

DISCRETIONARY TRUSTS AND QLD STATE TAXES

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Today's 'bubble and squeak'

Image - <https://www.thespruceeats.com/traditional-bubble-and-squeak-recipe-435202>

Discretionary trusts and state taxes



- ❖ Discretionary trusts and 'foreigner' surcharges
- ❖ Discretionary trusts and inadvertent payroll tax groups
- ❖ Amending discretionary trusts – what you can get away with
- ❖ Random tidbits

The problem with discretionary trusts



- ❖ Unique in that there is no beneficiary with a fixed interest
- ❖ Any fixed interest can be defeated with prior exercising of powers (distribution or accumulation)
- ❖ Discretionary nature = difficult to audit/predict the future
- ❖ How to govern the discretionary nature of a beneficiary's interest (?)
- ❖ Let's see how different taxes/States/Federal legislation deals

Property surcharges for foreigners



	Stamp duty (minimum)	Land tax (minimum)
Queensland	7%	2%
New South Wales	8%	2%
Victoria	8%	2%
South Australia	7%	N/A
Western Australia	7%	Commencing 1/6/20
Australia Capital Territory	N/A	0.75%
Tasmania	3%	N/A

Discretionary trust and foreigners



- ❖ Issue for property holding trusts
- ❖ Harmonised to relate to 'residential property' for stamp duty surcharges*
- ❖ Surcharge rates applying can double the stamp duty/land tax payable
- ❖ No harmonised definition of what constitutes a foreign trust**

Foreign trust for Qld stamp duty



- ❖ Trust where 50% **of trust interests** are **foreign interests**
- ❖ What's a trust interest in the context of a discretionary trust?
- ❖ '*Only a taker in default of an appointment by the trustee can have a trust interest*'
- ❖ Decoded – 'person who benefits when the trustee forgets to exercise a power'
- ❖ Commonly called the 'default beneficiary'
- ❖ Foreign interest is a trust interest held by a **foreign person** or a related person of a foreign person
- ❖ Foreign individual is an individual other than an Australian citizen or 'PR'
- ❖ Related person includes a family member (i.e. spouse, parents, siblings, lineal descendants etc)

What to look out for



- ❖ Discretionary trust acquiring Qld residential property
- ❖ Default beneficiary of the discretionary trust includes a foreign person
- ❖ May have Qld stamp duty surcharge problems
- ❖ *The cure:*
 - ❖ Structure discretionary trusts to not have foreign persons as default beneficiaries
 - ❖ Amend default beneficiaries of existing trust to remove foreign persons as default beneficiaries

Foreign trust for Qld land tax

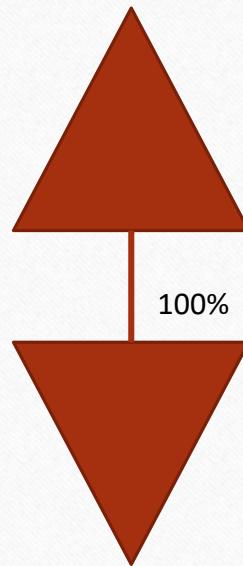


- ❖ Fun fact – use to be a different test – i.e. considered if a trust was an ‘absentee’
- ❖ As of mid-2019, aligns with the stamp duty definition
- ❖ **Important** – applies to all types of land held by a trust (i.e. not limited to residential land)
- ❖ **Also important** – some State land tax surcharges only applies to residential land

Practical example 1

No stamp duty issue as Unit Trust has not acquired residential land

Land tax issue as the 100% owner of a trust interest in the Unit Trust is a discretionary trust with 100% of the trust interests held by a foreigner



Unit Trust bought a golf course

Trustee – Foreign citizen
Default beneficiary – Foreign citizen

Identified by seeing the trustee's address on the trust deed



Foreign trusts and Qld land tax groups



- ❖ Section 22 Land Tax Act
- ❖ If there are at least 5 co-owners of land, they can be assessed by being owned by 1 co-owner as the trustee of the other co-owners (grouped)
- ❖ If the co-owners are grouped, then the Commissioner may make an assessment that the land is owned by a trustee of a foreign trust if 'foreign co-owners' hold at least a 50% interest in the land
- ❖ Foreign individuals are defined differently in this section. They are termed 'absentees' and the test if they ordinarily reside in Australia (although Australian citizens and PR holds cannot be an absentee)

Practical example 2



	Resident/foreign	Tenant in common %
Family trust	Foreign	12.5%
Dad, brother and sister	Foreign	18%
Client and mother	Residents	12%
Second family trust	Unsure	32.5%
Third family trust	Unsure	10%
Fourth family trust	Unsure	10%
Fifth family trust	Unsure	5%

Practical example 2



- ❖ Need to consider structure of family trusts of the family members who are not your client
- ❖ If 20% more interests are 'foreign', then technically a surcharge should be applied to the land
- ❖ In particular case study, the default beneficiaries of family trust included mum, dad, client, brother and sister. Given 3 of the default beneficiaries are foreigners, that already deemed it to be over a 60% foreign interest. Further, given client and mother are related persons to the foreigners, there is a 100% foreign interest
- ❖ Solution could be to amend the family trust deed to remove dad, brother and sister (to be considered later)

Don't structure in a vacuum



- ❖ Foreign Acquisition and Takeovers Act 1975 definition
- ❖ Trust is foreign if a foreign (or an aggregation of foreigners) has a substantial interest in the trust (20% and 40% respectively)
- ❖ Deeming provisions for a discretionary trust where every beneficiary able to receive a distribution is taken to hold the maximum percentage of income or capital of the trust they could receive
- ❖ Various States have adopted this broader definition and added variations to the definition
- ❖ Given clients use trusts to acquire multiple properties, better to structure discretionary trusts for property surcharges based on the most broad definition

Other State stamp duty definitions



- ❖ NSW largely adopts the FATA rules
- ❖ Vic adopts the FATA rules in relation to beneficiaries in receipt of the capital
- ❖ SA and WA also restricts a foreigner from being an appointor/principal
- ❖ NSW and Vic requires straight exclusions embedded as terms of the trust
- ❖ Note SA and WA came later (within past 2/3 years)
- ❖ Where will Qld go?

Payroll tax and discretionary trusts



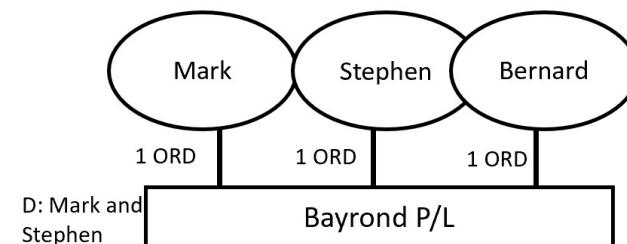
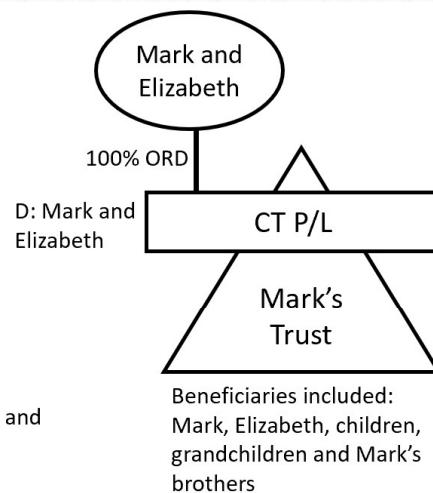
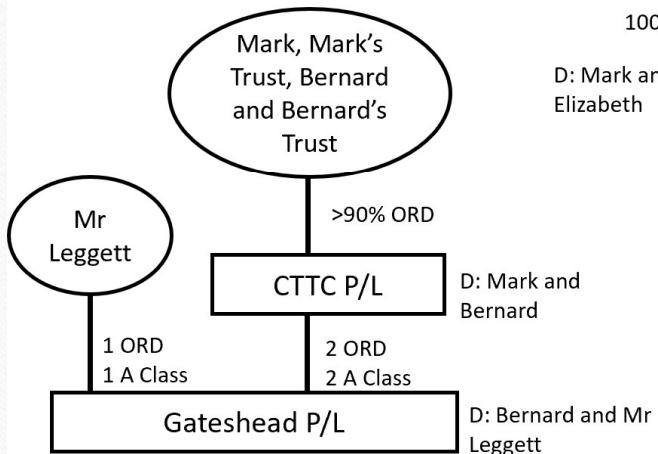
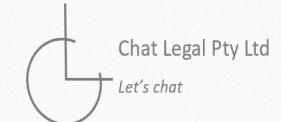
- ❖ Payroll tax imposed on businesses with aggregated wages exceeding \$1.1 million
- ❖ Anti-avoidance provisions available where businesses structure affairs to benefit from multiple thresholds
- ❖ Grouping occurs by common employees, common controllers and having a common members in two or more groups

What's it mean to control?

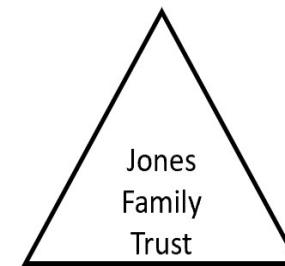
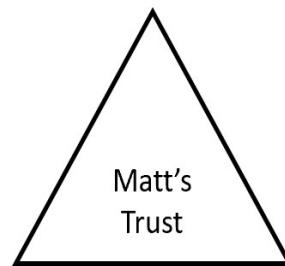
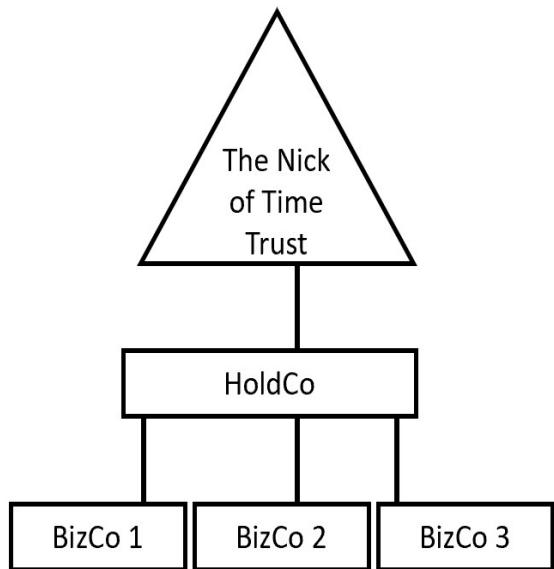
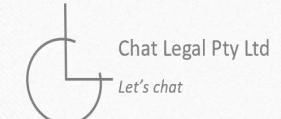


- ❖ Greater than 50% voting/beneficial interest (broadly)
- ❖ Multiple people owning interests can be grouped as a unit
- ❖ Controlling a discretionary trust is similar to the foreigner rule
- ❖ Specifically – any person who **may benefit** from a discretionary trust as a result of the trustee exercising a power or discretion...or failing to exercise a power or discretion is taken to be a beneficiary of the trust in respect of more than 50% of the value of the interests in the trust
- ❖ In otherwords, any potential beneficiary of a discretionary trust will be deemed to have a controlling interest in that trust and grouped
- ❖ If you have multiple trusts with a common beneficiary, then those trusts will be grouped due to having a common group member

The legal case



A more common case



Jones Family Trust holds share and property investments of Nick and Matt's parents. Given the age of the trust, Nick and Matt were named as primary beneficiaries of the Jones Family Trust. Nick's business (fast food franchises) pays \$800,000 in wages. Matt's business (dental) pays \$900,000 in wages.

Fixing discretionary trust groups



- ❖ De-grouping application based on a list of factors
 - ❖ Common resources?
 - ❖ Common management of entities?
 - ❖ Dependencies?
 - ❖ Commercial transactions between entities?
- ❖ Structuring right from the get-go
- ❖ Varying to get the structure right (i.e. deleting beneficiaries as certain members)
- ❖ Rejecting interests to get the structure right

Amending discretionary trusts



- ❖ Changing beneficiaries – above examples to not be a foreign trust or to avoid grouping unrelated businesses
- ❖ Deleting that ex-spouse as a beneficiary/trustee/appointor – divorce example
- ❖ Adding additional persons as beneficiaries
- ❖ Changing the trusteeship whether for succession, liability or saving cost purposes
- ❖ Changing the appointor/principal
- ❖ Updating the terms of the trust

Heads of duties for discretionary trust



- ❖ Change in legal ownership – there has been a transfer or an agreement for the transfer of dutiable property
- ❖ Change in way an entity holds the property (i.e. from an individual capacity to their capacity as trustee of a trust) – there is a creation or termination of a trust of dutiable property
- ❖ Change in beneficial ownership – there is a trust acquisition or trust surrender
- ❖ Applies to land and business assets
- ❖ Some exemptions can apply to business assets

Exemptions for discretionary trust



- ❖ Exemption from stamp duty on a change of trustee available provided no change in beneficiary interest
- ❖ If change of trustee as part of a change in beneficiary interest, then duty is paid on the beneficiary interest
- ❖ Exemption from stamp duty on changing of a trust interest if the trust is a 'family trust' and the change in interest occurs between family members
- ❖ Devil in the detail as it requires an analysis of the trust deed to determine the primary beneficiary relationship as well as the taker in default of appointment for capital

When to be aware of trust changes



- ❖ Change being made either changes the beneficiaries of the trust, or changes the trustee
- ❖ Removing an ex-spouse common as spouses are included as default beneficiaries
- ❖ Removing foreign beneficiaries who are default beneficiaries

Trap – corporate trustee duty



- ❖ Landholder duty applies to transfer of shares in company holding at least \$2 million in property
- ❖ Corporate trustee duty applies to transfer of shares in a company that acts as trustee for a trust holding *any* dutiable property
- ❖ **Trap** – May change shares in a company holding a residential investment property as trustee for a trust, and not consider any duty applying as the residential investment property is less than \$2 million
- ❖ Exemptions available if transfer of shares is between family members

Tip – family home and land tax



- ❖ No land tax for a family home in Queensland
- ❖ Exemption extends to discretionary trusts provided land used as family home for a beneficiary '*whose favour a power of appointment has been exercised*'
- ❖ Consider obtaining a refund
- ❖ There are a list of factors to consider to show Revenue Authorities that the land has been used as the family home

Take-outs on a slide



- ❖ Buying property in Qld? Tick the box excluding foreigners as beneficiaries
- ❖ Running a business with a discretionary trust in the group structure – consider if wages in the business and other family members businesses are getting close to \$1.1 million and if steps need to be taken to mitigate audit risks
- ❖ Amending a discretionary trust? Be careful if you are looking to amend the beneficiary class or change the trusteeship
- ❖ Transfer shares in a company acting as trustee? Consider corporate trustee duty
- ❖ Client's family trust owns the family home? Check if refunds are available for land tax not needed to have been paid

Questions?

Contact details



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