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## Income tax – liability of a legal personal representative of a deceased person

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### Relying on this draft Guideline

This Practical Compliance Guideline is a draft for consultation purposes only. When the final Guideline issues, it will have the following preamble:

*This Practical Compliance Guideline sets out a practical administration approach to assist taxpayers in complying with relevant tax laws. If you decide to use this Guideline and follow it in good faith, then the Commissioner will administer the law in accordance with this approach.*

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### **What this draft Guideline is about**

1. This draft Guideline is intended to provide the legal personal representative (LPR) of a deceased person with certainty about the extent of the deceased's outstanding tax liabilities for the period up to the time of their death.
2. Once an income tax return is lodged, the Commissioner generally has two or four years, depending on the circumstances, from the day on which he gives notice of an assessment to amend. Feedback from practitioners indicates that distributions of estate assets have been delayed until after the review period in case a claim is made by the Australian Taxation Office (ATO).
3. While an LPR's liability to pay any outstanding tax-related liabilities of a deceased person is limited to the value of the deceased's assets that come into their hands, an LPR may have to meet those liabilities personally if they distribute the estate assets with notice of a claim or a potential claim by the ATO.
4. This draft Guideline provides LPR's greater certainty in that it outlines when an LPR will be treated as having notice of a claim or potential claim by the ATO.
5. This draft Guideline is intended for smaller and less complex estates to enable the LPR to wind up such an estate without concern that they may have to fund any of the deceased's liabilities from their own assets.
6. While this draft Guideline seeks to provide greater certainty, an LPR does not have to distribute assets in the timing as set out in this draft Guideline. However, the LPR may choose to do so, based on what level of assurance from the ATO that they consider they need for their particular circumstances.
7. This draft Guideline **does not** deal with any liabilities that the LPR may have in relation to the deceased estate, that is, for the period after death.

### **Who this draft Guideline applies to**

8. This draft Guideline applies to an executor (an LPR) who has obtained probate of the deceased's will, or an administrator (also an LPR) who has obtained letters of administration of the deceased's estate provided:
  - in the four years before their death
    - the deceased did not carry on a business
    - the deceased was not assessable on a share of the net income of a discretionary trust
  - the estate assets consist only of:
    - public company shares or other interests in widely held entities
    - death benefit superannuation
    - Australian real property
    - cash and personal assets such as cars and jewellery, and
  - the total market value of the estate assets at the date of death was less than \$5 million.

This draft Guideline does not apply if probate or letters of administration have not been obtained because in these cases an LPR cannot be made personally liable for the deceased's outstanding tax liabilities. However, a different collection mechanism applies under sections 260-145 and 260-150 of Schedule 1 to the *Taxation Administration Act 1953* (TAA).

### **Draft Guideline**

9. An LPR's liability to pay any outstanding tax-related liabilities of a deceased person<sup>1</sup> is limited to the value of the deceased's assets that come into their hands.<sup>2</sup> However, an LPR may have to meet those liabilities personally if they distribute the estate assets with notice of a claim or a potential claim by the ATO.<sup>3</sup>

10. It is a question of fact whether the LPR had notice of a claim from the ATO. This draft Guideline sets out the situations when we will treat an LPR as having such notice and those when we will not.

### **Notice of amounts owing at time of death**

11. Because an LPR stands in the shoes of the deceased person regarding the deceased's outstanding tax related liabilities,<sup>4</sup> the ATO considers that the LPR has notice of any amount that the deceased owed to the ATO at the date of their death (in addition to charges accruing in respect of those amounts following death, such as interest).

### **Notice of liabilities from outstanding assessments**

12. Similarly, the ATO considers that an LPR has notice of any liabilities arising from the assessment of income tax returns that the deceased person had lodged, but that had not been assessed at the time of the person's death.

### **Notice of liabilities arising in respect of outstanding returns**

13. An LPR is required by law to lodge all income tax returns that the deceased person has not lodged, including for the period up to the date of their death.<sup>5</sup> The ATO considers that an LPR has notice of any liability arising from assessments of these returns. The LPR should also notify the ATO if a particular outstanding return is not required to be lodged because, for example, the amount of the deceased person's taxable income was below the tax free threshold.

### **Notice of liabilities arising from amendments or other changes**

#### *Lodgments and advice of no lodgments necessary by an LPR*

14. The ATO will not treat an LPR as having notice of any further potential ATO claim relating to returns the LPR lodged (or advised were not necessary) if:

- the LPR acted reasonably in lodging all of the deceased person's outstanding returns (or advising the ATO that they were not necessary), and

<sup>1</sup> As defined in subsection 995-1(1) of the *Income Tax Assessment Act 1997* (ITAA).

<sup>2</sup> *Deputy Commissioner of Taxation v. Brown* (1958) 100 CLR 32. *Patterson v. FCT* [1936] 56 CLR 507 at 518-519.

<sup>3</sup> ATO liabilities for periods up to the date of death rate equally with other unsecured creditors of the estate. For example, if a tax liability relating to a notice of claim or potential claim could not have been satisfied at time of distribution because of lesser priority than secured claims, it would not be required to be satisfied if it arose later.

<sup>4</sup> Subsection 260-140(2) of Schedule 1 to the TAA.

<sup>5</sup> Subsection 260-140(3) of Schedule 1 to the TAA.

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- the ATO has not given the LPR notice that it intends to examine the deceased person's taxation affairs within 6 months from the lodgment (or advice of non-lodgment) of the last of the outstanding returns.

#### *Lodgments and advice of no lodgments necessary by the deceased*

15. The ATO will treat an LPR as having notice of a further potential ATO claim relating to returns the deceased lodged (or advised were not necessary) before their death where, within 6 months from the lodgment (or advice of non-lodgment) of the last of the deceased's outstanding returns, the ATO gives the LPR notice that it intends to examine the deceased person's taxation affairs.

16. The ATO will also treat an LPR as having notice of a further potential ATO claim where, in the course of administering the deceased estate (including the preparation and lodgment of outstanding tax returns), an LPR becomes aware (or should reasonably have become aware) of a material irregularity (or irregularities) in a prior year return. In such a case, the ATO will treat the LPR as having notice of a further ATO claim in relation to that irregularity or irregularities.

17. However, the ATO will not treat the LPR as having notice of a potential ATO claim if the LPR brings any irregularity promptly to the attention of the ATO in writing (for example, by requesting an amendment) and the ATO does not, within 6 months, issue an amended assessment or indicate that it intends to review the issue.

18. Where the ATO has decided to review or examine the affairs of a deceased estate, it will notify the LPR. Where any tax liability amount arises, such as omissions of rental income from estate assets, the ATO will promptly amend relevant returns.

#### *Example – straightforward small estate*

19. *Alfred died on 1 June, 2015. Bill was appointed executor of Alfred's will. He obtained probate of it in July 2015. Alfred's estate consists of his main residence, shares in publicly listed companies and money in a bank account. The collective value of the estate is less than \$1 million. Up until his death, Alfred had been receiving a pension. Alfred had advised the ATO in 2012 that he was not required to lodge further returns.*

20. *Based on all of the information available to him, Bill determines that no return is necessary for the period from 1 July 2014 to 1 June 2015. Bill lodged a Return Not Necessary (RNN) Advice with the ATO on 31 October 2015. If the ATO does not notify Bill that it intends to review Alfred's tax affairs by 30 April 2016 (6 months from the time Bill lodged his RNN advice), the ATO will treat Bill as not having notice of any claim relating to Alfred's estate. Bill can distribute the estate to beneficiaries without risk of personal liability.*

#### *Example – small estate – material tax irregularity identified by the LPR*

21. *Peter died on 12 December 2015. Jill was appointed executrix of his will. She obtained probate in January 2016.*

22. *In the course of discharging her duties as executrix, Jill confirmed with the ATO that Peter had lodged all of his income tax returns other than the returns for the 2015 year and the final period to Peter's date of death.*

23. *In preparing those returns, Jill discovered that Peter had never returned rental income from a property that he had owned in Sydney since 2010. Jill included rental income from that property in the returns for the 2015 income year (\$20,000) and the period to Peter's date of death (\$10,000). She lodged both returns on 3 March 2016. Jill did not seek to amend any of Peter's earlier year assessments.*

24. On 4 April 2016, the ATO issued notices of assessment relating to the returns that Jill had lodged. Jill paid those assessments out of the estate's assets.

25. On 1 July 2016, Jill published a Notice of Intended Distribution (under State succession laws) for claims to be made within 30 days. On 4 August 2016, Jill distributed the remaining assets of the estate.

26. On 20 October 2016, the ATO wrote to Jill advising that Peter's assessments for the 2013 and 2014 years were being reviewed because of the non-reporting of rental income.

27. Jill had become aware of a material irregularity for those income years because she had discovered that Peter had not included rental income in his returns. Jill will be personally liable for any outstanding tax liabilities resulting from the amendment of Peter's 2013 and 2014 income tax assessments. Jill cannot avoid liability on the basis that she had no notice of it.

28. If Jill had brought the prior year irregularities to the ATO's attention when she lodged the outstanding returns Jill would not be personally liable because the ATO did not advise her within 6 months that it was intending to review the assessments.

### **Notice of liabilities where further assets discovered**

29. If further assets come into the hands of an LPR after what was thought to be the completion of the estate's administration, the LPR must reconsider the deceased's tax position. The identification of further assets might suggest that the deceased's taxable income was understated previously. The ATO will treat the LPR as having notice of a potential claim by the ATO to the extent of those further assets.

### **Example – further assets identified**

30. Vincent died on 26 November 2015. Ben was appointed executor of Vincent's will and obtained probate. To the best of Ben's knowledge, the assets included in Vincent's estate consist of his main residence, a number of rental properties that Vincent acquired using his superannuation lump sum, and some money in a bank account. Based on all of the information available to him including tax returns for earlier years, Ben determined that no return was necessary for the period from 1 July 2014 to 26 November 2015 because Vincent's income was below the tax free threshold. Six months after advising the ATO that no return was necessary, Ben proceeded to distribute the estate's assets.

31. In 2019, the ATO receives information that Vincent owned further assets, the income from which was not disclosed by Vincent or Ben (due to Ben not knowing of their existence).

32. The ATO issues amended assessments for the 2016 and four preceding income years. The ATO is not bound by this draft Guideline to refrain from issuing an assessment/amended assessment to reflect the income from the further assets. The ATO will seek to recover tax related liabilities from Ben up to the value of the further assets that come into Ben's hands as LPR.

### **Date of effect**

33. When finalised, this draft Guideline will apply from the date it is issued. It will be reviewed from time to time under the ATO's standard review process to ensure the currency and relevance of the content, and that the content remains aligned with Australian taxation requirements and industry practice.

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## Background and additional Information

### ***Deceased estates and legal personal representatives***

34. Succession law in Australia is State/Territory based. While the laws of each State/Territory operate in a broadly similar manner, there are differences. For example, in most States assets that a deceased person owned and which form part of their estate vest in their LPR once a grant of probate or letters of administration is obtained. In Queensland, those assets vest automatically in the deceased's executor if they died leaving a will.

35. An LPR is responsible for collecting the assets of the deceased person, paying their debts and funeral and testamentary expenses and distributing the remainder to the beneficiaries. An LPR will always remain such, so that if further assets of the deceased are identified after the estate was thought to have been fully administered, the LPR's duties continue in respect of those assets.

36. Not all assets that a person owned when they died will form part of their deceased estate. Most significantly, assets which they owned as a joint tenant will pass by survivorship to the surviving joint tenant(s) and superannuation benefits may be paid directly to a dependant. [These assets are not available to satisfy the debts of the deceased including outstanding tax liabilities.]

37. As to whether tax in respect of which an assessment was not made at the time of death is a debt of the estate, the Court in *Deputy Federal Commissioner of Taxation v. Brown*, observed that:

...for the purposes of Acts imposing death and probate duties, income tax upon a person's income, though not assessed until after his death has been held to answer the description of a debt due by the deceased *Commissioner of Stamps (WA) v. West Australian Trustee Executor and Agency* (1925) 36 CLR 98.<sup>6</sup>

38. Relevant Acts of the various States/Territories<sup>7</sup> ensure that an LPR who has satisfied certain advertising requirements is protected from claims of which they did not have notice at the time they distribute the assets of the estate.<sup>8</sup>

39. If the estate debts (including the funeral and testamentary expenses) exceed the value of the assets, then the estate is insolvent. An insolvent deceased estate may be administered in bankruptcy (under the Bankruptcy legislation or provisions in State/Territory Acts dealing with insolvent estates).

### ***Tax liabilities***

40. In considering an LPR's exposure to tax related liabilities, three distinct situations must be considered:

- liabilities relating to the period up to death and where probate/letters of administration is obtained – addressed by this draft Guideline
- liabilities relating to the period up to death and where no probate/letters of administration obtained – not addressed by this draft Guideline, and

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<sup>6</sup> Similarly, in *Taylor v. Deputy Federal Commissioner of Taxation* [1969] HCA 25, the High Court proceeded on the assumption that the making of an assessment was not a condition precedent to a claim arising from the Commissioner.

<sup>7</sup> For example, section 67 of the *Trusts Act 1973 (Qld)*; section 33 of the *Trustee Act 1958 (Vic)*; section 92 of the *Probate and Administration Act 1898 (NSW)* section 60 of the *Trustee Act 1925 (NSW)*; section 25A of the *Trustee Act 1898 (Tas)*; section 63 of the *Trustees Act 1962 (WA)*; section 29 of the *Trustee Act 1936 (SA)*.

<sup>8</sup> It is not the case that an LPR has notice only of the claims made in response to an advertisement. For example, if an LPR has notice of a claim prior to advertising that notice persists even if the creditor does not respond to the advertisement. If the LPR has no notice of a particular claim and the creditor does not respond to the advertisement, the LPR is not bound to satisfy it.

- liabilities relating to administration of the deceased estate (the period after death) – not addressed by this draft Guideline.

#### *Probate/Letters of Administration obtained*

41. Where probate/letters of administration has been obtained, section 260-140 of Schedule 1 to the TAA provides that an LPR stands in the shoes of the deceased for tax purposes. The LPR is required to provide returns and other information that the deceased was required to provide and must discharge any outstanding tax related liability. If the LPR fails to lodge a return or provide relevant information, the ATO can assess the amount of the deceased person's liability.<sup>9</sup>

42. A liability which a trustee has in respect of the period prior to the death of the deceased individual is a representative liability, such that the ATO cannot collect from the trustee more than the value of the deceased's assets that form part of the estate. The Court in *Barkworth Olives Management Limited v. DFC of T* 2010 ATC 20-172 explained the policy:

In summary, *Brown, Stapleton and Patterson* concerned taxing provisions which imposed a liability to tax upon a person who was appointed as a representative after the relevant income had been derived and who therefore had no opportunity during the period when that income was derived to make provision for any tax liability.<sup>10</sup>

#### *No probate*

43. Where probate/letters of administration are not obtained within 6 months of death, the Commissioner can determine the total amount of tax liabilities owed by the deceased person (including those for which no assessment has yet been made) under section 260-145 of Schedule 1 to the TAA.<sup>11</sup>

44. An LPR is not made liable in respect of a determination made under section 260-145 of Schedule 1 to the TAA, although property in their hands may be recovered to satisfy it.

45. Section 260-150 of Schedule 1 to the TAA empowers the Commissioner to authorise a person to seize and dispose of a deceased person's property in order to recover the deceased's outstanding tax-related liabilities determined under section 260-145 of Schedule 1 to the TAA, together with any reasonable costs incurred by the authorised person in so doing. For this purpose, the Commissioner may authorise a member or a special member of the Australian Federal Police or a member of a State or Territory police force, or any other person.

#### *Deceased estate*

46. A liability that an LPR has as trustee of a deceased estate under Division 6 of Part III of the *Income Tax Assessment Act 1936* (ITAA 1936) while it is being administered is a personal liability although the LPR has a right to be indemnified out of the estate's assets. The Court in *Barkworth Olives* observed:

.... there is no similar rationale for construing s 254(1)(e) as qualifying the ordinary operation of s 204 in its application to those sections in Div 6 of Pt III which expressly contemplate that a trustee will be made personally liable for tax as an exception to the general liability of beneficiaries.

<sup>9</sup> Subsection 260-140(4) of Schedule 1 to the TAA.

<sup>10</sup> At paragraph 40.

<sup>11</sup> *Bennett v. Commissioner of Taxation* [2015] AATA 455 and *Binetter v. FCT* [2016] FCAFC 163.

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41. For these reasons I construe s 254(1)(e) as having no potential application to limit a trustee's personal liability where the trustee is assessed to tax under a provision in Div 6 of Pt III, such as s 99A, which expressly provides for the liability of the trustee; that is so at least where the same person remains trustee during the whole of the period in which the relevant taxable income is derived and up to and including the date upon which the liability for tax accrues under s 204.

### **Collection of outstanding tax liabilities of deceased**

47. In the absence of fraud or evasion, the Commissioner cannot seek to recover estate assets that have been distributed to beneficiaries in order to satisfy outstanding tax liabilities of a deceased person. In *Deputy Commissioner of Taxation v. Brown* (1958) 100 CLR 32 the Commissioner raised assessments against the executors of the deceased person after the estate had been fully administered and sought to recover the amounts owing from them as an equitable debt from a beneficiary. The High Court, by majority, held that having regard to the structure of the Act, the beneficiaries were not liable. In particular, the Court held that the liability of any person to pay a debt for unpaid income tax is conditional upon the right of the Commissioner to assess that person and upon the correlative right of that person to appeal against the assessment (which right the beneficiaries did not possess).

48. The scope of an LPR's liability was considered in *Deputy Commissioner of Taxation (NSW) v. Taylor* (1968) 15 ATD 118 and on appeal in *Taylor v. Deputy Federal Commissioner of Taxation* (1969) 123 CLR 206. The relevant facts were as follows:

- **6 December 1954** – The testator died. At the time of his death the testator owned two properties; Beaumah and Kelly.
- **April 1955** – The deceased's LPR made the usual advertisements indicating that they were intending to distribute assets.
- **1955** – The LPR was paid an amount by a friend of the deceased. The LPR thought that the amount was the repayment of a gambling debt. In fact, the amount was attributable to a share trading profit which had not been returned by the deceased or the LPR. The Commissioner argued that the LPR should have been on notice of a possible claim for additional tax.
- **January 1958** – The devisee of 'Kellys' sought to have the transmission to her registered. Procedural irregularities meant the transmission was not registered when amended assessments were issued to the LPR.
- **March 1958** – The transmission of 'Beumah' was registered.
- **13 March 1959** – The LPR received a letter from the Commissioner indicating that returns were being reviewed and drawing the LPR's attention to section 216.
- **24 March 1961** – Amended assessments were made.

49. Amongst other pleas, the LPRs pleaded in defence they were not liable because they had advertised pursuant to section 92 of the *Probate and Administration Act 1898 (NSW)* and had no notice of any claim by the Commissioner.

50. The Supreme Court held that for an LPR to escape liability under section 216 of the ITAA 1936 the onus is on the executor to show that the distribution was made without notice of any claim by the Commissioner.

51. The Supreme Court found that the executors had effectively divested themselves of Beaumah (but not Kellys) without notice of a claim, contingent or otherwise, by the Commissioner. The High Court found that the plea under section 92 provided a good defence to the claim and that as the LPRs had done everything necessary to transfer

ownership of Kellys without notice of any claim by the Commissioner, it also was not available to satisfy the claim.

### **Insolvent estates**

52. Whether or not probate has been granted (or letters of administration have been obtained), the Commissioner may recover outstanding tax-related liabilities of a deceased person under Part XI of the *Bankruptcy Act 1966 (Cth)* (Bankruptcy Act).

53. Under section 244 of the Bankruptcy Act, the Commissioner may petition the Court for an order to have the deceased estate administered in bankruptcy if the outstanding tax-related liability or aggregated debts owed to two or more creditors is not less than \$5000. Where the Commissioner makes such a petition, the petition will be served on the LPR of the deceased estate. The LPR of the deceased estate may petition the Court to have the deceased estate administered in bankruptcy under section 247 of the Bankruptcy Act.

54. A petition under Part XI of the Bankruptcy Act does not require an act of bankruptcy, as is required under section 44 of the Bankruptcy Act. Although a determination by the Court is needed to make an administration order, a Court judgment is not required. However, the order is discretionary, and insolvency is clearly a matter which should generally be taken into account in exercising this discretion.

55. Part XI of the Bankruptcy Act provides for the property of the deceased to be vested in the Official Trustee in Bankruptcy and for the deceased estate of an insolvent debtor to be administered in a similar manner to the way bankruptcy would operate if the person were still alive. The bankruptcy procedure offers potential clawing back of assets and greater accessibility to the Court for directions as to the realisation of assets.

56. If a debtor dies before the presentation of a bankruptcy petition in the normal course of events, the petition will lapse and fresh proceedings must be undertaken under Part XI of the Bankruptcy Act. Where a debtor dies after the presentation of the petition but before a sequestration order has been made (or the petition is dismissed), an order may be made by the Court for the administration of the deceased estate. In circumstances where the debtor is made bankrupt before their death, the bankruptcy will continue after the debtor's death as if the debtor were still alive, unless the Court directs otherwise.<sup>12</sup>

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## **Commissioner of Taxation**

5 July 2017

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<sup>12</sup> Insolvent estates may be administered under State/Territory legislation relating to the administration of estates, in which case it will be conducted by the LPR, not the trustee in bankruptcy. The main difference between the two forms of administration is the potential availability of property disposed of *inter vivos* under the Federal provisions.

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## **Your comments**

57. You are invited to comment on this draft Practical Compliance Guideline including the proposed date of effect. Please forward your comments to the contact officer by the due date.

**Due date:** 2 August 2017  
**Contact officer:** Kevin Westbrook  
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## **References**

ATOlaw topic(s)	Income tax ~~ Trusts ~~ Other
Legislative references	ITAA 1997 ITAA 1997 995-1(1) TAA 1953 TAA 1953 260-140 TAA 1953 260-140(2) TAA 1953 260-140(3) TAA 1953 260-140(4) TAA 1953 260-145 TAA 1953 260-150 ITAA 1936 ITAA 1936 Div 6 Pt III Bankruptcy Act 1966 (Cth) Probate and Administration Act 1898 (NSW)