



# Estate Planning and Testamentary Trust Wills



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In recent years the term "Testamentary Trust" has been used to describe what is usually a Discretionary Family Trust established under a Will. Their popularity arises from the considerable benefits that can flow from their establishment under a Will. A number of these benefits arise from the fact that the assets of the trust while they may be controlled by a potential beneficiary, do not form part of that beneficiary's estate. This feature means that a beneficiary's inheritance through a testamentary trust can be highly beneficial in a number of circumstances.

## Bankruptcy

Unfortunately, the incidence of bankruptcy in our society has increased significantly. Often a wife will guarantee her husband's business venture and vice versa. To some extent we can all be at risk whether in traditional high-risk occupations or not. However, if the bankrupt's inheritance has been provided through a testamentary trust it will be protected from creditors.

## Divorce

As with creditors, an inheritance held within a properly prepared testamentary trust is unlikely to be the subject of a Family Court order in the case of a marriage breakup. It may be regarded as a financial resource and have some effect on the terms of a property settlement but this is a preferable outcome to the property being at the disposal of a Family Court order.

## Pension Benefits

The assets of a testamentary trust are not currently taken into account in establishing pension eligibility under the current means tested pension rules. However, income from the trust is taken into account for income test purposes.

## Spendthrifts and people with disabilities

It is not uncommon for people suffering a variety of disabilities to be unable to properly manage their financial affairs. At the same time, families wish to ensure that an adequate fund is set up to meet their reasonable needs but so as not to affect any pension rights they may have. The flexibility of a testamentary trust, especially if combined with a memorandum of wishes as to how the trust should be administered, can be an appropriate arrangement.

## Taxation Advantages

Although the above features are in themselves good reasons to consider a testamentary trust in your will, the major basis of their popularity is the considerable tax savings which can arise under Section 102AG of the Income Tax Assessment Act 1936 (I.T.A.T.). The effect of this section is that children under the age of 18 years who receive income from a testamentary trust are taxed on that income as an adult and therefore enjoy the normal tax free threshold (\$5,400.00 or \$6,150.00 if the low income rebate applies) and marginal tax rates which apply to adults. Without this special provision of the I.T.A.T. trust income to minors has a tax free threshold of only \$416.00 (or \$643.00 if the low income rebate applies) and thereafter the highest marginal rate applies to the minor's income.

The following example illustrates the advantages of establishing a testamentary trust compared with a traditional will provision.

Assume a husband dies leaving a dependant wife and three infant children. His estate is valued at \$500,000.00. If this were invested at (say) 8% per annum, it would generate an income of \$40,000.00.

## Traditional Will

Example 1: The husband's Will leaves everything to his wife. Her tax position (ignoring the Medicare levy) is therefore:

Beneficiary	Income	Tax	Net Income
Wife	\$40,000.00	\$8,380.00	\$31,620.00

## Testamentary Trust Will

Example 2: The husband's Will establishes a Testamentary Trust providing for the wife and three children to be beneficiaries. The family's tax position might be:

Beneficiary	Income	Tax	Net Income
Wife	\$10,000.00	\$ 680.00	\$ 9,320.00
Child 1	\$10,000.00	\$ 680.00	\$ 9,320.00
Child 2	\$10,000.00	\$ 680.00	\$ 9,320.00
Child 3	\$10,000.00	\$ 680.00	\$ 9,320.00
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	\$40,000.00	\$2,720.00	\$37,280.00
	=====	=====	=====

In example 2, the total tax bill is \$5,660.00 less than in example 1 and this level of saving may be possible for many years.

## Testamentary Trusts can be attacked

Even though a testamentary trust may be considered by a Will-maker to be a prudent provision for family members, like all provisions of a Will, it may be attacked by certain "eligible applicants" under a Family Provision application. The surviving spouse, children and certain dependants have a right to challenge a Will in this way. While there are strategies that may be used to frustrate or restrict family provision claims, they are unlikely to result in the same benefits provided by a testamentary trust.

## Never too late!

The I.T.A.T. provides a second chance to the family of a will-maker who has not established a testamentary trust. This second chance must be taken advantage of within three years of the date of death of a deceased. It enables a trust to be established from assets derived from the deceased and for the income to enjoy the same tax advantages as income derived through a testamentary trust. However, the effect of the provision is that the sum which may be used to establish the trust cannot exceed the amount which the "beneficiary" would have received from the deceased's estate had the deceased died intestate ie. without a Will.

## New Trends

Increasingly the traditional husband and wife Will ie. each to each other and then to the children is being replaced by a testamentary trust controlled by the surviving spouse and under which the spouse and children are potential beneficiaries. Wills along these lines can if the funds in the trust justify it provide that on the death of the spouse, sub-trusts come into existence for the benefit of each child and that child's family (and would be controlled by the child concerned). Increasingly, grandparents are providing education trusts for their grandchildren which have the added advantage of maximising the tax-free income that can be applied for the benefit of the grandchild.

## Conclusion

Testamentary trusts, while largely promoted as a tax saving mechanism have many other advantages. Their inherent flexibility makes them worthy for consideration in your overall estate planning strategies.

At Attwood Marshall we have a team that deal with Business Structuring, Asset Protection Planning, Wills, Estate Planning & Testamentary Trust matters. Our solicitors can assist you in making an estate plan so your assets are protected.

For enquiries regarding Estate Planning and Testamentary Trust Wills please contact Lesley Barnes on (07) 5506 8241 or by email [lbarnes@attwoodmarshall.com.au](mailto:lbarnes@attwoodmarshall.com.au).



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