Family Trusts

Family trusts have been a popular way of owning assets and conducting business operations in New Zealand.

Parties to a trust have specific roles and obligations.

Settlor

A settlor establishes the trust, signs the trust document, and transfers an initial settlement to the trustee(s). The initial settlement amount is usually relatively small (usually less than $100) with more substantial assets being transferred by way of sale or gift after the trust has been settled. The initial settlement and subsequent transfers of property are held on trust.

Trust deed

The trust deed is prepared by a solicitor or administered by an accountant or other person using a suitable precedent. It sets out:

- The purposes of the trust (i.e. who can benefit)
- What the trustee can do
- Investment powers
- Borrowing powers
- Period of the trust (with effect from 30 January 2021 the maximum duration is 125 years)
- Names of settlor, beneficiaries, trustee, and appointor(s)

Trustees

Trustees are responsible for all aspects of day-to-day management, investments etc., relating to the trust. Subject to the terms of the trust deed, a trustee can be a natural person or a company. The number of trustees is usually determined by the trust deed. The trustees have extremely wide legal and administrative responsibilities for the management of the trust.

The trustee(s) hold assets for the benefit of the beneficiaries of the trust. The trustee(s) of a discretionary trust generally have the power to make distributions of profits and capital to any beneficiary or beneficiaries.

The trust, through the trustees, can conduct virtually any type of business activity that is approved by the trust deed in basically the same way as any other business activity operates.

In a discretionary trust, the trustees decide how to distribute profits and capital gains. Subject to the terms of the trust, the trustee is not bound by any fixed or predetermined percentage of distribution.

Trustees owe significant obligations to the beneficiaries of the trust. They also have duties relating to tax and financial conduct. Their obligations are set out in the Trusts Act 2019 and the Income Tax Act 2007. Be aware of these obligations before accepting an appointment as a trustee.

Trustees’ Responsibilities

A trustee’s role is not necessarily onerous but does carry specific legal significance and responsibilities. A beneficiary can sue a trustee for a wrong-doing whilst acting as trustee that constitutes a breach of trust.

Trustees may wish to notify beneficiaries of their status when each beneficiary attains the age of 20 years. The Trusts Act 2019 introduced a presumption that trustees will give basic trust information to all beneficiaries.

Trustees’ decisions, whether made formally or not, are called Trustee Resolutions. It is good practice to record each resolution. Where this is not done at the time, the trustees should ensure that the minutes of the next trustee meeting record the resolution.

Trustees’ meetings should be minuted and all trust documentation should be maintained carefully.

Beneficiaries

Beneficiaries are the people for whom the trust was created. They can be divided into several groups:

- Primary beneficiaries – normally (but not necessarily) the settlors and present and future children
- Secondary beneficiaries - normally future grandchildren and great grandchildren
- Tertiary beneficiaries - other trusts, religious organisations, charities and so on
- Final beneficiaries are the beneficiaries who benefit at the end of the Trust

Appointor(s)

Appointers have the powers of appointment set out in the trust deed. Subject to the terms of the trust deed, the appointor(s) may have the right to add and remove trustees and beneficiaries, and to approve permitted changes provided for in the trust deed.

Advantages

The advantages of a trust include:

- Assets can be protected from a variety of people and organisations, such as:
  - creditors
  - family
  - asset and income tested benefits and assistance
- Income can be distributed or paid out for the benefit of family members
- The trust is ongoing. It has a life potentially of up to 125 years (with effect from 30 January 2021), unless it is wound up and distributed earlier

Disadvantages

Disadvantages include:

- additional legal and accounting costs to set up a family trust
- ongoing compliance costs to administer the trust. If the trustees own income producing assets, tax returns and full financial statements must be prepared annually. In addition, the trustee must maintain resolutions approving financial statements, beneficiaries' distributions, and all major transactions. A good accountant must usually be employed. There may also be reporting obligations if FATCA or the CRS applies
- A good knowledge of trustees' responsibilities is required. It is not wise for anyone to agree to act as a trustee until they are fully aware of their duties and responsibilities
- Trustees must administer balances owing to beneficiaries carefully. Any distributions that are unpaid can be demanded, as well as being included in the property of the beneficiary for relationship property and other purposes.
- Disgruntled beneficiaries have the power to sue trustees where trustees have acted in breach of trust. This is rare, but it reinforces the need for trustees to be fully aware of their responsibilities

Taxation

The trustee of a family trust pays income tax on taxable income that is not distributed to any beneficiaries. The trustee rate of tax is currently 39%, or 33% where the taxable income not distributed to beneficiaries is $10,000 or less (a 'de-minimis trust').

Income distributed to beneficiaries (other than minor children) is taxed at the beneficiary's marginal rate. In most cases any distribution from a trust to a child under the age of 16 at the trust's balance date will be taxed at the trustee's tax rate.

Trusts are not useful to everyone. Salary and wage earners, or people who derive their income principally from personal exertion are unable to obtain significant taxation benefits from a family trust.

If you would like to discuss the requirements for trusts or your responsibilities as a trustee, please contact us.