



Contents of a Will – Part 2

Issue 25 – 17 July 2009

Overview

Last week's Strategy Update considered the Contents of a Will pertaining to the personal circumstances of a Willmaker including timing of a Will, appointment of Executors, payments of debts and expenses, payments to specific beneficiaries, gifts to beneficiaries and the rules of construction of a Will.

What follows is Part 2 of the Contents of a Will.

1. Capital Gains Tax Consequences of Specific Gifts

In gifting specific investment assets in a Will, the Willmaker will need to be aware that not every asset is treated in the same way for capital gains tax (CGT) purposes.

There may be assets within a portfolio that are not subject to a capital gains tax liability because they were purchased by the Willmaker prior to the introduction of capital gains tax on 19 September 1985, or because the asset is a main residence. Other investment assets that a Testator holds, may not be exempt from a CGT liability.

The specific gifting of investment assets with different CGT status may bring about unintended inequality between Beneficiaries.

Implication: If a Willmaker is unsure, as to the CGT owing on an investment, advice should be sought from a financial adviser or accountant. Furthermore consideration should be given

to having liquid funds available to pay for any CGT liability. If liquid funds are available the Will should contain a clause specifying liquid funds can be used to pay for any tax consequences including CGT. Such a clause together with appropriate funding may then prevent unnecessary CGT.

2. Distribution of Personal Chattels

It is common for Wills to contain gifts of household articles and items of sentimental importance.

The principle of Ademption also applies to personal chattels. However, given that personal chattels are usually worth significantly less than investment assets, the consequences are often less dramatic.

Specific gifts of personal chattels included in the Will are binding on the Executor.

The alternative to gifting chattels in the Will is to prepare a separate list of wishes that accompanies the Will. If this list is in existence and executed in accordance to the Wills Act at the same time as the Will then it forms part of the Will and is also binding on the Executor. However, if the Willmaker updates the list on a regular basis without updating the Will the list will not be binding on the Executor.

Implication: When considering the two alternatives, it is a balancing act between certainty and flexibility. Gifts



contained within the Will are certain, but are more difficult to alter as this requires an amendment to the Will. A separate list allows frequent and flexible alteration but does not possess the same binding force.

If the Willmaker wants to guarantee the enforceability of a gift of a family heirloom or other personal chattel, the gift should be included in the Will.

If the Willmaker is making specific gifts of personal chattels, the chattels should be described in great detail so as to avoid confusion. The Willmaker may consider taking photographs of the chattels and storing the photographs with their original Will.

The Willmaker may also consider including a formula in their Will for the distribution of personal chattels such as a selection in turn by Beneficiaries or the purchase of the chattels from the Estate for market value.

The following is an example of a clause making reference to a non binding list of personal chattels:

I give my personal and household chattels as defined in the statute governing the administration of Wills and Probate ('my chattels') to my Executors, and it is my strong wish that my executors distribute my chattels in accordance with any list I may leave stored with my Will or my private papers and signed by me, PROVIDED THAT if I fail to leave such a list, or to the extent that any of my chattels are not listed or distributed, they will be distributed in accordance with the succeeding clauses of the Will.

3. Appointment of Guardians for Minor Children

If a Willmaker has young children or may have them in the future, the Will should appoint Guardians to take the care and responsibility of the children should they die prior to the children turning 18.

The appointment of a Guardian is usually included in the Will as a safeguard in the event that both parents dying before the children are 18 years old. The appointment of a Guardian may also avoid the possibility of disputes between family members. The court has an overriding discretion to appoint or remove a Guardian.

It is the Guardians responsibility to make the important life decisions on behalf of children appointed in their care. The Guardian must ensure that the children are adequately housed, clothed and educated. This may mean that the children reside with the nominated Guardian but this is not necessarily the case.

Implication: It is not uncommon for a Willmaker to be more concerned for the welfare of the children than the distribution of their financial assets. For this reason, uncertainty surrounding the appointment of an appropriate Guardian is often a stumbling block to the finalisation of a Will.

The appointment of a Guardian is potentially complex. In most cases, there are a range of personal, financial and legal issues to be addressed. The fact that the appointment of a Guardian is brought about by death places an additional stress on those involved.

In selecting a Guardian or Guardians, a Willmaker should attempt to appoint one or more people who:

- Are prepared to accept the responsibility. The Willmaker



should meet with the Guardians and discuss with them the nature and extent of the role and their wishes should the Guardians be called upon to act.

- Are of a similar age to the Willmaker and are young enough to assume responsibility or the children should they be required to act in the future. The ages of children at the time of making a Will are relevant to this decision.
- Hold similar, social, religious and cultural views to the Willmaker.

Where the Guardian is not also the appointed Executor, the Guardian will be required to liaise with the Executor in making decisions about the expenditure of the Estate on behalf of the minor Beneficiaries.

4. Guardianship Clauses

The following example of a Guardianship clause may assist in planning:

Appointment of Guardians

In the event that I die leaving children under eighteen (18) years, I appoint [name/s] of [address] to be their Guardian/s. It is my wish that my Executor exercises his powers so as to ensure that any person caring for any of those children whether as Guardian or otherwise) does not suffer, in the course of such care, a financial burden or loss.

In drafting a Will, the Willmaker should include instructions to the Guardians as to how they wish their children to be raised. Areas a Willmaker may wish to cover include:

- Where children should live
- Where children should go to school
- Maintaining contact with other family
- Ongoing use and other occupation of the family home by the Guardians, including the terms of this occupation. For example, are the Guardians required to pay rent to live in the home with the children?
- Use of Estate funds to modify the Guardians home for the purposes of accommodating the additional children. If the Will does not specifically allow for this, an order of the Court will need to be sought consenting to the expenditure
- The desire to keep the children together if applicable

Implication: Note any instructions as to how children should be raised should also be considered against the assets of the estate. Should there be a shortfall consideration should be given to ensuring correct funding exists to meet the requirements of children's and guardians needs.

5. Timing of Gifts

Generally, a Beneficiary cannot take his or her entitlement from an Estate until they turn 18.

However, a Willmaker can delay the Gift for a longer period if they can think it necessary. This is particularly the case where one of the Beneficiaries is to receive a substantial cash amount and the Willmaker does not wish them to take ownership of the gift until they are old enough to manage it.

For example, the Willmaker may choose to delay the gift until the Beneficiary turns 21 or 25



or older. Alternatively, the Willmaker may elect to stagger the release of the gift from the Estate over a number of years, (for example, one third at 18, one third at 21 and the balance at 25).

If a gift to a Beneficiary is delayed for a period of time, it will be necessary for the Executor to hold the Beneficiary's entitlement on Trust until the Beneficiary attains then specified age.

Implication: By delaying the gift, it does not prevent the funds from being applied for the benefit of the Beneficiary should the need arise. Delayed benefit payments to a Beneficiary can be structured having Testamentary Trusts. Be careful when discussing such issues such as Testamentary Trusts in Wills as clients can get confused. Furthermore as to advice on Testamentary Trusts in Wills a qualified solicitor may need to be consulted.

6. Maintenance, Education and Benefit

The Will should give the Executor the power to use the income and capital of the entitlement for the ongoing maintenance, education, advancement or benefit of the Beneficiary. A common example of such expenditure is the payment of school fees on behalf of the Beneficiary.

The following is an example of a specific clause enabling an Executor to make applications of the income and capital. If no such provision is included, the Executor will be required to act in accordance with the legislative provisions dealing with the application of income and capital which are often more restrictive.

My Executor will have the following powers:

To apply for the maintenance, education, advancement or benefit of a Beneficiary the whole or any part of the capital and income of that part of my Estate to which the Beneficiary is entitled or may in future be entitled. For the purposes of this subclause, my Executor may make payments (without seeing to their application) to the parent, Guardians or care giver of the Beneficiary and accept the receipt of the payee as an absolute discharge.

7. Disclaimer of an Estate Interest

A Beneficiary of a Will can refuse to accept a Gift made to them. In considering whether to accept or disclaim a gift, a Beneficiary should be aware of the following:

- The disclaimer must be of the whole gift and not only part of it. However, where a Beneficiary receives multiple separate gifts, one gift can be disclaimed and another accepted.
- A Gift made jointly to multiple Beneficiaries must be disclaimed by all Beneficiaries to be effective.
- A disclaimer is deemed to be a gifting of assets for Centrelink purposes. This means that the normal deprivation rules apply the disclaimed assets will still be assessed for the assets test for the deprivation period.
- A disclaimed gift will be treated as if the Beneficiary had not been left a gift. This Will should be read carefully, and the ultimate outcome of the disclaimer understood, before the interest is disclaimed.



- A disclaimer is potentially subject to stamp duty and capital gains tax.

Implication: Consideration should be given to whether a potential gift to a Beneficiary may produce unintended Estate Shrinkage.

8. Adjusting Beneficiary Entitlements

A Willmaker may need to include an adjustment clause in the Will that takes into account benefits received by one of the Beneficiaries from sources outside the Estate. Some of these non Estate assets may be distributed directly to a person who is also nominated as one of the Beneficiaries.

Implication: This may not bring about the outcome intended, and an adjustment may be required. Trust allocations and superannuation death benefits are two examples that may require adjustment.

9. Trust Allocations

While the unallocated assets of a Discretionary Trust do not form part of a personal Estate, the Will should deal with unequal balances in the allocated funds of the Trust. These balances are called 'loan accounts'.

The existence of loan accounts in a Family Trust results from the use of a Trust as an income splitting vehicle. The income of a Trust is taxed at the marginal rate of the Beneficiary who receives it by way of distribution, subject to rules dealing with unearned distributions to minors. Unequal loan allocations may exist because the Trustee of a Discretionary trust has distributed additional Trust income to one Beneficiary on a lower marginal rate for tax minimisation purposes.

Inequality arises because once the Trustee allocates the Trust income, the person to who the income is allocated becomes legally entitled to the allocation. The allocation is recorded as a liability in favour of the Beneficiary in the accounts of the Trust.

Implication: If the same person is also receiving an equal entitlement to the Estate distributed via the Will, they are receiving benefits over and above other Beneficiaries who do not have loan account balances, or have smaller balances within a Trust.

It is useful to remember that the inclusion of an adjustment clause in a Will ensures that all Estate Beneficiaries are treated equally from an Estate assets and Discretionary Trust allocations. In the absence of an adjustment clause, the Executor will not have the power to adjust unequal loan account balances.

10. Superannuation and the Estate

There are many tax advantages in paying a superannuation death benefit directly to one of the Willmaker's children to the exclusion of others where the chosen child is a death benefit dependant for taxation purposes.

A lump sum superannuation death benefit paid to a superannuation dependant for taxation purposes is tax exempt. By allocating the superannuation death benefits to a child who is a tax dependant, the overall taxation liability on the distribution of the death benefit is eliminated. However, as with the unequal Trust allocations, allocating superannuation death benefits to a child who is tax dependant has the potential to advantage one Beneficiary over another.



Implication: The Will should include an adjustment clause to take account of superannuation death benefits received directly by a Beneficiary. In the absence of an adjustment clause, the Executor will not have the power to adjust for superannuation paid directly to one of the Beneficiaries of the Will.

11. Gifts and Loans

An adjustment to a Beneficiary's entitlement under a Will may also be necessary where a Willmaker has made additional provision for a Beneficiary during the lifetime of the Willmaker.

If it is the intention for a gift or loan to be regarded as an advancement on the Beneficiary's inheritance, this should be clearly set out in the Will. Where intended the gift or loan to be in addition to a Beneficiaries inheritance, the Will should specify this and expressly forgive the loan or confirm the gift.

Implication: To avoid dispute, an agreement in writing prepared during a Willmaker's lifetime setting out the details of the transaction should be stored with the original Will.

12. Gifts to Charity

Charitable giving is an objective of many Willmaker's. It is an opportunity to contribute to the work of a favourite charity into the future. In considering a charitable Bequest, the Willmaker should be aware of the potential tax consequences of a charitable gift.

Implication: The income tax legislation has two concepts relating to charities:

- Tax exemption
- Tax deduction

Some organisations are tax exempt, and therefore the organisation pays no income tax on its activities. Some organisations are deductible gift recipients (DGRs), and therefore gifts made to them are deductible for the Donor. A number of charitable organisations qualify as both tax exempt and tax deductible. Other organisations, such as churches and religious organisations, are tax exempt only and are not DGRs. The nature of the gift and the taxation status of an organisation will affect the taxation consequences of a Bequest.

13. Gifts to Tax Exempt Organisations

When an asset passes from an Estate to a tax exempt organisation, the Income Tax Assessment Act deems that a Willmaker made the gift immediately prior to their death for market value. This is referred to as a CGT Event K3, and the Estate becomes liable for capital Gains Tax (CGT). This will not be relevant if the asset was acquired prior to the introduction of CGT on 20 September 1985 or if the asset is cash.

Implication: If it is intended to make a gift to an organisation that is tax exempt, it would be preferable to make the gift in the form of cash. If gifts are subject to CGT, such as shares or real estate, this may reduce the value of the gifts made to other Beneficiaries.

There is a notable exception to the principle that gifts made to tax exempt organisations should be made in cash. If a gift in a Will is made under the Cultural Bequests Program, the gift is exempt from CGT.



The Cultural Bequests Program is administered by the Federal Department of Communications, Information Technology and the Arts. Essentially the program encourages gifts of significant cultural items to public art galleries, museums and libraries by giving Donors a tax deduction for the market value of their gifts.

The gift can take any form other than an interest in land or a building. In addition, the property must be accepted by the institution receiving it for the inclusion in a collection that is maintaining or establishing. It is recommended that if the Willmaker wishes to make a non cash, charitable gift in the Will the Willmaker should first make contact with the intended recipient to discuss the nature of the gift and then seek advice about the likely tax consequences.

14. Gifts to Tax Deductible Organisations

The tax consequences of a gift to an organisation that is also a DGR are different. The Income Tax Assessment Act allows for a capital gain arising from a Testamentary gift to be disregarded provided the gift would have been deductible had it not been a Testamentary gift. Therefore, if the organisation that is intended to benefit is a DGR, provided the requirements of the Tax

Assessment Act are satisfied, the Estate will not be liable for the payment of CGT liability arising from the making of the gift.

Implication: When nominating a charity as a Beneficiary in a Will, the Willmaker must include the full and correct name of the charity that is intended to benefit.

Difficulties can arise where the reference to the charity is vague and there is more than one organisation of a similar name.

The Willmaker should also include a power in the Will for the Executor to pay an organisation that represents the successor to the nominated organisation that is likely to satisfy their charitable objectives. This ensures that the Executor will be able to complete the gift.

It is important to specify in a Will that the receipt of the secretary, treasurer or other authorised representative of the organisation is a sufficient discharge to the Executor.

To find out more about ili courses and workshops in respect to the Contents of a Will and Funding Requirement, Estate and Succession Planning please visit our website www.ili.com.au.

Copyright Notice

©ili.

All rights reserved. No part of this publication may be reproduced, stored in a retrieval system, transmitted or copied in any form or by any means (graphic, electronic, mechanical, photocopying, microcopying, scanning or otherwise) except as permitted under the Copyright Act, without the prior written permission of ili. Any enquiries should be addressed to ili.

Disclaimer

This publication is designed to provide accurate information regarding the subject matter which it covers. It is distributed on the understanding that ili is not engaged in rendering professional or expert services or advice (legal, accounting, financial planning or otherwise). The information provided in this publication does not constitute such advice or services and should not be relied on as such. If professional or expert assistance is required, the services or advice of a competent person should be sought.

Neither ili nor its directors, employees, associates, agents or other representatives and affiliates are liable for any liability, loss, damage or injury arising from or in relation to the direct or indirect use of, or reliance on, the whole or any part of the information contained in this publication. Without limiting the generality of the above, neither ili nor its authors, consultants and writers are liable or responsible for anything done or omitted to be done by any person in respect to this publication.

**For Further information please visit www.ili.com.au or contact:
Melinda Wood – ili Enquiries (02) 9251 3611 enquiries@ili.com.au**