Estate planning for property investors

Legal, accounting and tax issues

By Grant Harris*

Estate planning involves arranging your affairs to ensure the orderly transfer of your assets and wealth in such a way that your intended beneficiaries receive the maximum benefit and enjoyment. Importantly, it should also provide for your desired lifestyle whilst you are still alive.

Estate planning should be an efficient and effective transfer of wealth between generations that can achieve protection of assets from creditors, protection of family assets from children's matrimonial claims, financial protection and education for children/grandchildren and can pass control of business assets. Conferring with your children and intended beneficiaries is recommended in order to ensure future inheritances are in the most appropriate form.

This article is not intended to be a comprehensive analysis of the many different techniques available; it's a general outline of certain aspects only. Obtaining accounting and taxation advice is critical to ensure estate planning arrangements do not trigger tax issues or get caught by general tax-avoidance rules.

WILLS

There is much more to estate planning than just having a suitable will. However, a will is a fundamental part. It deals with assets that are held in your personal name, such as bank accounts, jewelry, cars, perhaps shares in a Look Through Company (which are popular with property investors), but not assets owned by other entities such as, for example, a company or a family trust.

Careful consideration should be given to distributions made under a will in terms of potential challenges, such as under the Family Protection Act 1955, and also to minimise the risk of someone receiving an asset directly that subsequently becomes subject to creditor or relationship property claims. Other important aspects of your will include the appointment of suitable executors and forgiveness of debt provisions (where appropriate).

FAMILY TRUSTS

A family trust may well already be a part of a property investor's legal structure and if so the matters covered below should be considered and tailored to existing structures as part of the estate planning process.

A properly structured, managed and administered family trust is a useful tool for estate and succession planning. As well as having asset protection benefits, they can provide the ability to make tax-efficient distributions and distributions to trusts established for beneficiaries. A will can also dovetail into the trust such that the residue of a personal estate can be transferred to the trust upon the death of the surviving spouse.

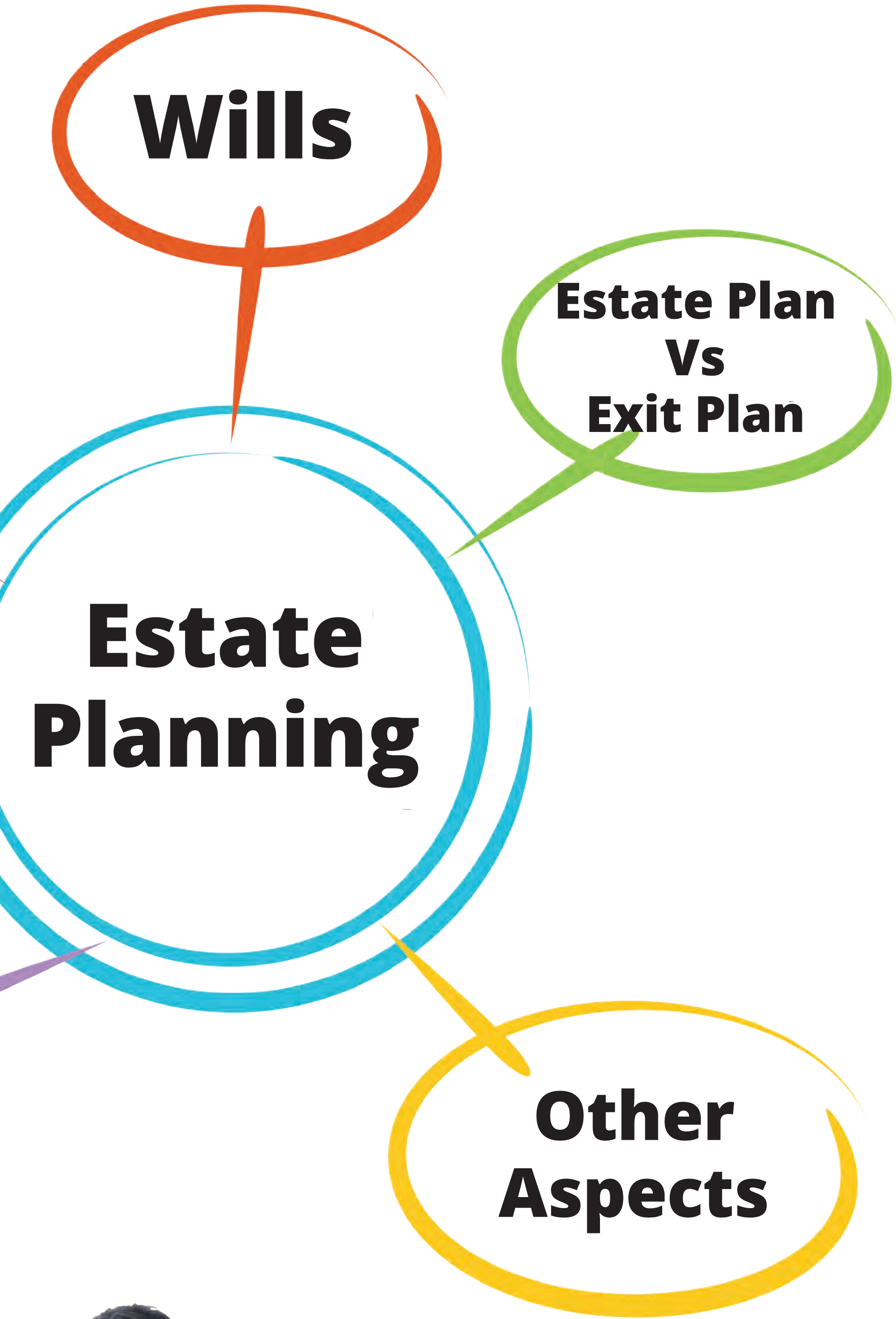
Family Trusts

Written instructions to the trustees record how a settlor of the trust wishes the trust to be administered after they have died. These written instructions are recorded in a Memorandum of Guidance/Memorandum of Wishes (Memo of Wishes) that, while not legally binding on trustees, is fundamentally important. The Memo of Wishes could provide general guidance on the application of trust assets, like for the purposes of beneficiaries' education, health, general welfare, etc, or can be very specific regarding certain assets and access to income, as well as the manner in which distributions are made to protect the beneficiary from, for example, relationship property claims.

The Memo of Wishes provides flexibility as it can be amended and updated from time to time should circumstances change without the need to make fundamental changes to the underlying trust structure.

The power to hire and fire trustees (the power of appointment) is an important check and balance in the estate plan and is the ultimate control of the trust assets after you have died. Therefore, someone suitable needs to be appointed to succeed in holding the power of appointment after your death. That could be addressed either in your will or by a separate deed (depending on how your Trust Deed has been drafted).

Having a suitably qualified independent trustee appointed is advantageous due to their impartiality and they can assist with the proper management and administration of a trust alongside the professional advisors.



OTHER ASPECTS

Enduring Powers of Attorney are important documents that supplement your estate documentation and are used by your attorneys should you become unable to deal with your own affairs or personal welfare (through mental incapacity, or otherwise).

Life insurance can be used as a means of paying down debt, to fund specific distributions and to provide funds to be invested for future family support and maintenance. Life insurance policies can be owned by a trust, with proceeds being used for the benefit of the trust and its beneficiaries.

Your estate plan should be reviewed from time to time, particularly if there is a change in family circumstances, change in assets or changes to tax or other legislation. Generally speaking, it's good to carry out a review every five years, or earlier should circumstances require.

ESTATE PLAN VS EXIT PLAN

Long-term property investors may have generated a sizeable property portfolio during their lifetime. As mentioned earlier, ensuring a desired retirement lifestyle is achieved should also be a priority rather than an investor squirrelling away unrealised capital gains for use by other family members after they have died.

When creating (or updating) a workable estate plan, older investors should consider:

- A review of the property investment portfolio on a property-by-property basis to ascertain the performance of specific properties and whether the "opportunity cost" of holding the property could generate a higher retirement income if other asset types or classes were held as an alternative. Reducing specific underperforming investment properties to pay down debt could increase retirement income rather than retaining high-capital-value, low-yielding or low-performing properties to generate future (potential) capital gains the benefit of which would be received by the next generation; and
- Properties structured using existing interest-only loans can be a pitfall if the investor intends to live off the rental income. There could be an unpleasant surprise should the bank subsequently require repayment of principal and interest, drastically increasing the required repayments and reducing the anticipated income from that property.

Of course, not all property investment portfolios will be the same, but the two above aspects are important considerations for older investors – which is more attractive: the largest possible portfolio or earning higher retirement income from a smaller portfolio?

HARRIS TATE
Lawyers • Notaries

***GRANT HARRIS**
is a Director of Harris Tate Ltd and Immediate Past President of the Tauranga Property Investors Association.
P +64 07 578 0059 **E** grant@harristate.co.nz
W www.harristate.co.nz

Disclaimer: This article is general in nature and should not be treated as professional advice. It is recommended that you consult your advisor. No liability is assumed by Harris Tate Ltd for any losses suffered by any person relying directly or indirectly upon the article above.