



YOU AND YOUR PROPERTY

Our regular contributor Michael Hofmann-Body is currently on sabbatical. In this issue property lawyer Jeremy Hucker, who is heading the HomeLegal team in Michael's absence, discusses Family Trusts and their suitability for owning a home.

People often consider purchasing property through a family trust. Indeed, there has been a proliferation in the number of Trusts created over recent years and it has perhaps become fashionable in some quarters to have one's house or other assets in a Trust. The evidence would also support this, as some estimates put the total number of Trusts in New Zealand in the vicinity of 400,000. The underlying reasons for establishing a Trust, however, may not be so well known.

I will explore some of the more relevant reasons for setting up a Family Trust.

The nuclear family is not as common as in the past. Second or third relationships are now common place and relationship property issues can be an important reason for establishing a Trust. An example is perhaps best illustrative of the point.

Mr A enters into a relationship with Mrs B. Both Mr A and Mrs B have previously been married and each has a child from their earlier relationship. Mr A has a son, Cain, and Mrs B has a son, Abel. If Mr A were to die, then a large portion of his estate may pass to Mrs B, notwithstanding that he may actually want this to go to Cain. If Mrs B were to then die, her estate including all assets and property received from Mr A's estate may end up going to Abel. This of course may cause some friction between Cain and Abel! If Mr A had formed a Trust prior to the commencement of his relationship with Mrs B, and transferred his assets to that Trust, the assets would be Trust assets and would fall outside the scope of his estate. Mr A's Trustees would then be able to distribute the Trust assets in keeping with Mr A's intentions.

Another common reason for forming a Trust is to protect inheritances from property

relationship claims. If we are to continue the example above, and if Cain were to enter into a relationship, he may wish to keep any distributions received from Mr A's Trust outside the scope of what would otherwise be relationship property. To do this, Cain could create his own Trust which would then receive assets or property from Mr A's Trust. Should Cain then separate from his partner, the assets received from Mr A's Trust should be considered Trust property (and not Cain's personal property) and, accordingly, a property relationship claim against those assets by Cain's partner is less likely to succeed.

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People in business also often form Trusts to keep business assets separate from their own personal property (for example the family home). Personal guarantees are often required in the course of operating a

business. However, assets that are in a Trust may not be available to creditors seeking to enforce such personal guarantee. Again, this is because assets in a Trust are considered Trust property and not personal property.

There may also be some tax benefits in establishing a Trust although with the recent budget announcements, professional advice should be sought. Income received from a Trust may be paid to beneficiaries at their tax rate and if those beneficiaries earn little or no other income, they may only be liable to pay tax at their lower tax rate. I must of course add a caveat here insofar as a Trust cannot be established for the sole purpose of reducing one's tax liability. However, if less tax is paid as an ancillary benefit, the Trust will still be valid.

I am also often approached by clients in their later years who wish to establish a Trust and then divest themselves of assets through that Trust in order to obtain a rest home care subsidy. Rest home care subsidies are available to those with only limited assets and the subsidies are means tested. Generally this is problematic, particularly when a Trust is set up in the later years of life, but like any tax relief that may be available through the establishment of a Trust, I see any benefit in respect of rest home care subsidies as being an ancillary purpose and in itself is not a good reason for establishing a Trust.

There can also be some cost savings in establishing a Trust at or prior to the time of purchase. The decision will also have a bearing on the documents that will issue from any mortgagee. Accordingly, legal advice at an early stage should be sought.

There are of course many other pros and cons to establishing a Trust and we would recommend you also take legal advice to discuss your own particular circumstances.