

Family law decisions may attract ATO attention

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At 2012 WTB 34 [1373] and 2012 WTB 39 [1586], the Family Court decisions in *Morton v Morton* [2012] FAM CA 30 and *Harris v Harris* [2011] FAM CAF 245, respectively, in relation to the potential exposure of assets held via family trusts on a matrimonial breakdown, were analysed.

This article considers a tax specific issue arising as part of *Harris v Harris*, relating to distributions from the trust in question to a company which was found not to be a beneficiary.

Facts of the case

A more detailed summary of the facts of the *Harris* decision is at 2012 WTB 39 [1586]. However, for the purposes of this article, below is an overview of the relevant facts.

One of the issues before the Court was whether a company (AB Pty Ltd) was the property of the relationship between the husband and wife.

AB Pty Ltd had been nominated to receive distributions from the family trust (which was the focus of the case). AB Pty Ltd was structured with the husband as sole director, secretary and shareholder.

As the husband was the sole shareholder, director and secretary, it was conceded by him that AB Pty Ltd was his "alter ego" for the purposes of the family law proceedings and therefore its assets would be available to the wife as part of the property settlement.

Threshold issue

Before determining the amount of the wife's entitlement to the assets of AB Pty Ltd, the Court considered whether the company was in fact a potential beneficiary of the trust.

On reading the trust deed for the family trust, the trial judge noted that AB Pty Ltd was not in fact a potential beneficiary of the trust. This meant that for the purposes of the property settlement, the company should be ignored as all of its potential value derived from the invalid distributions.

While the trial judge did not comment in detail, he did allude to the potential adverse taxation consequences for both the trust and company given their respective tax returns evidenced invalid distributions. While the ability for the wife to access the "assets" of AB Pty Ltd was denied due to the failure to ensure the purported distributions were valid, it was clear that a disgruntled beneficiary or third party (eg the ATO) could challenge the distributions.

Implications of decision

While the "wrongful distributions" (in the words of the Court) were not explored further, the decision highlights the importance that in almost every area where structures are used (whether they be trusts, companies or super funds), it is critical that someone takes responsibility for reading the source documentation before any steps are taken to rely on what might otherwise be assumed to be permitted.

Further, from an asset protection perspective, the conclusion that the company was the alter ego of the husband reinforces the importance of carefully considering the appropriate structure of entities, taking into account the relevant objectives in relation to asset protection (from both creditors and relationship breakdowns), tax effectiveness, and succession planning.

The article at 2012 WTB 34 [1373] relating to the decision of *Morton v Morton* [2012] FAM CA 30 is a useful example in this regard, as in this case a corporate beneficiary (that had validly received distributions from a related family trust) was held not to be an asset of the husband, due to the way it had been structured.