

# information PACK

## TRUSTS

RHODES DOCHERTY & CO

Chartered Accountants



### What is a trust?

A TRUST is an obligation on a person to hold property for the benefit of others (who are known as 'beneficiaries'). There are two main types of trusts used in business and investment structures:

- **Unit trust** - in a unit trust, beneficiaries must buy units in the trust - these units determine their entitlement to a share of the trust's profits.
- **Discretionary trust** - with a discretionary trust, the beneficiaries are not required to purchase units. Instead, the trustee has the discretion to direct profit distributions to certain beneficiaries, who are identified in the trust deed.

### How do I set up a trust?

A trust is established by the execution of a trust deed. The trust deed is a very important document, as it outlines the rules and regulations for the running of the trust, as well as the trustee's rights and responsibilities, and

the entitlements of the beneficiaries. It is important that the trustee(s) read and understand the trust deed, particularly in relation to their rights and obligations.

The trustee can be a person, more than one person, or a company.

The cost of purchasing a unit trust or discretionary trust is about \$655.00 plus stamp duty for the stamping of the trust deed. If you wish to set up a company to act as trustee of the trust, this will cost a further \$1,000.00.

## How does a trust work?

There is a slight difference between the operation of a unit trust and a discretionary trust, but broadly, the trusts both operate along the same lines.

Once the trust has been established, it will apply for a TFN and for an ABN. If you are intending to run a business through the trust, then it will generally also be required to apply for GST registration (and PAYG Withholding registration if you will have employees in the business).

GST registration is generally not required where the business is used solely to earn investment income, however if the trust's income is derived from commercial real property and the income is over \$75,000 per year, then the trust will have to register for GST.

Each year, the trust will prepare financial statements and an income tax return. A set of financial statements is also required for the company, if a corporate trustee is used.

Once the net profit of the trust has been determined, the profits are distributed to the beneficiaries:

- for a unit trust, each unitholder receives a share of the profits, determined by the number of units they hold;
- for a discretionary trust, the trustee decides which of the trust's beneficiaries will receive a distribution of profits.

The beneficiaries are then required to include the income in their income tax returns, together with any tax benefits associated with those distributions.



If the trust makes a loss during the financial year, that loss cannot be distributed to beneficiaries. It is instead carried forward to be recouped against the trust's future profits.

## What are the advantages and disadvantages of using a trust for my business/investments?

The **advantages** of using a trust are:

Flexibility in the distribution of income and capital - for discretionary trusts. The trustee is therefore at liberty to direct the income of the trust to the beneficiary with the lowest marginal tax rate.

Tax concessions earned by the trust retain their character in the beneficiary's hands - for example, if the trust holds a CGT asset for over 12 months, it is entitled to the 50% CGT discount - and this discount is passed on to the beneficiary when they declare the CGT income received from the trust. This makes trusts an attractive vehicle for investing in capital appreciating assets, and for building up a business for future sale.

Asset protection - trusts, particularly when combined with a corporate trustee, can assist with asset protection. This can be of particular importance when running a business through a trust.

The **disadvantages** of using a trust are:

Losses cannot be distributed to beneficiaries in the year they are incurred, but are carried forward indefinitely to be recouped against future profits.

Legislation to tax trusts in the same way as companies (i.e. tax at 30% on ordinary/trading income and no CGT concessions) was proposed by the Federal Government.

While the Government eventually rejected the legislation, there is every possibility that it could be considered again, in a modified form.

## Anything else I should know?

The decision to set up a trust should be carefully considered in the light of your overall, long-term financial plan. Trusts are extremely useful vehicles for businesses and investments in



some circumstances, but the benefits will not outweigh the costs in all cases.

Rhodes Docherty & Co has experienced staff who can advise you on whether a trust is the best vehicle for your business or investments.

### What's the next step?

If you require advice as to whether a you should establish a trust, or assistance in setting one up, please contact Rhodes Docherty & Co on (02) 9988 4033 to make an appointment.



### RHODES DOCHERTY & CO

Chartered Accountants

ABN 99 131 742 633

Suite 202, 164A Mona Vale Rd, St Ives

P0 Box 86, St Ives NSW 2075 Australia

Tel (02) 9988 4033 Fax (02) 9449 4229

Email: [accountants@rhodesdocherty.com.au](mailto:accountants@rhodesdocherty.com.au)

Website: [www.rhodesdocherty.com.au](http://www.rhodesdocherty.com.au)

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