Approximately right v precisely wrong: A further reminder in relation to tax equalisation clauses

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In a previous article in this *Bulletin* (reported at 2021 WTB 23 [502]), I considered an (argued) requirement for tax equalisation under a will; reiterating the conclusion that many specialist estate planning advisers argue that these style of clauses are rarely appropriate.

The decision in *Craven v Bradley* [2021] VSC 344 further highlights the difficulties that can arise in this area, particularly where adjustments are required for estimated CGT consequences.

Factual matrix

The will in this case gifted 2 properties to 2 of 3 sons of the willmaker, with clauses then designed to provide for distribution of the remaining estate in a manner to achieve 'equalisation' between the 3 sons, having taken into account the different values of the properties specifically gifted.

The relevant clauses designed to achieve the equality were along the following lines:

- If the remaining balance (of my estate) is more than 3 times the value of property X, then I give property X to my son A free of all duties and encumbrances, and after all costs associated with its transfer have been met from my estate, and the value of property X is included in the gift to my son A.
- If the remaining balance of my estate is less than 3 times of the value of property X, then I give property X to my son A free of all duties and encumbrances, provided he pays to my estate the difference between the value of property X and one-third of the balance of my estate as aforesaid.
- The value of property X should be determined by a registered valuer and on terms that would be granted to an arm's length purchaser from my estate.

In relation to one of the properties, the value of the property for the purposes of the will was to be calculated after deducting 'an amount equal to the capital gains tax liability my estate would pay if the property were sold at the date of my death'. The court accepted that this proviso was due to the willmaker's awareness of the tax-related differences between the 2 properties. That is, one property was the willmaker's main residence, and thus likely exempt from CGT at the date of death.

The court also noted that for the property that was the main residence, the will did not set any specific point in time for the valuation to be conducted.

Disputed issues

The key questions in dispute, and the decision of the court, were as follows:

- should CGT be calculated by reference to the willmaker's taxable income or to the estate's taxable income at the date of the willmaker's death - the court held the estate was the relevant taxpayer, and assumed a simplified understanding of how the CGT provisions operated in this regard; and
- how and at what date should the value of the main residence be ascertained (eg the date of the willmaker's death, the point in time when the son paid into the estate the difference between the value of that property and one-third of the remaining balance of the estate or the date the property was transferred to the son). In relation to this question, there is a statutory presumption in most states, other than Western Australia and the ACT (rebuttable by the provisions of a will),

that the relevant date is the date of the willmaker's death - the court held the statutory presumption was not rebutted and therefore the date of death was the relevant date.

Court clarification

The court also confirmed:

- The interpretation of a will is analogous to the interpretation of a contract. This brings with it a consideration of the purpose of the will, or the purpose of its particular provisions, as well as the facts known or assumed by the willmaker at the time that the will was executed, applying common sense and ignoring evidence of subjective intention (see *Marley v Rawlings* [2015] AC 129).
- No will is made in a vacuum (see *Perrin v Morgan* [1943] AC 399).
- The willmaker's intentions are not necessarily to be discovered by looking at the literal meaning of the words alone, if this leads to the frustration of their intentions. If, in the light of the surrounding circumstances, the literal interpretation gives rise to a capricious result which the willmaker can never have intended, then the literal interpretation should be rejected in favour of a sensible one, which accords with their intention (see *Re Lapalme; Daley v Leeton* [2019] VSC 534).
- If the law has consistently given a particular meaning to some word or phrase, that is the meaning which the word or phrase must, prima facie, be given when interpreting a particular will (see *ANZ Executors & Trustee Co Ltd v McNab* (1999) 3 VR 666).
- It is open to the court, in construing a will, to insert missing words which are clearly necessary to give effect to the willmaker's intention (see *Butlin v Butlin* [1966] HCA 4).
- If, in the context of the will read as a whole, and of the surrounding circumstances, the ordinary meaning of the words in the will do not make sense, extrinsic evidence is admissible under the 'armchair principle'. In effect, this means that the court is able to consider evidence of the circumstances surrounding the willmaker at the time of executing the will (see *Re Staughton; Grant v McMillan* [2017] VSC 359).
- A court is however not entitled to rewrite a will merely because it suspects the willmaker did not mean what is said in the will (see *Perrin v Morgan* [1943] AC 399). Thus, as profiled in the recent case of *Todd v Todd & Ors* [2021] SASC 36 (again, reported at 2021 WTB 23 [502]), the court may determine that there is nothing in a will to support an argument that it evidences an intention that the process of ascertaining the 'equal value' of bequests requires the taking into account future potential taxation liabilities.
- It may be that any required equalisation is only approximate, as was the case here where (for example) the son who did not receive a property would have to pay the costs of that investment if he wanted to obtain a property. These costs would include substantial stamp duty, whereas the other 2 sons received their properties free of that cost (given rollovers available on death under the stamp duty legislation).

Conclusion

As noted previously, it is therefore normally preferable to simply set out directions in the memorandum of directions to the trustees of the estate to ensure that they seek specialist advice at the point of administering the will to ensure that the optimal legitimate tax outcome is achieved for the estate (and therefore the underlying beneficiaries) as a whole.