

THE IMPORTANCE OF
ESTATE PLANNING
&
TESTAMENTARY TRUST WILLS

WILLS & ESTATE PLANNING

Having a legal, properly prepared Will is vitally important to ensure your final wishes in regard to the distribution of your estate are carried out. Without a legal Will, your estate could be distributed unfairly according to a formula set by each state and territory's probate laws. This could result in some of your relatives receiving more than you wished while other loved ones are not provided for in the way you intended.

A properly drafted Will ensures that the person you nominate administers your estate, that your estate is divided according to your wishes and makes the granting of probate quicker and less expensive, leaving more for your loved ones.

To ensure your assets remain within the family for their use and benefit, a [Testamentary Trust](#) should also be considered.

TESTAMENTARY TRUST WILLS

In recent years the term "Testamentary Trust" has been used to describe what is usually a Discretionary Family Trust established under a Will. Their popularity arises from the considerable benefits that can flow from their establishment under a Will. A number of these benefits arise from the fact that the assets of the trust while they may be controlled by a potential beneficiary do not form part of that beneficiary's estate. This feature means that a beneficiary's inheritance through a testamentary trust can be highly beneficial in a number of circumstances.

Bankruptcy

Unfortunately, the incidence of bankruptcy in our society has increased significantly. Often a wife will guarantee her husband's business venture and vice versa. To some extent we can all be at risk whether in traditional high-risk occupations or not. However, if the bankrupt's inheritance has been provided through a testamentary trust it will be protected from creditors.

Divorce

As with creditors, an inheritance held within a properly prepared testamentary trust is unlikely to be the subject of a Family Court order in the case of a marriage breakup. It may be regarded as a financial resource and have some effect on the terms of a property settlement but this is a preferable outcome to the property being at the disposal of a Family Court order.

Pension Benefits

The assets of a testamentary trust are not currently taken into account in establishing pension eligibility under the current means tested pension rules. However, income from the trust is taken into account for income test purposes.

Spendthrifts and people with disabilities

It is not uncommon for people suffering a variety of disabilities to be unable to properly manage their financial affairs. At the same time, families wish to ensure that an adequate fund is set up to meet their reasonable needs but so as not to affect any pension rights they may have. The flexibility of a testamentary trust, especially if combined with a memorandum of wishes as to how the trust should be administered, can be an appropriate arrangement.

Taxation Advantages

Although the above features are in themselves good reasons to consider a testamentary trust in your will, the major basis of their popularity is the considerable tax savings which can arise under Section 102AG of the Income Tax Assessment Act 1936 (ITTA). The effect of this section is that children under the age of 18 years who receive income from a testamentary trust are taxed on that income as an adult and therefore enjoy the normal tax free threshold (\$5,400.00 or \$6,150.00 if the low income rebate applies) and marginal tax rates which apply to adults. Without this special provision of the ITTA trust income to minors has a tax free threshold of only \$416.00 (or \$643.00 if the low income rebate applies) and thereafter the highest marginal rate applies to the minor’s income.

The following example illustrates the advantages of establishing a testamentary trust compared with a traditional will provision.

Assume a husband dies leaving a dependant wife and three infant children. His estate is valued at \$500,000.00. If this were invested at (say) 8% per annum, it would generate an income of \$40,000.00.

Traditional Will

Example 1: The husband’s Will leaves everything to his wife. Her tax position (ignoring the Medicare levy) is therefore:

Beneficiary	Income	Tax Net	Income
Wife	\$40,000.00	\$8,380.00	\$31,620.00

Testamentary Trust Will

Example 2: The husband’s Will establishes a Testamentary Trust providing for the wife and three children to be beneficiaries. The family’s tax position might be:

Beneficiary	Income	Tax	Net Income
Wife	\$10,000.00	\$ 680.00	\$ 9,320.00
Child 1	\$10,000.00	\$ 680.00	\$ 9,320.00
Child 2	\$10,000.00	\$ 680.00	\$ 9,320.00
Child 3	\$10,000.00	\$ 680.00	\$ 9,320.00
	<u>\$40,000.00</u>	<u>\$2,720.00</u>	<u>\$37,280.0</u>

In example 2, the total tax bill is \$5,660.00 less than in example 1 and this level of saving may be possible for many years.

Testamentary Trusts can be attacked

Even though a testamentary trust may be considered by a Will-maker to be a prudent provision for family members, like all provisions of a Will, it may be attacked by certain “eligible applicants” under a Family Provision application. The surviving spouse, children and certain dependants have a right to challenge a Will in this way. While there are strategies that may be used to frustrate or restrict family provision claims, they are unlikely to result in the same benefits provided by a testamentary trust.

Never too late!

The ITAA provides a second chance to the family of a Will-maker who has not established a testamentary trust. This second chance must be taken advantage of within three years of the date of death of a deceased. It enables a trust to be established from assets derived from the deceased and for the income to enjoy the same tax advantages as income derived through a testamentary trust. However, the effect of the provision is that the sum which may be used to establish the trust cannot exceed the amount which the “beneficiary” would have received from the deceased’s estate had the deceased died intestate ie. without a Will.

New Trends

Increasingly, the traditional husband and wife Will ie. each to each other and then to the children is being replaced by a testamentary trust controlled by the surviving spouse and under which the spouse and children are potential beneficiaries. Wills along these lines can if the funds in the trust justify it provide that on the death of the spouse, sub trusts come into existence for the benefit of each child and that child’s family (and would be controlled by the child concerned). Increasingly, grandparents are providing education trusts for their grandchildren which have the added advantage of maximising the tax-free income that can be applied for the benefit of the grandchild.

Conclusion

Testamentary trusts, while largely promoted as a tax saving mechanism have many other advantages. Their inherent flexibility makes them worthy for consideration in your overall estate planning strategies.

Our solicitors can assist you in making an estate plan so your assets are protected and are able to provide advise on such matters as Business Structuring, Asset Protection Planning, Wills, Estate Planning & Testamentary Trust matters.

ENDURING POWERS OF ATTORNEY - NSW

We strongly recommend that you consider appointing an **Attorney** and [Enduring Guardian](#) and also consider having a reserve Attorney and Guardian. Changes to the law in 2003 by the New South Wales State Government mean that an **Enduring Power of Attorney** no longer covers health and lifestyle issues and is restricted to property and financial matters.

Why have an Enduring Power of Attorney?

If you lose your mental capacity through injury or the onset of a medical condition (e.g. Alzheimer's or dementia) your spouse/partner/family cannot conduct your affairs on your behalf unless they hold an Enduring Power of Attorney. This is required to deal with Banks, Centrelink or transferring property. Please note the **Power of Attorney** must be an **Enduring Power of Attorney** and not a **General Power of Attorney**. This Attorney is restricted to financial and property matters.

In the event that no **Enduring Power of Attorney** is held and you lose your mental capacity, your affairs would be handled by the Office of the Protective Commissioner (also known as the Public Trust Office). Although your family could apply to the **Guardianship Tribunal** to be appointed as an Attorney or Guardian for you, the easier solution is to have the documents in place now.

WHAT IS AN APPOINTMENT OF ENDURING GUARDIAN?

An **Appointment of Enduring Guardian** appoints someone to act on your behalf as your **Guardian** in the event that you lose your mental capacity and cannot conduct your own affairs. The document is very similar to an [Enduring Power of Attorney](#) but it relates only to **health and lifestyle issues**. For example, if you required medical or dental treatment (which usually requires a consent form to be signed) this could not be undertaken if you have lost your mental capacity. Your **appointed guardian** can do this for you. Similarly, if you need to be moved into a nursing home or nursing facility because your condition has deteriorated, your Guardian can make the necessary arrangements on your behalf with the health authority. An Enduring Power of Attorney **does not** extend to these areas.

If you lose your mental capacity through injury or illness, your family cannot make these arrangements for you unless an Appointment of Enduring Guardian has been correctly signed. Your family would have to apply to the **Guardianship Tribunal** to be appointed as Guardians in order to look after your affairs. These applications are not always successful and the end result could be that a government agency (eg. Public Trust Office) is handling your affairs.

For more information on any of the above please contact Tony Rimac from PT Wealth Solutions on (02) 9891 1544 or email tony@ptws.com.au