

# Taxation Duties Of Executors

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Tax Files is contributed on behalf of the South Australian based members of the Taxation Committee of the Business Law Section of the Law Council of Australia.

As lawyers we are often asked to act as Executors for our clients.

We all know that the Executor is responsible for administering the deceased estate in the best interests of the beneficiaries.

There are a number of tasks that an Executor will need to undertake in carrying out this, such as locating the Will, applying for Probate if necessary, getting in the assets of the deceased, paying all the liabilities and distributing the Estate in accordance with the terms of the Will.

The duties of Executors however go beyond simply dealing with the estate matters but extends to dealing with the tax issues of the deceased as at the date of the death of the deceased and potentially with tax issues that arise during the course of the administration of the Estate.

There are some particular issues which Executors need to consider from a tax perspective. These include lodging a final taxation return for the deceased and any outstanding prior year returns, lodging taxation returns for the Estate itself and providing the beneficiaries with such information as is necessary to enable the beneficiaries to complete their own tax returns and in particular to enable them to deal with any tax ramifications on the distributions they receive. In some cases it may also mean paying the tax on behalf of the beneficiaries.

This article looks at some of the taxation issues that an Executor will need to consider.

Also note that you will need to consider if your professional indemnity excludes you acting as an Executor. If it does you may not wish to take up that role.

## PREPARING A TAX RETURN FOR THE DECEASED PERSON

As an Executor of a deceased estate it is likely that you will need to lodge a final tax return on behalf of the deceased person. You will also need to determine if the deceased failed to lodge prior year tax returns and if so, you will need to determine whether or not they need to be lodged. If you come to the conclusion that they should have been lodged, you will need to have them prepared and lodged.

## DECEASED ESTATE RETURN

If the deceased estate received income from any source after the date of death, then it is likely that an income tax return of the deceased estate will also need to be prepared. This return is a separate return from the date of death return of the deceased person.

## PAYING TAX ON THE INCOME OF THE DECEASED ESTATE

The Executor will also need to determine who pays the tax on the income derived by the deceased estate and also the applicable tax rate. Will it be a liability of the Executors or the Beneficiaries? This will largely depend on whether:

- the beneficiaries are presently entitled;
- if they are under any legal disability;
- if the deceased estate is fully administered.

Each of these will need to be determined and considered as at 30 June in each year of the administration of the estate.

I do not propose to comment further on these items in this Article but if you are an Executor you will need to carefully consider each of these issues. They are quite technical legal issues and you must ensure that you know how they operate and apply. If for no other reason you need to know how they apply to ensure that if you are personally liable to pay the tax on distributions that are made to beneficiaries that you make provision for payment as part of the administration of the estate.

As an Executor you cannot distribute the income or assets of a deceased estate until the debts of the deceased, including tax debts are fully paid. However you can make interim distributions if you are certain that the remainder of the assets will cover the debts.

If you make distributions without ensuring that there are sufficient assets to pay any tax payable in respect of those distributions you will be personally liable for that tax.

## CAPITAL GAINS TAX ISSUES

There are special rules that apply to the transfer of any CGT assets from a deceased estate to the Executors and to the subsequent beneficiaries. The general rule is that a capital gain or capital loss made on an asset acquired after 20 September 1985 is to be disregarded if when the person dies the asset passes to either their legal personal representative or to a beneficiary or from their legal personal representative to a beneficiary.

There are a few exceptions to this rule such as if the asset passes to a foreign resident or a tax advantaged entity.

Special rules apply where the particular asset is the principal place of residence of the deceased. You will need to be careful to deal with the principal place of residence in such a way to ensure that it remains the principal place of residence. This status may be lost if during the course of the administration of the Estate the principal place of residence is used for income producing purposes or if it is not disposed of (ie sold and settled) within two (2) years of the date of death.

## NON-RESIDENT BENEFICIARIES

If a beneficiary of an estate is a non-resident of Australia for tax purposes the Executor is liable to pay the tax on that beneficiary's share of the trust estate income that is distributed to that beneficiary. If you are sending any distributions overseas you should make

enquiries as to whether that beneficiary is a non resident for tax purposes.

When dealing with foreign beneficiaries it is now becoming more common to see Wills clauses which enable the Executor to deduct from any distribution to the foreign beneficiary the amount of tax payable in respect of that distribution. If you draft Wills you may wish to include such a clause in the future Wills that you draft if you don't already do so.

## SUPERANNUATION

When a person dies their superannuation entitlements are paid to their beneficiaries either directly or as part of their estate. Lump sum death benefits paid to superannuation dependants are generally tax free. The taxation of lump sum benefits paid to non-dependants and death benefit income streams depend on a number of factors, such as the ages of the beneficiaries and the deceased and the type of superannuation.

If you receive a death benefit as the Executor of a deceased estate, the estate pays the tax on behalf of the beneficiaries of the super benefits. Again you will need to ensure that you have sufficient assets in the estate to cover these payments.

## DIVISION 7A

One issue that is becoming increasingly prevalent in estate matters is the application of Division 7A of the tax legislation. Without going into that Division in detail the Division deems certain payments to shareholders of private companies and associates as dividends. You will need to take particular care where you are an Executor of the estate of a deceased person who held shares in a private company and who owed money to that company.

It may be that prior to death, the deceased and the Company had complied with the requirements of Division 7A by having a complying loan agreement in place and the minimum yearly payments required by the Division had been made. Having these in place avoids the deeming of dividends.

As Executor you will need to deal with that loan and continue to comply with the loan agreement. If however you determine

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that the requirements of Division 7A have not been complied with by the deceased (eg there may be no complying loan agreement) you will need to determine what the tax consequences are to you as Executor and in particular when and if a "deemed dividend" arose. This may mean you need to go back a number of years to see when the loan was made and how it has been dealt with since then.

To avoid the consequences of Division 7A, arrangements will need to be put into place to repay the loan. One thing you should not do is to have the company forgive the loan. The ATO takes the view that Division 7A will apply to treat the forgiveness of the loan as a dividend. That said, this may be the only course of action and you should only do so understanding the tax consequences of the forgiveness.

## CONCLUSION

The role of an Executor can be a complex one depending on the nature of the asset in the estate and the circumstances of the beneficiaries. The tax rules are not simple and do impose certain obligations and liabilities on Executors. If you agree to become an Executor you must ensure that you are aware of the potential personal tax liabilities that you may have. These obligations are in addition to your duties as an Executor and a legal practitioner and should not be taken lightly. **B**

# CPD Events

For further details and to register:  
www.lawsocietysa.asn.au  
cpd@lawsocietysa.asn.au

All sessions that are being held at LSSA, will be held at Level 10 Terrace Towers, 178 North Terrace Adelaide

**Ethical Trainwrecks and other Avoidable Disasters**  
WEDNESDAY 16 MARCH 2016  
9.00AM – 12.30PM 3 Units \*

**Small Practice Conference**  
THURSDAY 17 MARCH 2016  
9.00AM – 5.00PM 6 Units \*

**Public Sector Half Day Conference**  
FRIDAY 18 MARCH 2016  
12.30pm – 4.30PM 3 Units \*

**Achieving Work Life Balance**  
MONDAY 21 MARCH 2016  
9.00am – 5.00pm 6 Units \*

**Triple Your Memory and Halve Your Stress**  
TUESDAY 22 MARCH 2016  
9.00AM – 1.00PM 6 Units \*

**Risk and Practice Management Intensive**  
WEDNESDAY 30 MARCH 2016  
9.00AM – 1.00PM 3.5 Units \*

**Building and Leading Teams**  
THURSDAY 31 MARCH 2016  
9.00AM – 12.30PM 3 Units \*

**PC Renewal**  
WEDNESDAY 13 APRIL 2016  
5.30PM – 7.00PM 1.5 Units \*

**Family Law Cases Update**  
27 April 2016  
5.30PM – 7.00PM 1.5 Units \*

\*Total CPD Units are accurate at time of printing and should be taken as a guide only. **HAVE AN IDEA FOR A FUTURE SEMINAR?** We invite practitioners to tell us what seminar they would like to see conducted next. Email us at cpd@lawsocietysa.asn.au with your ideas.