

Family court continues attack on testamentary trusts following Budget death tax

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Background

As debate about the stealth style death tax imposed on testamentary trusts by the 2026 Budget continues, a recent decision from the Family Court is now wrecking further chaos on what had (up until a few short weeks ago) been the foundation of thousands of estate plans by older Australians.

The powers of the family court in relation to how the assets of discretionary trusts are treated on a relationship breakdown can be problematic for those wishing to leverage trust arrangements to protect wealth against relationship misadventure.

Arguably the highest profile case in modern times was the decision in *Kennon & Spry* (2008) 238 CLR 366, where a husband who was not a trustee, beneficiary or appointor of a trust was essentially deemed to have all the assets of the trust to in fact be his property (and therefore subject to orders transferring the wealth to the former wife).

While this decision has received significant attention, hindsight has shown that it in many respects is an outlier primarily due to the particularly unique factual matrix (including that the husband had taken a series of steps after the relationship with his wife had broken down designed solely to reduce her entitlements).

In many more common situations therefore assets of properly structured and operated discretionary trusts will at most be considered a resource of a relationship. This means that while the assets will be taken into account when dividing the property of the relationship (such that the party who is not involved with the trust may be entitled to a larger percentage of the relationship property) the assets of the trust will remain in the protected environment and not be able to be attacked.

Initial decision on Caldwell

The decision in *Caldwell & Caldwell* [2025] FedCFamC1F 506 provides a stark reminder of the key principles in this area.

In this case, following the breakdown of a 30 year marriage (with 3 adult children) the wife was wanting access to trust assets that housed intergenerational wealth of the husband that could be traced back to his great grandfather.

Each of the trusts in question had similar features including:

- A. the husband was a shareholder of the trustee company, with a sibling;
- B. the husband was an appointor, jointly with a sibling (however the husband had unilateral rights to remove his sibling);
- C. the husband was a potential beneficiary;
- D. while the wife had been a beneficiary, around 3 years before the relationship broke down she had been removed via a variation that ensured she became one of the 'excluded beneficiaries' being someone who was not a direct lineal descendant of the husband's father - this exclusion extended to any company whose directors and shareholders were not direct lineal descendants of the husband's father, and any trust whose beneficiaries were not all direct lineal descendants.

In the initial decision the court rejected all of the claims of the wife concerning the trusts, and the court comprehensively set out the key factors protecting the assets of the trusts as follows:

1. unlike in *Kennon v Spry*, the family had conducted a business over four generations, and while recent growth had been significant, this was largely due to the husband's father;
2. the origin of the trusts' assets did not reflect contributions made by the husband or the wife;
3. the husband was well remunerated throughout his working life in the family business and he and the wife amassed significant assets outside the trusts;
4. there was no long history of the husband exercising control over the trusts, indeed the husband had not received any distributions from the trusts either during the marriage or since separation;
5. If the husband, as sought by the wife, were to cause a distribution to be made from the trusts to himself to satisfy, in cash, a division of the net value of the assets of the trusts, it would have been in direct conflict with the unambiguous provisions in the trust deeds prohibiting a benefit whether direct or indirect to anyone other than the direct lineal descendants of the husband's father;
6. until his death, the husband's father was the appointor of each trust and held the only voting class shares in each of the trustee companies and there was no suggestion that he was acting as the puppet or alter ego of the husband;
7. the purpose of the trusts were clear, including due to the wishes of the husband's father as expressed in the second codicil to his will (see extract at the end of this article) which emphasised the intention to keep the business operating and to maintain the benefits emanating therefrom within the direct family. Such a recent restatement of intention (although in a codicil) must, in the court's view, have a direct impact upon the exercise by the trustees of their powers as it confirmed the narrow purpose of the trusts to only benefit direct lineal descendants;
8. while it was accepted that the husband had very wide powers, and in that sense could be said to control the trusts, his primary duties were to act in good faith and in accordance with the purposes of the trusts and to give real and genuine consideration to the interests of all potential beneficiaries (see *Owies v JJE Nominees Pty Ltd* [2022] VSCA 142). If the husband exercised his powers for the purpose of benefiting the wife whether directly or indirectly, even if not the dominant purpose, he would have been in breach of the proper purpose rule (see *Whitehouse v Carlton Hotel Pty Ltd* (1987) 162 CLR 285). It would also cause a diminishing of the trusts' assets and while no potential beneficiary had a legal or equitable interest in the trusts' assets, they each have a right to due consideration as an object of benefaction and a right to due administration of the trusts, and to enforce those rights.

Kennon unbundled

Helpfully, the court also provided a full summary the key facts reinforcing the above points, given earlier family law cases (including *Kennon v Spry*, *Harris & Dewell and Anor* [2018] FamCAFC 94 and *Harris & Harris* [1991] FamCA 124) as follows:

- (a) The trusts were established at the instigation of the husband's father, and he controlled the trusts until his death in 2022, which included the period during which key variations to the trusts were made;
- (b) There was no evidence that the husband's father was in any way acting as the puppet or alter ego of the husband;
- (c) The trusts were not a sham or the alter ego of the husband;
- (d) The husband did not assume a position of any real power within the trusts until after his father's death in 2022;
- (e) It was not suggested by the wife that the husband exercised, had taken steps to exercise, or had exercised in the past any control of the trusts (other than to the limited extent of his involvement in the variations to the trust deeds to include the clause granting him power to remove his brothers);

- (f) There was no evidence of the husband's intention to control the trusts and indeed there was a side agreement which indicated an intention to vary the trust deeds so as to delete the power of the husband to remove his brothers after the conclusion of the proceedings;
- (g) On a proper construction of the trust deeds as varied, and having regard to the second codicil of the husband's father, the purpose of the trusts was to facilitate the intergenerational management of the families' business, which had been in operation since [the early 1900s], for the benefit of future generations of the lineal descendants of the husband's father, and to preclude anyone who was not a direct lineal descendent from benefiting either directly or indirectly;
- (h) It was only in the pursuit of the purpose of the trusts that the powers residing in the husband could be validly exercised;
- (i) The wife was an excluded beneficiary within all trusts and not entitled to benefit from the trusts either directly or indirectly;
- (j) Neither the husband nor the wife (for the brief period that she was a potential beneficiary) had ever received distributions from the trusts;
- (k) The husband, his children, and other lineal descendants of the husband's father, all had equitable choses in action in relation to the trusts being a right to proper administration of the trusts and a right to be given due consideration as an object of benefaction of the trusts and to enforce those rights;
- (l) The assets of the trusts did not represent the labours or contributions of the husband and/or wife during their marriage but rather were built up by the family over four generations;
- (m) The husband was well remunerated for his efforts throughout his working life in the family business;
- (n) The husband and wife had accumulated significant wealth outside the trusts from which a just and equitable property settlement could be achieved;
- (o) The husband had not sought to divert assets that he and the wife had accumulated over their marriage;
- (p) If the husband were compelled by court order to seize control of the trusts and distribute capital to himself for the purposes of meeting a property settlement order in the wife's favour, such actions would be in direct conflict with the purpose of each trust to benefit only direct lineal descendants of the husband's father;
- (q) Even if the most appropriate analogy were that the trusts were a form of inheritance for the husband (and therefore potentially at risk of attack by the wife); to find that the trusts and/or assets of the trust were property of the husband for the purposes of claims would arguably disenfranchise the other potential beneficiaries, in particular, the husband's brothers who would be bound by such a finding;
- (r) It had been conceded by the husband that the trusts' assets were a financial resource for the purposes of the litigation with his former wife.

Appeal decision in Caldwell

On appeal however in *Caldwell & Caldwell* [2026] FedCFamC1A 81, while the minority judgment endorsed the initial decision, the majority rejected much of the reasoning.

The appeal court confirmed that here the assets of the trusts should be considered assets of the husband.

In doing so, the court did however note that:

A. a finding that the trusts and their assets are property of the husband did not necessarily mean the wife would in fact receive an adjustment from the trusts; that was a separate question to be determined at trial.

B. there can be occasions where assets derived from generational, family wealth will not attract the classification of property of the parties to the marriage; however the factual matrix here was not such a case.

The court also clarified the key misunderstandings in the initial decision as follows:

- (i) the argument that because the husband had control, but needed to take steps to exercise this control was irrelevant; he had effective control (even though he had not exercised this control) and this was sufficient to conclude the assets of the trusts were his property;
- (ii) so too, the fact that the trusts had been converted to lineal descendant (or 'bloodline') trusts (and excluded the wife as a potential beneficiary) was irrelevant in the context that the husband had the capacity to benefit himself;
- (iii) that is, the initial decision conflated the issue of assessment of the contributions of the parties with the question of whether the trusts were property. Issues such as the origin of the trust assets and restrictions imposed under the trust deeds were ones which are only relevant to the consideration of contributions of the parties, not to the threshold categorisation of the trusts themselves;
- (iv) the husband's power to change the trustee was not a fiduciary one (which would have effectively curtailed the scope of the power and reduced the prospect of the trust assets being held to be the husband's property); primarily because the terms of each of the trust deeds permitted the husband to exercise those powers for his own benefit.
- (v) ultimately the husband had the requisite control to make the assets of the trusts property of the husband, being 'control over a person or entity who, by reason of the powers contained in the trust deed can obtain, or effect the obtaining of, a beneficial interest in the property of the trust' (see Harris & Dewell (2018) FLC 93-839).

It should be noted, pending any further appeal, that the minority judge agreed with the trial judge and wrote what can arguably be described as a very strong judgement. In concluding that the trusts were not the property of the husband, essentially for the reasons set out earlier in this article, clarity was also provided about how to determine the intention of the 'settlor' of a trust.

Specifically, in the context of modern discretionary trusts (see *Baba v Sheehan* [2021] NSWCA 58), it is not the person who is technically the settlor whose intentions are relevant, but the person who caused the trust to be established, the founder or instigator, who will usually be someone other than a nominal settlor, and may be the initial appointor and in control of the trustee or the initial trustee (see *In Application of Walker Corporation Pty Ltd* [2022] NSWSC 1609).

Codicil extract:

I have discussed with my family at various times over the years the origins of the [Caldwell] business and the intention of my father and me that the [Caldwell] Business remains within the [Caldwell] family. The overall purpose and intent is that the [Caldwell] Business upon my demise should go to and be under the control of [the husband, his 2 brothers] or the survivors of them acting jointly. [The husband, and his brothers] are and have been working in and directing the business and I consider that all three of them should have the privilege and opportunity to take the [Caldwell] Business into the future.