

TESTAMENTARY TRUSTS

1. WHAT IS A TESTAMENTARY TRUST?

A testamentary trust is a trust that is created by a Will and only comes into existence on the death of the will maker. Similar to other trusts that can be created during your lifetime, testamentary trusts can be fixed or discretionary.

2. ADVANTAGES OF USING A TESTAMENTARY TRUST

2.1 **Taxation Advantages**

Under a testamentary trust, any income distributed to minors is taxed in the same way as if the minor was an adult, and the full tax free threshold and marginal rates thereafter apply to all income distributed to any minors.

Example

For example, if you had a property worth \$1,000,000 which was rented for \$50,000.00 per year, the calculations below show the difference between leaving the assets to your spouse, and leaving it in a Testamentary trust:

If left to your spouse, the \$50,000.00 per year income would be taxed solely as your spouse's income. Tax on the first \$50,000.00 of income is approximately \$8,550.00 (subject to access to rebates/concessions and not including Medicare levy)

If you had three children who were minors and the same asset was left in a Testamentary trust for the benefit of your spouse and children, the Trustee could distribute \$6,000 to each of the children tax free (Total \$18,000.00) and your spouse would only pay tax on the remaining \$32,000.00. Tax on \$32,000.00 is approximately \$3,900.00.

This would allow your spouse and three children to have access to at least \$24,000.00 tax free each year, saving them approximately \$5,000.00 in tax per year.

2.2 **Asset Protection**

A further advantage of a testamentary trust is that it enables you to quarantine certain assets for the benefit of your beneficiaries until they reach a certain age.

Examples:

- Assets of the trust would not be available to creditors in the event of any beneficiary going bankrupt.
- Protection of assets from any claims in the event that any of your beneficiaries go through any property settlement with an ex spouse.
- Keeping assets in a Testamentary trust, with someone other than beneficiaries involved in the role as trustee can mean that assets are not available for beneficiaries to use at their discretion and can be protected for the benefit of beneficiaries in the event that your beneficiaries, for example, having a gambling problem, are not able to manage their own financial affairs or suffer from a disability.

3. FREQUENTLY ASKED QUESTIONS

3.1 **Who controls the assets in the trust?**

The person appointed Trustee of the trust holds and controls the assets of the trust for the benefit of beneficiaries. The will-maker can appoint the trustee. For example, each of your adult children could be the trustee of their testamentary trust or your spouse could be the trustee of the trust created for the benefit of themselves and any minor children. The Trustee would then have control of assets and they can have significant discretion about how assets can be used or invested.

3.2 **Why would I want a testamentary trust?**

- Reduce tax for beneficiaries on income earned on assets by splitting income.
- Protecting beneficiaries who cannot manage their affairs.
- To set aside assets to be used to care for minor children.
- To set aside assets to be used to care for beneficiary with a disability.
- To quarantine the gift to beneficiaries from property proceedings if they are involved in family law dispute.
- Protecting inheritance from creditors of a bankrupt beneficiary.
- Protecting beneficiary from reduction to Centrelink benefits in certain circumstances.