Partnerships and trusts

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Partnerships and trusts

What are partnerships?

For tax purposes, a partnership is an association of people who carry on business as partners, or who receive income jointly. Partners contribute their time, talents and/or capital towards the partnership and, in return, share in both the profits/losses and responsibilities.

Partnerships are not treated as a separate legal entity for tax purposes. Partnerships do not usually pay 'salary and wages' to partners. All income received by partners, from a partnership, is treated as business income and may attract provisional tax. The partners have to declare, and are assessed on, their share of the net profit of a partnership in their individual tax returns. They are entitled to deduct their share of a partnership loss in their individual tax returns. They then pay tax, taking that profit or loss into account, at their individual rates of tax.

Partnerships require a separate partnership tax file number and must lodge a partnership income tax return at the end of the financial year.

Any entitlement to profits or losses, other than in equal shares, should be documented in the partnership agreement. Net profits or losses from renting out co-owned property should generally be shared according to the respective legal interests of the owners in the property. Partners generally share in the income of the partnership and are liable for the debts of the partnership. If a partnership asset is sold, any capital gains or losses relating to a partner's share in the asset must be disclosed in the individual partner's tax return, and not in the partnership tax return.

Most partnerships are clients of the small business (SB) line. Partnerships with income of more than $10 million are clients of the large business and international (LB&I) line. Where partnerships have no business income, they are clients of the individuals non business (INB) line.

The partnership statistics in this chapter have been compiled from partnership tax returns for the 1998–99 income year that were processed before 11 November 2000.

Client population

In 1998–99, a total of 504 160 partnerships lodged returns in Australia. This was down from 573 741 in 1994–95.

The location of partnerships reflects the geographic distribution of the Australian population, with the higher numbers of partnerships being in states with larger populations. Approximately 31% of partnerships were in New South Wales, followed by 22% in both Victoria and Queensland.

Figure 10.1: Number of partnerships

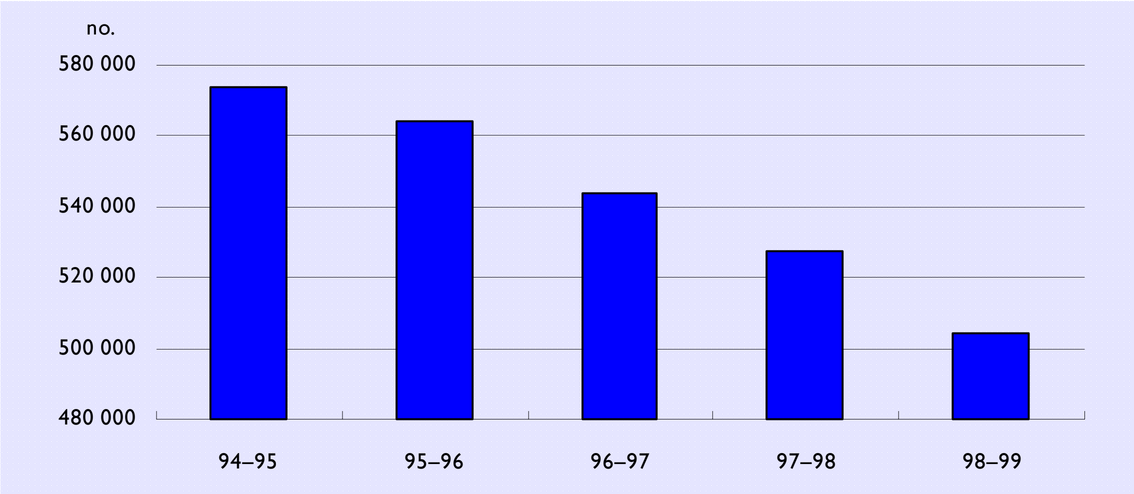
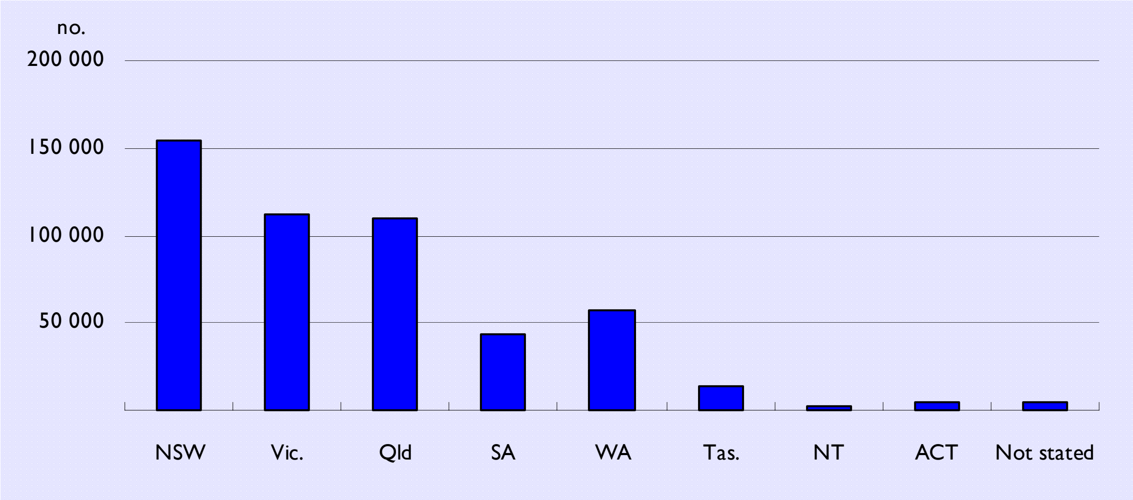


Figure 10.2: Partnerships by state



Industry

In 1998–99, of those partnerships where industry was stated, the largest proportion were in primary production (28%). This was followed by construction (16%) and retail trade (13%). Industry was not stated for 4% of total partnerships.

The type of industry varied according to the size of the partnership. For example, among partnerships that were clients of small business, the largest proportion (29%) were in primary production (see table 4.2). For partnerships that were clients of large business and international, the largest proportion (45%) were in finance, insurance, real estate and business services (see table 5.2).

The proportion of partnerships in each industry also varied according to their location. For example, the largest proportion of partnerships in the property and construction industries were in New South Wales. This result may have been influenced by the large amount of construction activity that was undertaken for the 2000 Olympic games.

Partnership income and expenses

In 1998–99, partnerships had a total business income of $105 billion. Most partnerships (91%) were clients of the small business line.

Table 10.1: Partnerships by industry

Industry[1]	Partnerships	
	no.	%
Primary production	134 603	27.7
Construction	77 396	15.9
Retail trade	64 990	13.4
Finance, insurance, real estate & business services	51 868	10.7
Property	38 717	8.0
Manufacturing	27 802	5.7
Transport & storage	24 385	5.0
Personal & other services	18 301	3.8
Accommodation, cafes & restaurants	15 055	3.1
Wholesale trade	12 141	2.5
Cultural & recreational services[2]	7 844	1.6
Health & community services	5 717	1.2
Communication	3 947	0.8
Education	1 917	0.4
Mining	931	0.2
Electricity, gas & water supply	342	0.1
Total industry stated	**485 956**	**100.0**
Industry not stated[3]	18 204	
Total	**504 160**	

1. The industry groups are coded using the Australian and New Zealand Standard Industrial Classification system. Prior to 1995–96, the Australian Standard Industrial Classification system was used. Therefore, it is not possible to do any long time series analyses for industry because the industry groups are not comparable.
2. Includes sports.
3. Includes partnerships that have registered a subsidiary return income from partnerships and trusts and registered under the government administration and defence code.

The total expenses claimed by all partnerships totalled $92 billion. The main type of expense was cost of sales, with 34% of all expenses linked to cost of sales. The second most common

Table 10.2: Income and expense items

Partnership		INB	SB	LB&I	Total
Partnerships	no.	42 873	461 145	142	504 160
Net rent	$'000	653 478	556 823	17 126	1 227 427
Gross interest	$'000	85 850	375 351	75 926	537 128
Gross dividends	$'000	22 190	110 497	26 623	159 310
Total Expenses	$'000	180	72 712 503	18 928 899	91 641 582
Net business income	$'000	63	9 363 408	3 254 183	12 617 654
Total business income	$'000	0	82 760 949	22 332 421	105 093 370

partnership expenses were depreciation (4%) and external labour costs (4%).

Between 1994–95 and 1998–99, the greatest increase in partnership expenses was for royalties (80%). This was followed by superannuation payments, which increased by 67% and other expenses, which increased by nearly 64%.

What are trusts?

A trust exists where a person, the 'trustee', is under an obligation to hold property for the benefit of other people, known as 'beneficiaries'. This obligation usually arises under the express terms of a trust, but may also be imposed by court order or declaration, or by the operation of law. Although the trustee holds the legal title to the property, they must deal with it in accordance with the terms of the trust for the benefit of the beneficiaries.

A beneficiary is a person for whom the property is held by the trustee or who falls within the class of persons who may benefit in respect of the trust property at the discretion of the trustee or another person. Beneficiaries can include public and charitable institutions, and the potential beneficiaries of a discretionary trust can include people not yet born.

A trust estate, for income tax purposes, includes the assets which are vested in, and under the control of, the trustee and are subject to the trust obligations. An annual return must be lodged for a trust, regardless of the amount of net income of the trust and even if the trust makes a loss for tax purposes.

A trust is not a separate taxable entity. As much as possible, beneficiaries who are entitled to income of the trust are assessed in relation to that income. The trustee is generally only assessed in respect of certain kinds of beneficiaries (such as non-residents and those under a legal disability) and where there is some part of the net income of the trust for tax purposes which is not assessable to a beneficiary. The net income of the trust is generally assessable to the trustee or the beneficiaries in the income year it is derived by the trust.

Most trusts are clients of small business. Trusts with income of more than $10 million are clients of large business and international, while trusts with no business income are generally clients of individuals and non-business.

Table 10.3: Partnership expenses

Expense	1994–95	1998–99	Change
	$m	$m	%
Cost of sales	31 611	30 986	-2.0
Total depreciation expenses	3 187	3 725	16.9
External labour	3 136	3 519	12.2
Interest	2 963	3 005	1.4
Rent	2 320	2 228	-4.0
Motor vehicles	2 360	2 153	-8.8
Repairs	1 802	1 939	7.6
Lease payments	638	807	26.5
Superannuation	288	482	67.4
Bad debts	113	115	1.8
Total royalty	81	146	80.2
Other expenses	25 964	42 541	63.8

Types of trusts

Fixed trusts: where people have vested and indefeasible interests in all of the income and capital of the trust at all times during the income year.

Hybrid trust: not a fixed trust, but one in which people might have vested and indefeasible interests in some of the income or capital of the trust during the income year.

Discretionary trusts: neither a fixed trust nor hybrid trust, but one in which people benefit from the income or capital of the trust during the income year at someone else's discretion (usually the trustee's).

Fixed unit trusts: a fixed trust in which interests in the income and capital of the trust are represented by units.

Public unit trusts: a fixed unit trust in which, at all times during the income year, more than 20 individuals hold vested and indefeasible interests, directly or indirectly, to at least 75% of the income of the trust, and more than 20 individuals hold vested and indefeasible interests, directly or indirectly, to at least 75% of the capital of the trust. An individual and his or her relatives and/or nominees are counted as a single individual for this purpose.

Public unit trusts—listed: a public unit trust in which any of its units were listed for quotation in the official list of a stock exchange in Australia or elsewhere during the income year.

Public unit trusts—unlisted: a public unit trust in which none of its units were listed for quotation in the official list of a stock exchange in Australia or elsewhere during the income year.

The trust statistics in this chapter have been compiled from trust tax returns for the 1998–99 income year, that were processed before 11 November 2000.

Client population

In 1998–99, a total of 455 841 trusts lodged returns in Australia, up from 363 198 in 1994–95.

The growth in trusts in recent years is likely to be related to the growth in the number of taxpayers who are seeking to hold and organise their assets and businesses in private discretionary trusts. Discretionary trusts enable the people who control the trust to achieve flexibility in relation to the distribution of income or assets of the trust.

The preference for a discretionary trust over a company structure or vice versa is dependent upon a range of factors including establishment and operating costs, the taxation treatment of income from companies compared with income from discretionary trusts, the capital gains tax treatment of shares compared with interest in a discretionary trust, and the relative level of the company tax rate.

In 1998–99, the greatest proportion of trusts were in Victoria (31%), followed by New South Wales (22%). The relatively high number of trusts in Victoria reflects the long-standing preference for using trusts for commercial activities, rather than other types of entities, in that state.

Industry

In 1998–99, of those trusts where industry was stated, the largest proportion was in the property industry (39%). This was followed by finance, insurance, real estate and business services (29%). Industry was not stated for 13% of trusts.

Figure 10.3: Number of trusts

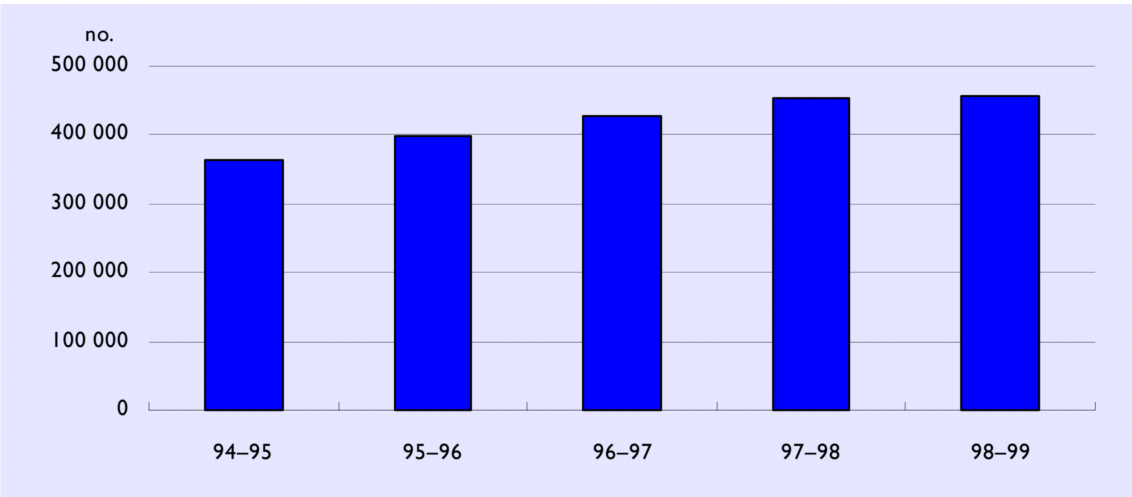


Figure 10.4: Trusts by state

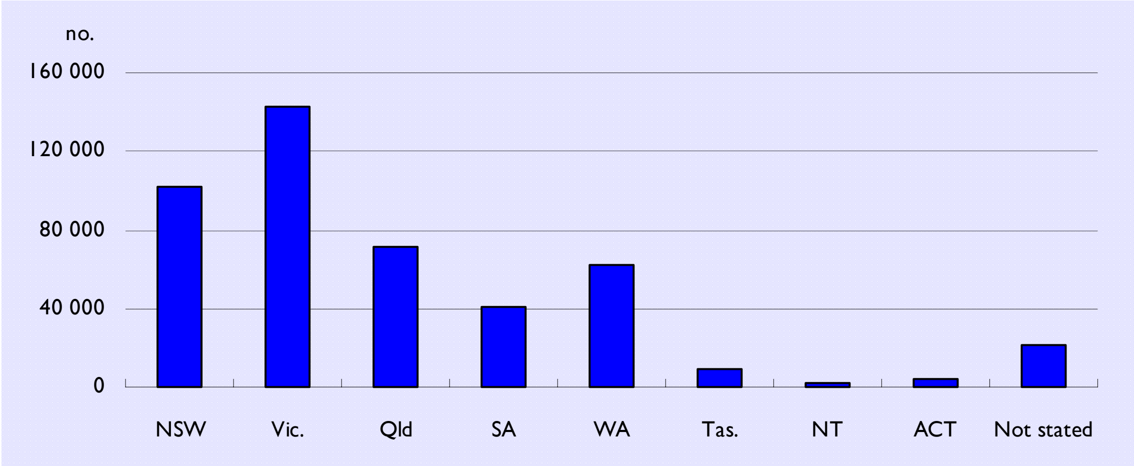


Table 10.4: Trusts by industry

Industry[1]	Number	Proportion[2]
	no.	%
Property	153 111	38.8
Finance, insurance, real estate & business services	115 383	29.2
Retail trade	25 572	6.5
Primary production	23 812	6.0
Construction	20 354	5.2
Manufacturing	12 644	3.2
Wholesale trade	8 651	2.2
Accommodation, cafes & restaurants	7 878	2.0
Health & community services	7 485	1.9
Transport & storage	7 613	1.9
Personal & other services	6 653	1.7
Cultural & recreational services[3]	3 012	0.8
Communication	1 008	0.3
Education	724	0.2
Mining	611	0.2
Electricity, gas & water supply	168	0.0
Total industry stated	**394 679**	**100.0**
Industry not stated[4]	61 162	
Total	**455 841**	

1. The industry groups are coded using the Australian and New Zealand Standard Industrial Classification system. Prior to 1995–96, the Australian Standard Industrial Classification system was used. Therefore, it is not possible to do any long time series analyses for industry because the industry groups are not comparable.
2. A proportion of 0.0% indicates a proportion of less than 0.05%.
3. Includes sports.
4. Includes trusts that have registered a subsidiary return income from partnerships and trusts and registered under the government administration and defence code.

Among trusts that were clients of small business, the greatest proportion (35%) were in finance, insurance, real estate and business services (see table 4.2). Similarly, for trusts that were clients of large business and international, 26% were in finance, insurance, real estate and business services and 26% were in the property industry (see table 5.2).

The proportion of trusts in each industry also varied according to their location. For example, the largest proportion of trusts in the mining industry (37%) were in Western Australia, reflecting the high incidence of mining activity in that state.

The growth of trusts and companies

In general, the rate of growth for trusts and companies has slowed over the last ten years. In 1998–99 the number of trusts increased by only half a per cent, and the number of companies increased by 2%.

The substantial drop in the growth rate of trusts is directly related to the government's August 1998 announcement (included in the new tax system proposals) of the intention to tax trusts like companies. Following this announcement new trust registrations fell significantly.

The overall increase in numbers over the past decade may reflect an increasing awareness of the advantages of incorporation and the use of companies as vehicles to obtain superannuation benefits for sole traders. Because the majority of trusts have a company as a trustee, the strong growth in trusts has contributed to increased numbers of trustee companies.

It may also reflect awareness of the different tax treatments for these entities. Companies have a flat rate of tax with no tax-free threshold, and

Table 10.5: Growth in the numbers of companies and trusts

Year	Companies		Trusts	
	no.	% growth	no.	% growth
1993–94	459 797	7.7	331 388	8.3
1994–95	494 967	7.6	363 198	9.6
1995–96	529 630	7.0	398 010	9.6
1996–97	559 520	5.6	427 431	7.4
1997–98	576 951	3.1	453 629	6.1
1998–99	589 624	2.2	455 841	0.5

trusts are untaxed on any net income of the trust to which beneficiaries are presently entitled. Shareholders of a company are assessable on any dividends that are paid or credited to them, subject to the operation of the imputation system. Beneficiaries are assessed on any net income related to the trust to which they are presently entitled.

Trust income and expenses

In 1998–99, trusts had a total business income of nearly $150 billion. The majority of trusts (73%) were clients of the small business line, while around 27% were clients of the individuals non business line. Less than 1% of trusts were clients of large business and international, which indicates that trusts were primarily used in small-scale operations, such as within a family structure. It is also more convenient for entities with total income greater than $10 million, to operate as companies rather than as trusts.

In 1998–99, the total expenses for trusts was $138 billion. The main type of expense for trusts was cost of sales—more than half (52%) of all trust expenses linked to cost of sales. This was followed by external labour costs, rent paid and interest paid (3% each). The main types of expenses did not vary significantly according to business line.

Between 1994–95 and 1998–99, the greatest increase in trust expenses was for royalties (162%). This was followed by superannuation payments (77%) and depreciation expenses (57%). Motor vehicle expenses experienced the smallest increase (24%).

Return form compilation

Partnership and trust return forms were lodged either electronically or in paper form. Copies of the forms are in the appendix. Statistics for most items shown on the return form are included in the tables.

Table 10.6: Income and expense items

Trust		INB	SB	LB&I	Total
Trusts	no.	121 900	333 289	652	455 841
Net rent	$'000	1 292 057	1 357 805	534 559	3 184 421
Gross interest	$'000	1 167 040	1 828 258	1 614 672	4 609 971
Gross dividends	$'000	861 746	1 576 293	828 361	3 266 399
Total expenses	$'000	173	126 937 301	11 247 450	138 184 924
Net business income	$'000	42	7 808 151	2 829 724	10 637 917
Total business income	$'000	0	135 054 003	14 138 141	149 192 144

Table 10.7: Trust expenses

Type of expense	1994–95	1998–99	Change
	$m	$m	%
Cost of sales	55 154	72 030	30.6
Depreciation expenses	1 954	3 064	56.8
External labour	3 654	4 732	29.5
Interest	2 409	3 514	45.9
Rent	2 547	3 636	42.8
Motor vehicles	1 232	1 527	23.9
Repairs	1 087	1 553	42.9
Lease payments	736	1 006	36.7
Superannuation	1 512	2 672	76.7
Bad debts	135	174	28.9
Royalty	97	254	161.9
Other	27 633	44 216	60.0

Detailed tables

The following detailed tables on partnerships and trusts can be found on the CD-ROM attached to this publication.

Partnerships

Table 1: All items by grade of net Australian income

Table 2: All items by industry

Table 3: Selected items by business line

Table 4: Selected items for income years 1989–90 to 1998–99

Trusts

Table 1: All items by grade of net Australian income

Table 2: All items by industry

Table 3: Selected items by business line

Table 4: Selected items for income years 1989–90 to 1998–99