

## TRUSTS UPDATE

*There have been recent legislative changes affecting the distribution of beneficiary income of a trust and more recently, policy announcements as to the repeal of gift duty. In this Special Edition of the Low Down, we take a closer look at those changes and how they will affect you and your trust administration.*

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### Repeal of Gift Duty

On 1 November 2010, the Government announced that gift duty is to be abolished. Legislation repealing the Estate and Gift Duties Act is expected to be introduced to Parliament later this month, with likely effect from 1 October 2011.

Gifting programs are widely used to transfer large assets without attracting gift duty, and are typically used by individuals to transfer ownership of their assets to a family trust. This is most commonly achieved by an individual selling an asset (to a trust, for example) in return for an interest-free loan. That debt is then progressively forgiven within the \$27,000 annual threshold for non-dutiable gifts.

The cost to the private sector of complying with gift duty requirements is estimated to be in excess of \$70 million per year. However, with over 99% of gift statements attracting nil gift duty and raising limited revenue for the Government, the Government is of the view that the cost of retaining gift duty exceeds any public benefit.

There are concerns about the impact that the repeal of gift duty will have on protection for creditors, income tax avoidance and social welfare means and asset testing. However, gifting programs have never prevented the instant transfer of legal title to assets in one transaction, rather, they have the effect of limiting the amount of the loan or debt that can be forgiven each year without attracting gift duty. Accordingly, gift duty only provides very limited creditor and means testing protection.

Although an individual will soon be able to transfer entire assets or large sums of money in one transaction without attracting gift duty, legislative protection already exists to prevent transactions that have the effect or intention of income tax avoidance, defeating or prejudicing creditors and transactions at under-value.

In respect of social assistance targeting such as asset-testing, particularly in relation to eligibility for the Residential Care Subsidy, the power already exists for the Ministry of Social Development to "claw back" assets that an applicant has divested within the five years prior to becoming eligible for the subsidy. This provision will now likely take on greater significance.

Whether or not it would be sensible for you to continue with your gifting program until October 2011 will depend on your individual circumstances. It may also be that to retain the ability to be repaid under a loan to your trust will better suit your individual circumstances than making an outright gift and then receiving future distributions of trust income or capital. We are happy to discuss this with you.

Of further note, a recent court decision has highlighted a possible tax issue for beneficiaries who receive interest free loans from trusts without a specified repayment date. It is therefore important to document beneficiary loans appropriately. We are happy to discuss any queries you may have in relation to income tax issues arising from any existing or potential beneficiary loans.

### Distribution of Beneficiary Income

Many New Zealand trust deeds have a form of "capitalisation" clause which essentially provides that, for income tax purposes, Trustees have a period of six months from the end of the trust's income year within which to distribute beneficiary income before it becomes part of the capital of the trust.

A recent amendment to the Income Tax Act 2007 now effectively extends that six month period for distributions to, at the latest, the date by which the Trust's tax return must be filed, if the Trust Deed provides for that extended period. In some cases, this may be up to 12 months.

Where the trust deed refers to a six month period for distributions, the trustees will be unable to take advantage of this extended period unless the trust deed is varied.

If you wish to take advantage of this extended period for distributions of beneficiary income, please do not hesitate to contact us so that we may discuss whether the variation of your trust deed is necessary.