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Did You Know?

When the electoral rolls closed for the 2007 federal election, 13.6 million Australians were registered to vote. Financial Demographics estimate that 2.5 million Australians aged 18 and over, are not registered to vote.

Source: www.findem.com.au

Testamentary trusts

In the previous issue of Timely Tips we mentioned the importance of having an Enduring Power of Attorney in place. Following a request from a reader, we are looking at Testamentary Trusts in this edition. If you would like to see specific topics addressed in future editions of Timely Tips, please email your request to TimelyTips@profinvest.com.au

A testamentary trust is a trust that is created on the death of a person by the operation of their Will. For example, the Will might include a bequest along the lines of *"I wish to leave the sum of \$10,000 to my son Matthew, once he attains the age of 18 years"*. If Matthew is currently under 18 years of age, then the funds will be held in trust for him until such time as he turns 18. In this example, a testamentary trust has been created.

Whilst a testamentary trust is very useful when wishing to have minors (i.e. children under 18 years of age) benefit from an estate, they may also be created to cater for adult beneficiaries, particularly for those under legal disability and in other circumstances where it may be prudent for the bequest to be held back from the beneficiary for distribution over an extended period or at a later date. For example, take the case of a beneficiary who is currently an undischarged bankrupt. If they were to receive an inheritance whilst an undischarged bankrupt, the inheritance could be claimed by the administrator of the bankrupt's estate for distribution amongst creditors. In such a case, it would be desirable for the proceeds of the estate not to be distributed until such time as the beneficiary's bankruptcy was discharged.

A testamentary trust may also prove useful in the case of the "spendthrift" beneficiary. That is, a beneficiary who can't manage their money effectively. This may arise as a result of the beneficiary having a drug or alcohol addiction, physiological problems, or simply compulsive spending habits. In these circumstances, a testamentary trust may allow for the bequest to be "drip fed" to the beneficiary over time, perhaps to assist with meeting their living costs,

children's education and the like. One further area where a testamentary trust may prove to be a very effective vehicle is in cases where a beneficiary of a deceased's estate is in receipt of social security benefits (e.g. the age pension). Benefits of this type are generally subject to an assets and an income test. Provided the social security benefit recipient is not also a trustee of the testamentary trust, the distribution of the bequest may be structured to occur over time so to have minimal impact on the beneficiary's entitlements to Government benefits.



Distributions for an estate via a testamentary trust can be structured in a number of ways. For example, the trust may provide for a distribution of income only (i.e. investment income earned on the underlying capital of the trust), a distribution of capital, or a combination of both. Generally distributions from the testamentary trust to the underlying beneficiaries will be made at the discretion of the trustee unless specific directions are made such as in the example mentioned earlier (*"once he attains the age of 18 years"*).

When a minor received unearned income, that income is generally subject to very high tax rates. In general terms, the first \$416 of unearned income is taxed at 0%, the next \$890 at 66%, and anything over \$1,306 at a rate of 45%. However, the more favourable adult tax rates apply where a minor receives income distributions via a testamentary trust.

getting you from **a** to **b**

Whilst a testamentary trust may be a very useful structure to distributing an estate's assets to beneficiaries who are minors, they can also be effective when distributing assets to adult beneficiaries.

Effective estate planning is a specialised area of advice and should not be approached on a "DIY" basis. Unfortunately hardly a week goes by without hearing examples of poor estate planning. This can often lead to a deceased person's estate ending up in the wrong hands, or being disputed, often resulting in a breakdown of family relationships. With this in mind, the services of a good solicitor who is competent in estate planning, along with an effective Will, can result in the right funds getting to the right people, at the right time, and in the most tax effective manner.

Source: Peter Kelly – Professional Investment Services

Changes to terminal illness benefits



Whilst the general thrust of a life insurance policy is to pay a pre-determined benefit to the policy owner in the event of the death of the insured person, many life insurance policies include a "terminal illness benefit". A terminal illness benefit is effectively the advance payment of the sum insured when a person is diagnosed as being terminally ill. Being terminally ill is defined in the relevant life insurance policy as not expecting to survive for a specified period of time, generally 6 months or 12 months.

The payment of a terminal illness benefit allows for the proceeds of the insurance to be paid out prior to death thereby allowing the life insured to help get their financial affairs in order whilst still alive.

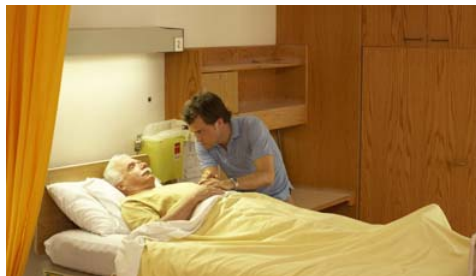
Many people hold their life insurance cover through superannuation. One of the difficulties that arose in the past relates to the payment of a terminal illness benefit where the life insurance cover was held through

superannuation. Take this simple scenario – Fiona is currently 47 years of age. She has life insurance through her superannuation fund and has recently been diagnosed as being terminally ill. She meets the requirements for payment of her insurance benefit under the policy's terminal illness benefit. The claim is admitted and the policy proceeds are passed to Fiona's superannuation account. Fiona now wishes to access her superannuation entitlements in order to get her financial affairs in order. In the first instance, as her superannuation benefits are preserved, she will need to meet a condition of release in order to be able to access her benefit. Being terminally ill, she may well be able to access her superannuation benefits on the grounds of being totally and permanently incapacitated, however this will depend on her personal circumstances.

Assuming Fiona meets a condition of release and is able to access her superannuation benefits, she now has to deal with the taxation consequences of accessing her superannuation benefits early, which could significantly reduce the amount of superannuation benefits she receives.

On 11th September 2007 the Government announced that, effective from 12th September, where a superannuation benefit is paid as a result of a person being diagnosed as being terminally ill, the benefit will be paid out tax free, irrespective of their age at the time of payment. Of course, a condition of release still needs to be met for the benefit to be paid prior to retirement.

This change represents a sensible and compassionate breakthrough for people who have the misfortune of being diagnosed as terminally ill and wish to attend to their affairs prior to death.



The relevant legislation to enact the changes has not yet been passed by parliament but the Australian Taxation Office has announced that measures have been put in place to implement this change effective from 12th September 2007.

Source: Peter Kelly – Professional Investment Services

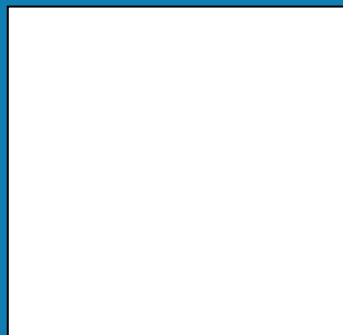
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