



To Trust or Not to Trust 4ed

A practical guide to family trusts



Purnell
LAWYERS



© NZ LAW Limited, 2021

Publisher: NZ LAW Limited, PO Box 132, Napier

Project management: Adroite Communications, Wellington.

Design/production: Mission Hall Creative, Wellington.

All rights reserved. No part of *To Trust or Not to Trust* may be reproduced or used in any form or by any means, electronic or mechanical, including photocopying, recording or by any information storage and retrieval system, without permission in writing from the publisher and credit being given to the source.

Disclaimer: Material published in *To Trust or Not to Trust* is true and accurate to the best knowledge of NZ LAW Limited. It should not be a substitute for legal advice. No liability is assumed by the publisher, nor any of its member firms, for any losses suffered by any person relying directly or indirectly on this booklet. A full list of NZ LAW member firms can be found [here](#).

ISBN 978-0-473-56136-9 (PDF)

Table of contents

Foreword	3
Establishing a family trust	5
What is a family trust? Is it for us?	5
The benefits of a trust	6
Important things to think about	6
Doing it right is important	7
Mistakes are not always fatal	7
Trusts Act 2019	9
Protection given by a family trust	11
Business owners	11
Trading and development trusts	12
Trading in land and property development	12
Relationship property claims	12
Children with special needs	13
Education trusts	14
Claims against estates	14
Minimising tax liability	15
A trust or a company?	15
State assistance and benefits	16
Capital gains or succession tax	16
Maximum duration of trusts	16
Confidentiality	16
Charitable purposes	17
Dealing with changes in the law	17
Transferring assets	19
The transferring of assets	19
Rest home subsidies	20
Gifting programme	20
Claims of a spouse or partner	20
Protection against creditors	21
Claims against estates	22
Timing is everything	22

Decisions to be made	25
The trust deed	25
Name of the trust	25
Trustees	26
Independent trustee	26
Appointer	27
Protector	27
Special trust adviser	27
Beneficiaries	28
One or more trusts?	28
How much control is too much?	28
Completing your estate plan	31
Your will	31
Letter of wishes	32
Enduring Powers of Attorney	32
Other documents	33
Family trust administration	35
A trustee's duties	35
Prudent investment	36
Trustee decision-making	37
Trustee liability	37
Tax	38
Foreign trusts	38
Accessing trust income	38
Accessing trust capital	39
Using a house owned by your family trust	39
Trusts carrying on business and investing	39
Relationship property issues	40
Life of the trust	41
What will a family trust cost?	43
Establishing a family trust	43
Annual costs	43
Glossary	44
Index	47



Foreword

The need to protect a family's assets is not a recent phenomenon. For hundreds of years people have wanted to safeguard their family's assets by sheltering them in a trust.

The use of family trusts has, however, increased significantly in recent times as the complexity and risk of conducting business increases, more levels of compliance are introduced, relationship property laws have been extended and society in general has become more litigious.

This 4th edition of *To Trust or Not to Trust* reflects the Trusts Act 2019 that came into force on 30 January 2021; it replaced the Trustee Act 1956. Written in modern clear language, this new legislation sets out (amongst other things) trustees' duties and obligations, amends some provisions for beneficiaries and allows trustees who are no longer mentally competent to be more easily replaced.

This guide provides an introduction to trusts if you are starting to think about protecting your assets. It also offers useful information if you are already familiar with the concept of trusts and how they can work for you.

Whatever stage you are at, we recommend that you read through this guide and then talk with us about the best way to meet your family's needs and to achieve the outcomes you desire. You will want to know about the options available to you and what impact they will have on the way you and your family protect, use and enjoy your assets in the future.

We do emphasise that a family trust may, or may not, suit your specific family circumstances, nor does one size fit all. However, for most families who want to safeguard their family's wealth, a trust structure to ringfence their assets is the best solution.

After reading *To Trust or Not to Trust*, do talk with us; we can advise you on the best structure to suit your family's requirements. Alternatively, do look [here](#) for your nearest NZ LAW Limited member firm.

Mark Henderson

Chair, NZ LAW Limited





Establishing a family trust

What is a family trust? Is it for us?

Trusts are a popular way for New Zealanders to protect their assets. There may be a number of reasons why you are considering setting up a trust or have been advised to do so.

A trust can offer a number of benefits and these are explained in this guide. Before you make any decisions about this, however, it's important that you understand what a trust is and how it works.

This guide sets out some of the important features of a trust and what is required in order for your trust to work as intended. If the legal obligations are not met or you have retained too much control, your trust may not be legally effective or you may be treated as still an owner so that there is no benefit to you.

New Zealand trust law is the result of centuries of development by Acts of Parliament and by the courts both here and, in earlier times, in England. Some of the more important rules have been updated by the Trusts Act 2019. We cannot, however, cover all the detailed rules here. If you need further explanations about some aspects or you have any questions, you should talk with us.

A trust is a legal arrangement under which a person (the trustee) holds money, property or other assets for the benefit of a specified person or people (the beneficiary or beneficiaries). Usually, the original owner of the assets (the settlor) will transfer the assets to the trustee after they have both signed a deed to record the terms of the trust. Of course, a trust may have two or more settlors, several trustees and a number of beneficiaries. It's possible, and quite common, for one person to be a settlor, as well as being one of the trustees and one of the beneficiaries.

At the heart of a family trust is the relationship between trustees and beneficiaries. There are other types of trusts –

charitable trusts, for example, that are established not for the benefit of individual people, but for charities or for charitable purposes.

The other essential element is trust property or assets: a trust arises whenever a trustee holds an asset on trust, but without an asset there is no trust.

The benefits of a trust

For many people the principal purpose of a family trust is to protect a family's assets and wealth against risk. This is done for a variety of reasons, some of which are to:

- ✦ Protect assets from business risk (if you own a business or have a senior management role in a business)
- ✦ Provide for special family needs, such as a child with a disability or impairment
- ✦ Protect your assets in a second marriage/relationship situation and/or relationship breakdown
- ✦ Prevent claims on your estate when you die (family protection and testamentary promise claims)
- ✦ Minimise tax liability
- ✦ Protect against income and asset testing for rest home charges (but be aware the rules could change and we cannot be certain a trust will enable you to qualify for a rest home subsidy)
- ✦ Provide funding for children's or grandchildren's education costs
- ✦ Allow family assets, such as a business or farm or holiday home, to pass to the next generation without exposing inheritances to relationship property or other claims, or
- ✦ Give to the community through a charitable trust.

Important things to think about

Once you have decided to go ahead with a trust, you need to think about which of your assets to transfer to the trust. There can be tax and other practical considerations. You may need accounting and legal advice about this, and also about how your assets need to be transferred. While there is no gift duty (it was abolished in 2011) or tax law to prevent you transferring all your chosen assets into the trust at once, there can be other factors to consider, see pages 19–23.

You also need to think about the trust deed which sets out the rules for your trust and how you want it to work.

Trustees will need to be appointed to run your family trust. This maybe you as settlor, and also perhaps your spouse or partner. One possibility that you could discuss with us is to use a company as a trustee.

In addition to the terms of the trust that are in the trust deed, trustees also have a number of legal duties. These are set out on pages 35–36. The trust deed may override some, but not all, of these duties. For example, section 35 of the 2019 trusts legislation requires trustees to treat all the beneficiaries impartially, but a deed may say that priority is to be given to the need and interests of a defined group of ‘primary beneficiaries’ (usually the settlors and their children).

Most family trusts now have two groups of beneficiaries:

1. ‘Discretionary beneficiaries’ who may benefit at any time while the trust is running, and
2. ‘Final beneficiaries’ who receive any remaining assets when the trust comes to an end.

Unlike a company or an incorporated society, a trust is not treated in law as if it were a separate person or entity. It is the trustees who represent the trust. All trust assets must be held in the name of the trustees who will be personally liable for trust debts unless the creditors agree to limit the trustees’ liability.

Doing it right is important

Even after you have set up your trust and put your major assets into it, you cannot just put the family trust papers away and forget about them. It’s important to keep careful record of all trust assets and trustees’ decisions. If you don’t do this, or if you are able to treat trust assets as if they still belong to you, you may be considered to still be an owner or part-owner. In that case, all benefits of having a trust to protect your assets could be lost.

Mistakes are not always fatal

You may have seen media coverage suggesting many trusts in New Zealand are shams or won’t stand up to scrutiny. If you never intended to operate a real trust, then it may be a sham and can be set aside.

If trustees are doing their best, however, and always intended to act as genuine trustees, then the courts are unlikely to say this is a sham.



Beneficiaries' right to information *Erceg v Erceg*¹

Michael Erceg was a successful entrepreneur who died in a helicopter crash in 2005. Ownership of his businesses had been transferred to two trusts before he died. The trust deeds listed a number of groups of discretionary beneficiaries including Michael's wife and children. Michael's brother, Ivan, was one of the many discretionary beneficiaries.

Ivan asked the trustees for a number of trust documents including documents relating to the businesses (bank statements, share valuations, etc).

The trustees refused and Ivan applied to the High Court. The case eventually reached the Supreme Court which agreed Ivan should not be given these documents.

The Supreme Court listed a number of factors which trustees should take into account before deciding whether or not to give information to a beneficiary. Very similar factors are now listed in the Trust Act 2019.

The court said the trustees can take issues of commercial confidentiality into account. It also said trustees do not need to make available the reasons for the decisions although they could release documents with sections redacted [blacked out].

¹ *Erceg v Erceg* [2017] 1 NZLR 320; [2017] NZSC 28.



Trusts Act 2019

The Trusts Act 2019 became part of our law on 30 January 2021.

This legislation made some important changes to trust law including:

- ✦ Trustees' duties are now set out in modern clear language
- ✦ Trustees' obligations to hold on to trust documents and to keep beneficiaries informed have been restated more clearly
- ✦ It is now possible to delegate the trustee's role during periods of temporary incapacity
- ✦ Trusts may now last for up to 125 years (previously most trusts could only last 80 years)
- ✦ Beneficiaries are now entitled to receive money or property from a trust at 18 years old unless the trust deed says otherwise, and
- ✦ It is now much easier to remove and replace trustees who are no longer mentally competent, and land titles can be corrected more easily.

The Trusts Act 2019 can be found [here](#) if you want read it for yourself. The Act does not cover all of the law relating to trusts in New Zealand. Much of the previous case law still applies.

If you have any queries, we can advise about the law generally relating to trusts.





Protection given by a family trust

For most families, the objective in establishing a family trust is to safeguard your family's assets against business and other risks. The sections below briefly describe some of the most commonly used protections offered by family trusts.

It's important to keep in mind that assets are only protected if they have been completely given away to a trust. If you have retained some assets, or the trust still owes you money, then this will be vulnerable to a variety of claims.

Business owners

Without a family trust, business owners run a considerable risk that their family assets could be vulnerable. A number of situations could bring this about, including:

- ✦ Creditors, if there is a business failure
- ✦ Compliance issues, resulting in action taken against you or your business under, say, workplace health and safety laws, and/or
- ✦ Action taken against directors or senior management of a company.

Trusts are not only for employers. Looking to the future, if you establish your own business or are in a senior position in a business, you should also consider some method of protecting your assets as this type of business activity may expose you to legal claims.

Trading and development trusts

Conducting business in New Zealand is carried out on a personal basis as a sole trader, or through a joint venture, partnership, company or trust. When a trust is used as a vehicle to run a business it's commonly called a 'trading trust' or a 'development trust'.

Trading in land and property development

Special rules apply if your business involves trading in land or developing real estate. These activities need to be separated from your other business and personal assets to avoid association for tax purposes.

There are specific tax rules covering land sales and associated persons. If you are a property dealer or developer anyone you are associated with can also be taxed as a property dealer or developer. This can happen unwittingly. The result can be that a profit may be taxable when the property is sold. If you can avoid being treated as associated, and if you retain the property long enough to meet the 'bright-line rule', you may not have to pay income tax on any profit. There is more on the bright-line rule in the Glossary.

The structures that need to be put in place in these circumstances are complex; we would expect your accountant to be involved, as well as us, in advising about this.

Even if you do separate dealings with property from your personal finances, you can still be caught by the bright-line rule.

Relationship property claims

Trusts are often used to help avoid claims by a former spouse or partner, for example, a claim against your son or daughter's inheritance. When a couple separates – whether they were married or in a civil union, de facto or same sex relationship – the basic rule is that they share equally in all 'relationship property'. These are the assets they have built up together during their relationship. There are some exceptions, such as inherited property, and the court has some overriding discretion. In reality, however, it's easy for an inheritance to become relationship property if, for example, you use inherited money to pay off your joint mortgage.

The best advice is usually to sign an agreement contracting out of the Property (Relationships) Act 1976. We can draw this up for you.

Another solution is to ensure that any inheritance is kept in a trust, separate from relationship property. Putting your children's inheritance in a trust can help avoid claims from a rogue son-in-law or daughter-in-law.

Before you enter a de facto relationship, marriage or civil union, if you have significant assets you should carefully consider how best to protect your personal assets in case you later separate or one of you dies.

The equal sharing rule does not apply to short duration relationships (usually less than three years). However, transferring your assets to a trust just before the three-year period ends is not likely to be effective. Relationship property law has claw-back rules which apply if you have given away assets with the intention of defeating a future claim. The courts may also compensate a former partner who has contributed to a property, even if it is held in a trust.

If you are going into a second or subsequent relationship, civil union or marriage, and you have children from an existing or from previous partnerships, it's even more important to ensure that your assets are preserved in order to make the division of property fair and just, and to ensure your children's interests are preserved.

The Claymark Trust decision: *Clayton v Clayton*²



The Claymark Trust was set up by Mr Clayton to hold land around his sawmilling business. He, his wife and four children were beneficiaries. After the couple split up, Mrs Clayton claimed a share of the trust property. However, the Supreme Court decided it was a 'nuptial trust' and, under s182 of the Family Proceedings Act 1980, the court decided to split the properties equally between two trusts – one each for Mr and Mrs Clayton

2 *Clayton v Clayton* [2016] NZSC 30; [2016] NZFLR 189.

Children with special needs

A trust can help to ensure your assets are safeguarded for a child with special needs such as a disability or impairment. This protection may be given through the family trust, or by setting up a separate trust for the individual child. You should be aware, however, that trust assets can be treated by the authorities as financial resources that should be used first before asking for government help, such as a benefit.

The trustees can exercise their discretion to make available to the beneficiaries any income and/or capital to help meet their legitimate cash requirements. The trust could also make loans for capital needs such as housing, or even to buy a home for occupation by a beneficiary.

Similar protection can be arranged when you have doubts about the ability of a child or other family member to manage their financial affairs.

You may feel the need to protect your children or other family members from their own folly or lifestyle. It can be left up to the trustees to give these children control of some or all of the assets held in trust at a future date and, in the meantime, provide for their reasonable needs.

Education trusts

Sometimes parents or grandparents want to establish a separate trust or trusts to help fund education costs for their children or grandchildren. Often these trusts specify levels of education to be funded, such as high school costs, boarding fees and/or tertiary level expenses.

Claims against estates

Establishing a trust will help protect your estate against family protection and testamentary promise claims.

Family protection

If your will doesn't provide adequately for your spouse or partner, children, grandchildren or other close family members you may have been significantly financially supporting, claims may be made against your estate after your death under the Family Protection Act 1955.

The claimant/s must show that you had a moral obligation to provide for them and that your will did not provide for their adequate maintenance and support. If provision is made under your trust for those for whom you have a moral obligation to provide, claims can usually be avoided. However, your children – in particular – have a right to be acknowledged as members of the family.

Testamentary promises

A testamentary promise claim can be made against an estate if the deceased promised to reward someone by his or her will in return for work or services. These claims are made under the Law Reform (Testamentary Promises) Act 1949. To support a claim there must have been something done for you by the claimant, such as looking after you without being paid (for example, housekeepers or companions).

While evidence is needed to prove the claim, often the promise will be implied in the circumstances. Assets held in a trust at your death are not part of your estate and cannot be claimed under the testamentary promises legislation.

Minimising tax liability

Establishing a trust principally to avoid paying tax is not likely to be effective. If there is a tax saving by establishing a trust, it must be seen as an incidental benefit, not the sole or dominant purpose of the trust.

Tax savings can be made if the trustees have flexibility to decide which beneficiaries should receive income each year. Trusts are taxed at the maximum individual rate (currently 33%) but income distributed to beneficiaries is taxed at their own personal rate. Using a trust for tax-efficiency requires careful advice.

A decision as to how much income is to be allocated to a beneficiary must be made within 12 months of the balance date for the trust.

The 2011 Supreme Court decision, *Penny & Hooper v Inland Revenue*, emphasises that an artificial arrangement intended mainly to avoid tax can be ignored by Inland Revenue (IRD) for income tax purposes even if the trust itself is perfectly valid.



*Penny & Hooper v Inland Revenue*³

Two surgeons (Mr Penny and Mr Hooper) each put their business into a company. Each company was owned by a family trust. In each case the company paid the surgeon a salary far lower than what he was previously earning. Most of their earnings were channelled through their trusts. Because this reduced the amount of tax in each case, the IRD invoked the anti-avoidance rule in the Income Tax Act 2007.

The Supreme Court agreed with the IRD: the trust and company arrangement was legally valid but the surgeons must pay income tax on what they actually earned, not just the notional salary. The surgeons also had to pay \$25,000 towards the IRD's legal costs.

³ *Penny & Hooper v Inland Revenue* [2011] NZSC 95; [2012] 1 NZLR 433.

A trust or a company?

Other structures such as look-through companies (LTCs – previously called loss attributing qualifying companies), partnerships, and portfolio investment entities (PIEs) may offer tax advantages for individual investors. It's important to remember, however, that these structures do not offer the asset protection available through a trust.

State assistance and benefits

There are strict rules if you want to apply for a government benefit or assistance such as legal aid, student loans, the unemployment benefit, etc. These rules have been in place for a long time. Assets transferred to a trust can be treated as resources that you should use first before asking for government help.

Even if you have transferred assets to a trust of which you are not a beneficiary, you may still be denied assistance from the state.

The same is also true of using a trust in order to qualify for a rest home subsidy. In that situation, there are strict limits on how much you may put into a trust each year. There's more about this on pages 19–23.

Capital gains or succession tax

Unlike most countries, New Zealand does not currently have any capital gains tax, or any inheritance or estate tax. Gift duty (a tax on gifts of large amounts) was abolished in 2011. This means property of substantial value can now be immediately given to a trust.

At the time of writing, it seems New Zealand will not be adopting either a capital gains tax or any form of wealth tax in the near future. Different types of capital gains tax are imposed in countries such as Australia, the UK and USA. Depending on the type of tax selected, a trust may reduce the impact of such taxes but it is impossible to advise about a possible future tax.

Maximum duration of trusts

By law, most trusts cannot last forever. Under the Trusts Act 2019, a maximum of 125 years is allowed for trusts other than purely charitable trusts.

If your assets are owned by a trust they may be preserved for the next generation. It must be remembered, however, that most trusts will mature after 125 years and the process must then be started again. Families should take this trust life cycle into account.

Confidentiality

There is currently no requirement for public registration or disclosure for private trusts. A trust's annual accounts and activities are not available to anyone else except the settlor, trustees and the beneficiaries. Court decisions indicate that trustees have a duty to inform beneficiaries (see the *Erceg* case on page 8).

The basic principle is that trustees are accountable to beneficiaries. Therefore beneficiaries are entitled to sufficient information to be able to hold the trustees

to account. The court has a discretionary power to order the trustees to give information to beneficiaries whatever the trust deed may say.

The best advice is to keep the beneficiaries informed and work with them. Beneficiaries are usually entitled to see deeds, accounts and the record of decisions of the trustees, but are not entitled to know the reasoning of the trustees when exercising their discretion.

Charitable purposes

Charitable trusts and foundations must be registered in order to obtain their tax-exempt status. Trust information is publicly available on the Charities Register, unless you ask for confidentiality.

Your family trust could include named charities or charitable purposes generally as potential beneficiaries. If charitable purposes or named charities are included, the trustees can make charitable payments without the need to register as a charity.

Since 2008, trustees have been entitled to a tax rebate up to 100% of trust income distributed for charitable purposes.

Dealing with changes in the law

There is always the possibility of changes to trust law, or associated laws affecting trusts.

The Trusts Act 2019 made some important changes to trust law. At the time of writing, the Law Commission is looking at proposed changes to relationship property law.

No one knows what future law changes there may be or when they may occur. It is comforting to know, however, that the fundamental structure of a trust has stood the test of time over hundreds of years.

If there are changes to the law, modern trust deeds usually provide the trustees with a power to vary some of the terms of the trust, which may ensure the provisions of the deed can be adjusted to comply with law changes. It's important that your trust deed includes wide powers to resettlement and to vary the trust.





Transferring assets

Any asset can be transferred to your family trust. It's generally recommended, however, that you only transfer assets which are likely to increase in value. For most people this usually involves transferring their family home, and perhaps rental property and some investments such as a share portfolio. We can discuss with you which assets should be considered.

If you're considering transferring assets such as rental properties to your trust you should talk with your accountant about the tax implications of such a transfer, including tax on depreciation recovered.

The transferring of assets

When assets are transferred to a trust, they are effectively being given away. The law requires that trust funds must be kept quite separate from your own personal assets, therefore when you put anything into a trust it's treated as a gift.

The law now allows you to give away as much as you like at any time. The previous gift duty or tax no longer applies (it was abolished in 2011). In some circumstances, however, giving assets away can have adverse consequences.

There are three particular situations where it is particularly important to get specific advice about how to go about transferring assets to a trust. These are:

1. Where there are potential relationship property claims
2. If you are looking for protection against possible future creditors, and
3. If you have concern about the cost of rest home care at some future time.

Rest home subsidies

An application for a rest home subsidy is likely to be declined if you have given away substantial amounts, whether to a trust or to anyone else. Under the current rules, you may gift only \$27,000 a year (reducing to \$6,000 a year during the five years before you apply for a subsidy). Your combined gifting as a couple must be below those limits.

During the five-year gifting period, if too much has been given in one year, the gifts can be averaged over the following years to keep within the prescribed limits.

Gifting prior to that five-year period cannot be averaged out, but it's sometimes possible to reverse the transfer of assets in order to qualify for a subsidy. The rules are complex and the Ministry of Social Development has a stringent regime of assessing whether or not you may have 'deprived' yourself of assets, or income from assets. If you attempt to qualify for a rest home subsidy by completing a single gift, it's unlikely to be effective.

Gifting programme

In order to keep within the Ministry of Social Development's limits, it's possible to use what is known as a 'gifting programme.' This usually involves:

- ✦ Selling assets to the trust at their full market value
- ✦ Leaving the amount of the 'sale price' owing as a debt, and
- ✦ Reducing that amount by a gift of \$27,000 each year (per couple).

Of course these are all paper transactions; no money changes hands apart from legal fees. It's important to keep full records of the sale, acknowledgement of debt and annual gifting. There should also be records to establish the market value of the assets, for example, a report from a registered valuer (local council rates assessments may not be a good guide). We can prepare these documents – sale, acknowledgement of debt and annual gifting – for you so that you can be sure they are legally effective.

You should remember, however, that the rest home subsidy rules can change at any time. A trust set up according to the rules that applied in the past may not be effective at the time you come to apply for a rest home subsidy.

Claims by a spouse or partner

As mentioned earlier in this guide (pages 12–13), it's possible to transfer an asset to a trust in order to avoid the risk of a claim by a future spouse or partner. The law does, however, allow 'claw-back' of an asset which has already become

relationship property or was transferred in order to defeat the rights of your spouse or partner at the time. The court may also compensate a former partner or spouse who has made contributions to a property, even if it is held in a trust.

The Law Commission is currently looking at proposed changes to relationship property law. Future changes may restrict the use of trusts to ringfence property that was owned before the relationship started. While a gifting programme, spreading the transfer of the value of the assets over a number of years as noted on page 20, is sometimes recommended because of concerns about rest home subsidies, using a gifting programme may have adverse results if there is a claim by a spouse.

Widower John



John is a widower in his early 50s. He hopes to remarry eventually, but he also wants to ensure that the property he and his late wife built up together is passed on to their children in due course. He transfers all his property to a trust. As he is not yet in a relationship, he can transfer everything outright. He is not intending to defeat the rights of a spouse or partner – he doesn't have one yet – so the claw-back rules in the Property (Relationships) Act 1976 don't apply. Gifting spread over a longer period would be risky because of the claw-back rules. John is better transferring everything immediately.

Protection against creditors

Trusts are often recommended if you own your own business. You may need protection against possible claims from creditors. There's nothing wrong with putting assets into a trust if you don't have any liabilities at the time, or if you retain sufficient assets to meet your potential liability. In this situation it makes sense to put everything into a trust immediately. You may need to talk with your accountant and complete a solvency statement which will show the actions you are taking are not designed to defeat the rights of creditors.

Another option, depending on your circumstances and the advice of your accountant, may be to adopt a variation of the gifting programme. This would involve selling assets at market value to the trust, leaving the purchase price owing, giving away as much as possible of that amount but leaving enough still owing to you from the trust to cover liabilities such as a mortgage.



Jane and her business

Jane's business is going well but she is concerned that if anything did go wrong, she and her husband Tom could lose their family home. Before Jane and Tom transfer their property and their investments to a trust, they are advised to sign a solvency statement. Their lawyer draws up gifting documents tailored to their specific circumstances. They 'sell' their property at market value to the trust, treat most of the sale price as a gift and leave some money owing to them by the trust which is sufficient to cover any liabilities such as their mortgage and business borrowings.

Claims against estates

Assets may be transferred to your trust in order to avoid the risk of a claim against your estate under the Family Protection Act 1955, the testamentary promises legislation or other laws. Assets which are held in a trust don't form part of your estate and are not subject to attack under this legislation.

If a gifting programme has been used as part of the arrangements for transfer of assets to a trust, then the amount still owing to you at your death is part of your estate. This can be claimed under the Family Protection Act 1955 and similar legislation. If a gifting programme is used for some other reason, it's important that the amount left owing to you by the trust is completely given away before you die.

Timing is everything

What assets you give to the trust, and how you go about putting those assets into your trust, will depend on your reasons for wanting to establish a trust in the first place. Many people have more than one reason for wanting to form a trust. In this situation, it's important to be clear which is the most important because this may help you decide whether you need a gifting programme or not.

Each person's circumstances will be slightly different and it's important you talk this over with us. As time goes by, you will need to make changes and it's important you review the way your trust has been set up to make sure it still meets your needs.

While there can be no hard and fast rules, as a general guideline, if your main concern is:

- ✦ To ensure there are no claims against your estate after you die, then you need to give as much as possible to a trust during your lifetime
- ✦ About a claim by a possible future spouse or partner, then anything which might possibly be treated as a relationship property later on needs to be in a trust and completely gifted before the relationship starts. If you are already in a relationship, talk with us about an agreement to contract out of the Property (Relationships) Act 1976
- ✦ Possible future creditors, then you should gift as much as possible to your trust while still retaining enough in your own name to meet current known liabilities, or
- ✦ Rest home costs, then you could consider a gifting programme within the limits set by the Ministry of Social Development. It's important to remember that these rules can change. By the time you need rest home care, the rules may be totally different.

If you've a gifting programme it's important to discuss this with us to check that you're within the current rules before completing each year's gifting.





Decisions to be made

There are a number of important decisions that must be made when you're considering establishing a family trust. These include deciding when to establish your trust, who should be the trustees, who will be beneficiaries and so on. These are discussed in more detail below.

The trust deed

The trust deed sets out the rules about how your trust is to be managed and who is to benefit. As it can often be difficult to change at a later time, the trust deed needs to be as flexible as possible, while at the same time reflecting your intentions in setting up the trust.

Most modern trust deeds give the trustees power to make changes to the administration clauses. Either the trustees or a named appointer may be given power to add and remove beneficiaries. There is a limit as to how far you can go in allowing major changes to a trust. If changes later prove necessary and there is no power to do this under the trust deed, it may be necessary to apply to the High Court which would be very expensive.

Name of the trust

The trust deed will usually give a name for the trust. A distinctive name should be chosen that will help maintain the separation between your own assets and those of the trust. There is no central register of trust names, so any name can be chosen within reason.

The name should be easily recognisable, for instance a name such as the Smith Family Trust may not stand out from the crowd. Many people are creative with the trust name and others prefer simplicity by using the family name such as the Tom & Jane Green Family Trust.

Trustees

Trustees hold the title to trust assets in their own names and have the power, subject to the trust deed, to deal with those assets as they see fit. Trustees must:

- ✦ Be over 18 years of age
- ✦ Be mentally capable
- ✦ Be aware they have a personal liability for any losses that may be incurred by the trust because of their own dishonesty or negligence
- ✦ Understand that they are personally liable for taxes and other charges, such as property rates, payable by the trust
- ✦ Acknowledge that they may be personally liable for trust debts, or guarantees given by the trustees, although an independent trustee may be able to contract to have their liability limited to the value of the assets held by the trustees, and
- ✦ Be trustworthy, as they must manage the trust's affairs in a way that will provide the maximum benefits possible to the beneficiaries.

Settlers can be both trustees *and* beneficiaries of their own trust.

The trust deed should give at least one person the power to appoint additional trustees and to remove any trustee from office. The settlor usually has this power of appointment and removal, and the settlor should be able to pass this power on to others while alive, or by his or her will.

Independent trustee

If you are a trustee of your own trust, it's recommended that an independent trustee is also appointed; this helps to protect the trust from a claim by a former spouse or partner, or creditors that the assets are still at the disposal of the settlor.

The independent trustee could be, for example, a trusted friend or a professional adviser. We can advise about setting up a company to act as a trustee. Such a company should not be confused with the statutory trustees recognised by the legislation such as Perpetual Guardian.

Setting up a company to be the trustee can have some advantages: the company will not retire, die or become mentally incapable. It also allows for a range of people (the directors are normally the partners or directors of the professional firm) to sign documents for the trust management company rather than relying on a single person who may be overseas or otherwise unavailable. However, there can be disadvantages with this arrangement and you need good legal advice before you decide to appoint such a company as a trustee. For example, the company

may qualify as a 'financial entity' and be required to file additional information because of Foreign Account Tax Compliance laws (FATCA).

Independent trustees should not be able to benefit under the trust, so that they are truly independent.

Trustees have personal liability for any losses the trust may incur. Independent trustees may, by agreement with individual creditors, have their liability limited to the assets of the trust, in order to limit any future claims against them, other than as a result of their own dishonesty or negligence.

Appointer

Most trust deeds say who is to have power to appoint and remove trustees. Often this person is given a formal title such as 'appointer' and is given power to hand on this role to someone else.

Some mechanism for replacement of trustees on death or incapacity is important. You should check what your deed says about the removal of any trustee, including the settlor, who no longer has mental capacity. The appointer may also be given power to appoint and remove beneficiaries.

Protector

Some trust deeds provide for a protector to be appointed. Protectors are not trustees, but their approval may be required for a range of important decisions such as capital or income distributions, or variations to the trust deed. Protectors don't need to be involved with the trust on a day-to-day basis or to sign documents such as bank loan and security documents.

This arrangement simplifies the administration of the trust but retains the involvement of an independent person in major trustee decisions.

Special trust adviser

It's also possible to appoint a special trust adviser (previously known as an advisory trustee) to work with the trustees. As with the role of protector, this role can be restricted to specific trust assets. The law gives trustees protection if they act in reliance on advice from a special trust adviser.

Appointing a special trust adviser can be a good way to make use of the knowledge or experience of a family member or friend, or to involve someone from the wider family group.

Beneficiaries

Anybody can be a beneficiary of a trust. The most common groups of beneficiaries are relatives, close friends, charities and other trusts established for the benefit of these beneficiaries. A charitable trust, a company or another trust can also be a beneficiary.

To meet a family's changing needs, most trust deeds include the power to add more beneficiaries after the trust has been established. Some trust deeds say that this power ceases when one spouse/partner dies. This can avoid the surviving spouse/partner being seen to favour a new partner or stepchildren. It is, however, becoming more common for trust deeds to allow this appointer role to be handed on from settlor to someone else, or to two or three people, when the settlor dies or is no longer mentally competent.

It's important to remember that discretionary beneficiaries don't have an automatic right to receive benefits from the trust; they only have a right to be considered by the trustees when the trustees decide to make benefits available. This means that the group of beneficiaries you choose should be wide enough to include people who you actually want to benefit from the trust but not so wide that the trustees have to consider the needs of a large disparate group. Beneficiaries also have rights to trust information.

You will also need to think about who will receive whatever remains of the trust assets when it is wound up. These people are usually called the 'final beneficiaries'.

One or more trusts?

It may be that more than one trust should be established to protect the interests of a single family. This arrangement is particularly suitable where:

- ✦ There's a particular need to separate the ownership of a family's business assets from its lifestyle assets, such as the family home or holiday house
- ✦ One or both partners have children from previous relationships; setting up a separate trust for each partner ensures that the interests of each partner's own children will be protected, or
- ✦ A business activity is being carried on.

How much control is too much?

Setting up a trust involves giving away property to the trust. You can retain some powers but it's important not to go too far. If you retain too much control you may find you do not get all the benefits of a trust.

Clayton v Clayton⁴ – Vaughan Road Trust decision



Mr Clayton set up a trust but retained extraordinarily wide powers: he was the only trustee; he had power to appoint and remove trustees; he had power to add and remove beneficiaries; he was allowed to act completely in his own personal interest; he did not need to consider the needs or welfare of any other beneficiary.

The Supreme Court decided Mr Clayton had such wide powers that he could take back any of the trust assets at any time he wanted to. The court therefore considered this was relationship property and the trust property should be shared equally with his former wife under the Property (Relationships) Act 1976.

The case demonstrates the risks of retaining too much control.

⁴ *Clayton v Clayton* [2016] NZSC 29; [2016] NZFLR 230.

Webb v Webb⁵



After Mr and Mrs Webb were married in New Zealand, Mr Webb set up the Aorangi Trust that held property in the Cook Islands. Mr Webb also set up the Webb Family Trust that owned shares in his business.

Mr Webb had arranged for a business colleague to sign as settlor on the trust deed for the Webb Family Trust, but the court ruled Mr Webb was the real settlor and must be treated as the settlor for legal purposes. The court decided that Mr Webb had never relinquished control over the trust assets. Under both trust deeds, Mr Webb retained power to take back the trust assets at any time. Mr Webb was the only trustee of the Aorangi Trust. In the Webb Family Trust, Mr Webb was only one of the trustees but 'the bundle of rights which he retained is indistinguishable from ownership,' said the court.

The trust assets were therefore treated as matrimonial property and Mrs Webb was entitled to a half share.

⁵ *Webb v Webb* [2020] UKPC 22 – a decision of the Privy Council on appeal from the Cook Islands.





Completing your estate plan

Establishing a family trust doesn't stop when the trust deed is signed. There is other important documentation that should be aligned with your family trust deed including:

- ✦ A will dealing with your personal estate
- ✦ A letter of wishes, and
- ✦ Enduring Powers of Attorney (for property, and for personal care and welfare)

You may also need to have a relationship property agreement if relationship property is being transferred to the trust.

The transfer of a house or land to the trust will also require further legal documents to register the change of ownership; it may also be necessary to prepare and register new mortgage documents. If a sale and gifting programme is needed (see page 20), this will require a number of different documents.

Your will

Your new will should include provisions about:

- ✦ Specific gifts or items to be left to named people
- ✦ Other household and personal items
- ✦ Your other remaining assets, usually given to your trust
- ✦ The debt owed to you by your trust, if any, which would normally be forgiven
- ✦ Transfers of your powers to appoint and remove trustees under the trust deed
- ✦ Appointment of guardians if you have young children, and
- ✦ Any instructions regarding organ donation, funeral arrangements, cremation or burial.

Letter of wishes

It's also a good idea to sign a letter of wishes when the trust is established. This sets out in detail your actual intentions for the trust and, in particular, it covers things such as:

- ✦ How trustees should deal with the trust assets
- ✦ When and how you think the beneficiaries should receive distributions, and
- ✦ How the trust will operate after your death.

A letter of wishes provides useful guidance for the trustees who will operate the trust after your death. It is not, however, binding on the trustees. The letter can be updated at any time by you, as settlor.

Enduring Powers of Attorney

You should also sign Enduring Powers of Attorney (EPAs) covering both your personal property, and your personal care and welfare. These documents give a named person, the attorney, the power to act on your behalf.

Property

An EPA in relation to property can cover all of your personal assets which include any land and buildings that you own as well as bank accounts, vehicles and any other form of personal property. You can state when this EPA is to take effect, which could be at any time, or only if you become incapacitated, mentally incapable, or if you travel or move overseas.

A property attorney may be a person such as your spouse or partner, friend or your lawyer, or one of the three recognised trustee corporations. You may appoint more than one attorney.

Personal care and welfare

For the EPA in relation to personal care and welfare, you would generally appoint a close family member or a friend as attorney. An organisation cannot be appointed to this position.

This type of EPA can only be used if you become mentally incapable of looking after your own personal care and welfare. Your attorney can ensure your welfare, medical and residential needs are taken care of. You may only appoint one person as attorney, but you may also appoint a replacement (in case the first one named is no longer able to act).

Other documents

We may also recommend that you sign a document to delegate your role as trustee. This will state who can sign documents on your behalf in certain circumstances such as short term incapacity. An EPA cannot be used in respect of a trustee's role.





Family trust administration

It's important that your family trust is administered correctly. If you and the trustees fail to treat the trust as a genuine trust, or you can be seen to be in complete control, all of the benefits of having a trust may be lost (see page 29).

Trustees have a number of duties in law. The trust deed may affect how these duties apply. It's also important that trustees remember that they are only allowed to do those things which they have legal power to do. Again, there are some standard powers set out in law, but the trust deed can expand on these.

A trustee's duties

These are now set out in the Trusts Act 2019. There are mandatory duties and default duties. The trust deed cannot override the mandatory duties. Default duties can be modified or excluded by the trust deed. The deed can either say this explicitly or it can be implied. We have a duty to explain the clauses which do this.

The mandatory duties of trustees are:

- ✦ Section 23: Duty to know terms of trust
- ✦ Section 24: Duty to act in accordance with terms of trust
- ✦ Section 25: Duty to act honestly and in good faith
- ✦ Section 26: Duty to act for benefit of beneficiaries or to further permitted purpose of trust, and
- ✦ Section 27: Duty to exercise powers for proper purpose

The default duties of trustees are:

- ✦ Section 29: General duty of care
- ✦ Section 30: Duty to invest prudently
- ✦ Section 31: Duty not to exercise power for own benefit
- ✦ Section 32: Duty to consider exercise of power
- ✦ Section 33: Duty not to bind or commit trustees to future exercise of discretion
- ✦ Section 34: Duty to avoid conflict of interest
- ✦ Section 35: Duty of impartiality
- ✦ Section 36: Duty not to profit
- ✦ Section 37: Duty to act for no reward
- ✦ Section 38: Duty to act unanimously

Above all, the trustees are obliged to act honestly and in good faith for the benefit of the beneficiaries.

Prudent investment

The trust deed may contain specific rules about how the trustees are expected to invest. If not, then the trustees must invest prudently.

Prudent investment is defined in detail in the law. It's not just a matter of trustees doing what they consider to be prudent. Prudent investment by trustees requires them to invest in the way that an ordinary prudent person would do when investing money that is held for the benefit of other people.

The Trusts Act 2019 sets out a number of factors which trustees should take into account, where appropriate, when making investment decisions. These include:

- ✦ The objectives or purpose of the trust
- ✦ Desirability of diversifying trust investments
- ✦ Nature of existing trust investments
- ✦ Need to maintain the real value of the trust
- ✦ Risk of capital loss or depreciation
- ✦ Potential for capital gain or growth
- ✦ Likely income return

-
- ✦ How long the proposed investment is for
-
- ✦ How long the trust is likely to last
-
- ✦ Marketability of the proposed investment, ie: can it be cashed in if need be?
-
- ✦ Total value of the trust fund
-
- ✦ Tax issues
-
- ✦ The likely effect of inflation, and
-
- ✦ Investment strategy.
-

Although not all of these matters will necessarily be relevant in all circumstances, they do provide useful guidance for any trustee when making investment decisions.

A passive trustee who merely rubber-stamps the decisions of co-trustees could be exposed to claims by beneficiaries for losses incurred by the trust.

Trustee decision-making

Section 38 of the Trusts Act 2019 requires trustees to agree unanimously on any decisions they take. However, it is possible for the deed to say that a decision of a majority of the trustees will be binding.

If only a majority decision is required, all the trustees are still responsible for the decision; some people may not accept appointment as a trustee on those terms.

The trustees may agree that for some activities such as operating a bank account, they will allow one or more trustees to control the account. These arrangements should be recorded in the minutes of a trustees' meeting. The trustees need not record the reasons for their decisions, only the decision itself.

Trustee liability

Trustees are personally liable for all debts incurred by the trust, including income tax and GST liabilities. Where loans are arranged from banks or other lenders, it's customary for the liability of independent trustees to be specifically limited to the net assets of the trust. It's also quite reasonable for independent trustees to request a settlor to personally indemnify the independent trustees against any losses they incur as a result of the trusteeship.

Personal liability can be avoided by having a company act as a trustee. This is advisable if the trust is GST-registered, or is a trading or development trust.

If your independent trustee is a trust management company, however, a director has further responsibilities and liabilities. There is also a risk the company could

qualify as a financial institution (FI) under the laws relating to international exchange of tax information, for example, US legislation such as FATCA. In that case, additional compliance and information filing may be required.

Tax

Each trust is different in terms of its tax liability. Where appropriate, trustees should take specialist accounting advice to ensure the trust complies with its tax obligations.

It should be noted that a trust is a separate taxpayer; it must file a tax return if it receives income.

The trustees need to decide, within 12 months following the end of each financial year, how any income earned by the trust will be treated. This needs to be recorded in a signed resolution or minute. The trust income can be:

- ✦ Distributed to all or some of the beneficiaries and taxed at their tax rate (there are limitations for distributions to children under 16)
- ✦ Treated as trust income and taxed at the trustee rate (currently 33%), or
- ✦ A mixture of these options.

If a resolution isn't passed within the 12-month timeframe, the income will be treated as trustees' income and taxed at the 33% tax rate. As a result, any potential tax savings will be lost.

Foreign trusts

You may have heard discussions about 'foreign trusts.' These are typically trusts where neither the settlors nor any of the beneficiaries have lived in New Zealand. Usually the trust assets are all overseas and no tax is payable in New Zealand. This guide is not intended for people in this situation. The purpose of this guide is to advise ordinary New Zealanders who will meet their legal obligations but want to protect their property from other risks.

Accessing trust income

Under most modern trust deeds, distribution of trust income is totally at the discretion of the trustees. They may do any of the following:

- ✦ Accumulate and retain within the trust all or any part of the trust's income
- ✦ Make distributions of income to any one or more of the beneficiaries in any proportion, and/or

-
- ✦ Credit income to the current account of any beneficiary within the trust. The income will then be taxed as beneficiaries' income and will be payable to the beneficiary on demand.
-

Accessing trust capital

During the term of the trust, distributions of capital are usually made at the discretion of the trustees. Some trusts don't allow capital distributions or they may limit the percentage of the capital that can be distributed. Capital can usually be paid to any one or more of the discretionary beneficiaries.

If you are a beneficiary of the trust, you can receive distributions of capital if the deed permits and if the trustees decide to make such a payment. Alternatively, if you are owed money by the trust, you may be able to access the trust capital by demanding repayment of all or part of the outstanding loan (subject to the terms of the loan agreement).

Using a house owned by your family trust

If your family trust owns the family home, the trust can make the house available to you and your family to live in, provided that you are beneficiaries of the trust. The trust may allow you to live in the house on the basis that you pay the rates, insurance premiums and other day-to-day outgoings in lieu of rent. This decision of the trustees should be recorded in writing and should be reviewed regularly as part of the trustees' review of the trust's investment policy. There are usually no income tax implications for beneficiaries living in a property owned by the trust.

Trustees should ensure that the insurance policies for the family home, as well as rates demands, are in the name of the trust or trustees.

Contents policies should be in the personal name of the settlor, unless there are items which have been transferred to trust ownership, in which case two contents policies may be necessary.

Trusts carrying on business and investing

The Trusts Act 2019 now gives the trustees an unrestricted power to act as if the trust were a real person with few limitations on what the trustees can or cannot do. Trusts can therefore conduct a business in the same way as a real person. Some care needs to be taken, however, where a trust is conducting a business as legal, taxation and risk management issues can arise.

As a risk management tool when carrying on a business, more than one trust is sometimes recommended in order to divide the ownership of the family home and passive investments from business ownership. Trusts which have a fund manager

to manage investments may have additional compliance requirements under international tax information exchange rules, such as FATCA.

Relationship property issues

If you are currently married, or in a civil union or de facto relationship of more than three years' duration, then it's likely that all or a significant part of your assets will be relationship property. If you and your partner separate at any point after the three-year threshold, that relationship property must, except in certain limited circumstances, be divided equally between you both. There are some circumstances in which the three-year period is reduced significantly, including having a child living with you.

Assets fully transferred to a trust before the start of any relationship will be trust assets, not your own property. So they should not be subject to relationship property claims, although there are claw-back rules in the Act.

Any debt not gifted to the trust may be relationship property if it has not been protected as separate property. We may recommend an agreement to contract out of the Property (Relationships) Act 1976 to avoid these complications. Transferring family assets to a family trust, therefore, has a significant impact on your relationship property rights.

It's particularly important for you to understand the effects of the relationship property legislation and other rules of law on your family trust arrangements as:

- ✦ In some cases, transferring assets to a trust will mean you no longer have relationship property rights which you would have had otherwise
- ✦ If relationship property is transferred to a family trust, the court has the power to compensate an aggrieved spouse or partner who has been disadvantaged by the trust arrangement
- ✦ Under section 182 of the Family Proceedings Act 1980, if a married couple divorces, the court can rewrite a trust they had set up before or during their marriage – this applies also to civil union couples but not to de facto couples, and
- ✦ A former spouse or partner may have a claim based on contributions made to a trust property, for example, redecoration, gardening or other improvements, and the courts may award compensation for contributions made.
- ✦ The Law Commission is currently reviewing the law relating to relationship property. Some of these rules could change in the future.



***Ward v Ward*⁶** **(Section 182, Family Proceedings Act 1980)**

This 2009 Supreme Court decision illustrates how section 182 can work.

Mr Ward was part-owner of a family farm. He bought out the other owners shortly after he married Mrs Ward. Some years later the Wards set up a trust and transferred the farm to it. The beneficiaries were Mr Ward, Mrs Ward and their children. Three years later the Wards separated and the relationship between them deteriorated so that they and their independent trustee could not reach unanimous decisions as required by law.

The Family Court resolved the impasse by dividing the property between two trusts; one for Mrs Ward and the children, and one for Mr Ward and the children. Mr Ward appealed but both the Court of Appeal and the Supreme Court agreed with the division into two trusts.

⁶ *Ward v Ward* [2009] NZSC 125; [2010] 2 NZLR 31.

When relationships terminate and a trust owns the assets, the trustees will generally ensure a fair resolution is reached. In most circumstances, the trustees would resolve to transfer half the value of a jointly established trust to each of the partners or to a new trust established by each of them. Alternatively one partner could continue with the existing trust and the other partner could establish a new trust and have half the value of the joint trust transferred to it.

Your trust deed can include a clause to say what is to happen to the trust assets if you separate. You should talk about what you envisage in the event of separation.

Life of the trust

The law now allows for trusts to last for up to 125 years, but a shorter period can be stated in the trust deed. Usually, the trust deed will allow the trustees to distribute the trust assets before the 125 years is up. This greater flexibility allows the trustees to decide the best time to distribute, taking into account family members' needs and abilities, as well as tax considerations and investment opportunities.





What will a family trust cost?

Establishing a family trust

There are legal and other expenses involved when establishing a family trust. The cost will vary depending on the time spent in helping you reach a decision on what is best for you and the need to develop a tailored structure to meet your family's specific needs.

Generally this cost will include drafting a trust deed, new wills for you and your partner or spouse, a letter of wishes, EPAs and perhaps also a relationship property agreement, or a delegation of the trustees' functions.

If you are transferring your family home or other real estate to your trust, there will be costs for the preparation and registration of documents to transfer ownership and redocument any mortgages. For those settlors with a mortgage on the property being transferred, there will be costs to rearrange the loan securities.

Annual costs

You should allow for the time and cost involved with meetings of trustees, accounting and administrative requirements, and possibly gifting documents.

If your trust is to receive income and pay expenses, a separate bank account should be opened. Trustees have a duty to keep trust money separate from their own personal funds. Having a trust bank account can make it easier to prepare financial statements and tax returns.

While each trust has different requirements, we can give you a cost estimate to establish your family trust, to transfer the assets to it and for the annual cost to run your trust.

Glossary

Advisory trustee: Appointed in the past to provide advice to the trustees, an advisory trustee was not a legal trustee, but the trustees could rely on this advice. Now known as a 'special trust adviser' – see page 46.

Alter ego trust: A trust which is a 'puppet of the settlor'. This term was first adopted in Australia which has quite different matrimonial laws. The New Zealand courts have ruled that this is simply a form of sham trust; see 'sham trust' on page 45.

Appointer: The person who is given power to appoint and remove trustees and/or beneficiaries. Usually the settlor will have this power initially but may hand it on to someone else (if the trust deed provides for this).

Beneficiary: A person, company, another trust or other entity that is entitled to receive benefits from a trust.

Bright-line rule: Profits made on the sale of residential property within 10 years of purchase, or five years if it is a new build, are taxable income. The rule does not apply to your main home, inherited property or if you are an administrator of a deceased estate.

Courts: In New Zealand, the courts which may deal with trust matters, in ascending order, are the Family/District Court, High Court, Court of Appeal and the Supreme Court.

Delegation: Sections 70–73 of the Trusts Act 2019 allow trustees to sign a power of attorney (but not an EPA) so that someone else can take over their role as trustee in some circumstances such as temporary incapacity.

Discretionary beneficiary: A discretionary beneficiary may receive benefits from the trust but only if the trustees decide to provide benefits to the beneficiary. A discretionary beneficiary may also be a final beneficiary.

Distribution: Payment or transfer of an asset from a trust to a beneficiary.

Enduring Power of Attorney (EPA): Under an EPA another person is appointed to act on your behalf. This power can apply to your own property and/or your personal care and welfare. A property EPA can either be effective immediately it is signed or might only become effective if you lose mental competence. It's your decision when this EPA will become effective.

Family Court: Deals mainly with separation, divorce, care of children and relationship property. Sometimes, however, the Family Court becomes involved in trust issues.

FATCA: Foreign Account Tax Compliance Act. This is part of the US tax code but has indirect effect in New Zealand through an agreement signed by the US and New Zealand governments. Certain financial

institutions (including some trustees) may be required to file information with New Zealand authorities.

Final beneficiary: A beneficiary who is entitled to share in the remaining trust assets when the trust comes to an end, usually after 125 years.

Forgiveness of debt: A debt is forgiven when it is acknowledged that all or part of a debt owing to you doesn't need to be repaid. This is a gift that must be recorded in a deed.

Gift: A gift is made when an asset is transferred to another person or organisation and nothing is received in return. Gifts can be made to a trust either by directly transferring assets or by forgiving all or part of a debt the trust owes to you. If you apply for a rest home subsidy from the government, there are strict limits on the amounts of gifts made previously – see page 20.

Gift duty: A form of tax abolished in 2011. The tax was usually avoided by a notional sale to a trust at market value, leaving the sale price owing and then reducing that debt by the maximum allowed (\$27,000 per 12 months). This was known as a gifting programme.

Gifting programme: A system of annual gifting in reduction of debt traditionally used to avoid gift duty as above. Now used mainly where there are possible rest home issues – see page 20.

High Court: The main court which has authority in respect of trusts.

Independent trustee: A trustee who is not a beneficiary.

Letter of wishes: A written summary of goals and objectives for a family trust. It can also be known as a 'note for guidance for trustees' or a 'memorandum of wishes'.

Power of attorney: A document that states who may sign documents or make decisions on your behalf. A simple power of attorney is cancelled if you are no longer mentally competent but an Enduring Power of Attorney (EPA) remains in force even if you become mentally incapacitated.

Primary discretionary beneficiary: Beneficiary given priority ahead of the other beneficiaries. Since the law normally expects all beneficiaries to be treated in an even-handed manner, it's usually wise for the trust deed to make it clear who are to be the main beneficiaries, for example, the settlors during their lifetimes and then their children.

Protector: A person appointed by the settlor and usually the person who has the power to appoint or remove trustees and beneficiaries. Protectors can be given other powers such as approval of distributions.

Settlor: A person who creates a trust by transferring assets to trustees subject to the provisions of a trust deed.

Sham trust: A structure which was set up to look like a trust but was never intended to be a trust; the supposed settlors treat the assets as their own. In practice, the court requires considerable proof that the settlor deliberately intended to deceive before it will say a trust is a sham.

Special trust adviser: This adviser can be named in the trust deed or can be named later on by the trustees. The trustees can rely on this advice. In many situations, the trustees are protected from liability if they rely on this advice.

Supreme Court: The highest court in New Zealand.

Trust capital: Assets of the trust. These could include real estate, term deposits and share investments, and include the increases in the value of these assets, and gifts made to the trust.

Trust deed: The document that establishes the trust and includes a set of rules for the operation of that trust.

Trust income: The money a trust makes from the investment of its capital. It can include interest, rent and share dividends.

Trustee: A person appointed to hold trust assets for the benefit of beneficiaries. A trustee has legal control of the trust assets.

Trusts Act 2019: This is the main law dealing with trusts in New Zealand. It came into force on 30 January 2021; it replaced the Trustee Act 1956.

Will: A legal document that specifies how you want your personal assets to be administered and distributed after your death.

Index

A

Advisory trustee 44; see also special trust adviser
Alter ego trust 44
Appointer 27, 28, 44
Assets 6, 7; see also property
 Business owners 11
 State assistance eligibility 16, 20, 23
 Timing of transfers 22–23
 Transferring 19–23

B

Bank account 37
Beneficiaries 5, 28, 44
 Age of receiving money or property 9
 Discretionary 7, 8, 28, 44
 Final 7, 45
 Primary 7, 45
 Provision of information 8, 9, 16–17
Benefits (welfare), eligibility 16
Bright-line rule 12, 44
Business, conducting 39–40
Business owners 11

C

Capital distribution 27, 39
Capital gains tax 16
Charitable purposes 17
Charitable trusts 6, 17
Children
 Education costs 6
 Property interests 6, 12, 13, 21, 28
 Special needs 6, 13–14
Civil unions see relationship property
Claw-back rules 13, 20–21, 40
Claymark Trust decision 13
Clayton v Clayton 13, 29
Company
 Compared with a trust 15
 As a trustee 26–27, 37–38
Confidentiality 8, 16–17
Costs 43
Courts 44
Creditor claims 21–22, 23, 26
D
De facto relationships see relationship property

Delegation of trustee role 9, 33, 44
Development trusts 12
Disabilities or impairments 6, 13–14
Distributions 27, 38–39

E

Enduring Power of Attorney (EPA) 32, 44
Erceg v Erceg 8
Estates, claims against 14, 22–23

F

Family Court 41, 44
Family home 19, 22, 28, 39, 43
Family Proceedings Act 1980 40, 41
Family Protection Act 1955 14, 22
Family protection claims 6, 14
Financial entity 27
Foreign Account Tax Compliance laws (FATCA) 27, 38, 40, 44–45
Foreign trusts 38
Forgiveness of debt 45

G

Gift 45
Gift duty 6, 16, 45
Gifting programme 20,
21, 22–23, 45

H

High Court 8, 25, 45
Holiday house 6, 28
House owned by trust 39

I

Income distribution 27,
38–39
Income Tax Act 2007 15
Independent
trustees 26–27, 45
Information provision 8,
9, 16–17
Inherited property 6, 12, 21
Investment
 Managing 39–40
 Prudent 36–37

L

Land
 Titles 9
 Trading in
 development 12
Law changes 17
Law Reform
(Testamentary Promises)
Act 1949 14
Letter of wishes 32, 45
Liability of trustees 7, 26,
37–38

Lifestyle assets 28
Look-through companies
(LTCs) 15

M

Matrimonial property *see*
relationship property
Mental capability 9, 26,
27, 28, 32, 44

N

Name of trust 25

P

*Penny & Hooper v Inland
Revenue* 15
Portfolio investment
entities (PIEs) 15
Power of attorney 45;
see also Enduring Power
of Attorney
Property 6; *see also* land
 Enduring Powers of
 Attorney (EPAs) 32
 Trading in property
 development 12
Property (Relationships)
Act 1976 12, 21, 23, 29, 40
Protector 27, 45
Prudent investment 36–37

R

Record keeping 7, 17
Relationship
breakdown 6
Relationship property 6,
12–13, 17, 26, 29, 40

Children from previous
relationships 28
Effects of legislation
and rules of law 40–41
Gifting assets to avoid
future claims 12–13,
20–21, 23
Three-year
threshold 13, 40

Rental properties 19
Rest home subsidies 6, 16,
20, 21, 23
Risk of conducting
business 3, 6, 11, 39

S

Settlor 5, 16, 26, 28, 45
 As trustee 7, 26, 27
Sham trusts 7, 45
Solvency statement 21, 22
Special trust adviser 27,
44, 45
State assistance,
eligibility 16
Succession tax 16
Supreme Court 8, 13, 15,
29, 41, 46

T

Tax
 Charitable purposes
 rebate 17
 Land sales
 association 12
 Liability, minimising 6, 15
 Obligations 38

Testamentary promise claims 6, 14, 22

Trading trusts 12

Transferring assets *see under* assets

Trust capital 46; *see also* capital distribution

Trust deed 6, 7, 17, 25, 46

Trust income 46; *see also* income distribution

Trustees 5, 7, 26, 46

Accountability 16–17

Appointment, removal and replacement 9, 26, 27

Company as a trustee 26–27, 37–38

Decision-making 37

Delegation of role 9, 33, 44

Duties 7, 9, 35–36

Independent 26–27, 45

Liaability 7, 26, 37–38

Trusts

Benefits 6, 11–17

Compared with companies 15

Control 28, 29

Description 5

Maximum duration 9, 16, 41

More than one trust needed 28, 41

Name 25

Summary of reasons for establishing 22–23

Trusts Act 2019 3, 5, 8, 9, 16, 35, 36–37, 39, 44

W

Ward v Ward 41

Wealth tax 16

Webb v Webb 29

Will 31, 46

V

Vaughan Road Trust decision 29



611 Mackay Street
PO Box 31, Thames 3500
DX GA25514
T 07 868 8680 | F 07 868 8718
info@purnell.nz | www.purnell.nz

