

TD 2019/14 - Income tax: will a trust split arrangement of the type described in this Determination cause a new trust to be settled over some but not all assets of the original trust with the result that CGT event E1 in subsection 104-55(1) of the Income Tax Assessment Act 1997 happens?

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Taxation Determination

Income tax: will a trust split arrangement of the type described in this Determination cause a new trust to be settled over some but not all assets of the original trust with the result that CGT event E1 in subsection 104-55(1) of the *Income Tax Assessment Act 1997* happens?

❶ Relying on this Ruling

This publication (excluding appendix) is a public ruling for the purposes of the *Taxation Administration Act 1953*.

If this Ruling applies to you, and you correctly rely on it, we will apply the law to you in the way set out in this Ruling. That is, you will not pay any more tax or penalties or interest in respect of the matters covered by this Ruling.

Further, if we think that this Ruling disadvantages you, we may apply the law in a way that is more favourable to you.

Arrangements this Determination covers

1. There are many forms of arrangement that can be described as a trust split. For the purposes of this Determination, 'trust split' refers to an arrangement where the parties to an existing trust functionally split the operation of the trust so that some trust assets are controlled by and held for the benefit of a subset of beneficiaries, and other trust assets are controlled and held for the benefit of others.¹ A trust split usually involves a discretionary trust that is part of a family group. A common reason given for 'splitting' the trust is to allow different parts of the family group to have autonomous control of their own part of the assets held on trust (that is, their own part of the trust fund).

2. A trust split in this sense will exhibit all or most of the following features:

- The trustee of an existing trust is removed as trustee of part/some of the trust assets and a new trustee is appointed to hold those assets.
- Control of the original trustee is changed such that control passes to a subset of the beneficiaries of the original trust. The new trustee is controlled by a different subset of beneficiaries.
- A different appointor is appointed in respect of the part of the fund held by the new trustee, the control of the new appointor aligned with the control of the new trustee.

¹ This is one sense in which the term 'trust split' is commonly used.

- The rights of indemnity of the trustees are segregated such that each trustee can only be indemnified out of the assets held by that trustee.
 - The expectation is that the new trustee will exercise its powers in respect of the assets it holds independently of the original trustee to benefit one subset of beneficiaries to the exclusion of others. The original trustee is also expected to exercise its powers in respect of the assets held by it independently of the new trustee to benefit instead a different subset again to the exclusion of others. This is so whether the range of beneficiaries that can benefit from particular assets is expressly limited.
 - The rights, obligations and powers of the trustees and beneficiaries remain governed by the one deed.
 - The original trustee and new trustee keep separate books of account.
 - The new trustee may also seek to apply for a new tax file number and/or Australian business number, and commence to lodge a separate return in respect of the income derived from the assets it holds.
3. It is assumed in this Determination that the steps needed to implement the trust split arrangement are able to be achieved at law², including by valid amendment of the trust deed as necessary, without bringing the whole trust to an end for trust law purposes and thereby resettling the trust.

Ruling

4. Yes. A trust split as described in this Determination will result in the creation of a trust by declaration or settlement as the trustee has new personal obligations and new rights have been annexed to property. This will cause CGT event E1 in subsection 104-55(1) of the *Income Tax Assessment Act 1997* (ITAA 1997)³ to happen.

Example 1 – separating the control of some of the assets of an existing trust that results in creation of a new trust

5. *The Star Trust is a discretionary trust that was settled in 1980 to benefit John Smith and his family members being his spouse, children, grandchildren and their lineal descendants. John has two children from his first marriage – Ben and Holly Smith. He has two children with his second spouse, Jane Smith.*
6. *The trustee of the Star Trust is Star Trustee Pty Ltd (Star Trustee). The trust deed gives the trustee the absolute discretion to appoint income to any one or more of the beneficiaries.*
7. *The assets of Star Trust are 300 shares in Sun Pty Ltd.*
8. *John Smith passed away in 2010. Since his death, Star Trustee has been controlled by Jane and Ben. Jane and Ben are also the current appointors in respect of the whole trust.*

² Other legal considerations beyond tax that may impact on the decision to undertake a trust split might also include, for example, section 197 of the *Corporations Act 2001* which deals with liabilities of a director for debts incurred by the company while acting as trustee.

³ All legislative references in this Determination are to the ITAA 1997 unless otherwise indicated.

9. Since John's death, there has been conflict between the children from his first marriage, and Jane and her children.

10. To allow the two branches of John's family some level of autonomy and limit the amount of interaction required between them, Star Trustee varies the trust deed pursuant to a power of amendment, and deeds of appointment are executed to implement a trust split as follows:

- (a) A new company owned and controlled by Jane is created, Moon Trustee Pty Ltd (Moon Trustee).
- (b) Ownership and control of Star Trustee is changed such that control of this company is now held by Ben and Holly.
- (c) Star Trustee is removed as trustee of 100 shares and Moon Trustee is appointed as trustee of those shares in its place.
- (d) In accordance with the deeds executed, the remaining 200 shares held by Star Trustee are designated as the corpus of the Star Trust and the 100 shares to be transferred to Moon Trustee are referred to as the corpus of the Moon Trust.
- (e) Jane resigns as appointor in respect of the Star Trust and is appointed as appointor in respect of the Moon Trust.
- (f) Star Trustee's rights of indemnity are limited so that it can only look to the assets that remain in its control to satisfy its rights to be indemnified (200 shares in Sun Pty Ltd).
- (g) Moon Trustee's rights of indemnity are similarly limited to the assets that are in its control (100 shares in Sun Pty Ltd).
- (h) Legal ownership of 100 shares in Sun Pty Ltd is transferred from Star Trustee to Moon Trustee.
- (i) No changes are made to the range of beneficiaries in favour of whom either trustee can exercise its power of appointment. However, the expectation is that Moon Trustee will hold 100 of the Sun Pty Ltd shares for the benefit of Jane and her children to the exclusion of Ben and Holly, and conversely Star Trustee will hold the remaining 200 Sun Pty Ltd shares for the benefit of Ben and Holly to the exclusion of Jane and her children.

11. The arrangement puts in place a complete segregation of the obligations, powers and rights of the trustees attached to the different assets they respectively hold. Each trustee has a separately identifiable parcel of trust property to which their separate trust obligations (and rights, as trustee) attach, comprising separate trust funds. The separation of the trust estates is expected to be borne out by the exercise of the respective trustee's powers.

12. For these reasons, the trust split causes new rights and obligations to be created over the shares transferred to Moon Trustee. These new rights and obligations amount to the creation of a new trust over those shares. The new trust is created by settlement in respect of the transferred shares causing CGT event E1 to happen.

Example 2 – separating the control of some of the assets of an existing trust that does not result in creation of a new trust

13. The Kingdom Family Trust is a discretionary trust settled in 1970 for the benefit of Ian King and his family members – his wife Maria and his children Katarina and Laura. Ian King is the current appointor of the Kingdom Family Trust.

14. *The trustee of the Kingdom Family Trust is Emperor Pty Ltd (Emperor), a company jointly owned by Ian and Maria. Together with their daughters, Ian and Maria are also the directors of Emperor.*

15. *The Kingdom Family Trust is in the business of property development and the operation of retirement villages. Ian is 70 years old and wishes to reduce his involvement in the family's business activities.*

16. *Ian and Maria King decide that now is an appropriate time for greater responsibility for the administration of the Kingdom Family Trust to be placed on Laura who is currently taking increased responsibility for the property development business. To facilitate the desired succession planning goal, the trust deed is amended to:*

- (a) *allow for the appointment of additional trustees in respect of some of the assets of the trust fund*
- (b) *allow for separate appointors in respect of the different parts of the trust fund*
- (c) *provide that in making a determination about how to distribute the net income of the trust fund for a particular accounting period, each trustee of any separate part/s of the trust fund must take into account the losses incurred by the other parts of the trust fund and expenses of the trust as a whole*
- (d) *require all trustees to act together in respect of decisions which one trustee reasonably believes requires agreement of all trustees including but not limited to*
 - (i) *selection of an accountant for preparation of the trust tax return*
 - (ii) *incurring joint expenses*
 - (iii) *amending the trust deed*
 - (iv) *determining an earlier vesting date for the trust, and*
- (e) *give each trustee recourse to all of the trust assets where the assets held by that trustee are insufficient to fully satisfy its right to be indemnified.*

17. *A Deed of Appointment was subsequently executed appointing Rainbow Pty Ltd (Rainbow) as an additional trustee over all assets relating to the property development business of the Kingdom Family Trust. Laura and Ian King are the directors and shareholders of Rainbow. Emperor is removed as trustee over all assets relating to the property development business.*

18. *The identity of those who control Emperor remains unchanged.*

19. *Laura is appointed as appointor in respect of that part of the trust fund that Rainbow holds as trustee and Ian King resigns from that role. Ian King remains appointor in respect of the remainder of the trust fund (being the assets Emperor continues to hold).*

20. *Both parts of the trust fund continue to be governed by the terms of the original trust deed as amended.*

21. *The range of potential beneficiaries entitled to benefit from the trust as a whole does not change.*

22. *Each trustee keeps separate accounts in respect of the assets they hold, but the results are consolidated for the entire trust fund and a single tax return is prepared for the Kingdom Family Trust as a whole.*

23. *Considering all the elements of the arrangement, it cannot be concluded that the assets transferred to Rainbow have been subjected to new personal obligations and new rights annexed to that property. The Kingdom Family Trust continues as one trust, albeit with two trustees, each separate trustee assuming primary responsibility in respect of a specified portion of the trust fund. The preconditions to subsection 104-55(1) are not satisfied and implementation of the arrangement does not cause CGT event E1 to happen.*

24. *Example 2 is illustrative of a scenario that is not a 'trust split' as described in this Determination.*

Date of effect

25. Subject to paragraph 26, this Determination applies before and after its date of issue. However, this Determination will not apply to taxpayers to the extent that it conflicts with the terms of a settlement of a dispute agreed to before the date of issue of this Determination (see paragraphs 75 and 76 of Taxation Ruling TR 2006/10 *Public Rulings*).

26. It is recognised that the Commissioner's view of the potential CGT implications of the arrangement discussed in this Determination may have been subject to conjecture prior to the publication of TD 2018/D3⁴ on 11 July 2018. The Commissioner will not devote compliance resources to apply the views expressed in this Determination to arrangements entered into before this date. However, if the Commissioner is asked or required to state a view (for example, in a private ruling or in submissions in a litigation matter), the Commissioner will do so consistently with the views set out in this Determination.

Commissioner of Taxation

13 December 2019

⁴ Draft Taxation Determination TD 2018/D3 *Income tax: will a trust split arrangement of the type described in this Determination cause a new trust to be settled over some but not all assets of the original trust with the result that CGT event E1 in subsection 104-55(1) of the Income Tax Assessment Act 1997 happens?*

Appendix 1 – Explanation

❶ This Appendix is provided as information to help you understand how the Commissioner’s view has been reached. It does not form part of the binding public ruling.

27. CGT event E1 happens when a trust is created over a CGT asset by declaration or settlement.⁵ The CGT event happens at the point in time the trust is created.⁶

28. There is no case law dealing directly with the tax implications of an arrangement of the type described in this Determination as a ‘trust split’.

29. The phrase ‘you create a trust over a CGT asset’ is to be understood by reference to the general law of trusts.⁷ This directs attention to the fundamental nature of a ‘trust’ over an asset and what is involved in ‘creating’ such a trust.

30. A trust has been described as:

- (a) ‘An obligation enforceable in equity which rests on a person (the trustee) as the owner of some specific property (the trust property) to deal with that property for the benefit of a certain person (the beneficiary) or persons ...’.⁸
- (b) ‘A relation between the trustee and beneficiary in respect of certain property ... which arises when the owner of a legal or equitable interest in property is bound by an obligation recognised by and enforced in equity to hold that interest for the benefit of others’.⁹

31. In *DKLR Holding Co (No 2) Pty Ltd v Commissioner of Stamp Duties*¹⁰, Hope JA described the ‘very nature of a trust’ in terms of a personal obligation of a trustee annexed to property to hold the property for the benefit of another. Hope JA emphasised that both elements were necessary for the existence of a trust: a personal obligation not annexed to property is insufficient to constitute a trust and, conversely, a right annexed to property but without any concomitant personal obligation is likewise insufficient.

32. Each description highlights the dual character of a trust, comprising both personal obligations of a trustee and concomitant rights of the beneficiaries annexed to the trust property. In order to ‘create’ a trust there must be a creation both of personal obligations *and* of rights annexed to property.

33. In *Commissioner of Taxation v Commercial Nominees of Australia Ltd*¹¹ (*Commercial Nominees*), the Full Federal Court noted that the use of the term ‘trust estate’ and ‘fund’¹²:

... must be taken to refer to the conglomeration of property in respect of which trust obligations and corresponding rights exist from time to time. Putting it another way, a trust estate or a superannuation fund will be that property the ownership of which is divided between trustee and beneficiary.¹³

⁵ Subsection 104-55(1).

⁶ Subsection 104-55(2).

⁷ *Commissioner of Taxation v Bamford* [2010] HCA 10 at [36].

⁸ Ford and Lee 1990, *Principles of the Law of Trusts*, 2nd edn, Sweet & Maxwell Ltd at [1.010].

⁹ *Jacobs’ Law of Trusts* (8th ed at [1-01]).

¹⁰ [1980] 1 NSWLR 510 at [15].

¹¹ [1999] FCA 1455.

¹² As the term is defined and used in Part IX of the *Income Tax Assessment Act 1936*.

¹³ [1999] FCA 1455 at [51]

34. The litigation in *Commercial Nominees* and *Commissioner of Taxation v Clark*¹⁴ (*Clark*) was concerned with the tax impact of certain changes to an existing trust. In those cases, the legal question before the Court went to whether an existing trust had come to an end such that the assets of the original trust were now held on a different trust. Thus the High Court on appeal from the decision of the Full Federal Court in *Commercial Nominees* observed¹⁵:

... The trusts under which the fund operated in 1994-95 were constituted by the original trust deed in 1988 as varied by the exercise, in 1993, of a power of amendment. The property the subject of the trusts did not alter at the time the amendments took effect. Persons who were the members of the fund before the amendments remained the members of the fund after the amendments. The fund, both before and after the amendments, was administered as a single fund, and treated in that way by the regulatory authority.

The eligible entity established in 1988 did not come to an end in 1993, and it did not divide into two eligible entities ...

35. Similarly in *Clark*, Edmonds and Gordon JJ in their joint judgment noted that it was significant that 'the Commissioner never contended, either before the primary judge or on appeal, that there was a cessation in the continuum of trust property such as to leave it open to find that the trust estate as originally constituted had come to an end'.¹⁶ Their Honours concluded (emphasis added)¹⁷:

...When the High Court in *Commercial Nominees* spoke of trust property and membership as providing two of the indicia for the continued existence of the eligible entity or trust estate, the Court was not suggesting that there had to be a strict or even partial identity of property for the first and objects for the second. It was speaking more generally: that there had to be a continuum of property and membership, which could be identified at any time, even if different from time to time; and without severance of one or both **leading to the termination of the trust in question**. In the present case, the Commissioner never contended, nor on the evidence could he, that there was a severance in the continuum of trust property and objects of the CU trust. Their identity changed from time to time, but not their continuum.

36. The trust splitting arrangements considered in this Determination stand in contrast with the issues raised by the matters before the Courts in *Commercial Nominees* and *Clark*. The question posed by a trust split is not whether the original trust has come to an end. Rather, the question is whether the assets transferred to the new trustee are settled on a new trust fund that has been separated from (or carved out of) the original trust fund.¹⁸ A similar point is made in TD 2012/21¹⁹ where it is observed that the effect of a change to the terms of a trust pursuant to the valid exercise of a power contained within the trust's constituent document might be such as to lead to a particular asset being subject to a separate charter of rights and obligations giving rise to the conclusion that the asset has been settled on terms of a different trust.²⁰

¹⁴ [2011] FCAFC 5.

¹⁵ *Commissioner of Taxation v Commercial Nominees of Australia Limited* [2001] HCA 33 at [36–37].

¹⁶ *Clark* at [53].

¹⁷ *Clark* at [87].

¹⁸ See, for example, *Commissioner of State Revenue v Lam & Kym Pty Ltd* [2004] VSCA 204; *Oswal v Commissioner of Taxation* [2013] FCA 745.

¹⁹ Taxation Determination TD 2012/21 *Income tax: does CGT event E1 or E2 in sections 104–55 or 104–60 of the Income Tax Assessment Act 1997 happen if the terms of a trust are changed pursuant to a valid exercise of a power contained within the trust's constituent document, or varied with the approval of a relevant court?*

²⁰ See paragraphs 11 and 27 to 29 of TD 2012/21.

37. More useful for present purposes are the decisions of the Full Federal Court in *Aussiegolfa Pty Ltd (Trustee) v Commissioner of Taxation*²¹ (*Aussiegolfa*) and the Supreme Court of South Australia in *Dyda P/L & Anor v Commissioner of State Taxation*²² (*Dyda*).

38. In *Aussiegolfa*, the Full Federal Court considered whether a class of units in a unit trust (the DomaCom Fund) were units held on a separate and distinct trust. Of note for present purposes, Steward J made the following observations from his analysis of a number of court decisions from Australia and the UK²³:

I derive the following general propositions from the foregoing survey of statutory language, context and purpose, as well as from the authorities:

- (a) first, that the word “trust” in s 70E(2)(a) (of Part 8 of the *Superannuation Industry (Supervision) Act 1993* which contains the in-house asset rules applying to regulated superannuation funds) is apt to refer to a singular continuing relationship of trust with the possibility of multiple and changing beneficiaries, in respect of multiple and changing items of property;
- (b) secondly, that within that singular relationship there may be created sub-funds which may not constitute separate and distinct trusts;
- (c) thirdly, the creation of a sub-fund would probably constitute a new or separate relationship of trust where there was, to use the language of Hoffmann J, a segregation of assets, the appointment of a new trustee, and the exhaustion, by the terms of the sub-fund, of the beneficial interest in the property of the fund;
- (d) fourthly, the creation of a sub-fund would probably not constitute a separate and distinct relationship of trust where the fund remained subject to the provisions of the original settlement and its property remained available, whether contingently or otherwise, to be deployed for the trust’s original purposes, or to use the language of Lord Wilberforce, to “fall back into the rest of the settled property”;
- (e) fifthly, a key consideration would be whether the other beneficiaries, who were not members of the new sub-fund, could be said to enjoy, whether contingently or otherwise, an equitable interest in, or equitable rights over, the assets or income of the sub-fund. Conversely, it will be relevant to determine whether the members of the sub-fund had, whether contingently or otherwise, an equitable interest in, or equitable rights over, the other assets or income of the original trust. Asking such questions will assist in determining whether the terms of issue of the sub-fund had segregated the sub-fund from the original trust;
- (f) finally, the question as to whether a given sub-fund is a separate trust turns upon a close analysis of the terms governing that sub-fund. Those terms will reveal the intentions of the parties. Each case will, as Edmonds J has emphasised, need to be judged on its particular facts.

39. The Court concluded that the holders of the units in the sub-fund that was at the centre of the dispute in *Aussiegolfa* did not have any rights or interests in any other part of the DomaCom Fund and that a separate trust had been created.²⁴

40. The arrangement considered by the Supreme Court of South Australia in *Dyda* has similarities to the trust splitting arrangements considered in this Determination. The Court

²¹ [2018] FCAFC 122.

²² [2013] SASC 156.

²³ [2018] FCAFC 122 at [206].

²⁴ [2018] FCAFC 122 at [220–221].

in *Dyda* considered whether a series of steps to transfer control of real property to the Dyda group gave rise to a stamp duty liability. The land in question was held in a unit trust, the Woodville Property Trust. Units in this trust were held by two family trusts, the Meeuwissen Family Trust and the Young Family Trust.

41. The transfer of the control of the real property was effected through a series of steps.
- (a) First Dyda was appointed as trustee of the part of the trust assets of the Woodville Property Trust which comprised the real property. This part of the trust was to be known as the Burleigh Avenue Trust.
 - (b) The trust deed was amended to allow for a new type of units, funding units, which could receive income in priority to all existing units.
 - (c) Dyda in its capacity as trustee of the Burleigh Avenue Trust issued to Dyda in its capacity as trustee of the Burleigh Avenue Trust No 4 one funding unit.
 - (d) Dyda Nominees was appointed as trustee to part of the Meeuwissen Family Trust comprising one ordinary unit in the Burleigh Avenue Trust. This was henceforth known as the Burleigh Avenue Trust No. 2.
 - (e) John Dyda was made guardian and appointor of the Burleigh Avenue Trust No. 2.
 - (f) Similarly, Dyda Nominees was appointed as trustee to part of the Young Family Trust comprising one ordinary unit in the Burleigh Avenue Trust. This was henceforth known as the Burleigh Avenue Trust No. 3.
 - (g) John Dyda was also made guardian and appointor of the Burleigh Avenue Trust No. 3.

42. The appellants argued that the transactions implemented did not involve the conferring of a benefit in relation to the trust property in any form, that is, 'nothing was conferred on anybody as nothing additional was done to create in any person rights apart from the rights that existed under the existing discretionary trusts'.²⁵

43. Stanley J rejected the argument of the appellants, concluding.²⁶

The appointment of Dyda Nominees as trustee of the Burleigh Avenue Trust No. 2 and No. 3, was in each case, effectively the resettlement of the units under a new trust rather than the appointment of a new trustee to existing trusts. The requisite continuity of the trust did not exist.

The continuity of trusts was broken because of the transfer of control of these two discretionary trusts to the Dyda group, which occurred on 8 March 2007. This was achieved by the appointment of Dyda Nominees as the trustee, and by the appointment of John Dyda as the appointor and guardian under the trusts. In his capacity as guardian, John Dyda could control the distributions of some income and of all of the capital of the trusts. A member of the class of potential beneficiaries of the trusts who was not a member of the Dyda group could not realistically expect ever again to receive any distributions under the trusts. This conclusion is reinforced by the granting of indemnities. Accordingly, Dyda Nominees acquired an absolute interest in the ordinary units.

44. Although *Dyda* concerned the South Australian state stamp duty implications of the arrangement implemented, the analysis leading to the conclusion that the arrangement caused the resettlement of assets under a new trust rather than the appointment of a new

²⁵ [2013] SASC 156 at [33–34], summarising the appellant's submissions.

²⁶ [2013] SASC 156 at [143–144].

trustee to an existing trust is equally applicable to the existence of a separate trust relationship in an income tax context.

Settlement of assets on terms of a different trust

45. The appointment of an additional trustee to an existing trust fund would not, without more, give rise to an E1 event. The usual position applying to a trust with multiple trustees is that the trustees share one office of trustee and must act unanimously in respect of the assets of the fund.²⁷

46. The steps involved in the arrangement discussed in this Determination can be contrasted with the mere appointment of an additional trustee.

47. A trust split as defined for the purposes of this Determination is directed to achieving a functional separation in the operation of the trust. The intent is that those who control and can benefit from the part of the trust corpus that is transferred to the new trustee will be different from those who control and benefit from the remaining assets held by the original trustee. In these arrangements, the existing trustee is removed as trustee in respect of some of the assets of the existing trust estate and a new trustee is appointed to hold those assets. The intended result is that the existing trustee will no longer have fiduciary obligations in respect of the transferred assets, and no entitlement to indemnification out of those assets for expenses incurred after the introduction of the new trustee. Likewise, the new trustee will have no fiduciary obligations in respect of the assets retained by the pre-existing trustee, nor any rights to be indemnified out of those assets. As a consequence, each particular trustee's obligations and powers relate to particular assets only. Further, in relation to the assets it holds, each trustee exercises its powers independently of the other and is solely responsible for the manner in which those powers are exercised.

48. These factors lead to the conclusion that there is no longer one trust fund over all of the assets. Instead, there are two distinct trust funds which are both administratively and legally separated.

49. In addition, given the intended separation of trustee obligations and powers, attempts to administer a 'split' trust as a single trust fund would encounter immediate practical problems. Each trustee will only receive the income derived from the assets it holds and is only able to seek to make good its right to be indemnified from those assets, and only for expenses properly incurred in carrying out its trust duties. The parties typically intend that each trustee individually calculates the income of the trust that arises from the assets it holds and individually determines how that income is to be dealt with. As such, a trustee of a loss-making fund would have no surplus income available for distribution but rather a loss intended to be carried forward and recouped only against future income (if any) of that fund, with the full surplus income in the other trust fund remaining available for distribution by the trustee of that trust fund.

50. Finally, although the range of beneficiaries and the terms of the trust deed may be consistent between both trust funds at the time that the new trustee is appointed, the terms of the trust instrument do not prevent the instrument being varied by each trustee individually as it relates to the assets it holds. Through the exercise of such powers it is conceivable that the range of beneficiaries, the trust terms and even the vesting date applicable to the individual funds may be caused to differ. This fact again points to there no longer being a single trust fund.

²⁷ See, for example, *Beath v Kousal* [2010] VSC 24 at [18-19].

51. A useful check on this analysis can be obtained by considering the result of a potential challenge by an aggrieved beneficiary to an exercise of a trustee discretion after the implementation of a trust split.

52. While the identity of those entitled to benefit from the original trust as a whole, as set out in the trust deed, may remain unaltered in the course of the implementation of the trust split, in exercising its discretionary power of appointment, each trustee must give real and genuine consideration to how, and in respect of whom, the power should be exercised, having regard to the purpose for which the discretion has been conferred.²⁸

53. In ascertaining the purposes for which the discretionary powers of appointment have been vested in each trustee, a court could be expected to have regard to extrinsic evidence as to the reasons for, or object of, the reorganisation, as well as the circumstances surrounding the reorganisation, in construing the scope of the powers and discretions vested in each trustee under the trust deed. This is so notwithstanding that on their face, the trustee discretions conferred by the trust deed are wholly unfettered.²⁹

54. These circumstances lead to the conclusion that the trust powers and discretions vested in the original and new trustee have purposes distinct from each other, notwithstanding that they are contained within the same trust deed and are on identical terms. These distinct purposes could be expected to be recognised and given effect to by a court in the event that a disappointed beneficiary attempted to raise an action against a trustee. Returning to Example 1 in paragraphs 5 to 12 of this Determination:

- (a) Assume the Moon Trustee thereafter distributed all the income from the 100 Sun Pty Ltd shares to Jane. The parties' intent is that post the transfer of the 100 Sun Pty Ltd shares to Moon Trustee, those shares will be held for the benefit of Jane and her children and Moon Trustee would accordingly only make distributions of income derived from those shares between Jane and her children. Any challenge by Ben or Holly of the Moon Trustee's decision to only distribute to Jane would be contrary to this intent and it might be expected such a challenge would fail.
- (b) Assume instead the Moon Trustee thereafter distributed all the income from the 100 Sun Pty Ltd shares to Ben or Holly. This would be inconsistent with the parties' intent that post the transfer of the 100 Sun Pty Ltd shares to Moon Trustee, Moon Trustee would hold those shares (and the income derived from those shares) for the benefit of Jane and her children and not for the benefit of Ben or Holly. As such, Jane would have a basis to challenge the trustee's actions and such a challenge might be expected to succeed.³⁰

55. These expected outcomes are consistent with, but not a necessary precondition to, the conclusion that, in transferring the 100 Sun Pty Ltd shares to Moon Trustee, those shares are subject to a new charter of rights and obligations – that those shares have been settled on terms of a new trust to be held for the exclusive benefit of Jane and her children.

²⁸ *Edge v Pensions Ombudsman* [1998] Ch 512 at [535]; *Attorney-General (Cth) v Breckler* [1999] HCA 28 at [7].

²⁹ Use of extrinsic evidence of this type is permissible at law: *Byrnes v Kendle* [2011] HCA 26 at [113]; *Schmidt v Rosewood Trust Ltd* [2003] 2 AC 709 at [27–31]; *Karger v Paul* [1984] VR 161 at [175]; *Hartigan Nominees Pty Ltd v Rydge* (1992) 29 NSWLR 405 at [429–431].

³⁰ Of course as Jane is the designated appointor for the Moon Trust, if Moon Trustee were to act in this way it would also be expected Jane would exercise her powers as appointor to remove the trustee and replace it with an entity that would respect the intention of the parties in 'splitting' the trust.

By declaration or settlement

56. The second element necessary for CGT event E1 to happen is that the creation of the trust is by declaration or settlement.

57. A trust is created by declaration within the meaning of subsection 104-55(1) when it is created by words or conduct sufficient to demonstrate an intention to create an express trust over property.³¹ Where a trust split is implemented by executing a deed of variation, or similar document, the terms of the agreement will demonstrate an express intention to hold the transferred assets subject to the terms of the trust deed. This suffices to create a trust over those assets by declaration.

58. A trust is created by settlement when property is vested in a trustee for the benefit of others.³² A trust split involves a transfer of existing trust property to, and the vesting of this property in, a new trustee for the benefit of others. Therefore, there is the creation of a trust by settlement.

59. In short, a trust split involves the creation of a new trust by declaration and/or settlement, and CGT event E1 happens when that new trust is created.

³¹ *Kafataris v Deputy Commissioner of Taxation* [2015] FCA 874 (*Kafataris*) at [26].

³² *Taras Nominees Pty Ltd as Trustee for the Burnley Street Trust v Commissioner of Taxation* [2015] FCAFC 4 at [5]; *Kafataris* at [31].

References

Previous draft:

TD 2018/D3

Related Rulings/Determinations:

TR 2006/10; TD 2012/21

Previous interpretative decisions:

ATO ID 2009/86

Legislative references:

- ITAA 1936 Pt IX
- ITAA 1997 104-55(1)
- ITAA 1997 104-55(2)
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