

**‘Keeping it in the family’: family trusts, family relationships and tax  
minimisation**

by

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A trust is a relationship, based in confidence, whereby property is held by one party, known as the trustee, on behalf of other parties, known as the beneficiaries. A practitioner literature celebrates the trust's 'versatility', facilitating 'a whole range of "tricks" with particular aspects of property ownership: nominal title, benefit and control' (Moffatt et al. 2005: 4). It is a distinctively English institution, originating in twelfth-century English law (Marcus 1992: 26) and found across British settler societies, including Australia and the US.

Trusts serve two purposes in particular. First, trusts are extensively used for familial purposes. For example, a 2004 British government survey found that the 'main motivation for setting up a trust related to having the ability to control assets', such as 'passing them on to children or grandchildren; providing for a beneficiary in a particular way; withholding assets until children reach a certain age; and ensuring money stays within the "bloodline"' (Bard and Brockington 2006: 12). Second, they are used to protect assets from creditors, not least the tax office. A 2003 Australian study of 'red flags of risk' in relation to tax evasion among the very wealthy, for example, found that 'trust distributions' were the best 'red flag' of all – followed by 'capital loss creation', and 'use of an offshore entity in a country that may be a tax haven' (Braithwaite et al. 2003: 225).

A growing body of research directs attention to ways in which social and economic processes are mixed together (Smelser and Swedberg 2005). Family trusts exemplify this point. This paper explores the socio-economic dynamics of family trusts, in particular the articulation between familial and tax-related purposes.

### **A 'thing in itself'**

There is an immense social science literature directed towards dramatic changes in family structure and meaning since the 1970s. The changes are overwhelmingly understood in terms of 'the pursuit of personal autonomy' and 'individualisation' on the one hand (McDonald 1988; Beck and Beck-Gernsheim 1995) and the 'deinstitutionalisation of the family' on the other (Cherlin 2005). In this

context, it is not surprising that social scientists have largely ignored family trusts. After all, they affect a small part of the population, compared with the great family changes sweeping through all sections of society.

The US anthropologist George Marcus is an outstanding exception to this indifference. His magisterial study of dynastic families in late twentieth-century America highlights the importance of legal arrangements – especially family trusts – ‘in structuring social relations’ within dynastic families. The trust as it evolved in Massachusetts is especially favoured as an instrument of private capital, on account of being able to ‘simultaneously serve the family as an investment trust, a voting trust for blocks of shares in corporations, a coordinating directorate for the close management of several businesses, and a holding company for a pattern of controlling interests in a number of corporations’ (Marcus, 1992: 28). The trust is understood as ‘merely a legal device’ by the second generation, allowing it to operate in much the same style as it did for the first-generation entrepreneurial founder. The third generation feels itself more affected by the framework of the trust; the fourth generation experiences it ‘as a monolithic legacy which controls extended family relationships more than it is controlled by them’ (Marcus, 1992: 25). By this stage it has the quality of a ‘Durkheimian collective representation’ for descendents and beneficiaries, independent of their collective wills (Marcus 1992: 17).

In close connection, a growing body of legal and financial experts – Marcus describes them as ‘insiders-outsiders’ -maintains the formal organisation of capital across the generations and branches of the dynastic family. Their increasing role informs the ‘monolithic “thing in itself” quality of collective capital experienced by family members’ (Marcus, 1992: 25). As a result, the distribution of technical knowledge among family members increasingly defines their relationship to collective capital and each other. Some family members work closely with the experts and have an intricate knowledge of the legal machinery; others do not. Beneficiaries who want to challenge existing arrangements must know at least as much as the experts, or employ their own. Inertia and a

comfortable existence discourage them from doing so. The complexity of the formal organisation itself becomes a bulwark against fragmentation.

Marcus argues that the influence of legal arrangements in structuring social relations extends beyond dynastic families. In giving presentations about his research, Marcus was 'truly amazed' by the number of listeners who approached him with stories about the 'problems that trusts, wills, and symbolic legacies had caused in their family histories'. Their stories were evoked by the 'elicit screen of a mythic dynasty saga' provided by his talks. The markers of class characteristic of dynastic families – 'exclusive social circles, distinctive patterns of consumption, being taken care of by the managers of collective wealth itself' -did not prevent this identification among his audience, 'who were of modest or even middle-class backgrounds' (1992: 6).

Briefly, Marcus's study highlighted the socio-economic dynamics of family trusts, above and beyond their tax purposes; their pervasive influence as a class institution among wealthy elites; and their wider influence among the propertied middle class.

### **This study**

Since Marcus's study, an advice literature concerning family trusts has emerged, directed to a popular market. The literature is uneven across countries, but the unevenness is itself revealing. It provides a useful point of departure for exploring the socio-economic dynamics of family trusts in the 2000s.

In the US advice on trusts is embedded in an advice literature on the intergenerational transfer of wealth. This reflects the fact that the main tax advantages of trusts in the US pertain to estate taxes – and not income taxes, on account of punitive taxes on trust income. Only 2% of families in the US are liable to estate taxes (IRS 2008), which makes the market for advice small but rich. There are scores of titles within the genre. This paper draws upon three titles directed towards different niche within the market. Hughes' *Family Wealth: Keeping it in the family* (from which the

title of this paper is drawn) is pitched at the top end of the market: this is highlighted in a chapter – albeit not for the ‘vast majority of readers’ -about private trust companies, which are ‘prohibitively expensive for families with less than \$60 million’ (2004: 147). Neeleman, Garrity and Baris’s *Estate Planning for the Healthy Wealthy Family* (2003) is pitched more broadly; it does not include a guide to private trust companies. Silver Lake’s *Family Money* explicitly pitches itself to ‘middle class people’, noting that they ‘can and sometimes do leave enough money to children and grandchildren to make their lives better’ (2002: 1).

The advice literature outside the US is tiny. There do not seem to be any advice books pitched to the UK market – or, if there are, they are well hidden. In Australia there are two books by the one author: Renton’s *Family Trusts: A plain English guide for Australian families of average means* (2007) and *Learn More about Family Trusts* (2006). Australia is one of the few countries in the world without estate taxes, so these books are not framed in terms of intergenerational transfer. The main tax advantages of trusts in Australia pertain to income tax, where income arises through business and investment, but not wages or salaries. In turn, Renton’s books are framed in terms of financial advice for ‘average’ families, especially ‘share and property investors and the owners of small businesses’ (2006: xvii). This is a growing market. The number of trusts lodging tax returns in Australia increased from about 120,000 in 1988-89, to more than 500,000 in 2003-04, an average growth of almost 20% per annum (Renton, 2007: 330).

The books are overwhelmingly written by legal and financial experts – Marcus’s ‘insidersoutsiders’. The experts are mostly men. Of the books considered here, there is one partial exception. The first-named author of *Estate Planning for the Healthy, Wealthy Family* is a lawyer; the others, one of them a woman, are psychologists. In all instances, the books are pitched primarily to middle-and mature-aged men. The covers, for example, are ‘cool’ in their images and colours, striking a solid and restrained tone; and stories designed to elicit reader identification involve male protagonists.

Advice books do not provide a window into popular practice around trusts. Rather, they provide normative guidelines for what people ought to do. They are a 'cultural tool kit'. To this end they are full of stories -parables of a kind -designed to illustrate best and worst practice. For example, Neeleman et al. warn that 'if you use a trust as the vehicle for making transfers to your spouse or children, you must clearly and unambiguously state the purposes of the the trust and the standards and guidelines that are to govern the trustee in furthering those purposes':

As an extreme case, consider one notorious trust agreement that directed the trustee to distribute \$250,000 to the settlor's child "upon marrying." This child took advantage of the precise wording and married multiple times to collect his "bounty" each time. (2003: 104)

Specifically, advice books provide a vehicle to explore cultural assumptions around the use of trusts, including the articulation between their economic and familial uses.

### **Tax advantages**

Advice books acknowledge at the outset the tax advantages of family trusts. Their articulation with the broader financial advice literature in different jurisdictions underlines the centrality of tax considerations in setting up trusts. The books differ in the amount of tax advice they provide; the more up-market the book, the less advice. Hughes' *Family Wealth* barely deigns to discuss the subject. The author states: 'I assume that the long-term tax benefits of trusts are known to most readers and that these advantages will be explained fully by their attorneys, accountants and other financial planners' (2004: 100).

In the US the primary tax advantage of trusts lies in sheltering assets from estate taxes. Estate taxes currently kick in when an estate is worth US\$2 million, whereupon it is taxed at a flat rate of 45%; a few years ago the ceiling was US\$1million. Accordingly, trusts present advantages for more affluent families only (IRS 2008). Specifically, they provide a means of reducing the value of an estate, without surrendering control of the assets. The complexity of trust law, operating at both

state and federal levels, gives rise to a smorgasboard of trust structures, varying across states and designed for different ends. For example, a *shelter trust* minimises the exposure of a surviving spouse to estate tax; an *irrevocable life insurance trust* circumvents estate tax liability on the proceeds of life insurance; and a *qualified personal residence trust* minimises the estate tax liability on transferring a residence to children (Neeleman et al. 2003: 108-19).

In Australia the primary tax advantage of trusts lies in income splitting among beneficiaries for the purposes of income tax. It applies only to income from business and investment, not salaries and wages. The advantage is greatest for the wealthiest families, but extends to small business owners, farmers, sole traders, sub-contractors, consultants and self-funding retirees. In this context, trusts provide a means of redistributing income among family members from one year to the next in order to minimise tax liability. There is no advantage when all beneficiaries are already in the top tax bracket; the advantage is greatest when one or more beneficiaries earn little or nothing. As Renton discreetly puts it, families where ‘only one partner is the breadwinner’ have most to gain (2007: 156); so do those with with dependent children aged 18 and over (Renton 2007: 331-3). There is also advantage in managing changing circumstances from one year to the next – notably, in relation to workforce participation, income fluctuation and capital gains.

### **Family considerations**

Advice books are emphatic about the importance of family considerations in family trusts. The more upmarket the book, the more this is the case. Silver Lake’s *Family Money*, for example, asks at the outset, ‘Who is family? And what does that mean?’ (2002: 1). It proceeds to demand that readers ask themselves some ‘basic questions’ about their family values before they decide upon the legal vehicles to use in managing their estate. Hughes’ *Family Wealth* is even more concerned with philosophy, principles and practices. It barely considers the legal vehicles at all. Above all, trusts ‘protect assets’ from the ‘possibly imprudent spending habits [of beneficiaries], inappropriate influence from others, and the claims of their creditors’ (Neeleman et

al. 2003: 101). For example, Hughes tells the story of a wealthy client in his late 60s who had decided to split his estate between his wife and children. What I learned was that his wife, a woman in her sixties, had no formal or informal business education. He paid all the bills and made all the financial decisions. She had siblings who had poor financial histories and were constantly seeking financial assistance from her. His eldest son, just forty, had been divorced once, was in a second “so-so” marriage, and had children from each marriage. His daughter, in her late thirties, was single, a physician, and had already been named in two malpractice claims. Neither claim had resulted in a judgement against her, but the experience had left her frightened. After hearing these facts, I asked him frankly whether he expected the fortune he had worked hard to create and wanted to leave to the people he loved would be preserved or dissipated by his plan. (2004: 98)

To the extent that trusts protect assets, they provide support for family members. In this sense, they amount to a ‘family welfare system’. This is unambiguous in circumstances where beneficiaries cannot attend their own interests, notably minors and adults with serious disability or addictions (Renton 2007: 21, 208; Neeleman et al. 2003: 150-2). Yet most circumstances are more ambiguous. In the case of Hughes’ client, for example, a trust promises protection against his wife’s predatory siblings, his son’s disgruntled exes, and his daughter’s litigious clients, thereby guaranteeing them a constant stream of income for the rest of their lives. By the same token, it removes their capacity for making mistakes, and learning from their mistakes. In this context, Hughes observes that ‘all too often in the beneficiary’s eye, the control and ownership have both resided with the trustee’ (2004: 112). More generally, trusts carry the same risk that right-wing critics have observed of welfare systems generally, creating a kept class of welfare dependents – or, in Silver Lake’s words, ‘generations of dissolute heirs surrounded by scheming advisors’ and ‘trust fund brats’ (2002: 251). The more upmarket advice books devote substantial attention as to how to manage this risk. Their advice is overwhelmingly sociological in orientation, directed towards social engineering

through institutional devices and inculcation of values. Neeleman et al. emphasise that trusts should not only 'protect assets', but also 'promote values'. In other words, trust provisions should be directed towards character development. For example: 'Generally, the trustee should not make distributions to a beneficiary if in the trustee's judgement such distribution would negatively affect the beneficiary's motivation to become productive and self-reliant' (2003: 105).

On a more ambitious scale, Hughes advocates a trans-generational family infrastructure. Accordingly, he advises a 'social compact' among family members reflecting their 'shared values' (2004: 19), and a 'system of representative governance' (including a constitution) to enact the compact. Hughes elaborates:

For any system of governance to provide a means for excellent decision making over a long period of time, it must be inculcated into the belief systems of every member of the family in every generation. The system must come to be seen as the foundation for each individual members's success and for the family's overall success. A part of this process of transcendence is the constant reaffirmation by family members of the values expressed by the governance system. (2004: 21)

### **'Keeping it in the family'**

For the most part advice books about family trusts are not troubled by the distinction between tax advantages and family considerations. There is an implicit assumption that the two ends are one and the same. Trusts protect family assets from all manner of threats including tax officials, thereby 'keeping it in the family'. In this sense, the books provide a normative foundation for tax minimisation,. The more assets at stake, the more talk there is about family values.

Yet advice books suggest more complex currents beneath the surface. Trusts have different tax advantages in different jurisdictions, but their common thread is that they create a collective family entity. Advice books confirm Marcus's observation in the 1980s that trusts structure family relationships not only among the rich, but among the propertied middle class – especially in

Australia, where the tax advantages spread more widely. Trusts structure family relationships partly through the creation of a family welfare system, and partly through provisions directed towards family organisation and values. These patterns are at odds with dramatic changes in family structure and meaning since the 1970s. Specifically, the influence of family trusts highlights that the pursuit of personal autonomy and the deinstitutionalisation of the family only go so far, at least among the propertied classes.

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