Estate Planning

Overview of estate planning

Aon Hewitt Financial Education Series

Estate Planning refers to the process of planning and documenting your wishes for the distribution of your assets when you die. Estate planning not only deals with the assets that you own personally, but those that you control as well. Estate planning can also involve the use of insurance policies and should also consider how your super benefits are to be paid after your death.

Introduction to Estate Planning

A good estate plan requires the involvement of skilled legal, accounting and financial specialists to ensure that the right assets end up in the right hands at the right time. There are some basic elements that should be considered when addressing your estate planning needs:

- Having sufficient assets available to meet your wishes upon death;
- Ensuring beneficiaries receive the entitlements that you intended for them to receive;
- Any taxation associated with the transfer of assets is minimised;
- Beneficiaries with special needs are protected;
- Ownership or control passes to a beneficiary at the right time.

Wills

A Will enables you to direct how your assets are to be dealt with after your death. Everyone, even with modest assets, should have a current and valid Will to ensure that their wishes are clearly expressed on their death. It is especially important for anyone living in a de facto/interdependent relationship or who is separated or divorced.

Keeping your Will up-to-date when circumstances change is the most important aspect of an estate plan. It should be reviewed at least every five years or whenever your circumstances change. This will include the birth of a child or grandchild, a marriage or divorce and even the purchase of large assets. It is highly recommended that you review your existing Wills in conjunction with your solicitor.

If you die without a Will, or an incomplete Will, you are said to have died ‘intestate.’ With no Will in place, your estate will be split based on the rules contained in the Wills and Probate and Administration Act of the state you reside in. This prescribes the precise order of persons who will share and benefit from the intestate estate. The fundamental principle is that the estate will pass to the next of kin of the deceased in order of statutory priority, meaning that your estate may not be distributed how you would have liked. For additional information regarding the scheme of distribution laid down by statute law, you should consult your legal adviser. Usually the next of kin (adult) with an entitlement to the largest share of the estate applies for letters of administration.

By doing this, he/she is applying to the court to be the administrator responsible for the administration of the estate in accordance with the statutory order of distribution of an intestate estate.

A properly executed Will ensures that after your death:

- Assets will be invested or distributed according to your wishes. This is the function of the executor(s). You should choose an executor who is unlikely to predecease you, who is readily available and if possible, is someone in tune with your wishes. It is quite common to have more than one executor appointed.
- Funds are held in trust for beneficiaries. It is possible that some funds may be held for some time in trust for beneficiaries who haven't yet reached the age you nominate for them to receive the bequest, for example young children or grandchildren.

Disposal of Assets

Depending on the timing of an estate settlement, and the taxation situation of individual beneficiaries, capital gains tax (CGT) can have a substantial impact on those who receive and later sell assets from a deceased estate. For more information, review the 'Capital Gains Tax (CGT) Implications for Deceased Estates' fact sheet under the Key Investment Concepts Financial Education Series.

Assets that form part of a deceased's estate and are ultimately disposed of by the deceased's Will, are called Estate Assets. Such assets include:

- All assets you own personally;
- Your shares in a company;
- Your share of any asset you own as tenant-in-common;
- Any super death benefit or life insurance policy proceeds paid to your estate;
- Your interest in any partnership assets, unless agreed otherwise;
- The right to recover any funds owed to you; and
- Any rights you hold under any contract or agreement.

Assets that are not directly controlled by a person do not form part of their estate and cannot be disposed of by their Will. These assets called Non-Estate Assets include:

- Assets you own as a joint tenant such as your home or bank account (these pass automatically to the other joint tenant(s));
- Assets held in a trust (the trust deed governs what happens to these assets);
- Assets owned by a company (only the company can deal with its assets); or
- Super death benefits or life insurance policy proceeds paid directly to a beneficiary.

Appointing an Executor

An important aspect we would like to highlight is whom you will appoint as an Executor. The Executor is responsible for carrying out your wishes as expressed in your Will and has fundamental control of the process. You need to ensure that the person you select will be able to perform this role. The administration of your estate can be time consuming and is likely to require a high level of knowledge of investing, taxation, accounting and law.

Super Death Benefit Nomination

Generally, super doesn't form part of your estate unless the trustee of the super fund pays the super benefits to your estate. Instead you are able to nominate one or more beneficiaries who will receive your super when you die. There are strict rules around who you can nominate and the tax that may be payable when they receive the funds. For more information, please refer to the 'Death Benefit Nominations' fact sheet under the Superannuation Financial Education Series.

To nominate a beneficiary, you can either make a binding, non-binding or non-lapsing binding nomination.

Binding Nomination

A binding death nomination is binding on the trustee of the fund. This means that the trustee must pay the nominated beneficiaries as directed by you, provided your nominated beneficiaries qualify as dependants at the relevant time, and that the nomination is valid. A binding nomination generally speeds up the payment of benefits upon death.

Non-binding Nomination

A non-binding nomination, is as the name suggests not binding on the trustees of the super fund. This means the trustee has the discretion as to who receives benefits from the fund when you die and the benefit is paid. However, the trustee will use your nomination as a guide when distributing your benefits upon death.

Non-lapsing Binding Nomination

A non-lapsing binding death benefit nomination is effectively a binding nomination that doesn't expire. Unlike a binding death benefit nomination which will lapse if not renewed at least every three years, a non-lapsing nomination will not expire unless you revoke or make a new nomination. Whilst a valid non-lapsing nomination doesn't expire, it is important that you review your nomination regularly and ensure that it is updated in the event your personal circumstances change. A nomination may become invalid under certain circumstances including events such as marriage, divorce or death of a nominated beneficiary.

Talk to your financial adviser about putting in place a super death benefit nomination.

Power of Attorney

By signing a Power of Attorney, you give someone authority to act on your behalf.

The Power can be unlimited, in that your Attorney can do whatever you can do legally; or, the Power can be limited to certain things (e.g. to dealing with your shares only) or limited in time (e.g. for one month while you are overseas).

Powers of Attorney have extremely broad scope and careful consideration should be given to which individual, individuals or company is chosen to act as the Attorney. The Attorney can effectively make legal, financial and personal decisions on an individual's behalf and as such, when making the appointment requires a significant level of trust and comfort.

By not appointing an Attorney, if in the future you become unable to make decisions or communicate your wishes, financial decisions may have to be made by the Public Trustee.

Because of its legal effect, any Power of Attorney must only be signed after obtaining the advice of your solicitor, so please consult your solicitor for further details on Powers of Attorney.

There are generally three types of Powers of Attorney depending on the State or Territory law prevailing, however you should check with your solicitor which types of attorney are available in your State or Territory:

General Power of Attorney

This type is normally used in a limited capacity. For example, you may wish the Attorney to conduct a specific transaction such as the purchase of a property or you may be going overseas for a prolonged period and wish for the Attorney to manage your affairs in your absence. However, if you become mentally incapable of managing your own affairs, the General Power of Attorney becomes null and void.

Enduring Power of Attorney

This type of Power of Attorney remains valid even when a person is deemed to be mentally incapacitated. This means that should you lose your capacity due to accident, stroke or a degenerative disease; the Attorney can step in and manage your affairs on your behalf.

The risk of giving this type of power is that you are unable to revoke it if the court has determined that you can no longer make your own decisions (unless the Attorney is not acting in your best interests). It is possible to give someone an Enduring Power of Attorney over your affairs that are not valid unless you become mentally incapacitated. The courts of Australia can appoint someone with legal authority to make decisions on your behalf if an Enduring Power of Attorney has not been appointed and you lose your capacity to make your own decisions. Because of its legal effect, a Power of Attorney must only be signed after obtaining the advice of your solicitor.

Enduring Power of Attorney – Medical Treatment

This type allows you to authorise an Attorney to make decisions regarding medical treatment. Typically, it is prepared when you want to express a preference in relation to the administration of a particular medical treatment, for example no blood transfusions or DNR (Do Not Resuscitate) instructions.

Testamentary Trusts

Another aspect of estate planning you may wish to consider to ensure your family is well provided for when you die, is setting up a tax-effective testamentary trust, which is simply a trust established under a person's Will. When you die a portion of the assets of your estate are placed in this trust, rather than being paid out to beneficiaries. Each year the trustee can decide on the most tax-effective way to distribute the trust's income and capital.

Some of the specific reasons for setting up a testamentary trust are:

- To split income in a tax-effective manner.
- To protect pension entitlements of spouses.
- To shield a beneficiary's entitlement from creditors.
- To relieve certain beneficiaries from asset management responsibilities (e.g. minors, the elderly, the incapacitated or the financially unsophisticated).

Income from a testamentary trust is taxed at normal 'adult' rates, regardless of the age of the beneficiary. So a minor, your child or grandchild, for instance, can receive up to $18,200 income from the trust each year without paying any tax. If the same income were earned outside this trust, a child could only receive $416 per year tax free, as penalty rates of tax apply to 'unearned income' over $416.

Due to its legal and financial effect, a testamentary trust must only be set up after obtaining the advice of your solicitor. A testamentary trust may not be suitable for everyone and, if set up, must be reviewed as circumstances change.