



## Testamentary Trust Wills

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### What is a Testamentary Trust?

A Trust is an obligation for a person or an entity (“Trustee”) to hold property for the benefit of beneficiaries. A Testamentary Trust is a Trust established within a valid Will and comes into effect upon the death of the Will maker. Incorporating provisions for a Testamentary Trust in a Will makes the administration more complex if the Trust is activated.

In many cases where a Will has testamentary trust provisions, each beneficiary (usually the spouse and/or children) is given the option of whether to take the share given to him or her either in their own right or in a Testamentary Trust. The beneficiary may, at the time the estate is being administered, consider his or her then circumstances. This gives flexibility.

### Why have a Testamentary Trust in a Will?

There are a number of benefits for certain beneficiaries to receive the share of the estate into a Testamentary Trust.

#### 1. Potential bankruptcy and asset protection

In the case of a beneficiary who is operating his or her own business, either solely or through a corporate entity where guarantees may be given, or a professional liable to a claim for damages for negligence (for example a doctor or lawyer), or other person at risk of bankruptcy, the share of an estate received into a Testamentary Trust means that it cannot be accessed by creditors of the nominal beneficiary.

#### 1. Relationship breakdown and asset protection

If the intended beneficiary is in a situation of possible relationship breakdown, then there may be protection of the assets held for the benefit of that beneficiary if held in a Trust. Those assets are not classed as “assets of the beneficiary” although they may be treated as “financial resources”

available to the beneficiary. Generally, the Family Court cannot make an order requiring distribution of those assets to the other partner. But it may be important to put special provisions in the trust to ensure that the beneficiary is not in sole control (or considerable control) of the Trust.

## 1. Protection of minor, spend thrift or disabled beneficiaries

Where there are beneficiaries of an estate who are minors or have difficulties managing their financial affairs, are vulnerable to pressures or have a disability, then establishing a Testamentary Trust can protect their inheritance. This is usually referred to as a “protective trust”. Another person or persons is appointed as Trustee/s to control the investment and distribution of funds. The distribution may be of capital or income, either as directed in the Will or it may be determined at the discretion of the Trustees in their wisdom, from time to time.

## 1. Tax advantages

Like a Family Discretionary Trust, it is possible to distribute income to beneficiaries of the Trust on lower tax rates. But there is a significant advantage for a Testamentary Trust under current Australian tax laws, for potential beneficiaries under 18 years. In the case of a Family Trust, only \$416.00 per annum can be provided to a minor tax free. But in the case of a Testamentary Trust, up to \$18,200.00 per annum can be distributed to persons under 18 years tax free. (*\* these figures current as at March 2021*)

Thus, where the intended primary beneficiary is already a high-income earner, but he or she has or is likely to have young children, there are significant advantages in creating a Testamentary Trust as income can be distributed to minors (often through the parent) and used for the maintenance, education (school fees) and advancement of the child under 18 years.

## Operation of a Testamentary Trust after the Will maker dies

When a person dies, the executor named in the Will has duties to collect the assets of the estate and distribute the net estate according to the Will. Where a Testamentary Trust is created in a Will (and a beneficiary opts to take his or her share of the net estate in the form of a Testamentary Trust), then assets are transferred in the first instance to the executor, and the executor transfers those assets to the Trustee/s of the Testamentary Trust.

There is usually documentation to record the transfer especially if the executor and the Trustee are one and the same (often a spouse). The ATO does not treat that transfer as an event for CGT purposes.

The Trustee/s of the Testamentary Trust can then invest the assets (or maintain the investment in their then form including real estate) and if appropriate, over time change the investments as required.

The Testamentary Trust operates as a separate Trust to the deceased and the estate of the deceased. A Tax File Number separate from the deceased and the deceased's estate must be obtained for this new Trust.

Under trust and tax laws, the Trustee must keep proper records of investments, income, expenses and distributions and prepare financial statements, usually at least annually. The fees incurred depend on the complexity of the Trust investments.

The Testamentary Trustee has the liabilities of any other Trustee, both at common law and under the *Trustee Act*.

## Number of Trustees appointed

If more than one person is appointed as the **initial** Trustee, then the *Trustee Act* provides that a Trustee cannot resign or be discharged unless there are two Trustees to continue to act.

Frequently two Trustees are appointed in circumstances where there is a beneficiary who is vulnerable or in need of protection.

## Existing Family Trust of Will Maker

The assets held by a Will maker in a Family Trust are not assets of that person to be left in a Will. However, loan accounts owed by or owing to the Family Trust are assets or liabilities of the estate on death.

If the assets are in a Family Trust, there is no point in including those in a Testamentary Trust. However, special provision needs to be included for shares in any Corporate Trust or power of appointment in the Trust Deed held by the Will maker.

## How long does a Testamentary Trust last?

The Trustee of the Trust may vest (end) the Trust at any time and distribute the assets.

In South Australia, the rule against perpetuities has been abolished and there is no limit to the time the Trust may last. But after 80 years from date of death of the Will maker, the Supreme Court can, on the application of a person interested, order that the Trust vest (be ended). Unless the assets in the Testamentary Trust are very significant, it is likely that the assets will be distributed long before 80 years from date of death.

In other states, the Trust must end within 80 years and the assets be distributed. Some Trusts created outside SA specifically provided that the law of South Australia apply to them.

## Costs of Testamentary Trust Wills

The legal costs to advise on, obtain instructions for and create a Testamentary Trust Will are substantially more than a “simple Will”, given the complexity involved.

There can be various options and alternatives to discuss depending on the extent and type of assets of the Will maker.

## Further information

For further information about testamentary trust wills, please contact us.

## Contact Daenke Lawyers

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