# Unit trusts

## Features and operations

### Key points

- The income and assets of a unit trust are held by the trustee on behalf of the unitholders
- The unitholders own units in the unit trust and have certain rights to income and capital distributions, and the power to change the trustee
- The trustee has the day to day control of the activities of the unit trust, subject to the rights of the unitholders and the terms of the trust deed

## History of trusts

1. Trusts were first used as legal structures in England in the Middle Ages. Originally, it was necessary for a trust to have specific beneficiaries with fixed interests.

2. The use of trusts for trading and investment ventures became popular in Australia during the 1970s and trusts are now a very common form of business and investment structures.

## Main features

### There must be a trust fund or property

3. The initial trust money is paid by way of subscription for a nominal number of units by the initial unitholders.

### There must be a trustee

4. The trustee is the legal owner of the trust property. While the title to the property is registered in the name of the trustee, the trustee holds the property subject to the duties and responsibilities outlined in the trust deed.

### Beneficiaries

5. A trust must have identifiable beneficiaries. These are the unitholders.

## Common features and terms

### Changing the trustee

6. A majority of unitholders have the power to change the trustee.

## Practical aspects of unit trusts

7. The law of trusts is quite complex but, on a day to day basis, the use of the trust for investment and business purposes is relatively simple.

### Unpaid distributions

8. One aspect, which needs constant attention, relates to the build-up of loan accounts in favour of the unitholders.

9. The trust deed provides that distributions of income do not actually have to be paid out to unitholders but may be recorded as journal entries with the amount of the income distribution being left as a loan owing to the unitholder.

10. It is therefore important to monitor the level of all loan accounts in a trust (preferably on an annual basis) as steps can be taken to make sure that the amount of the loan accounts is kept under control. However, it is difficult to do this after the event.

## Liability of trustees/directors

11. The trust estate itself is not a separate legal entity. It is the trustee who holds the trust property and is responsible for trust liabilities.

12. All transactions entered into in respect of the trust are entered into by the trustee, which is personally liable.

13. Where individuals are trustees, they will be personally liable for all debts of the trust.

14. If the trustee is a company, the directors of the company are subject to the normal obligations and liabilities of company directors.

15. However, the trustee (and therefore the directors) is entitled to be indemnified out of the assets of the trust for all liabilities properly incurred in carrying on the trust activities.

16. Under the CGW Structures deed, the trustee does not have a right of indemnity personally against any of the unitholders. The right of indemnity is limited to the extent of the trust assets.

17. Therefore, creditors of the trust are also limited in their claims to the assets of the trust and cannot sue the unitholders personally unless the unitholders also happen to be directors or have provided personal guarantees.

18. Where a company acts as trustee, the directors may be personally liable for debts incurred by the trustee in circumstances prescribed by the *Corporations Act 2001* and other Acts that impose personal obligations on directors. However, the extent of the liability of directors of a corporate trustee is not any greater than the liability that would attach to the directors of a normal company.

19. Essentially, directors will not be personally liable where they have discharged their duties (subject to some exceptions).

## Taxation treatment of trusts

20. The provisions governing the taxation of trust income are contained in a separate division of the *Income Tax Assessment Act*.

21. Although the trust is not a separate legal entity, the trustee is required to calculate its ‘net income’ as if it were a separate taxpayer for the purposes of the tax law.

22. Generally, the trustee is not taxed on its income. The procedure is that the income is distributed to the unitholders who are then taxed on their share of the income. One exception to this is if income is distributed to children who are unitholders but who are under the age of 18 years. In those cases, the trustee will be assessed.

23. If for any reason, the trustee elects not to distribute part of the trust income but to accumulate it within the trust, then that accumulated income is also taxed at the top marginal rate.

24. It is important that decisions on the distribution or accumulation of income are properly minuted. This should generally be done before 30 June each year.

## Administration

25. The trust should have a bank account, which should be opened in the name of the trustee acting as trustee.

26. If a company acts as trustee, it will be necessary to pay the annual review fee to the Australian Securities and Investments Commission and to comply with the administrative requirements of the *Corporations Act 2001* (Cth).

27. The trust estate will be required to prepare and lodge tax returns on an annual basis. As indicated above, the trustee is not generally taxed on the income but the ATO requires that returns are lodged on behalf of the trust so it can calculate the tax payable by the beneficiaries on their share of the income of the trust.

28. It is possible to vary the trust deed if the need arises but care needs to be exercised as to what changes are made and how these are implemented because some changes to trust deeds can attract substantial duty under the *Duties Act 2001* (Qld).

## Effect on your Wills

29. We recommend that you review your Will once you have established a trust.

30. If you hold assets in a trust structure, those assets are outside the scope of your Will. The assets, which can dispose in your Will, are the units you personally hold in the trust and the shares in the trustee company (if any).

31. The persons who hold the shares in the trustee company effectively control the trust and are therefore in a similar position to the executors under your Will. Therefore, some care is needed in drafting the Will to ensure that the trust assets are properly administered and disposed of.