

Gift Duty Abolition

(Not As Straightforward As It Seems)

Last year the Government announced that it proposed to abolish gift duty from 1 October 2011. The abolition proposal was included in a bill introduced to Parliament in early December last year.

Consequences

The abolition of gift duty will have far-reaching consequences for the many New Zealanders who have established trusts. The law change will provide an opportunity to consider existing structures and assess how gifting can be utilised as part of an overall estate planning exercise. We recommend that careful consideration be given to any decisions relating to gifting, including taking independent advice before existing debt balances are forgiven.

Ramifications

The bill as introduced is very simple but the change will have ramifications in other areas of law, for example relationship property, creditor protection, insolvency and inheritance law. It is anticipated that the Parliamentary select committee will receive a number of submissions on the proposed abolition. Until the legislation is passed, planned for July 2011, no steps should be taken to fast track gifting programmes or make any decisions in anticipation.

What does the law change mean?

The proposed law change will provide new opportunities for asset planning involving trusts and/or family agreements. It will equally provide constraints and potential for conflicts with trusts coming under attack.

Opportunities

The abolition of gift duty will provide opportunities to:

- Review any existing trust debts. Debts should not be forgiven without seeking independent advice as it may be appropriate that the debt remains in place to protect the lender's position, for example as separate property.
- Gift assets directly to a trust without undergoing a lengthy gifting programme. Although this appears to provide a convenient quick fix there may be circumstances, for example retirement planning or relationship property issues whereby it may be beneficial for the lender to retain all or some of the trust debt.
- Review old, inflexible and restrictive trust structures, for example mirror trusts. This can be achieved by transferring trust assets to the beneficiaries and then for the beneficiaries to readvance the assets to a modern flexible trust.

Gifts will still need to be recorded through a deed of gift to avoid the gift to the trust being deemed a loan. There will no longer be a need to file a gift statement with the Inland Revenue Department.

Constraints

A word of caution. The proposed law change must be considered against existing legislation. Even though a gift has been made, it does not mean the assets are safely in the trust. Any decision to gift must be considered in relation to the circumstances of the person making the gift.

There is an ability to call back/cancel gifts under existing legislation. (Property Law Act 2007 (creditors), Insolvency Act 2006 (bankruptcy), Property (Relationships) Act 1976, Social Security (Long Term Residential Care) Regulations 2006). This includes presumptive provisions. For example a gift made within two years of bankruptcy is presumed to be made at a time when a bankrupt is unable to pay their debts and therefore can be cancelled (Insolvency Act). The Ministry of Social Development has the power to treat any gifts that have been made by an applicant for a residential care subsidy, possibly through the entire life of a trust, when making an assessment for a residential care subsidy.

There is likely, in our view, to be greater scrutiny of trusts to assess the timing of gifts. This means there will be an even greater need for vigilance in trust administration and care in structuring trusts and transferring assets to trusts. In particular, it is important to ensure trust assets are kept separate and not intermingled with personal assets and are not subject to recall thereby creating liabilities for trustees.

Law Commission

The abolition of gift duty is likely to be the first step in future changes to the law which will affect trusts.

The Law Commission has released a series of papers relating to the status of trusts. It is proposed that the existing Trustee Act, which was passed in 1956, be reviewed and modernised. One of the outcomes is likely to be stricter compliance requirements for trusts.

In these recessionary times trusts are being scrutinised in greater detail by the Courts, creditors, family members and beneficiaries. These potential challenges can in most instances be repelled with careful trustee decision making together with scrupulous trust administration and record keeping.

Summary

The abolition of gift duty may provide opportunities for arrangements concerning trusts but it may also create new perils for trustees and people who establish trusts.

The opportunities will be to enable divestment of assets to advantage or to exit old restrictive trusts and move to new modern and flexible trusts.

The responsibilities and potential liabilities of trustees are likely to be heightened as a result of the law change.

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