A FATE WORSE THAN DEATH

KEEPING AN ESTATE OUT OF COURT

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The passing of the baby boomer generation means that there is a significant generational transfer of wealth. This is the generation that bought a house in the western suburbs for 10,000 pounds in the 1960s, that created Gorton style companies spitting control and dividends to reduce death taxes and trading trusts for the farm, and compulsory superannuation from 1991.

Estate litigation appears to be limited to probate claims, challenging the testator's will on the basis that the testator lacked testamentary capacity, the testator did not known and approve the contents of the will,[1] or executed the will whilst subject to undue influence; and family provision claims,[2] challenging the testator's estate on the basis that adequate provision was not made for the applicant's education, maintenance and advancement in life.

However, scratch below the surface of many Corporations Act disputes and there is often a deceased estate – the oppression of the minority, winding up on the just and equitable ground, and breach of director's duties, arising from splitting the shares between beneficiaries and disagreement about the direction of the company as a going concern (or whether it should just be wound up), and the benefits received by the beneficiaries actively involved in the enterprise as opposed to the passive shareholder beneficiaries. Similarly, many real property disputes often involve a deceased estate – section 66 Conveyancing Act applications to force a sale, caveats, and claims of equitable interests arising from the beneficiary whose business uses the farm or the commercial lot, the beneficiary who has paid for improvements, the beneficiary who is *not quite ready* to leave the house, or dispute between the beneficiaries about developing the property, waiting for the market to improve, or selling as is, now.

Accordingly, prudent estate planning is not just a personal issue, but is part of prudent corporate and commercial risk management.

medical opinion

A testator must have testamentary capacity to execute will., that is [3]

a. capacity to understand the nature of the act of making a will and its effects;
b. understanding the extent of the property the subject of the will, and

[1] Mekhail v Hana [2019] NSWCA 197
[2] Chapter 3 Succession Act 2006 (NSW); Family Provision Act (ACT)
[3] *Carr v Homersham* [2018] NSWCA 65 per Basten JA

c. the capacity to comprehend moral claims of potential beneficiaries, to recognise moral claims and, if more than one, weigh them and choose between them
d. that there are no conditions that interfere with capacity for decision making, such as a disorder of the mind or insane delusion

The gold standard is a contemporaneous opinion, from a specialist such as a geriatrician or consultant neuropsychologist, which considers the testator's capacity to sign a particular will.

A doctor's certificate confirming that the testator "has capacity" may not be sufficient. Capacity varies day by day, and during the day; and the test of capacity is different depending on the task[4] – capacity to give consent for a medical procedure is different from capacity for a power of attorney and capacity to execute a will, and capacity to execute a will may depend on the complexity of the particular will.[5]

Similarly, an ACAT assessment that the person can remain living at home may not be sufficient, or a MMSE score above 24/30 may not be sufficient – MMSE is a screening tool not a diagnosis, and analysis of the score depends on what particular questions the testator got right and whether they involve memory and abstract reasoning.

identification of assets

The testator's advisors need to confirm with the testator what the testator owns. This is important to establish that the testator has capacity to know the extent of their estate, and that they know and approve the contents of their will. However, it is also important because if the testator and the advisors do not properly identify and characterise the assets, and then properly allocate the assets, it may lead to litigation between beneficiaries, creditors and other stakeholders.

The testator's advisors should not completely rely on the testator's statements about what the testator owns.

First, the assets may be owned as joint tenant such as jointly owned houses and joint bank accounts. Dangerously, testators may create an "informal power of attorney" by adding a child on their bank account to facilitate the operation of the account, such as payment of bills and withdrawal of cash for testators who find it difficult to get to the bank. However, it is important to check whether the child is a signatory, *or a joint owner of the account* – otherwise, the helpful child may receive an unintended windfall.

[4] Guthrie v Spence [2009] NSWCA 369; 78 NSWLR 225
[5] Hobhouse v Macarthur-Onslow [2016] NSWSC 1831

Second, a testator may disclose what the testator *controls,* rather than what the testator *owns.* The testator may consider that they control the assets of the company, such as the company car, but the testator owns the shares in the company, rather than directly owning the assets of the company. The testator may control a discretionary family trust, but the testator may be the trustee or may own or control the trustee company rather than directly owning the trust assets.

Third, the testator's advisors should check the source documents, such as ASIC registers and land titles searches. However, this may not provide the complete picture. The testator may be *registered on title* as the owner but the testator may own the asset in their capacity as trustee or in their capacity as a partner of the partnership. The testator's advisors should check financial statements and tax returns to see how the asset has been treated, and the ASIC source documents to confirm whether the shares are owned beneficially.

Fourth, the testator's advisors should ask the testator if they are aware of any family discretionary trusts, and should check the testator's recent tax returns. It may be that there has been a distribution from the trust to the testator that the testator has never physically received (or perhaps even been aware of) which are unpaid present entitlements. These are assets of the estate, and the executor's claim requiring the trustee to pay out the unpaid present entitlements may threaten the solvency or continued operation of the discretionary trust.

The testator's advisors should be careful about the long term operation of the will. If the testator leaves their car to a beneficiary, should the gift be adeemed if the testator sells the existing car and buys another car? Does the car include if the testator sells the sedan and buys a motorhome Winnebago? If the testator leaves particular real estate to a beneficiary, should it extend to the accommodation bond which is purchased from the proceeds of sale?

The court may have power to construe a will if there is ambiguity on the face of the will or ambiguity in light of the surrounding circumstances,[6] or to rectify a will if there is a clerical error or the will does not effect the testator's instructions.[7] However, this will depend on evidence. Notably, there may be no *genuine* misunderstanding about what the testator really intended, but the uncertainty may give a disgruntled obstinate beneficiary leverage to negotiate a better deal.

[6] Section 34 Succession Act 2006
[7] Section 27 Succession Act 2006

The testator's advisors should confirm if there are any digital assets or other intellectual property. The advisors should also check whether the testator is a party to any continuing royalty agreements, outstanding option agreements or is a member of a collecting society.[8]

The testator should confirm if the testator has made any outstanding loans to any beneficiaries or other debtors, or if the testator otherwise wants to ensure that advances or gifts are taken into account in dividing the testator's assets. There is a presumption that all advances during a testator's lifetime are gifts,[9] so if the testator does not want the advance treated as a gift, the testator needs to say so. Further, loans that are more than six years old are time barred and extinguished and cannot be revived. Therefore, if the testator wants the advance taken into account, the testator should include a "hotchpot" clause than advances are taken into account, rather than requiring all "loans" to be repaid.

The testator's advisors should confirm the liabilities, and whether the loans are secured against particular assets or crossed and secured across a number of assets. The advisors should also check the business accounts – a testator may not realise but the "money they get from the business" may be treated as drawings from the partnership or part of their Division 7A loan.

solicitor notes

The solicitor's evidence is likely to be the best evidence of capacity, knowledge or approval, and supporting construction or rectification of the will.

However, there is a real risk of the evidence being unreliable because of the passage of time. The solicitor should make contemporaneous file notes.

A handwritten contemporaneous note with scrawls and abbreviations will be more compelling than a later created typed file note – indeed disposing the rough note and replacing it with a typed note may itself arouse suspicion.[10]

The solicitor should keep the file note with the will.[11] The testator may wish to keep a copy of the notes in case the lawyer passes away, and/or the law firm collapses and it is unclear where the records may be.

will kit wills and hand-made wills

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[8] See further Catanzariti TM "Death and the Maiden – Probate and Copyright" 2018) 45 (2) Aust Bar Rev 183-192
[9] *Calverley v Green* (1984) 155 CLR 242; Kemi v Wood [2013] NSWSC 180
[10] Mekhail v Hana [2019] NSWCA 197
[11] Ryan v Dalton; Estate of Ryan [2017] NSWSC 1007

Clients should be discouraged from will-kit wills or handmade wills. The cost may far exceed the cost of a professionally prepared will because of the legal costs ultimately involved.[12]

Even if the intent and substance of the will is not genuinely in dispute, there may be issues which require the intervention of the court and it is not enough to obtain the consent of the beneficiaries. This is especially the case in estates involving real property, shares or superannuation, where capital gains tax exemptions, death benefit dependant exemptions and stamp duty concessions depend on a transfer being in conformity with the will.

The issues with a willkit will or handmade will may include

- failing to properly execute the will in front of two witnesses requiring an application for the court to be satisfied that the testator intended the document to be their will;[13]
- failing to nominate an executor which requires an application for letters of administration with the will annexed and requires consent or service of all beneficiaries;
- ambiguously describing or mis-describing an asset or otherwise requiring a construction claim or a rectification (in circumstances where there is no independent evidence of what the testator may have meant)[14]
- failing to dispose of the residue or otherwise creating a partial intestacy which may lead to an expensive search for next of kin;
- mis-describing a charity or the terms of charitable gifts requiring a rectification or worse a cy-pres scheme which requires the intervention of the Crown Solicitor.

The other main problem with will-kit or hand made wills is not a problem with the will itself, but the lack of professional witnesses who can later provide evidence to support the will or the testator's intentions with respect to an ambiguous or mis-described gift. The best evidence may be the solicitor who prepared the will – the solicitor may have professional experience in assessing capacity, should have file notes to refresh their memory, may be comfortable in giving evidence, and is completely independent and disinterested. The nice lady at the court house or the man at the post office may not cut it – they may only vaguely remember the testator, and may not have even read the document they were witnessing.

selection of executor

[12] See the extensive litigation relating to The Estate of Laura Angius starting with *Estate Angius [2013] NSWSC 1895*
[13] Section 8 Succession Act
[14] Salier v Angius [2015] NSWSC 853

The executor not only distributes the estate, but manages the estate pending distribution, has the right to appoint directors of a company solely owned by the testator or otherwise exercise the testator's voting rights, may be required to make discretionary decisions such as whether to sell a property and invest the estate pending the distribution, and may become the trustee of a discretionary trust or a trustee of a minor's interest until the minor reaches majority.

A testator may wish to appoint all of the children, or the spouse and all of the children. However, this may lead to conflict, paralysis and ultimately litigation.

Alternatively, a testator may appoint one person. However, the testator needs to consider the potential for conflicts of interest, such as the person being the trustee and also the object of the testamentary discretionary trust, or the person or the person's children being the remainder beneficiaries of a life estate or right of residence, or just plain sibling rivalry.

The testator may appoint a professional executor such as a trustee company (such as NSWTG, Perpetual Trustees) or a solicitor, but should be aware that they will charge commission and professional fees.

The testator should consider the health and age of the proposed executor if the executor will be required to manage the assets for some time.

division of assets

The testator needs to clarify if any of the assets are strategically important to a business undertaking, and if so, create binding leases, licences or easements during the testator's lifetime.

The testator may wish to specifically devise assets to a number of beneficiaries. However, this may lead to issues if the beneficiaries do not agree what to do with the asset, whether to operate the company's business or wind it up, whether to retain the land to develop it, whether to retain the house until the market improves, or dispose it. There should be a deadlock mechanism including opportunities to exit. However, this may depend on the other beneficiaries' ability to finance a buy-out.

Alternatively, the testator may not specifically devise any assets and give the beneficiaries a share of residue. A beneficiary may elect to take an asset in specie in lieu of their legacy or share of residue. However, there may be issues if more than one beneficiary wants the asset. There is a risk that the executor prefers one beneficiary's request over another. The testator may give a particular beneficiary a first right to take the asset in specie, or may introduce a "dutch auction".

The testator needs to clarify whether any of the assets are leveraged, and if so whether it is intended that the loans will be discharged by the beneficiary of the assets, from the particular asset or asset class, or by the estate generally. Generally speaking, unless the will provides otherwise, the devisee of property that is mortgaged takes the property subject to the mortgage,[15] and the devisee of property that generates income and incur expenses before the distribution of the property is entitled to the income but must bear the burden of the expenses.[16] However, expenses such as capital gains tax are borne by the whole estate even though land tax is borne by the property.[17]

family provision claims

An estate is still vulnerable even if the will is robust, the assets are properly described, and the testamentary structure is considered.

The claimants against an estate may be a person who is excluded, a person who is included who wants more and/or person who is included who wants something different.

The testator needs to be encouraged to be completely candid and disclose as much information as possible about the people in the testator's life, the good, the bad and the ugly, the cause of any dispute and any estrangement. It is better to be aware of the potential claimants and plan for a claim and obtain information directly from the testator about the potential claimant, rather than being surprised after the testator has passed away, when the testator cannot provide any assistance.

A particularly elusive and slippery class of claimant is the de facto. What distinguishes a de facto from a girlfriend or boyfriend? When does a de facto relationship start and when does it end? Is it possible for one person to consider that they are in a de facto relationship whilst the other person considers that it is a non-committed relationship? Section 21C of the *Interpretation Act* provides that in determining whether two persons have a relationship as a couple for the purposes of sub-section (2), all the circumstances of the relationship are to be taken into account. The determination of the existence of a de facto relationship is essentially impressionistic and the most significant factor may be a mutual commitment to a shared life.[18]

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15 Locke Kings Act reflected in section 145 Conveyancing Act 1919 (NSW)

16 *Lloyd v Frape* (1922) 23 SR (NSW) 11; *O'Brien v McCormick* [2005] NSWSC 619 at [39] per Campbell J.

17 Sam Wardy v Gordon Salier; William Wardy v Gordon Salier; Hassiba Wardy v Estate of late Edmond Wadih Wardy [2014] NSWSC 473

18 *Robson v Quijarro* [2009] NSWCA 365,

The most reliable evidence are spontaneously created documents including medical admission records referring to next of kin, doctor's records, Centrelink records, and birthday and wedding invitations and Christmas and Easter cards (and who they are addressed to). Other documents may be self-serving such as the informant on the death certificate describing themselves as de facto.

There may be other claimants that the testator may not have anticipated.

This may include persons claiming to be a biological child. DNA testing may be required, which may involve testing against the testator's relatives or against the biopsies which may be retained by NSW Health.

This may include persons claiming to be dependant because of occasional assistance provided by the testator. A person may make a family provision claim if they are a grandchild or a member of the household, and wholly or partly dependant on the testator. This includes grandchildren or step-children raised by the testator in loco parentis. In *Page v Page*, Basten JA noted that the issue is whether the relationship is such that it would create *an ongoing obligation* towards the applicant, that the person takes over social, moral and legal obligations, such that the community may expect provision to be made for the applicant's maintenance and advancement in life.[19] In recent cases, the Family Provision List Judge, Hallen J says that dependents means[20]

> "any person who would naturally rely upon, or look to, the deceased, rather than to others, for anything necessary, or desirable, for his, or her, maintenance and support."

Dependence includes financial dependence and emotional dependence. In McKenzie v Baddeley ,[21]the court said that "partly" does not require substantially dependant, but requires more than trivial or minimal, and perhaps means "significantly". In *Morrison v Carruthers*, Bergin CJ referred to the Oxford Dictionary, and referred to "substantially" ("of real importance or value") and "significantly" ("of real import").[22]

A pattern of generosity, and occasional or regular gifts does not make a person dependant. Dependence needs to be considered *in the context of the applicant* – does the applicant *depend* on the gifts. Making generous gifts does not create an obligation, but may be characterised as voluntary support, generosity and indulgence.[23] In *Siddle v Ellis*, the testator gave gifts to her partner's son

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[19] Page v Page per Basten JA at [11]
[20] Fede v Dell'Arte at [57] per Hallen J**; Sammut v Kleemann [2012] NSWSC 1030 at [37] per Hallen J**
[21] McKenzie v Baddeley [1991] NSWCA 197
[22] Morrison v Carruthers [2010] NSWSC 430 per Bergin CJ at [12]
[23] Pearson v Jones [2000] NSWSC 799 per Master Macready; Griffiths v Craigie [2014] NSWSC 1339 at [138] per Hallen J

and paid for a number of his expenses, but the applicant could not demonstrate that he was d*ependent* on her.

In *Morrison v Carruthers*, Bergin CJ explained this by distinguishing between expectation and dependence. She said [24]

> "It is important in this regard to draw the distinction between expectation and dependence. If an adult receives payment on a regular basis from the deceased and chooses not to obtain money from another available source because of the expectation of regular payment from the deceased, that does not amount to dependence within the meaning of that term in the Act. Financial dependency in the case of a healthy adult who is able to work means a necessity to rely on the deceased because there is no other source of finance available.
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> Although the Court's task in this regard has been described generally as one involving the consideration of "past events and future probabilities", I am of the view that in claims brought by healthy adult grandchildren who are able to work, dependence should be assessed by having regard to matters including: (a) the applicant's cost of living showing the break up of expenses on a weekly/monthly/or other (depending on the particular circumstances of the case) basis; (b) the income of the applicant (excluding the amount received from the deceased); (c) the amount received from the deceased on a weekly/monthly/or other basis; (d) whether the applicant was able to work and earn income to meet the reasonable costs of living that was otherwise provided by the deceased; (e) whether other sources of finance/income were available to the applicant to meet those living costs; (f) whether the applicant was able to work and chose not to do so; and (g) if the applicant chose not to work, whether that choice was necessary in all the circumstances, for instance, to care for the deceased; or infants; or elderly or infirmed members of the family."

However, claims may also be made grandchildren and children of a partner who *claim* to be dependant because the testator provides occasional financial assistance such as paying school fees, giving them a car, or for am paying overseas trip, and allowing them to stay at the house for a few months. The claimant may not ultimately be successful if the dependence is slight, but the

[24] Morrison v Carruthers per Bergin CJ at [12] to [13]

estate still needs to incur costs in defending the claim and may ultimately find it more cost effective to pay to resolve the claim than go to trial.

notional estate

In NSW, a claimant may make a claim against the testator's actual estate, and also the testator's notional estate. Generally speaking, this incorporates assets that the testator has the *power* to transfer into the testator's own name, even though the testator has not done so. This extends the available estate beyond assets that the testator *owns* to assets that the testator *controls*.

Part 3.3 "Notional Estate Orders" ensures that the family provision principles are not frustrated by the testator's financial manoeuvring and financial shuffling, the "Part IVA" of the Succession Act.

The purpose of the provisions is to extend the powers of the court to the "full range of benefits and advantages controlled by testators", and not just the assets owned by the testator in the testator's personal name,[25] to allow the courts to make provision where the testator has transferred assets "into a structure over which the testator had a measure of practical control", even though the testator lacked actual ownership of the assets.[26]

Property may be designated as notional estate if the testator entered into a "relevant property transaction" before the testator's death.[27] A relevant property transaction is very widely defined - a testator has entered into a "relevant property transaction" if the testator did, directly or indirectly, or omitted to do any act which results in property being held by another person or subject to a trust and the testator did not receive full valuable consideration.[28]

For example, the testator who owns a house as a joint tenant has the power to sever the joint tenancy, a testator with superannuation death benefit has the power to direct that the superannuation should be paid to the testator's estate, and the testator who is the trustee of a discretionary trust or who controls the trustee company through owning a majority of the shares or being the sole director or who is the appointor of the trust could distribute the trust asset to the testator.

The court does not have to trace the property that was distributed to a beneficiary when making an order pursuant to *section 79 Succession Act.* Therefore, if the court is satisfied that someone has received a distribution from the deceased's estate, it is possible to designate any of that person's

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[25] *Wentworth v Wentworth* (unreported, Bryson J, 14 June 1991) at 107 per Bryson J
[26] *Belfield v Belfield* [2012] NSWSC 416
[27] section 80(1) Succession Act
[28] section 75(1) Succession Act

property as notional estate, even if that property is not something into which it would be possible to trace any specific property of the deceased. There does not need to be a causal connection. [29]

The testator may attempt to quarantine the testator's assets from any claim. However, the only sure way of quarantining the assets *is to transfer the assets out of the testator's control.* And that may be a step too far for a testator.

Any transfer may be "clawed back" into the estate if it is within 1 year of the testator's death if the testator had a moral obligation to make adequate provision for a person, or within 3 years if the transaction was entered into with the intention, wholly or partly, of denying or limiting provision being made out of the estate to a family provision applicant.[30] Accordingly, if there are commercial transactions occurring within the three year period, such as inter-generational farm transfers, or the house needs to be re-financed through family members to finance an accommodation bond, or the business undertaking needs to be transferred because the bank requires the active working stakeholders to give a bank guarantee rather than the matriarch giving the bank guarantee, then there should be file notes setting out the commercial reasons for the transaction so that the transaction is not vulnerable.

[29] *Phillips v James* [2014] NSWCA 4 at [73] to [76] per Beazley P; *Charnock v Handley* at [190] to [196] per Hallen J

[30] Section 80 Succession Act