

FAMILY LIMITED PARTNERSHIP

The Family Limited Partnership has developed as the centrepiece of an estate plan. The Limited Partnership owned and controlled by the family and family trusts, gives us the opportunity to accomplish what we did not need to do prior to 19th September 1985, the introduction of Capital Gains Tax Legislation in Australia.

Asset protection, is defined as control and continuity of a united family resource base - and, frequently, substantial reduction of the capital gains tax burden to the family. The Family Limited Partnership is an engine which makes all other estate planning procedures work at optimum capacity.

Our firm was among the first in the nation to use the limited partnership to meet the demand of professionals, business owners and land owners for protection of their family's resource base. The same plan, combined with a family trust and other unit trusts also avoided capital gains tax and produced significant income tax savings.

We follow the trends in the United States of an increasingly litigious society. In the words of Denver attorney, Barry Engel, "a 'someone must pay' attitude seems prevalent in our society today". "Economics drives the legal system. Personal experience proves that much can be achieved by knocking the 'profit' out of the pursuit any seasoned litigator would confirm that it is one thing to WIN a judgement and another thing to correct a judgement"¹.

1 Barry Engel, Asset Protection Planning, A Critical Part of any Estate Plan.
CCH Financial and Estate Planning Reports
#30,001, Jan 1992 at 25,050.

CONTROL AND CONTINUITY

Traditional estate planning prior to 1985 involved the division of the family financial resource base. Gifts, or transfers at death, split family property into parts - and - over time, the family resource base was reduced to nothing. The division of property frequently resulted in a division of the family with contests over ownership and control of property which could be sold. The Family Limited Partnership, Testamentary Trust or Limited Liability Company converts family property into non-controlling units of ownership. What passes to members of the family are units or shares in an entity owned and controlled by the family.

FULLY INTEGRATED PLANNING

We believe that the single biggest mistake that families make is to plan piece meal over a period of years. They seek to “play the game” without having all of the necessary pieces on the playing board. First, all necessary pieces must be formed and placed into service so that the pieces may be moved.

The Family Limited Partnership does not work alone to accomplish all of a family’s estate planning objectives. A management trust or living trust developed as a part of the estate plan is designed to avoid capital gains tax and to minimise the costs of the settlement of an estate. Trusts formed for children and their descendants (The Testamentary Trust) can preclude the loss of a child’s inheritance as a result of a divorce proceeding or financial misfortune. The Testamentary Trust can also pass significant value from generation to generation without capital gains tax. A trust formed by one spouse for the other can protect assets, and own life insurance to insure the continued support and maintenance of the spouse who is the beneficiary of the trust without the inclusion of the assets of the trust in the estate of either spouse.

FAMILY TRUST AND INHERITANCE DAMAGE CONTROL

Our objective in a fully integrated financial, tax and estate plan is that no one in the family own record title to anything in his or her name. Typically, all investment property is owned and managed by a Family Limited Partnership. A management trust (or living trust) owns and manages the limited partnership units, the residential property, and tangible personal property. There is nothing of public record which will indicate what our clients own - nor will there ever be a public record of personal and confidential financial information. Privacy is important to almost everyone we represent. Privacy also promotes asset protection. People who don't own anything don't get sued.

Why make gifts of record title to property to a spouse or to children? Outright ownership of property invites litigation. Outright ownership of property invites a reoccurrence of the capital gains tax with passing of each generation - until nothing remains.

Testamentary trusts, can protect a family member's inheritance and build a protected financial resource available to supplement a child's inheritance.

It is unfortunate that many parents delay significant estate planning out of fear that "too much, too soon" can kill a descendant's incentive to work and to be a productive member of society. It is important for you to know that you can create a control mechanism that will enable, and not disable, a child.

Please read the letter of wishes at Appendix 1. You will then understand what this kind of planning is all about. The Family Limited Partnership is a control mechanism. The family foundation is another control mechanism designed to perpetuate the community and personal responsibility of children and grandchildren, as active foundation participants, and the family's good reputation in the community.

LIFE INSURANCE PLANNING

Are we proponents of life insurance? You bet we are. Life insurance provides a source of liquidity which is often needed by the family, particularly a dependant spouse. Some of the businesses who lost everything in this past decade were able to restart and rebuild by

borrowing against life insurance policies. And, life insurance can be used as a hedge in the large to very large estate to provide the liquidity a family might need to survive a negative change in the tax laws.

Professional life insurance planning utilizes a business life insurance trust. Planning with a Family Limited Partnership provides the family with options.

- The gift of partnership units into a business life insurance trust can feed the trust with funds to pay for the policy
- A Family Limited Partnership can buy a term benefit in a modified reverse split-dollar plan, helping a life insurance trust pay for the policy premiums until a policy is in a paid-up status - without the “roll out” problems associated with traditional split-dollar plans
- A Family Limited Partnership can buy and own life insurance on a partner’s life

CONCLUSION

“There are two systems of taxation in the country
.... one for the informed
.... one for the uninformed”

The same is true for those who consider themselves at the mercy of the Legal system and fickle regulation by our government. Those persons are vulnerable only because they don’t know any better or, knowing the risk, do nothing.

There is probably nothing we cannot accomplish if we are given the opportunity to plan - NOW - and to put all of the needed pieces into play. For those who are informed - and do nothing! The greatest source of revenue for a trust’s and estate’s attorney is the unplanned estate - the Probate - the Discovery and Valuation of property - a contest with the Taxation Office - “Hail Mary” efforts to find the money, and liquidate assets, to pay the Capital Gains Tax - and, maybe, with an emotional will contest thrown in.

Yes, the laws will change. Good positive planning anticipates these changes and provides the needed flexibility so that the plan can likewise change. There

are those who want the protection of their family resources, but are concerned that the Family Limited Partnership might fail due to a change of the law or the outcome of a contested proceeding. Those seeking to reduce the Capital Gains Tax burden to their families are concerned a change of the tax laws or a contest by the Taxation Office as to the business purpose of the organisation, might not reduce the Capital Gains Tax burden to the family. They sometimes elect to do nothing.

AUSTRALIAN LEGAL SYSTEM

AUSTRALIAN GOVERNMENT

These persons are on a railway track. A train labelled “Australian Legal System/Australian Government” is bearing down on them. They are afraid to jump to the left or to the right out of fear that the ‘boogey man’ might get them. Legal advisors, concerned with any procedure they do not fully understand, advise their clients to stay on the track.

Those who have these doubts, and favour doing nothing, could ask themselves these questions:-

“What do you have to lose in forming a Family Limited Partnership or Limited Liability Company and a Testamentary Trust?”

“What do you stand to lose if you do nothing?”

It is always important to focus on what is important in life. None of us set out in life to build a financial empire for our children. We can pass to our children a legacy built upon a work ethic, responsibility, and a good family reputation - through thoughtful planning.

Estate planning is more than a game. It deals with the very real issues of death, disability, and the care of the family.

Appendix 1 Distributions from Trust - Letter of Wishes

APPENDIX 1

DISTRIBUTIONS FROM TRUST LETTER OF WISHES

This is a typical letter which many of our clients use to guide a trustee or committee of trustees in making distributions from a long-term trust. The letter of wishes is designed to preclude the “too much, too soon” damage which can ruin a descendant’s incentive to work and be a productive member of society.

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LETTER OF WISHES

FROM: MILES DAVIS AND REBECCA DAVIS

TO: TRUSTEE

This instrument is delivered to you to express our wishes as to distributions of trust income and principal from the trust. This long-term trust has been established for our children, Julie, Samuel, Sandra and Jason and for their descendants. We realise that we cannot require that you make distributions according to our wishes. This instrument may be helpful, however, to indicate our objectives and to serve as written evidence thereof in the event any member of my family should allege that you are acting unfairly.

Attached are documents pertaining to the distribution of our estate as the result of our deaths. This documentation will identify the members of our family, and the objects of our bounty. We ask that you be guided by this documentation in making distributions of income and principal from the trust after our deaths. We intend from time to time to amend, supplement, and update this instrument. If we fail to do so, you may rely on any documentation or other information provided by our family which may evidence our intent.

We are truly concerned about the harm which distributions of trust income and principal may have on members of our family. History is replete with the ruin caused by money received by children and great-grandchildren and the resulting waste of human potential untested by the need to work and to be productive. Too much, too soon, can destroy rather than nourish. We re-emphasise emphatically the non-binding guidelines given to you in the trust instrument as to the use and distribution of trust income and principal. Distributions to any family beneficiary are to be limited, even to the suspension thereof, to the extent distributions have, or may likely have, a tendency to retard a family member’s incentive to work or to be a productive member of society. It is important to us that each member of our family, including each and every descendant, develop and have a strong work ethic; that each family member be a productive member of society; and that each family member provide for those who are dependant upon that person for their care and support.

If a family member fails to provide for the support of a spouse and children, you are permitted to provide that support, by-passing the family member entirely.

You may use a matching funds concept, providing, for example, distributions from the trust in an amount or percentage which approximates the earned income (or percentage of earned income) of the family member for any calendar year. You may provide one or more members of our family with a capital resource which promotes enjoyment rather than financial support. For example, you may acquire a home or holiday residence for a family member and in a manner which protects the resources from loss as the result of divorce or financial hardship. We do not object to any use of the trust fund which will improve a child's lifestyle without increasing that person's dependency on the trust for financial support.

A family member may devote his or her life to teaching or social service. We hope to encourage and enable any member of my family to make this choice. You may make distributions from the trust to supplement the income of any family member to enable that person to continue his or her unselfish path in life, and to preclude an abandonment of his or her path for lack of sufficient financial resources to continue.

You may reward accomplishment and distinction which comes of persistence and hard work.

You may carefully investigate and evaluate any business opportunity available to a member of our family. We wish to promote enterprise, but not foolishly. If you consider that the family member has sufficient training, experience and temperament to make a success of a business opportunity, you are encouraged to use the trust fund as a financial resource for this purpose. You may provide financial assistance (1) through loans to the family member, or (2) by investing or co-investing in the business opportunity, or (3) through a guarantee of payment to enable a family member to secure a loan. You may also provide financial assistance in the form of an outright distribution of trust principal if you consider that the importance of financial assistance to the family member outweighs the tax planning objectives of this trust.

We discourage any "joint venture" or "joint enterprise" which would put the trust fund as a whole at risk and expose the trust as a whole to joint and several liability for the debts and tort liabilities of the business enterprise.

The trust fund may also serve as a retirement plan for members of our family. The future of our economy is at best unknown and uncertain. We do not know that members of our family will have the opportunity to set aside funds for their retirement, and you may use this trust to enable a family member to retire at a reasonable retirement age.

This trust fund may also serve as a disability plan. It is our desire that any family beneficiary who may become disabled, and unable to lead a productive life, receive sufficient financial support and maximum physical, mental, and vocational rehabilitation. We ask you take care in making distributions to or for a disabled family member. Distributions may cause the loss of governmental or social benefits to which the family member may otherwise have been entitled. I am not so much concerned with the reduction of the trust fund to provide for financial support otherwise provided by a governmental or social welfare organisation. We are concerned with the loss of opportunity which a disabled family member may have for programs provided only by governmental and social welfare agencies. Act with care and upon the advice of informed counsel.

The trust instrument provides that you may make distributions to a charitable organisation or Trust. This provision is made with the understanding that charitable planning can be an important option in Estate and Tax planning. You may make distributions to one or more charities at the request of any family member. However, we ask that you investigate the charity before you make a distribution. We do not wish to support a religious “cult” or order which lacks sufficient recognition or reputation in the community, especially any organisation which has a reputation in the community for the exploitation of its members.

We have provided in the Trust instrument that you may separate the Trust Fund into separate Trusts. This may be an important consideration since the Trust is long-term in nature and well likely to continue through many generations of our family. The division may be made according to family line. For example, the trust may become cumbersome to administer if five great-grandchildren and their descendants are then the family beneficiaries. In this case, it may be prudent to divide the Trust Fund into five separate Trusts, each Trust dedicated to a particular line of the family. In so doing, we ask that you consider any increased cost of administering separate Trusts relative to the value of the Trust Fund as a whole. We ask that you employ the services of a qualified Tax Advisor to insure that a division will not adversely affect the Tax Status of the Trust and its beneficiaries.

Because it is improbable that you will know every member of our family in generations to come, you are authorised to empanel a board of Family advisors. You should encourage annual or more frequent meetings of the advisors and encourage their active participation with distributions from the Trust, as an expense of administration, for their travel related expenses and as reasonable compensation for their time. You may be guided in the exercise of your discretionary authority by the recommendations of the family advisors.

It is unfortunately common for the Trust Beneficiaries to force distributions from the Trust with the threat of litigation against the Trust. You may be threatened with claims of personal liability for fiduciary malpractice. We sincerely ask that you not yield to the use of the legal system to exort payments from the Trust. Agressively defend any claim which you consider to be unjust. You may use the Trust Fund to do so. You may completely suspend any future distributions to a family member who makes unjust demands. If you are of the opinion that your personal exposure to loss is too much, we ask that you appoint, or seek the appointment of, another Trustee who will undertake the Risk.

There is nothing more important to us than our family. We wish to nourish, not harm, our family for generations to come with the family financial resource which is produced as the result of this Trust. We ask that you tend to administration and preservation of the Trust with care and with good judgement.

2 October, 1995
Miles DAVIS
Rebecca DAVIS