Perpetuity Legal.

Duty and taxation issues in deceased estates

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Acknowledgement of traditional owners and country

This session is being held on the lands of the Wurundjeri people of the Kulin Nation and on behalf of LPLC I wish to acknowledge them as the traditional owners of the land.

I also acknowledge the traditional owners of the lands which all of those joining us online today are living, learning and working on.

I would also like to pay my respects to their Elders past and present, and any Elders of other communities who may be present today.

Disclaimer

The information contained in this presentation is general information only and is not intended as legal advice.

If you or your clients require information other than that of a general nature in relation to the matters which we will discuss in our presentation today, legal advice relevant to the particular circumstances must be obtained.

Agenda

Key taxation and duty concerns that arise in estate administration and practical tips to help manage the risks.

The webinar will cover:

- Taxation when dealing with non-resident executor
- Distributions to non-resident beneficiaries
- Capital Gains Tax and main residence exemption
- SMSF and distribution of death benefits
- Effect of family provision claims on Stamp Duty
- Land Tax and Vacant Residential Land Tax

Non-resident Executors

- The taxation status of an estate changes if the executor is a ‘non-resident’
  - Even if deceased and all assets are Australian
- When is an estate deemed to be a non-resident estate?
  - For Australian taxation purposes:
    - an LPR is treated as a trustee and the estate they are administering is treated as a trust estate – see definition of ‘trustee’ in s6(1) ITAA 1936
    - a trust estate is taken to be a resident trust estate in relation to a year of income if a trustee the trust estate was a resident or the central management and control of the trust estate was in Australia at any time during that year of income – s95(2) ITAA 1936
    - ‘resident’ is defined ’ in s6(1) ITAA 1936 and includes the ‘ordinary concepts test’ ‘the domicile test’ and the ‘183-day test’
  - The estate will be treated as a non-resident trust estate for tax purposes if the grant of administration is made solely to an executor or administrator who is not an Australian resident for tax purposes.

Non-resident Executors | Tax and Duty

Income Tax

- An estate with a non-resident executor will not have access to the tax-free threshold available to resident estates (currently $18,200 per annum for three years after death).
- Estate may incur higher non-resident rate on any income earned from Australian assets after death – see Part II Schedule 1 Income Tax Rates Act 1986

Capital Gains Tax

- Foreign resident capital gains withholding (FRCGW) - CGT clearance certificate may not be available and will result in the purchaser withholding 15% sale proceeds (for contracts signed after 1 January 2025 and for contracts signed before that date different rate applies)
- Estate may not be entitled to the 50% capital gains tax discount on the sale of 'Taxable Australian Property' if it is not assessed by the Commissioner under s99 ITAA 1936. Important to note that s99 ITAA 1936 is at the Commissioner's discretion.

Non-resident Executors

Some other practical hurdles

- Funeral arrangements
- Grant application
- Payments of expenses and liabilities
- Collection, sale and distribution of estate assets

Non-resident Executors

Case study

Jane was an Australian resident and died leaving two children Sam and Paul. The estate is comprised of RAD of $750,000 and a share portfolio made up of CBA, Telstra and BHP shares worth about $2 million with a combined cost base of approximately $500,000.

Sam lives in US with her husband and has resided in US since 2005. Paul is lives in Country Victoria. Sam is nominated as the sole executor of Jane's Will as she was very close to her mum and the estate is distributed equally between Sam and Paul. Sam and Paul wish to sell the shares and divide all the cash between themselves.

Sam contacted Rob, a legal practitioner in Victoria, who drafted Jane's Will. Rob assured Sam that as the grant applications and other documents can now be signed electronically, he can prepare a grant application on her behalf.

Non-resident Executors

With tax and duty consequences associated with a non resident executor, consider:

- Appointment of resident executor(s)
- Appropriate advice to testator when making the will

If the will lists a non-resident person as an executor?

- If there is another resident executor nominated, application with leave reserved
- If there is a substitute executor nominated, consider renunciation
- If the beneficiaries are sui juris and able to take on the responsibility, consider renunciation and then apply for letters of administration with the will annexed
- Raise the issues, confirm in writing and keep records.

Distributions to non-resident beneficiaries
(from Resident estate & Resident deceased)

A non resident beneficiary can trigger additional taxation issues and liability for the estate.

- The LPR is responsible for the payment of tax when the foreign resident beneficiary is made presently entitled to income of a tax resident estate
- Consider CGT event K3 – s 104.215 ITAA 1997 where a non-taxable Australian property owned by a resident deceased passes to a foreign resident beneficiary

Example

In specie distribution of shares listed on the ASX to a foreign resident beneficiary may trigger a capital gains tax liability payable by the estate (not the beneficiary)

Distributions to non-resident beneficiaries
(from Resident estate & Resident deceased)

Case study

Using the same case study with the following changes.

- Paul is the executor and decides to split the RAD payment and transfer the share portfolio equally between Sam and himself.
- Assume the shares were purchased by Jane between 1990 and 2005.
- What if the Will gifted the RAD payment to Paul and the shares to Sam?

Distributions to non-resident beneficiaries
(Resident estate & Resident deceased)

Issues

- Identify different tax consequences
- Administrative work and associated costs

Options

- Give appropriate advice to executors or refer them for specific advice
- Appropriate advice to testators regarding specific gifts to foreign residents
- Retain records of the advice provided
- Use of testamentary discretionary trusts - doesn’t void the tax but may increase the options to manage taxation issues

CGT and the main residence exemption

In general terms, a deceased main residence will not attract capital gains tax if it meets certain requirements. Legislation - s 118-195 ITAA 1997.

Important criteria is:

- it was acquired by the deceased on/ after 20 September 1985 (so CGT applies)
- it was the deceased's main residence immediately before death and not being used to produce income - note partial exemptions may apply in some situations
- the disposal of the main residence occurs within 2 years of the death of the deceased (this requires sale and settlement).

CGT and the main residence exemption

Some variations that apply to retain the main residence exemption.

Disposal after 2 years but from death until disposal it was occupied by;

- the spouse of the deceased immediately before death (except where the spouse was living permanently separately from the deceased)
- a person having a right of occupancy pursuant to the will
- an individual to whom the ownership interest passed as a beneficiary of the deceased and the CGT event was brought about by that individual.

CGT and the main residence exemption

- PCG 2019/5 -The Commissioner has ‘safe harbour’ rules that give an additional period up to 18 months after the expiry of the 2-year sale period for settlement of the property
- You can apply to the commissioner to extend the 2-year period for disposal
- The Commissioner notes that the circumstances that caused the delay beyond the two-year period are more important than the length of the delay, and that the amount of any potential capital gain or loss is not relevant as to whether the discretion is exercised or not.

CGT and the main residence exemption

Cost base rules – generally

- Pre-CGT dwelling (i.e. was acquired by the deceased prior to 20 September 1985)
    - Market value on the date of death
- Post CGT dwelling (i.e. was acquired by the deceased after 20 September 1985)
    - Same costs base as the deceased

CGT and the main residence exemption

Pre-CGT dwelling owned with another person

- Need to check when the deceased originally acquired the property as a co-owner (joint proprietor or tenants in common)
- If the other owner died after 20 September 1985, the interest is deemed to have been acquired by the survivor as a post CGT interest - s128.50 ITTA 1997
- Death and transfer of a co owners interest in a main residence is important for the main residence exemption and or cost base calculation.

CGT and the main residence exemption

Further variations that apply to retain the main residence exemption.

The deceased was living in a nursing home when they died.

S 118.145 ITAA 1997 - Can continue to treat the dwelling as their home for:

- up to six years if the property is rented out to produce income, or
- indefinitely if it is not used to produce income.
- Note, they cannot treat any other property as their main residence for that period even if they are living in it.

CGT and the main residence exemption

Further variations that apply to retain the main residence exemption.

If deceased was a foreign resident

- Critical date 30 June 2020
- For a property sold after 30 June 2020, main residence exemption is not available to a foreign resident ***unless*** they have been a foreign resident for less than 6 years and satisfy the life events test.
    - This test is satisfied if the owner or a family member is diagnosed with a terminal illness, a family member dies, or the owner is involved in a marriage breakdown
- The above rules also apply to the LPR of such deceased.

CGT and the main residence exemption

Case study

Using the same case study with the following changes.

- Jane's estate also included a home in Moonee Ponds, which she inherited from her husband Tom after his death in 2001. Tom had purchased the home in 1984. Jane was moved to a care facility 5 years before her death. Paul as her attorney arranged for her house to be rented during that time.
- After her death, Paul as her executor, sold the house but settlement was finalised 3 years from the date of her death.

CGT and the main residence exemption

Key takeaways:

- Advise on the main residence exemption and timeframe
- Identify any acquisition from a co-owner (date and cost base)
- Ascertain the cost base of the property
- Document the reasons for any delay in the sale – check compliance with the safe harbour rules
- Seek taxation advice where appropriate

SMSF and distribution of death benefits

WHO	SIS DEPENDANT	TAX DEPENDANT	FORM & MANNER
Spouse / domestic partner	**YES**	**YES**	**Lump sum or pension**
Minor children	**YES**	**YES**	**Lump sum or pension**
Adult children – financial dependants	**YES**	**YES**	**Lump sum or pension*** (note limitations re pension 18 to 25)
Adult children –non financial dependants	**YES**	**NO**	**Lump sum**
Financial dependants and inter-dependants	**YES**	**YES**	**Lump sum or pension***
Estate	**YES (r 6.22 SISR)**	**Look through**	**Lump sum**

SMSF and distribution of death benefits

- In general terms an industry fund will calculate the tax to withhold before paying entitlements to a beneficiary
- If paying to an estate the industry fund usually pay the gross entitlement and lets the LPR calculate and pay the tax.
- Similar rules will apply if payment is made from SMSF

SMSF and distribution of death benefits

Who has the obligation to pay the tax?

Case study

Using the same case study with the following changes.

- Jane was the sole member of an SMSF. At the date of her death, she had a member balance of $900,000 with 70% taxable component and 30% tax free component. After her death, Paul as her LPR, was appointed as the director of the trustee of the fund.
- Paul resolved to distribute the death benefits to Jane’s estate.
- Assume both Sam and Paul are residents of Australia.
- What if Paul had instead resolved to pay the death benefits directly to Sam and himself as Jane’s surviving dependants?

Effect of family provision claims on Stamp Duty

In general, the transfer of an asset from a deceased estate to a beneficiary, made in accordance with the will, a will amended by the court, intestacy or pursuant to a court order is exempt from duty.

Duties Act 2000

- Section 42(1) - exempts from duty a transfer of dutiable property not made for valuable consideration by the legal personal representative of a deceased person to a beneficiary, where the transfer is made under and in conformity with the trusts contained in a will or arising on an intestacy, or the transfer relates to a property that is the subject of a trust for sale contained in the will of the deceased person.

Effect of family provision claims on Stamp Duty

Duties Act 2000

- Section 42(2) - exempts from duty the vesting of any dutiable property by virtue of section 13 of the Administration and Probate Act 1958 (i.e. property vesting in the LPR)
- Section 42(3) - exempts from duty a transfer of dutiable property not made for valuable consideration by a legal personal representative of a deceased person to a beneficiary to the extent that the transfer is made in satisfaction of the beneficiary's entitlement arising under the will of the deceased person or arising on an intestacy.
- Section 10(1) - 'dutiable property' to include an interest under a will or codicil of a deceased person disposing of property

Effect of family provision claims on Stamp Duty

Duty consequences

- Section 97(4) Administration and Probate Act 1958 - an order made by the Court under Part IV of the APA has effect as a variation to the deceased's will or the intestacy rules
- Where a transfer of dutiable property by the legal personal representative of a deceased person pursuant to a Court order made under Part IV of the Administration and Probate Act 1958 is in conformity with the order, the transfer will be exempt from duty under section 42 of the Duties Act

However, a deed of family arrangement or claims made under Part IV of the Administration and Probate Act 1958, without a court order, may trigger a payment of duty.

Effect of family provision claims on Stamp Duty

Key takeaways:

- Advise that a deed of family arrangement may have duty implications
- Calculate the Duty implications vs the costs of obtaining a court order
- Also note the risk of court order not being made as proposed by the parties
- Provide advice and keep records of such advice

Effect of family provision claims on Stamp Duty

Case study

Using the same case study with the following changes.

- Jane's estate comprised of her PPR valued at $1.3M and a share portfolio valued at $700,000. Assume both Sam and Paul are residents of Australia. Sam is appointed as executor and the Will provides for equal distribution between Sam and Paul.
- Paul makes a claim on the estate claiming his needs are much higher than Sam's and he was living with Jane for the last 10 years and wants to keep the house. Sam is well off and loves her brother and decides to let Paul have the house on the basis that she gets the share portfolio. To minimise costs, Rob, the estate's solicitor drafts a deed of family arrangement confirming the agreement between the parties. Following the signing of the deed, the parties submit consent orders with the Court dismissing the proceedings issued by Paul.

Land Tax and Vacant Residential Land Tax

Generally, surcharge land tax rates apply to land held by trustees of trusts

The surcharge rate does not apply to an estate during the period it is an administration trust, being the period from the date of death until the end of concessionary period which is the earlier of the:

- third anniversary of the date of death of the deceased, or further period approved by the Commissioner, or
- date of completion of administration of the deceased estate.

Land Tax and Vacant Residential Land Tax

State Revenue Office considers the administration of an estate completed when any of the following occurs:

- Completing of administration duties except for distribution to beneficiaries
- Interim distributions made and LPR has indicated that the estate has sufficient funds to discharge all debts and cover all expenses.
- When LPR first assents to the transfer of an estate land to a beneficiary of trustee of a trust
- Completion of the final accounts of the estate.
- LPR commences holding land as trustee for a testamentary trust.
- Estate land is transferred to the person entitled to it under the will or intestacy.

Land Tax and Vacant Residential Land Tax

Note: A legal personal representative must notify SRO at the commencement and completion of administration of a deceased estate

- Within one month of appointment and one month of completing of administration – s46K Land Tax Act 2005(Vic)
- SRO states that there may be penalties for failure to comply with this requirement

Land Tax and Vacant Residential Land Tax

Land tax and the deceased’s Principal Place of Residence (PPR)

The PPR land tax exemption can apply for a concessionary period being the earlier of;

- the third anniversary of the person’s death or
- the day on which the deceased’s interest in the land vests in the trustee of the testamentary trust or
- the land vests to the beneficiary.

Note: The SRO may extend the concessionary period if a request with appropriate supporting evidence is made.

Land Tax and Vacant Residential Land Tax (VRLT)

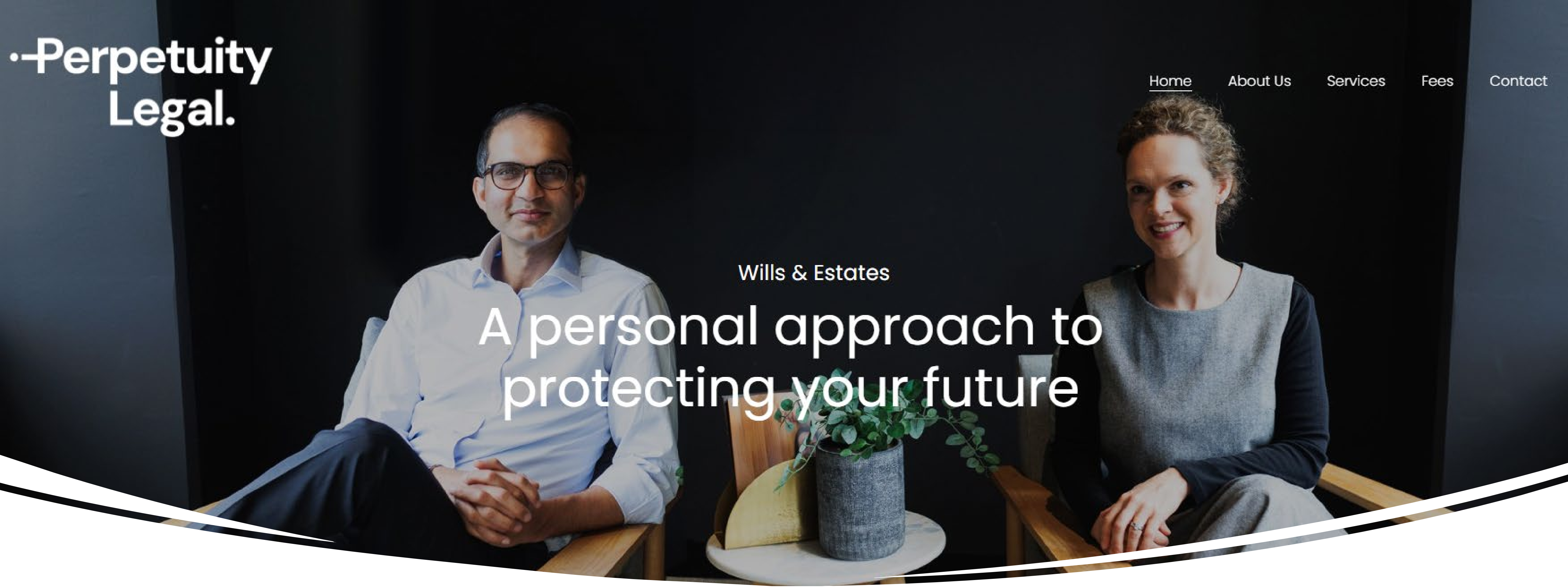
For deceased's estates:

- If the property is exempt from land tax, it will be exempt from VRLT
- The PPR concession period (criteria in previous slide) also applies to VRLT
- For any other property of the estate, they would be subject to the tax regime (just as it would have in the hands of the owner)

Key takeaways

- Tax and duty considerations are critical when advising testators and executors/administrators
- The rules are complex and nuanced- always check the details
- Always confirm the residency of the testator and beneficiaries
- Keep detailed records of advice provided and confirm scope of advice when dealing with tax issues
- Engage tax advisers for more detailed advice when appropriate

Any questions?



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