



Series 4

An alternative to trusts and company structures

« An alternative investment structure

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Generation Life Investment Bonds, which combine tax efficiency and flexibility, offer a powerful long-term wealth accumulation alternative to traditional and complex investment structures such as trusts and companies.”





An alternative to trusts and company structures

The superannuation system is generally considered the most tax-effective way of providing for long-term savings, given the generous tax concessions available. More recently, there has been an increased focus by Government on limiting superannuation concessions and the use of superannuation as a tax-friendly wealth accumulation and estate planning vehicle - refocusing superannuation to provide an adequate level of income and savings in retirement.

With this in mind, investors may seek to supplement (or an alternative to) superannuation to achieve a more desired or customised level of income savings in retirement and generate additional wealth for estate planning and intergenerational wealth transfers. When considering how to implement strategies to reach your financial goals, it's important to choose the structure that will provide you with the desired outcome both in the short and long terms.

Superannuation is a well-known tax-effective structure for investing and providing for the future. Structures to also consider include trusts, companies, and investment bonds. These structures are not subject to superannuation contribution cap limits or additional superannuation related taxes.

“A smarter way to grow, protect, and transfer your wealth tax-effectively. Generation Life Investment Bonds make it simple.”



Navigating investment structures

1.

Using a trust structure

A trust structure is a legal arrangement where one party (the trustee) holds and manages assets for the benefit of a specified party (the beneficiary). Trusts are often used in estate planning, asset protection, and tax strategies.

Common types of trusts include fixed trusts (such as unit trusts), family or discretionary trusts, testamentary trusts, special needs trusts, and charitable trusts. Each serve different purposes and offer various benefits in terms of control, privacy, who can be a beneficiary, how income and assets can be distributed, asset protection, and tax implications.

While there are many types of trusts that can serve multiple purposes, generally, a trust will seek to distribute income and realised capital gains annually to its beneficiaries in line with a tax year. Trust beneficiaries are then taxed on those earnings based on their own tax rates, such as their marginal tax rate if the beneficiary is an individual.

Trust structures may therefore not be tax-effective where a beneficiary's income levels place them in higher marginal tax brackets. The use of child beneficiaries (such as grandchildren) may also not be effective, given the high marginal tax rates up to a maximum 66% on distributions above the phased tax free threshold for minors.

Introducing additional investment structures can also add complexity, costs, and compliance risks, which must be managed on an ongoing basis. Upfront establishment costs, appointing the right trustees to manage the trust, and ongoing costs should all be considered.

For example, where a testamentary trust is established under a will for estate planning, the practicalities of managing the trust on an ongoing basis may prove expensive or burdensome for appointed trustees. Additional tax complexities and costs can arise in situations where testamentary trusts also hold non-estate assets.

2.

Using a company structure

A private company can be used to hold investments, with all earnings (both income and realised capital gains) taxed at 30%, unless the company qualifies for a lower 'base rate entity' company tax rate. In some cases, a company may be set up as a beneficiary of a trust and is often referred to as a corporate beneficiary or bucket company. The term 'bucket' is used because the company sits below a trust (as a beneficiary) and is used to pour money into it, which may help reduce tax (at least temporarily).

When a company distributes its earnings (as dividends), the shareholders will pay tax on those earnings (which are 'grossed up' to include the value of imputation credits) based on their marginal tax rate. Rules apply to ensure that profits, distributed or transferred out to an individual, are included as assessable income at the individual's level.

Company structures can assist with deferring the payment of tax on earnings until those earnings are distributed. However, ultimately, profits distributed will be taxed in the hands of shareholders. Company structures can also be costly to maintain and will require financial accounts and annual tax returns to be completed.

Additional complexities and management can be involved under a private company structure, including managing the requirements under Division 7A, which is an anti-avoidance provision that treats all non-compliant payments and benefits paid to shareholders as unfranked dividends.



3.

Investment bonds as an alternative

Investment bonds can be described as a combination of a managed fund and a life insurance policy. Key features of an investment bond include:

- Ongoing invested earnings are taxed at an effective tax rate of up to 30% in the hands of the issuer. Generation Life Investment Bonds generally range between 10%–15%¹ through our unique tax-aware management process.
- No additional investor tax to pay if you hold it for at least 10 years.²
- No investor tax payable on earnings if the investment bond is withdrawn at any time (either within or after 10 years) due to certain defined events, including the death of the life insured nominated under the investment bond.
- The freedom to withdraw funds when needed, which can be used for any purpose.
- Flexible succession and estate planning features to control the transfer of ownership or future benefit payments without creating a taxable event.
- Investments can be made by individuals, joint owners, trusts, or companies.

Tax simplicity

Unlike a typical trust or managed fund, investment bonds are not a flow-through tax structure, which means their ongoing earnings are treated and retained within the investment bond. Earnings from an investment bond aren't included in an investor's annual tax return, as the investment bond pays tax on the earnings within the structure, simplifying the investor's tax affairs.

The difference between the tax paid by the investment bond at an effective rate of up to 30% and what an investor (including a trust beneficiary or company shareholder) would have paid at their (usually higher) marginal tax rate is retained and reinvested. The compounding benefit of this over time can be substantial.

An investment bond investor is also not required to provide their Australian Tax File Number.

Tax-effective

Investment bonds can also provide added tax benefits when compared to having a company hold investments. Investment bonds have special tax rules not available to companies, that provide opportunities to deliver better after-tax return outcomes.

The tax on investment bond earnings payable is effectively capped at the investment bond tax rate, which is an effective rate of up to 30% - with no income to be reported by investors, and no investor tax to pay. Additionally, Generation Life investment bonds operate on 'revenue' account, meaning that any realised (otherwise capital) losses can be immediately used to reduce the investment bond's level of tax assessable earnings and do not need to be carried forward until future capital gains are realised to offset against.

Generally, companies (as well as trusts and personal investors) do not hold their investments on 'revenue account', and therefore cannot benefit from 'bringing forward' immediately the future tax benefit of realised capital losses that are not able to be offset against realised capital gains. This helps an investment bond reduce the tax payable by it, with the tax savings immediately reinvested to take advantage of compounding returns.

Investment bonds will also generally have a significantly larger universe of investments it can invest in compared to a privately held company, providing greater opportunities to tax-effectively manage their underlying investments.

Passing on wealth

Investment bonds can also be a cost-effective, tax-effective and convenient way to pass on your wealth to your dependants and others, with minimal fuss. Investment bonds have features that can be used in conjunction with, or as an alternative to, conventional estate planning tools – such as a will, a testamentary trust (for future gifting and for making intergenerational wealth transfers), and superannuation. Importantly, investment bonds can be structured to pass outside of your estate, helping reduce the potential for family conflict that would otherwise arise from potential challenges by aggrieved parties, while also reducing the cost and time involved in managing probate requirements.

Investment bonds provide the ability to transfer benefits on your passing to your nominated beneficiaries tax-free. Investment bonds also provide options to pass on ownership in the future or on your passing, with the added flexibility to restrict or control the recipients level of access to funds in the future. Should a recipient require access to funds, investment bonds can also provide the flexibility to have a third party approve withdrawal requests made by the recipient.

An investment bond's ownership can also be transferred without capital gains tax consequences, providing the potential for seamless inter-generational wealth transfer.

Creditor protected

Similar to trusts, investment bonds can also provide protection from creditors in the event of bankruptcy. This protection applies to the investment bond itself, as well as any proceeds from the investment bond received on or after the date of bankruptcy.





What if I already have a trust structure in place?

If you currently operate your investments within a trust structure environment, you may still be able to further enhance the after-tax returns distributed to trust beneficiaries.

Investment bonds can, in addition to being owned by an individual or joint investors, also be owned by any type of trust arrangement and enjoy the benefits, wide range of investment choice, and ownership flexibility that investment bonds provide.

Deciding on distributable income

A trust can reduce its distributable income if invested in an investment bond. Unlike other investments such as shares, managed funds, and term deposits, investment bonds do not distribute 'taxable income' to investors unless a withdrawal is made within the first 10 years or if an event, such as the death of the life insured, results in a death benefit payment.

Whilst the trust remains invested in the investment bond, there is no annual income (from the investment bond) for the trust to distribute. This can be beneficial, particularly where trust beneficiaries are subject to higher marginal tax rates, or where the beneficiaries may be minors and subject to minor tax rates. Because investment bonds do not distribute earnings, they are a simple and cost-effective way to manage distributions from a trust structure.

If a withdrawal from the investment bond is made by a trust within the first 10 years, the proceeds of the withdrawal can be allocated by the trust to its beneficiaries, with any tax assessable component allocated by the trustee to its beneficiaries. The trust's beneficiaries would also be entitled to receive the benefit of up to 30% tax offset to reduce any personal tax payable on the earnings component of the withdrawal.

Withdrawals made after 10 years,² or any withdrawals due to the death of the life insured, can be allocated to beneficiaries by the trust with no assessable income required to be declared by the beneficiaries.

If the trust receives a non-tax assessable death benefit payment from the investment bond, due to the death of the nominated life insured, the trustee can either retain the funds within the trust, or the trustee can distribute the tax-free proceeds to the trust's beneficiaries. No tax would be payable by either the trust or its beneficiaries on the receipt of proceeds from the bond in the event of death.

Case study

Boosting trust investment efficiency

Meet Sarah...

Sarah is in her early 40s, the sole beneficiary of her family trust, and is currently on the highest marginal tax rate of 47% (including the Medicare levy).

Sarah's current situation...

Sarah's family trust is invested in a cash fund earning an annual return of 5% p.a. (before tax). She doesn't require annual income distributions.

Sarah would rather her trust invest in an investment bond over 10 years and not invest directly in the cash fund.



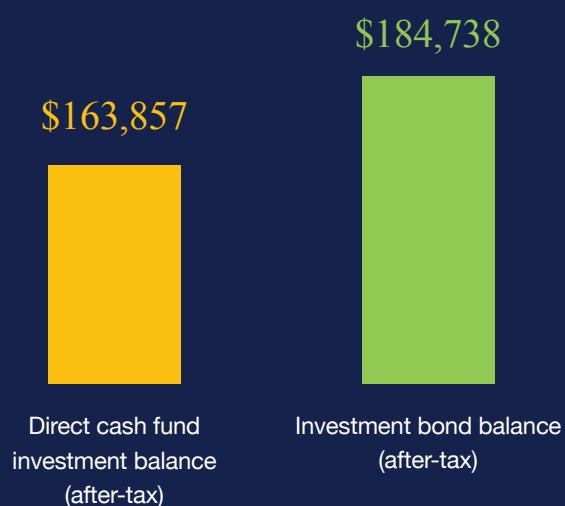


Sarah's solution...

By the trust investing \$100,000 in an investment bond, Sarah's family trust can manage the timing and amounts of distributions each financial year. As Sarah is the sole beneficiary, her declared annual taxable income from the trust would be nil if no withdrawals were made.

If Sarah were on a lower marginal tax rate, there would also be the potential to manage tax bracket creep. If Sarah's trust continues to hold the investment bond beyond 10 years, she would not pay tax on proceeds from the investment bond via the trust.²

After 10 years:



This represents an additional return of nearly 21% on the original invested amount after 10 years' time. Furthermore, Sarah eliminates the continued taxable income reporting required with managed funds, enabling greater tax efficiency.



Capital gains tax events

There are also no trust level or personal capital gains tax (CGT) consequences when modifying the trust's investments in an investment bond. There are no realised gains generated that require distribution to trust beneficiaries.

Simplicity

Replacing a trust's investment exposure with an investment bond can help simplify investment administration. Accessing a large and diversified range of investment strategies through a Generation Life Investment Bond can reduce the administrative effort required of a trustee, including tax monitoring and reporting.

Wealth transfer

Wealth or asset transfers by a trust to beneficiaries may occur for a number of reasons, including the trust ceasing to serve a purpose (i.e. a trust wind-up), a pre-defined event under the trust's rules, or at the direction of the trustee. Where a trust transfers ownership of its assets, often referred to as an 'in-specie' transfer, a CGT event will occur as the transfer is a disposal. You may make a capital gain or loss from the CGT event according to the usual CGT provisions that apply to that asset.

Unlike most other assets, the transfer of an investment bond owned by a trust to a trust's beneficiary will generally not trigger a CGT event, as special CGT exemption rules apply to the transfer of ownership of investment bonds.

Owning an investment bond under a trust arrangement can also provide wealth transfer and estate planning benefits. Trusts that own an investment bond have the flexibility to transfer the investment bond's ownership at any point in time or at a nominated future date using the Future Event Transfer feature of a Generation Life LifeBuilder bond. Investment bonds can provide the flexibility and portability required to tax-effectively manage the transfer of wealth through trusts.

For example, setting up an investment bond within a testamentary trust can also help in transitioning the trust's assets tax-effectively to beneficiaries and can provide asset protection benefits.

Obtain financial advice

Each structure will have its merits, but importantly, whatever structure is chosen, it should help deliver the financial outcomes you require. It's important that you discuss your wealth creation and estate planning needs with your financial adviser, who can assist you in ensuring your investments meet your needs.



About Generation Life

At Generation Life, we know that finding the right investment partner is important for your future success.

We've been helping Australians since 2004 across all life stages and across multiple generations. Today, we are a pioneer in providing market leading investment bond and investment-linked lifetime annuity solutions to help secure the financial future of many Australians and their families.

As part of an ASX listed company, we're passionate about innovating and providing the best outcomes for our investors. We believe in putting our investors at the heart of everything we do.



Outthinking today.

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1. Estimated average tax rates being the estimated average annual tax as a percentage of earnings for each 12-month period over a period of 15 years. Actual tax amounts payable are not guaranteed and may vary from year to year based on, amongst other things, the earnings of an investment option.
2. Subject to not breaching the 125% rule which requires that contributions in a year do not exceed 125% of the previous year's contributions. Where the year is based on the bond's anniversary date.

Disclaimer

The contents of this document reflect our general understanding of current tax and other Australian laws and guidelines which can vary from time to time. They do not represent financial, legal or tax advice to investors which should be independently obtained, to help make investment decisions that are relevant to the circumstances of each investor.

The illustration for Sarah on page 9 does not take into account any fees or charges.

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