



Guide To...

Estate Equalisation

When planning for the distribution of their estate, a parent may wish to leave the family business to one or more of their children. This may be common in the farming community or where a parent has been grooming one child to take over their place in the family business. But what happens where one child is catered for in this manner and another is not? Times have changed over the past 50 or so years, and it may not be acceptable for one beneficiary to be left all assets at the expense of other potential beneficiaries. State legislation provides potential beneficiaries with the right to claim further provision from an estate, i.e. “contest the Will” if it can be established that they have not been adequately provided for in the Will. This may result in the asset having to be sold to provide some cash for all other potential beneficiaries (often with an accompanying capital gains tax bill!). Despite the best intentions of the parent, their wishes can be changed.

How does the strategy work?

Estate equalisation is specifically concerned with the equitable passing of a family business to the next generation. Estate equalisation is the process where one asset (i.e. the family business) is bequeathed to one child and an asset of equivalent value is bequeathed to the other(s). Often the only method of providing this ‘asset of equivalent value’ is through life insurance. The value of the insurance policy is realised on the death of the parent insured and is the amount of insurance cover. An estate equalisation strategy may complement a “Business Will” (Also known as a Buy/Sell agreement). This may be relevant where family members are in business with one another – for example, if two brothers are in business together, one brother may want to pass their interest to one of their children in the event of their death (and provide another asset to the other child), but the second brother may not have children interested in being part of the business and would want his brother to buy his interest out.

The Benefits

- Designed to facilitate your wishes being carried out through your Will.
- Can help prevent family rows over inheritance.
- Can reduce the chance for your Will to be challenged in court.
- Can protect the value of your estate, since assets do not have to be sold (often with an accompanying capital gains tax bill!).

Case Study

Ted, a widower and third generation farmer, has worked on the family farm his whole life. Ted has groomed his son, Stephen, to take over the farm (valued at \$1.2 million, including a current uncrystallised \$294,000 capital gains tax liability) when he decides to retire. Ted suffers a stroke while drenching the sheep and dies a few days later. In his Will, Ted left the entire farm to Stephen. Realising this would be an unfair result for his two daughters, Carol and Laurel, whom he also wants to provide for on his death, Ted had taken out a life insurance policy so that his daughters would receive a lump sum amount of \$906,000 - each equivalent to the value of the farm left to Stephen less the capital gains tax liability. In this way, Ted has ensured his wishes to maintain the farm within the family are carried out yet managed to treat all his children fairly.

Tips and Traps

- Family Maintenance provisions vary in each State. You should get professional legal advice in relation to the provisions in your State, including whether arrangements made under an estate equalisation strategy will be sufficient under each State's provisions.
- An uncrystallised capital gains tax liability may reside in the business passed onto the child(ren). To ensure all beneficiaries are treated equitably and to account for the future payment of this and any other liabilities, the insurance benefit provided to the other child(ren) may be less than the 'full' value of the asset.
- There are a number of different ways of ensuring the life insurance proceeds are received by the intended beneficiaries. Some of these methods include having the intended beneficiary as the policy owner, nominating them as a beneficiary of the policy, or through the operation of your Will. Each alternative may have different legal and tax outcomes which you should consider before settling on a particular arrangement.
- To maintain fair treatment amongst your children, you should update your insurance cover in line with the (increasing) value of your business. Failing to do this may lead to one or more beneficiaries receiving less than others.
- An estate equalisation strategy addresses one issue in estate planning. Comprehensive and professional estate planning advice should also be obtained, acted upon, and regularly reviewed.

If you have any queries in relation to the content of this material, please do not hesitate to contact Kate Kimmorley the Principal Financial Adviser at Kimmorley Financial Management on (07) 5591 1725.

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