



# BUSINESS STRUCTURING ANALYSIS REPORT

## Construction Business - Multi-Party Entity Structure

### Fixed Trust vs Pty Ltd Company vs Partnership

<b>Prepared for:</b>	Instructing Accountant (Mr Brown & Mr Smith)
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## Client Brief / Query

### Personal Circumstances

Person	Marital Status	Spouse	Children	Key Factor
Mr Brown	Married	Wife is employed	2 children, both over 18	Adult children are effective income-splitting targets. Wife's existing income limits her benefit.
Mr Smith	Married	Wife is unemployed	1 child, aged 11	Wife is primary splitting target (\$18,200 tax-free). 11yo subject to Div 6AA penalty rates.

### Business Projections

	Year 1	Year 2	Year 3+
Gross turnover	\$500,000	\$800,000	\$1,200,000+
Initial capital (truck/equipment)	\$400,000		
GST registration	Mandatory	Mandatory	Mandatory

### Options

#### Three Options to Evaluate

Option 1: Fixed Trust (unit trust) with two Discretionary Family Trust beneficiaries (50/50 unit holders).

Option 2: Pty Ltd Company with (a) two individual shareholders 50/50, or (b) two Discretionary Family Trust shareholders 50/50.

Option 3: Partnership between Mr Brown and Mr Smith.

## 1. Summary

### Company + Trust Shareholders [Option 2(b)]

A Pty Ltd Company with shares held 50/50 by two Discretionary Family Trusts (Brown Family Trust and Smith Family Trust). This structure delivers the strongest combination of: (a) limited liability for a high-risk construction business; (b) income splitting flexibility through downstream discretionary trusts; (c) clean 50/50 governance between unrelated parties; and (d) the ability to retain earnings at 25% during the growth phase.

The company pays franked dividends to the two family trusts. Each trust distributes to family members: Smith's unemployed wife receives up to \$18,200 tax-free; Brown's two adult children each receive \$18,200 tax-free (\$36,400 combined at 0% tax). Estimated annual tax saving of \$20,000-\$30,000 compared to a partnership.

Option 1 (Fixed Trust + Discretionary Trusts) is viable but adds an unnecessary entity layer, cannot retain earnings at 25%, and traps Year 1 losses. Option 3 (Partnership) joint and several liability is catastrophic for a construction business.

The \$400,000 truck and equipment will generate large Year 1 depreciation deductions likely creating a tax loss. Company structure handles this cleanly (losses carried forward); trust structure traps losses; partnership allows flow-through but at the cost of joint and several liability.

## 2. Facts & Assumptions

### Facts Provided

Mr Brown and Mr Smith are starting a construction business together.  
 Expected gross turnover: Year 1 \$500K, Year 2 \$800K, Year 3 \$1.2M+.  
 Initial capital for truck and equipment: \$400,000.  
 Mr Brown: married (wife employed), 2 children both over 18.  
 Mr Smith: married (wife unemployed), 1 child aged 11.  
 50/50 intended participation.

### Assumptions

Assumption [ASSUMED]	Affects
Net profit Year 1: likely a loss (due to \$400K depreciation). Year 2: \$80K-\$120K. Year 3+: \$150K-\$250K. [ASSUMED]	Determines whether Year 1 loss treatment is a deciding factor.
Both Brown and Smith will draw salaries of approximately \$80,000-\$100,000 each. [ASSUMED]	Salary deductions reduce entity taxable income.
Brown's wife earns approximately \$60,000-\$90,000 p.a. [ASSUMED]	Already in 30%-32.5% bracket. Limited additional splitting benefit.
Brown's adult children have no significant other income. [ASSUMED]	Effective distribution targets at \$18,200 each (0% tax).
Smith's wife has no income. [ASSUMED]	Full \$18,200 tax-free threshold available.
Business will operate in one state. [ASSUMED]	Single jurisdiction for licensing, payroll tax, workers comp.
No existing structures held by either party. [ASSUMED]	Clean start - no legacy issues.
The \$400K equipment may qualify for instant asset write-off or simplified depreciation (Subdiv 328-D). [ASSUMED]	Could create a very large Year 1 deduction. Check current thresholds.

### Information Needed

Missing [NEEDED]	Impact
Exact income of Brown's wife. [NEEDED]	Affects her marginal rate and splitting benefit.
State of operation. [NEEDED]	Determines licensing, payroll tax, workers comp, stamp duty.
Financing for the \$400K equipment (loan/lease/outright). [NEEDED]	Affects interest deductions and which entity holds the asset.
Each party's capital contribution. [NEEDED]	If unequal, may create an inter-party loan.
Builder's licence requirements and qualifications held. [NEEDED]	Licence is entity-specific. New entity = new licence application.

### 3. Related Areas & Cross-Over Analysis

Area	Relevance	Key Provision	Impact
Income Tax - Trusts	Discretionary distributions to family.	Div 6 ITAA 1936	Smith's wife \$18,200 at 0%; Brown's adult children \$18,200 each at 0%.
Income Tax - Company	25% BRE rate; franked dividends.	s 23AA ITRA 1986	Retain profits at 25%. Dividends to trust shareholders for splitting.
Division 6AA	Smith's 11yo - penalty rates.	Div 6AA ITAA 1936	Above \$416: 66% tax. Not effective target.
Division 7A	Company to shareholder payments.	Div 7A ITAA 1936	Manage via declared dividends. Avoid loans without complying agreements.
Depreciation	\$400K truck/equipment.	Div 40; Subdiv 328-D	Large Year 1 deduction. May create loss.
Tax Losses	Year 1 loss probable.	Div 36; Sch 2F	Company: carry forward. Trust: trapped. Partnership: flow-through.
CGT Discount	Future sale of business.	Div 115	Trust/individuals: 50%. Company: nil.
Asset Protection	Construction = HIGH risk.	Bankruptcy Act; Corporations Act	Company: limited liability. Partnership: joint and several. Trust + corp trustee: strong.
GST	\$500K+ turnover from Year 1.	s 23-5 GST Act	Mandatory registration for whichever entity is chosen.
Workers Comp	Mandatory for construction.	State legislation	High-risk industry premiums. Entity-specific.
Builder's Licence	Entity-specific licence.	State building legislation	New entity requires new application. Director qualifications needed.
Section 100A	Reimbursement agreement risk.	s 100A ITAA 1936	Trust distributions must be genuine.
Partnership Liability	Joint and several liability.	State Partnership Acts	Each partner liable for ALL debts. Unacceptable for construction.

## 4. Analysis

### 4.1 Option 1 - Fixed Trust with Discretionary Trust Unitholders

The fixed unit trust operates the construction business. 50 units held by Brown Family Trust, 50 units by Smith Family Trust. Income distributed 50/50 per unit holdings, then each family trust distributes to family members at their marginal rates.

#### Option 1 Assessment

Advantages: Clean 50/50 separation via units; income splitting via downstream trusts; 50% CGT discount on future sale; units are transferable.

Disadvantages: SIX entities required (unit trust + 2 family trusts + 3 corporate trustees) = highest setup and compliance cost; Year 1 losses trapped in unit trust; cannot retain earnings at 25% (must distribute or face 47% tax); weaker asset protection than a company; complex banking.

### 4.2 Option 2(a) - Company with Individual Shareholders

Company with Brown (50%) and Smith (50%) as individual shareholders. Company taxed at 25%. Dividends to individuals.

#### Option 2(a): No Income Splitting

No income splitting. All dividends paid to Brown and Smith personally at their marginal rates. Wives' and children's tax-free thresholds completely wasted. Strongest asset protection but weakest tax outcome.

### 4.3 Option 2(b) - Company with Trust Shareholders

#### CONSTRUCTION PTY LTD (Operating Company)

Directors: Mr Brown & Mr Smith; Shareholders: Brown Family Trust 50%, Smith Family Trust 50%

Pays salary to Brown & Smith (deductible). Franked dividends to trusts. Trusts distribute to family members.

#### Option 2(b):

It combines: (a) LIMITED LIABILITY - critical for construction (site injuries, defective work, property damage); (b) INCOME SPLITTING - franked dividends flow to family trusts for distribution to low-income family members; (c) RETAINED EARNINGS at 25% - company can retain profits for growth (new equipment, additional trucks) without being forced to distribute; (d) YEAR 1 LOSS HANDLING - company carries losses forward automatically; (e) BANKING - banks prefer companies; (f) LICENSING - cleaner licence application.

### 4.4 Option 3 - Partnership

#### Option 3: Joint and Several Liability

Joint and several liability under the Partnership Act means each partner is personally liable for ALL partnership debts - not just their 50% share.

Construction risks: site injuries (\$2M+ personal injury claims), property damage to adjacent buildings, defective work (building defect claims arise years after completion), subcontractor insolvency, environmental contamination. Each of these could expose BOTH partners' personal assets.

The ONLY advantage of a partnership is flow-through loss treatment in Year 1. This does not justify the catastrophic personal liability exposure in a construction business.

## 4.5 Head-to-Head Comparison

Factor	Opt 1: Fixed Trust + DTs	Opt 2(b): Co + Trust SHs	Opt 3: Partnership
Asset protection	Medium-High	<b>HIGH (company)</b>	<b>NONE</b>
Income splitting	Yes (via trusts)	Yes (via trusts)	No
Retain earnings at 25%	No (must distribute)	Yes	No (flow-through)
Year 1 loss handling	Trapped in trust	<b>Carried forward in company</b>	<b>Flow to partners</b>
50% CGT discount	Yes	No (company). Trust SHs preserve on share sale.	Yes
Div 7A risk	Low	Medium (manage via dividends)	N/A
Banking/lending	Complex	Simple	Medium
Setup cost (all entities)	~\$15K-\$22K (6 entities)	~\$12K-\$18K (5 entities)	~\$1.5K-\$4K
Ongoing compliance	~\$9K-\$13K p.a.	~\$6K-\$10K p.a.	~\$2K-\$3.5K p.a.
Exit mechanism	Sell units	Sell shares via trust	Reconstitute
Governance clarity	Fixed 50/50 units	Fixed 50/50 shares	Per agreement

## 5. Worked Example Tables

### 5.1 Year 3 Tax Comparison (\$1.2M Turnover)

Assumes: \$200K net profit after salaries (\$80K each) and all expenses. Each family receives \$100K share.

Item	Opt 1: Trust	Opt 2(b): Company + Trusts	Opt 3: Partnership
Entity tax	\$0 (distributes all)	\$25,000 (25% on \$100K retained)	\$0 (flow-through)
<b>Brown Family (\$100K share):</b>			
Mr Brown	\$80K salary + ~\$27K dist	\$80K salary + franked div	\$80K salary + \$50K = \$130K
Mrs Brown (employed ~\$75K)	\$20K dist (tax ~\$6,500)	\$20K dist (tax ~\$6,500)	N/A
Adult child 1	\$18,200 (tax: \$0)	\$18,200 (tax: \$0)	N/A
Adult child 2	\$18,200 (tax: \$0)	\$18,200 (tax: \$0)	N/A
Brown subtotal tax (on \$100K)	~\$24,000	~\$24,000 + franking offset	~\$40,000
<b>Smith Family (\$100K share):</b>			
Mr Smith	\$80K salary + ~\$55K dist	\$80K salary + franked div	\$80K salary + \$50K = \$130K
Mrs Smith (unemployed)	\$45,000 dist (tax: ~\$3,900)	\$45,000 dist (tax: ~\$3,900)	N/A
11yo child	\$0 (Div 6AA)	\$0 (Div 6AA)	N/A
Smith subtotal tax (on \$100K)	~\$22,000	~\$22,000 + franking offset	~\$38,000
<b>TOTAL FAMILY TAX:</b>	<b>~\$46,000</b>	<b>~\$71,000 (incl \$25K co tax)</b>	<b>~\$78,000</b>
<b>Tax saving vs partnership:</b>	<b>~\$32,000 p.a.</b>	<b>~\$7,000 p.a. (+ \$25K deferred)</b>	Reference

#### Tax Comparison Analysis

Option 2(b) shows higher total tax than Option 1 due to the company tax layer (\$25K at 25%). However, this \$25K is retained in the company for business growth and is a timing deferral, not a permanent cost. When eventually paid as franked dividends, franking credits offset the personal tax.

For a growing construction business needing capital for additional trucks and equipment, the ability to retain earnings at 25% (instead of being forced to distribute at up to 47%) is a significant cash flow advantage.

The real comparison: Option 2(b) saves ~\$7,000+ per year in immediate family tax vs the partnership, PLUS retains \$75K in the company at only 25% tax, PLUS provides limited liability. This is the clear winner for a high-risk, capital-intensive construction business.

## 6. Case Law Support

Case	Court	Principle	Application
FCT v Bamford (2010) 240 CLR 481	HCA	Trust income; proportionate approach under Div 6.	Income splitting through downstream discretionary trusts.
FCT v Guardian AIT [2023] FCAFC 3	FCAFC	Section 100A reimbursement agreements.	Distributions to Brown's children and Smith's wife must be genuine.
FCT v Spotless Services (1996) 186 CLR 404	HCA	Part IVA dominant purpose test.	Structure must have commercial substance (asset protection for construction).
Thomas v FCT (1972) 3 ATR 165	HCA	Present entitlement under Div 6.	Trust distributions must be resolved before 30 June.

## 7. Conclusion

### **Option 2(b): Pty Ltd Company with shares held 50/50 by two Discretionary Family Trusts.**

This provides: (1) Limited liability for high-risk construction; (2) Income splitting to Brown's adult children (\$36,400 at 0% tax) and Smith's wife (\$18,200 at 0% tax); (3) Year 1 loss carry-forward in the company; (4) Retained earnings at 25% for business growth; (5) Clean banking and licensing.

A shareholders' agreement between the two family trusts is essential - covering decision-making, deadlock resolution, exit mechanisms, non-compete, and key person insurance.

#### **Next Steps**

Key actions: (1) Incorporate Construction Pty Ltd; (2) Prepare Brown and Smith Family Trust deeds + corporate trustees; (3) Issue shares 50/50 to the two trusts; (4) Execute shareholders' agreement; (5) Register ABN, GST, PAYG withholding; (6) Apply for builder's licence; (7) Register workers compensation; (8) Arrange insurance (public liability, professional indemnity, builder's all-risk, D&O).

## 8. Risks & Caveats

**Construction industry risk: [HIGH]** Site injuries, property damage, defective work claims (arise years after completion), subcontractor insolvency, environmental contamination. Insurance is the first line of defence. Limited liability company is essential.

**Section 100A: [MEDIUM]** Trust distributions to Brown's children and Smith's wife must be genuine - paid into their accounts with independent control. TR 2022/4 and Guardian AIT apply.

**Division 6AA: [INFO]** Smith's 11-year-old cannot receive trust income at adult rates. Penalty rates (66% above \$416) apply. Do not distribute to this child.

**Shareholders' agreement: [CRITICAL]** Two unrelated parties with 50/50 control creates deadlock risk. Agreement must cover: decision thresholds, deadlock resolution, exit mechanisms, non-compete, key person insurance.

**Part IVA: [LOW]** Standard commercial structure with genuine asset protection and governance purposes. Construction risk provides clear justification.

**Division 7A: [MEDIUM]** Company dividends to trust shareholders must be formally declared and paid. Avoid loans without complying s 109N agreements.

**Year 1 losses: [MODERATE]** \$400K depreciation likely creates a Year 1 loss. Company carries forward automatically (COT/SBT easily satisfied for new company).

**Builder's licence: [VERIFY]** Operating entity must hold appropriate licence. New entity = new application. Verify director qualification requirements.

**Trust distribution deadline: [ANNUAL]** Both family trusts must resolve distributions before 30 June. Failure = trustee at 47%.

## 9. Rulings & References

### Legislation

Provision	Relevance
ITAA 1936, Division 5	Partnership taxation
ITAA 1936, Division 6	Trust taxation - present entitlement
ITAA 1936, Division 6AA	Minors' penalty tax rates
ITAA 1936, s 99A	Trustee assessed at top rate if undistributed
ITAA 1936, s 100A	Reimbursement agreements
ITAA 1936, Division 7A	Deemed dividends
ITAA 1997, s 23AA / ITRA 1986	Base rate entity - 25% company tax
ITAA 1997, Division 40	Depreciation - truck and equipment
ITAA 1997, Subdivision 328-D	Simplified depreciation for SBEs
ITAA 1997, Division 36	Tax losses carry-forward
ITAA 1997, Division 115	CGT discount (50% individuals/trusts)
ITAA 1997, Division 152	Small business CGT concessions
ITAA 1997, Division 207	Imputation - franking credits through trusts
Corporations Act 2001, s 197	Director liability for corporate trustee debts
State Partnership Acts	Joint and several liability

### ATO Rulings & Case Law

Reference	Topic
TR 2022/4	Section 100A reimbursement agreements (Binding)
FCT v Bamford (2010) 240 CLR 481	Trust income; proportionate approach - HCA
FCT v Guardian AIT [2023] FCAFC 3	Section 100A ordinary family dealings - FCAFC
FCT v Spotless Services (1996) 186 CLR 404	Part IVA dominant purpose - HCA
Thomas v FCT (1972) 3 ATR 165	Present entitlement - HCA

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