



## *The Way to Go Out*

### *A challenging and complicated task to achieve simplicity for your clients*

By Tony Crilly

I was moved the other day by a story told by a friend of mine who attended a funeral of an avid motorcycle enthusiast. At the funeral there were specific directions for the helmet of the deceased and his leathers to be placed on the coffin and during the church service one of his best friends revved a Ducati motorcycle outside. Everybody has individual wishes about how they want to depart and perhaps it is more important for those who are left behind than the one leaving.

*In my view this applies to the estate planning process in its entirety.*

Whether it is the transfer of a property or dictating the terms of a valid will, your wishes should be properly documented. Recently, I have found that retired clients seek greater simplicity in their estate planning documents. Quite often the key document is a binding nomination for death benefits to be paid from a self-managed superannuation fund. I always recommend that our clients have a separate company to act as trustee of a SMSF. In this way, all of the investments can be made in the name of that company as trustee and if one person of a couple should die, then no change to the name of the trustee holding the investments need occur. A surviving member can act as sole director of a trustee company without the need to involve another person or relative.

Consideration really needs to be given to whether it is appropriate for a child of a member to act as trustee to make up the minimum requirement of two individuals as trustee of a SMSF.

The directions in the will are also important; there should be a clear appointment of an executor as a director and shareholder of a trustee company.

In the case of second marriages and mixed families, it can sometimes be crucial to ensure that a binding nomination is properly effected.

By appointing an independent executor as director and shareholder of a trustee company for the purposes of administration, there is a greater chance that the wishes of a deceased will be carried out.

Sometimes this can be complicated because the assets in the fund are largely property-based and a sale program needs to be implemented to achieve sufficient cash to pay out the death benefit.

Often this is covered with a binding nomination stating that the member's account is to be paid as a percentage, or entirely to the legal personal representative to be distributed in accordance with the terms of the will. It is also important to keep in mind that if the death benefit is paid to an estate trust, then there may be significant protective mechanisms and tax advantages for the chosen beneficiaries.

Some of the key mechanisms contained in a testamentary trust in a will include:

#### ▼ **Family proceedings**

If a beneficiary is subject to proceedings in the Family Court, the executors can assume control of a trust established in a will to protect the capital. Of course, it is always going to be taken into account in relation to the relevant resources of the parties, but not directly as divisible matrimonial property.

#### ▼ **Bankruptcy**

If the primary beneficiary is the subject of insolvency proceedings, then they should be deemed ineligible to act as trustee exercising any discretion over an estate trust. It is important to keep in mind that it is a discretionary trust and there is a wider class of beneficiaries that must be considered in making gifts of capital or income.

Once that person is clear of bankruptcy, they may be reappointed to act as trustee of their estate trust.

#### ▼ **Disability**

If, due to some unfortunate accident, a primary beneficiary suffers a severe disability and requires care, the executors, or alternative trustees, can be appointed to act on behalf of that person. This ensures that the capital and income of the trust is preserved for the benefit of that person suffering the disabling event and they can continue to manage the money during that period. If it is only of a temporary nature and the person recovers, they can then be deemed eligible again to act and resume

their role as trustee. If it is a permanent situation, then it is essential to have the alternative trustee continue to invest the funds for the benefit of that person and their care. It might also include consideration of the other beneficiaries such as their children or other dependants.

### **Life of a trust**

It is difficult to express in a simple way all that might be required during the life of a trust set up in a will. Potentially, it can have operation for up to eighty years from the date of death. Given that some of these estate trusts may have substantial capital derived from the estate, the life of the trust could be over several generations. It is quite common that they have a cascading effect, such that if a child, as a primary beneficiary of an estate trust, should die or become disabled, then their children are to take that person's interest and, on the same terms, this could have a splintering effect on the capital and ultimately the terms of the trust will be very important.

Clients generally want to say what they want to do with their money in one page. Clearly, if the benefits of a discretionary testamentary trust are to be incorporated, this is almost impossible. To cater for clients who want protective mechanisms and the ability to distribute amongst a wider class of beneficiaries, a simpler version of a testamentary trust can be drafted.

This becomes challenging from a legal perspective because you risk eliminating a specific power for the trustee that may be required in the future.

For example:

*What specific provision must be made for the trustee to set aside capital of the fund to purchase a primary residence for a primary beneficiary? Does there need to be a separation of the general power to purchase real estate and to purchase real estate for use and occupation by a primary beneficiary?*

These are the questions that need to be carefully considered when drafting a testamentary trust in a will.

### **Conflicts**

Conflict situations need to be considered very carefully when appointing more than one trustee. Often there are two trustees acting as executors and continuing trustees of an estate trust. If those trustees are at loggerheads about the sale of an asset during administration and investment of the proceeds for the future life of the trust, who decides? Clearly, it is undesirable to have the trustees spending the beneficiaries' money running off to court to have a judge resolve their dispute. This is expensive and uncertain and may not in the end achieve the result that anybody desires.

A common recommendation is that a defaulting dependant trustee be appointed for the purposes of resolving disputes between trustees. Many clients prefer a trusted accountant or financial adviser, even though there may be some conflict of interest given their role.

It is critical to understand the relationship between a discretionary family trust set up during a person's lifetime and the ownership of assets. Clients often misunderstand the role of that separate trust and confuse the right of ownership inside that trust of an asset. Clearly, there is no absolute entitlement from a trust unless the trustee has resolved to vest money or property in a particular beneficiary.

In addition, there are more often than not beneficiary loan accounts on the balance sheet of the family trust that need to be taken into account. For instance, if, over many years of investment, a family trust has allocated in each tax year income to a beneficiary, but it has never actually been paid, this will create a beneficiary loan account. These loan accounts can be large and can be called upon by the executor to be repaid. If it was the intention to leave certain beneficiaries in control of a family trust and certain beneficiaries to have the benefit under a will, there can be problems.

Rather than dealing with the overall estate plan as a total wealth solution, there can be greater benefit in having the beneficiary loan accounts repaid to the estate and form part of the testamentary trust contained in a will. This is because the beneficiaries, perhaps being the children of the deceased, may have children themselves. A testamentary trust has certain protective mechanisms and the benefit of being able to distribute income to children under eighteen years of age, without them being taxed at adult rates. A family discretionary trust does not have this ability.

The administration, in the future, of a family trust can also be an issue. Once again, that issue of a deadlock between two individual trustees can cause problems and legal expense. The fact that there is total discretion about distribution of capital and income can cause disharmony between family members. The opportunity to *split* or *clone* trusts has been lost due to recent changes in the tax legislation. Previously, family trusts could be split on parallel terms and different children appointed as the controllers of those trusts after they were split. Now, the full assets of the trust will be assessable for CGT on the split or clone of a trust. Clients generally do not want to take that path given the costs to the estate. A better result can be achieved by vesting the trust in the deceased and distributing to estate trusts through the terms of the will.

So, undeniably it is a complicated process, even though clients seek simplicity. In the end, it is their choice about *the way to go out*. A client's wishes should always be observed; they know their chosen beneficiaries better than we do and, as long as they understand the consequences, that is fine. One item that is never usually negotiable is the ability of the trustee to amend the trust, allowing a second opportunity to rectify any powers that have not been included but should have been due to the specific desires of the client.

It is a challenging, but interesting area of the law and one which will no doubt cause disputes in many families. The harder families work at getting it right whilst they have the opportunity, the better the outcomes generally are in the long run.