

SUCCESSION LAW

ESTATE PLANNING

What is Estate Planning?

Estate planning is the shorthand term given to arranging your affairs and planning the transfer or administration of your assets after your death in an appropriate manner.

Estate planning means putting your affairs in order to ensure an efficient distribution of your estate. It involves planning and documenting your wishes for after your death. Done properly, estate planning helps to ensure that your family and beneficiaries receive the full benefit of your assets without excessive fees, taxation liabilities or disputes between them. It can also help you to better manage your affairs now, while you are alive.

Main Issues

The issues which should be considered in estate planning include:

- (a) the taxation, including capital gains tax consequences of the transfer of assets by you;
- (b) asset protection;
- (c) income protection;
- (d) protection of beneficiaries;
- (e) family law issues (particularly potential exposure to claims made by spouses or partners of children);
- (f) ownership and control of assets;
- (g) income tax and CGT consequences of the disposal of assets by beneficiaries;
- (h) other revenue issues such as stamp duty;
- (i) claims made by family members contrary to a testator's wishes;
- (j) providing for family members in special circumstances; and
- (k) providing appropriate mechanisms after your death, for the ongoing administration of the assets in your estate for the benefit of the people you wish to benefit.

Wills

A Will can be an important tool to enable the restructuring of the ownership of family assets which will occur on your death. It is the most basic tool for estate planning and is the most critical part of the overall management of your financial affairs after you die. But it is not the only part since a Will can only deal with the assets which you actually own when you die. Other considerations arise such as how assets are owned (e.g. as joint tenants so that they automatically pass to the survivor outside the Will), trusts and superannuation funds.

Capital Gains Tax (CGT)

CGT arises on the disposal of almost any asset in Australia. Death itself is generally not a CGT event.

However, the subsequent disposal of assets by beneficiaries will trigger CGT in many cases.

Consideration must be given to the CGT consequences of any proposed distribution of assets by a testator. Estate planning seeks to minimise the CGT consequences of inheritances such as by taking advantage of roll-over relief in certain circumstances. As well, it may be desirable to "even up" the division of assets between beneficiaries after taking into account the CGT liabilities that will arise if particular beneficiaries inherit particular assets or by forgiving or releasing debts owed to the testator.

Testamentary Trusts

A testamentary trust is simply a trust created by a Will and therefore only comes into effect on death. Under the present law, children who receive income from a trust established by a Will (a testamentary trust) are generally treated as adults for income tax purposes. It is particularly important to ensure that the trust instrument (i.e. the Will) satisfies the requirements of the relevant legislation governing the drafting of Wills and also takes proper advantage of the income tax relief granted to children by testamentary trusts. This means that the income flowing from the trust to minor children will be treated as "excepted trust income" and will therefore:

- (a) be subject to the usual adult tax-free threshold; and
- (b) only be subject to tax at the ordinary progressive rates applying to adults.

Taking proper advantage of these rules can greatly improve a family's overall tax position if one of the parents dies.

Post Mortem Trusts

If a testator dies without establishing a testamentary trust, some "after death" tax planning is possible. This could, for example, include:

- (a) settling some or all of the inheritance on a child (so that the income generated by the settlement is treated as "excepted income"); or
- (b) settling some or part of the income on a trustee for the benefit of a child, so that the same treatment will apply.

However, these "post mortem trusts" have a number of inbuilt restrictions so that, for example, the excepted income levels for tax purposes may be significantly reduced. It will also be necessary for the relevant assets to eventually vest in (i.e. become the property of) the beneficiary. A testamentary trust, on the other hand, can continue for a number of generations while a "post mortem trust" cannot.

Family Discretionary Trusts

Family discretionary trusts often provide significant tax and asset protection benefits. However, they may not

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enable the same tax benefits to continue after death. If all your assets are held in a discretionary trust, there may be no benefit to be gained from utilising a testamentary trust in your Will. Accordingly, consideration must be given to the consequences of death on the discretionary trust and whether all your assets should continue to be administered by the discretionary trust. Estate planning involves reviewing and determining who will take effective control of any existing or future discretionary trusts when you die.

Family Companies

Significant family and business assets are often controlled by proprietary companies. The question of who should control the family company, both before and after death, is often an important issue. Control may be affected by rights or restrictions on shares or issuing additional shares. Consideration must therefore be given as to who will control these assets by controlling the family company after you die, and also whether mechanisms should be built into the company's constitution (memorandum and articles) to deal with death and succession issues.

Superannuation

Superannuation can be an effective estate planning tool, particularly if a self-managed superannuation fund (SMSF) is employed, perhaps together with binding nominations. Superannuation proceeds may be paid to the estate (and therefore be governed by the Will) or they may be paid directly to a particular family member or dependents without passing through the estate (and so fall outside the scope of the Will).

Investments in a superannuation fund provide a very effective and protected environment. Consideration should be given as to who will control the trustee of the SMSF following death, and who the members of the fund should be. As well, it may be necessary to decide whether lump sum pay-outs should be made or directions should be given for pension streams or annuity payments. The range of tax-advantaged beneficiaries from superannuation funds, however, is more limited than under other arrangements such as discretionary trusts.

Insurance

Mostly people wish to ensure that their surviving family continue to enjoy as high a lifestyle as possible after their death. If there are insufficient assets in the estate to provide this, it may be advisable to take out additional life insurance to fund payment of debts and/or be available for family members. In some circumstances it may also be advisable to flow the insurance pay-out through a superannuation fund. If a beneficiary has been nominated for a life insurance policy, the nomination overrides the Will and the proceeds of the policy do not form part of the person's estate. Taxation, asset protection, flexibility and access questions arise as well as the purpose and likely consequences of such insurance.

Mutual Wills Agreements

In many cases, particularly involving blended families, people wish to ensure that their own children and other dependants will continue to inherit from them even if they die before their partner. They also wish to ensure that the assets which they have acquired during their lifetime will be protected and available for their beneficiaries when their partner dies. Since the law generally allows freedom of disposition by Will, and since Wills can generally be amended or revoked at any time, one method of providing greater certainty for survivors is for the testators to sign a mutual wills agreement.

Family Provisions Claims

Many members of a person's extended family and other people who are "dependent" in a very wide sense, may have a claim on a person's estate. Generally, people making the claim must establish need as well as the inadequacy of the provisions made for them or failure to make provision for them at all. In these matters, the court has regard to the assets in the estate as well as what the testator did or did not do in relation to his property before death. The court can also take "notional estate" which was no longer owned at death, into account. The court can decide that the estate should be distributed differently to the manner stated in the Will. Consideration must therefore be given to family histories and relationships as well as to the consequences of things which have occurred before death or would occur under the Will.

Special Beneficiaries

If a potential beneficiary is disabled or impaired or if other particular circumstances affect the beneficiary (e.g. alcohol, drugs or membership of an undesirable group) or if they are unable to look after their own affairs for some other reason, then it may be necessary to establish a protective trust or make other particular arrangements under the Will.

Other Aspects

Other aspects that should be taken into account in estate planning include:

- (a) potential claims by creditors of beneficiaries;
- (b) claims by spouses (including spouses of beneficiaries); and
- (c) claims by partners (including de facto and same sex partners).

Conclusion

For effective estate planning, a thorough appreciation of all the relevant circumstances and objectives is necessary. This involves knowing and understanding the testator's:

- (a) existing structures and estate planning arrangements;
- (b) age, health and family;
- (c) assets and liabilities, both actual and contingent;
- (d) overseas assets;
- (e) wishes as to inheritance of assets; and
- (f) commercial and other objectives.

Expert professional advice and assistance should be obtained for your estate planning.

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