What is a discretionary trust?

A discretionary trust (also known as a family trust) is a type of trust established during a person's lifetime. The trust may be established for asset protection, succession, or tax planning purposes.

Key terms

The key aspects of a discretionary trust are:

1. The trust terms – these are set out in the trust deed and specify the manner in which the trust is to be managed by the trustee.

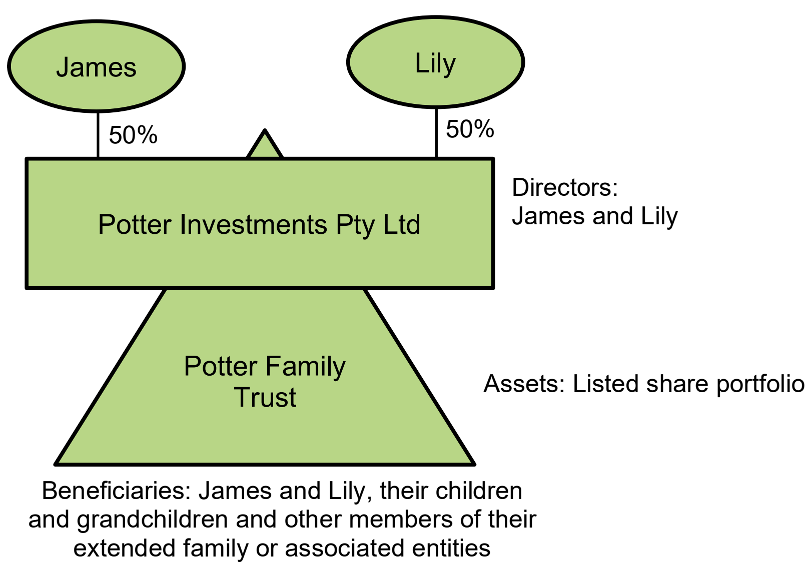
2. The trustee – this is the person (or people), or in some cases a company, responsible for the administration of the trust. The trustee makes decisions as to how the assets of the trust are invested and when and how the trust will distribute income or capital to the beneficiaries.

3. The beneficiaries – these are the people who are eligible to receive income or capital from the trust and are usually limited to the immediate family members of the person or family establishing the trust (such as a spouse, children and grandchildren).

Some trust deeds also nominate an 'appointor' of the trust, which is the person (or people) with the power to appoint and remove trustees.

Example

By way of example, a discretionary trust for a simple family group, with a corporate trustee could be structured as follows:



Benefits

Discretionary trusts can be used in a range of circumstances. The primary benefits of a discretionary trust (compared to owning assets in an individual's personal name) are:

1. The trustee can distribute income from the trust to a range of eligible family members each year, who are each taxed at their marginal tax rates on the income. This allows the income of the trust to be 'split' in a tax effective manner as the family's circumstances change over time.

2. Assets which are held in a discretionary trust are generally protected in the event an individual beneficiary becomes bankrupt. By contrast, any assets that a person holds directly in their personal name, would usually be made available to their creditors in the event of bankruptcy.

3. Family trusts can be an effective succession planning tool. For instance, control of a family trust can often be transferred to the next generation with no adverse tax or stamp duty costs, while transferring assets owned by an individual to their children during that individual's lifetime may give rise to significant tax and stamp duty consequences.

For more information about discretionary trusts, please contact Clover Law on 0400 503 111 or patrick@cloverlaw.com.au.