Tax and estate planning in 2020: what has changed?

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In light of ongoing changes to the taxation regime and the expanding wealth of Australia's ageing population, there has for many years been a growing need for estate planning to utilise appropriate structuring. Estate planning related areas have largely been outliers from radical simultaneous rule overhauls. 2018 was an exception to this position, with a range of changes announced. Indeed, the 2018 changes were, in theory, destined to see a potentially radical impact on a number of areas, including trust vesting, trust splitting, testamentary trusts, excepted trust income and family law roll-overs. One year on, however, the question needs to be asked: what has actually changed? Arguably, 2019 has shown that most critical aspects of the 2018 changes remain in a state of flux. With the post-baby boomer intergenerational wealth transfer wave gathering pace, the inertia during 2019 in a number of key areas is disappointing.

Introduction

In light of ongoing changes to the taxation regime and the expanding wealth of Australia's ageing population, there has for many years been a growing need for estate planning to utilise appropriate structuring.

This time last year, an article in this journal argued that 2018 had seen more changes in key estate planning areas in that calendar year than in each of the previous 30 years combined.[1] In particular, potentially important shifts in approaches across the following areas were explored:

- trust vesting;
- trust splitting;
- testamentary trusts and excepted trust income; and
- capital gains tax (CGT) roll-overs on relationship breakdowns.

Twelve months on, this article explores the status of each of the above areas, while also exploring three of the key estate planning related developments in 2019, namely:

1. the latest instalment in arguably the highest profile estate planning exercise in Australia's recent history (involving Lang Hancock, Gina Rinehart and her children);
2. the application of the so-called "safe harbour rule" under the small business restructure roll-over rules in Subdiv 328-G of the *Income Tax Assessment Act 1997* (Cth) (ITAA97); and
3. the use of (binding) financial agreements.

Final trust vesting ruling

In August 2018, the Australian Taxation Office issued its ruling in relation to trust vesting with TR 2017/D10 (finalised as TR 2018/6). The ATO also published details of its administrative approach.[2]

As flagged in last year's article, however, a range of important trust vesting questions remain unanswered.

Set out below is each question identified, a summary of what the position appears to be, and an acknowledgment that there has been no further substantive statement from the ATO in relation to any of these issues.

In what situations will a power of variation be deemed to be too narrow to allow an extension of a vesting date?

Generally, the decision in *Jenkins v Ellett*[3] is a useful point of reference here, given that it explains a number of principles concerning variations, including:

- if an attempt is made to amend fundamental provisions (such as appointor powers or indeed the amendment power itself), there must be a specific ability to do so under the trust instrument;
- conversely, ancillary provisions — of which it is argued the vesting date will generally be categorised as — should be able to be amended so long as there is a robust power of amendment in the trust deed;
- that said, the trust deed may expressly prohibit certain amendments, thereby effectively "hard-wiring" those clauses — again, the vesting date may be such a provision, depending on the terms of the trust deed; and
- the exercise of a power of amendment must comply with any restrictions on the exercise of power, for example, the need to obtain prior consent from a principal or an appointor. The case of *Re Cavill Hotels Pty Ltd*[4] is also often quoted in this regard.

If a power of variation expressly permits retrospective amendments, why will this not allow a vesting date to be extended after it has passed? (TR 2018/6 is blunt in its view that a trust vesting date can never be extended once it has passed.)

In situations where a purported amendment is not within the powers under the deed (or has the consequence of destroying the "substratum" of the trust), it will be held to be invalid and ineffective (see, for example, *Kearns v Hill*[5]).

However, where a deed from establishment expressly contemplates retrospective amendments, it is difficult to see how the ATO can sustain an argument that a variation that complies with the terms of the deed is invalid. In other words, with a properly crafted power of variation, the retrospective extension of a vesting date should be possible.

If there are no default beneficiaries and a trust vests without the trustee being aware, will the trustee of the trust be taxed on all income and capital gains derived (at the top marginal rate, with no CGT discount), pending the assets of the trust being distributed?

Arguably, this question, which we understand was raised during consultation about the draft ruling, is relatively simple to answer. Indeed, there are only two choices, yes or no.

The conservative view appears to be that the answer the ATO will apply here is, yes.

Alternatively, if there are no default beneficiaries, does the ATO instead believe that the assets of the trust pass on a resulting trust to the settlor?

The debate about whether discretionary trusts need provisions that detail how assets will be distributed in the event of a trustee failing to make a decision is longstanding, and arguably unresolved.

For those wishing to avoid being the subject of the next test case to resolve the issue, the conservative view appears to be that the lack of a default provision for capital means that the trust may be held to be void. If this is the case, the invalidity will be deemed to be from the date of creation of the trust, but only if the trustee fails to make a determination to distribute all of the capital on or prior to the vesting day.

While it is often possible to amend a trust deed to insert a default provision for capital, this amendment can potentially result in CGT and stamp duty being payable on the gross assets of the trust — generally, also an unacceptable risk.

Given that most trust deeds contain a clause excluding the settlor of a trust from being a beneficiary, in order to ensure that the trust is not subject to adverse tax consequences as a "revocable" or resulting trust under s 102 of the *Income Tax Assessment Act 1936* (Cth) (ITAA36), the issues here are, in a word, complex.

Perhaps it is understandable that the ATO has chosen not to provide guidance on this issue, either generally or in the context of trust vesting.

Is the position in PBR 1012191260298 still accepted as correct?

In PBR 1012191260298, the ATO confirmed that, where a bare trust that owned shares in a pre-CGT company had made all distributions of income to the same person when the trust vested to that same person, the beneficial interest was not taken to have changed. In other words, the vesting of the trust did not change the majority underlying interests in the company's assets for the purposes of the application of Div 149 ITAA97.

As PBR 1012191260298 remains available on the ATO website, it is assumed that the position adopted in it also remains correct.

Can a trustee resolve to change the jurisdiction under which a trust is administered to South Australia, and thus have any vesting date essentially abolished?

The answer to this question is potentially an entire article in itself.

South Australia has a unique approach (in Australia) in relation to perpetuity periods, having essentially abolished the rule against perpetuities (which is generally 80 years) and allowing trusts to potentially last indefinitely.

Broadly, it appears to be accepted that the settlor of a new trust should be able to nominate a trust's governing law and jurisdiction as South Australia to avoid the rule against perpetuities, even where the trust may otherwise be more closely connected with another jurisdiction.

In *Augustus v Permanent Trustee Co (Canberra) Ltd*,[6] the court held that a provision in a trust deed purporting to establish the trust under the laws of New South Wales was effective in validating a disposition that would otherwise have been void under Australian Capital Territory law. In particular, the court held that it was open to the settlor to specify the governing jurisdiction of the trust.

Applying, by extension, the logic set out above in relation to the ability to amend a trust deed to extend a vesting date, with a wide power of variation, it should also therefore be possible to change the jurisdiction under which a trust is administered.

If an individual default beneficiary of a vested trust dies before the trustee distributes the assets to them, do those assets pass in accordance with their will, without tax consequence due to Div 128 ITAA97?

Arguably, the answer to this question must be yes — if only on the basis that the inverted answer would seem to create an untenable position.

What approach will the ATO have in relation to lost trust deeds, where it is impossible to confirm the date of vesting?

Again, the answer to this question is potentially an entire article in itself.

The conservative, although admittedly unhelpful, best practice approach in relation to a lost trust deed is to find it. Where this is unsuccessful, the next best alternative is a court-approved replacement deed. Again, a broadly unhelpful solution in most situations.

It would seem reasonable to assume that the ATO is unlikely to adopt a conciliatory approach to any tax-related issues with a lost trust deed, although, in saying this, the CGT aspects on any vesting are likely to be the least of the taxpayer's concerns.

Trust splitting

In July 2018, the ATO released its views on trust splitting in TD 2018/D3.

There are a range of concerns with TD 2018/D3 for all trust advisers. The key issue, however, is that TD 2018/D3 remains in draft.

Critically, TD 2018/D3 also assumes a single factual matrix which is very specific, and it lists a number of line items that may, or may not, be a part of a trust splitting arrangement.

Many trust splitting arrangements involve a change of trustee in relation to specific assets and few (or indeed none) of the other features listed in TD 2018/D3 (for instance, no changes to the appointors, right of indemnity or range of beneficiaries).

Given the extended delays in finalising TD 2018/D3, there must be a legitimate question as to its correctness.

Practically, it also seems apparent that the ATO will not issue private rulings on trust splitting arrangements while TD 2018/D3 remains in draft, or at least, it will not issue positive rulings.

Certainly, proceeding with a trust splitting that corresponds exactly with the (one) example in TD 2018/D3 would seem unnecessarily risky. However, there are other approaches that may provide analogous pathways to those otherwise achieved by a trust splitting, for example:

- memorandums of directions;
- the bespoke crafting of trust control roles (such as appointor, principal, guardian or protector powers);
- family councils;
- bespoke trustee company constitutions;
- trust cloning (where other CGT roll-overs are available, given the abolition of the CGT "cloning" exemption on 31 October 2008 for inter vivos discretionary trusts);
- independent trustees; and
- gift and loan back arrangements.

> *"... with a properly crafted power of variation, the retrospective extension of a vesting date should be possible."*

2018 federal Budget attack on excepted trust income

The announcement in the 2018 federal Budget that "the concessional tax rates available for minors receiving income from testamentary trusts will be limited to income derived from assets that are transferred from deceased estates or the proceeds of the disposal or investment of those assets" was, for many, a surprise.

As is usually the case with Budget announcements that attack perceived arbitrage revenue opportunities, the exact impact of the changes will revolve almost entirely around how the legislation is crafted.

Thus, as flagged in last year's article, advisers in the estate planning industry should likely continue to be concerned about what the government means by suggesting that the mischief to be addressed is "that some taxpayers are able to inappropriately obtain the benefit of (a) lower tax rate by injecting assets unrelated to the deceased estate into testamentary trusts".

In turn, the Budget statement that the "measure will clarify that minors will be taxed at adult marginal tax rates only in relation to income of a testamentary trust that is generated from assets of a deceased estate (or the proceeds of the disposal or investment of these assets)" also has the distinct prospect of having much wider consequences than might otherwise be expected.

In a similar vein to the unfinalised trust splitting ruling, the significant delays in any progress in this area are problematic.

Another previous article in this journal[7] explained that, pursuant to Div 6AA ITAA36 and, in particular, s 102AG(2)(a)(i), excepted trust income is the amount which is assessable income of a trust estate that resulted from a will, codicil or court order varying a will or codicil.

Where income is excepted trust income and it is distributed to minors, those minors are taxed as adults, rather than being taxed at the normal penalty rates that otherwise apply to unearned income.

In October 2019, the draft legislation implementing the 2018 Budget announcement was finally released for consultation.[8]

With the unexplained retrospective effect from 1 July 2019, the new rules were crafted as follows:

> "(2AA) For the purposes of paragraph (2)(a), assessable income of a trust estate is of a kind covered by this subsection if:
>
> (a) the assessable income is derived by the trustee of the trust estate from property; and
>
> (b) the property satisfies any of the following requirements:
>
> (i) the property was transferred to the trustee of the trust estate to benefit the beneficiary from the estate of the deceased person concerned, as a result of the will, codicil, intestacy or order of a court mentioned in paragraph (2)(a);
>
> (ii) the property, in the opinion of the Commissioner, represents accumulations of income or capital from property that satisfies the requirement in subparagraph (i);
>
> (iii) the property, in the opinion of the Commissioner, represents accumulations of income or capital from property that satisfies the requirement in subparagraph (ii), or (because of a previous operation of this subparagraph) the requirement in this subparagraph."

As seems to be increasingly the case, the proposed changes see a simple and discrete tax leakage issue on announcement morph into rules that will have far-reaching implications during the legislative drafting process.

Some of the key initial concerns with the draft legislation are:

- the proposed amendments refer to property which was "transferred to the trustee of the trust estate … from the estate of a deceased person";
- to the extent that the trustee of the testamentary trust borrows money (or indeed assumes the borrowings that the deceased was liable to at the date of death) to acquire assets, it appears that income from the assets acquired partially funded by debt would not qualify for excepted trust income treatment;
- similarly, where distributions are made by the trustee to a beneficiary and they are then lent back to the trustee, it seems unlikely that the re-contributed amounts would qualify for excepted trust income treatment;
- the second and third limbs of the eligibility test in proposed s 102AG(2AA)(b) refer to "the opinion of the Commissioner";
- in a self-assessment tax system, this approach creates significant uncertainty for the taxpayer and in turn tax professionals, and also makes it almost impossible

(at least until substantive case law is developed) for a taxpayer to challenge the Commissioner's opinion where they objectively believe that the Commissioner has formed an incorrect or unjust opinion;

- in an area that already has substantial compliance costs, hardwiring subjective tests into the law guarantees further significant costs to taxpayers and is likely to lead to increased administrative issues for the Commissioner;
- many testamentary trusts will exist for decades and the assets originally received from the deceased estate will inevitably be sold over time so that the trust can re-invest in other assets;
- under the proposed changes, a scenario is created where many trusts will be entirely dependent on the Commissioner forming a favourable opinion under the second and third limbs of the new legislation, despite not having taken any steps which could be considered inappropriate;
- the legislation is focused on "the deceased person concerned", and it is unclear why this restriction is relevant. For example, for most couples who both implement testamentary trusts, it will be the case that they will die at different times and there will often be a desire to transfer assets between testamentary trusts;
- it is clearly the case that the excepted trust income rules should continue to apply in situations where a couple both implement testamentary trusts. To argue otherwise would again see the proposed amendments extend significantly beyond the stated intent of the announced measure and impact taxpayers in a range of circumstances where there is no inappropriate tax benefit received by a beneficiary;
- there is arguably no basis for limiting the range of beneficiaries entitled to access the excepted trust income regime to those contemplated by the testamentary trust as originally drafted. Testamentary trusts can potentially last for well over 100 years from the date they are prepared. The only certainty over this type of time period is that there will be changes to the family unit. The Commissioner already has significant power to manage any inappropriate variations to beneficiary classes (eg via the family trust election regime and the trust resettlement rules);
- by adopting an inclusive test (where income only qualifies for excepted trust income status if it is included within one of the three abovementioned limbs), the legislation creates significant administrative difficulties when attempting to "trace" assets and income across multiple financial years. In contrast, an "exclusive" test (where the default assumption is that the trust income qualifies as excepted trust income) would be significantly more robust. Such an approach could simply be subject to a specific exclusion in relation to income from assets which were inappropriately "injected" into the testamentary trust;
- given the tracing requirements mandated by the proposed new rules, the legislation, if it is to proceed as crafted, should arguably expressly confirm that property transferred from a deceased estate to a testamentary trust and then later from the testamentary trust to any other trust, including an inter vivos trust, continues to access the excepted trust income regime; and
- the legislation does not address how assets that are acquired by a testamentary trust as a consequence of the willmaker's death, but are not directly from the willmaker personally, will be treated. An important example in this regard is whether superannuation death benefit payments and insurance policy payouts to an estate will be considered legitimate capital amounts from which to source excepted trust income.

In the context of the proposed changes, it is timely to revisit PBR 1051238902389 which considers the situation where an inter vivos family discretionary trust was distributing to a testamentary trust.

In contrast to the approach of the draft changes, the ruling sees the ATO adopt a more collaborative approach.

Briefly, to the extent relevant, the factual matrix was as follows:

- a willmaker was the ultimate controller of a family trust;
- the willmaker's estate plan attempted to mandate that the assets of the family trust be sold and the cash distributed directly (and equally) to four testamentary trusts established under the will;
- it was acknowledged by the parties that the directions of the willmaker were an attempted fettering of the trustee's discretion. Therefore, while they could be taken into account, they were not to be binding; and
- the assets of the family trust were sold and the intention was to then have the cash distributed to the testamentary trusts.

When determining that the income of a prescribed person (eg including a minor) as a beneficiary of a testamentary trust, even if sourced from a distribution made by a family trust, is excepted trust income (ie the minor could be taxed at adult rates) of the beneficiary, the ATO confirmed the following:

- following the decision in *The Trustee for the Estate of the late AW Furse No. 5 Will Trust v FCT*,[9] a case which was explained in detail in last year's article, all that is necessary for the assessable income of a trust estate to be excepted trust income is that the assessable income be the assessable income of the trust estate and that the trust estate be as a result of a will;
- thus, any amounts representing a distribution from a family trust to a testamentary trust are "assessable income of a trust estate that resulted from a will", and therefore will be "excepted trust income", unless otherwise excluded;
- again, largely following the analysis in the *Furse* decision, the main exclusions (namely, either that the parties are not dealing at arm's length or the arrangement is one predominately driven by achieving the tax benefit) were held not to be applicable and thus access to the excepted trust income provisions was confirmed;
- while the outcome in this private ruling is a positive one, distributions by family trusts to testamentary trusts will clearly be denied access to the excepted trust income regime if the rules announced are legislated as initially drafted; and
- regardless of whether the announced changes become law, the utility of properly crafted testamentary trusts is

likely to remain a key estate planning tool, given the range of other benefits, for example:

– asset protection;
– limited liability (assuming a corporate trustee is used);
– asset management flexibility; and
– wider CGT and income tax planning.

Family law CGT roll-overs

The decision in *Ellison v Sandini Pty Ltd*[10] provided clarity for tax practitioners who are assisting clients involved in a relationship breakdown. In particular, the split decision of the Full Federal Court reconfirmed the generally accepted historical position in relation to CGT roll-over relief on marriage breakdowns.

While perhaps not directly related to estate planning, given that the majority of family groups endure at least one relationship breakdown, it is an area which specialist estate planning advisers must have a working knowledge of.

Among a range of technical issues, the case explored the requirements to access the CGT roll-over relief contained in Subdiv 126-A ITAA97 for relationship breakdowns.

In unwinding the original court decision, which held that the roll-over relief was available for assets transferred to a family trust controlled by one of the parties, the Full Federal Court confirmed that relief is only available where the asset is being transferred to the spouse personally.

Thankfully, 2019 has not seen any substantive iterations in this particular space. That said, however, it is timely to revisit another aspect in the family law area that is increasingly being used as an estate planning tool, namely, financial agreements.

Financial agreements can be used as an estate planning tool in a number of ways, and in particular in:

– later life relationships (ie where couples have children from previous relationships); and
– situations where parents effectively mandate that, in order for their children to benefit under an estate plan, each child must first enter into a financial agreement with their spouse.

High Court summary

The High Court has given guidance in relation to the manner in which parties to a financial agreement must conduct themselves if they are wanting the agreement to be binding. In particular, the High Court unanimously allowed an appeal from the Full Court of the Family Court of Australia in the case of *Thorne v Kennedy.*[11]

The High Court held that two substantially identical financial agreements, a pre-nuptial agreement and a post-nuptial agreement, made under Pt VIIIA of the *Family Law Act 1975* (Cth) should be set aside.

Mr Kennedy and Ms Thorne (both pseudonyms) met online in 2006.

Ms Thorne, an Eastern European woman then aged 36, was living overseas. She had no substantial assets.

Mr Kennedy, then aged 67 and a divorcee with three adult children, was an Australian property developer with assets worth over $18m.

Shortly after they met online, Mr Kennedy told Ms Thorne that, if they married, "you will have to sign paper. My money is for my children".

Seven months after they met, Ms Thorne moved to Australia to live with Mr Kennedy with the intention of getting married.

About 11 days before their wedding, Mr Kennedy told Ms Thorne that they were going to see solicitors about signing an agreement. He told her that if she did not sign it, the wedding would not go ahead.

An independent solicitor advised Ms Thorne that the agreement was drawn solely to protect Mr Kennedy's interests and that she should not sign it.

Ms Thorne understood the advice to be that the agreement was the worst agreement that the solicitor had ever seen. She relied on Mr Kennedy for all things and believed that she had no choice but to enter the agreement.

On 26 September 2007, four days before their wedding, Ms Thorne and Mr Kennedy signed the agreement. The agreement contained a provision that, within 30 days of signing, another agreement would be entered into in similar terms.

In November 2007, the foreshadowed second agreement was signed. The couple separated in August 2011.

In April 2012, Ms Thorne commenced proceedings in the Federal Circuit Court of Australia seeking orders setting aside both agreements, an adjustment of property order and a lump sum spousal maintenance order. One of the issues before the primary judge was whether the agreements were voidable for duress, undue influence, or unconscionable conduct. The primary judge set aside both agreements for "duress".

Mr Kennedy's representatives appealed to the Full Court of the Family Court, which allowed the appeal. The Full Court concluded that the agreements should not be set aside because of duress, undue influence, or unconscionable conduct.

By grant of special leave, Ms Thorne appealed to the High Court. The High Court unanimously allowed the appeal on the basis that the agreements should be set aside for unconscionable conduct and that the primary judge's reasons were not inadequate.

A majority of the court also held that the agreements should be set aside for undue influence. The majority considered that, although the primary judge described her reasons for setting aside the agreements as being based on "duress", the better characterisation of her findings was that the agreements were set aside for undue influence.

The primary judge's conclusion of undue influence was open on the evidence and it was unnecessary to decide whether the agreements could also have been set aside for duress.

Ms Thorne's application for property adjustment and lump sum maintenance orders remains to be determined by the Federal Circuit Court.

What does the decision mean?

As flagged in the above summary, the key issues undermining the validity of the financial agreement in this matter related to the conduct of the husband and the

existence of unconscionable conduct and (by majority) undue influence.

Unconscionable conduct was summarised as follows:[12]

> "A special disadvantage may also be discerned from the relationship between parties to a transaction; for instance, where there is 'a strong emotional dependence or attachment' … Whichever matters are relevant to a given case, it is not sufficient that they give rise to inequality of bargaining power: a special disadvantage is one that 'seriously affects' the weaker party's ability to safeguard their interests."

Undue influence is said to occur when a party is deprived of "free agency" when entering into an arrangement. In other words, when there is something so strong that the influenced party is under the belief that, while the document is not what they want, they feel compelled to sign it anyway.

The High Court listed the following six factors (noting that they are, however, not exclusive) as relevant when assessing whether there has been undue influence in the context of financial agreements:

- whether the agreement was offered on a basis that it was not subject to negotiation;
- the emotional circumstances in which the agreement was entered, including any explicit or implicit threat to end a marriage or to end an engagement;
- whether there was any time for careful reflection;
- the nature of the parties' relationship;
- the relative financial positions of the parties; and
- the independent advice that was received and whether there was time to reflect on that advice.

Admittedly, with the benefit of hindsight, arguably, the case does not significantly change the position in relation to the effectiveness of financial agreements. In particular, if the arrangements had been put in place earlier in the relationship, or at least not so approximate to the wedding, that would have increased the robustness of the agreement.

Similarly, if steps had been taken to ensure that the independent lawyer was able to endorse the appropriateness of the agreement by way of a collaborative negotiation, it would have almost certainly been the case that the arrangements would have been upheld.

The ongoing saga of Lang Hancock's estate plan

Last year's article had a particular focus on the tax aspects surrounding the vesting of a trust established by Gina Rinehart's father (Lang Hancock) under his estate plan — and the level of influence that the case had on the subsequent ATO trust vesting ruling, TR 2018/6.

Another aspect of the litigation surrounding the trust deed that made it all the way to the High Court in 2019 (see *Rinehart v Hancock Prospecting Pty Ltd*[13]), concerned the ability for parties to ensure the confidentiality of agreements entered into by mandating arbitration in the event of dispute (instead of court proceedings).

In attempting to claim against Gina Rinehart for the alleged mismanagement of trust assets, two of her children commenced court proceedings. To support their argument that they were not obligated to instead proceed to private arbitration, they claimed that their signatures on the original agreements (requiring arbitration to be undertaken, not court proceedings) were as a result of misconduct and undue influence by their mother, among others.

In confirming that the disputes were required to be resolved via arbitration, the court confirmed that:

- while there is historical case law confirming that, whenever arbitration is agreed between parties, it applies to all disputes unless the language of the clause makes it clear that certain questions are intended to be excluded, this is not the position in Australia;
- furthermore, there is no overriding assumption that parties who include an arbitration clause in an agreement are likely to have intended any dispute arising out of the relationship to be decided by arbitration, not court proceedings;
- rather, any arbitration clause should be considered in the context of the overall factual matrix, or in the words of the court, "by reference to the language used by the parties, the surrounding circumstances, and the purposes and objects to be secured by the contract";
- in this case, the evidence overwhelmingly supported a conclusion that confidentiality was a key aspect of the agreement between the parties, and thus arbitration applied to all disputes; and
- specifically, the court confirmed that it was "inconceivable that [any] person would have thought that claims … raising allegations such as undue influence, were not to be the subject of confidential dispute resolution but rather were to be heard and determined publicly, in open court".

Subdivision 328-G and the safe harbour rule

Being a federal election year, the 2019 election campaign will arguably be most remembered for the stark differences in tax policies, and the impact in turn of those policies on the result. In this context, the historical announcement by the then Treasurer (the Hon. JB Hockey, MP) on 12 May 2015 that "new businesses create new jobs. That is why we will … [allow] … business owners to … receive tax relief when restructuring their existing business" is perhaps a timely throwback quote.

The above statement, heralding the introduction of Subdiv 328-G ITAA97, being the small business restructure roll-over relief, has been followed by many (arguably expected) limitations overlaid on what was otherwise pitched as a deliberately generous regime.

However, in recent times, the ATO has been active in providing context to its view of the way in which the rules operate.

In addition to the two ATO law companion guidelines (namely, LCG 2016/2 and LCG 2016/3), a series of private rulings has been published, for example:

- PBR 1051401566911, which relates to the transfer of units in a unit trust from a company to a trust, and confirms no tax consequences (including under Div 7A) due to the application of the Subdiv 328-G roll-over;

- PBR 1051286776633, which relates to the tax-exempt transfer of assets from a company to a wholly owned subsidiary company;
- PBR 1051386393245, which relates to the tax-exempt transferring of a client base of an individual and company to a trust;
- PBR 1051386604629, which relates to the transfer of pre-CGT land from an individual taxpayer to a new discretionary trust and confirms that the pre-CGT status of the land is maintained following the transfer; and
- PBR 1051401067097, which relates to the transfer of shares held by an individual in a company to a newly settled discretionary trust, whereby access to the relief under Subdiv 328-G was denied.

There is now also clarity from the ATO in relation to the application of the "safe harbour rule" in PBR 7920126593966.

Background

Briefly, the factual matrix in PBR 7920126593966 (relevantly) was as follows:

- A, B and C were brothers and, in partnership, owners of a grazing property known as "XYZ", in equal shares as tenants in common;
- XYZ was acquired before September 1985 and is a pre-CGT asset;
- the partnership carried on a grazing business on the XYZ property;
- the aggregated turnover of the partnership between A, B and C, as well as their associates, was under $10m in the relevant financial year;
- it was proposed to transfer the XYZ property and grazing business owned by the partnership into a newly established trust structure (New Trust); and
- a family trust election would be made in favour of A in relation to the New Trust.

The ATO confirmed that the roll-over under s 328-430 ITAA97 was satisfied, allowing the transfer of the pre-CGT property into the New Trust, retaining its pre-CGT status.

"Genuine" test and the safe harbour rule

One key issue to date under Subdiv 328-G ITAA97 that has been the subject of some uncertainty relates to the requirement under s 328-430 that the proposed "transaction is, or is part of, a genuine restructure of an ongoing business". In particular, if, when relying on the safe harbour rule in s 328-435 ITAA97, is it also a requirement that the proposed restructure satisfy the definition of a "genuine restructure".

Relevantly, s 328-435 confirms that, for the purposes of s 328-430(1)(a), a transaction is deemed to be a genuine restructure of an ongoing business if, in the three-year period after the transaction takes effect:

- there is no change in ultimate economic ownership of any of the significant assets of the business that were transferred under the transaction;
- those significant assets continue to be active assets; and
- there is no significant or material use of those significant assets for private purposes.

Thus, on a plain reading of the legislation, it would appear that s 328-430(1)(a) is automatically satisfied if the conditions in s 328-435 are satisfied. Furthermore, the explanatory memorandum (EM) to the Tax Laws Amendment (Small Business Restructure Roll-over) Bill 2016 (which introduced Subdiv 328-G) confirmed that a small business "will be taken to satisfy the requirement" in s 328-430(1)(a) if the abovementioned three conditions are met.

Thus, as explained in the EM, it is only if a small business does not satisfy the requirements of the safe harbour rule that it need demonstrate that the transaction is otherwise a genuine one.

ATO view

The ATO confirms the above conclusions, specifically quoting LCG 2016/3, that, where the safe harbour rule is met:

- it is not necessary to consider whether the arrangement would otherwise be a transaction that is deemed to be a genuine restructure of an ongoing business under s 328-430(1)(a); and
- there is no limit or expansion to what would otherwise be considered a transaction that is a genuine restructure of an ongoing business within the ordinary meaning of the phrase.

Thus, in the factual matrix of PBR 7920126593966, the decision by the taxpayer to rely on the safe harbour rule removed the need to consider any aspects of the arrangement, even those that might have gone to whether it was otherwise a genuine arrangement.

The successful reliance is, however, subject to the taxpayer meeting the three conditions in s 328-435 throughout the three-year period after the transaction takes effect. If this occurs, the requirement under s 328-430(1)(a) is deemed to be satisfied at the time of the transaction.

Ongoing issues

In addition to the potential "claw back" of relief for any failure to meet the three conditions in s 328-435 throughout the three-year period after the transaction takes effect, there are two key aspects that will need to be borne in mind in analogous situations to those set out in PBR 7920126593966.

First, the New Trust (and any trustee company) will show a date of establishment well after 1985. Thus, anyone reviewing the New Trust and its assets may, arguably with justification, conclude that its assets are all post-CGT assets. An error that would result in potentially devastating consequences for the taxpayer, and perhaps in turn the advisers who made the incorrect assumption.

In theory, the prospect of such an oversight should be remote. In practice, we are aware of the identical error being made pursuant to historical roll-overs under Subdiv 122-A ITAA97 (where the company transferee was registered in the 2000s, and yet was in fact a pre-CGT company for tax purposes).

Second, the ruling is expressly stated to be subject to the general anti-avoidance provisions under Pt IVA ITAA36. The manner in which Pt IVA could be said to apply in a situation

where the safe harbour rule is satisfied is perhaps difficult to conceptualise.

Given the number of private ruling applications apparently made in relation to the appropriate interpretation of Subdiv 328-G more generally, arguably, the conservative approach, at least in the short-term, appears to be that a private ruling should be obtained before seeking to rely on Subdiv 328-G.

Conclusion

In modern estate planning, significant complexities from the interaction between the legislation relating to tax, trusts, bankruptcy, family law and superannuation have been omnipresent.

The estate planning space has largely been exempt from radical simultaneous rule overhauls. 2018 was arguably an outlier to this position, at least in recent years. 2019 has shown, however, that many of the most critical aspects of the 2018 changes remain in a state of flux.

With the post-baby boomer intergenerational wealth transfer wave gathering pace, the inertia during 2019 in a number of key areas is disappointing.

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Author note

Arguably, the issues with TD 2018/D3 are only partially addressed by the final ruling, TD 2019/14, that was released in December 2019. TD 2019/14 does include a second example explaining how the ATO believes a form of resettlement free trust split can be implemented.

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