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Unit Trusts after the Federal Budget

The Federal Budget has introduced new taxes on trusts and in the process created significant uncertainty for property acquisition structuring decisions moving forward.

To quote Donald Rumsfeld, we have known knowns, known unknowns and unknown unknowns.

The Government announced a minimum 30% tax on the taxable income of discretionary trusts. Some beneficiaries receiving distributions will have an off-set for the tax paid by the trustee.

The Budget Papers say that various types of trust are exempt from the new tax. These are "fixed and widely held trusts (including fixed testamentary trusts), complying superannuation funds, special disability trusts, deceased estates and charitable trusts".

Also, certain types of income are exempt from the new trust. These are "primary production income, certain income relating to vulnerable minors, amounts to which non-resident withholding tax applies, and income from assets of discretionary testamentary trusts existing at announcement".

The first question is whether a unit trust will count as a "fixed trust". The ATO has a description of fixed trusts in Practical Compliance Guideline 2016/16. The usual form of unit trust used for property syndicates and private joint ventures might not fit the description in PCG 2016/16.

Does this mean that private unit trusts will be treated as discretionary trusts? We will have to wait for the legislation, but the exclusion of widely held trusts is a clue that the Government is going to treat a closely held unit trust in the same way as a discretionary trust.

The next issue relates to the credit for the tax paid by the trustee. Beneficiaries that are not corporate beneficiaries will receive a non-refundable credit. The exclusion of corporate beneficiaries .

The "some beneficiaries" is a known unknown. The government announced that distributions to companies will not be subject to the off-set. The reason given is to avoid the corporate beneficiary creating a refundable franking credit that reduces the minimum tax. The result is double taxation for income distributed to corporate beneficiaries and significant restriction on the use of "bucket companies".

What is not clearly stated is whether distributions to other discretionary trusts will be subject to the credit. The simplest interpretation of the announcement is that a distribution to a corporate beneficiary means a company receiving the distribution beneficially, rather than as trustee. But again, we need to see the draft legislation.

Given these uncertainties, investment structures need considerable thought until the landscape becomes clear.

For existing investments, the Government foreshadowed roll-over relief to move out of structures affected by the new tax. Again, we need to see the draft legislation before decisions can be made. No doubt State and Territory Treasurers will be anticipating a spike in Transfer Duty collections.