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Tantalising opportunities for trust restructures under new Subdiv 328-G

- by Matthew Burgess, Director, View Legal

The new Subdiv 328-G rollovers (**the provisions**) commencing 1 July 2016 provide significant opportunities for Small Business Entities (**SBE**) to restructure into a more appropriate entity, assuming the "genuine restructure" provisions can be satisfied. While the restructure requirements have been reported previously (see 2016 WTB 7 [180]), this article considers a number of opportunities to restructure discretionary trusts. In particular:

- trust cloning with or without a Family Trust Election (**FTE**);
- trust splitting and effectively limiting the range of potential beneficiaries without causing a resettlement; and
- restructuring out of trusts with heritage issues.

The new rollovers were introduced via the *Tax Laws Amendment (Small Business Restructure Roll-Over) Bill 2016* (reported at 2016 WTB 5 [127]) which passed all stages without amendment and received Royal Assent on 8 March 2016.

Ultimate Economic Ownership (UEO) and cloning

Section 328-430(1)(c) requires the UEO of assets being transferred remain the same, or in the same proportion after the restructure. While this is relatively simple for companies or sole-traders, it presents difficulties for trusts, where beneficiaries do not have a direct and absolute interest in the assets of the trust (merely a right to due administration).

As previously discussed by John Middleton (see 2015 WTB 49 [1774]), trust cloning of discretionary trusts is again available following its abolition on 31 October 2008 through the provisions without causing any CGT consequences. Where a trust makes (or has previously made) an FTE pursuant to Sch 2F of the ITAA 1936, the provisions ensure (under s 328-440) access to the roll-over if the cloned trust has made the same FTE.

Historically, the Tax Office had set out its view of how to implement a valid trust clone for tax purposes in the (now withdrawn) Taxation Ruling TR 2006/4.

Although not free from controversy, the Tax Office was of the view that in order to implement a valid trust clone, it was necessary for the "beneficiaries and terms of both trusts (to be) the same".

In this context, the position of the Tax Office was that any FTE made by the original trust would need to be made by the cloned trust in order to gain access to the tax concessions.

Under the UEO rules, in situations where there is either no FTE made by the original trust or a desire for the cloned trust to not make a FTE, the provisions still allow cloning to take place so long as there is "no material change" between the original trust and the cloned trust.

It is assumed, pending more detailed comments from the Tax Office, that withdrawn TR 2006/4 will provide at least a framework for how to interpret the concept of "no material change". Given that there is a discrete roll-over available under the provisions for trusts that have identical FTEs, it is reasonable to conclude that the no material change requirement will be satisfied regardless of the approach taken by either trust in relation to a FTE.

Anecdotally, prior to 31 October 2008, there was some debate as to whether "reverse clones" could be implemented without tax consequence. In other words, consolidating assets across 2 or more trusts into one trust. Again, under the provisions, it seems clear that reverse cloning will be available, so long as each trust has made the same FTE, or alternatively, the "no material change" test can be satisfied.

Trust splitting

With the Tax Office providing some clarity in relation to trust splitting through Private Binding Ruling Authorisation Number 1012921290075 (**Ruling**) (reported at 2016 WTB 6 [144]), the provisions appear to provide further opportunities to structure a comprehensive split.

In the Ruling, the Tax Office confirmed its view that narrowing the class of potential beneficiaries of each split trust to a separate family unit would cause a resettlement. Relying on the FTE safety net, it should be possible to limit the range of potential beneficiaries to individuals or classes of individuals falling within the specific family group.

Similarly, all other substantive aspects of a trust split, including limiting the right of indemnity for each trustee to only the assets of the split trust, will fall within the ambit of at least the "identical FTE" aspect of the provisions.

Whether a traditional trust split can also be used, for example, to extract certain assets out of the reach of a pre-existing FTE, for example, by relying on the "no material change" provisions, is more debatable. In particular, from a stamp duty perspective, access to duty concessions in most states for trust splitting relies on any split trust still forming part of the original trust, in which case, any FTE made would need to continue to apply for tax purposes.

Heritage trusts

Where a trust deed has heritage problems, such as limited variation powers or a proximate vesting date, the provisions can be used to transfer the assets to a "clean skin" trust deed, avoiding the difficulties and costs associated with making an application to Court to vary the deed.

While there have been a number of Court decisions in recent years allowing the extension of a vesting date to avoid adverse impending revenue consequences, it should be noted there are similarly a number of cases where the Court has denied such an application (see *Re Arthur Brady Family Trust; Re Trekmore Trading Trust* [2014] QSC 244; *Re Plator Nominees Pty Ltd* [2012] VSC 284; *Stein v Sybmore Holdings Pty Ltd* [2006] NSWSC 1004 and *Paloto Pty Limited v Herro* [2015] NSWSC 445).

In any event, the costs of a Court application itself would appear to be able to be avoided if the provisions can be accessed.

In theory, the new rules will also provide a potential pathway in other problematic areas of an existing trust such as narrow beneficiary classes, mandated (but now inappropriate) appointor or principal roles and, potentially, lost trust instruments.

Future focus

While the provisions appear to meet many of the tax-related issues facing SBEs wishing to restructure, other potential transaction costs, particularly stamp duty, will need to be carefully considered before implementing a rearrangement. With New South Wales, following the lead of Victoria and South Australia, set to abolish stamp duty on business transfers from 1 July 2016, it is hoped that all states fall into line in the near future.

[*Thank you to John Middleton, Clayton Utz, for reviewing a draft of this article.*]