How-to Guide

Establishing a Land Tax Unit Trust – Negative Gearing

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Description	This guide looks at buying a rental property and negative gearing with a trust.
Other relevant guides	- *How to set up a discretionary trust* - *How to set up a unit trust*
Documents required	- *Resolution to establish a unit trust* - *Unit Trust deed* - *Application for units (Unit Trust)* - *Resolution to issue units (Unit Trust)* - *Unit certificate (Unit Trust)* - *Resolution to acquire property*
Notes	Prior to considering the following material, it is recommended that you read the "How to" Guides dealing with the establishment of a discretionary trust and the establishment of a unit trust. The following steps should be undertaken in relation to the strategy of negative-gearing with a Land Tax Unit Trust.

Step 1 – Establish a Land Tax Unit Trust (see "How To" Guide – Land Tax Unit Trust)

Establish a Land Tax Unit Trust with the individual who is going to borrow and claim the negative gearing as the initial unitholder. The trustee could be that person and their spouse or a company. The sole unitholder cannot also be the sole trustee.

EXAMPLE: If Sue and Bill are married and Bill is to borrow and acquire units and be the sole unitholder the following combinations of trustee are allowed:

- Bill and Sue,
- Sue,
- XYZ Pty Limited

NOTE: The initial ordinary Unitholder of this Land Tax Unit Trust will be the individual wishing to negative gear (i.e. the borrower)

Step 2 – Acquire the property

The trustee of the Land Tax Unit Trust enters a contract for sale of land. It is important that the trustee be able to prove that it paid for the property with funds of the trust. This is normally achieved by opening a bank account in the name of the trust and taking the deposit from that account.

NOTE: The trustee of the Land Tax Unit Trust must resolve to acquire the property on behalf of the trust before the exchange of the contract for its sale.

WARNING: The Land Tax Unit Trust must be executed before the trust conducts any business, including the exchange of contracts for the acquisition of real property.

Step 3 – Arrange the loan

Arrange the loan in the name of the person who wishes to claim the losses from the property. This is normally the high income earner. Other people including the trustee may act as guarantors for the loan.

NOTE: The financier will usually require a copy of the trust deed.

Step 4 – Issue additional ordinary units

Issue to the initial unitholder (i.e. the borrower) ordinary units equal to the cost of the property including stamp duty and legal fees. The units can be issued prior to settlement.

NOTE: The number of units in the unit trust on issue should equal the cost of the property plus stamp duty and legal fees.

Step 5 – Settle the property

Settle the property with the funds from the bank together with any other money to come from the unitholder.

NOTE: The name of the trustee should appear on the title certificate.

Step 6 – Administration

Depending on the nature of the property acquired and the amount of rental income to be received by the unit trust, the unit trust may require some or all of the following:

1. Registration for GST;
2. Application for a Tax File Number; and
3. The opening of bank accounts.

NOTE: The unit trust should have a tax file number and a bank account.

Other Important Information

1. The perpetuity period for trusts is dependent upon the proper law of the trust. In Queensland the perpetuity period is 125 years. In South Australia the perpetuity period has been abolished. In all other states it is 80 years;

2. A sole trustee of a unit trust may also be one if its unitholders, but not the only one;

3. The unitholders of a unit trust can unanimously call on its trustee to distribute the trust's income or capital to them;

4. Additional unitholders can be added at any time;

5. If a trust is acquiring real property, then the trust must have been in existence and evidenced in writing prior to the exchange of contracts for its purchase;

6. A unit trust is eligible to receive the general 50% Capital Gains Tax discount;

7. The trustee of a unit trust is obliged to distribute its income and capital to its unitholders in proportion to their respective unitholdings;
8. Distributions of the income of a trust to minors (i.e. people under 18 years of age) are generally taxed at the penal rate of 66%;

9. If the trustee of a trust is sued for an amount representing more than the available assets of the trust, they will generally become personally liable;

10. If a business is conducted through a trust, then its trustee should be a company;

11. If a trust is merely a passive investor in income-producing assets, its recommended that senior people from the group of people who will benefit under it are made its trustees;

12. There are taxation concessions when a superannuation fund invests in a unit trust (subject to certain restrictions).

NOTE: The above information is meant as a general guide only, and the information applies to NSW Unit Trust deeds provided by Macquarie Group Services.