Tax and estate planning in 2023: the road ahead

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Understanding holistic tax and estate planning is critical for all tax advisers. In 2023, the extraordinary monetary value involved in the intergenerational wealth transfer of Australia's "baby boomer" population will continue to escalate. Arguably, tax-driven estate planning changes have largely avoided significant government and court intervention. However, since around 2018, this previous position appears to have permanently shifted with a range of measures targeted at ensuring baby boomers – and their chosen beneficiaries – pay their "fair share" of tax. Subsequent years have seen significant evolution in a number of areas, including superannuation, the treatment of tax equalisation provisions, trust loan accounts, trust vesting, testamentary trusts, and excepted trust income. Near 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 over the last 12 months.

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:

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

Twelve months on, this article examines the following key tax structuring and estate planning related developments in 2022, namely:

- trust distributions and trustee duties;
- regulating the assets of related entities;
- asset protection and the "gift and loan back" strategy; and
- superannuation.

Trustee duties and powers under discretionary trusts

The decision of *Mantovani v Vanta Pty Ltd (No. 2)*[2] related primarily to a lost trust deed, an issue explored in previous articles in this journal.[3]

Helpfully, however, the decision also sets out a summary of the key duties owed by a trustee, noting that the office of trustee carries with it a number of strict obligations and duties, many of which are fiduciary in nature.

Fiduciary duties are generally seen as the most onerous of all legal duties and, where they apply, they require a person to act solely in another party's interests.[4]

The case specifically confirms that the duties of a trustee include:

- to become thoroughly acquainted with the terms of the trust and all documents relating to or affecting the trust property;[5]
- to adhere rigidly to the terms of the trust and conform to and carry out the wishes of the settlor as expressed in the deed of trust, which is said to be "perhaps the most important duty" of a trustee;[6]
- to keep and render proper accounts and report to beneficiaries or to a court regarding the administration of the trust;[7]
- to act fairly and impartially between beneficiaries;
- to administer the trust property in a way so as to avoid benefiting one beneficiary, or set of beneficiaries, at the expense of another;[8]
- to make an application for judicial advice where the trustee requires advice or direction in relation to the management or administration of trust property or the interpretation of a trust instrument.[9]

In relation to the last-mentioned duty (ie to seek advice), it should be noted that a failure to seek advice has been held to be at the trustee's "own peril". This is because any departure from the terms of the trust, and any negligence in the performance of the duties of the trust, will amount to a breach of trust.

Similarly, any acts in contravention of the duties imposed on the trustee by the trust or in excess of its powers will also be a breach of trust.[10]

The ability of a court to review, and potentially unwind, a decision of a trustee, including for a breach of fiduciary duties, is in many respects predicated on the trust adviser's mantra profiled often in this journal, namely: "read the deed".

The issues in this regard can be particularly critical in relation to discretionary trusts where, at least in theory, there are few limitations placed on a trustee concerning most key aspects of the administration of the trust.

In a sentence, the rule that the courts appear to apply is that a trustee's decision cannot be reviewed unless, on the material before the trustee, it is one that no reasonable trustee could have made.

What this rule means in any particular factual matrix can, however, be somewhat nuanced.

Key decision

In the case of *Owies v JJE Nominees Pty Ltd*[11] (*Owies*), the appeal court reached an opposite conclusion to the trial judge in relation to the appropriateness of various distributions made by the trustee.

The key error of the initial judge was said to be the adoption "of an unduly narrow view of the evidence and the structure of the trust deed as a whole".

Relevantly, the court confirmed the following key principles in relation to any review of the exercise of a trustee of discretionary powers:[12]

> "In considering the nature of the power to distribute annual income, the starting point must be the nature and purpose of the trust having regard to the terms of the trust deed".

Here, the settlor confirmed in the trust deed their desire to make "provision for the Primary Beneficiaries and the General Beneficiaries". Further:[13]

> "An obvious, but unstated, premise on which the trustee would be expected to discharge its duties is that it would generally be informed about the differing circumstances, needs and desires of each beneficiary as an incident of the familial bonds that underpin the trust and explain its purpose."

If those familial bonds become strained or broken (as they did here), neither the purpose of the trust to provide for the family as a whole, nor the requirement that the trustee properly inform itself, would change.

While the trust deed did contemplate unequal distributions across the beneficiaries (due to the width of the discretionary powers given to the trustee), the exercise of all of the powers had to take into account the purpose of the trust and the default distribution clause that provided that the three children would be entitled in equal shares.

Distributions that did not provide anything to any of the children were considered by the court as being "remarkable".

As explained in *Pitt v Holt*[14] (*Holt*), there is a distinction between distributions that are plainly beyond power (for example, to a person who is not in fact a potential beneficiary) and those dispositions that are within power, but in respect of which there has been some breach of duty (that is, a distribution to a potential beneficiary where the trustee has failed in its duty to give proper consideration to relevant matters or its duty to give real and genuine consideration to the power).

Using the principles in *Holt* therefore, a breach of trustee duty, for example, due to a failure to give due consideration to the interests of a beneficiary or object of a power, does not automatically lead to the decision being set aside and its consequences reversed. Rather, it is necessary for those aggrieved with the breach to establish that the decision should be set aside; it would then be necessary for the court to determine any defence that might be raised in answer.

That is, the distributions are not void, only voidable – a key factor in *Owies* given that the aggrieved beneficiaries had not applied for the distributions to be set aside. Thus, despite the court concluding that the distributions were inappropriate, they remained undisturbed.

The outcome in *Owies*, where a court-unwinding of historical distributions was essentially only avoided due to a technicality in relation to the way in which the proceedings by the aggrieved beneficiaries were crafted, is a stark reminder for trustees, and trust advisers.

In particular, there are onerous obligations that must be discharged before a trust resolution is valid at law – aside from any questions as to the validity or appropriateness of the proposed distribution from a tax planning perspective.

Furthermore, as shown in a decision involving a well-known Australian business family, namely, *Smorgon v ES Group Operations Pty Ltd*[15] (*Smorgon*), advisers in the tax and estate planning space have additional reason for vigilance in this area.

In *Smorgon*, a disgruntled potential beneficiary of a number of discretionary trusts – despite not being a primary beneficiary of most trusts in the group – applied to court seeking access to a vast array of information concerning the trusts.

While access was denied in relation to many of the trusts, in relation to two trusts where the relevant beneficiary was in fact essentially a "primary beneficiary" (and there were no clauses in the trust deed restricting disclosure), access to the trust deeds, profit and loss statements and balance sheets was given by the court, despite the trustee's attempts to deny the beneficiary.

Related entity assets

The decision in *Lewis v Lewis*[16] is centred on a company restructure, driven by an apparent desire to implement estate planning strategies during the lifetime of the willmaker.

The relevant proposed restructure was summarised in the decision as involving the following broad steps:

- an investment company owned by the willmaker, which owns a significant listed share portfolio, makes a Div 7A loan to the willmaker;
- five new companies, owned by new trusts, acquire the listed shares from the investment company at value,

vendor-financed by the investment company on interest-free and unsecured terms; and

- the vendor-financed loans and are released or forgiven and the investment company is wound up.

Interestingly, the proposal would have triggered a CGT cost of around $500,000. While hindsight always makes restructure planning easier, there were arguably a number of potential alternative pathways that would have achieved the same commercial outcome, without causing a taxable event.

The court confirmed that the transactions would be unwound, with the five companies required to hold all assets on a constructive trust for the original investment company for the following breaches of duty by the willmaker:

- breach of fiduciary and statutory duties as a director by entering into transactions that were not for the benefit of the investment company;
- taking steps whereby the willmaker put herself in a position of conflict between the duty to the investment company and her personal interest – the effect of the transactions was to transfer all of the investment company's assets to five other companies. In particular, the willmaker obtained for herself the power to appoint both capital and income, including to herself to the exclusion of any of her children; and
- breach of the statutory good faith obligations under s 181 of the *Corporations Act 2001* (Cth) to act in the best interests of the corporation and for a proper purpose.

Ultimately, the transactions could only have potentially stood with the informed consent of the other shareholder of the investment company.

In the context of the above case, it is relevant to observe a further key estate planning heuristic, namely, that a willmaker can only transfer assets under the will that they legally and beneficially own. This means that assets ranging from those owned in a joint tenancy, to superannuation fund assets, to assets owned via trusts are all unable to be regulated via a person's will, nor are they able to enjoy access to the CGT roll-over otherwise available on death under Div 128 of the *Income Tax Assessment Act 1997* (Cth) (ITAA97).

From first principles, these same rules also apply to assets owned by companies. As seems to be the case in every key area of holistic tax and estate planning, however, care is required in relation to the exception to any general rule.

For assets owned in companies where the willmaker is the sole shareholder and director of the company, there are a series of cases that confirm that it is possible to use a will to mandate the company transfer assets in a certain way. The line of thinking in this regard appears to have first developed in cases in the late 1960s and early 1970s.

For example, in *Re O'Callaghan (dec'd)*,[17] the key relevant conclusion was that where (paraphrasing) "a willmaker who conveys to their executor a direction to reduce into possession an asset not owned by the willmaker, and the executor has from the willmaker the power to do so, the executor is bound to do so, and to deal with it by way of disposition in the way that the willmaker has directed".

In reaching this conclusion, the court referenced a number of early cases that had also supported the outcome, such as *Re Leigh's Will Trusts*[18] and *Re Bowcock (dec'd); Box v Bowcock*.[19]

More recently, in the decision of *Ireland v Retallack*[20] (*Ireland*), no party to the proceedings seemed to question the assumption that the willmaker had the ability to require the executor appointed as "managing director" of a company to deal with the assets of the company as instructed under the will.

While for many estate planning specialists this line of reasoning is unsettling in the context of the mantra that willmakers can only regulate personally owned assets under their wills, on another view, perhaps these cases are simply examples of a pragmatic approach by the courts.

In particular, there would generally be no restriction on a sole shareholder and director achieving their intentions by (for example) amending the constitution for the company specifying issues such as how assets are to be transferred and who the directors will be on certain triggering events, such as death.

> "… the proposal would have triggered a capital gains tax cost of around $500,000 …"

The decision in the case of *Re Lewis's Will Trusts*[21] makes the arguments in the historical cases clear. In this case, the willmaker was the majority shareholder (as opposed to the sole shareholder) in a company. The attempt by the willmaker to mandate how certain assets of the company were to be dealt with on death was held to be invalid. The standard position that assets of a company are not something that individual shareholders have the authority to regulate under their will was confirmed.

At the risk of confusing the position, however, there is authority to suggest an exception to the exception.

In particular, in *Ireland*, the factual matrix was such that the willmaker (who owned 989 of the 990 shares on issue in the relevant company) directed under their will how the assets of the company were to be transferred.

The court confirmed that, so long as the executor "controlled" the company, they were permitted, and indeed obligated, to follow the directions. The only potential limitation to this aspect of the rule was any oppression of the minority shareholder. This possibility was held in this case to be unlikely, given the person holding the one other share was named under the will as the intended recipient of the gift of the company asset.

Arguably, the historical cases highlight a level of ignorance in relation to tax (and duty) consequences. In particular, the gift of an asset by a company due to a direction under a will is likely to trigger both Div 7A of the *Income Tax Assessment Act 1936* (Cth) (ITAA36) and CGT consequences (as well as stamp duty), with no roll-overs for the transfers that would generally otherwise be available for gifts under a will.

The decision in *Wheatley v Lakshmanan*[22] provides a modern and detailed analysis of the key rules in this area, with the case starkly highlighting the risks of ignoring the tax consequences of related entities under an estate plan.

At the heart of the factual matrix in this case was a clause in a will that purported to gift to a child of the willmaker an unencumbered commercial property — with a further tax and asset protection-driven direction that the property "be placed into a trust or superannuation fund of (the child's) choice".

However, the relevant property was owned by a company of which the willmaker was, at all material times (ie both at the date of the making of the will and at the date of death), the sole shareholder.

In confirming that the purported gift of the property was ineffective, the court stated:

- the general position is that a willmaker cannot bequeath something that they do not own;
- it may be that, where a willmaker conveys to the executor a direction to reduce into possession an asset not owned by the willmaker, and the executor is armed by the willmaker with the power to get the asset (eg by directing that all relevant assets are to be held on trust under the estate), they will be bound to do so — and then deal with the asset as directed by the will (see *Re O'Callaghan (dec'd)*[23]);
- that is, if there is the conferral of power on executors to deal with shares in a company that owns the assets in question as if they were beneficial owners, coupled with express gifts under the will, this can give rise to an implication that the trustee was required to use the shares of the company to ensure that the assets of the company are transferred as set out in the will;
- that said, the court commented that it may also be that the earlier cases were in fact decided incorrectly — a point that the court did not need to resolve on the basis that, in the will here, the requisite power was not granted to the executor of the will in any event;
- as submitted to the court, the key reason for suggesting that the previous cases may be wrong at law is that they are vague in clarifying how exactly an executor exercising rights as a shareholder can cause the relevant company to divest itself of the assets purportedly bequeathed. That is, the shareholders do not manage the company's affairs, rather, the directors do, and a court should not construe a will in a manner that would or might place the directors in a position where their statutory duties as directors are in conflict with the willmaker's intentions, based on a conflation of ownership with the management (or day-to-day conduct) of a company;
- the further suggestion that there should be a rectification of the will was also rejected due to a lack of evidence that the willmaker intended to create the power for the executor to achieve the gift of the property owned by the company; and
- there was no evidence supporting the ability for the court to correct a "clerical error" — rather, it seemed that either the willmaker did not make clear, or the lawyer drafting the will did not understand, that the property in question was owned via a company.

Ultimately, while the aggrieved beneficiary was granted a cash settlement pursuant to a court order as part of a family provision application, this amount was significantly less than the value of the property in question and was also arguably partially reduced by a tax cost that the estate incurred.

In this regard, a key aspect of the decision related to the tax consequences of the various proposals considered by the court. The potential tax liability was said to be in the region of $1m.

Relying on the advice of a specialist tax adviser, the court made the following observations (in the context of the implications of a company owned by the willmaker distributing one of its assets to a beneficiary under the will):

- the estate, for tax purposes, would be deemed to be a trust under s 6(1) ITAA36;
- any payment of any amount by the company to the executor of the estate would be a dividend assessable under s 44 or Div 7A ITAA36, and, if the moneys were paid to the executor who then used them to pay the purported gift under the will, the recipient of the gift would be subject to income tax on a flow-through basis;
- if instead the company distributed to the estate and no particular beneficiary was eligible to receive those moneys, the trustee would be taxed (at the highest marginal rate) under s 99A ITAA36;
- an argument that the payment by the company to the beneficiary as a form of notional estate order would not constitute a deemed dividend had been rejected by the ATO in a private ruling[24] issued before the trial — the ATO instead determining that the payment would in fact be treated as a deemed dividend under Div 7A;
- this private ruling in turn references TR 2014/5 in concluding that the reasoning from a family law perspective also applies in the succession law setting and, as such, the requirement in s 109J(b) ITAA36 to access an exemption from the deemed dividend regime is not satisfied; and
- the use of the word "unencumbered" in the gift provision of the will was held to be intended to be in its common parlance, that is, referring to mortgages or charges secured on the property, not the embedded tax liability. Thus, any income tax liability should be largely ignored by the court when determining the appropriate provision to be made for the aggrieved beneficiary. This conclusion

was reinforced by the fact that the tax liability only arose subsequent to the sale of the property, on the distribution of the proceeds of sale – and furthermore the purported gift was held to be invalid in any event.

The court also observed that it seemed likely that tax issues "overtook" common sense during the litigation and contributed to the high level of legal and accounting costs, which the court stated it was inclined to place a significant cap on in terms of what the estate would be liable to pay for.

The exact cap in this regard was confirmed in *Wheatley v Lakshmanan (No 2)*.[25] In this subsequent decision, the court held that, in relation to costs that were over $620,000 for the plaintiff and more than $450,000 for the estate, the estate was effectively required to pay its own costs and a net amount of $160,000 of the plaintiff's costs.

This outcome was after a careful analysis by the court, balancing between depriving the plaintiff of a substantial portion of the legacy ordered in her favour and the estate being further burdened by costs. Given the plaintiff received an award of $820,000 as further provision under the initial judgment, her final net position was likely in the region of $350,000.

Tax minimisation, estate planning and asset protection

Where asset protection strategies are problematic due to the tax (and stamp duty) costs of transferring assets, a relatively well known approach is to implement a "gift and loan back" arrangement.

In broad terms, a "gift and loan back" involves the owner of an asset gifting an amount equal to their equity in the asset to a family trust (or low-risk spouse). The family trust then lends an amount of money to the owner and takes a secured mortgage over the property or registers a security interest on the Personal Property Securities Register over the personal assets of the individual that the protection is intended for.

The gift and loan back approach ensures that there are no CGT or stamp duty consequences to achieving asset protection, subject to the claw-back rules under the bankruptcy regime.

Historically, arguably, the leading case in relation to gift and loan back arrangements was seen as *Atia v Nusbaum* (*Atia*).[26] In summary, the circumstances of this case were as follows:

- Dr Atia (a cosmetic surgeon) entered into a gift and loan back style arrangement with his mother;
- when Dr Atia's mother subsequently called in the debt, Dr Atia argued that the loan and mortgage were not intended to be actually binding and were only a pretence to protect against situations where Dr Atia was sued professionally;
- in particular, Dr Atia argued that his mother was only calling in the debt secured by the mortgage because he had married his girlfriend against his mother's express wishes;
- the court found that all aspects of the legal documentation, including a deed of gift, loan agreement and registered mortgage, had been validly signed; and
- the court confirmed that the legal effect of the signed documentation was exactly as the parties intended it to be and there was no mistake or sham involved. This meant that Dr Atia's mother was allowed to enforce recoverability of the debt and, if necessary, exercise her rights under the registered mortgage.

In *Re Permewan*,[27] the focus was on the removal of an executor of a deceased estate. Relevantly, the factual matrix was as follows:

- a son was the executor of a will for his mother;
- the son was involved in assisting the mother in implementing a gift and loan back arrangement to essentially remove all value from the estate around 17 months before the mother's death;
- the legitimacy of the gift and loan back arrangement was being challenged by a daughter of the mother (as a prelude to challenging the estate of the mother for more provision than what was provided for under the mother's will); and
- there were allegations that the son, in his role as executor, had no intention on behalf of the estate in pursuing an investigation of the veracity of the gift and loan back arrangement.

In the subsequent decision of *Re Permewan No. 2*,[28] the court had to determine how the costs of the case should be borne. This was in the context that the son and his lawyers had conceded that the promissory notes (which had been prepared to evidence both the initial gift and the subsequent loan under the arrangement) had not been validly delivered – impliedly in part because the documentation was dated before the date the trustee company of the trust was registered – and thus the arrangement failed.

To reach its decision on costs, the court explained its views on the legitimacy of the arrangements, assuming that the promissory notes had been effective, with a focus on two key aspects, namely, whether the gift and loan back was void due to either:

- public policy; or
- being a sham.

The court concluded, prior to considering the above points, that the mother did not have $3m in cash to pay to the trust if the promissory notes were called on. Rather, she would have had to liquidate her assets and, even if she did so, the obligation to pay CGT on the realisation of those assets would be likely to have left a shortfall.

Furthermore, the court held that the transactions were not a bona fide inter vivos gift as the mother had no intention of disposing of her property during her lifetime.

Instead, it was held that the documents which recorded the transactions were executed contemporaneously with the mother's will and were only ever intended by her to take

effect on her death. That is, the trust was never intended to call on the promissory notes or attempt to enforce the loan while she was alive. The court stated that, if that had occurred, the mother would have been placed in the position of having to sell her assets (and pay the CGT) to meet her obligations – and the court believed she never intended to do so. The court concluded that the evidence of both the lawyers and accountants for the mother supported this.

The court also concluded that it was "almost certain" that the transactions would have been unenforceable as being contrary to public policy, because:

- the transactions were illusory in that, contrary to reality, they were designed to make it appear that the mother had departed with her property. That conduct amounted to dealing with her property in a testamentary fashion;
- the sole purpose of the conduct was to ensure that there was so little, if anything, left in the estate on death (meaning any challenge against the estate would have no prospect of success); and thus
- the effect of enforcing the transactions would have been to defeat or circumvent the public policy on which the rules concerning challenges against estates are based and would thereby be generally regarded as injurious to the public interest.

The court also concluded that it was "almost certain" that the transactions were a sham, as:

- despite the promissory notes, there was never any intention for the mother or the trust (which she controlled) to pay the amounts of the gift or loan (and trigger the CGT costs); rather
- the transactions were only ever intended by her to take effect on death.

The conclusions in *Permewan No. 2* in relation to both the public policy and sham aspects are on one view only relevant to the question of costs in that particular case. That said, the comments made by the court are a radical departure from cases such as *Atia* (which was not considered in *Permewan No. 2*) where, on an ostensibly similar factual matrix, the concept of a gift and loan back arrangement being void as a sham was expressly rejected. This was on the basis that, where the implementation documentation evidences a genuine agreement reached between the parties, the suggestion of a sham is untenable. That is, where the documents are, on their face, effective, it is not for the court to speculate about the reasons for the transactions being entered into.

Furthermore, a transaction is not a sham merely because it is carried out with a particular purpose or object. If what is done is genuinely done, it should not be deemed to be "undone" merely because there was an ulterior purpose in doing it, such as managing CGT costs or protecting assets from creditors (see *Donnelly v Edelsten*[29] being another, arguably very relevant, case not considered in *Permewan No. 2*).

Similarly, these earlier cases did not entertain any arguments in relation to public policy being a relevant consideration when determining the effectiveness of a gift and loan back arrangement – arguably, at least in part, because, if there was in fact a public policy concern with arranging personal affairs to minimise the risk of a challenge against an estate, the notional estate regime (as exists in New South Wales) would be law in other states.

While the comments in *Permewan No. 2* concerning gift and loan back arrangements are not binding on any other court, they create significant uncertainty for advisers in this area, given the decision completely ignores other leading decisions in the area that each reached contrary conclusions.

At a minimum, *Permewan No. 2* is a reminder for advisers in this area that they must ensure that all legal documentation is validly implemented. Furthermore, advisers must ensure that the relevant asset owner is aware of and, if necessary, willing to incur the CGT consequences of disposing of the assets the subject of the gift and loan back arrangement.

Superannuation and estate planning

The "notional estate" rules that apply in NSW provide that, in certain circumstances, assets or estates that have a connection to NSW, that are not owned personally by a deceased, can still be subject to attack when the estate itself is challenged.

The potential range of assets at risk under the notional estate regime is highlighted by the decision in *Benz v Armstrong*.[30]

In a situation where the personal assets of the deceased, that would have passed to children from his first marriage under the will, were negligible, the application of the notional estate provisions instead created a pool of available assets in the region of $18m.

While the second wife of the deceased (who would have otherwise received all of the wealth) retained more than half of the assets, four adult children from the first marriage received amounts in the region of $1m (two children) and $2m (two children, noting that one child appears to have secured their payment by calling in a credit loan owed by a family trust (controlled by the deceased) to that child, that was held to be repayable on demand).

The allocations to the adult children were despite the fact that the court concluded that all of the children had a relatively privileged childhood, including attending private schools and receiving a university education. Further, none of the children had particularly dire financial or medical issues.

The court confirmed its view that the deceased's testamentary intention was that his children receive an inheritance from him.

Furthermore, given the deceased had a moral obligation to his children, it was extraordinary to think that (in the absence of some far more serious fracture in the relationship with his children) the deceased would have intended his children to obtain nothing at all from his very large estate, particularly when the second wife had already

obtained substantial wealth, both through the relationship and under the will.

Specifically, in relation to the notional estate regime, the court confirmed that:

- all parties appear to have accepted that the family trust fell within the description of "a paradigm case for the intended application of the notional estate provisions". However, given (following the repayment of the credit loan) there would likely be a deficit in the trust, this aspect was not considered further;
- in relation to the deceased's superannuation entitlements (that were in the region of $13m and were subject to a valid binding death benefit nomination (BDBN) within three years of the date of death), the court also concluded that these should form part of the notional estate — even though the death benefit payment would have been received tax-free by the surviving spouse, and instead would be taxable on reallocation to adult children;[31]
- the court acknowledged that, in the case of *Carr v Douglass*[32] (*Carr*), it was held that the failure to renew a BDBN could trigger the notional estate rules as at the date of failure (not at the date of death) because it denied the estate the benefit of the deceased's interest in the superannuation fund. However, the relevant date being the date of failure (as opposed to the date of death) meant that, under the rules, the necessary intention to defeat a notional estate claim also needed to be proved;
- the court also quoted the decision in *Wardy v Salier*[33] that the purpose of the notional estate provisions is to extend the powers of the court in NSW to the full range of benefits and advantages controlled by willmakers, and therefore, insofar as any question of construction presents a choice, an approach that promotes this purpose is preferred;
- thus, here the deceased's failure to revoke his BDBN in the 12 months prior to death (the time period within which the intentions of the deceased are irrelevant[34]) and give a replacement BDBN (in favour of his legal personal representative, to ensure that the entitlements passed into the estate for distribution under the will) was a transaction within the meaning of the notional estate rules, and would also have been caught had there been a failure to make any BDBN at all;[35]
- ultimately, the court concluded that the omission to revoke a BDBN was analogous to an omission to sever a joint tenancy (another situation that is subject to claw-back under the notional estate rules) in light of the fact that the deceased's BDBN could have been revoked at any time prior to death. Therefore, it was not until the moment of death that the failure took effect;
- while this conclusion was acknowledged to perhaps be inconsistent with the reasoning in *Carr*, a distinction was drawn between the omission to renew a BDBN (which was said to take effect when the BDBN lapses) and the failure to revoke or change a BDBN (which subsists up until the date of death); and, furthermore,
- the reasoning in *Carr* was questioned, given other cases where the absence of a valid BDBN meant that the transaction took effect on the resolution of the trustee to distribute the death benefits following the death of the superannuation member. In other words, it was held unnecessary to establish that the failure to revoke was with the intention (wholly or partly) of denying or limiting provision out of the estate within the meaning of the notional estate regime.

In the context of this case, it seems clear that only the removal of funds from superannuation, or a BDBN that is non-lapsing and "double entrenched" in the trust deed (ie unable to ever be changed) — and, in each instance, implemented at least three years before the date of death (the relevant time period for claw-back where the deceased has the intention of defeating claims[36]) — will be outside the NSW notional estate regime.

Non-lapsing BDBNs

For many years, there was a level of debate about whether self-managed superannuation funds (SMSFs) were permitted to offer BDBNs and if so, whether any such BDBN would automatically lapse after three years.

According to reg 6.17A(7) of the *Superannuation Industry (Supervision) Regulations 1994* (Cth) (SISR94), a BDBN regulated by that provision lapses:

- at the end of the period of three years after the day it was first signed, or last confirmed or amended, by the member; or
- if the governing rules of the fund fix a shorter period — at the end of that period.

A similar level of confusion arguably existed in relation to the form of a BDBN, for example, if witnesses are needed, how many should there be? This confusion existed despite the fact that the ATO answered the question succinctly in 2008,[37] where the Commissioner confirmed the view that s 59 of the *Superannuation Industry (Supervision) Act 1993* (Cth) (SISA93) and reg 6.17A SISR94 do not apply to SMSFs.

That is, the governing rules of an SMSF may permit members to make death benefit nominations that are binding on the trustee, whether or not in circumstances that accord with the rules in reg 6.17A SISR94 (including, as one example, if witnesses are needed and, if so, how many are needed).

The decision in *Hill v Zuda Pty Ltd*,[38] as relevantly confirmed by the High Court in *Hill v Zuda Pty Ltd*,[39] provides judicial support for the longstanding approach of the ATO. In this case, the court also specifically confirmed the interpretation that s 59 SISA93 and reg 6.17A SISR94 do not apply to SMSFs, and cross-referenced the decisions in *Munro v Munro*[40] and *Cantor Management Services Pty Ltd v Booth*[41] as further support for this conclusion.

This meant that the failure of the BDBN to comply with reg 6.17A (in that it was made more than three years before

the death of the member and was not witnessed by two witnesses) was irrelevant to the question of whether it was binding on the trustee of the SMSF.

Similarly, the position in relation to non-lapsing BDBNs for non-SMSFs (eg retail, industry, corporate and small APRA funds) has also been the subject of longstanding debate.

The approach that appears generally accepted for non-SMSFs and BDBNs can be summarised as follows, noting that APRA has specifically confirmed in *Prudential Practice Guide SPG 280 – Payment standards* that non-lapsing BDBNs are possible:

- "standard" BDBNs are lapsing and will comply with s 59(1A) SISA93. This means that they will also be regulated by, and need to comply with, reg 6.17A(7) SISR94;[42]
- it is possible, however, for non-lapsing BDBNs to be created under s 59(1)(a) SISA93. This section is not caught by reg 6.17A(7) SISR94 and therefore any BDBN made pursuant to this section does not automatically lapse;
- arguably, the key aspects of ensuring that the non-lapsing BDBN is in fact valid are that the trust deed for the fund must permit the approach and that the trustee of the fund must consent to the BDBN and the form it can be made in[43] (for example, including the number of witnesses); and
- in contrast, standard lapsing BDBNs do not require the consent of the trustee.

Conclusion

For tax and estate planning advisers, the complexities from the interaction between revenue-related legislation and decided cases across key areas such as tax, trusts, superannuation, wills and estates have become increasingly problematic.

As observed previously, significant and ongoing changes appear to be the "new normal" for all advisers specialising in holistic tax and estate planning as we head into 2023.

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17 [1972] VR 248.

18 [1970] Ch 277.

19 [1968] 2 NSWR 697.

20 [2011] NSWSC 846.

21 [1985] 1 WLR 102.

22 [2022] NSWSC 583.

23 [1972] VR 248.

24 Although not expressly stated in the decision, it seems likely that the relevant private binding ruling in this regard is PBR 1051799201069.

25 [2022] NSWSC 851.

26 [2011] QSC 44.

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28 [2022] QSC 114.

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31 Div 302 ITAA97.

32 [2016] NSWSC 854.

33 [2014] NSWSC 473.

34 S 80(2)(b) of the *Succession Act 2006* (NSW).

35 *Kelly v Deluchi* [2012] NSWSC 841.

36 S 80(2)(a) of the *Succession Act 2006* (NSW).

37 SMSFD 2008/3.

38 [2021] WASCA 59.

39 [2022] HCA 21.

40 [2015] QSC 61.

41 [2017] SASCFC 122.

42 Which mandates a number of specific requirements in relation to issues such as the information that the trustee must provide the member, the avatar of the recipient, the manner in which the BDBN is witnessed, and the fact that the maximum length of time the BDBN can remain valid is three years.

43 S 59(1A) SISA93.