Trust tax planning 101: avoid lost trust deeds

- by Matthew Burgess, Director, View Legal

One of the key trustee duties of any form of trust is to know the terms of the trust deed and keep the original wet (not electronically!) signed trust instrument safe and secure. This duty is very difficult to discharge however if the trust deed is lost.

The case of *Jowill Nominees Pty Ltd v Cooper* [2021] SASC 76 ("Jowill") provides a recent insight into the issues a court will consider where a trust deed has been lost. Court application being the only pathway to achieve a solution that is binding on beneficiaries and third parties such as revenue authorities, as well as protecting the trustee where an original trust deed has been lost.

Factual matrix

Broadly, the factual matrix involved a trust that was established in 1976 and for many years had as its substantive asset shares in Coopers Brewery Limited. The original trust deed was unable to be located and there was also no copy of the document.

There was however an advice letter from a lawyer in 2007, based on a review of the original trust deed that explained a number of key provisions including the range of beneficiaries. Other aspects were also able to be reverse engineered, such as the probable perpetuity period and the fact that the deed likely permitted capital distributions.

The capital distribution power was assumed to exist by the Court on the basis of the lawyer's evidence that if it did not, this would have been flagged in the advice letter, particularly because the lawyer confirmed no trust deed read in 45 years of practice failed to contain such a provision.

Decision

The Court confirmed that under the relevant state-based Trustee Act, it could vary the trust deed (effectively adopting a new deed here), so long as the following tests were met (all of which were primarily due to the evidence of the lawyer that provided the 2007 advice letter):

- there is good reason to make the proposed exercise of powers;
- the proposed exercise of powers is in the interests of beneficiaries;
- the proposed exercise of powers will not result in 1 class of beneficiaries being unfairly advantaged to the prejudice of another class (here it was critical that all beneficiaries were represented before the Court);
- the proposed exercise of powers accords as far as reasonably practicable with the spirit of the trust;
- the proposed exercise of powers will not disturb the trust beyond what is necessary to give effect to the reasons for the revocation or variation; and
- the application is not substantially motivated by a desire to avoid or reduce the incidence of tax.

The deed approved by the Court was based on a precedent as at 1978 of the firm that had likely drafted the trust deed, adjusted to align with the advice from 2007.

While the Court did consider a request to simply revoke the trust, it ultimately confirmed its preference to approve the, varied, adopted trust deed as it was the least disruptive approach. The Court confirmed the trustee could choose to exercise its discretion to make a capital distribution of the assets of the trust (which was its intention) and subsequently vest the trust, relying on the terms of the court-approved deed.

Vesting issues

If a trust deed cannot be found, commercially it can often be the case that the most responsible approach is for the trustee to wind up the trust. Indeed, there may be disgruntled beneficiaries or third parties that essentially force a trustee to adopt this course.

Any vesting of a trust and subsequent distribution of assets, with or without court approval, is likely to trigger a range of revenue consequences, particularly taxation and stamp duty.

These revenue consequences normally arise where a positive determination is made by the trustee to vest a trust - the trustee will usually resolve to make 1 or more beneficiaries absolutely entitled to the assets (or specific assets) of the trust.

While not intended to be an exhaustive list, the revenue related ramifications of a trust vesting can include:

- CGT being payable on the increase in the value of any assets being transferred since the date they were acquired (see TR 2018/6, although noting that in the *Jowill* decision, it may well have been the case that the assets were pre-CGT and therefore the transfer of assets on vesting would not have triggered a CGT cost, rather the assets would become post-CGT in the hands of the new owners);
- income tax being payable on non-capital assets, such as plant and equipment and trading stock;
- stamp duty being payable on the transfer of the assets, to the extent they comprise dutiable property in the relevant jurisdiction (again noting that in the *Jowill* case, the main assets appeared to be non-dutiable property such as shares in non-land rich companies);
- additional tax, stamp duty and commercial costs being incurred to subsequently transfer the assets out of the name of the recipient beneficiary (if they want the assets then re-routed to a trust environment);
- asset protection exposure for the beneficiary receiving the assets in the event they subsequently commit an act of bankruptcy;
- considering the impact of the rule against perpetuities (which may effectively prevent a distribution to another trust if this causes the assets to remain within a trust environment for more than 80 years, other than perhaps in South Australia); and
- where an individual receives the assets, the need to update their estate plan to reflect the additional assets owned in their personal name.

Conclusion

If the vesting of a trust is being anticipated by the parties, many of the consequences above can be adequately managed through appropriate planning.

All planning opportunities are however predicated on the trustee knowing the terms of the trust deed, which in turn is predicated on not losing the document!