Argyle Lawyers

# Relationships: A practical overview of family law, estate planning and related family issues

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# Introduction

Married and de facto partners should understand that their relationship may fail despite their best intentions.

Australian Bureau of Statistics (ABS) data suggests that Australia's current divorce rate is 40% – and this does not include de facto relationships.

The rates of remarriage and subsequent divorce are also high. Other ABS data shows that more than 36% of marriages involve at least one partner who was previously married.

Unfortunately, second and subsequent marriages are more likely to fail than first marriages, according to a study, Love can hurt, divorce will cost, released several years ago by the National Centre for Social and Economic Modelling at the University of Canberra.

Points to consider, even before a new relationship begins, include understanding how the Family Court divides marital property in contested property cases, steps you can take to protect your current and future finances, and how to safeguard the welfare of children from previous relationships.

It is also crucial to understand the implications of the breakdown of a relationship. This may affect other family members and business interests, as well as for your estate planning, superannuation, family home and tax affairs.

The Family Court's powers, in most States, were extended to include property disputes between de facto (including same sex) couples, where separation occurred after 1 March 2009.

The Argyle Family Legal Office brings together expertise from a range of our specialist lawyers to offer guidance to our clients.

# Part One: Before entering a relationship

If you are contemplating beginning a new relationship, either living as a de facto couple or entering into a marriage, you should carefully consider what may occur if the relationship were to fail and what steps you can take to minimise the adverse effects of a separation.

A major consideration will be the assets and liabilities both partners may bring into the relationship, since there may be a substantial disparity in each person's financial situation at the beginning of a relationship.

One person may have, for instance, sizeable child support and spousal maintenance obligations from an earlier relationship whereas the other person may have relatively simple financial affairs. Confronting these issues at the beginning of a relationship is important.

Possible steps to take before commencing a relationship include:

## 1. Make a list of your assets, resources, liabilities and other financial obligations

This exercise will enable you to properly assess your financial position. Your new partner may agree to undertake the same exercise.

The recording of assets, liabilities and obligations of both spouses can have several fundamental benefits.

First, each partner will enter the relationship with an understanding of the other's financial position, reducing the possibility of later misunderstandings and surprises.

Second, establishing each partner's financial position can be of assistance in discussing a binding financial agreement with your partner. A binding financial agreement can be made in the event of parties living together or intending to marry. (Binding financial agreements are discussed in more detail below.)

The making of such lists by both partners will clearly identify any disparities in wealth. One partner may have been particularly successful in business or have inherited significant assets for example.

Your list of assets and liabilities should include, for example, superannuation entitlements, shares in listed and unlisted companies, options, business interests, interests in any trust, expected inheritances, and information in respect of patterns of distributions from discretionary trusts.

Upon separation if you and your partner cannot agree as to the division of your assets, the Family Court will make the decision for you instead.

When making orders for a property settlement following the breakdown of a relationship, a judge or a magistrate will assess the contributions each spouse has made to the accumulation of matrimonial assets. This assessment takes into consideration the initial contributions of each party at the beginning of the relationship and during the relationship.

Therefore, evidence of what each person brings into the relationship can safeguard your interests in the future.

Your financial records also will be of assistance if a valuation is required of a company, partnership or trust. This would occur where there is a company, partnership or trust in existence at the time of separation which forms part of matrimonial property.

## 2. Consider a binding financial agreement

Couples are increasingly entering into binding financial agreements before marrying or before entering de facto relationships.

A binding financial agreement has even greater significance particularly in circumstances where there is a second or subsequent relationship and one spouse has substantial assets which may include for example, extensive business interests or large investment portfolios.

A binding financial agreement is a private agreement which provides how the assets and liabilities of the parties will be divided in the event of a separation. Depending upon the circumstances, such agreements often stipulate that each spouse will keep at least the assets they introduced into relationship.

Binding financial agreements can be made before a relationship begins, during a relationship and after a relationship has broken down.

The Family Court cannot override the terms of a binding financial agreement unless one of the parties to the agreement for example can prove fraud, duress or unconscionable conduct when the agreement was made, or, the agreement does not meet the specific requirements of the Family Law Act.

The Family Court can also set aside a binding financial agreement if there has been a material change relating to a child's circumstances which would cause hardship if the agreement were enforced.

Binding financial agreements may be used as a means to give certainty to parties entering into a relationship. They address the uncertainty of a court ordered property division which may arise where parties subsequently fail to agree about how their joint assets and liabilities are to be divided at separation. This uncertainty is due to the wide discretionary powers of judges or magistrates in the Family Court who make orders about the division of matrimonial property.

Binding financial agreements, while not being invincible, can however give valuable protection if properly and thoughtfully prepared.

Each partner must obtain independent advice from a separate family lawyer before entering into a binding financial agreement and the lawyer must sign a certificate of independent legal advice on behalf of their client when the agreement is signed. The certificate of independent legal advice is then attached to the binding financial agreement.

The Family Law Act provides for three types of binding financial agreements. Section 90B refers to binding financial agreements entered into before the marriage (referred to as prenuptial agreements). Section 90C refers to binding financial agreements entered into during the marriage (referred to as mid-nuptial agreements), either before or after the marriage has broken down. Section 90D relates to binding financial agreements which are made after divorce (referred to as post nuptial agreements).

A binding financial agreement can be terminated by another written agreement pursuant to s90J of the Family Law Act and is referred to as a Termination agreement.

Couples entering into binding financial agreements who do not intend to marry but live in a de facto relationship can also enter into similar agreements either before they enter into a relationship, during the relationship and after the relationship has ended.

Binding financial agreements are private agreements. There are no records of the numbers of couples entering into binding financial agreements as they are not scrutinised by the Family Court. It is important therefore if you enter into a binding financial agreement that the agreement is retained in a safe place.

A binding financial agreement would be particularly useful for:

- a couple entering into a second marriage who may need to protect their existing assets and make financial provision for children of previous marriages;
- high net worth couples who want certainty about an outcome in the event of separation and who also want to plan for estate and other financial matters;
- parents with substantial assets who want to provide their children with certainty before they marry or during the marriage. A binding financial agreement would safeguard any assets their children may inherit or protect an existing interest in a family trust or a family company;
- professionals who marry after they have established their careers and who have their own established asset base.

The requirements for binding financial agreement are:

- the agreement must be in writing;
- the agreement must be signed by each of the parties;
- the agreement must specify what section of the Family Law Act applies for example s90B of the Family Law Act for pre-nuptial agreements, s90C of the Family Law Act for a mid-nuptial agreement and s90D for a post nuptial agreement, where the parties have divorced;
- the agreement must deal with property and financial resources and may include provisions for spousal maintenance;
- one party must retain the original agreement and the other a copy of the agreement;
- there must be certificates of independent legal advice annexed to the agreement signed by the solicitors for each of the parties.

## 3. Prepare for potential challenges with 'blended' families

A person entering a second or subsequent relationship should be aware of the potential tensions that could arise between a new partner and children from previous relationships.

For instance, a second spouse may not necessarily want her late husband's adult children from his first marriage to benefit from his estate.

Parties entering into a new relationship therefore should review their estate planning given their changing circumstances.

Try to avoid leaving your family a legacy of bitter disputes over your estate in the event of your death. Perhaps ask yourself a seemingly straightforward question: What are the likely expectations of my spouse and my children? This may influence the drafting of your Will.

Aside from estate planning issues, both partners in a new relationship should take into account the general welfare issues of their children from previous relationships. The 'blending' of families can cause some unexpected difficulties where, for example, there are agreements for parenting orders which provide for shared care arrangements. Such agreements may involve provisions as to holiday care arrangements and restrictions on moving interstate or within the state.

## 4. Consider making a new Will

In NSW, for instance, marriage generally revokes a will unless made in contemplation of that particular marriage. Divorce generally revokes provisions making gifts to a former spouse as well as a former spouse's appointment as executor, trustee or guardian of the Will.

A new relationship may encourage you to make another Will reflecting your changed circumstances while making provision for any children from other relationships.

## 5. Review your superannuation death benefit nomination

You may have nominated a preferred beneficiary with your superannuation fund or you may have made what is known as a binding death benefit nomination (if provided for in your fund's trust deed).

Some binding death benefit nominations may be drafted to become invalid upon specific events such as divorce or marriage.

In any case, either divorce or remarriage should prompt you to review either your binding death benefit nomination or your non-binding nomination of a preferred beneficiary.

Superannuation death benefits can generally only be paid directly to a deceased fund member's dependants, as defined in the Superannuation Industry (Supervision) Act 1993, or the legal personal representative (the executor of the deceased's estate).

A dependant of a deceased member is defined in superannuation law as a spouse (including a de facto partner), children of any age, or a person who is financially dependent on the deceased at the time of death. Another group of eligible dependants are those who had a so-called "independency" relationship with the deceased (which can include having a close personal relationship, living together, or providing domestic or financial support – by either person).

If a binding death benefit nomination is not in place, the trustees of a superannuation fund generally have the discretion to determine which eligible dependants will receive a deceased member's superannuation death benefits (including insurance death benefits). Alternatively, the trustees may decide to pay the benefits to the deceased's legal personal representative, depending upon the circumstances.

Significantly, a Will can only direct how superannuation death benefits are distributed if the benefits have first been paid by the fund trustee to the deceased's legal personal representative (executor of the estate).

## 6. Make a new power of attorney if appropriate

A new relationship should prompt you to consider making a new power of attorney or enduring power of attorney. A power of attorney and enduring power of attorney give another person the power to make financial decisions on your behalf.

Powers of attorney and enduring powers of attorney as well as the appointment of an enduring guardian are discussed further in this booklet.

# Part Two: During a relationship

In broad terms, the issues facing a couple during a relationship are generally similar to those faced before the commencement of a relationship. As already noted, parties can enter into a binding financial agreement during the relationship. This may be relevant if one party is about to enter into a new business venture, for example.

Other issues to consider during a relationship include the purchase of property with a new partner, review of Wills and superannuation death benefit nominations, possible claims against your estate in the event of your death, loans or gifts to children, and the establishment of a family company or a family trust.

## 7. Purchase of a property with a new spouse

If you decide to purchase real estate with your partner, you can hold the property in two ways either as joint tenants or as tenants in common (usually in equal shares or in shares which may reflect your contribution to the acquisition of the property).

If you own a property as joint tenants and your partner survives you, he or she will become the sole owner by right of survivorship. Even though you may have made provision in your Will for your share of the property to be distributed for example to children from your previous relationship, such provisions would be invalid.

However, if you own the property as tenants in common, your share of the property forms part of your deceased estate and you can specify in your Will who is to receive it.

## 8. Superannuation death benefits

If a binding death benefit nomination is not in place, superannuation fund trustees generally have the discretion to decide which eligible dependants will receive the deceased member's superannuation death benefits. The trustees may, alternatively, decide to pay the benefits to the deceased's legal personal representative.

Superannuation legislation defines dependants as the deceased's spouse, children and other persons who depended on the deceased. A fund trustee will most likely make a decision in favour of a spouse rather than making a distribution to financially independent adult children.

Couples who have entered into a new relationship may want to ensure that their financially independent adult children from a previous relationship receive some of their superannuation entitlements in the event of their death. For example binding death benefit nominations may provide that your adult children receive a certain percentage of your superannuation death benefits with the remainder going to your current spouse.

## 9. Challenges to your Will

Under the Succession Act 2006 (NSW) and similar legislation in other states and territories, your Will may be contested if certain criteria are not met. This is a matter to consider if you have entered into a new relationship.

Those eligible to make an application to contest your Will under NSW law include; your married or de facto spouse (including same sex partners) at the time of death, former spouses, your children, and a person who was a member of the same household and financially dependent upon you. This could include a stepchild in certain circumstances.

The court, after a hearing, will decide whether the deceased had made adequate provision for the maintenance and education and advancement in life of the eligible person.

It is unlikely however that the court, for instance, would make orders in favour of a former spouse who received assets pursuant a family law property settlement or a binding financial agreement, unless all of the assets had been dissipated and the former spouse could establish financial hardship. However even if those circumstances were to occur the former spouse may not be successful in making a claim. Each case depends on its own set of facts and circumstances.

## 10. Family trusts

The Family Court can make orders in relation to third parties to a marriage; third parties include entities such as family trusts and/or private companies.

Factors to think about during a relationship where there are family trusts or family companies involved include whether one spouse has effective control of a trust or a company, patterns of distributions from a trust, or whether you should make your partner a director of a family company. The relationship between trusts and family law is a complex subject which you are urged to discuss with a specialist family lawyer if relevant to your circumstances.

## 11. Gifts or loans to children

Parents are increasingly helping their adult children pay for the deposit on their first homes. However, many parents often fail to consider the possible consequences of their child separating from their partner in these circumstances.

Consider the example of parents who decide to contribute $50,000 towards the deposit for their adult child’s first home.

What will happen to the $50,000 if their child later separated from his or her partner? How would the Family Court view the money advanced by the parents? Will the court treat the contribution as a loan or a gift?

These are important questions to think about before you advance any money to your adult children.

Consider providing the money by way of a loan rather than a gift. The loan should be documented in a deed of loan. It may be further secured by way of a mortgage over the property to be purchased.

The deed of loan should stipulate when and how the loan is to be repaid as well as any interest payable (if relevant).

A mortgage can be particularly important if the adult child is borrowing money for business purposes. A registered mortgage will take priority over unsecured creditors if the business were to fail.

Alternatively, an adult child receiving a loan from their parents could enter into a binding financial agreement with their partner. A term of the agreement would make specific provision for the repayment of the loan in the event of separation to the parents.

# Part Three. When a relationship ends

When a relationship ends either you or your partner may want to enter into a binding financial agreement (if you do not already have one), stipulating how your assets will be divided. Alternatively, your settlement could be documented by way of a consent order.

A consent order is an agreement which is filed in the Family Court and is subsequently ratified by the court. When parties file consent orders they must also lodge with the court a collaborative document setting out their assets and liabilities. Once the court seals the consent order it becomes binding and enforceable.

A consent order can also document arrangements about where children of the relationship will live and what schools they may attend, for example. A binding financial agreement cannot include provisions for parenting arrangements, it can only deal with financial matters.

Other matters to consider when a relationship ends involve living arrangements for children of the relationship, dissolving the marriage, reviewing child support payments and estate planning.

## 12. Estate planning documents

You should review your estate planning and associated matters after separation. This includes your Will, enduring power of attorney (or power of attorney) and appointment of an enduring guardian.

Given that the person appointed under your enduring power of attorney (or power of attorney if applicable) is authorised to deal with your financial matters, it is crucial to revoke the documents if one of the appointed attorneys is your estranged spouse. (An enduring power of attorney continues to have effect in NSW, for instance, if you lose the mental capacity to make decisions.)

The person appointed as your enduring guardian is authorised to deal with all of your non-financial matters if and when you no longer have the medical capacity to do so. Again, if one of your guardians is your estranged spouse, he or she should be replaced.

Your Will should be high in your priority of estate planning documents to review. If at the date of your death you have not been divorced and your estranged spouse is named in your Will as the sole beneficiary of your estate, he or she will remain the sole beneficiary under NSW law.

Unlike a marriage or divorce, a separation has no effect on the validity of your Will. A former spouse named as an executor and/or beneficiary under your Will should be replaced immediately if that is your intention.

When negotiating a binding financial agreement or a property settlement following the breakdown of marriage or de facto relationship, spouses can enter into an agreement, known as a deed of release. A deed of release is an agreement by each spouse in which they each promise not to make a claim against each other's estate.

However, you should note that a deed of release does not necessarily prevent parties bringing claims against each other's estate in circumstances where the court has not approved the deed and granted the release beforehand.

An application for approval of a deed of release can be made during the lifetime of the parties to the deed as well as by their personal legal representative (the executor of the deceased's estate). However if you are not able to make such an application to the court, a deed of release is still a worthwhile agreement to negotiate, as it is evidence of the parties intentions, in the event such a claim is made in the future.

If you or your partner have children from a previous relationship, the position is more complex. Your children are eligible persons who may contest your Will whether or not they are living with you or your spouse – and whether or not you had any contact with them.

If the children of your new partner (your stepchildren) are living with you, they may also become eligible to contest your Will.

You cannot enter into a deed of release on behalf of your children.

## 13. Superannuation death benefit nominations

Superannuation death benefits in most circumstances do not form part of your estate. Therefore it is not sufficient to change your Will at the time your relationship fails.

If you have made a valid binding death benefit nomination with your superannuation fund in favour of your estranged spouse, you should consider revoking it under the governing rules of your superannuation fund. If you do not revoke the nomination, the trustee has no choice but to pay the benefit to your former spouse in the event of your death.

If a binding death benefit nomination is not in place (as discussed earlier), superannuation fund trustees generally have the discretion about which eligible dependants under superannuation law will receive a deceased member's superannuation death benefits. The trustees may, alternatively, decide to pay the benefits to the deceased's legal personal representative (the executor).

If your relationship fails, you may wish, for example, to leave all of your superannuation death benefits to your adult children. You would have to make a new binding death benefit nomination to ensure that this occurs.

## 14. Severance of joint tenancies

If you own real estate with your former spouse as joint tenants, rather than as tenants in common, the property cannot form part of your deceased estate. Your interest under a joint tenancy would pass to the surviving joint tenant.

You should therefore consider severing the joint tenancy immediately upon separation and even before you reach an agreement about the division of matrimonial property. You can then make a new Will immediately.

# Part Four: Negotiating a property settlement

## 15. Settlement planning and structured settlements

When a relationship fails, there are often serious financial and personal implications involving the assets you seek to retain as part of your property settlement.

One spouse, for instance, may gain ownership of a family business as part of their property settlement. In turn, other family members may become worried about whether this will disturb existing business succession planning.

It is important that any other directors or partners of your business be kept informed of the progress of your settlement discussions, in the event that you do not have the protection of a binding financial agreement.

Furthermore, where there are valuable assets such as family companies, trusts, partnerships or a mix of investment properties as well as the family home, it is important to obtain specialist advice about the structure of the property settlement (including taxation advice) so as to maximise the potential benefits of your settlement.

We are able to provide guidance regarding the structure of your property settlement, before and after settlement.

We also offer an "assessment" to couples who are about to separate. This assessment provides advice as to how the Family Court may divide matrimonial assets in their specific circumstances.

This assessment may help you to reach a settlement with your former spouse, thereby avoiding costly court proceedings and emotional strain.

As well, we offer alternative dispute resolution and mediation services to assist our clients to reach a settlement.

Significantly, couples who negotiate their settlements have more control over the outcome of their property settlement. It should not be overlooked that the Family Court has a wide discretion when making orders about the division of matrimonial property. Neither party has control over the outcome of a settlement. Once you embark upon a contested hearing settlement is left in the hands of a judge or a magistrate.

# Part Five: How does Family Court divide assets?

If you and your partner are unable to reach an agreement as to how your assets will be divided, a judge or magistrate of the Family Court will order the division instead.

In most cases where matrimonial assets may be typically a home, a small share portfolio, superannuation and perhaps a negatively geared property, the court tends to notionally divide the assets equally in circumstances when there has been a long marriage. In this instance there is less emphasis on analysing each of the parties' contributions. However because there is no concept of an equality of division in the Family Law Act, there is no set formula for the division of assets.

With shorter marriages, the court will place more weight when dividing matrimonial property on the initial financial contributions of each spouse. Their contributions during the relationship will generally be reflected in the final division of assets.

## 16. Four-step approach

In every case the Family Court applies a four-step process when deciding how to divide assets between the parties.

### 16.1 Step one. Identifying the net asset pool

All property is generally included in the pool of matrimonial assets whether acquired before, during or after separation.

The asset pool will include property such as superannuation savings, shares in public and private companies, any interest in a trust (where the spouse is a controller), an interest in any business or partnership, bank accounts, furniture, artwork, wine collections, cars, jewellery, real estate and other investments such as options, entitlements to long service leave and undistributed deceased estates.

Next liabilities are quantified to determine a net pool of assets. Examples of liabilities include credit card debts, mortgage loans, personal loans, hire purchase loans etc. Often there may be disputes as to whether a particular liability is to be considered as a matrimonial liability.

### 16.2 Step two. Assessing the contributions that each party has made to the accumulation of the assets

Step two involves the consideration of financial and non-financial contributions (such as homemaking and parenting contributions) to the acquisition and conservation of assets during the relationship.

Gifts from parents, for example, are generally treated as a financial contribution by the party whose parents made the gift.

The assessment of such contributions generally involves an analysis of contributions made during the relationship and considering the history of the relationship.

### 16.3 Step three. Assessing the future needs of both parties

The third step involves a consideration of each of the parties future needs, taking into account such factors as age, health, income earning capacity, the length of relationship (where relevant), financial circumstances of a new relationship and the financial resources of each party. Consideration is also given to who will look after the children of the marriage in the future, and what standard of living is reasonable in the circumstances.

An example of a financial resource is an interest one party may have as a beneficiary in a trust where that party has no control over the trust. In this situation, the court can only take into account in a notional way the beneficiaries' right to receive distributions from time to time.

A further example of a financial resource is when one party receives an inheritance after separation and they can clearly prove the other party has made no contribution to the inheritance. In that situation the court may deem the inheritance to be a financial resource of the person who received the inheritance and not property to be divided between the parties.

A judge or magistrate may readjust the division of assets (after considering each party's contributions to matrimonial property) to reflect greater future needs of one party.

### 16.4 Step four. Examining whether the proposed property division is just and equitable

This final step involves the judge or magistrate looking at the proposed division of assets and determining whether the division is fair and reasonable to both parties. This is a subjective consideration.

## 17. Full and frank disclosure between parties

The Family Law Act requires both parties to make full and frank disclosure of their financial positions when negotiating a settlement.

This requirement ensures that each of the parties and the court are fully informed before a decision is made about the division of assets of the marriage. Financial disclosure is taken seriously by the court. There may be severe penalties imposed by the court and upon parties who fail to make such disclosures.

Any person involved in a property settlement should not risk a finding against them of non-disclosure of their assets. This can be detrimental and costly. For instance, the court can set aside a property settlement if there was incomplete or inaccurate disclosure by one of the parties. Or the court may give one party all of the available assets and leave the person who fails to make a disclosure with nothing.

Parties must exchange financial statements while they are negotiating a settlement. These include such documents as tax returns, bank statements, superannuation statements, and financial statements for any company, partnership or trust in which one party is involved.

## 18. Superior contribution

A superior contribution or the wealth creator principle may apply in situations where there are substantial matrimonial assets, for example, where the marital pool of assets is at least $7 million and upwards. In these circumstances, the Family Court may award a much larger share of the asset pool to the spouse who can demonstrate that his or her special skill or abilities have created the wealth. This tends to be the position even where there has been a long marriage. These skills have been referred to by the Family Court as special skills, or superior contributions or extra contributions.

Depending upon the circumstances, the spouse who was the wealth creator will seek a larger share of the property settlement on the basis of his or her involvement in the wealth creation.

In these cases, the judge or magistrate may take into consideration such factors as ownership of the business assets, company or trust structures, involvement of the parties in strategic business decisions, personal liability or exposure relating to a business, or the giving of guarantees etc.

If one party can convince the court of their superior contribution or special skill they may receive an adjustment in their favour of between 60% to 70% of the net pool of assets.

# Part Six: taxation issues

## 19. CGT exemptions

In general terms, certain assets are exempt from CGT including:

- Assets acquired before 20 September 1985.
- Cars and motor cycles.
- Personal use assets costing less than $10,000.
- Main residences.

## 20. CGT rollover relief upon a relationship breakdown

Automatic CGT rollover relief applies when assets are transferred between parties pursuant to a Family Court order (including a consent order) or binding financial agreement following the breakdown of a marriage or a defacto relationship.

The effect of this is that the spouse transferring the asset disregards any capital gain that would otherwise be payable. However, the spouse who receives the asset will eventually have to pay any CGT when the asset is eventually disposed of – perhaps in many years' time.

If a main residence (previously referred to as a principal place of residence) is transferred between spouses following the breakdown of relationship, CGT will generally not be payable when the property is eventually disposed of – provided it is still used as a main residence until disposal.

## 21. Transfers from a company or trust to a spouse

CGT rollover relief applies when assets are transferred from a company or trust to a spouse pursuant to a court order or binding financial agreement upon the breakdown of the relationship. However for the CGT rollover relief to apply, the transfer of property must be to a spouse and not to a company or trust controlled by the spouse or associated with the spouse. (As later discussed, there may be, however, consequences under Division 7A of the *Income Tax Assessment Act* 1936, on the transfer of a property from a private company or trust to spouse.)

## 22. CGT rollover relief is not always appropriate in family law disputes

There may be instances where it would be beneficial for the controlling spouse to buy out the exiting spouse rather than rely on the CGT rollover relief. For example, if a business was started by the parties and has increased in value over the years, it may be in the controlling spouse's interest to crystallise the value of the business at the date of the breakdown of the relationship rather than take advantage of the CGT rollover provisions. This may be the position especially in relation to business goodwill. As the business was started by the parties in this illustration, the goodwill cost base is nil.

If the controlling spouse, say, buys the exiting spouse's interest in the business, the small business CGT concessions may apply. This may be for the benefit of both the controlling spouse and also the exiting spouse.

## 23. Division 7A consequences on the transfer of an asset between spouses

The transfer of an asset or cash payment from a private company to one of the parties could be deemed as a dividend - even if the Family Court ordered the transfer.

Division 7A of the Income Tax Assessment Act 1936 deals with three instances where a private company may be automatically deemed to have paid a dividend to an associate:

- Payments made by the company to a shareholder or shareholder's associate.
- Loans by the company to a shareholder or shareholder's associate (discussed in more detail below).
- Debts owed by a shareholder or a shareholder's associate to the company if the debts are forgiven.

Deemed dividends arising from the transfer of a property or other payments pursuant to a court order may be franked if related to the breakdown of a marriage or de facto relationship, otherwise generally deemed dividends are automatically unfranked.

## 24. Loan accounts and Division 7A consequences

Loans to associates of a private company – including shareholders, spouses, and related entities – may become the subject of the deemed dividend provisions.

Division 7A provides that a loan from a company to an associated person will automatically be deemed a dividend unless certain requirements are met.

A loan on commercial terms is excluded from Division 7A provided a written loan agreement is in place, with interest, capital payments and other factors which meet strict criteria.

As discussed, forgiveness of a loan will trigger the deemed dividend provisions under Division 7A.

A loan could be assigned to the spouse who will retain the company after a breakdown in a relationship. However, it is important to obtain the relevant indemnities to ensure that the spouse exiting the company is protected from any tax liabilities that may result.

## 25. Part IVA considerations

A matter that should be addressed in any family law settlement involving tax restructuring or tax advice is the potential impact of the general anti-avoidance provisions of Part IVA of the Income Tax Assessment Act 1936.

Broadly, the anti-avoidance provisions are directed at arrangements entered into with the sole or dominant purpose of gaining a tax benefit.

## 26. Stamp duty

The transfer of the matrimonial home from one spouse to the other spouse pursuant to an order of the Family Court or a binding financial agreement is exempt from stamp duty in every State and Territory.

As stamp duty laws can vary from State to State, we will focus on the position in NSW and Victoria in relation to other assets.

Pursuant to a Family Court order or binding financial agreement, other assets are exempt when transferred from one spouse to the other spouse including; listed and unlisted shares and other real estate (such as investment properties and holiday homes). Transfers of assets from a spouse to a company or trust are dutiable - even if such transfers are pursuant to a binding financial agreement or Family Court order.

## 27. Taxation and realisation costs

The Family Court may take into account potential capital gains tax (CGT), as well as other taxes and realisation costs, when considering the division of assets:

- If there is no intention (or the evidence does not establish) that one party has to sell a CGT asset in the short term, the court generally would ignore any potential CGT liability. That is, the court would not include a potential CGT liability in the pool of assets to be divided.

- If the court finds that the sale of a CGT asset is imminent. CGT is more likely to be included as a liability when identifying the net pool of assets to be divided between the parties.

## 28. Company tax losses

Taxation losses in a company to be retained by a spouse may also be a significant consideration. This is because tax losses can reduce the tax that is ultimately paid on future profits earned by the company.

# Part Seven: Tax effective child support

Child maintenance trusts can be a highly tax effective way to pay child support following the breakdown of a marriage or de facto relationship while ensuring that valuable assets are conserved for a child's long term security.

Child support is paid to the spouse who is the primary carer of children of the relationship. If parties cannot agree on the level of child support to be paid, the Child Support Agency will make an assessment of child support based on a prescribed formula. If parties can agree on the level of child support to be paid to the primary carer of the children they can elect to enter into a private agreement known as a binding child support agreement. A binding child support agreement may cover payments such as health cover, school fees, extra-curricular activities as well as periodic child support payments.

A child maintenance trust provides a means to pay child support in the equivalent of pre-tax income, leading to large annual tax savings for higher income earners in particular.

Statistics from the Australian Bureau of Statistics show that half of the divorces in Australia involve children, truly highlighting the significance of child maintenance trusts.

In simple terms, a parent transfers sufficient income producing assets into the trust to generate at least the required support payments for children who are named as trust beneficiaries.

The beneficiaries of a complying child maintenance trust must eventually acquire the trust held assets in their own right when the trust eventually ends.

Typical times for a trust to terminate, as stipulated in the trust deed, vary widely. Some trusts end after all beneficiaries reach a particular age such as 18, 21, 25 or older. Others trusts may end when the children's education (secondary or tertiary) is completed.

Significantly, assets within a child maintenance trust are protected from creditors and trustees in bankruptcy should a parent later experience financial difficulties. Further, the flow of child support payments from the trust is uninterrupted if parents lose their employment and their source of income.

A practical consideration is that both parents of a child must consent to the use of a child maintenance trust to pay child support.

Fortunately, the quarantining of assets in a trust for the children's long term benefit should provide considerable comfort to both parents following the breakdown of a marriage or de facto relationship – particularly if at least one former spouse intends to enter another relationship and perhaps have other children.

## 29. How child maintenance trusts save tax

The key to the trusts' tax effectiveness is straightforward.

Income generated from assets transferred as a result of a family "breakdown" into a child maintenance trust for the benefit of children is treated as "excepted trust income" under Division 6AA of the Income Tax Assessment Act 1997. (See Tax Ruling 98/4 for the tax office's interpretation of the law on these trusts and a discussion of the various provisions.)

This means that trust income received by beneficiaries under 18 is subject to standard adult tax rates – with the $6000 tax free threshold and graduated marginal tax rates – instead of the punitive rates that ordinarily apply to the trust or investment income of minors.

Under anti-avoidance tax provisions, trust or investment income received by a minor is usually subject to a tax free threshold of just $416 (effectively higher with the low income tax offset) and then the entire amount above this threshold is taxed at punitive rates.

## 30. Protection for trust assets

As mentioned earlier, assets held in a child maintenance trust are inaccessible to creditors. This should give reassurance to separating parents about the long term sustainability of child support payments.

## 31. Negotiations between spouses

Depending upon the circumstances, some separating couples may agree to accept a smaller percentage of the property pool to enable sufficient assets to be transferred into a child maintenance trust thereby securing their children's future financially.

However, as mentioned earlier, both parents of a child must consent to the use of a child maintenance trust to pay child support.

A parent who is reluctant to agree to the use of a child maintenance trust may change his or her mind if an intended trust held asset, such as a small commercial property for example, is likely to produce child support payments in excess of the child support assessment.

## 32. Control of the trust

Depending upon the wording of the trust deed, the parent who contributes the assets to a child maintenance trust may be the controller of the trust. However both parents may decide to become joint trustees of the trust.

## 33. Effective trust deeds

A child maintenance trust is effectively a modified discretionary trust.

The Argyle Child Maintenance Trust is designed to meet child support obligations; make flexible payments to the beneficiaries; maximise tax advantages for both the beneficiaries and the parent who contributes the assets to the trust; and allow for tax effective loans to beneficiaries.

Further, the Argyle Child Maintenance Trust provides for the tailoring of trustee powers – narrowly or widely to suit the circumstances – and for the protection of trustees.

## 34. CGT and stamp duty considerations

Parents who are considering contributing assets already owned by them into a child maintenance trust should be aware that the transaction could trigger capital gains tax on capital gains during their ownership, as well as stamp duty on the transfer.

The possibility of becoming liable for CGT at this point may be a factor in deciding which assets are contributed to the trust.

Small business owners may be eligible for small business CGT concessions and exemptions on “active” business assets, including commercial real estate occupied by a business, on their transfer to a child maintenance trust.

Another possible tax issue is when trust held assets eventually vest in the beneficiaries. CGT may become payable by the beneficiaries at this point on any increase in the value of the assets while held in the trust. However, the beneficiaries would typically be eligible for the 50% CGT discount for individuals.

# Part Eight: Splitting of Superannuation

Under the Family Law Act, superannuation is treated as property which like other assets of the relationship may be divided between couples upon the breakdown of a marriage or a de facto relationship.

Part or all of the superannuation entitlements of one spouse may be transferred to the other spouse.

Significantly, superannuation savings are not necessarily divided in the same proportions as other matrimonial assets. They may be divided into different percentage splits or specific dollar amounts.

In some instances, separating couples may decide not to split their combined superannuation savings but each retain their own superannuation entitlements.

The trustees of the superannuation fund which is the subject of a splitting order must give their consent to the wording of the order or in the binding financial agreement, except when the superannuation entitlements are in a self-managed superannuation fund and the parties are trustees of the fund.

## 35. Taxation and superannuation splits

A superannuation benefit which is transferred from the superannuation account of one spouse to the superannuation account of the other spouse under a binding financial agreement or court order is treated as a rollover between funds.

The tax free and taxable components of the superannuation benefit are proportionately divided between spouses, and the superannuation benefit is not subject to the standard superannuation contributions tax.

In-specie transfers of assets, such as real estate or shares, between self-managed superannuation funds are also subject to CGT rollover relief.

# About Us

Argyle Lawyers through takes a holistic approach to providing legal services; focussing on individual and family needs. We provide advice designed to assist you and your family create, build and protect wealth through generational wealth transfer.

Our multi-disciplinary specialists – covering such areas as family law, estate planning, asset/wealth protection, property, taxation, superannuation and succession planning for family businesses - provides an advisory service, and identifies needs and objectives to support your family.

# About the Author


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Glenda has specialised in family law for more than 20 years and is a Family Law Accredited Specialist (one of the first such specialists in New South Wales). Her extensive experience makes Glenda an obvious choice to deal with complex high value property settlements with considerable business, personal, and superannuation assets at stake.

Glenda champions the use of alternative dispute resolution and mediation services to prevent long and costly litigation as well as to reduce the stress of matrimonial breakdown. When there is no other option, she conducts litigation and negotiates complex settlements supported by practical and achievable advice.

Glenda sensitively handles: property matters for married and/or de facto couples, including same sex couples; high value property settlements; binding financial agreements; superannuation and family law; child support and spousal maintenance matters; guardianship applications; children's matters; child maintenance trusts; and international child abduction (under the Hague Convention).

Among Glenda's clients for family law and de facto matters are Australian and overseas high net worth individuals.

Glenda's interests outside the law are many and varied and include listening to early and classical music, and reading American and medieval history.