

Special disability trusts

While they can be complex, special disability trusts have some really worthwhile benefits.

BY CRAIG MELDRUM

Most discussions on disability trusts start with parents wanting to set up a structure for the benefit of their disabled child to ensure that assets and income are used for their care, maintenance, support, education and entertainment. Concerns raised are generally around asset protection, taxation and estate-planning issues.

But what about social security? Anyone who has ever applied for the Centrelink disability support pension or the carer's payment/allowance knows full well the assets and income tests and medical hoops that need to be jumped through to qualify. What they don't always know is that if they are income support recipients themselves, gifting money directly to their disabled child will be caught under the deprivation rules, and starting a family discretionary or other fixed trust for the benefit of their disabled child or relative will be caught under the trust attribution rules. Without going into either in any detail, a gift of assets, or the setting up of a non-specific (all needs) protective trust for the benefit of a disabled relative can reduce the social security entitlements of the donor, the donor's spouse or the disabled relative.

In order to remove some of the barriers inherent in making financial provision for a severely disabled relative, the Federal Government amended the *Social Security Act*

1991 (SSA 1991) to encourage immediate family members to establish a special class of trust called a Special Disability Trust (SDT), designed exclusively for the care and accommodation of the disabled relative.

One of the main benefits is that trust income and assets up to the value of \$563,250 (as at 1 July 2010) do not affect the family member's social security payments or payments to a person under the *Veterans' Entitlements Act 1986*. The SDT asset threshold was originally set at \$500,000 on 20 September 2006 and is indexed annually. In addition, the social security deprivation rules which normally penalise gifting in excess of a nominal amount of \$10,000 per annum (or \$30,000 in any rolling five-year period) – and this same limit applies to couples as well as to singles – do not apply. For SDTs, gifts to the trust (to a total of \$500,000) from parents or immediate family members (ie, natural parents, legal guardians, adoptive parents, step-parents, grandparents, and siblings) will not affect the donor's social security payment or payments to a person prescribed under the Act.

Now or for the future

Grantors can establish SDTs while they are alive or as part of their wills. It is when included in a will as part of a parent or relative's estate planning that SDTs really earn their stripes. Without an SDT, there is the possibility that disabled beneficiaries under a will may lose some or all of their pension and entitlements when they receive their inheritance. For example, without an SDT, a disabled person who becomes entitled to \$500,000 under their parent's will would immediately become ineligible for a government pension.

Requirements and eligibility

A special disability trust must meet certain requirements. For example, it must:

- be "protective" in nature
- have only one principal beneficiary

(ie, the person for whom the trust is established)

- provide only for the accommodation and care needs of the principal beneficiary
- have a trust deed that contains the clauses as set out in the model trust deed
- have an independent trustee
- provide annual financial statements and conduct independent audits.

The disabled person in question must meet the definition of "severe disability" to be eligible to be a principal beneficiary. A principal beneficiary who has reached 16 years qualifies if the person:

- has an impairment that would qualify that person to receive a disability support pension, or to receive a service pension, or to receive an income support supplement, or
- has a disability that would qualify a carer for that person for a carer's allowance, or
- is living in an institution, hostel or group home in which care and funding is provided, and
- is not working and has no likelihood of working for a wage at or above the relevant minimum wage.

If the principal beneficiary is below 16 years old, the person must have a severe disability or severe medical condition within the meaning of the SSA (s1209M(4) SSA 1991). Statutory impairment tables (s94 SSA) detail the degree of physical, intellectual or psychiatric impairment based on medical, social and work function resulting in a continuing inability to work. The concept of severe disability or severe medical condition is covered in s197 SSA.

Assets and income

In terms of the assets able to be held within the trust, they cannot include an asset transferred to the trust by the principal beneficiary or his or her partner unless the transferred asset is a bequest or a superannuation death benefit and the transferor received the asset within three years of the

transfer or include any compensation received by the principal beneficiary.

The assets and income of the trust also cannot be used to pay an immediate family member or child of the principal beneficiary for care services or accommodation or be used to purchase or lease property from an immediate family member or a child of the principal beneficiary. This is to protect the interests of the principal beneficiary. It should be noted that in this regard, in determining the assessable assets of the SDT, the value of any right or interest in the beneficiary's principal home is disregarded.

It is important to note that there are rules governing the eligibility of transfer of assets to an SDT. One of the common questions I have received (where an adviser or accountant is seeking to maximise a client's social security payments) is; "when can they get the capital back?" No such luck. This transfer of assets to a SDT is an irrevocable gift. Section 1209Z of SSA shows that a transfer qualifies if the donor:

- is an immediate family member of the principal beneficiary
- receives (or the donor's partner receives) a social security or service pension
- is of pension age
- does not receive consideration for the transfer
- transfers the asset unconditionally.

Where neither the donor nor the donor's partner has reached pension age or is in receipt of a pension, the donor is deemed to have made the transfer at the time that the donor or the donor's partner reaches pension age. Accordingly, donors who do not initially qualify may take advantage of the concessional measures later when they do qualify.

An SDT ceases to qualify where the trust deed fails to comply with the statutory requirements or at the date of the death of the principal beneficiary.

Assets held by the trust form part of the principal beneficiary's estate.



What about tax?

There are no specific taxation benefits to mention where SDTs are concerned. They do not alter the income tax treatment of the transfer of assets and the taxation of beneficiaries of the SDT. Assets such as shares, units in trusts and real estate held on capital account transferred to the SDT to provide income or accommodation for the principal beneficiary carry potential CGT liabilities arising on the transfer of a CGT asset.

Where the beneficiary is a minor, and the child of the trustee, under

s102 ITAA 1936, the Commissioner may assess the trustee, rather than the minor, to pay income tax.

Generally, social security disability support pensions are exempt from income tax. However, income from an SDT is taxable under the ordinary trust rules (Part III, Div 6A ITAA 1936). A beneficiary who is presently entitled to a share of the net income of the trust and is not under a legal disability is taxable on that income at individual tax rates (section 97 ITAA 36). However, where a beneficiary is under a legal disability, the trustee must withhold and remit tax on that income as if a separate individual at individual tax rates (s98 ITAA 1936).

A beneficiary under a legal disability will not have to lodge a tax return, unless in receipt of other income (s100 ITAA 1936; Determination TD 92/159). Where no beneficiary is presently entitled to the trust income, the trustee may be assessed at the top marginal rate, unless the Commissioner exercises his discretion.

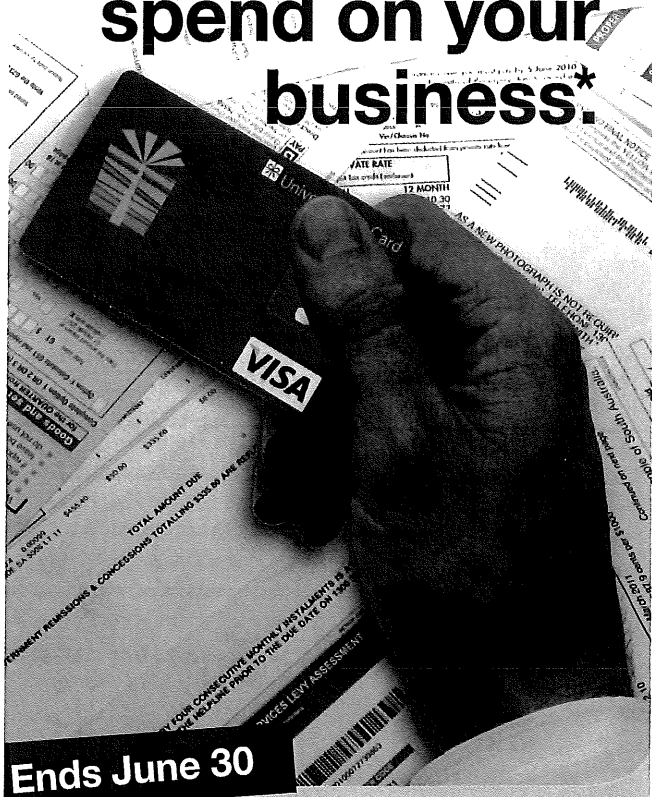
Encouraging disability trusts

As at 20 March 2009, the Government said some \$55.5 million in contributions had been made to SDTs. In order to make them more accessible and increase uptake, proposed changes have featured in the past two Federal Budgets.

In the 2009 Federal Budget, the Government announced it would ensure that the unexpended income of an SDT is taxed at the relevant beneficiary's personal income tax rate, rather than automatically at the top personal tax rate plus Medicare Levy (under s99A ITAA 1936), with effect from the 2008-09 income year. The Government also announced that it would extend the CGT main residence exemption to include a residence that is owned by a special disability trust and used by the principal beneficiary of the trust as their main residence, with effect from the 2009-10 income year.

Tax Laws Amendment (2010 Measures No 3) Act 2010 came

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There are some very beneficial outcomes for both the donors and the intended beneficiary.

into effect 29 June 2010 to secure these changes.

As part of the 2010 Federal Budget, the Government announced additional measures to be introduced from 1 January 2011. The proposed changes include:

- the ability to work up to 7 hours a week in paid employment (excluding work in an Australian Disability Enterprise)
- the trust can pay for the beneficiary's medical expenses, private health fund, and the maintenance expenses of the Trust's assets
- the trust can spend up to \$10,000 each financial year on discretionary items not related to the care and accommodation needs of the beneficiary of the trust.

At the time of writing, the abovementioned proposed Budget changes had not been introduced to Parliament.

In summary

Parents and other relatives have an opportunity to establish an SDT – to care and provide accommodation for a severely disabled relative – that offers significant social security concessions for the donor and the disabled relative. Parents with severely disabled children who are not entitled to social security benefits due to the value of their assets may be able to transfer sufficient assets to an SDT to satisfy the means tests and qualify for entitlements.

There are some very beneficial outcomes for both the donors and the intended beneficiary and I believe the time taken to set up the SDT correctly, so that it qualifies for the social security concessions and so there are no adverse income tax and CGT consequences, will create a real value add for your clients and a specialisation for your practice. ▽



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Accountancy plus

How to establish a profitable financial services practice.

BY ELISE MICHELMORE

Most good accountancy practices have the potential to be great financial services practices. That's because they already have a client base to market to, they already have the trust of those clients, and many of those clients already have the need for – and may be already looking for – financial services. So it's a little surprising that a significant number of accountancy practices fail when they attempt to set up a financial services capability in their practice.

Financial services can include financial planning, investments, risk insurance for individuals and business owners, and mortgage and finance broking. Below are some tips to help ensure your financial services practice is successful.

Seven steps to success

1. If you don't have anyone in your practice who is experienced in financial services, you should either hire someone who is or you should outsource your financial services to external professionals who will fee-share with you. Don't run the risk of ruining your firm's reputation by sitting an inexperienced financial adviser in front of your clients. And don't under-estimate how long it takes to learn the ins and outs of financial services from scratch and to then become proficient in their delivery to clients.

Obtaining the basic education level (the RG146 certificate) is just the start of what is, for most

people, a long formal and informal education process. Plus there's the requirement for 30 or so CPD hours a year just to retain the authority to dispense financial advice.

2. Find a licensee that is flexible enough to enable you to provide your clients with financial services in-house and/or by referring your clients to their professionals.

You also need to be confident they have a full service offering for accountants, including technical and investment education, back office support, paraplanning, marketing, compliance, a client education program, and a prudent approach to financial advice. The key is that the licensee has enough people with enough experience to guide you every step of the way in setting up your financial services practice and running it.

3. Restrict your marketing efforts to creating awareness and leads within your existing client base. Until you have exhausted the potential in your filing cabinets, it is a waste of time and money 'fishing' elsewhere. In fact, you would be better off spending your marketing dollars to recruit more accounting clients, and then convert those clients into financial services clients.

Your marketing of financial services to existing clients would typically include promoting the new service via letters or email, client newsletters, your website, distributing client educational material, new signage and perhaps a launch event.

You should also strongly consider asking all clients to complete a financial services questionnaire next time they meet with you so you can determine which clients need your assistance.



Ensure

4. Ensure your staff understand the importance of your financial services offering and how it can help your clients. You also need to teach your staff how and when to introduce your new service to clients, and how to refer clients to your financial adviser.
5. Appoint someone as general manager of your financial services offering to ensure it is given the resources and priority it needs within your practice, is properly promoted to clients, and is seen as a 'value add' by clients.
6. Get easy wins early by initially introducing your new offering to those clients who you know already have a strong need for financial services. The most effective way to do that is to invite these clients in for a consultation, or to raise it with them next time they meet with you or call you.
7. Make sure your fee model, for the services you provide in-house, is appropriate for the provision of financial services and properly compensates your practice not only for the time involved but also for all the ancillary expenses incurred in providing the service – licensee costs, compliance, adviser education (time and costs), marketing, research and so on. A fee model would typically include an upfront fee and an annual fee for financial planning, and would be fee-for-service based on asset value. This model helps align the fee with the interests of the client because if the client's portfolio rises in value, so does your annual fee, and vice-versa.



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