

# How can I protect a beneficiary with special needs?

Estate Planning Client Guide

If you are concerned that a beneficiary of your estate may find it difficult to handle an inheritance, a protected trust could offer them more security.

Assets inherited directly by your beneficiaries as a lump sum become part of their personal assets and under their control. As a result, the wise use of these assets is dependent upon the beneficiary's ability to manage their own financial affairs.

## What is a protected trust?

Some beneficiaries may not be able to handle a direct inheritance for a variety of reasons, such as:

- physical incapacity
- advanced age
- drug addiction
- mental incapacity
- minor status
- gambling addiction

Leaving an inheritance directly to a beneficiary with special needs such as these may lead to the loss or misuse of their inheritance. One way to provide protection for a beneficiary whose inheritance may be vulnerable is the creation of a protected trust, which is a type of testamentary trust.

The emphasis of a protected trust is upon the specific needs of a particular beneficiary. The structure of the trust is designed to protect the beneficiary.

## What is a testamentary trust?

In general, a trust describes an ownership structure where the assets of the trust are owned by one person or organisation (the trustee) but held for the benefit of other individuals or organisations (the beneficiaries).

A testamentary trust is a trust that is created within and by your Will but does not take effect until your death.

A testamentary trust differs from a family trust, as a family trust is created by deed and commences during your lifetime.

A testamentary trust may be created using specified assets, a designated portion of your estate or the entire remaining balance of your estate. Multiple trusts may be created by the one Will.

## How does a protected trust operate?

In a typical protected trust:

- A proportion of the estate is held on trust during the life of the beneficiary with special needs, or until they reach a specified age.
- The trustee has the power to use the income and capital of the trust for the ongoing benefit of the beneficiary for a variety of approved purposes specified in the Will.
- During the financial year, sufficient income and capital is distributed to the beneficiary to meet the cost of the approved purposes. Any remaining income is either accumulated within the trust or distributed to other beneficiaries as directed by the Will.
- Upon the death of the beneficiary with special needs, the capital remaining in the protected trust is transferred to other nominated beneficiaries.
- If so desired by the Will maker, the beneficiary may become entitled to the capital of the trust on reaching a specified age or meeting another condition specified in the Will, at which time control of the trust is transferred to the beneficiary.

It is common for a Will maker to provide a lesser share for a beneficiary with special needs, with the expectation that Government benefits will look after their needs. This approach may increase the potential of that beneficiary bringing a claim against the estate for greater provision.

A protected trust will normally be a mandatory trust imposed upon the beneficiary due to their vulnerable state. It is therefore important that a protected trust is sufficiently funded to cover the administrative cost of operating the trust.



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## Case study

Andrew and Marcia have a combined estate of net worth \$1,250,000. Their two teenage children are their beneficiaries.

Andrew and Marcia are concerned that, in the event of their deaths, their children are not sufficiently mature to use their inheritance responsibly. They wish to use a protected trust to ensure that:

- the children are adequately provided for and supported during their developing years, but
- the value of the inheritance is preserved until the beneficiaries are able to manage their financial affairs.

As a result, Andrew and Marcia's Wills provide that any inheritance received by a child shall be held in a protected trust with the following conditions:

- Until each beneficiary reaches 21 years of age, their access to the income and capital of the trust is limited to specified approved purposes including:
  - education expenses
  - hospital and medical expenses
  - rent or accommodation charges
  - electricity, gas and other utility payments
  - maintenance and income support at the discretion of the trustee.

- At the age of 21, the beneficiary is able to request that the income of the trust be applied to them for any purpose, but the capital of the trust remains preserved.
- At the age of 25, the beneficiary is given full control of the trust, with the ability to either continue the trust for tax planning purposes or terminate it.

A protected trust operating in this manner ensures that each child is adequately supported and provides them with gradual access to the financial benefits of the inheritance. By the age of 25 years, the beneficiaries will have become accustomed to applying the inheritance responsibly and are less likely to misuse the trust on gaining control.

## Would you like further information?

For further information please contact your AET Estate Planner on 1800 882 218.

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