(i) the member is the sole director of the body corporate; or*
> *(ii) the member is one of only 2 directors of the body corporate, and the member and the other director are relatives; or*
> *(iii) the member is one of only 2 directors of the body corporate, and the member is not an employee of the other director; and*
>
> *(b) if the trustees of the fund are individuals:*
>
> *(i) the member is one of only 2 trustees, of whom one is the member and the other is a relative of the member; or*
> *(ii) the member is one of only 2 trustees, and the member is not an employee of the other trustee; and*
>
> *(c) no trustee of the fund receives any remuneration from the fund or from any person for any duties or services performed by the trustee in relation to the fund;*
>
> *(d) if the trustee of the fund is a body corporate--no director of the body corporate receives any remuneration from the fund or from any person (including the body corporate) for any duties or services performed by the director in relation to the fund.*

7.5 However, whilst subsections 17A(1) and (2) of the SIS provide that members of a self-managed super fund must also be trustees, or directors of corporate trustees, subsection 17A(3) provides that certain other persons may be trustees, by providing that:

> *(3) A superannuation fund does not fail to satisfy the conditions specified in subsection (1) or (2) by reason only that:*
>
> *(a) a member of the fund has died and the legal personal representative of the member is a trustee of the fund or a director of a body corporate that is the trustee of the fund, in place of the member, during the period:*

(i) beginning when the member of the fund died; and

(ii) ending when death benefits commence to be payable in respect of the member of the fund; or

(b) the legal personal representative of a member of the fund is a trustee of the fund or a director of a body corporate that is the trustee of the fund, in place of the member, during any period when:

(i) the member of the fund is under a legal disability; or

(ii) the legal personal representative has an enduring power of attorney in respect of the member of the fund; or

(c) if a member of the fund is under a legal disability because of age and does not have a legal personal representative:

(i) the parent or guardian of the member is a trustee of the fund in place of the member; or

(ii) if the trustee of the fund is a body corporate--the parent or guardian of the member is a director of the body corporate in place of the member; or

(d) an appointment under section 134 of an acting trustee of the fund is in force.

7.6 Circumstances in which entity that does not satisfy basic conditions remains a self managed superannuation fund.

7.7 The term “legal personal representative” for the purposes of subsection 17A(3) of the SIS Act is defined in section 10 of the SIS Act as:

> *... means the executor of the Will or administrator of the estate of a Deceased person, the trustee of the estate of a person under a legal disability or a person who holds an enduring power of attorney granted by a person.*

7.8 *Ioppolo v Conti* is authority for the proposition that the SIS Act permits, but does not require, the executor of a deceased member’s estate to be appointed as a trustee of a self-managed super fund.

7.9 The broad facts in *Ioppolo v Conti* were that:

(a) Mrs Francesca Conti and Mr Augusto Conti established the “Conti Superannuation Fund” in 1992.

(b) The Conti Superannuation Fund was established pursuant to the terms of a trust deed.

(c) Pursuant to the trust deed, Mr and Mrs Conti were the Fund’s trustees and members.

(d) The trustee mandated that the Fund was to be conducted pursuant to the terms of the SIS Act, so as to obtain favourable tax treatment which was given to complying superannuation funds.

(e) Since the establishment of the Fund (in 2002), Mr and Mrs Conti made contributions to the Fund. Those contributions were recorded in the accounts of the Fund as standing to the benefit of their respective member accounts.

(f) Mrs Conti passed away on 5 August 2010.

(g) On 28 October 2010, probate of Mrs Conti's Will was granted to her son and daughter, them being the executors of the late Mrs Conti's estate.

(h) Mrs Conti's son and daughter (who are the executors) were issue from a previous marriage of Mrs Conti (that is, they were not Mr Conti's biological children).

(i) On 3 February 2011, Mr Conti (in his capacity as trustee of the Fund) determined that the benefit standing to the account of his wife were to be paid to him rather than to any of her children. Mr Conti did this after obtaining legal advice.

(j) After making the determination, Mr Conti elected to take the benefit in the form of a pension, with the pension being paid to him out of the assets of the Fund.

(k) On 4 February 2011, Mr Conti resigned as a trustee of the Fund and Augusto Investments Pty Ltd was appointed the trustee of the Fund.

(l) Agusto Investments Pty Ltd was a company which Mr Conti was a sole director.

7.10 The executors commenced proceedings claiming:

(a) As a trustee of the Fund, Mr Conti was required pursuant to section 17A of the SIS Act to appoint one of them to act as a trustee of the Fund in place of the late Mrs Conti.

(b) Until such an appointment was made, Mr Conti had no power to deal with the interest that the late Mrs Conti had in the Fund in his capacity as trustee of the Fund.

(c) The executives contended that Mr Conti's determination to confer the interest of the late Mrs Conti to himself was void, and that Mr Conti had acted in bad faith in making the determination by preferring his own interest to the interest of Mrs Conti's children.

7.11 The Western Australian Court of Appeal dismissed the executor's claims, and upheld the decision at first instance (see *Ioppolo & Hesford v Conti* [2013] WASC 389).=

7.12 Martin CJ at [71] considered that there were no words in subsection 17A(3) of the SIS Act which mandated the appointment of a legal personal representative to be a trustee, or a director of a corporate trustee of a self-managed superannuation fund. It was observed at [71] that:

> *Significantly, however, there are no words in s17A(3), or any inference of legislative intension to be drawn from the operation or effect of the subsection viewed in the context of the section or in the context of the SIS Act as a whole, to suggest that a fund is obliged to utilise the opportunities for compliance provided by the subsection either within any particular time, or at all, if there are other means by which the fund can be brought into compliance. Nor is there anything in the language in of the subsection or any inference of legislative intent to be drawn from the effect of the subsection viewed in the context of the section or the SIS Act as a whole to suggest that any constraint is placed upon the powers of the trustee unless and until the opportunities for compliance provided by the subsection are utilised.*

7.13 The other provisions in s17A(3) are, as the executors rightly concede, permissive rather than mandatory. There is no sufficient basis to construe par(a) of s17A(3) differently. Rather, Martin CJ at [72] observed that:

> *To the contrary, a consideration of other provisions of the SIS Act compels the conclusion that s17A(3) should be construed in accordance with its natural and ordinary meaning – that is, as providing opportunities for compliance with the other requirements of the section which might, or might not, be taken up. As I have noted, pt 6 of the SIS Act contains a number of provisions with respect to the governing rules of superannuation entities and includes s52 which contains a number of specific convents to which trustees have regulated funds are subject. If it had been the intention of the legislature to impose obligations upon trustees for the protection of the interests which beneficiaries or dependents of deceased members may have in the benefit standing to the account of a deceased member, Part 6 of the Act would have been the obvious place in which to provide such obligations, rather than in s17A which stipulates the conditions which must be met in order for a regulated fund to achieve the tax concessions which attend satisfaction of those conditions.*

7.14 The Western Australian Court of Appeal also rejected the executor's claim that Mr Conti had acted in bad faith in making the determination that the late Mrs Conti's interest in the Fund should be conferred on him. In the context of the burden of proof, Martin CJ at [81] observed of the lack of discharge of the burden that:

> *As it is the executors who assert that Mr Conti did not exercise a discretion conferred upon him as trustee of the Fund in a bone fide manner, they carry the burden of proving that assertions on the*

balance of probabilities. They have made no attempt to discharge that burden other than by asserting that an inference is to be drawn as to Mr Conti's reasons from the terms of the letter of advice received from Norton & Smailes. No attempt was made to adduce evidence as to the respective financial positions of Mrs Conti's children, as compared to Mr Conti, and Mr Conti was not cross-examined on his Affidavit. If and to the extent that Mrs Conti's wishes were relevant to the exercise of the discretion, as the Master pointed out, the evidence with respect to her wishes was equivocal, given the terms of the Will are inconsistent with binding beneficiary nomination forms which she executed both before and after her Will. It is therefore impossible to draw an inference of lack of bona fides from, for example, an assertive failure to take into account the clear and unequivocal wishes of a deceased. It was open to Mr Conti to consider that the subsequent execution of the binding nomination meant that the expression of intension in the Will had been superseded, and was no longer worthy of weight as an expression of the intention of the deceased member as to what should happen on her death.

7.15 The Western Australian Court of Appeal noted that the Deceased had made binding beneficiaries nomination forms, which had both lapsed. Those nomination forms nominated Mr Conti as the recipient of a death benefit from the Fund. Martin CJ at [74] considered that:

> *There is a cogent argument to the effect that the beneficiary nomination form is executed by Mrs Conti, although deprived of their characteristic as being binding beneficiary nominations by the lapse of time, nevertheless, satisfied the requirement of identifying a person nominated by her as a person she wished to receive her benefit in the event of her death, which is an apt way of describing the role of a Nominated Dependent.*

7.16 As a result, Martin CJ considered that (given the lapsed nomination forms) the only way that the executors could succeed in their argument of lack of bona fides was to demonstrate that the *"... Mr Conti, in his capacity as trustee, failed to address the question of whether it would be inequitable or inappropriate to pay the benefit to himself..."* ([75]).

7.17 However, Martin CJ considered that that question did not need to be resolved as there was no evidence capable of sustaining the conclusion that the exercise of the discretion miscarried ([76]).

7.18 Martin CJ at [77] observed that:

> *In the course of presenting oral argument on these issues, Senior Counsel for the executors advanced a nuanced position not previously evident in either the*

pleadings, the proceedings before the Master, the grounds of appeal or the written submissions in support of those grounds. It was asserted that it should be concluded that there was in fact no exercise of discretion by the trustee, but rather, Mr Conti simply determined that he should have the benefit of Mrs Conti's interests in the Fund for himself. Assuming, for the sake of argument, that it is open, notwithstanding the way in which the case was conducted before the Master, it is difficult to see how this proposition adds anything to the executors' fundamental argument, which is to the effect that it should be concluded the exercise of the trustee's discretion miscarried because he did not give full and proper consideration to the competing interests of the prospective beneficiaries as required by the principle enunciated in Karger v Paul as developed by the High Court in Finch v Telstra Super Pty Ltd. But whichever way the argument is presented, it must fail on the evidence.

7.19 Martin CJ observed that Mr Conti's evidence advanced a series of propositions, which was based on information that he received in advice from solicitors. These propositions included that the executors (in their capacity as children of the deceased) only have a right to be considered by the trustee in the exercise of the discretion of who to pay out any death benefit ([79]).

7.20 The executor's argument (which was not accepted) was that Mr Conti acted pursuant to the legal advice, but excluding that portion of the advice which refers to the right of Mrs Conti's children to be considered in the exercise of the trustee's discretion. The Court considered that *"there is simply no basis in evidence for drawing any inference to that effect"* ([80]).

7.21 It was also noted that there was a clause in the trust deed which provides that a trustee may exercise a power or a right even where there is a conflict of interest, provided that the power of right is exercised in a bona fide manner. There was no argument that that particular provision was offended.

8. Pensions and death of a member – what takes precedence – the pension or the binding death benefit?

8.1 Whilst issues surrounding binding death benefit nominations, or the exercise of a trustee's discretion to pay out a death benefit have been ventilated, an issue that has not been fully explored are the implications of a deceased member of a superannuation fund who was in receipt of a pension.

8.2 In particular, what takes precedence, a binding death benefit nomination, or the terms of a pension?

8.3 Subsection 59(1A) of the SIS Act provides that:

... the governing rules of a superannuation entity may, subject to a trustee of the entity complying with any conditions contained in the regulations, permit a member of the entity, ***by notice given to a trustee of the entity in accordance***

> ***<u>with the regulations, to require a trustee of the entity to provide any benefits in respect of the member on or after the member's death to a person or persons mentioned in the notice</u>****, being the legal personal representative or a dependant or dependants of the member.* [emphasis added]

8.4 Further, Sub-Regulation 6.17A(4) of the SIS Regulations provides that if certain other Sub-Regulations are satisfied (the satisfaction of which I may determine upon receiving further instructions), then a trustee of a superannuation fund ***must*** pay a benefit on or after the death of a member in accordance with a (binding) death benefit notice.

8.5 The Commissioner, in Self Managed Superannuation Fund Determination SMSFD 2008/3, entitled *Self Managed Superannuation Fund: is there any restriction in the Superannuation Industry (Supervision) legislation on a self managed superannuation fund trustee accepting from a member a binding nomination of the receipts of any benefits payable in the event of the member's death?* considers that both section 59 of the SIS Act, and Regulation 6.17A of the SIS Regulations do not apply to self-managed superannuation funds.

8.6 Further there is a view that if the Deceased had made a genuine 'reversionary pension', then the reversionary pensioner (pursuant to the terms of the reversionary pension) will override any nomination made in a binding death benefit nomination. This is because a pension is seen as a contractual arrangement, which overrides (or suspends) the operation of the trust deed.

8.7 In this regard, the Australian Taxation Office's superannuation technical minutes of March 2010 (**'the Technical Minutes'**), the ATO considered the following scenario:

> *A member of a SMSF was in receipt of an account based pension in which his Wife was nominated as the reversionary. He also completed a valid BDBN in favour of his daughters. Following his death, the trustees are unsure which should take precedence - the reversionary nomination or the BDBN*

8.8 In such a circumstance (i.e. where there is a reversionary pension and binding death benefit nomination in place), there are three potential outcomes, either:

8.8.1 the pension remains on foot and the pension to the Wife continues until such time as the Wife dies. When that occurs, then balance in the original Deceased's account is then available for the trustees (of the Fund) to payout as a death benefit (as per the original Nomination); or

8.8.2 the pension remains on foot and now belongs to the Wife. In the event of the Wife's death, the benefits will be paid to the Wife's beneficiaries or to the Wife's estate; or

8.8.3 the reversionary element cannot fetter the trustee's powers and they are bound to stop the pension to the Wife and distribute the benefits as per the Nomination. Any contractual requirement is not able to be overturned by the requirements of the trustee to follow the law or the deed.

8.9 The ATO's view (which it should be noted is not necessarily the correct legal position) that in such a circumstance:

> *However, we would suggest that a pension that is a genuine reversionary pension, that is, one which under the terms and conditions established at the commencement of the pension reverts to a nominated (or determinable) beneficiary must be paid to* the reversioner*. It is only where a trustee has a discretion as to the beneficiary who is entitled to receive the deceased member's benefits and the form in which the benefits are payable that a death benefit nomination is relevant. It must be remembered that section 59 of the SIS Act and regulation 6.17A of the SISR are necessary because of the general trust law principle that beneficiaries cannot direct trustees in the performance of their trust.*

8.10 The issue is not free from doubt, and will depend upon (amongst other things):

8.10.1 the terms of the Fund's deed;

8.10.2 the terms of the Nomination; and

8.10.3 the terms of any pension, and whether it was a reversionary pension.

Denis Barlin

1 May 2017