CHILD MAINTENANCE TRUSTS

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The Australian Tax legislation provides that a Child Support Trust can be established following a family breakdown.

A family breakdown is defined as including legal obligations arising not only from the breakdown of live-in relationships but also where parentage has occurred outside of such a relationship.

Such a Trust is set up to provide support for a child (or children) where there is an obligation to provide support for the child and income that is distributed to the child (or physically to the Resident parent) is taken to satisfy that obligation.

Such a Trust allows Child Support payments to be made in a tax-effective manner.

The general tax-free threshold for children is $416.00, after which every additional non-employment income dollar (such as Trust distributions) is taxed at the top marginal rate of tax of 48.5%.

A Child Maintenance Trust which complies with Section 102AG of the Tax Act provides for “excepted trust income” to the minor which will only attract the normal adult tax rates, including the larger tax-free threshold (currently $6,000.00) as well as lower marginal tax rates. By way of example, for a maintenance paying parent who is on the top marginal tax rate to effect a Child Support payment of $15,000.00 per year without a Child Maintenance Trust would require approximately $29,000.00 (gross) per year, whereas with a Child Maintenance Trust would require approximately $17,000.00 (gross) per year, an annual saving of approximately $12,000.00.

Other benefits of such a Trust include:

- segregating cash or assets into a Trust separate from the parents, to provide ongoing support for the children;
- Trust assets are protected from external creditors;
- Income Tax saved by the Trust can accumulate within the Trust until the child reaches “vesting age”;
- The funds settled on the Trust can be borrowed, provided the capital is ultimately repaid and will benefit the children;
- The establishment of such a Trust requires the consent of both parents. It is most advantageous if the contributing parent is receiving a taxable income of at least $80,000.00 per year and has significant other assets;
- Where the children have a number of years of support prior to reaching 18 years;
- Where the parents are comfortable leaving some assets to the children at the vesting date;
- The initial property settled has a value of at least $200,000.00.

The Tax Office requires that the income must derive from the investment of property transferred beneficially to the child, i.e. the child will acquire it when the Trust ends. Accordingly, the parents who initially contributed the asset to the Trust cannot allow the asset to come back to them at a later date.

Child Support Trusts are not for everyone, but when used correctly can have significant financial benefits. Consideration of such a Trust requires careful financial, taxation and legal advice.