SMSFAdviser

# Could a testamentary trust help secure wealth transfer?

***By Keeli Cambourne, Deputy Editor, SMSF Adviser and Matthew Burgess, Director, View Legal***

With the government circling around super with a raft of changes and legislative policy amendments combined with the latest suggestion that superannuation be 'ring-fenced' to pay for aged care, many SMSFs are beginning to look to wills and discretionary testamentary trusts to help protect inheritances and ensure they go the distance for beneficiaries.

Matthew Burgess, director of View Legal, said in light of fundamental changes to the taxation regime and the expanding wealth of Australia's aging population, there is a growing need for estate planning to utilise appropriate structuring.

A testamentary discretionary trust is a discretionary trust set up in a will. It differs from the main type of discretionary trust that is set up by a trust deed while the beneficiaries are still alive. This latter type is called an inter vivos trust by lawyers and a family trust by everyone else.

"It is well established that wills utilising testamentary trusts should be the starting point for any comprehensive estate planning exercise to ensure wealth passes efficiently to the intended recipients and that the transfer takes place at the intended time," he said.

"The difficulty in many estate planning exercises is that serious attempts to devise and implement a plan are often not made until some 'triggering event' stimulates action."

Mr Burgess said often the triggering event, such as marital breakdown or illness, can jeopardise putting appropriate strategies in place.

Many solicitors are now also recommending them thanks to tax benefits and protection from kids' estranged spouses.

"Most trusts are governed by a trust deed which sets out how the trust must be run, what the trustees can do in running the trust and who the beneficiaries are," Mr Burgess said.

"Discretionary trusts have been used as a tax effective asset-owning vehicle for a long time and as such there are a number of trusts that are governed by trust deeds that were drafted when the tax and trust laws were significantly different."

One of the primary benefits of an SMSF testamentary trust is the protective barrier it forms around the assets from family law and creditor claims.

The structure ensures the assets within the trust are not held directly by the beneficiaries, thereby shielding them from potential legal disputes or insolvency proceedings.

According to law firm Abbot and Mourly, a discretionary trust enables the trustee of the trust to:

1. Distribute capital to a range of beneficiaries (a person receiving a capital payment or asset of the trust)
2. Distribute income to beneficiaries including streaming specific types of income such as dividends, capital gains, interest and foreign income
3. Conduct business and other operations including investment for the benefit of the beneficiaries of the trust

The trustee has a wide range of discretion which it exercises generally each year, no later than 30 June, so that the trustee is not taxed on the trust's income at 45 per cent. By streaming income and specific types of income enables the trustee to spread the income around ensuring that the tax liability is spread across the family thereby lowering overall family average tax rates.

Plus having assets in a trust protects them from beneficiary and trustee creditors.

Mr Burgess said an SMSF testamentary trust also offers a safeguard against family provisions claims on the estate. By circumventing the estate and directing super benefits into a testamentary trust, the exposure to litigation is minimised, ensuring these assets reach the intended beneficiaries.

He said often testamentary trusts are structured to limit the range of beneficiaries to “lineal descendants”, where the will maker restricts the discretionary powers of the trustee so they may only distribute income or capital (or both) to the will maker’s children and grandchildren, excluding any spouse of the children and/or grandchildren.

“It is necessary to review a trust deed periodically to ensure that it allows the trustees to operate the trust in the most tax-effective way,” he said.

“Generally, testamentary trusts are seen as particularly useful to ensure concessional tax treatment is available to distributions of capital and income to infant beneficiaries as well as to protect accumulated wealth from wastrel or spendthrift beneficiaries.

“They are also good to ensure infant children or disabled beneficiaries are cared for and to help protect inheritances from attack by the Family Court and trustees in bankruptcy as well as avoiding an unintended loss by a beneficiary of their government-sourced pension or other benefits, although there is limited scope for this.”