

# TRUST DISTRIBUTIONS



## KEY TAKE AWAYS

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- Don't ASS-U-ME
- Read the deed
- Accountants and lawyers should be leveraging off from each others:
  - Accountants will generally be closer to the strategy of the distribution.
  - Lawyers can ensure complex resolutions are effective.

# 1. CASE STUDY



## CASE STUDY

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- The Barnaby Trust was established by a deed of settlement in December 1976 in QLD.
- The vesting date of the Barnaby Trust is 80 years from the date of establishment or such earlier date if the Trustee shall in its absolute discretion in writing appoint.
- The Barnaby Trust was established to benefit the children, grandchildren and remote issues of the 'parents'.
- The 'parents' was defined to be James and Joyce Barnaby.

## CASE STUDY

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- The Barnaby Trust has made a family trust election with James as the test individual. James is now deceased.
- The Trustee of the Barnaby Trust is Kiwi Pty Limited (the Trustee). The directors of the Trustee are Anne Elizabeth Barnaby and Margaret Rose Barnaby who are the daughters of the 'parents'.
- Under clause 11 of the deed, the Trustee has the power to appoint a new trustee.

## CASE STUDY

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- The Beneficiaries are defined as follows:
  - The parents and the children, grandchildren born and to be born of the parents and the spouses, widows, widowers of the said children and grandchildren and any person related by blood or by marriage to any of the said beneficiaries other than and always excluding the Settlor himself.
  - Any person who is or has any time been employed by or has contracted with any of the beneficiaries hereunder.

## CASE STUDY

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- Any of the following entities whether formed in Australia or elsewhere which the Trustee at any time and from time to time may nominate in writing as a Beneficiary namely:
  - The Trustee (in its capacity as such Trustee) of any Trust or settlement (hereinafter called “an eligible Trust”) the beneficial interests of which must vest within the perpetuity period applicable to the Trusts hereby created and under which any beneficiary hereinbefore referred to has any interest whether absolute or contingent and whether liable to be defeated by the exercise of any power of appointment or revocation or to be diminished by the increase of the class to which he belongs; and

## CASE STUDY

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- Any corporation (hereinafter called “an eligible corporation”) at least one share in which is owned by any beneficiary hereinbefore referred to or at least one share in which is owned by the Trustee of an eligible Trust; and
- Any other legal entity at least one share or other interest (whether present or contingent) in which is owned or held by any beneficiary hereinbefore referred to or is owned or held by the Trustee of an eligible Trust or by an eligible corporation; and
- Any person or persons company or body (to be known as a ‘School Beneficiary’) conducting a school or like educational institution at which any of the beneficiaries named or defined herein may attend from time to time.



## CASE STUDY

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- Can the Barnaby Trust distribute to other trusts which have not yet been established?
- What distribution restrictions would the 'other trusts' have to have in respect of their family members?
- Are there any special requirements that the soon to be established other trusts require in their trust deeds?
- Are there any other issues you can identify?

# 2. WHO



# WHO

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- Who are the beneficiaries?
- Is there uncertainty in who can be a beneficiary through the lack of defined terms (spouses, relatives, issue)?
- Have there been events that may have impacted on who could be a beneficiary?
- Have documents and powers been validly exercised changing beneficiaries?
- Have beneficiaries been excluded (in the original document or by variation)

# WHO

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- Family trust elections, or interposed entity elections?
  - Family trust distributions tax
- Discretionary beneficiary's interest is just a 'mere expectancy'
- Beneficiary's interest based on the terms of the trust deed
- Distributions to trusts and 'wait and see' – *Nemesis Australia Pty Ltd*
- Notional settlor clauses

## EXAMPLES

(iii) Any and all of the children, grand-children or grand-children of the mother and the father whether living at the date of this Deed or born hereafter;

(b) *Child, Children and Issue* includes ex nuptial children and legally adopted children;

<b>Spouse</b>	Means a lawfully married spouse and includes where a person is a widow or widower.
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## EXAMPLES

F. "Nominated Beneficiary" means any person or limited or unlimited liability company or any trust who is nominated as hereafter provided to become an eligible beneficiary. The following shall not be capable of being nominated as aforesaid;-

(i) a person referred to in paragraphs (i) to (x) inclusive of the definition of "the Eligible Beneficiaries" contained in this clause; or

(ii) the Settlor; or

(iii) any person or company who or which is or has been a trustee of this Trust;

(iv) the legal personal representatives of the mother or the father in such capacities and who or which is at the relevant time the subject of a subsisting nomination made under clause 2(c) hereof.

## EXAMPLE

### "Exclusion from Benefits

Notwithstanding any definition or other provision in this Deed of Settlement, it is hereby declared that:—

- (a) the Settlor, his estate and any corporation or trust in which the Settlor or his estate has any actual or contingent beneficial interest are specifically excluded from all or any benefits whatsoever under this Trust;  
... and
- (b) *any person who donates, assigns or transfers for less than full market value any item of property to the Trustee with the intention that such item of property be added to the Trust Fund will be specifically excluded from all or any benefits whatsoever under this Trust."*

## EXAMPLE

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13.14 Despite a contrary term of the Deed, if a Beneficiary is a **Foreign** Person, then the share of an amount of Income of the Trust in an Income Year or Capital at any time which the Trustee may distribute to such Beneficiary, must not exceed the maximum percentage the Trustee can distribute without breaching the *Foreign Acquisitions and Takeovers Act 1975 (Cth)*.



# EXAMPLE

## 22. Distribution Restrictions

22.1. The Trustee shall not make a distribution or do any other act which would:

- (1) cause the Trust to become a “foreign trust” for the purpose of the *Duties Act 2000* (Vic) or the *Duties Act 2001* (Qld); or
- (2) cause the Trustee to be a “foreign person” for the purpose of the *Duties Act 1997* (NSW) or the *Land Tax Management Act 1956* (NSW); or
- (3) cause the Trustee to be a “foreign person” for the purpose of the *Foreign Acquisitions and Takeovers Act 1975* (Cth).

22.2. Clause 22.1 shall not be varied while the Trust Property includes an interest in real estate (including without limitation as purchaser under a contract for sale) in New South Wales,

Queensland or Victoria or for a period of three years following the sale or disposal of the last such interest in real estate.

## FIXES?

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- Appointing beneficiary
- Varying the trust deed
- Trust cloning
- Distributing to an interposed entity
- Rectification

## A COMMENT

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- Foreign investment in property
- Trusts can include foreigners, if they do, however, they need to consider the applicable 'FIRB', Stamp Duty and Land Tax consequences.

# 3. WHAT



# WHAT

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- Income or capital?
- What is income?
- Income for tax purposes
- Income under the trust deed
- Difference between income definitions
- *Bamford*, TR 2012/D1 and *Colonial First*
- Absence of definition of income

# WHO

- Income according to accounting principles
- Income according to tax legislation (section 95)
- Income determined by trustee

	No Income definition	Equalisation Definition	Re-characterisation Definition
<b>Distributable Income</b>	accounting income	accounting income	accounting income
		assessable capital gain	assessable capital gain
			non-assessable capital gain
			disregarded capital gain
	franked dividend	franked dividend	franked dividend
		Div 7A dividend – payment	Div 7A dividend – payment
<b>Distributable Capital</b>	assessable capital gain		assessable capital gain
	non-assessable capital gain	non-assessable capital gain	non-assessable capital gain
	disregarded capital gain	disregarded capital gain	disregarded capital gain
	Div 7A dividend – payment		Div 7A dividend – payment
<b>ATO Excluded Distributable Income</b>	market value substitution capital gain	market value substitution capital gain	market value substitution capital gain
	franking credit	franking credit	franking credit
	Div 7A dividend -loan	Div 7A dividend -loan	Div 7A dividend -loan
	CFC & Transferor Trust attributable income	CFC & Transferor Trust attributable income	CFC & Transferor Trust attributable income
	Part IVA deemed income and assessable capital gain	Part IVA deemed income and assessable capital gain	Part IVA deemed income and assessable capital gain
	trust distribution receipt of excluded distributable income	trust distribution receipt of excluded distributable income	trust distribution receipt of excluded distributable income

ALTERNATIVES

# WHAT

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- Truly tailoring what 'distributable income' is:
  - Reclassifying income and capital gains – *Forrest v FCT* (can't change context)
  - Reclassifying and allocation of outgoings – *Cajkusic v FCT* (want to avoid no distributable income)
  - Allocation of capital losses
  - Non-recoupment of revenue losses

# WHAT

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- Streaming – *Bamford and TLAM No. 5*
  - Classifying separate classes of income (capital gains or franked dividends)
  - Ensuring specific entitlement



# WHAT

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- Streaming traps
- Capital gains
  - No trust income (can't distribute)
  - Capital gain on individual asset
  - Asset revaluation account (ensuring specific entitlement is followed through)
  - Splitting between income and capital to effect specific entitlement)

# WHAT

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- Franked dividends:
  - Ability to be classed as one class of income to avoid franking credits trapped
  - Expenses against relevant franked dividends
  - Franking credits cannot be separately streamed
- Franking credits:
  - Confirming exact calculations on basis dividends can be fully franked with difference franking credits attaching to the same amount

## EXAMPLE 1

- (j) "Income" of the Trust includes all profits or gains taken into account in calculating the net income of the Trust, and exempt income, as defined in Section 95(1) of the Act, notwithstanding that the whole or any part thereof may otherwise include Corpus of the Trust.
- (b) The Trustee may at any time prior to the vesting date distribute Corpus or any part thereof to any Corpus Beneficiary in such amount as it thinks fit. The Trustee shall make a record of such distribution and upon the vesting date or earlier termination of this Trust take such payments into account as it thinks fit.

## EXAMPLE 2

(a) when making any determination in relation to Income of the Trust Fund, which income or which part of the income or which class of income (whether by reference to source nature or otherwise) of the Trust is the subject of any particular determination or determinations and the income the subject of any such determination shall be treated for all purposes as being paid, applied, set aside or accumulated as the case may be from the income or part or class so identified. Without limiting the generality of the foregoing, it is further expressly provided that in making any determination in relation to Income of the Trust Fund, the Trustee may in the Trustee's sole discretion determine and identify that the whole or any part of any one or more of the following shall be paid, applied, set aside or accumulated for the benefit of one or more or any class of beneficiaries of the Trust:

(b) To maintain in the Trustees absolute discretion (with no obligation on the Trustee so to do), for the purpose of exercising its powers under Clause 3, separate accounts or accounting procedures in relation to each class or source of income and allocate costs or deductions as between those sources and to make a determination in relation to the income from each source, and the powers of the Trustee as set forth in Clause 3 shall be read and construed as if the references therein to determinations in respect of the income or net income of the Trust included in the alternative a reference to the income or net income from each source as aforesaid.

(c) To make an interim distribution of capital of the trust fund (including any capital gains which the Trustee may derive from time to time) whether in cash or by way of in specie distribution of assets of the fund or otherwise howsoever, and on such terms and conditions as the Trustee shall in its absolute discretion determine.'

# 4. WHEN



## WHEN

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- Historical ATO position – IT 328 and IT 329, now withdrawn
- Tax position – A beneficiary's present entitlement must arise at the latest by the end of the income year – *FCT v Ramsden*
- Trust position – Read the deed
- Adopt the earlier period
- Note concessions for specific entitlement for capital gains (i.e. contracts where the final amount is not known until settlement)

## WHEN

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- 'Contingent' style distributions (i.e. whatever amount to equal \$180,000)
- TD 2012/22EC
- *Lewski v FCT*

## WHEN

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- ‘...should the Commissioner of Taxation disallow any amount as a deduction or include any amount in the assessable income of the trust...100% to Australian Commercial Underwriting Pty Ltd’
- Above variation was authorised pursuant to the trust deed but no present entitlement would arise.



# 5. WHY



# WHY

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- Small business capital gains tax concessions:
  - Connected with
  - Small business concession stakeholder
- Trust losses:
  - Pattern of distribution test
  - Income injection test
- Division 7A
- Section 100A

# 6. HOW



## WHY

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- Read the deed
- Some deeds have obscured limitations based on various aspects of tax law – i.e. a limitation on distributions to 39% of the total distributions
- Other deeds just have specific consents required, or notice periods
- Are procedures required, including if resolutions can be made orally, and then later recorded in writing

## EXAMPLE 1

1.1.10. "Maximum Percentage " means the percentage specified in Part 12 of the Schedule.

3.14. Notwithstanding this Clause 3 the Trustee may not pay, apply or set aside an amount in excess of the Maximum Percentage of the income from the Trust Fund in any year to or for the benefit of:

3.14.1. a Secondary Beneficiary unless that Beneficiary is an Approved Secondary Beneficiary; or

3.14.2. a Tertiary Beneficiary unless that Beneficiary is an Approved Tertiary Beneficiary.

**PART 12 (MAXIMUM PERCENTAGE) THIRTY NINE PERCENT (39%)**

## EXAMPLE 1 CONT.

discretion.

8. Add the following clause 35:

### **Limitation of Entitlements**

36. Notwithstanding any other provision of this Deed, when exercising the Trustee's discretion under clauses 3.1, 4.2 and 4.3:

- (i) the Trustee must not distribute more than 39% of the income of the Trust Fund distributed in that year to any Beneficiary who is not an Unlimited Beneficiary, and that beneficiary's Small Business CGT Affiliates; and
- (ii) the Trustee must not distribute more than 39% of the capital of the Trust Fund distributed in that year to any Beneficiary who is not an Unlimited Beneficiary, and that beneficiary's Small Business CGT Affiliates.

## EXAMPLE 2

### Trustee must not exercise certain powers until Appointor has been given notice

- 5.12 The Trustee may exercise any of the following powers where it has given the Appointor at least three day's written notice of the exercise of the power, including specific details of how the power is to be exercised:
- 5.12.1 The power to Distribute capital.
  - 5.12.2 The power to resolve in writing how capital is to be Distributed on the Vesting Day.
  - 5.12.3 The power to Distribute Income or accumulate it.
  - 5.12.4 The power to resolve in writing how Income is to be Distributed.
  - 5.12.5 The power to choose a person to whom capital or Income is to be Distributed.
  - 5.12.6 The power to create a sub-trust.

# 7. WHERE





## WHERE

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- Talking about foreign beneficiaries
- Section 98 ITAA 1936
- 45% rate of tax for a non-resident individual
- Withholding tax
- Capital gains and loss of 50% discount
- Ultimate beneficiary reporting rules
- Foreign tax offset credit
- Conflicting tax laws of a foreign jurisdiction

# 8. CASE STUDY



**Any takers?**

## CREDITS

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Special thanks to all the people who made and released these awesome resources for free:

- Presentation template by [SlidesCarnival](#)
- Photographs by [Unsplash](#)

# THANKS!

ANY QUESTIONS?

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