

I LOVE REAL ESTATE PROFESSIONAL SERIES

# THE SMSF & ADVANCED STRUCTURE ONLINE TRAINING EVENT 2020



*How Smart, Savvy Real Estate Investors Use SMSF And  
Advanced Asset Protection And Structure Techniques  
To Maximise Their Portfolios*



# 3. ADVANCED STRUCTURING, TRUSTS, ASSET PROTECTION & LEGAL STRUCTURES

DEREK SKY &  
HILARY SOMERVILLE

# THE SMSF & ADVANCED STRUCTURE ONLINE TRAINING EVENT



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Derek Sky  
and  
Hilary Somerville

The information provided is of a general nature only. This is not intended to be a substitute for legal advice.  
You should take legal and accounting advice specific to your situation before undertaking any investment decisions based on this presentation.

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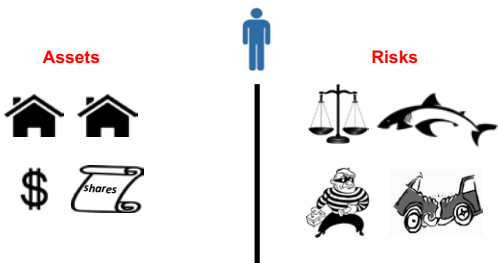
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## What is Asset Protection ?

Asset protection is the separation of assets from risk.



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## Life Without Asset Protection

All of your assets are exposed to your personal risks.  
If you face liability, your assets may be lost.



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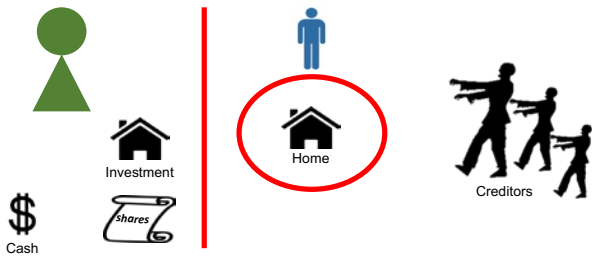
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## Life With Asset Protection

All of your assets are still exposed to your personal risks.  
However, assets held in structures are protected.



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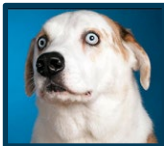
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## Asset Protection – Why Bother ?

Asset protection is something that should concern everyone.  
Some examples are relatively rare...



**Vet Sues Client  
for Defamation**  
Facebook and other online reviews  
lead to significant costs.

**Meth House: Gold Coast  
Family Sue Agent**

**Tenant sues over electric  
shock from light fitting**  
The 50 year old suffered an electric  
shock after touching an exposed wire he  
had asked to be repaired.

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## Common Risks – Business Risk

If a business fails, the business owner will be at risk from:

- lenders (the business overdraft or equipment finance);
- clients who have not had their products or services delivered;
- the landlord of the business premises;
- suppliers of trading stock or materials;
- business partners;
- employees for unpaid wages or superannuation;
- the ATO for unpaid taxes and super guarantees.



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## Common Risks – Loss of Value

Investments may fail.

If an investment loses value, that can impact on other assets you own.



If a flood, for example, causes the value of a property to drop, you may not have sufficient equity in the property to pay out a loan.

If the loan must be repaid, other assets of yours will be used by the bank to meet the debt.

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## Who Needs to Protect their Assets ?

Everyone should consider asset protection.

More than 27,000 personal insolvencies in Australia in 2018-19.

Consider your risks:

- business
- investments
- hobbies
- spouse
- family



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## The Asset Protection Tools

Separation of assets from risks:

- trust and company structures.

Minimising risk:

- insurance for professional risk;
- good practices, such as a safety checklist; and
- document for business relationships:
  - shareholders agreement;
  - joint venture agreement;
  - buy / sell agreement.



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## What are Structures ?

Asset protection structures might be called 'structures', 'entities', 'vehicles'.  
They are separate legal entities.



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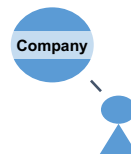
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## Types of Structures

- Companies
- Trusts, which include...
  - Discretionary trusts
  - Unit trusts
  - Hybrid trusts
  - Bare trusts
  - SMSFs



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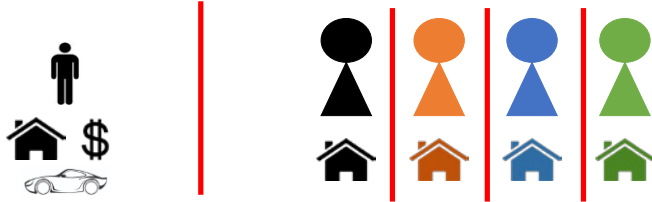
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## Asset Protection Through Structuring

Structuring works because there is a legal difference between you and your structures.  
The assets and liabilities of your structures are separated from you.  
The structures are also separated from one another.



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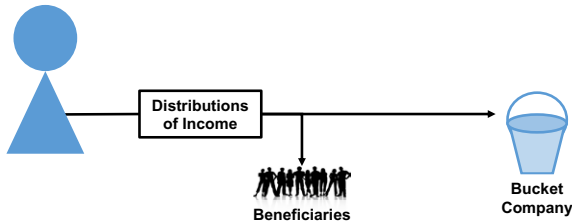
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## Other Benefits of Structures – Tax Planning

Asset protection structures also provide tax planning advantages.

Discretionary distributions can be made to beneficiaries with lower tax rates.  
Corporate beneficiaries (bucket companies) can allow access to the company tax rate.



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## Other Benefits of Structures – Succession Planning

Asset protection structures may make succession planning simpler.  
You can leave control of structures to certain beneficiaries.

Asset protection structures may protect your estate from a claim or the impact of a claim. (Except in NSW.)

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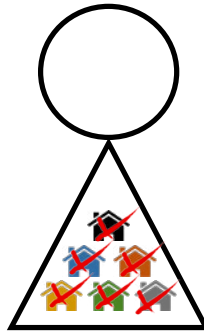
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## Limits on Structures – Risk Within the Structure

The assets owned by a structure are **all** vulnerable to that structure's risks.

Consider the risks within the structure.  
Assets within one structure should be limited.



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## Limits on Structures – Your Roles of Risk

Directors of companies can be held liable.

Biggest risk for the director of the corporate trustee of an investment trust is guaranteeing borrowings from a bank.

A personal guarantee allows a bank access to the director's personal assets to pay the structure's debts.



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## Limits on Structures – Tax Planning Limits

Structures may not be useful for negative gearing.

If you have a tax strategy which requires offsetting personal income with losses, a structure may not assist.

Discretionary trusts cannot distribute losses.

Take accounting advice.



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## When to Consider Asset Protection

The best time to consider asset protection is right now.

There are important events to re-consider your asset protection:

- receiving a lump sum of money (inheritance, sale of an asset)
- when you are acquiring an asset (property, business or your home)



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## When to Establish a Structure

Get market ready when you are ready to go to market.



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## How Long Does it Take to Establish Structures ?

It depends upon the type of structure.

A good timeframe is 1 – 2 weeks.  
Structures can be established urgently.



In States with nominee provisions, you may have more time.  
Take advice from your lawyer or conveyancer on the process.



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## What if You Have Already Signed a Contract ?

It depends where the property is.

In States with nominee provisions, you may be able to set up the trust after contract and nominate the trust as the buyer.

Take advice from your lawyer or conveyancer on the process.

In the other States, it may be too late.

You may be able to rescind the contract and enter a new one.

Beware double stamp duty!



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## Who is Involved in a Structure ?

The roles in a structure are critically important. The choice of person will affect:

- Serviceability
- Control
- Succession planning
- Who can receive income



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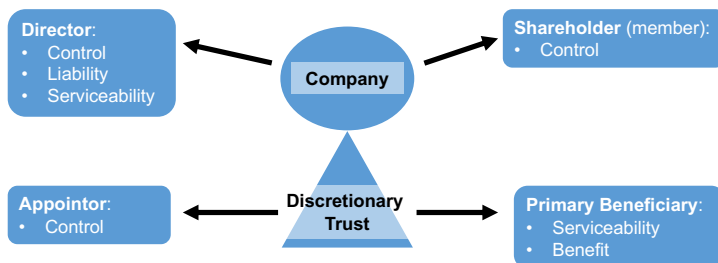
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## What do the Roles Involve ?



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## How is a Structure Established ?

You should establish structures with professional assistance.

You require legal and accounting advice.

It is not 'one size fits all'.



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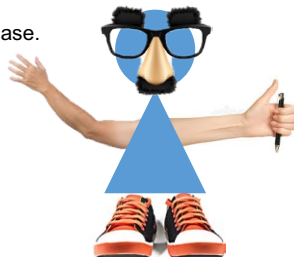
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## Running Your Structure

The structure is a separate entity.

The structure applies for finance.

The structure signs the contract for purchase.



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## Structures Must be Run as a Separate Entity

You must run your structure as a separate entity.

Decisions should be reflected in Minutes.



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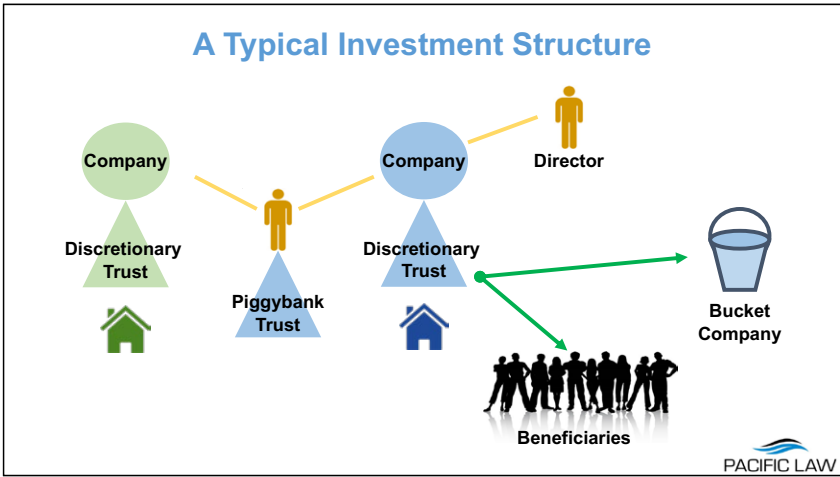
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### You Have Your Structure, Now What ?

The next steps might be:

- deciding upon the right investment strategy
- finding the right investment property
- applying for finance
- contributing funds required for the investment

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### Contributing Funds to a Trust

You have your investment structure, now what?  
Where does a trust get money to purchase property?



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## Gift or a Loan ?

Is the interest tax deductible?  
Where is the equity held?

Depends upon the source of the funds.

Interest on a loan is tax deductible.  
Interest on a gift is not tax deductible.



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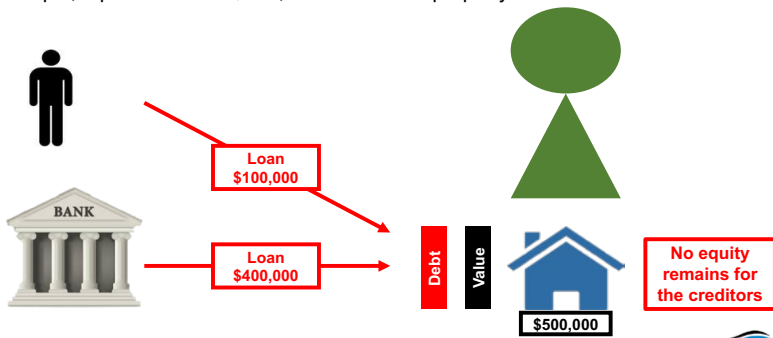
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## Loaning Funds to a Trust

Example, a purchase of a \$500,000 investment property.



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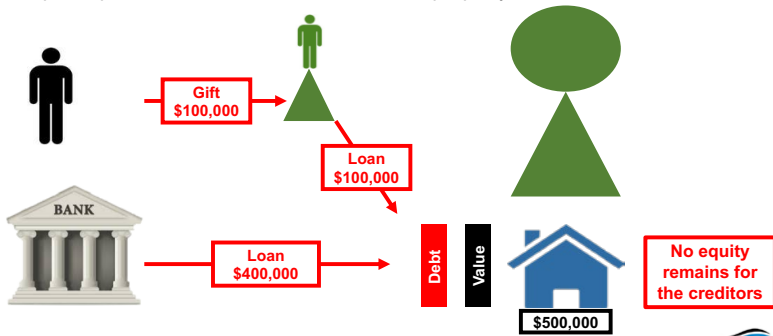
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## Giftting Funds to a Trust

Example, a purchase of a \$500,000 investment property.



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## The Terms of a Loan

The loan from you to your investment trust:

- should be in writing
- should specify the terms (interest rate, repayment date)
- can include interest (eg the same rate as the source of funds)

**Evidence** is required for:

- ATO, State Revenue
- Creditors

**Details** are required for your accounting records.



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## Protecting Existing Assets

If you are already in a position where you hold assets and you are concerned about risk, there are steps which can be taken.



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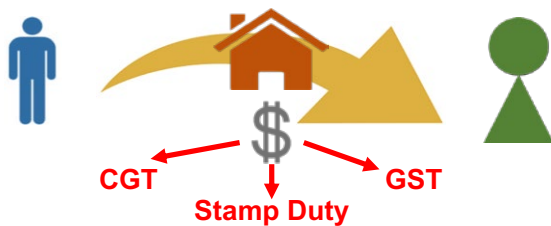
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## Asset Protection by Transferring Assets

Transfer of assets can move the asset away from risk.

However, the cost of the transfer is likely to be high.

A transfer of a fixed asset may attract capital gains tax, stamp duty and GST.



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## Protection of Equity in Existing Assets

A **Gift and Loan Back** arrangement is used to protect the equity in existing assets.

The arrangement involves a gift of funds to the piggybank trust and then borrowing those funds back again.

This works in two ways:

1. it reduces equity exposed to your risks; and
2. allows for security to be registered over existing assets.



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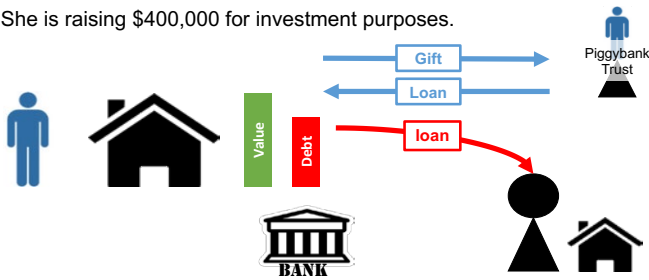
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## The Gift and Loan Back – an Example

Our example is Maria.

Maria owns her home which is worth \$500,000.

She is raising \$400,000 for investment purposes.



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## Clawback

Clawback applies to transaction which are for less than full value.

Assets can be brought back into your bankrupt estate.

Clawback might be applied to:

- Transfers made for less than market value
  - Time limit (2 years, 4 years or 5 years)
- Transfers to defeat creditors
  - No time limit
- Transfers by third parties to defeat creditors



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## Security

Whenever money is loaned, including to related parties, you must consider if security is required.

Security might be a mortgage or a caveat.



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## Asset Protection for a New Home

Your home will generally be held personally rather than by a trust.  
The owner should be the lower-risk spouse.

Consider:

- past risks
- current assets
- borrowing capacity



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## The Equity in a New Home – What is at Risk ?

Funding a new home provides an opportunity for asset protection.  
Remember, it is the equity in the property which is subject to your risks.



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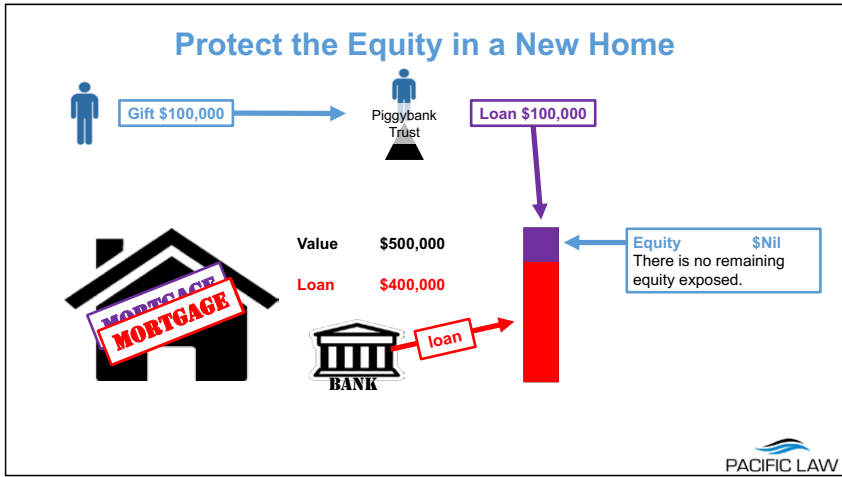
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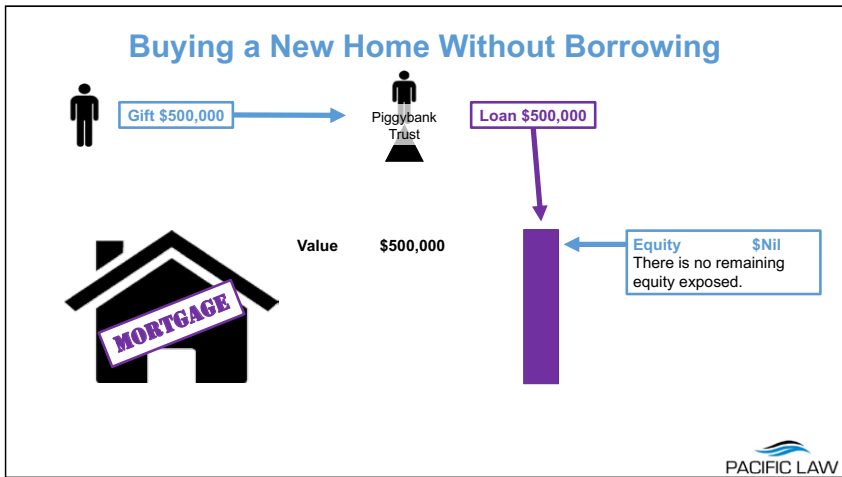
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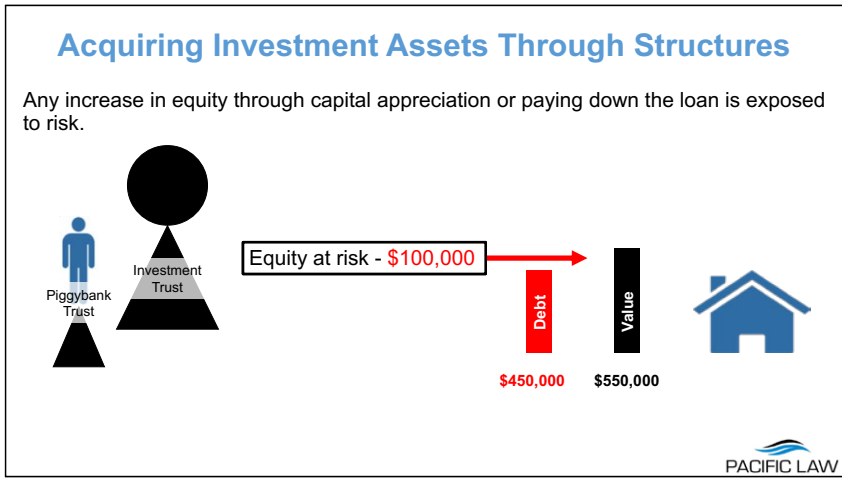
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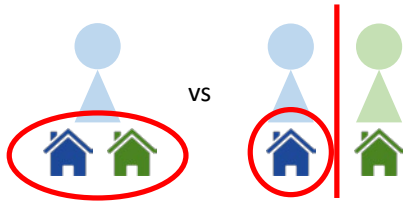
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## What About a Second Property or Project ?

A trust can hold multiple assets. The question is whether it should.

Saving costs vs Quarantining risk



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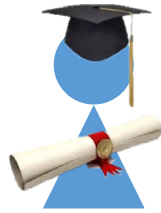
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## Advanced Structures

More advanced structures include:

1. Larger project structures, such as unit trusts;
2. Structures to make your career as a property investor easier, such as:
  - Admin trusts; and
  - Consulting trusts;
3. Joint venture structures.



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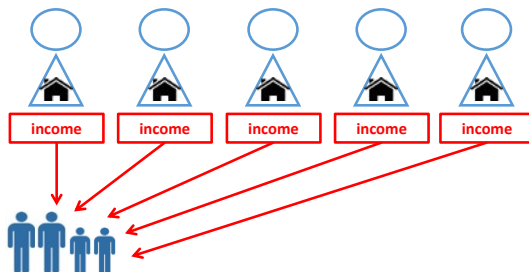
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## Admin Trusts

An admin trust is used to simplify administration of multiple investment properties.

Usually...



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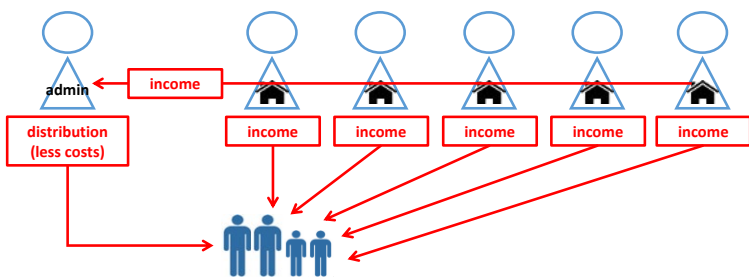
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## Admin Trusts

With an admin trust...



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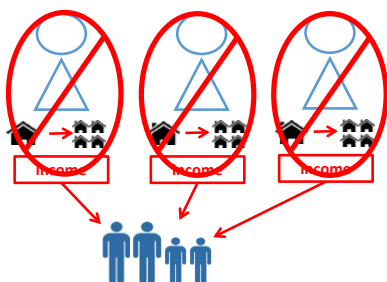
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## Consulting Trust

A trust used to provide a steady stream of income.

Usually...



Each structure's income is separate.

The banks will not be comfortable treating the profits as a steady, reliable income for borrowing purposes.

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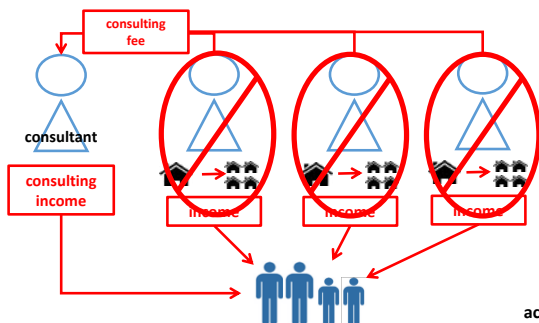
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## Consulting Trust



The consulting trust is kept long-term.

The bank will treat the income as a steady source of income for borrowing purposes.

\*Take advice from your accountant and loan broker\*

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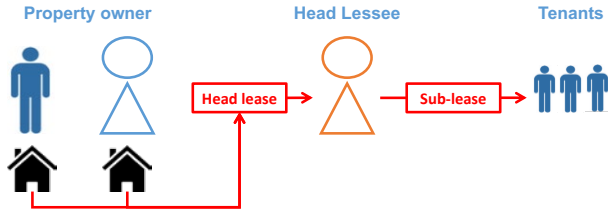
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## Head Lease Trust

The head lease trust is used to take a lease of the property from the property owner and then sub-lease the property to the tenants.



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## Joint Venture Structures

The structure for the project will be driven by the deal itself.

What is each party contributing ?

**Capital**      **Borrowing capacity**  
**Time**              **Skills**  
**Finding the deal**

Are the parties contributing in the same way?

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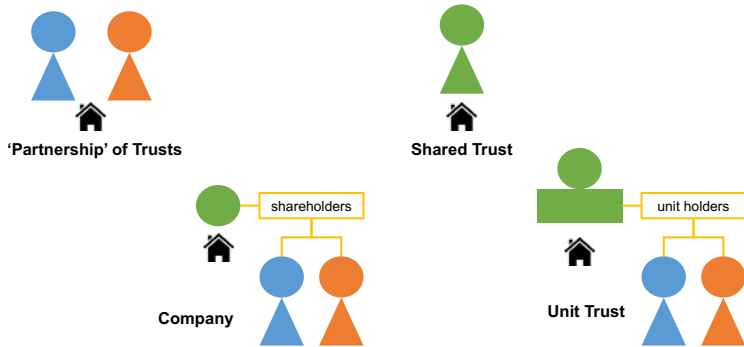
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## Joint Ventures – Joint Serviceability



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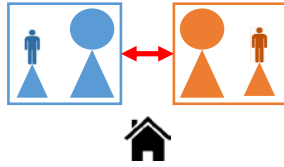
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## Partnership of Trusts

Two or more independent structures hold property as tenants in common.

### Advantages

- Fixed ownership
- Simplicity of the structure
- Independent succession



### Disadvantages

- Two names on contracts
- More challenging for banks
- Shared succession



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## Shared Discretionary Trust

Two parties shares the benefit and control of the trust.

### Advantages

- One name on contracts
- Flexible distributions



### Disadvantages

- No fixed ownership
- Dealing with losses
- Joint succession in control



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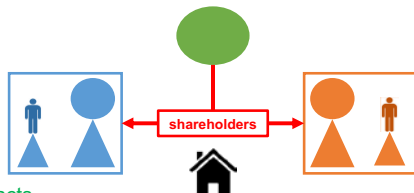
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## A Company Directly

Two parties share the control and ownership of a company.

### Advantages

- One name on contracts
- Fixed ownership
- Company tax rate



### Disadvantages

- No CGT discount



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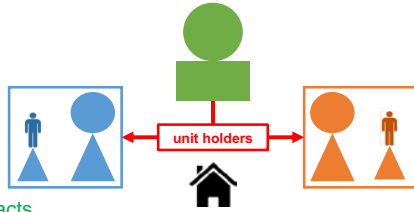
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## A Unit Trust

Two parties share the control and ownership of a unit trust.



### Advantages

- One name on contracts
- Fixed ownership

### Disadvantages

- Establishment cost
- Administration Costs




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## Joint Ventures – Worker / Capital

Capital and Serviceability Partner



Working Partner




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## Joint Ventures – Serviceability / Capital

Serviceability Partner



Capital Partner




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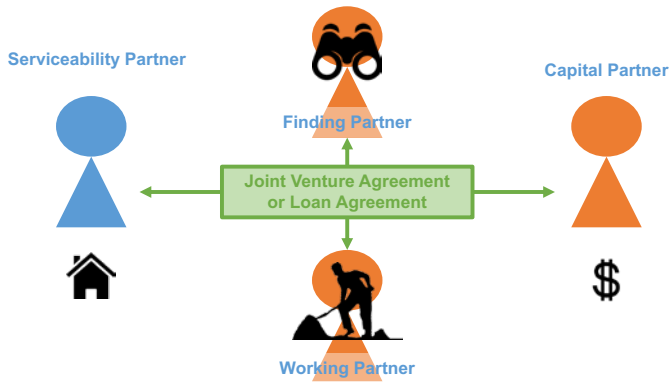
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## Joint Ventures – Complex Projects



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## Joint Ventures – The First Steps

What is the deal?  
Do you all have the same project in mind?



- Common areas of dispute:**
- Initial capital contributions
  - Further capital contributions
  - Managing the project
  - When to sell
  - How the profits are divided

Joint Venture Checklist: [www.pacificlaw.com.au](http://www.pacificlaw.com.au) under 'Learn More'

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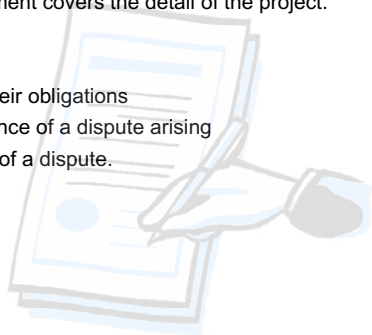
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## Joint Venture Agreements

A Joint Venture Agreement covers the detail of the project.

The advantages are:

- the parties know their obligations
- it minimises the chance of a dispute arising
- it reduces the costs of a dispute.



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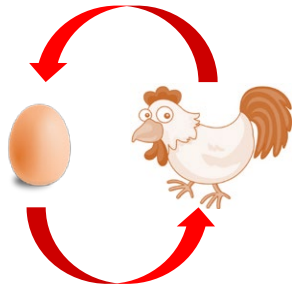
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## When is the Joint Venture Agreement Signed ?

Do you secure the property first or sign the JV Agreement first?



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## Tailored Structures

Sometimes specific advice is required to tailor a structure to particular circumstances.

This allows consideration of specific issues to do with:

- longer-term intentions
- taxation and stamp duty considerations



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## Tailored Structures – Example 1

Adam is purchasing a property **in Queensland** for \$600,000.

The unimproved land value is \$480,000.

Adam will subdivide the property, keep the existing house, build a new dwelling on the subdivided lot and retain the properties in the longer-term.

After subdivision the properties will have an unimproved land value of \$280,000 each (total \$560,000).



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### Tailored Structures – Example 1

Key issue: after the project is completed, the combined holdings will attract land tax of \$5,020 (on \$560,000).

Option: use two trusts to attract separate land tax thresholds.

Each trust holds a half share in the property with an unimproved land value of \$280,000.

This is below the threshold in Qld.

No land tax is payable, saving \$5,020 per year (less the cost of administration of the second trust).



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### Tailored Structures – Example 2

Anna and Bodhi are purchasing a property and undertaking a joint venture in New South Wales.

Anna and Bodhi will subdivide the property, retain the existing dwelling, and build a new dwelling on the subdivided lot.

Each of them wants to retain one of the separate dwellings in the longer-term.



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### Tailored Structures – Example 2

Key issue: Anna and Bodhi want to separately hold property after the subdivision however a transfer of each property from both of them to each of them separately will attract stamp duty.

Option: Anna and Bodhi can take advantage of NSW partitioning provisions to obtain a stamp duty concession.

The property is purchased in separate structures as tenants in common in equal shares. Assuming that each of the two lots created in the subdivision are of equal value, no stamp duty is paid on the partition.



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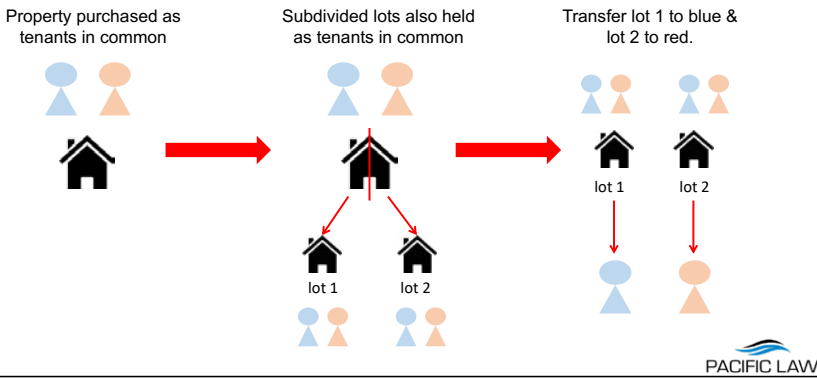
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### Tailored Structures – Example 2 – the Process




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### Tailored Structures – Example 3

Charlotte is purchasing a property and undertaking a development in Victoria.

Charlotte will subdivide the property, retain the existing dwelling, and build a new dwelling on the subdivided lot.

Charlotte will either sell or retain the old dwelling but wants to retain the new dwelling as her principal place of residence.




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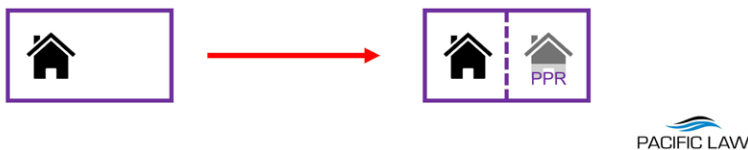
### Tailored Structures – Example 3

Charlotte can take advantage of a stamp duty concession in Victoria.

Charlotte can transfer a lot from a discretionary trust to her name personally with a stamp duty concession.

Charlotte can undertake the project, with its associated risks, in a trust structure but then take ownership of the PPR in her name personally.

This will ensure access to the capital gains tax exemption for her PPR.




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## Premium Foreign Stamp Duty

Additional stamp duty on the purchase of certain residential land by a foreign buyer.

A foreign buyer might include individuals, companies and trusts.

The premium applies in all Australian States.




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## Premium Foreign Duty and Discretionary Trusts

The premium has a very broad application to discretionary trusts.

	What is a Foreign Trust?
Qld	50% of primary beneficiaries are foreign
NSW	foreign person holds an interest of 20% or more
Vic	foreign person holds an interest of 50% or more
SA	trustee, appointor, named beneficiary or default beneficiary is foreign
WA	foreign person holds control or more than 50% of takers in default
Tas	foreign person has 'substantial interest' (all discretionary trusts)




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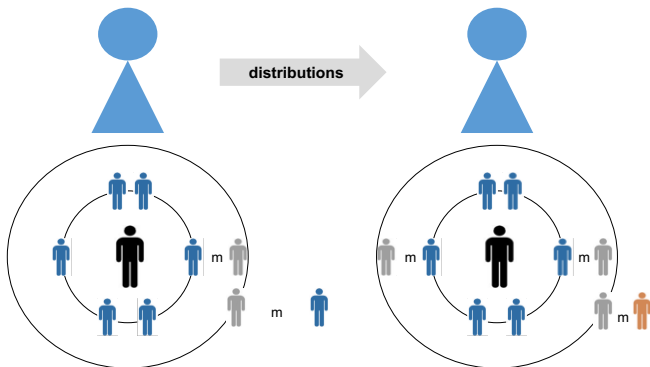
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## Foreign Stamp Duty in NSW, Victoria & Tasmania




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## Premium Foreign Stamp Duty Rates

Stamp Duty assuming a purchase price of **\$500,000**.

State	Rate	Duty	Premium Duty	Total Duty
NSW	8%	\$17,932	\$40,000	\$57,932
Vic	8%	\$25,070	\$40,000	\$65,070
Qld	7%	\$15,925	\$35,000	\$50,925
S.A.	7%	\$21,330	\$35,000	\$56,330
W.A.	7%	\$17,765	\$35,000	\$52,765
Tas	8%	\$18,247.50	\$40,000	\$58,247.50




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## Discretionary Trusts and Land Tax

The use of discretionary trusts can lead to higher land tax.

State	Individual Threshold	Trust Threshold
NSW	\$734,000	Nil
Vic	\$250,000	\$25,000
Qld	\$600,000	\$350,000
S.A.	\$450,000	\$25,000*
W.A.	\$300,000	\$300,000



\*SA has special provisions which apply from 1 July 2020.




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## Land Tax in NSW

Land tax has the biggest impact on discretionary trusts in NSW.  
Assume a purchase of property with an unimproved land value of \$500,000.

NSW Land tax for a discretionary trust - \$8,000

NSW Land tax for an individual - nil

**Does the asset protection and income tax advantage outweigh the land tax burden?**




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## NSW Land Tax Unit Trust

A unit trust structure which can access land tax threshold in NSW.

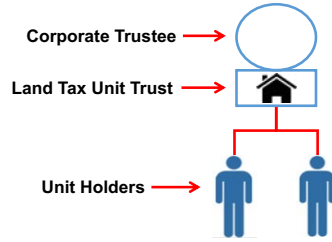
Units must be personally owned.

This reduces asset protection.

The units are exposed to the unit holder's risk.

No discretionary distribution of income.

Tax minimisation is limited.



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## Premium Foreign Land Tax

Additional land tax each year on holding land.

State	Rate	Applies to
NSW	2%	Foreign owners
Vic	2%	Foreign owners (narrower definition than Stamp Duty)
Qld	2%	Absentee owners
ACT	.75%	Foreign owners
SA, WA, Tas	NA	Not Applicable

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## Foreign Investment Review Board

FIRB rules apply to the purchase of real estate in Australia.

A foreign trust is where a foreign person has an interest of 20% or more.

FIRB rules apply throughout Australia.

The FIRB rules are complex and vary depending upon the purchasing entity and the type of land purchased.

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## Premium Foreign Duty and Land Tax - Actions

- for **new purchases** – review trusts for premium duty
- for **existing holdings** in Victoria, NSW and ACT review trusts for premium land tax
- for purchases throughout Australia consider FIRB
- amend trusts where necessary



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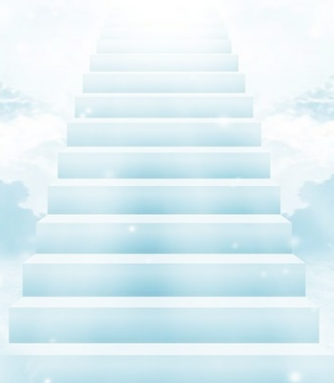
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## Succession Planning



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## Succession Planning

Succession planning is the process of making sure that in the event of your death or incapacity:

1. the right people have control of your affairs;
2. the right people receive your assets; and
3. the right people take control of your structures.

It is asset protection for your family and loved ones.



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## Succession Planning for Companies

A **director** is replaced by the shareholders.



A **shareholder's** shares pass to their estate or continue to be held by the trust.



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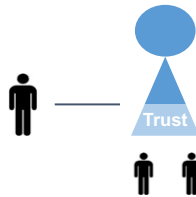
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## Succession Planning for Trusts

A person who is **trustee** is replaced by the appointor.  
A company trustee continues as trustee.

An **appointor** ceases to hold that role.  
The successive appointor takes over.



The **primary beneficiary** role does not change.



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## The Key to Succession and Trusts

Control the control.

Who will become the appointor?

Whoever takes control of a trust has discretion.

- Will the new controllers **know** what you want?
- Will the new controllers **do** what you want?



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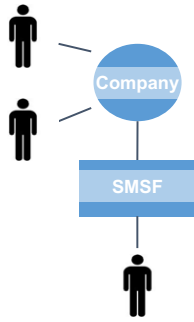
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## Succession Planning and SMSFs

A director ceases that role.  
A sole director must be replaced.

The member's share in the corporate trustee passes under their Will.

The member's death benefit is paid out.



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## How is a Death Benefit Paid

The trustee of the SMSF pays the death benefit to:

- spouse
- child
- financial dependent
- the legal personal representative of the deceased

Depending upon the recipient, the payment might be a pension or a lump sum.  
It is important to consider new changes to the rules regarding Transfer Balance Caps.



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## Death Benefit Nominations

Binding vs non-binding

- Certainty vs flexibility

Highly technical provisions

- Rules at law
- Rules under the trust deed.



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## Taxation of Death Benefits

The tax on death benefit payments depends upon:

- whether the recipient is a dependent
- whether the payment is a lump sum or income stream
- whether the funds are taxable or tax-free
- the age of the deceased person and the recipient

For a non-dependent receiving a lump sum, it may be as high as 30%.



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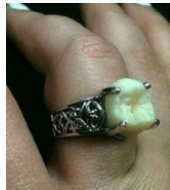
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## Succession Planning – The Role of the Will

Your Will is part of your succession planning. It will deal with:

- appointment of your executor;
- funeral directions;
  - burial cremation;
  - unusual requests;
- guardianship of children;
- gifts of your personal estate.



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## Smarter Wills – Testamentary Discretionary Trusts

A discretionary trust created by your Will.

Advantages:

- Asset protection
- Tax minimisation
- Bloodline features.



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## Testamentary Trusts – An Example

Charles dies with net assets of \$1,000,000.

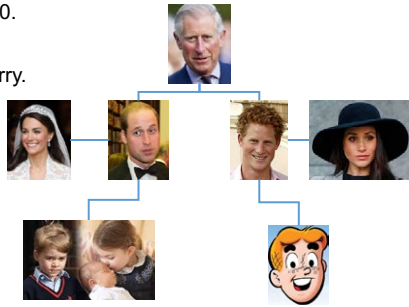
Charles has two children, William and Harry.

William is married.

William has three children:

- George
- Charlotte
- Louis

Harry has recently married and has one child, Archie.



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## TDT Advantages – Asset Protection

Personal assets of beneficiaries are exposed to their risks.

Assets held by a trust are not. The funds are protected from risk.



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## TDT Advantages – Tax Planning

Charles's estate has a value of \$1,000,000.

His two beneficiaries are William and Harry.

Each will receive \$500,000.

Assuming a simple Will, the funds are received personally.

Assuming incomes of \$60,000 for Harry and \$150,000 for William and a return of 5% on the benefit from the estate (\$25,000), the tax consequences are:

- For Harry, tax of \$8,125. (At the rate of 32.5%.)
- For William, tax of \$9,250. (At the rate of 37%.)



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## TDT Advantages – Tax Planning

Harry and William receive their gift of \$500,000 through a Testamentary Discretionary Trust structure receives the \$500,000. The income of \$25,000 is earned in the fund.

For Harry, Archie receives \$18,200 tax-free.  
Harry receives \$6,800 taxed at 32.5%, \$2,210.  
(Meghan has independent income.)  
This is a tax saving of \$5,915.

For William, tax of \$0. (George receives \$18,200 tax-free and Charlotte receives \$6,800 tax-free.)  
This is a tax saving of \$9,250.



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## TDT Advantages – Bloodline Trust

Commonly in Testamentary Trusts, spouses are excluded from benefit.

This has two advantages:

- protecting assets for bloodline descendants; and
- preventing (to some extent) the assets being exposed to the breakdown of a relationship.



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## Protecting an Estate from a Claim

You can minimise the likelihood or impact of a claim through:

- proper succession planning
- structuring an estate (except in NSW)

NSW Notional Estate.



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## Protective Trusts or Special Disability Trusts

Protective Trusts or Special Disability Trusts can protect vulnerable beneficiaries.

Very specific terms are required.



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## Enduring Power of Attorney

Appoint someone to manage your affairs during your lifetime.

- Financial decisions
- Healthcare and personal decisions

Enduring means it continues if you lack capacity.

Are there any special provisions required?

Do you need a General Power of Attorney for your companies or trusts?



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## Advance Health Directive

An Advance Health Directive allows you to specify your healthcare wishes in a legally binding way.

The effectiveness varies State to State.

A directive will help to prevent disputes among family members, as your wishes are known.



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- Property Development
- Conveyancing
- Joint Ventures
- Option Agreements
- Asset Protection
- Succession Planning
- Deceased Estates
- Franchising
- Leases
- Business Transactions

The information provided is of a general nature only. This is not intended to be a substitute for legal advice. You should take legal and accounting advice specific to your situation before undertaking any structuring or asset protection measures.

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