REABURN SOLICITORS

TESTAMENTARY TRUST WILLS – WHAT ARE THEY?

Wills incorporating Testamentary Discretionary Trusts are becoming more popular as the "baby boomers" age with greater wealth, children and in some cases blended families.

A "Testament" is a Will and a "Trust" is a relationship whereby one person (or persons) holds property or assets on behalf of or for the benefit of another. The holder of the property is the Trustee.

The creation of a Testamentary Trust in a Will has both advantages and disadvantages. These are:

Advantages

1. The flexibility given to the Trustees to allocate income and sometimes capital with the benefit of real time knowledge, something a testator (the deceased) cannot have;

2. The Trust is a device to keep the inheritance separate from the assets of the beneficiary and hopefully protected from creditors and spousal claims in the future;

   Many clients are concerned about protecting their assets. They want to make sure that the assets remain in their family and are used to benefit family members. In particular clients are concerned about:

   (a) Spendthrift children or those with addictions;

   (b) Their surviving spouse passing assets to their children and not a new partner;

   (c) Their beneficiaries being divorced and forced to split their inheritance with their spouse;

   (d) Their beneficiaries being made bankrupt particularly those in high risk occupations, or in highly leveraged businesses;

   (e) Looking after children with disabilities;

3. The advantage of the separation of control and benefit in testamentary trusts protects the assets of the trust from legal action involving the beneficiaries personally;

4. Tax benefits of distributions to minor children. At this time, they are taxed as if they are adults, at normal marginal rates, and not at the penalty rate for income received from an ordinary inter-vivos family trust (Latin for "between the living") – so made during the donor's (the person giving the asset) lifetime;

5. Further tax benefits for the distribution of income, capital gains and franked dividends to the beneficiary who can use them in the most tax efficient way.

Disadvantages

1. The ongoing cost. They require more ongoing administration than an outright gift such as yearly tax returns and possibly legal advice. There should be sufficient assets in the trust to warrant the expense;

2. Care must be taken that income distributed to a beneficiary is spent on that beneficiary so that a large loan account does not build up in their name perhaps undermining the main beneficiary's position, or becoming available for a claim in a beneficiary bankruptcy;

3. There may be a claim by a disgruntled beneficiary or family member. In a purely Discretionary Testamentary Trust particularly where the primary beneficiary does not have full control, the beneficiaries are in fact left nothing. They only have the fond hope of the testator that the Trustees will "do the right thing";

4. If the beneficiary does have full control, by being the sole Trustee, then the protection in a case of bankruptcy is lost as they have the power to distribute the whole of the income and/or capital to themselves. For this reason there should always be 2 Trustees;

5. The beneficiaries may simply not want the Trust arrangement. They may want to receive their entitlements from the Estate immediately. This may lead them to make a Family Provision Claim asserting that no proper provision has been made in the Will for them. This can lead to expensive and protracted Court proceedings.

6. The Trust may no longer be appropriate at the time of death because assets have been dissipated or distributed during the lifetime of the Will maker.