

Business Results Limited

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TRUSTS

What is a trust?

Many centuries ago an adventurer was travelling to a distant land. He said to a friend, "Here is my money, use it to look after my family while I am away". The adventurer (Settlor) had created a family trust. The friend had become the trustee. The family members were the beneficiaries. When we talk of a family trust we are doing the same thing as the adventurer did except we usually stay in New Zealand!

Sometimes the settlor would hand some written instructions to the trustee. This document is called a trust deed.

After a time people started to consider questions such as:

- Could the settlor be a trustee?
- Could a trustee be a beneficiary?

The answer is anyone can be any of the three, settlor, trustee or beneficiary. Theoretically one person could be all three *so long as* there is at least one person who is a beneficiary and not a trustee or settlor.

Most, if not all solicitors advise their clients to have an independent trustee, someone who is not a beneficiary and maybe not even a close family member.

We endorse this advice! If you ask us to be a trustee then we will be happy to act for a passive trust but it will be through a company which we will specifically set up to be your trustee.

A trust cannot carry on indefinitely; they must wind up 80 years after they were established.

Benefits of Trusts:

- 1 Protection from Estate Duty. It could easily be reintroduced.
- 2 Protection against claims from creditors, which include bankruptcy. Anything owned by a trust does not belong to you so cannot be taken away. If you are bankrupted the trust has to have owned the assets for two years at the time of your bankruptcy.
- 3 If your income is derived from a trust, your national super is likely to be protected against a super surcharge or other means test.
- 4 Rest home subsidy protection. The government usually reviews all transfers to a trust over the previous five years.
- 5 Asset protection for children and grandchildren.

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- 6 Trust can be used as a final beneficiary under wills, reducing the risk of estate duty for a surviving spouse.
- 7 Protect capital against irresponsible children.
- 8 Flexibility to cater for differing beneficiary needs.
- 9 Ease of administration of deceased estate.
- 10 Distributions to beneficiaries can save some tax.
- 11 There can be some protection of assets in the event of a relationship breakdown.

Some Things To Look For In A Trust Deed:

Solicitors prepare trust deeds, and store them as standard forms in their computers. They personalise these to suit the client. Read your trust deed carefully and make sure you understand it and it suits your needs.

Also, since a word processor has been used, make sure there are no errors like having someone else's family as beneficiaries. It has happened!

If you cannot understand it, ask us! Some of the things which we suggest you should ask your solicitor to consider including in a family trust are:-

- Specifically exclude the prudent person requirements contained in the Trustee Amendment Act 1988 to minimise any risk of beneficiaries challenging the actions of trustees at a later date. Further, the prudent person rule will often not suit many small family trusts, particularly, for example, if the intention is to invest in real estate only.
- If it is a husband and wife family trust make sure the trust deed gives power to both to hire and fire trustees. Sometimes standard trust deeds give the power to the husband only.
- Include an express power to resettlement a trust. That means transfer everything to a new trust.
- Make sure the clause dealing with voting of trustees suits you. I.e. who has power to make decisions?
- Discuss "license to occupy the family home" with the solicitor - if you want to hasten the trust's ownership. It may help you speed the transfer of ownership but there can be disadvantages.
- It is usually best to give the maximum possible powers to your trustees. You may wish to cater for after thoughts by giving trustees the power to add beneficiaries.
- Watch out for any clause excluding a spouse from being a beneficiary if he/she should remarry. These clauses are not uncommon in wills. Do you really want to impose this restriction on your spouse in a trust?

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What should you put in a trust?

You transfer assets to a trust by selling them at their current value. The trustees record the purchase price as a debt owing to you. Any gain in value (e.g. from your home) from the date of the sale belongs to the trust. We recommend that the assets you put into the trust are appreciating assets, like your home or other real estate, shares, etc.

We recommend that you assign (or transfer) your life insurance into the Trust as well. The advantage of this is that the proceeds flow directly into the Trust. Usually, after death, the cash payout is much quicker as the all the Trust has to do is produce the Policy document and the death certificate.

You should then further enrich the trust by making gifts to it. The maximum gift anyone is permitted to make, without paying gift duty, in any twelve months period is \$27,000. There are a few minor exceptions such as ordinary presents to the family. Remember, if you exceed the maximum, you are required to pay gift duty which is on a sliding scale.

You can sell as many assets to the trust as you like. If your reason for having a trust is to protect assets, as it should be, then sell as much as you can and make yourself poor. The exceptions to this rule are:

1. If it is a disadvantageous from a tax perspective.
2. If it is going to be significantly more costly to account for the assets in the trust than it would be if you continued to hold them in your own name.

Memorandum of Wishes:

Because a Trust may have to last for a long time – up to 80 years – Trust Deeds are very seldom specific, say 'my house is to be split between my family in equal shares'. Thus the Trustees usually have very wide powers. These powers are referred to as discretionary. In other words the Trustees can decide as they go along who, amongst the beneficiaries are in need of their help.

However you can, as settlor, add a document to the Trust Deed which, although not binding on the Trustees, gives them instructions as to what you would like to happen. In other words you can suggest a limit as to how much they distribute to whom. It is good sense to ask your legal advisor about a Memorandum of Wishes.

Power of Appointment:

As mentioned above all Trusts contain a clause about the appointment of Trustees, and who holds that power! We believe that this is one of the most important clauses in the Deed and that power of appointment should be yours, absolutely! When you die you should give that power of appointment to some one that you trust. This can be done through your will, which is why we recommend that you have new wills drawn up when you set up a Trust – see below.

Wills:

It is important that your will is reviewed and, if necessary updated, from time to time. This is particularly so when you set up a Trust as you should pass on the Power to Appoint Trustees in your will. Now it may be that the person to whom you are passing this power is also your executor under your will but, also it may not be!

Secondly, it is important in your will to forgive (or remit) any debt that the Trust owes you as at the date of death. This means that the Trust gets to keep all the assets that you have

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given to them rather than some of those assets coming back, on your death, into your estate.

Finally, you can also leave any assets to the Trust in your will. You may have bought something in your own name instead of buying it in the trust's name and this takes care of this oversight.

So, review and, if necessary, amend your will when you set up a Trust.

Taxation:

Income earned by a trust does not belong to its beneficiaries unless the trustees decide to distribute the income to them. While a trust may, it does not have to distribute any income to beneficiaries. A trust is therefore useful as a method of avoiding paying income tax at 39%.

Important things to remember:

- Always keep trust's finances separate from all others.
- Sometimes a trust should have a separate bank account.
- Trustees may allocate some or all of the income to beneficiaries but this must be done within 6 months of balance date, usually by 30 September each year. Contact us early.
- Minute all your decisions **and then** carry them out. Otherwise it may be difficult to prove whether a transaction was on behalf of the trust or a beneficiary.
- All trustees must sign minutes, if the trust deed requires this. It is no good getting an "independent" trustee's signature later.
- When distributing to beneficiaries, ensure the minute contains the words 'having considered the interests of all beneficiaries.....' It is important to show their interests were all considered before the decision was made. See us for a suitable form of trust minutes.
- When lending money to your trust, usually by selling assets to it, record the loan as being "interest free repayable on demand." Interest free loans, which do not have this qualification, can be deemed gifts, possibly subject to gift duty.
- It is best to let your solicitor carry out the transfer of assets to the trust and to produce the deed which sets out the debt that the trust owes you.
- It is also better to let the solicitor carry out the gifting program, to ensure that each and every year the debt is reduced by the maximum. If you want to gift faster than the \$27,000 each person can gift in anyone year, remember, gift duty will be payable!
- Keep beneficiaries informed. It is recommended you send them copies of the trust's accounts.
- Avoid lots of small transactions to keep the costs of accounting down.

Finally!

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A Trust is NOT the same as a company. Companies have advantages if you operate a business just as Trusts have advantages for the accumulation of assets that are appreciating.

Please talk to us before you rush off and set up a Trust. We recommend that if you decide a Trust is a good option for you then you, ourselves and your legal advisor should sit down and confirm the best approach for you.

WARNING:

The information supplied here is simplified and condensed. It is only a guide and should not be relied upon as a substitute for professional advice.