Tax and estate planning in 2022: the year ahead

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Appropriate tax and estate planning strategies will remain critical in 2022 in light of ongoing changes to the taxation regime, expected further amendments to fund COVID-19 government spending, and the massive intergenerational wealth transfer of Australia's "baby boomer" population. Historically, tax and estate planning related areas have largely been outliers from radical rule overhauls. Since 2018, this historical position appears to have permanently shifted with a range of announcements. Subsequent years have seen significant evolution in a number of areas, including trust vesting, trust splitting, testamentary trusts, excepted trust income and family trusts. At the start of a new calendar year, it is timely to explore a number of the most critical developments in the tax and estate planning arena.

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 leverage appropriate tax structuring strategies.

Around this time last year, an article in this journal[1] explored a number of key tax and estate planning related changes, including:

- the ability to structure testamentary trusts (TTs) to minimise the risk that assets will be attacked on the relationship breakdown of a beneficiary;
- the latest guidance from the High Court in relation to the deeming rules that can apply to assets otherwise registered as owned as a joint tenancy;
- the use of enduring powers of attorney to manage superannuation death benefit nominations; and
- the impact of lost trust deeds of an inter vivos discretionary trust.

Twelve months on, this article examines the following key tax structuring and estate planning related developments in 2021, namely:

- a specific tax detriment following the 2018 Federal Budget attack on TTs;
- tax equalisation clauses in estate planning exercises;
- family law and tax equalisation;
- tax-aware family law settlements;
- the tax consequences of changes of trusteeship;
- the impact of loan accounts; and
- trust rectification and tax planning.

A specific tax detriment following the 2018 Federal Budget attack on TTs

The announcement in the 2018 Federal Budget[2] 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 the deceased estate or the proceeds of the disposal or investment of those assets" was, for many, a surprise.

Thus, as flagged in previous articles,[3] 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 the testamentary trust".

With the unexplained retrospective effect from 1 July 2019, the new rules (which are set out in s 102AG(2AA) of the *Income Tax Assessment Act 1936* (ITAA36))[4] have already caused significant concern.

Pursuant to Div 6AA ITAA36,[5] excepted trust income (ETI) 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.

A key question in relation to the rules is the way in which the restrictions operate with regard to ETI in the context of a husband and wife preparing wills incorporating TTs. In particular, are there any tax consequences that flow from preparing (say) the husband's and wife's wills to reflect that, in the event that the husband predeceases the wife (for example), the wife's will provides that her assets will be gifted into the TT previously set up under the husband's will.

Focusing solely on the ETI position, the new rules unfortunately make it clear that, in this situation, the income earned on the wife's assets gifted to the husband's TT will not give rise to ETI. The reason for this is that the legislation mandates that the property must be "transferred to the trustee of the trust estate to benefit the beneficiary *from the estate of the deceased person* concerned" (emphasis added).

An extract from the submission on the draft legislation on this point (which was at the time, and apparently continues to have been, ignored) that our firm made is as follows:

> "The draft 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."

Unfortunately, for all advisers in this space, there is now a further complication that needs to be managed that potentially increases the tax-related administration aspects of deceased estates. That said, despite the changes (and issues like those outlined above), TTs are likely to remain a key tax planning strategy for many advisers and their clients.

Tax equalisation clauses in estate planning exercises

Many specialist tax and estate planning advisers argue that the tax equalisation provisions in wills are rarely appropriate.

The case of *Todd v Todd*[6] (*Todd*) further reinforces a number of the issues in this regard. Relevantly, a key clause in the will provided that the assets be "divided between [the beneficiaries] in such a manner so as to ensure that as at the finalisation of the administration of my estate all of my said children have received an equal value of bequests under this my will".

In question was whether the accumulated (latent) capital gains tax liability attached to each of the key assets should be taken into account when determining the value of the individual bequests or, alternatively, should they be ignored.

The will itself was unclear on the approach to take and the court confirmed that the cases were similarly confused, and indeed possibly in conflict. The court did however confirm the general principles outlined below.

Whether the incidence of CGT should be taken into account when valuing a particular asset varies according to the circumstances of the case, including the method of valuation applied to the particular asset, the likelihood or otherwise of that asset being realised in the foreseeable future, the circumstances of its acquisition, and the evidence of the parties as to their intentions in relation to that asset.

If the court orders the sale of an asset, or is satisfied that a sale of it is inevitable or would probably occur in the near future, or if the asset is one which was acquired solely as an investment and with a view to its ultimate sale for profit, then, generally, allowance should be made for any CGT payable on such a sale when determining the value of that asset for the purpose of the proceedings.

If none of the circumstances referred to above apply to a particular asset but the court is satisfied that there is a significant risk that the asset will have to be sold in the short- to mid-term, the court:

– should not make an allowance for the CGT payable on such a sale when determining the value of the asset;
– may take the risk into account as a relevant factor; or
– should attribute weight to that factor, varied according to the degree of the risk and the length of the period within which the sale may occur.

There may be special circumstances in a particular case which, despite the absence of any certainty or even likelihood of a sale of an asset in the foreseeable future, make it appropriate to take the incidence of CGT into account when valuing that asset. In such a case, it may be appropriate to take the CGT into account at its full rate, or at some discounted rate, having regard to the degree of risk of a sale occurring and/or the length of time which is likely to elapse before that occurs. Arguably, this last point is a practical example of "the vibe" principle, popularised in the movie, *The Castle*.

In *Todd*, the court held that there was nothing to support an argument that "value" should notionally bring potential future CGT liabilities to account. Furthermore, the will evidenced no intention that the process of ascertaining the equal value of bequests required the taking into account of the future potential taxation liability.

It was also held to be incorrect to say that a property bequeathed to a person in the highest bracket of income tax payable for a given year would have a higher value had it been bequeathed to a person who had nil taxable income. This is because such a proposition ignores the fact that CGT liability in respect of a property only arises when (and if) that property is disposed of, and only then will the resultant tax payable (if any) be able to be determined.

Practically, there are a myriad of reasons why tax equalisation clauses are rarely appropriate, for example:

– often a client will only want to take into account the tax position in relation to a particular asset (for example, superannuation). This can lead to significant imbalances in relation to other assets in the estate — most typically, a family home which, like superannuation, can often be received tax-free by a beneficiary;
– while there are embedded tax attributes in relation to certain assets, there can also be embedded tax attributes with the recipient, for example, if a beneficiary is a non-resident at the date they receive the asset, this can trigger a completely different tax outcome as compared to a beneficiary who is an Australian resident. Often these issues will change radically between the date of drafting the will and the date of death;
– where assets are to pass via a TT, this can cause a wide range of potential tax differentials, many of which may be unknown for a significant period of time;
– similarly, to the extent that there are assets held in related entities (for example, family trusts or private companies), there may be a wide range of potential tax ramifications which again may be unknown for a significant period of time;
– the calculations in relation to the net position of each beneficiary can potentially be limitless, for example, additional payments made to one beneficiary to compensate for the fact that they received assets that may have a latent tax liability may cause a further tax liability, which then would trigger a further payment, which of itself would cause a further tax liability; and
– most clauses in this area are also crafted with reference to precise tax provisions at a particular moment in time — there is a material risk that those tax rules will have changed by the time the will actually comes into effect.

The decision in *Craven v Bradley*[7] (*Craven*) further highlights the difficulties that can arise in this area, particularly where adjustments are required for estimated CGT consequences. The will in this case gifted two properties to two of three sons of the will-maker, with clauses then designed to provide for distribution of the remaining estate in a manner to achieve "equalisation" between the three 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 three 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 three 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 will-maker's awareness of the tax-related differences between the two properties, that is, one property was the will-maker's main residence and thus likely to be 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.

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

– whether CGT should be calculated by reference to the will-maker's taxable income or to the estate's taxable income at the date of the will-maker's death: the court held that 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 will-maker'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 will-maker's death: the court held that the statutory presumption was not rebutted and therefore the date of death was the relevant date.

A summary of the key points made by the court is set out below.

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 will-maker at the time the will was executed, applying common sense and ignoring evidence of subjective intention.[8]

No will is made in a vacuum.[9] The will-maker'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 light of the surrounding circumstances, the literal interpretation gives rise to a capricious result which the will-maker can never have intended, the literal interpretation should be rejected in favour of a sensible one which accords with their intention.[10]

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.[11]

It is open to the court, when construing a will, to insert missing words which are clearly necessary to give effect to the will-maker's intention.[12]

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 will-maker at the time of executing the will.[13]

A court is, however, not entitled to rewrite a will merely because it suspects that the will-maker did not mean what is said in the will.[14] Thus, in the case mentioned above of *Todd*,[15] 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 in *Craven* 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 two sons received their properties free of that cost (as roll-overs are available on death under the stamp duty legislation).

In light of the significant range of difficulties outlined above, generally it is 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.

Family law and tax equalisation

Somewhat in contrast to the preferred position in relation to tax equalisation under an estate plan, the impact of tax generally in family law property settlements is arguably compulsory. The recent decision in *Lacey & Lacey*[16] provides a useful reminder of some of the key issues in this regard, as summarised below.

Where, as was the case in *Lacey*, a spouse is the sole director and shareholder of a company and there is no doubt that the company is the alter ego of the spouse, the property of the company can be considered as the property of the spouse. This means that the court can make an order in relation to the property of the company without having to rely on the powers under s 90AE(2)(b) of the *Family Law Act 1975* (Cth), which relate to orders imposed on third parties and in part mandate that the court must take into account the tax effects of the order on the parties, and on the third party.[17]

In *Lacey*, due to the tax consequences of the proposed orders (both CGT on forced asset sales and Div 7A ITAA36), the overall proportional share of the parties' assets assessed by the trial judge would not be achieved in a just and equitable manner if tax was ignored, making the initial trial decision unsustainable.

In relation to the proposed receipt of cash from the company by the former wife, the court held that this would probably be deemed as a dividend in her hands and trigger a tax liability under Div 7A because the husband was the sole shareholder in the company and, as his former spouse, the wife would be characterised as an "associated entity".

The court held that the parties (and their advisers) were at least partially responsible for leading the primary judge into the error of ignoring the tax consequences because neither of them presented any evidence on the issue. That said, because the error was legal rather than factual, the tax consequences justified the granting of, and could be argued in, the appeal.

While the Family Law Act allows the imposition of conditions limiting the scope of any rehearing,[18] in this case, the rehearing was to be unconfined because around three years had passed since the initial trial. In other words, a complete retrial of the entire proceedings was ordered.

Ultimately, any family court order or property settlement should also specifically include tax-related indemnities, a point that also seemed to have been missed in the initial trial.

Tax consequences of changes of trusteeship

The starting point for any change of trusteeship is always the terms of the trust deed. In this regard, the "read the deed" mantra is regularly highlighted.

Assuming the trust deed creates the relevant power, and the change of trustee documentation follows the procedure mandated by the trust instrument, there are two key revenue issues to be aware of, namely:

1. CGT; and
2. stamp duty provisions in the relevant jurisdiction (which are outside the scope of this article, other than to note that, while there are generally no stamp duty consequences for merely changing a trustee, the rules to gain access to the relevant exemption are different in each state and territory).

Arguably, the most commonly triggered CGT event is the disposal of a CGT asset (being CGT event A1).

A question that regularly arises, particularly in estate planning and asset protection exercises, is whether a change of trustee triggers CGT event A1.

Relevantly, the *Income Tax Assessment Act 1997* (Cth) (ITAA97)[19] provides as follows:

- CGT event A1 happens if you dispose of a CGT asset; and
- 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 beneficiary owner; or
  - merely because of a change of trustee.

Therefore, it is generally accepted that CGT event A1 does not occur as a result of a change in the trustee and the ATO acknowledges this position.[20] Similarly, there are numerous private binding rulings that confirm the same outcome.[21]

The case of *Advanced Holdings Pty Ltd as trustee for The Demian Trust v FCT*[22] highlights the risks in this area.

In summary, the key issues in relation to the purported change of trustee were as follows:

- the deed required that the principal first remove the trustee if the principal was wanting to appoint a new trustee;
- the documentation did not support an argument that the principal did in fact remove the incumbent trustee;
- furthermore, the documentation failed to effectively evidence the trustee itself resigning and also did not comply with the written notice of intention to resign mandated by the trust deed as needing to be given two months before any trustee resignation;
- while there was a "Notice of Removal of Trustee" signed by a director of the trustee company, as this was signed in the director's personal capacity and not as a director, it was held to be invalid;
- the "Notice of Removal of Trustee" document was also not a valid reliance on the principal powers as the notice was drafted on the assumption that the trustee had in fact already resigned;
- the signed "Deed of Retirement and Appointment of Trustee" also referred to the minutes of the previous trustee company being tabled at the meeting of the directors of the (purported) new trustee company, and yet no such minutes could be produced to the court;
- separately, the documentation that was available was further undermined by the fact that the accountants for the trust produced and backdated documents (leaving an email trail confirming their conduct) in an attempt to create the impression that the change of trustee had in fact occurred many years earlier; and
- there were also allegations (that the court decided it did not need to resolve) that the backdated documents had been further doctored from the actual documents signed in an attempt to create the desired tax outcome.

One of the consequences of the failed change of trusteeship was that the, purported, new trustee was unable to demonstrate that one of the assets it was owner of (being units in a unit trust) were in fact held on trust. This meant that the potentially concessional tax treatment on distributions from the unit trust were instead taxed in the company in its own right.

A number of key issues in this regard were explored in more detail in the appeal decision of *Advanced Holdings Pty Ltd as Trustee for The Demian Trust v FCT*.[23]

While the appeal case essentially confirmed the original decision, the following statements made in the appeal judgment are noteworthy in relation to the way in which trusts are managed (at least for tax purposes).

As a general rule, a court should give effect to the objective intention sought to be achieved where the words of an instrument allow that intention to be given effect. However, the court cannot give effect to any intention which is not expressed or plainly implied in the language of the document, as to do otherwise would be to engage impermissibly in "gratuitous, groundless, fanciful implication".[24]

To the extent of any ambiguity in the terms of a document, the court should construe the clause so that the operation of the trust is advanced.[25]

In this case, a claimed "implied removal" of a trustee lacked the essential words that pertained to what the court referred to as "a straightforward concept". This was held to be fundamental and prevented any favourable interpretation for the taxpayer. Any interpretation other than that demanded by the words of the document (ie an appointment, but no retirement, of trustee) meant that the court would have needed to cross a line from simple construction into rectification.

Statutory provisions, such as s 251A(6) of the *Corporations Act 2001* (Cth) which provides that a minute of a meeting properly recorded and signed is evidence of the proceeding to which it relates unless the contrary is proved, do not mean that such a minute is automatically conclusive evidence of happenings at a meeting unless the contrary is proved. Whether the contrary is proved must be judged on the whole of the evidence. If the evidence establishes that an event recorded in a minute did not occur, the fact of its recording in the minute has no effect.[26]

Thus, where there are other findings of fact firmly adverse to the quality of corporate management by a director, a court is not obliged to accept, at face value and for all purposes, the existence and efficacy of challenged underlying transactions referred to in a company minute.

The court acknowledged that this reality may present a sobering book-keeping reminder to directors of small companies. That said, it was also confirmed that the evidentiary rules established under the statutory provisions are not intended to circumvent the need to establish the efficacy of all of the underlying transactions recorded in a company's minutes in all cases.[27] In this case, the underlying transactions were squarely in issue and their efficacy open to being doubted.

Finally, given that it was found that the taxpayer was not only aware that his accountant had prepared backdated documents, but was also aware of his wilful and reckless inattention to the correctness of the relevant tax returns, the court confirmed that the penalties imposed (of 75% of the tax shortfall amount, further increased by 20%) were appropriate.[28]

This conclusion was reinforced by the finding that the taxpayer's advisers also took steps to prevent or obstruct the ATO.

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Impact of loan accounts

High-profile cases, such as *Clark v Inglis*[29] and *Fischer v Nemeske Pty Ltd*,[30] emphasise the interplay between beneficiary loan accounts, tax and estate planning.

The decision in *McCarthy v Saltwood Pty Ltd*[31] provides another reminder in this area.

In a factual matrix where the integrity of various loan accounts on the balance sheet of a "standard" family discretionary trust was at the heart of litigation commenced following the death of the ultimate controller of the trust, a number of relevant observations were made, as summarised below.

Within certain parameters, the provisions of the Corporations Act[32] (which, essentially state that books of accounts kept by a body corporate are admissible in evidence in any proceeding and are prima facie evidence of any matter stated) may be helpful.

Thus, cases such as *Livingspring Pty Ltd v Kliger Partners*[33] have confirmed that, while the books are prima facie evidence of the matters stated in them, the weight of that evidence is to be measured in accordance with the common sense of the tribunal of fact. This means that the evidence constituted by the company's books may be outweighed by other evidence (including evidence adduced by the proponent of the books, even if the opponent does not give evidence about them), or by some quality or characteristic of the books themselves, even if there is no other evidence.

For example, if a book has the appearance of a draft or (being electronic) has a file title indicating that it is a draft, that alone may be sufficient (all other things being equal) for the tribunal of fact to reject the book as evidence of the matter stated in it, particularly if the book contains inconsistencies or ambiguities or the matter otherwise demands explanation.

In this case, the court accepted that the usual practice was that, at the end of each financial year, the balance of beneficiary loan accounts was debited for funds utilised and credited with income distributed in accordance with the purported resolutions and that the accounts validly reflected this approach.

While there was evidence that any resolutions for distributions were made well after the end of the financial year (and were therefore unlikely to be valid for tax purposes), this did not mean that they were invalid under the deed, nor were the default distribution provisions under the deed enlivened.

The fact that the will-maker essentially appeared to act as sole director of the company, even though there were other directors, did not invalidate resolutions that the will-maker made on behalf of the company.

In particular, while there was no suggestion that the distributions were outside the ambit of the trustee's discretion, it was argued that the trustee had not lawfully made the relevant decision because of the lack of the requisite quorum (at least two directors were required under the constitution) and there were failures to provide directors with formal notices of meetings.

However, the absence of other directors was held not to have detracted from the inference that the will-maker was purporting to make these decisions on behalf of the company.

While s 1322 of the Corporations Act does provide that a proceeding may be invalidated because of procedural irregularity, this will only be where the court is of the opinion that the irregularity has caused or may cause substantial injustice that cannot be remedied by any order of the court. In this regard, the court confirmed that the irregularities in relation to the resolutions failed to cause substantial injustice for the following reasons:

- the other directors were well aware that the decisions in question were made by the will-maker;
- in consultation with the accountant on a yearly basis, the other directors were content with the arrangement of the will-maker essentially acting as a sole director;
- neither of the other directors requested access to the financial reports, or made any effort or request to attend the accountant with the will-maker, review any of the relevant material prior to preparation of the documents, or indeed played any role at all in respect of the financial affairs of the company and the trust, including in the preparation of the end-of-year financial accounts;
- rather, each director was content to simply sign off on the signing pages given to them without discussion;
- since each director was an adult, they had individual responsibilities as a director;
- it was held probable that each director would have had a reasonable understanding of when the meeting with the accountant was to take place and the relevant decision was to be taken, or at the very least, could have made enquiry about those events. There is no suggestion that either ever made such an enquiry.

Ultimately, therefore, there was no basis for a finding that the irregularities caused substantial injustice.

In the context that the deed permitted distributions "to or for the benefit of … General Beneficiaries living from time to time …", a purported distribution to the will-maker after they had passed away was held to be invalid.

As the discovery of this invalid distribution was well after the time at which the deed otherwise required distributions to be made, the amount needed to be allocated in accordance with the default provisions of the trust deed.

Trust rectification and tax planning

A significant number of tax and estate planning exercises that involve a trust see issues arise in relation to trust deeds that, with the aid of hindsight, were not drafted in the way intended. In some instances, there is a need to consider the ability to amend a trust deed by way of rectification.

A recent useful reminder in this regard is the decision in *Wilstead No. 5 Pty Ltd v Smyth.*[34] In this case, due to an apparent error in the drafting of the deed, at least one of the adult parents of infant children was excluded as a potential beneficiary of the trust.

The adult parents had however been receiving distributions from the trust for many years before the error was discovered. The deed also did not seem to have a valid default distribution provision on vesting, with the court observing that the clause was "difficult" to understand.

In accepting the evidence that the intention on establishing the trust had been to include the adult parents as the primary beneficiaries, the court confirmed a range of important points, as set out below.

To address the apparent error by way of arguing a presumed contrary contractual intention is only available where, on an objective construction, the deed results in an absurdity or inconsistency. Here, any potential absurdity or inconsistency arose only due to the subjective intention of the parties. Therefore, the only potential remedy was via rectification.

Rectification was permitted on the basis that the evidence provided clear and convincing proof that, at the time of execution of the trust deed, the trustee and the settlor had a common intention that the adult parents would be primary beneficiaries of the trust.

Furthermore, the inconsistency between the actual common intention and the terms of the trust deed was a result of the wording that the court was being asked to rectify.

While it was argued that the fact that distributions had been made to the adult parents on the assumption that they were primary beneficiaries supported the rectification application, the court confirmed that this did not in fact assist.

In particular, the distributions did not indicate an actual common intention at the time the trust deed was executed. Rather, the distributions were simply evidence that the parties acted on the basis of the actual common intention after that time (a point not relevant to the rectification application).

Pursuant to the Trusts Acts (and similar legislation) in most Australian states and territories (although not NSW), there is power for a court to make prospective variations to trust instruments. The NSW provisions are however more limited. This power can be extremely important where there is no, or a very narrow, power of variation in a trust instrument.

One of the leading cases in NSW in relation to court variations is *Re Dion Investments Pty Ltd.*[35]

In broad terms, the case involved a trust deed set-up in 1973, which the trustee was wanting to amend so as to be able to better manage the trust property. The relevant legislative provision in NSW gave the court the power to amend a trust instrument provided it was "expedient" for the management or administration of trust property.

In rejecting a request to amend the deed by inserting a comprehensive variation power (which in turn would have allowed the trustee to make such changes to the trust deed as it deemed appropriate from time to time), the court confirmed that:

- the legislative provisions in NSW did not allow the court to simply insert into the deed a comprehensive power of variation;
- only specific powers (in contrast to wide discretionary powers) with respect to a particular dealing will be granted under the NSW legislation;
- it was however permissible in NSW for the court to confer particular and limited powers in relation to certain issues, such as how to account for income and capital gains and related tax-driven provisions; and
- despite not originally crafting its variation request along the lines that the court said was permissible, the trustee was permitted to make further submissions in accordance with the court's recommendations for immediate approval.

Interestingly, in the subsequent decision of *Re Dion Investments Pty Ltd*[36] in relation to the same trust, the court authorised a further variation to ensure that the "foreign person" land tax surcharge could be avoided. This was in light of the fact that the trust deed did not give the trustee the ability to exclude foreign persons as beneficiaries. In particular, the relevant power of variation was limited to "trusts" (granted to persons who had all died and therefore had lapsed), not the "powers" — a distinction perhaps most famously explored in the decision of *Jenkins v Ellett*[37] (discussed in an article published in a previous issue of this journal[38]).

The court confirmed that the requirements in the legislation were all met, namely:

- there needs to be a "proposed dealing", being a "sale, lease, mortgage, surrender, release, or disposition, or any purchase, investment, acquisition, expenditure or transaction";
- the dealing must be, in the court's opinion, "expedient"; and
- the dealing must be incapable of being effected because of an absence of power.

Relevantly, the court confirmed that the existence of a tax advantage can form the basis of the "expediency" in the management and administration of the trust property requirement; here, the land tax saving was over $100,000.

This conclusion was reached notwithstanding that the order would adjust or even destroy the rights of some (potential) beneficiaries to the extent that they met the definition of a "foreign person".

The same outcome was granted in the case of *Re Cecil Investments Pty Ltd*[39] (*Re Cecil*) where the trust deed permitted only a variation to the "powers", not "trusts". This case also confirmed that previous attempted variations to the trust deed were invalid as they breached the limitation set out in the power of variation against anything that purported to change beneficiaries who were takers-in-default of appointment.

A comprehensive power of variation is arguably one of the most important aspects of any trust deed.

It is important to keep in mind that the legislation is worded differently in each state and territory. In particular, in Queensland, Western Australia and Victoria, there are more widely drawn provisions than the NSW law considered in *Re Dion*. Similarly, the South Australia legislation also offers wider provisions in comparison to NSW. Reference should therefore always be had to the specific wording of the legislation in the relevant jurisdiction.

Re Cecil is also useful as it confirms that there have been a number of examples as to where tax savings or advantages form a basis of expediency in the management and administration of trust property — one of the key tests that generally needs to be satisfied.

In particular, the decision lists the following examples:

- "… the powers conferred on the Court … should not be withheld merely because their exercise is sought to enable the avoidance of a revenue impost …";[40]
- "As well, the minimisation of the capital gains tax and stamp duty on the trust property provides a separate basis upon which the conferring of the power is expedient";[41]
- "modernisation of the trust deed … with consequential tax benefits, is expedient in the management or administration of the property vested in the trustee…";[42]
- the scope of the court's powers includes preserving trust property and making it financially productive "…which included planning to minimise the impact of tax and duty on the trust property…";[43] and
- "… there are numerous decisions of this Court to the effect that the tax effective administration of a trust is a matter to which regard may properly be had in considering whether or not to exercise discretion".[44]

Conclusion

In modern estate planning, significant complexities from the interaction between the legislation relating to tax, trusts, family law and loan arrangements have become increasingly ubiquitous.

Significant and ongoing changes appear to be the "new normal" for all advisers specialising in holistic estate planning as we head into calendar year 2022.

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6 [2021] SASC 36.

7 [2021] VSC 344.

8 *Marley v Rawlings* [2015] AC 129.

9 *Perrin v Morgan* [1943] AC 399.

10 *Re Lapalme; Daley v Leeton* [2019] VSC 534.

11 *ANZ Executors & Trustee Co Ltd v McNab* [1999] 3 VR 666.

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13 *Re Staughton; Grant v McMillan* [2017] VSC 359.

14 *Perrin v Morgan* [1943] AC 399.

15 [2021] SASC 36.

16 [2020] FamCAFC 73.

17 *Gallieni & Gallieni* [2012] FamCAFC 205.

18 *Ruscoe & Walker* [2001] FamCA 268.

19 In particular, s 104-10 ITAA97.

20 TD 2001/26.

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22 [2020] FCA 1479.

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24 *Fell v Fell* [1922] HCA 55.

25 *Re Baden's Deed Trusts* [1969] 2 Ch 388.

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28 [2021] FCAFC 135 at [186]-[187].

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43 *Barry v Borlas Pty Ltd* [2012] NSWSC 831.

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