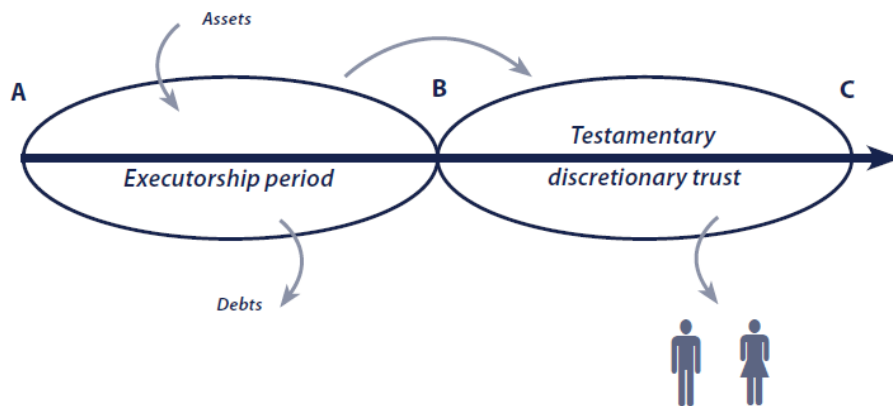


Testamentary discretionary trusts

- 1 A testamentary discretionary trust is a trust established in someone's will. It comes into existence only when the person dies. A lineal descendant testamentary discretionary trust is a trust established in someone's will for the benefit of their lineal descendants.



- 2 Let's assume that someone died at point **A**. The executor's job involves finding all the assets, paying out any debts and usually, at point **B**, distributing what's left to the beneficiaries.
- 3 If there is a testamentary discretionary trust, part or all of what's left remains in the estate and is distributed later – at any time between point **B** and point **C**, depending on the terms of the will. Point **C** can generally be up to 80 years from point **A**.
- 4 A will can establish more than one testamentary discretionary trust.

Who controls the assets?

- 5 Whoever is named in the will as trustee controls the trust assets. Like any trust, a testamentary discretionary trust can be as flexible or as fixed as you like. The trustee can be given full discretion or no discretion as to who should receive income and capital from the trust and when they should receive it.
- 6 The trustee is often the same person who was appointed as executor, and can also be a beneficiary. For example, a parent can establish a testamentary discretionary trust for each child's inheritance. Each adult child can be the trustee of their own trust, and may also be an executor.

Using testamentary discretionary trusts to split income with young children

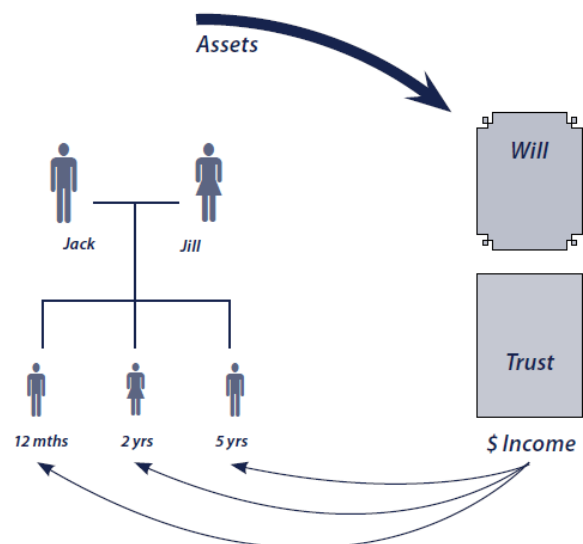
- 7 As an estate planning strategy, this can be of benefit:
 - (a) for families with small children;
 - (b) where extra income would be needed to support the surviving families should a parent die; and
 - (c) where minimising tax is important.

How does it work?

- 8 A testamentary discretionary trust is simply a trust established by someone's will.
- 9 Rather than all the deceased's assets being distributed by the executor upon death, some or all of the assets remain in trust for the benefit of a specific group of beneficiaries named in the will.
- 10 Trust income distributed to children, of any age, will be taxed at adult rates rather than the penalty rates that normally apply to minors' unearned income.
- 11 The trustee can have full discretion as to who receives trust income and capital, or restrictions can be provided.

Example

- 1 Jack included a testamentary discretionary trust in his will.
- 2 When he died, Jill used the trust to distribute income to herself and the children.
- 3 Jill was the trustee.
- 4 She was able to receive \$82,168 tax free each year for herself and the children.

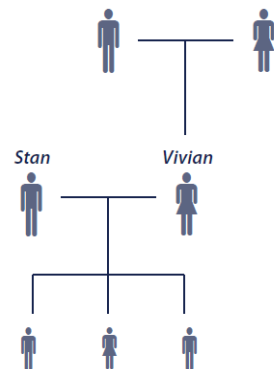


Estate planning and asset protection

- 12 Most people would be more than happy to receive an inheritance. However, for those who have put in place asset protection strategies or who could be facing bankruptcy, this can cause a problem.
- 13 People in financially high risk occupations, such as professionals, business owners and company executives, will often prefer not to receive inherited assets in their own names.
- 14 One solution is to include appropriate provision (such a testamentary discretionary trust) in the wills of people likely to leave them assets.

Example

- 1 Vivian owned and ran a high profile design company.
- 2 She had deliberately ensured that most of her assets were in her husband's (Stan's) name. At least this way, if the business went bad, their home and savings would be protected.
- 3 Unfortunately, when Vivian's parents died, she received the family beach house in her name.
- 4 Though the business was doing well, its future success was not guaranteed.
- 5 To protect the beach house from a possible trustee in bankruptcy, she transferred it to a trust – and paid \$23,000 stamp duty. This expense (and any capital gains tax) could have been avoided if Vivian's parents had included a testamentary discretionary trust in their wills.



Why use a lineal descendant trust?

- 15 A lineal descendant trust (**LDT**) is established for your lineal descendants – your children and grandchildren, and on down your lineal family tree. A properly drafted LDT can assist in keeping an inheritance out of the reach of the Family Court where a beneficiary is involved in a family law property dispute.

Protect inheritances from the in-laws

- 16 Many parents are concerned that the inheritance they leave to their children could end up in the hands of a son-in-law or daughter-in-law if their child's marriage breaks down.
- 17 If a child receives an inheritance in their own name, that inheritance will generally be intermingled with the child's other assets (e.g. by paying off a mortgage) and thus will become 'matrimonial property' available for distribution by the Family Court.
- 18 However, if you give each child their inheritance in a separate LDT provided for in your will, those assets can be kept apart and protected from direct distribution (even if income from the assets is reinvested within the trust from time to time).
- 19 How successfully the assets are protected depends on how the will and LDT are drafted and the circumstances at the time of drafting.

Example

- 1 When Mary died she left her only son Jack an inheritance of \$520,000.
- 2 Jack had been married to Jill for 10 years at the time. They separated shortly after.
- 3 Jack and Jill's matrimonial property amounted to \$300,000 after the mortgage was taken into account.
- 4 In determining the property settlement, the Court took into account Jack's inheritance. However, because of the terms of the LDT that held those funds, they were not available for distribution to Jill.
- 5 Jill got \$150,000 rather than the \$410,000 she might have otherwise received. She received half of the matrimonial property but no part of Jack's inheritance.

Information Source – This information has been provided by elawyer pty ltd.