The Tax Institute

Tax Update

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1. Cases

1.1 BBlood Enterprises – 100A and dividend stripping

Facts

The Blood Motor Group was a car dealership run by Brian Blood and his two business partners, Sean Blood and Darron Muir.

The Brian Blood Group consists of a series of companies that are wholly owned by a combination of Brian, his wife Fiona Blood and other members of Brian's family group. The Brian Blood Group also includes various trusts where Brian, Fiona and other members of Brian's family are discretionary beneficiaries.

The Brian Blood Group included Illuka Park Pty Ltd (**IP Co**), BBlood Enterprises Pty Ltd and B&F Investments Pty Ltd. Fiona was the sole director of IP Co and B&F Investments. Brian was the secretary for each of these companies. Fiona was also the sole director and secretary of BBlood Enterprises.

A trust in the group, the B&F Investments Trust, owned 40% of the shares in one of the head companies of the four tax consolidated groups that comprised the Blood Motor Group. Prior to 2015, the B&F Investments Trust received significant franked dividends income over time. The B&F Investments Trust had distributed most of its income to IP Co. As a result, IP Co had retained earnings of $7,421,722.

The Illuka Park Trust (**IP Trust**) was a discretionary trust established by a deed of settlement dated 15 February 2010 (**IP Trust Deed**). B&F Investments was the trustee of the IP Trust (**IP Trustee**). Until 31 March 2014, the property of the IP Trust was limited to $10 of cash on hand. It had not previously received any income.

IP Co was a 'General Beneficiary' of the B&F Investments Trust. IP Co was owned 99% by the IP Trustee and 1% by Fiona.

Fiona and Brian were 'Primary Beneficiaries' of the IP Trust. As Primary Beneficiaries, Fiona and Brian were also 'General Beneficiaries' in addition to any corporation of which either of them was a member or director.

Brian had received and had heavily relied on the advice of Fordham Business Advisors Pty Ltd (**Fordham**) since 1999.

On 25 March 2014 BBlood Enterprises Pty Ltd (**BBlood Enterprises**) was incorporated to be a new corporate beneficiary for the group.

<u>The Illuka Park Steps</u>

In or around 2013, Brian received advice from Fordham regarding a transaction involving a share buy-back. The transaction involved six steps that were actioned over a period of three-months involving members in of the Brian Blood Group as follows:

Step 1:

The B&F Investments Trust paid an interim distribution for its income of the year on at 31 March 2014 to the IP Trust, as to $123,238, and IP Co, as to $2,999,497. The entitlement owing to IP Co remained unpaid.

Step 2:

IP Co paid franked dividends to the IP Trust on 31 March 2014 ($121,739) and 30 April 2014 ($59,400) such that, with the income the IP Trust received from the B&F Investments Trust, the IP Trust had income of $304,377 for the year ended 30 June 2014.

Step 3:

The IP Trust Deed was varied so that the definition of income was changed from net income under section 95 of the ITAA 1936 (i.e. tax law income) to income to be determined by the trustee in accordance with ordinary concepts.

During the audit by the Commissioner, Mr Buckley, the long-term accountant for the group described the variation as intended to effect a 'standard ‘post Bamford’ amendment' and denied that it was part of the buy-back that occurred later.

Step 4:

On or about 25 June 2014 IP Co bought back all of the shares held by the IP Trust in IP Co pursuant to a share buy-back agreement. The statement of material information under sections 257D(2) and 257G of the *Corporations Act 2001* dated 10 June 2014 for the share buy-back included the following:

> *3. Reasons for the Buy-Back*
>
> *The reasons for the share buy-back is to simplify the share capital structure of the Company [IP Co] by having an individual own the shares rather than the trustee of a discretionary trust. This will enable more simple estate planning measures to be put in place.*

IP Co debited $99 of the purchase price to its share capital account and the remaining $10,189,770 to retained earnings. This gave rise to a deemed dividend in accordance with section 159GZZZP of ITAA 1936 (**Share Buy-Back Dividend**).

Step 5:

IP Co allocated a franking credit of $4,367,002 to the Share Buy-Back Dividend.

Step 6:

The IP Trustee distributed all of the IP Trust's income for the year ended 30 June 2014 to BBlood Enterprises. The income (according to the deed, being income according to ordinary concepts) distributed by the IP Trustee to BBlood Enterprises totalled $304,377. The amount remained unpaid.

While the proceeds of the Share Buy-Back were deemed to be a dividend for tax purposes, because of the effect of the Deed of Variation, the Share Buy-Back Dividend was not income of IP Trust for the year as it was a receipt of capital and not trust income under ordinary concepts.

As BBlood Enterprises was made presently entitled to the whole of the income of the IP Trust for the year, BBlood Enterprises was assessed on the IP Trust's tax law income, including the Share Buy-Back Dividend under section 97 of ITAA 1936. However, BBlood Enterprises paid no additional tax because the Share Buy-Back Dividend was fully franked and the tax payable on the Share Buy-Back Dividend was wholly offset by the franking credit.

The IP Trust retained the amount of the Share Buy-Back Dividend as corpus of the trust. However, it was not liable to pay tax under section 99A of the ITAA 1936 in respect of the Share Buy-Back Dividend, because it was not 'income' of the trust to which no beneficiary was presently entitled.

The following flow chart sets out the transactions:

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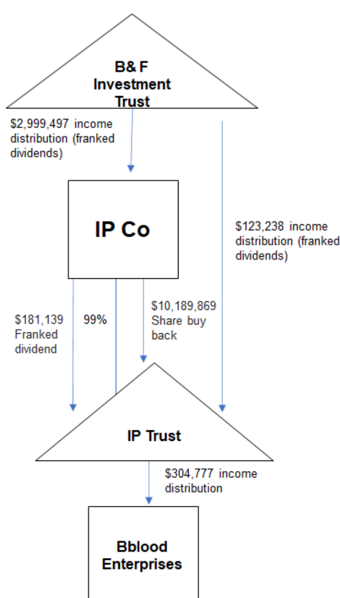

All of the legal documents for the Illuka Park Steps were prepared by the law firm Maddocks.

Assessments

The Commissioner issued an assessment to the IP Trustee dated 11 August 2020 (**IP Assessment**). Under the IP Assessment, the IP Trustee was liable for tax in respect of the relevant trust income. The Commissioner issued the assessment on the basis that section 100A of the ITAA 1936 applied because:

1. the Iluka Park Steps constituted an agreement, arrangement or understanding;
2. the agreement, arrangement or understanding was not entered into in the course of an ordinary family or commercial dealing;
3. a 'reimbursement agreement' for the purposes of section 100A does not require that the 'payment' referred to in section 100A(7) be in the form of a reimbursement;
4. within the terms of section 100A(8) and (9), the arrangement was entered into for the purpose of securing that a person would be liable to pay no tax or less tax than if the arrangement had not occurred; and
5. BBlood Enterprises' present entitlement arose due to a reimbursement agreement within the meaning of section 100A.

Accordingly, the Commissioner concluded that the IP Trustee was assessed on whole of the net income of the IP Trust for the year under section 99A of the ITAA 1936.

In raising the assessment the Commissioner considered that section 207-35 of the ITAA 1997 applied to include both the amount of the Share Buy-Back Dividend and the franking credit on that amount in the income of the IP Trustee for the year. Section 207-35 of the ITAA 1997 relevantly provides as follows:

> *(5) Subsection (6) applies if:*
>
> *(a) a *franked distribution is made, or *flows indirectly, to the trustee of a trust in an income year; and*
>
> *(b) the assessable income of the trust for that year includes an amount (the franking credit amount) that is all or a part of the additional amount of assessable income included under subsection (1) in relation to the distribution; and*
>
> *(c) disregarding Division 6E of Part III of the Income Tax Assessment Act 1936, the trustee of the trust is liable to be assessed (and pay tax) in respect of an amount (the assessable amount) under section 98, 99 or 99A of that Act in relation to the trust.*

(6) Despite any provisions in Division 6 of Part III of the Income Tax Assessment Act 1936, for the purposes of that Division, increase the assessable amount ***by so much of the franking credit amount as is equal to:***

(a) ... [not presently relevant] ...

(b) if the trustee of the trust is liable to be assessed (and pay tax) under section 99 or 99A of that Act—the sum of:

(i) the trustee's share of the franking credit on the distribution; and

(ii) the amount mentioned in section 207-37. [This is the amount of the Share Buy-Back Dividend],

On this point, the IP Trustee contended that the lead in words emphasised above meant that the amount assessed under section 207-35 was limited to the franking credit amount, that is, the amount of the Share Buy Back Dividend was not assessable. Ultimately, in court, the IP Trustee conceded this was a drafting error in the law.

In addition to disagreeing with the Commissioner on the application of section 100A of the ITAA 1936 and section 207-35 of the ITAA 1997, the IP Trustee argued that the IP Assessment was an amended assessment as the ATO had previously assessed the IP Trustee by inserting an entry into the ATO portal that indicated that the IP Trustee had been assessed for the year ended 30 June 2014. That entry indicated that no tax was payable by the IP Trustee. Accordingly, the IP Assessment was excessive as it was issued outside of the limited amendment period under section 170(1) of the ITAA 1936 and the Commissioner was otherwise not authorised to issue it.

The Commissioner considered that the entry on the ATO portal was not an 'assessment' within the meaning of section 170(1) of the ITAA 1936 and that, in any event, the Commissioner can always issue an assessment in relation to a reimbursement agreement under section 100A in accordance with section 170(10) of the ITAA 1936.

The IP Trustee argued that the decision in *Metlife Insurance Ltd v Federal Commissioner of Taxation* [2008] FCAFC 167, concerning the power of the Commissioner to amend an assessment under section 170(10AA) of the ITAA 1936 to give effect to the disposal of an asset on settlement but with the CGT event happening at the of contract, meant that the Commissioner would not rely on section 170(10) of the ITAA 1936. *Metlife* indicated that the power to amend in section 170(10AA) required a change in circumstances (i.e. the settlement of the sale of the property) following the assessment and was not a power to amend at any time. The IP Trustee contended that there was no change in circumstances here.

The Commissioner also issued an alternative amended assessment to BBlood Enterprises dated 15 August 2019 (**BE Assessment**)**.** The BE Assessment was issued on the basis that BBlood Enterprises was not entitled to claim a tax offset for the franking credits under section 207-150(1) of the ITAA 1997. The Commissioner contended that this was because the Deemed Share Buy-Back Dividend was made a part of a dividend stripping operation in accordance with section 207-155 of the ITAA 1997.

Issues

1. Was the Commissioner authorised to issue the IP Assessment to the IP Trustee?
2. Did section 100A of the ITAA 1936 apply so that BBlood Enterprises was not presently entitled to some or all of the income of the IP Trust for the income year ended 30 June 2014?
3. If section 100A applied, did section 207-35(6) of the ITAA 1997 increase the tax liability of the IP Trustee under section 99A of the ITAA 1936?
4. Was the deemed dividend component of the share buy-back purchase price paid to the IP Trustee a distribution 'made as part of a dividend stripping operation' as defined in section 207-155 of the ITAA 1997?

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Decision

The IP Assessment

Thawley J found that the IP Assessment issued to the IP was an original assessment and was not an amended assessment. His Honour noted that, for section 170(1) of the ITAA 1936 to apply, the Commissioner must have previously served an assessment on the taxpayer. The mere insertion of an entry onto the tax portal was not the 'service' of an assessment and, accordingly, as the IP Assessment was an original assessment, section 170 of the ITAA 1936 did not apply to prevent the Commissioner from issuing the IP Assessment.

Thawley J noted that it was, therefore, unnecessary to consider whether section 170(10) of the ITAA 1936 authorised the Commissioner to amend the assessment.

Section 100A of the ITAA 1936

Thawley J noted that the effect of the Illuka Park Steps was as follows:

1. IP Co transferred its retained earnings to the IP Trust;
2. for trust purposes, the IP Trust received ordinary income of $304,376 and capital of $10,189,770;
3. for tax purposes, BBlood Enterprises was assessed on whole of the net income of the IP Trust, including both the ordinary income ($304,376) and the Share Buy-Back Dividend ($10,189,671) but was only entitled to the ordinary income. No further tax was paid on the Share Buy-Back Dividend as BBlood Enteprises was entitled to a franking credit which wholly offset the tax payable on that portion;
4. the amount of the Share Buy-Back Dividend was retained in the IP Trust as corpus of the trust and the IP Trustee was not assessed on it under s 99A of the ITAA 1936.

Thawley J considered section 100A of the ITAA 1936 as follows:

1. *Agreement* - there was an 'agreement' within the meaning of section 100A as there was an agreement to enter into a series of connected transactions or steps, being the Illuka Park Steps. Thawley J did reject the Commissioner's arguments that the initiation and planning of the agreement comprised part of the agreement;

2. *Ordinary family or commercial dealing* - Thawley J held that the arrangement was not in the course of an ordinary family or commercial dealing. In this respect his Honour noted that it is not a question of whether each individual step may be an ordinary family or commercial dealing but whether the agreement as a whole was entered into in an ordinary family or commercial dealing. Thawley J accepted that analysing individuals steps was still relevant for the overarching consideration.

   Thawley J noted that a dealing may not be an ordinary family or commercial dealing if it is 'contrived or artificial or involved more than was required to achieve the relevant objective' although the mere fact it is complex will not, in and of itself, mean that it is not an ordinary family or commercial dealing.

   Thawley J noted that a lack of commercial motivation or commercial justification is relevant to ascertaining whether it is an ordinary family or commercial dealing.

   In this case, Thawley J considered that there was no commercial justification for the arrangement, with his Honour noting, for example, that it was not explicable on the basis of family succession.

   Thawley J noted that a distribution of $300,000 and a share buy-back, on their own, may be ordinary family or commercial dealings but that the arrangement needed to be viewed as a whole. However, even if the transactions were looked at in isolation, there was a lack of sensible family or commercial rationale.

3. *No 'reimbursement'* - Thawley J rejected the contention that a 'reimbursement agreement' for section 100A required there to be a 'reimbursement' of some form;

4. *Tax avoidance purpose* - Thawley J considered that the agreement was for a tax avoidance purpose as the distribution of IP Co's retained earnings through the Share Buy-Back was done to achieve a mismatch between the trust income and the net income of the IP Trust so that the retained earnings of IP Co would not be subject to further tax. Thawley J did not accept that, in determining whether there was a

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tax avoidance purpose, it was necessary to identify a counter-factual or alternative postulate (being a hypothetical transaction to compare the actual transaction against) as was necessary under Part IVA;

5. *Connection between present entitlement and reimbursement agreement* - Thawley J noted that section 100A requires a 'but for test' in that the present entitlement must arise out of the reimbursement agreement. Thawley J rejected an argument by the IP Trustee that this requirement involves an assessment as to what the trustee would have been reasonably expected to do but for the reimbursement agreement. Thawley J held that this was not the correct approach, and the question was simply whether the present entitlement arose out of the agreement comprising the Illuka Park Steps, or arose by reason of an act, transaction or circumstance that occurred in connection with, or as a result of, that agreement.

The tax liability of the IP Trustee

Thawley J held that the IP Trustee was taxable to the extent to which the Commissioner determined. Because section 100A applied to BBlood Enterprises' present entitlement to income of the IP Trust, section 207-35(5) was satisfied and section 207-35(6) applied to the present case.

Thawley J rejected the IP Trustee's argument that the Share Buy-Back Dividend was not assessable to the trustee as not being supported by the statutory context and considered that there had clearly been an erroring the drafting of section 207-35(6) of the ITAA 1997 and considered it necessary to read the provision as not including the words '*so much of the franking credit amount as is equal to'.*

Accordingly, section 207-35(6) increased the IP Trustee's liability under section 99A by an amount equivalent to the value of the Share Buy-Back Dividend and the whole of the franking credit.

Dividend stripping

The alternative BE Assessment would apply if the Commissioner was unsuccessful in its case regarding the application of 100A. The Court also found that the deemed dividend was part of a 'dividend stripping operation' as defined by section 207-155 of the ITAA 1997. Accordingly, in the event that section 100A did not apply, section 207-150 of the ITAA 1997 applied.

COMMENT – this case is presumably the reason why the ATO guidance on section 100A indicated that a 'red zone' arrangement would be one where the trustee amends a trust deed to allow it to determine what income of the trust is so as to retain funds in a trust.

Citation *BBlood Enterprises Pty Ltd v Commissioner of Taxation* [2022] FCA 1112 (Thawley J, Melbourne)
w https://www.austlii.edu.au/cgi-bin/sinodisp/au/cases/cth/FCA/2022/1112.html

1.2 Minerva – Part IVA and stapled structures

Facts

Minerva Financial Group Pty Ltd (**MFG**) is a member of a group of companies and trusts which carries on the financial services business known as the Liberty group.

Liberty obtains capital through a process called 'securitisation', which involves the pooling of loan receivables and related securities (typically mortgages) into securitisation trusts, in order to fund loans that it arranges for its customers.

For securitisation trusts established prior to 2008, Liberty Financial Pty Ltd (**Liberty Financial**) was the holder of residual income units (**RIUs**) and residual capital units (**RCUs**). The RIUs entitled Liberty Financial to the balance of the income of the securitisation trusts after payment of interest and fees as well as the recoupment

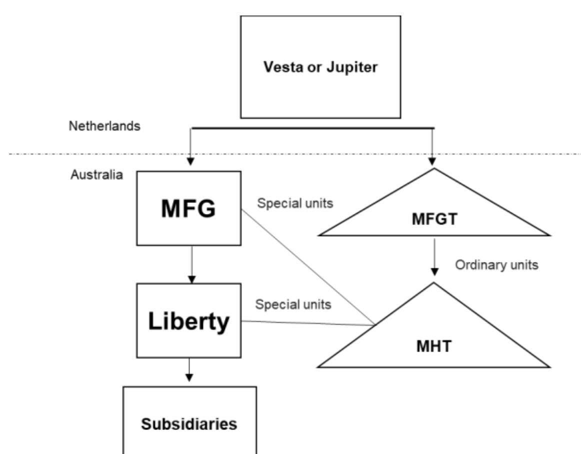
of any losses. The RCUs entitled Liberty Financial to the balance of the capital of the securitisation trust after payment of the principal.

In 2007-2008, Liberty was planning to conduct an initial public offering (**IPO**). In anticipation of the IPO, Liberty restructured so that the Liberty group parent company, Jupiter Holdings NV (incorporated in the Netherlands and later replaced by Vesta Holdings BV) owned interests in two 'silos' of Australian entities as follows:

1. a corporate silo and income tax consolidated group, comprising MFG, its wholly owned subsidiary Liberty Financial and Liberty Financials' wholly owned subsidiaries; and
2. a trust silo, comprising Minerva Financial Group Trust which held all the units in the Minerva Holding Trust.

As part of the restructure, Liberty Financial and Secure Credit Pty Ltd (**Secure Credit**) held 'special units' in the Minerva Holding Trust. MFG, as the trustee, had the discretion to distribute the Minerva Holding Trust's distributable income to the special unitholders. However, in each of the income years ended 30 June 2012 to 30 June 2015, the trustee chose not to exercise its discretion to make any (or any substantial) distribution to the special unitholders. The trustee of the Minerva Financial Group Trust, as the holder of the RIUs, was, therefore, entitled to the majority of the distributable income for each year.

The structure is depicted as follows:



The effect of the income flowing through the trust silo to the non-resident owners (Jupiter or Vesta) was that the income was subject to 10% withholding tax (as it was interest income), as opposed to the 30% corporate tax rate that would have applied had it continued to have been derived in the corporate silo. The Minerva Holding Trust lent the funds to Liberty Financial via interest free, undocumented loans. The unpaid present entitlements owing to Minerva Financial Group Trust and Jupiter or Vesta were not settled by cash payment.

The intention was that new securitisation trusts would be established within the trust silo under the Minerva Holding Trust, instead of under the operating company Liberty Financial, which had been the case in the past.

The anticipated IPO did not proceed.

On 23 November 2016 and 11 January 2017, the Commissioner made determinations under Part IVA to cancel the tax benefits obtained in connection with three alleged schemes by including in MFG's assessable income in the tax years ended 30 June 2012 to 30 June 2015, an amount equal to the omitted income in each year, being:

1. 2012 financial year: $24,836,839 and $806,104;
2. 2013 financial year: $31,761,081 and $3,138,723;
3. 2014 financial year: $46,048,587 and $7,875,741; and
4. 2015 financial year: $53,649,735 and $5,341,506.

Notices of amended assessments were issued by the Commissioner to give effect to the determinations.

On 27 January 2017, MFG objected to the amended assessments, including the Commissioner's decision not to remit the shortfall interest charge in each of the relevant years.

On 14 May 2020, the Commissioner disallowed MFG's objections to the amended assessments and also upheld the decision not to remit the shortfall interest charge for the 2012 financial year. Due to section 280-170 of Schedule 1 to the TAA, MFG did not have the right to object to the decision not to remit the shortfall interest charge for the 2013, 2015 and 2015 financial years. Under that section an objection can only be made against a decision not to remit the shortfall interest charge if the amount not remitted is more than 20% of the additional tax due.

On 6 July 2020, MFG appealed the objection decision made by the Commissioner to the Federal Court of Australia.

First alleged scheme

The first alleged scheme was the following steps:

1. establishing the trust silo;
2. nominating Minerva Holding Trust as the RIU holder of the securitisation trusts established from 2009; and
3. directing income from the securitisation trusts through Minerva Holding Trust.

The Commissioner argued that, had the first alleged scheme not been carried out, it would have been reasonable to expect that Liberty Financial would have been nominated as the RIU holder of each Minerva Holding Trust securitisation trust. Further, Minerva Holding Trust would not have lent funds to Liberty Financial that it obtained as the RIU holder of the Minerva Holding Trust securitisation trusts because Liberty Financial would have been entitled to receive those funds directly. Accordingly, the Commissioner argued that MFG as the head company of the income tax consolidated group, would have continued to derive the residual income from the securitisation trusts.

Second alleged scheme

The second alleged scheme was the following:

1. transferring ownership of the units in Minerva Financial Group Trust from MFG to Jupiter Holdings NV in December 2007;
2. the failure of MFG to distribute greater than nominal amounts of Minerva Holding Trust's distributable income to the special unitholders in Minerva Holding Trust (Liberty Financial and Secure Credit); and
3. the trustee of the Minerva Holding Trust lending money to Liberty Financial.

The Commissioner argued that had the second alleged scheme not been carried out, MFG acting as the trustee of Minerva Holding Trust would have exercised its discretion to distribute all or substantially all of the distributable income of Minerva Holding Trust to Liberty Financial and Secure Credit as the special unitholders of Minerva Holding Trust (which were the companies in the MFG tax consolidated group) in the years ended 30 June 2012 to 30 June 2015.

Third alleged scheme

The third alleged scheme was the failure of MFG as trustee of Minerva Holding Trust, to distribute greater than nominal amounts of Minerva Holding Trust's distributable income to the corporate silo through the special unitholders, Liberty Financial and Secure Credit and lending money to Liberty Financial.

MFG did not dispute that it obtained a tax benefit in connection with the alleged schemes. However, MFG contended that obtaining a tax benefit was not the dominant purpose of any of the schemes. MFG stated that the decision to separate the newly formed securitisation trusts from the operating assets of the business was to optimise the Liberty group's capital structure and improve access to funding, including by way of an IPO. MFG

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had received consistent professional advice recommending an IPO of stapled securities, consisting of a unit in a trust holding the passive financial assets and a share in a company holding the operating assets.

Whether the dominant purpose of each scheme was to obtain a tax benefit is to be evaluated according to the eight factors set out in section 177D(2)(b) of the ITAA 1936:

(i) the manner in which the scheme was entered into or carried out;

(ii) the form and substance of the scheme;

(iii) the time at which the scheme was entered into and the length of the period during which the scheme was carried out;

(iv) the result in relation to the operation of this Act that, but for this Part, would be achieved by the scheme;

(v) any change in the financial position of the relevant taxpayer that has resulted, will result, or may reasonably be expected to result, from the scheme;

(vi) any change in the financial position of any person who has, or has had, any connection (whether of a business, family or other nature) with the relevant taxpayer, being a change that has resulted, will result or may reasonably be expected to result, from the scheme;

(vii) any other consequence for the relevant taxpayer, or for any person referred to in subparagraph (vi), of the scheme having been entered into or carried out; and

(viii) the nature of any connection (whether of a business, family or other nature) between the relevant taxpayer and any person referred to in subparagraph (vi)

Issue

Was the dominant purpose of each scheme to enable MFG to obtain a tax benefit?

Decision

O'Callaghan J considered the three schemes separately, with each scheme being evaluated according to the factors set out in section 177D(2) of the ITAA 1936.

First Scheme

O'Callaghan J held that a reasonable person would not conclude that MFG entered into or carried out the first scheme for the dominant purpose of enabling it to obtain a tax benefit in connection with the scheme. The basis of this finding was that there were commercial factors driving the structure and the structure was consistent with advice that MFG received being that the structure was preferable in order to implement an IPO.

O'Callaghan J disregarded the evidence of the ATO's expert on the commerciality of the stapled structure as the ATO's expert acknowledged that he had never been involved in an IPO.

Second Scheme

O'Callaghan J held that a reasonable person would conclude that MFG entered into or carried out the second scheme for the dominant purpose of enabling it to obtain a tax benefit in connection with the scheme. The basis of his Honour's decision was that MFG was unable to proffer any commercial reasons as to why almost all of the income derived by Minerva Holding Trust was distributed to the non-resident unitholders instead of the resident special unit holders. His Honour stated as follows:

The applicant was unable to provide any cogent reason, other than the tax benefit, why the decision was taken in each of the relevant years to direct no more than 2% of MHT's net income to the special unitholders. The applicant submitted that neither LF nor Secure Credit had an 'entitlement' to the income from the RIUs and that the power of the trustee of MHT to distribute income to the special unitholders was discretionary. So much, unsurprisingly, was accepted by the Commissioner. But neither factor goes to the relevant question of dominant purpose, objectively viewed.

O'Callaghan J concluded that the manner in which the scheme was entered into or carried out and the time at which it was carried out were the key factors that led to the finding that the dominant purpose of the scheme was obtaining the tax benefit.

Third Scheme

As with the conclusions for the Second Scheme and given the similarities between the Second Scheme and the Third Scheme, his Honour held that a reasonable person would conclude that MFG entered into or carried out the Third Scheme for the dominant purpose of enabling it to obtain a tax benefit in connection with the scheme.

COMMENT – while the arrangement in this case was complex, fundamentally the trustee of MHT decided not to distribute to particular beneficiaries so as to reduce tax in Australia, and Part IVA was held to apply. There is little distinction between this case and choosing to distribute to a low income spouse to support a family, in circumstances where the ATO have indicated they will not apply section 100A.

Citation *Minerva Financial Group Pty Ltd v Commissioner of Taxation* [2022] FCA 1092 (O'Callaghan J, Melbourne)
w http://www.austlii.edu.au/cgi-bin/viewdoc/au/cases/cth/FCA/2022/1092.html

1.3 Oxby – conspiracy theorist tax advice

Facts

Steven Oxby had a good history of tax compliance and lodged his tax returns through an accountant up until the income year ended 30 June 2018.

In August 2019, Steven attended a two-day seminar about historic and constitutional law. According to Steven, the seminar stated that taxation is not compulsory and that all living expenses are tax deductible based on a theory that 'we first must sustain ourselves in order to produce labour from which we can gain an income'.

On 6 February 2020, Steven lodged his income tax return which included a total deduction of $74,502 for 'Other Work-Related Expenses'. Steven is in his fifties and previously worked as an equipment manager for an ophthalmic company. At the time this case was being heard, he was not working and was trying to set up a gardening business. The costs comprising the work-related expenses claim included rent, house and health insurance, clothing, recreational activities, home and car maintenance, food, phone bills, dependent costs, and utility bills such as gas, electricity and water.

Steven also lodged an affidavit dated 4 February 2020 with his tax return. The affidavit referred to the work-related expenses deduction, stating:

15. The amount of $74,501.72 disclosed at "Other work-related expenses" within page 4 of the Tax return is an amount spent as living costs in sustaining the life of the principal creditor and living soul answering to the name "Steven Russell Oxby".

16. The sum of $72,710.00 with held was derived from the productivity of the labour of the living soul answering to the name "Steven Russell Oxby", being property of the living soul and is to be immediately remitted to the living soul.

17. Productivity of labour is not taxable and is omitted from the Tax Acts definition of the word "Income".

Steven was assisted in preparing his tax return and the accompanying affidavit by a person from the organisation that presented the seminar, whom Steven knew was not a qualified tax agent. When asked why Steven did not seek assistance from his accountant, Steven stated that 'presenting my tax return as a sovereign, natural-born man – as opposed to a commercial entity – he [the accountant] wouldn't understand that'.

The Commissioner conducted an audit of the 'Other Work-Related Expenses' claimed by Steven. The Commissioner wrote to Steven via SMS on 17 June 2020 and by letter on 18 June 2020 asking for further information to confirm the deductions and enclosing a 'Voluntary Disclosure form' to be returned to the ATO by 10 July 2020.

Steven did not provide the evidence. On 14 July 2020, the Commissioner issued an audit decision disallowing the full amount of the expenses he had claimed. The Commissioner also issued a notice of assessment excluding the deduction and a notice of assessment for a shortfall penalty of $15,153 on the basis that Steven had made a false or misleading statement which resulted in a shortfall amount.

On Steven's behalf, Steven's accountant, Mr Webb, lodged an objection to the penalty assessment on the basis that Steven had not been intentionally reckless because he had followed the advice he received at the seminar. Mr Webb submitted that Steven had not taken reasonable care and a lesser shortfall penalty should apply. Mr Webb also attached an amended 2019 income tax return that increased Steven's gross income and claimed deductions for car expenses.

On 11 November 2020, the Commissioner allowed the increase in gross income and the car expenses in part. The Commissioner also allowed the objection to the penalty assessment in part by adjusting it to reflect the new tax payable, which reduced the penalty from $15,153 to $14,354. The Commissioner also remitted the shortfall interest charges related to the additional income, due to the voluntary disclosure.

On 7 August 2021, Steven applied to the AAT for review of the Commissioner's decision dated 11 November 2020 and represented himself.

Under section 284-75(1) of Schedule 1 of the TAA, a person is liable to an administrative penalty if they, or their agent, makes a statement to the Commissioner that is false or misleading in a material particular.

However, under section 284-75(5) of Schedule 1 of the TAA, a person will not be liable for an administrative penalty in relation to a statement that is false or misleading in a material particular, if they and their agent (if relevant) took reasonable care in connection with making the statement.

There is a 'safe harbour' provision in section 284-75(6) of Schedule 1 of the TAA that protects a taxpayer from penalties where they have provided all relevant information to a registered tax or BAS agent and the agent has made the false or misleading statement, and the agent was not reckless or intentionally disregarding the law.

The base penalty amount for recklessness is 50% of the shortfall amount, while the base penalty amount for a failure to take reasonable care to comply with a taxation law is 25% of the shortfall amount.

Issue

Should the AAT exercise the discretion under section 298-20 of Schedule 1 of the TAA to remit the whole or part of Steven's penalty assessment?

Decision

The AAT observed that the 'theory' presented by the seminar was no more than a 'groundless and illogical fringe-theory' that has no foundation in Australian law.

Was Steven liable to a penalty for making a false or misleading statement?

The AAT found that the 'Other Work-Related Expenses' claim was false because it was wrong. The costs claimed were not legally permissible deductions. Further, the statement could also be viewed as misleading, because it included non-work-related expenses. Furthermore, Steven was provided with an opportunity to correct the statement and his failure to do so could also be viewed as misleading.

The AAT did not accept that Steven took reasonable care in making the statement to the ATO. The AAT noted that Steven had departed from his past good compliance practice of lodging his returns with the assistance of a qualified tax agent.

The AAT stated that an ordinary person in Steven's position would have checked the information provided by the seminar with a qualified tax agent or with the ATO and by not doing so he had not taken reasonable care.

Was Steven reckless or careless in making the statement?

The AAT found that Steven had deliberately avoided seeking advice from his accountant and sought to verify the information with other organisations that espoused similar theories to those presented that the seminar. Steven also knew that the person presenting the seminar was not a lawyer or accountant. While Steven was not intentionally dishonest and he believed, and continues to believe, the information provided by the seminar, his actions were reckless. A reasonable person in Steven's position would have questioned the information and sought verification from an appropriately qualified professional.

Steven was not able to rely on the 'safe harbour' provisions in section 284-75(6) of Schedule 1 of the TAA, because the person assisting him with his tax return was not a registered tax agent.

Is there any other basis on which the penalty should be remitted?

The AAT found that Steven had been objectively reckless and that the 50% penalty assessed by the Commissioner was appropriate.

TIP – PS LA 2012/5 provides guidance regarding when a statement is false and misleading and the concept of 'reasonable care'. *Miscellaneous Taxation Ruling* 2008/1 also provides guidance on the Commissioner's view of the meaning of 'reasonable care', 'recklessness' and 'intentional disregard'.

Citation *Oxby and Commissioner of Taxation* [2022] AATA 3239 (Senior Member Dr M Evans-Bonner, Perth)
w https://www.austlii.edu.au/cgi-bin/viewdoc/au/cases/cth/AATA//2022/3239.html

1.4 Wulf – deductibility of rental property repairs and improvements

Facts

Peter Wulf purchased a house in July 1983.

In or around March 2008, Peter began to rent out the property. Two families were tenants between 2008 and August 2014. A third family left overnight without notice after two months. This was in breach of the lease and they were owing rent when they left.

Peter provided evidence that on leaving the property, the tenants deliberately blocked all the drains in the house and turned on all the taps. The water overflowed and caused significant damage to the kitchen, ensuite, main bathroom and adjacent toilet and laundry. In the kitchen, all of the shelving was rendered immediately unusable. The flooding also caused the waterproofing to fail in the bathroom, shower, walls and wooden floors.

Some repair works were undertaken immediately in the bathrooms and kitchen, including replacing the shelves in the cupboards. Peter noted that despite these repairs, the kitchen continued to deteriorate over time, as the cupboard doors started to fall off, mould was growing and the bench tops lifted.

A fourth family rented the property for seven months before breaking the lease due to a family separation.

A fifth family rented the property for two years between September 2015 and September 2017. Peter gave evidence that these tenants broke off the showerhead in August 2017, which caused flooding of the ensuite. In September 2017, a water pipe burst under the sink, flooding the main bathroom and adjoining toilet and laundry.

Significant works were undertaken in the income year ended 30 June 2018. These included:

1. rebuilding the bathroom with a new smaller bath, vanity, including a new basin and a shower with new fittings including a new shower screen;
2. stripping the tiles and fittings in the bathrooms, waterproofing up to at least 200mm above the floor and installing new tiles and fittings;
3. removing and replacing the wall sheets, sink, plumbing fittings and range hood in the kitchen; and
4. replacing all cabinetry in the kitchen, including overhead cabinets that were not water damaged.

Section 25-10 of the ITAA 1997 relevantly provides:

> *(1) You can deduct expenditure you incur for repairs to premises (or part of premises) or a depreciating asset that you held or used solely for the purpose of producing assessable income*
>
> *…*
>
> ***No deduction for capital expenditure***
>
> *(3) You cannot deduct capital expenditure under this section.*

Peter claimed deductions for the costs of these works in his income tax return for the income year ended 30 June 2018.

The Commissioner denied these deductions.

Peter objected to the assessment.

The Commissioner disallowed the objection on the basis that the expenditure was capital in nature because, as a matter of fact and degree, the works amounted to improvements. In disallowing the objection, the Commissioner also submitted that the works amounted to renewals or reconstructions of entireties.

On 25 November 2022, Peter applied to the AAT for review of the objection decision.

Peter submitted that the works did not change the character of the property and were not improvements. In support of this submission, Peter stated that the work done to the bathroom, ensuite, laundry and toilet did not change the footprint or layout. Each fitting was in the same location and the only changes were more contemporary fittings to comply with water efficiency requirements. Peter also stated that the works were done on a budget and to match the previous bathroom fittings.

In relation to the kitchen works, Peter stated that the works were to make good the previous kitchen that was significantly damaged as a result of the actions of the tenants and noted that none of the works went outside the existing kitchen footprint. Peter submitted that the works did not change the character of the property but rather restored the efficiency of the property's functions to a standard required to rent the property.

The Commissioner submitted that the question should not be limited to whether something was remedied. The Commissioner argued that the examination of whether the works amounted to improvements required broader consideration of whether the works brought the property into a more valuable or desirable form such that there was a greater efficiency of function. The Commissioner referred to such works as enhancements to the property's income-producing ability, market value or expected life. In support of these submissions, the Commissioner relied on evidence from the tradesperson that the works increased the effective life of the bathroom and ensuite. The Commissioner also observed that the rent was increased during this period, which the Commissioner argued evidenced an increase in the property's income-producing ability as a result of the works.

Issue

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Were the costs of the works undertaken in the income year ended 30 June 2018 deductible?

Decision

The AAT examined the expenditure line by line and determined that some costs were in the nature of repairs and deductible under section 25-10 of the ITAA 1997, while others were capital improvements and deductible in future under section 43-10 of the ITAA 1997.

In reaching its decision, the AAT considered the test formulated by Kitto J in *Federal Commissioner of Taxation v Western Suburbs Cinemas Ltd* [1952] HCA 28, which focuses on future benefits and, in the facts of that case, future savings in revenue outgoings. The AAT also described paragraphs [55] and [56] of the ATO Taxation Ruling TR 97/23 in relation to 'repairs done at the same time as improvements' as being an accurate summary of the relevant authorities.

The AAT found that significant damage had occurred to the stud walls and floor of the kitchen, bathroom, ensuite, laundry and toilet because of flooding. To examine this damage, it was necessary to remove the wall coverings which included much, if not all, of the wall tiles in the bathroom and ensuite and to a lesser extent in the toilet and laundry. The cost for this work was deductible, as the work was necessary, was a repair and not in the nature of an improvement. The work relating to replacing the walls and floor of the toilet and laundry were also found to be repairs which would have little impact on the market or rental value of the house and would have little enduring impact on future repair or maintenance expenses.

The AAT found that the waterproofing and replacement fittings and cabinetry for the kitchen and bathroom were capital improvements. A properly waterproofed modernised kitchen, bathroom and ensuite, even when done on a prudent budget, can be expected to produce revenue savings over time and extend the useful life of the asset.

As some costs were found to be repairs and others were found to be capital in nature, the labour costs associated with the works were to be apportioned. The AAT remitted the invoices for the construction labour to the Commissioner to apportion in accordance with the AAT's findings.

TIP – this case emphasises that in determining whether something done constitutes a ‘repair’ is a matter of considering each piece of work done to identify whether there has been a mere ‘repair’ or whether the work constitutes an ‘improvement’. It is not enough to simply determine that the item was in need of repair or replacement, and being able to increase rent after works are done is an indication that those works constituted an ‘improvement’.

Citation *Wulf and Commissioner of Taxation* [2022] AATA 3094 (Senior Member K James, Melbourne)
w http://classic.austlii.edu.au/cgi-bin/sinodisp/au/cases/cth/AATA/2022/3094.html

1.5 Rizkallah – deductions for rental property

Facts

On 30 September 2009, Rebecca Rizkallah acquired a newly constructed property located at 3/18 Gosling Street, Greenacre, NSW (**Greenacre Property**) for $300,000. Rebecca funded the acquisition of the Greenacre Property using a loan from the Commonwealth Bank of Australia.

On 14 June 2011, Rebecca moved into her parents’ house at 5/18 Gosling Street Greenacre, NSW (**Parents' House**) and she let the Greenacre Property to a tenant.

On 5 May 2015, George Daouk arrived in Australia as the holder of a partner visa sponsored by Rebecca. Following his arrival in Australia, George lived at the Parents’ House with Rebecca. Shortly before they married, Rebecca became aware that George had a gambling problem.

On 9 August 2015, Rebecca and George married. They lived together at the Greenacre Property for about one month, following which Rebecca returned to live at the Parents’ House. While they were living apart, the couple’s relationship was ‘on and off’, and they formally separated at the end of 2015.

On 25 September 2015 Rebecca and George entered into a tenancy agreement (**Tenancy Agreement**) under which George agreed to pay Rebecca monthly rent of $1,016 in cash to live in the Greencare Property. Rebecca asked her family, who are in the building industry, about the agreed rent and they said it was 'reasonable'. The Tenancy Agreement was meant to be temporary as Rebecca was hoping that she and George would reconcile.

George was unable to pay rent regularly as he was still dealing with a gambling addiction. The total amount of rent Rebecca received averaged $1,000 per month for the 2016 income year, and $1,016 per month for the 2017 income year. Rebecca paid for the utilities, contents insurance, strata fees, council rates and all expenses related to the maintenance of the Greenacre Property.

On or around 1 August 2017, Rebecca and George reconciled, and Rebecca moved back into the Greenacre Property. Rebecca and George had a first child in September 2017 and a second child in May 2019. Rebecca and the children slept at the Greenacre Property, but she and George were separated.

Rebecca incurred interest expenses on the bank loan as follows:

1. $11,900 for the 2016 income year; and
2. $13,600 for the 2017 income year

Rebecca incurred other outgoings for the Greenacre Property as follows:

1. $1,381 for the 2016 income year; and
2. $2,477 for the 2017 income year.

On 20 November 2002, NJR Formwork Pty Ltd (**NJR**) was registered. It was deregistered on 22 April 2013. NJR was a company operated by Rebecca's father and brother. NJR built both the Greenacre Property and the Parents' House.

Rebecca claimed deductions for repair/maintenance works performed by NJR in respect of the Greenacre Property. All tax invoices issued by NJR to Rebecca for repair/maintenance works done on the Greenacre Property were dated after the date of NJR's deregistration.

Rebecca claimed that the Greenacre Property was substantially improved during the relevant years, and she claimed capital allowance deductions in relation to the construction cost for those structural improvements carried out by NJR on the Greenacre Property in the amount of $198,000.

On 19 August 2016, Rebecca lodged her income tax return for the year ended 30 June 2016. Rebecca reported rent of $12,000 and included as deductible rental expenses outgoings totalling of $37,520. The outgoings were made up of:

1. interest expense $17,085;
2. capital allowances $8,910; and
3. other deductions (including repairs/maintenance) $11,525.

On 18 August 2017, Rebecca lodged her income tax return for the year ended 30 June 2017. Rebecca reported rent of $12,200 and included as deductible rental expenses outgoings totalling $39,620. The outgoings were made up of:

1. capital allowances $13,160;
2. interest deductions $15,200; and
3. other deductions (including repairs/maintenance) $11,260.

On 6 November 2017, the Commissioner commenced an audit of Rebecca's tax affairs for the relevant years and invited her to make a voluntary disclosure.

On 19 December 2017, Rebecca made representations to the Commissioner that the rent paid under the Tenancy Agreement was decided on the basis that it was similar to other units in the same strata, and neither Rebecca nor any of her associates were residing at the Greenacre Property.

On 13 June 2018, Rebecca:

1. made a voluntary disclosure that the Greenacre Property had not been renovated/improved and that she had incorrectly claimed deductions for the post-acquisition capital works, and she wished to withdraw all deductions relating to supplies made by NJR; and
2. requested the Commissioner consider a BMT depreciation report as substantiation for her allowable deductions relating to capital allowances in her 2016 and 2017 income tax returns.

On 22 August 2018, the Commissioner issued amended assessments for each of the relevant years, disallowing the rental deductions claimed by Rebecca. On 22 August 2018, the Commissioner also issued penalty assessments for each the relevant years at the rate of 50% for recklessness.

On 31 October 2018, Rebecca lodged a Notice of Objection to the amended assessments and the penalty assessments.

On 6 March 2019 the Commissioner notified Rebecca that the objection in respect of the amended assessments for the relevant years would be disallowed and on 20 September 2021 notified her that the objection in respect of its penalty assessments would be disallowed.

On 19 May 2020, Rebecca lodged a review application with the AAT for review of the objection decision relating to the amended assessments and on 14 October 2021 lodged an application for review of the objection decision relating to penalty assessments.

Issues

1. Were the losses and outgoings incurred by Rebecca for her rental property deductible under section 8-1(1)(a) of the ITAA 1997?
2. Was Rebecca excluded from deducting these losses and outgoings in whole or in part as they were a loss or outgoing of a private or domestic nature under section 8-1(2)(b) of ITAA 1997?
3. What was the amount, if any, of the administrative penalty to be imposed on Rebecca under section 284-75 of Schedule 1 to the TAA?
4. Should the administrative penalty be remitted pursuant to section 298-20(1) of Schedule 1 to the TAA?

Decision

Issue 1

The AAT held that the characterisation of an outgoing for the purposes of section 8-1 of the ITAA 1997 is a question of fact to be determined by reference to all the circumstances surrounding its incurrence, including what the expenditure was for and what it was intended to achieve.

The AAT found that the losses and outgoings incurred by Rebecca in excess of the rental income derived from renting the Greenacre Property to George were not 'necessarily incurred in' gaining or producing assessable income. Rebecca rented the property to George so that he would have a place to live in close proximity to her which would facilitate their attempt to reconcile their relationship. The rent paid by George was sufficient to cover Rebecca's mortgage repayments and was not intended to gain or produce assessable income.

Issue 2

The AAT found it was not necessary to answer this question. However, for completeness, the AAT, citing Taxation Ruling IT 2167 *Income Tax: rental properties – non-economic rental, holiday home, share of residence, etc,* noted that expenses incurred in gaining or producing rental income pursuant to an arm’s length agreement are allowable deductions but that, where an agreement is not arm’s length, the taxpayer must

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demonstrate the terms of the agreement were on commercial terms. In Rebecca's circumstances, she leased her property to George who at all relevant times was her husband.

The AAT found that the Tenancy Agreement between Rebecca and George was not consistent with commercial practices and was not on commercial terms. This is because:

1. George paid, on average, a weekly rental of $229 in the 2016 income year and $262 in the 2017 income year. A rental comparison report provided by the Commissioner showed that during the relevant periods the lowest rent for a comparable property in the area was $450 per week; and
2. the rental income received by Rebecca during the relevant years was well below market rate and significantly below that of an arm's length market value. The non-commercial nature of the Tenancy Agreement is further demonstrated by the absence of the following that would normally exist in an arm's length arrangement including:
   (a) no tenancy agreement was lodged with NSW Fair Trading;
   (b) no rental bond was lodged with NSW Fair Trading;
   (c) no contemporaneous documentation relating to the Tenancy Agreement or agreed terms exists; and
   (d) no contemporaneous documentation relating to late or unpaid amounts of rent exists.

The explanation for the low rent paid by George lay in the familial and domestic relationship between him and Rebecca. The determination of the rent payable under the Tenancy Agreement was based on private or non-income earning considerations. Consequently, the AAT found that all the outgoings for the Greenacre Property cannot be said to have the character of expenses incurred in gaining or producing assessable income.

As a matter of apportionment, the AAT found it was very difficult to determine an appropriate apportionment of the losses and outgoings because Rebecca's evidence was unclear as to how often she was living at the Greenacre Property during the relevant period while she and George were attempting to reconcile. It was accepted by the parties that if there is insufficient information to enable a final decision, the working rule suggested in IT 2167 should be applied.

This allows income tax deductions for losses and outgoings incurred in connection with the rental property to be allowed up to the amount of rental income that has been substantiated. Applying the working rule suggested in IT 2167, the AAT found that the deductions for losses and outgoings incurred by Rebecca in connection with the rental property be allowed up to the amount of the rental income in the relevant years.

Issue 3

The AAT found that Rebecca was reckless and upheld the administrative penalty of 50% for each of the relevant years. This is because:

1. Rebecca was given the opportunity to make a voluntary disclosure when she was advised she was being audited in November 2017;
2. Rebecca and her tax agent continued to provide the Commissioner with invoices which were incorrectly dated and/or were not relevant, and gave the Commissioner incorrect information;
3. in June 2018, Rebecca made a voluntary disclosure conceding the claimed depreciation expenses and all the expenses she claimed to have incurred with NJR. She did not provide an explanation as to why NJR invoices dated during the relevant years had been provided to the Commissioner when NJR had been deregistered in 2013. Further, when audited Rebecca provided the invoices from NJR, which apparently had incorrect dates on them. It was unclear why the invoices were provided, given that they did not relate to the tax period in question. If they had been correctly dated, they would have been issued at a time when NJR was deregistered indicating that the invoices were in fact false;
4. Rebecca and her tax agent were unable to identify and substantiate the rental expenses incurred until well into the current review process. At no stage had Rebecca or her tax agent provided an explanation as to why these substantial rental expenses were claimed without information or documentation to verify their accuracy;
5. Rebecca's decision to lodge income tax returns which included rental expenses without proper substantiation or verification for the amounts of expenses claimed was reckless;
6. Rebecca included in her tax return claims for deductions knowing that there was a real, as opposed to a fanciful, risk that the information on which these were based was incorrect. A reasonable person in the

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position of Rebecca would have seen there was a real risk that this may in turn lead to an incorrect assessment by Commissioner of her tax liability.

Issue 4

The AAT found that Rebecca was guided by the misleading and inaccurate advice provided to her by her tax agent and members of her family in relation to the decisions she made to lease the Greenacre Property to George at a non-commercial rent, and to claim deductions in her tax return for outgoings she did not actually incur. Rebecca made a genuine attempt to meet her tax obligations and made an effort to '*do the right thing'*, despite recklessly including false and misleading statements in her tax return and making claims for deductions for which she was not entitled.

The AAT found it was appropriate to exercise the discretion under section 298-20(1) of the TAA to remit the penalty by 25%.

Citation *Rizkallah v Commissioner of Taxation* [2022] AATA 3081 (Senior Member Dr L Kirk, Sydney)
w http://classic.austlii.edu.au/cgi-bin/sinodisp/au/cases/cth/AATA/2022/3081.html

1.6 Dowsing – default assessment penalty

Facts

Caleb Dowsing failed to submit his tax return for the 2017 income year despite the Commissioner contacting Caleb and his tax agent on various occasions between 6 March 2019 to 7 May 2019. Caleb was granted extensions of time and continued to fail to submit his tax return.

On 21 May 2019, the Commissioner issued a default formal warning letter to Caleb stating that if he did not lodge his 2017 tax return by 18 June 2019, the Commissioner would issue a default assessment and impose a default assessment penalty of 75% of the tax payable under the assessment.

Caleb failed to submit his 2017 tax return by 18 June 2019, and the Commissioner made a default assessment on 1 July 2019.

The Commissioner issued a notice of assessment for the 2017 income for $6,657 which was paid by Caleb, but later, the Commissioner issued an administrative penalty of $4,993.

With the help of a family accountant, on 31 May 2021, Caleb lodged an objection against the penalty assessment on the basis that Caleb faced difficulty over the previous few years due to his gambling and drug addiction which affected his mental health, family relationships and suffered instability in his life all while accruing debt.

After the Commissioner disallowed the objection, Caleb, through his accountant, sought a review of the penalty assessment in the AAT, asking for 100% of the penalty to be remitted.

The Commissioner primarily relied upon the principles set out at clause 3A of the *Practice Statement Law Administration 2014/4: Default assessment penalty (***PS LA 2014/4***)* which explains the discretionary powers the Commissioner has in order to remit administrative penalties.

Clause 5K of PS LA 2014/4 provides guidance about when remission of a penalty may be appropriate. In particular, the Commissioner considered the following statement as relevant in Caleb's circumstances, 'the entity understood the obligation to lodge but circumstances beyond its control affected its ability to lodge'.

The Commissioner paid particular attention to the above principle as it was relevant to Caleb's circumstances. Caleb was aware of his obligations to lodge the 2017 tax return but did not do so due to circumstances that he believed were beyond his control, affecting his ability to lodge.

It was noted that Caleb has previously completed his past tax returns through his accountants and was otherwise compliant up until 2017.

Caleb submitted that his gambling and drug addiction had detrimentally impacted areas of his life such as his mental health, his work, family and relationships. The AAT acknowledged that Caleb was honest about his struggles and commended him for turning his life around for the better, however submitted the circumstances were not entirely out of his control.

Issues

1. Was Caleb liable to an administrative penalty under section 284-75(3) of Schedule 1 of the TAA 1953?
2. Should the Commissioner exercise the discretion under section 298-20(1) of Schedule 1 of the TAA 1953 to remit 100% of Caleb's penalty?

Decision

The AAT noted that Caleb's circumstances arose, at least partly because of his poor life choices. It was noted that he was able to function to some extent and his circumstances were not entirely out of his control.

The AAT also considered that some of Caleb's poor life choices that had impacted him detrimentally arose after January 2019 and were not relevant to his failure to lodge the 2017 tax return.

The AAT concluded that Caleb was liable for an administrative penalty and was not satisfied that the administrative penalty was excessive or otherwise incorrect. The AAT confirmed the Commissioner's decision to apply the penalty.

COMMENT – if faced with a final notice to lodge a return, it may be best to lodge a return that overstates taxable income and later amend the assessment, rather than allow a default assessment to issue, which will almost certainly result in a 75% penalty.

Citation *Dowsing and Commissioner of Taxation (Taxation)* [2022] AATA 3173 (Senior Member Dr M Evans-Bonner, Perth)
w https://www.austlii.edu.au/cgi-bin/viewdoc/au/cases/cth/AATA/2022/3173.html

1.7 Robis Consulting – cash flow boost

Robis Consulting Pty Ltd was incorporated in 1999. Robert Johnson, his wife, Marilyn Johnson and their son, Ross Johnson are the directors. Robert and Marilyn are the sole shareholders.

Robert is a highly experienced actuary and is also qualified as a Certified Practising Accountant, although he has never practised as a CPA.

Robis Consulting provided actuarial and related consultancy services. Typically, the activities of Robis Consulting were driven by Robert since its incorporation. Robert was responsible for preparing the company’s activity statements and made all the salary and wage decisions.

The level of activities of Robis Consulting varied in the last 10 years.

Between July 2010 and August 2015, Robis Consulting had full-time operations based in Australia.

Between September 2015 and October 2017, operations were scaled back due to Robert working full-time in the UK.

Between November 2017 and June 2019, the company was largely dormant due to a health scare at which point Robert chose to retire. Robis Consulting was also in receipt of a substantial non-compete payment during that time. The non-compete arrangement ended in December 2019.

Between July 2019 and June 2020, Robert sought to recommence the company's business activities and met with various high-level executives in the insurance industry. This resulted in Robis Consulting entering into a service agreement to provide training services for the Institute of Actuaries of Australia (**IAA**).

Robis Consulting commenced work for IAA in November 2019. The work commenced in November 2019 was first invoiced by Robis Consulting in January 2020 and paid by IAA on 29 January 2020.

Between July 2019 to February 2020, no directors' fees were declared and no PAYGW was withheld.

In its March 2020 activity statement, Robis Consulting accounted for directors' fees as wages in the total amount of $69,500 with PAYGW withholding of $24,846. No actual payment was made in March 2020 for the directors' fees. Directors' fees were declared in the months following March 2020 at lower amounts.

Robis Consulting did not maintain any direct record of the decision to pay directors' fees other than the business activity statement. There were no minutes or record of resolutions of Robis Consulting, nor payslips issued.

Robis Consulting asserted that there was a constructive payment of directors' fees in March 2020 by declaring earlier directors' drawings to be directors' fees during March 2020. The Commissioner accepted in principle that directors' fees may be paid constructively but did not accept that Robis Consulting did so in this case.

Following an investigation by the Commissioner, the Commissioner refused payment of the cash flow boost for March 2020. Robis Consulting objected to the Commissioner's decision.

The Commissioner disallowed the objection on the basis that Robis Consulting had not discharged the burden of proving two grounds, namely:

1. that Robis Consulting had paid wages in the form of directors' fees in March 2020 and therefore had an obligation to withhold PAYGW (Payment Issue); and
2. that Robis Consulting had not entered into or carried out a scheme for the sole or dominant purpose of making it entitled to the cash flow boost for March 2020 or increasing its entitlement for the period (Scheme Issue).

Issue

Is Robis entitled to the cash flow boost for the March 2022 period?

Decision

<u>Payment Issue</u>

On the balance of probabilities, SM Olding favoured Robert's account regarding the declaration of wages to allow Robis Consulting to succeed on the Payment Issue.

There was no dispute that in principle the directors' fees could be taken as constructively paid by offsetting the fees against earlier directors' drawings.

In evidence to support that the decision to declare the earlier directors' drawings to be directors' fees was made in March 2020, as opposed to in April 2020 when the activity statement would have been prepared, Robert stated that he relied on the company's bank statements, and as the statements could not be altered once closed off at the end of the month, he would make such decisions during the month.

SM Olding took into account that Robert's evidence by its nature was necessarily self-serving and needed to be taken with caution, but without adopting a default position that it was untruthful. SM Olding took into account

that Robert presented as a straightforward witness who readily acknowledged matters that were against Robis Consulting's case.

The AAT also considered there was no contemporaneous documentary evidence in support of the assertion that the directors' fees were declared in March 2020. Whilst not best practice, SM Olding noted that this was not an uncommon position for small businesses. SM Olding accepted Robert's evidence that he had determined in March 2020 to declare the earlier directors' drawings to be directors' fees.

Scheme Issue

The AAT considered that Robis Consulting had not entered into or carried out a scheme for the sole or dominant purpose of making it entitled to the cash flow boost for March 2020.

The parties accepted that Robert was the controlling mind of Robis Consulting.

SM Olding found Robert's explanations credible and consistent. On balance, SM Olding was satisfied that Robert was truthful in his assertion that he had determined to declare wages was made for other reasons and not mainly to obtain or increase cash flow boost.

The Commissioner had suggested there was a scheme in circumstances where no directors' fees were paid prior to March 2022. Robert explained that he had only recommenced work through Robis Consulting in November 2019 after initially having retired following a health scare. In the context of Robert's working history, the AAT accepted this to be a reasonable explanation. Robert further explained that although work commenced in November 2019 the first invoice was only issued in January 2020 and paid on 29 January 2020. It was only after this time that Robis Consulting determined to pay directors' fees. The AAT considered in the context of small business that the delay of about two months between the receipt of the first invoice payment from the IAA and the declaring of directors' fees was not remarkable.

Citation *Robis Consulting Pty Ltd and Commissioner of Taxation (Taxation)* [2022] AATA 2832 (Senior Member Olding, Sydney)
w https://www.austlii.edu.au/cgi-bin/viewdoc/au/cases/cth/AATA/2022/2832.html

1.8 Trustee for the Lubiana Family Trust – wine equalisation tax

Facts

The trustee for the Lubiana Family Trust trading as 'Stefano Lubiana Wines' is a winemaker producing ultra-premium wines. The directors of the trustee are Monique Lubiana and Steve Lubiana.

The Lubiana Family Trust objected to assessments made by the Commissioner regarding the calculation of the taxable value for the purposes of wine equalisation tax under the *A New Tax System (Wine Equalisation Tax) Act 1999* (Cth) (WET Act). The Commissioner disallowed the objections, and the Lubiana Family Trust appealed the decision to the AAT.

At the hearing, the Lubiana Family Trust argued that it was only required to pay wine tax on 'wine' for wine tax purposes. Wine is defined as *the product of the complete or partial fermentation of fresh grapes*. The business argued that the amount paid for by customers was for the supply of:

1. the fermented grapes contained in their product;
2. the bottle and other packaging;
3. the goodwill, reputation and romance attributable to the product; and
4. the delivery of the product.

The business purported that the amount which is 'wine' for tax purposes is not the net amount invoiced to the customers. The price paid by the customer for the packaging, goodwill and delivery must be excluded from the taxable component of the amount.

Monique provided evidence as to how the wholesale distribution worked, and that the reputation of Stefano Lubiana Wines allows for the price to be higher than that of their competitors, as customers appreciate and respect the story behind Stefano Lubiana Wines.

The primary argument of the Lubiana Family Trust was that they were selling four different items to the consumer.

Issue

Whether the business has discharged the burden of proving the invoiced amounts in their entirety were not payments in connection with supplies that are sales of fermented grape products, and the amounts should be reduced by the amount attributable to one or more of the packaging, goodwill and delivery components.

Decision

The AAT found that the business did not seek to differentiate, or separate the wine to the packaging, goodwill and delivery elements. In not separating each component, the sale was consistent with a single transaction.

The AAT relied on the case *Re Food Supplier and Commissioner of Taxation* [2007] AATA 1550 which held that items which are integral, ancillary or incidental to the main item may be treated for GST purposes in the same way as the main item. The AAT held that there is no reason why this analogy should not apply to this case.

The AAT referred to the case of *EMI (Australia) Limited v Commissioner of Taxation of the Commonwealth* (1971) 45 ALJR 349 to define the meaning of the expression 'the amount for which the goods are sold'. This case defined the term *amount* to mean the sum total of all moneys that the buyer promises, expressly or tacitly, to pay to, or for, the seller in order that he, the buyer, may get good title to the goods that he has agreed to buy.

The AAT accepted that the story behind Stefano Lubiana Wines may play a role in the premium prices charged by the business, but did not accept that this goodwill and reputation is separate from the sale of the product. The AAT held that a transaction for the sale of wine, no matter how revered the brand may be, cannot sensibly be characterised as separate sales of fermented grape product and goodwill, reputation and romance associated with the brand.

In relation to the packaging element, the AAT held that it is artificial to separate out and attribute a separate price for goods supplied in a container where the parties have not themselves done so, and the container has no inherent value to the customer, other than acting as a vessel for the supply of the product.

The AAT further noted section 9-65 of the *A New Tax System (Wine Equalisation Tax) Act 1999* (Cth) which provides:

*(1) This section deals with situations in which a *container is associated with wine (the contents) that is the subject of a *taxable dealing. The aim of this section is to ensure that the *taxable value will include a component for the container, even though parties may have allocated a separate amount to the container.*

(2) If:

*(a) the taxable value of the dealing is calculated by reference to the *price (excluding wine tax and GST) for which the contents were sold; and*
(b) the parties have allocated a separate amount to the container;

then the taxable value is increased by so much of the value of the container as is recouped by the seller in connection with the sale of the contents.

(3) If the taxable value of the dealing is not calculated as mentioned in subsection (2), then the taxable value is increased by so much of the value of the container as could reasonably be expected to have been recouped by you in connection with a hypothetical sale of the contents at the time of the actual taxable dealing with the contents

The AAT noted that while this section did not have a direct relation to the present circumstances, it reinforced the concept that the container forms part of the consideration for the sale of the wine, and therefore part of the taxable component, even in circumstances where it has in fact been separately costed.

The AAT considered whether the cost of delivery may be excluded from the taxable value where the customer pays a single price for wine delivered to their premises.

In relation to delivery, the AAT relied on the case *NZWINEIMPORTS Pty Limited v Commissioner of Taxation* [2016] AATA 824 where it was held that the amount for which the goods were sold was the contract price for the delivered goods without any deduction for delivery costs.

The AAT concluded that their decision was consistent with the object of the WET Act and it was not appropriate to deduct any amount for the value of the container/packaging, goodwill or delivery elements.

The AAT confirmed the Commissioner's decision.

Citation *Trustee for Lubiana Family Trust v Commissioner of Tax* [2022] AATA 2826 (Deputy President McCabe, Senior Member Olding, Sydney)
w https://www.austlii.edu.au/cgi-bin/viewdoc/au/cases/cth/AATA/2022/2826.html

1.9 Australian Karting Association – trust distributions to beneficiaries

Facts

Karting Australia is the national body responsible for promoting the sport of 'go-kart' racing in Australia. Karting NSW is a non-for-profit association responsible for promoting and conducting karting races in New South Wales and the Australian Capital Territory. Karting NSW is an ordinary member of Karting Australia under Karting Australia's constitution.

In 2005, a discretionary trust, the AKA Track Development Fund, was established by AKA Inc, Karting Australia's predecessor, of which Karting Australia, was trustee. From October 2005, State member organisations, including Karting NSW, would collect and remit driver levies paid by every driver who entered a race to Karting Australia, who would invest these funds in bank deposits and receivables. There were loans made to Karting NSW from Karting Australia for the purpose of track development. The obligation to pay interest was suspended, subject to the borrower complying with the terms of the loan. In the event of a default, the principal sum and accumulated interest became immediately payable at the option of Karting Australia.

Karting NSW was expelled as an ordinary member of Karting Australia on 21 January 2019, which Karting Australia relied upon as an event of default under the three loans. Karting Australia applied to the Supreme Court seeking to recover principal and interest from Karting NSW under three loans, in amounts totalling approximately $157,000. Karting NSW cross claimed for unpaid distributions as a beneficiary of the trust totalling $616,065. These amounts had been credited to Karting NSW's loan account with the trust. Karting NSW's claim was advanced as an action at law for money had and received, not an equitable claim of a beneficiary entitled to moneys from a trustee.

The primary judge held that the accelerated payment provisions of the loan agreements were a penalty and therefore unenforceable. The claim by Karting Australia in respect of the loans was dismissed.

The primary judge upheld Karting NSW's cross claim for unpaid distributions. The primary judge confirmed that Karting Australia had the power under clause 7 of the Trust Deed to pay out capital and make distributions of trust property. Karting Australia dealt with the capital sums, including the driver levies, by crediting those amounts to loan accounts in the names of the ordinary member beneficiaries. The Court held that the effect of crediting these amounts to the beneficiaries' loan accounts, was to distribute the amounts to the beneficiaries. That is, these funds were held on bare trust in favour of the beneficiary in the amounts set out in the loan accounts and were repayable on demand by each beneficiary.

The primary judge confirmed that this conclusion was consistent with the net assets of the trust being $1 at the end of each financial year, those accounts showing the total liabilities of the trust, which included the amounts in the loan accounts, and the fact that the trustee declared for each year that the financial statements of the trust fairly represented the financial position of the trust.

The primary judge referred to authority that 'where a trustee admits a debt to a beneficiary, an action for money had and received lies at the suit of the beneficiary'.

In response to the fact that Karting Australia did not make any resolutions to distribute the amounts to Karting NSW, the primary judge confirmed that the intention of the directors of a company may be determined by reference to what they say or do. Therefore, the fact that there was no board meeting or resolution did not mean that the trustee's intention had not been sufficiently established.

Karting Australia appealed the primary decision to the Court of Appeal.

On appeal, Karting Australia contended that no amount was payable to Karting NSW because:

1. the trustee intended to make a conditional distribution to beneficiaries, in the sense that payment of the amount distributed was deferred to the date of vesting of the Trust; or
2. the trustee intended to make no distributions to beneficiaries. Karting Australia submitted that the accounts of the trust were an inadequate basis to infer that the trustee had resolved to make distributions to the beneficiaries as recorded in the accounts.

Issues

1. Did the trustee intend to make a conditional distribution to the beneficiaries of the trust?
2. Did the trustee intend to make no distribution to the beneficiaries?

Decision

Issue 1

The Court of Appeal noted that the 'conditional distribution' argument was raised for the first time on appeal, and it was a proposition which was contrary to Karting Australia's position at trial. Therefore, the Court of Appeal found that Karting Australia was precluded from relying on the new point on appeal given the prejudice that would arise to Karting NSW.

Despite this finding, the Court of Appeal also confirmed that the 'conditional distribution' argument should also be rejected for the following reasons:

1. the trustee's liability to Karting NSW is not a contingent liability. A contingent liability is usually disclosed by way of a note to the accounts of an entity and not recorded as an actual liability. In this case, the accounts of the trust recorded the amounts owing to the beneficiaries as actual liabilities;
2. the unpaid distributions recorded in the accounts of the Trust were made by the trustee crediting the beneficiaries' loan account and were payable at call;
3. the notes to the accounts of the Trust from 2015 do not support the conditional distribution argument, rather they are consistent with the trustee's intention that by crediting the amount of the unpaid

distributions to beneficiaries' loan accounts, such amounts would remain available to the trustee for the purposes of the Trust; and

4. there was no evidence that the accounts were inaccurate or mistaken.

Therefore, the 'conditional distribution' argument was not accepted by the Court of Appeal.

Issue 2

The Court of Appeal confirmed that, as an incorporated association (not a company under the Corporations Act), Karting Australia was not required by the terms of the trust deed to pass any resolution of its committee to exercise its power of distribution.

Even if a resolution was required, the Court of Appeal found that the conduct of Karting Australia in crediting the distributions to Karting NSW's loan account from 2005 to 2012 and acknowledging the debt owing to Karting NSW in its audited accounts, justified the inference that the trustee's intention was to make the unpaid distributions to beneficiaries, including to Karting NSW.

Further, the Court of Appeal found that the conduct of the trustee in approving the audited accounts of the trust justified the inference that the trustee resolved to make distributions to the beneficiaries, including Karting NSW. In addition, there was a notation in the 2014 financial statements which corrected errors in the 2013 financial statement regarding the amounts disclosed as beneficiary loans. The Court of Appeal inferred that by correcting these errors, Karting Australia specifically turned their minds to the issue which was disputed at trial, that is, they confirmed that there was an adjustment to the beneficiaries' loan account. The Court of Appeal found this was inconsistent with Karting Australia's no distribution argument.

In addition, there was no evidence which suggested there was a common intention of the trustee and beneficiaries to accumulate the income of the trust until the vesting date.

Accordingly, the Court of Appeal did not find any error by the primary judge in rejecting the no distribution argument.

Karting Australia's appeal was dismissed.

Citation *Australian Karting Association Ltd v Karting (New South Wales) Incorporated* [2022] NSWCA 188 (Meagher JA, Gleeson JA and Simpson AJA, New South Wales)
w http://www.austlii.edu.au/cgi-bin/viewdoc/au/cases/nsw/NSWCA/2022/188.html

1.10 Cymtow – NSW surcharge land tax

Facts

For the 2017 to 2021 land tax years (**Relevant Years**), Cymtow Pty Ltd (**Cymtow**) as trustee for the Stanavacs Trust, Lanlex No 127 Pty Ltd (**Lanlex**) as trustee for the TBH Family Trust and Cybir Pty Ltd (**Cybir**) as trustee for the Cybir Trust owned land which was residential land within the meaning of the *Land Tax Management Act 1956* (NSW) (**LTMA**).

Each trust was at all material times a discretionary trust.

On 4 February 2020, a letter was prepared for each of the Stanavacs Trust, TBH Trust and Cybir Trust, signed by Christian Hardin and Carolyn Bain (the **Instruments**). The operative sentence of each letter read as follows:

> *This letter is to notify that the trust deed [Trust] is amended to exclude beneficiaries who are not Australian citizens effective immediately.*

As at 4 February 2020, Christian and Carolyn were directors of Cymtow, Lanlex and Cybir.

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Clause 32(1) of the Stanavacs Trust Deed relevantly provided as follows:

> *…the Trustees for the time being may at any time and from time to time by deeds revocable or irrevocable revoke add to or vary all or any of the Trusts herein contained…*

Clause 14 of the TBH Trust Deed provided that the trustee could at any time by written or oral resolution or deed amend any provision of the trust deed, subject to certain conditions. Relevantly, these conditions stipulation that no variation:

> *may be in favour of or for the benefit of the Ineligible Beneficiaries or result in any benefit to the Ineligible Beneficiaries; or*
>
> *shall affect the beneficial entitlement to any amount set aside for any Beneficiary prior to the date of the variation alteration or addition.*

Clause 16.1 of the Cybir Trust Deed relevantly provided as follows:

> *With the consent of the Appointor, the Trustee may amend this Deed … in any way except:…*
>
> *It may not change the entitlement of any person to any capital or income appointed, paid or applied for the benefit of that person…*

As at 4 February 2020, Bruce Hardin was the appointor of the Cybir Trust. Bruce did not endorse the Instrument in respect of the Cybir Trust Deed.

On 16 December 2020, following oral communications between Bijay Upadhyay (the accountant acting for Cymtow, Lanlex and Cybir) and the Chief Commissioner's officer, the Chief Commissioner agreed to extend the deadline for amending the trust deeds for each trust from 31 December 2020 to 15 January 2021 to comply with the requirements of section 5D of the *Land Tax Act 1956* (**LTA**).

On 14 January 2021, each of the Stanavacs Trust Deed, the TBH Trust Deed and the Cybir Trust Deed were varied to ensure that none of the trustees would be taken under section 5D of the LTA to be a foreign person for purposes of section 5A of the LTA.

The Chief Commissioner assessed Cymtow, Lanlex and Cybir as liable to pay surcharge land tax on properties they owned for the Relevant Years.

Cymtow, Lanlex and Cybir sought a review of the Chief Commissioner's decision. They contended that the Instrument was sufficient to exclude foreign persons as benefitting from under the respective trust deeds.

Clause 66(2)(a) of the LTMA relevantly states as follows:

> *the trustee is exempt from that land tax* [being surcharge land tax] *if the terms of the trust have been amended, before payment of the land tax is due and before midnight on 31 December 2020, so that the trust prevents a foreign person from being a beneficiary.*

Section 66(3) of the LTMA relevantly states as follows:

> *A trust that satisfies the no foreign beneficiary requirement under section 5D of the Land Tax Act 1956 immediately before the commencement of that section is considered for the purposes of that section to prevent a foreign person from being a beneficiary of the trust (without having to satisfy the no amendment requirement under that section).*

Issues

1. Were the Instruments sufficient to ensure that none of the three trustees was to be taken under section 5D of the LTA to be a foreign person for purposes of section 5A of the LTA?

2. Did certain dealings in December 2019 between Bijay and the Chief Commissioner modify or limit the rights of the Chief Commissioner to assess Cymtow, Lanlex and Cybir with surcharge land tax in respect of the Relevant Years?

Decision

Issue 1

The NCAT determined that Cymtow, Lanlex and Cybir failed to discharge the burden of proof to demonstrate that the Instruments were effective to exclude non-Australian citizens from participation as beneficiaries of the relevant trust.

The NCAT concluded as follows:

1. in respect of the Stanavacs Trust, the Instrument was not in the form required by clause 32(1) of the trust deed, and therefore did not operate as an effective amendment to the trust deed for the following reasons:
   (a) it did not comply with the legal formalities required as a matter of general law to create a deed;
   (b) the Instrument was not executed in accordance with section 127(1) of the *Corporations Act*;
   (c) the Instrument made no reference to sealing or delivery in a manner sufficient to indicate that the Instrument was executed to take effect as a deed;
   (d) the Instrument was not expressed as a deed for the purpose of section 127(3) of the *Corporations Act*;
2. in respect of the Cybir Trust – no evidence was provided as to whether consent of the Instrument was endorsed by Bruce (as the appointor) for the purpose of clause 16.1 of the trust deed, and consequently, failed to operate as an effective amendment to the trust deed; and
3. in respect of the TBH Trust and the Cybir Trust, there was no factual basis to conclude that the Instruments satisfied the conditions imposed by section 14 of the TBH Trust Deed and section 16.1(b) of the Cybir Trust Deed.

Therefore, the Instruments were not effective in ensuring that foreign persons were excluded from benefiting under the trusts.

Issue 2

The NCAT was not satisfied that the Chief Commissioner's officer, in his conversation with Bijay, extended the deadline for making the required amendments under section 5D.

Nonetheless, the NCAT confirmed that there is no statutory power under the transitional provisions in Part 34 of Schedule 2 to the LTMA for the Chief Commissioner or any of his officers to extend on a case-by-case basis the 31 December 2020 deadline. Further, neither the Chief Commissioner nor any of his officers are bound by any extension which he or they may have purportedly granted.

Therefore, the Chief Commissioner's decision under review was affirmed.

Citation *Cymtow Pty Ltd as trustee for Stanavacs Trust; Lanlex No 127 Pty Ltd as trustee for TBH Family Trust; Cybir Pty Ltd v Chief Commissioner of State Revenue* [2022] NSWCATAD 314 (Senior Member AR Boxall, Sydney)
w http://www.austlii.edu.au/cgi-bin/viewdoc/au/cases/nsw/NSWCATAD/2022/314.html

1.11 Bennett – NSW land tax principal place of residence exemption and adjoining properties

Facts

During the 2017 to 2021 land tax years (**Relevant Years**), Sonja Bennett owned two adjoining properties in Tempe, Number 36 and Number 38. Number 36 was acquired by Sonja in October 1989. Number 38 was

acquired by Sonja in June 1994. Separate free-standing houses were originally located on each of Number 36 and Number 38.

During the Relevant Years, Number 36 was occupied by Sonja as her principal place of residence and, consequently, was exempt from land tax.

In 1994, Sonja removed the fence on the boundary between Number 36 and Number 38. Around this time, she engaged a builder to construct an annex between the rear sections of the two houses. The annex was an enclosed space and installed doors linked Number 36 and Number 38 through this annex.

The removal of the fence gave Sonja access to the back shed of Number 38 which she used to store tools and garden equipment. Two doors were also installed to give Sonja access to the rear of the garage at Number 38 to be used as a shed, study/office or workshop. Sonja stated that she used the shed 3 or 4 times per week for storage, to paint, listen to music or for her orchid planting. Sonja also constructed greenhouses on the rear of Number 38 to accommodate her collection of over 400 orchids which she tended to every day. Sonja used the verandah at the rear of Number 38 to store other materials.

From 2016, Sonja granted leases to tenants to occupy the front of the house on Number 38. During the Relevant Years, Number 38 was tenanted.

From 2016, Sonja claimed:

1. the tenants did not have access to the backyard of Number 38, the shed, the verandah or to Number 36;
2. when there were no tenants occupying Number 38, she regularly entered Number 38, allowed family and friends to reside there and used the space as a workspace; and
3. in late 2019-2022, Number 36 and Number 38 suffered extensive storm damage however, due to COVID-19 lockdowns she was unable to conduct the necessary repairs. Sonja claimed that it was her intention, once those repairs were undertaken, to use both Number 36 and Number 38 as her residence as she had done before 2016.

On 26 February 2021, the Chief Commissioner issued a land tax assessment for Number 38. Sonja objected to the assessment, and on 15 December 2021, the Chief Commissioner disallowed the objection. Sonja then applied to the NCAT seeking a review of the Chief Commissioner's decision.

Sonja contended that she was entitled to the principal place of residence exemption (**PPR Exemption**) in respect of Number 38, as Number 36 and Number 38 (collectively, the **Properties**) are the site of a single residence and together form a parcel of residential land used and occupied by her as her principal place of residence. While Number 38 was tenanted during the Relevant Years, Sonja contended that in each case the tenancy was an excluded residential occupancy for the purpose of clause 4(1) to Schedule 1 of the LTMA.

In the alternative, Sonja contended that if she is not entitled to the PPR Exemption, she is entitled to a concession on the taxable value of the land at Number 38 under clause 10B of Schedule 1 of the LTMA on the basis that the Properties should each by considered 'flats'.

Relevantly, clause 13(a) of Schedule 1 to the LTMA provides that the PPR Exemption does not extend to a parcel of residential land that is comprised of 2 or more lots of land that is used and occupied by the owner as a principal place of residence unless:

1. the lots are adjoining; and
2. the lots are in the same ownership; and
3. the lots are the site of a single residence (excluding any additional residential occupancy that may be disregarded under clause 4).

Clause 13(2)(b) provides that for the purposes of clause 13, separate buildings erected on separate lots are not to be regarded as a single residence if the buildings are separately occupied or capable of being used for separate occupation.

Clause 4(1) to Schedule 1A of the LTMA provides that an occupancy may be disregarded if the residential occupancy is an excluded residential occupancy. Clause 4(4) provides that if land is comprised of two or more lots, the excluded residential occupancy must be located on a lot that is also used and occupied by the owner of the land for residential purposes.

Clause 10B to Schedule 1A of the LTMA provides for a concession to apply where 'land' owned by a person is the site of a 'flat' that is used and occupied by the owner as a PPR and there is also situated on the land one or more other flats that are used, or adapted for use, as a separate occupation to that of the owner. If clause 10B applies, section 9C of the LTMA applies to reduce the taxable value of the land in respect of the proportion of the land occupied by the owner's flat.

The Chief Commissioner contended that Sonja was neither entitled to a PPR Exemption or a concession under clause 10B in respect of Number 38.

During the NCAT proceedings, Sonja provided evidence of a Google Maps aerial photograph of the Properties. She also provided some photos of Number 38 and a short video of a person exiting Number 36 which led out to the annex, crossing the annex and entering Number 38.

Sonja did not provide any photographs of the Properties during the Relevant Years, including the annex.

Issues

1. Were the Properties the site of a single residence pursuant to clause 13 of Schedule 1 to the LTMA?
2. If so, were the Properties together used and occupied by Sonja as her principal place of residence during the Relevant Years?
3. If the answer to questions (1) and (2) is Yes, was the occupancy of Number 38 by tenants an excluded residential occupancy for the purposes of clause 4(1) of Schedule 1 of the LTMA?
4. If the answer to either questions (1) or (2) is No, was the concession in clause 10B in respect of multi-occupancy land available?

Decision

Issues 1 to 3

The NCAT noted Sonja's assertion that, while the Properties were originally separate buildings, the construction of an annex created one interconnected building. The NCAT agreed with the Chief Commissioner that the evidence tendered by Sonja, or the lack of photographic evidence of the physical structure during the Relevant Years, was not sufficient to discharge her burden of proof.

Namely, there was no evidence as to the dimensions of the annex, photographs of the annex during the relevant Years or corroborative evidence from other witnesses (e.g., evidence from tenants, friends or family).

Sonja also submitted that she built an extension of her living space. However, there was no evidence of an internal configuration of Number 36 and Number 38, and no evidence as to the internal layout of Number 36.

The NCAT concluded that during the Relevant Years, separate buildings erected on Number 36 and Number 38 were separately occupied or capable of being used for separation occupation such that, the Properties were not to the site of a single residence.

Given this conclusion, there was no need for the NCAT to determine whether Sonja used the Properties together as her principal place of residence, or to determine whether the occupation of Number 38 by tenants was an excluded residential occupancy for the purposes of clause 4(1) of Schedule 1A to the LTMA.

Issue 4

The NCAT determined that there was no basis for Sonja to be granted a concession under clause 10B in respect of Number 38.

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The NCAT noted that Sonja had an exemption for Number 36 as it was her principal place of residence. However, the NCAT stated that Sonja failed to provide evidence that the parts of the land at Number 38 which Sonja had exclusive access to (e.g., garden and shed) could be a 'flat' as defined in section 3 of the LTMA.

The Chief Commissioner's decision was affirmed.

Citation *Bennett v Chief Commissioner of State Revenue* [2022] NSWCATAD 324 (Senior Member S Dunn, Sydney)
w http://www.austlii.edu.au/cgi-bin/viewdoc/au/cases/nsw/NSWCATAD/2022/324.html

1.12 Appeal Update – Bosanac

The High Court has allowed the appeal of Bernadette Bosanac from the decision of the Full Federal Court that she held 50% of her interest in a property on resulting trust for her former husband, Vlado (see our April 2021 and September 2021 Tax Training Notes).

The case involved the ownership of the matrimonial home of Vlado and Bernadette, of which Bernadette was the sole registered proprietor. Vlado was an undischarged bankrupt and owed money to the Commissioner of Taxation at the time of his bankruptcy. The Commissioner sought a declaration that Bernadette held 50% of her interest in the home on trust for Vlado.

Bernadette contended that she owned the whole of the home legally and beneficially and relied upon the presumption of advancement – this is a rule of equity that provides that, in respect of certain relationships, a benefit conferred on one person by another person, such as contributing to the purchase price of a property acquired solely in the first person's name, will not give rise to a presumption that the first person holds the property, or part of it, on resulting trust for the second person.

The 'presumption' of advancement applies to benefits conferred by a husband on his wife (but not vice versa and not with respect to de facto relationships) or by a parent to a child.

The Commissioner contended that the principle in *Cummins* qualifies the presumption of advancement in relation to matrimonial property.

At first instance, the Federal Court considered that *Cummins* had not changed the presumption of advancement as it applied to the matrimonial home and, accordingly, found that Bernadette did not hold any interest in the home on trust for Vlado.

The Commissioner appealed to the Full Federal Court.

The Full Federal Court allowed the Commissioner's appeal. The Full Court did not accept that the High Court in *Cummins* had qualified the presumption of advancement. However, it noted that the presumption of advancement can be rebutted and that in *Cummins* the High Court was noting that, if certain facts exist, as was referred to in *Cummins*, it may be inferred that a trust was intended. In this case, the Full Federal Court considered that the presumption of advancement was rebutted given the following:

1. the circumstances involved a substantial borrowing by Vlado. He was liable for the loan but did not have legal title to the asset purchased with the loan. The Full Court considered that the significance of this transaction permitted a drawing of an inference of a trust consistent with Cummins;
2. Vlado later used the property as security for other borrowings;
3. neither Vlado nor Bernadette gave evidence on the circumstances of the purchase of the home;
4. Vlado and Bernadette purchased the property to be their matrimonial home and made it their family home shortly afterwards; and
5. the whole of the purchase price was paid from joint borrowings.

Bernadette appealed to the High Court.

The High Court allowed Bernadette's appeal.

The High Court noted that there two presumptions – being the presumption of advancement and the presumption of resulting trust but that the role of the presumptions is to determine the intention of the parties. Given this role, the presumptions only have a role to play where the intention of the parties is unclear from the totality of the evidence.

The High Court refused an invitation from the Commissioner of Taxation to abolish the presumption of advancement, noting that it is an entrenched landmark of Australian law.

Citation *Bosanac v Commissioner of Taxation* [2022] HCA 34 (Kiefel CJ, Gageler, Gordon, Edelman and Gleeson J, Perth)
w https://eresources.hcourt.gov.au/downloadPdf/2022/HCA/34

1.13 Other tax and superannuation related cases from 7 September 2022 – 12 October 2022

Citation	Date	Headnote	Link
Signium Pty Limited and Commissioner of Taxation (Taxation) [2022] AATA 2824	5 August 2022	SUPERANNUATION guarantee charge assessments – penalty assessments – whether penalty assessments excessive – nominal interest of superannuation guarantee charge – superannuation shortfall assessments – decision under review varied	https://www.austlii.edu.au/cgi-bin/viewdoc/au/cases/cth/AATA/2022/2824.html
Lin & Ors v Lin & Ors (No 2) [2022] VSC 542	16 September 2022	TRUSTS – Appointment of appointor of two discretionary trusts – Validity of deeds of appointment of appointor – Interpretation of trust deed – Principles of construction of trust deed – Plain and ordinary meaning of words used in trust deed – Byrnes v Kendle [2011] HCA 26; (2011) 243 CLR 253 – Schreuders v Grandiflora Nominees Pty Ltd [2016] VSCA 93.	http://www.austlii.edu.au/cgi-bin/viewdoc/au/cases/vic/VSC/2022/542.html
Shah v Chief Commissioner of State Revenue [2022] NSWCATAD 311	23 September 2022	TAXES AND DUTIES – surcharge purchaser duty – foreign person – presence in Australia subject to limitation as to time imposed by law – interest remission – penalty remission	https://www.caselaw.nsw.gov.au/decision/1835d7c26c6df9a5f68e80ed
Deputy Commissioner of Taxation v GTGF Australia Ltd (receivers and managers appointed) [2022] FCA 1148	26 September 2022	TAXATION – interlocutory application for summary judgment on taxation debts – notices of assessment in respect of assessed taxation debts and administrative penalties are conclusive – running balance account statements confirmed by certificates are prima facie correct – no defences with reasonable prospects of success raised – summary judgment entered	http://www.austlii.edu.au/cgi-bin/viewdoc/au/cases/cth/FCA/2022/1148.html
Chambers v Commissioner of Taxation [2022] FCA 1163	30 September 2022	SUPERANNUATION – Application for review of decision of Commissioner of Taxation – where AAT found that the decision was not reviewable by the Tribunal under s 25 of the Administrative Appeals Tribunal Act 1975 (Cth) – whether Tribunal erred in refusing to remit the matter to Commissioner for redetermination – where applicant contends decision is reviewable under s 20P of the Superannuation (Unclaimed Money and Lost Members) Act 1999 (Cth) – where s 20P does not operate to make decision reviewable under s 25 of AAT Act – where applicant alleged apprehended bias on part of President of AAT – where no such bias established – proceeding dismissed	http://www.austlii.edu.au/cgi-bin/viewdoc/au/cases/cth/FCA/2022/1163.html

2. Legislation

2.1 Progress of legislation

Title	Introduced House	Passed House	Introduced Senate	Passed Senate	Assented
Treasury Laws Amendment (2022 Measures No. 2) Bill 2022	3/8	26/9	26/9		
Treasury Laws Amendment (2022 Measures No. 3) Bill 2022	8/9				
Treasury Laws Amendment (Electric Car Discount) 2022	27/7	8/9	8/9		

2.2 TLAB 3 2022

On 8 September 2022, *Treasury Laws Amendment (2022 Measures No. 3) Bill 2022* was introduced into Parliament. The bill is intended to make a number of changes to various laws, including:

1. amending the *Foreign Acquisitions and Takeovers Act 1975* (Cth) to double the maximum financial penalties for contraventions of provisions that relate only to residential land;
2. amending the TAA 1953 to allow protected information to be disclosed to Australian government agencies for the purpose of administering major disaster support programs approved by the Minister; and
3. making make amendments to reduce the tax rate on certain income earned by foreign resident workers participating in the Pacific Australia Labour Mobility scheme from marginal rates starting at 32.5 per cent to a flat 15 per cent.

2.3 FBT Exposure Draft Legislation – record keeping

The *Treasury Laws Amendment (Measures for Consultation) Bill 2022: FBT record keeping* has been released for public consultation.

The proposed legislation gives the Commissioner the power to modify, by legislative instrument, existing FBT record keeping obligations to allow employers to rely on existing corporate records, to finalise their FBT returns where the Commissioner considers the alternative records adequate. This is to provide an alternative to employers to preparing employee declarations and other FBT prescribed records.

In addition, exposure draft legislative instruments dealing with travel diaries (*Fringe Benefits Tax Assessment – Adequate Alternative Records (Travel Diaries) Determination 2022*) and relocation transport expense payments (*Fringe Benefits Tax Assessment – Adequate Alternative Records (Relocation Transport) Determination 2022*) have also been released for public consultation. These legislative instruments also prescribe adequate alternative records for the purposes of keeping travel diaries and transport expense payments.

Treasury Laws Amendment (Measures for Consultation) Bill 2022: FBT record keeping
Fringe Benefits Tax Assessment – Adequate Alternative Records (Travel Diaries) Determination 2022
Fringe Benefits Tax Assessment – Adequate Alternative Records (Relocation Transport) Determination 2022
w https://treasury.gov.au/sites/default/files/2022-09/c2022-316648-draft-bill_0.pdf
https://treasury.gov.au/sites/default/files/2022-09/c2022-316648-draft-relocation-transport-instrument.pdf
https://treasury.gov.au/sites/default/files/2022-09/c2022-316648-draft-travel-diaries-instrument.pdf

2.4 Unfrankable distributions

The Government has released draft legislation, the *Treasury Laws Amendment (2022 Measures for a later sitting) Bill 2022,* which seeks to give effect to integrity measures announced as part of the 2016-17 Mid-Year Economic and Fiscal Outlook. These measures prevent the distribution of franking credits where a distribution to shareholders is funded by particular capital raising activities.

The Bill proposes to amend the ITAA 1997 by adding distributions funded by capital raising to the list of distributions that are unfrankable.

The Bill provides that a distribution by an entity is funded by capital raising if, broadly:

1. the distribution is not consistent with an established practice of the entity of making distributions of that kind on a regular basis. The following matters must be taken into account when determining whether an entity has a practice of making distributions of a certain kind on a regular basis:
   (a) the nature of the distributions before the relevant distribution was made;
   (b) the timing of such distributions;
   (c) the amount of such distributions;
   (d) any explanations given by the entity for making such distributions;
   (e) the amount of the franking credits on, and the franking percentages for, such distributions;
2. there has been an issue of equity interests in the entity or another entity; and
3. it is reasonable to conclude in the circumstances that either:
   (a) the principal effect of the issue of any of the equity interests was to directly or indirectly fund some or all of the distribution (*principal effect test*); or
   (b) any entity that issued or facilitated the issue of any of the equity interests did so for a purpose (other than an incidental purpose) of funding the distribution or part of the distribution (*purpose test*).

The Bill identifies a number of matters that must be take into account when determining the principal effect of the issue of equity interests of the purpose of an entity involved in an issue of equity interests. These matters include:

1. the extent to which the time (or times) at which any of the equity interests were issued differs (or differ) from the time at which the relevant distribution was made;
2. the extent to which the amount of the funds from the issue of any of those equity interests differs from the amount of the relevant distribution;
3. the extent to which the financial position particular entities changed as a result of the relevant distribution (or any part of the relevant distribution) and the issue of any of those equity interests:
   (a) the entity that made the relevant distribution;
   (b) an entity that, before, at or after the time at which the relevant distribution was made, was a connected entity of that entity;
4. the use of the funds from the issue of any of those equity interests;
5. whether there are any reasons for the issue of any of those equity interests other than the funding the relevant distribution (or any part of the relevant distribution);
6. the extent to which the issue of any of those equity interests was underwritten (whether formally or informally);
7. other distributions (if any) made by the entity that made the relevant distribution (whether before, at or after the time at which the relevant distribution was made);
8. any other relevant consideration.

The measures, once law, are intended to operate with respect to distributions after 12 noon, ACT time, 19 December 2016.

w https://treasury.gov.au/consultation/c2022-314358

2.5 Labor signals delay to franked dividend hit

The Australian Financial Review has reported that the ALP is considering delaying the start date for the proposed change to franking of franked dividends funded from capital raisings.

Originally it was intended that the changes would apply from December 2016, being when the changes were first announced by the former Liberal government.

w https://www.afr.com/policy/tax-and-super/labor-signals-delay-to-franked-dividend-hit-20221005-p5bn97

2.6 Excluded classes of transactions and entities for third party reports on shares and units

Certain market participants, listed companies and trustees are required to report to the ATO on transfers of their shares and units by investors. Some classes of transactions are exempted from the reporting requirements by the determination of the Commissioner.

Determination LI 2022/30 was made by the Deputy Commissioner under subsection 396-70(4) of Schedule 1 to the *Taxation Administration Act 1953* (Cth). LI 2022/30 repeals *Excluded Classes of Transactions and Entities for Third Party Reports on Shares and Units Determination 2018* (F2018L00473). LI 2022/30 applies with retrospective effect and commences on 1 July 2017.

LI 2022/30 maintains all the exemptions from F2018L00473 and contains two additional exemptions being:

1. in relation to erroneous transactions that have been reversed; and
2. where a company has shares listed for quotation on both an Australian financial market and a foreign financial market, only the off-market transactions relating to the shares listed for quotation on the official list of an Australian financial market need to be reported.

Entities to which LI 2022/30 applies

LI 2022/30 applies to the following entities:

1. companies with shares listed for quotation on the official list of an Australian financial market;
2. trustees of a unit trust; and
3. trustees of a trust (other than a unit trust) with shares held in a company or units in a unit trust to which one or more beneficiaries of the trust are absolutely entitles, in relation to the transactions in an income year for which the trustee does not give the Commissioner of Taxation an income tax return.

TIP – this is the instrument that provides that the trustee of a unit trust does not need to report changes in unit holdings to the ATO if it has both fewer than 10 unit holders and less than $5 million in market value of assets.

ATO Legislative Instrument LI 2022/30
w https://www.ato.gov.au/law/view/document?docid=ops/li202230/00001
w https://www.ato.gov.au/law/view/document?docid=ESO/ESLI202230/00001

2.7 Draft Legislative Instrument – Margin Scheme valuations

The ATO has published a draft legislative instrument LI 2022/D14 that is intended to replace the current determination (*New Tax System (Goods and Services Tax) Margin Scheme Valuation Requirements Determination 2020* (F2020L00346)).

Among other things, the draft instrument adds new requirements that the valuation must include:

1. the name and effective date of all professional standards recognised in Australia for the making of real property valuations as advised by the valuer's accrediting professional industry body and that were complied with by the valuer; and
2. a signed declaration that the valuation has been undertaken in accordance with all the legal and professional standards in Australia for the making of real property valuations, that are effective at the date of issue of the valuation.

There is to be a transitional rule that a valuation that complies with the former legislative instrument will still be valid in determining the margin for property sales occurring up to 3 months after the new instrument is effective.

The draft is open for consultation until 12 October 2022.

ATO Legislative Instrument LI 2022/D14
w https://www.ato.gov.au/law/view/document?docid=OPS/LI2022D14/00001
w https://www.ato.gov.au/law/view/document?docid=ESO/ESLI2022D14/00001

2.8 WA – land tax amendments

The *Land Tax Assessment Amendment Bill 2022* (WA) seeks to amend the *Land Tax Assessment Act 2002* (WA) to:

1. replace the existing caravan park land tax exemption with a new caravan park and residential park land tax exemption;
2. provide a new land tax exemption for homeowners living in full-time care; and
3. introduce a general notification requirement for landowners.

New caravan park and residential park land tax exemption

The existing caravan park land tax exemption is only available for 'dwelling park land', being land that 'is, or is part of, a caravan park or camping ground' and is either operated pursuant to the *Caravan Parks and Camping Grounds Act 1995* (WA) or by a local government, and is 'used solely for dwelling park purposes'. The new land tax exemption provides an exemption from land tax for parks that provide low-cost holiday accommodation (such as caravans and camp sites), sites used as a person's primary residence or a mixture of both.

A full exemption from land tax will apply to a park if:

1. the park provides short-stay holiday accommodation only and at least 75% of the park sites are caravan or camp sites;
2. the park provides long-stay accommodation for permanent residents only and at least 75% of the park sites are owner-occupied sites subject to a site-only agreement; and
3. the park provides a combination of both short-stay and long-stay accommodation and at least 75% of the short-stay sites are caravan or camp sites and at least 75% of the long-stay sites are owner-occupied sites subject to a site-only agreement.

A proportional exemption from land tax may be available if the 75% threshold requirement is not met.

If the Bill is passed, this amendment will have retrospective effect from 1 July 2020.

Home owners living in full-time care

The Bill provides an exemption from land tax if the owner of a residential property has moved into a full-time care facility and their property is not rented. If the Bill is passed, this amendment will have retrospective effect from 1 July 2020.

General notification requirement for landowners

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The Bill introduces a general notification requirement for landowners if they receive an exemption from land tax or a concession. The Commissioner will first be required to notify landowners if an exemption or concession applies to their land and set out the events or circumstances which may affect the exemption of concession. The landowners will then be required to notify the Commissioner of an occurrence of an event or circumstances which may affect their exemption from land tax or concession.

If the Bill is passed, this amendment will commence on the day after the Royal Assent.

w https://www.parliament.wa.gov.au/parliament/bills.nsf/538CE0798AB1D424482588C3000DAC85/$File/Bill%2B85-1.pdf

2.9 ACT – land tax changes

The *Taxation Administration (Amounts Payable—Land Tax) Determination 2022* has been issued which sets out how the land tax rates and foreign ownership surcharge in the ACT will be determined from 1 October 2022.

The Determination states that land tax is made up of a fixed charge of $1,462 (a 5% increase from 2021-2022), and a specified marginal rating (remains unchanged from 2021-2022).

The rate of the foreign ownership surcharge remains unchanged from the previous year, being 0.75% of the property's base value.

The Determination revokes the previous determination which continues to apply for the period 1 July 2021 to 30 September 2022.

Taxation Administration (Amounts Payable—Land Tax) Determination 2022
w https://www.legislation.act.gov.au/di/2022-218

2.10 Queensland land tax scrapped

On Friday 30 September 2022, the Queensland Premier, Ms Palaszczuk announced she would scrap the amendments to the land tax legislation which sought to calculate how much a Queensland property owner owed in land tax based on the total value of all properties they owned in Australia.

w https://www.afr.com/politics/palaszczuk-scraps-controversial-qld-land-tax-change-20220930-p5bm82

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3. Rulings

3.1 Use of an individual's fame by related entities

The ATO has released *Draft Taxation Determination* TD 2022/D3 regarding the use of an individual's fame by related entities.

The draft Determination applies to arrangements where an individual with fame enters into an agreement with a related entity (such as a discretionary trust or company) for the use of the individual's name, image, likeness, identity, reputation and signature. The related entity then enters into contracts with third parties, authorising the use of the individual's fame for a fee.

The draft Determination is only concerned with the income that arises from the use of the individual's fame. Importantly, it does not apply to income derived by a related entity where an individual is engaged by the related entity to provide services to a third party. It also does not apply to fees earned by a related entity from exploiting copyright, trademark or registered design rights licensed to the entity.

The draft Determination provides that an individual with fame has no property in that fame and, therefore, cannot transfer that fame to another entity. As such, a related entity that is party to an agreement cannot authorise the use of the individual's fame and derive fees. The fees paid for the use of the fame is assessable to the individual as ordinary income under section 6-5 of the ITAA 1997.

The draft Determination notes that, while there is no proprietary right in the fame, an individual may have a limited cause of action if the use of their image misleads the public.

In 2017 the ATO released PCG 2017/D11 which accepted that up to 10% of a person's income from exploiting their fame could be alienated to a related entity. This guidance was however withdrawn on 24 August 2018 when the then Government announced it would legislate in relation to the alienation issue. In recognition of the 2017 guidance the draft TD states that someone who structured their arrangement in accordance with that PCG up to 5 October 2022 (the date the draft determination was released) will not have compliance activity applied to them in relation to the 2019 – 2023 income years. In relation to people not structured in accordance with PCG 2017/11 the draft Determination is to have effect for all income years.

The draft Determination is open for comment until 4 November 2022.

COMMENT – this matter was to be dealt with by way of legislation. Presumably the ATO draft determination means that Treasury will no longer be proceeding with a change to the law.

It is interesting that the ATO view is that a related entity cannot derive income from exploiting another's fame, when clearly, as a matter of contract, that can occur.

ATO reference *Draft Taxation Determination TD 2022/D3*
w https://www.ato.gov.au/law/view/document?DocID=DXT/TD2022D3/NAT/ATO/00001

3.2 Residency tests for individuals

The ATO has published a *Draft Taxation Ruling* TR 2002/D2 on the residency tests for individuals. The draft Ruling replaces IT 2650 and TR 98/17.

The draft Ruling was prepared to update the ATO's public position to reflect recent developments in case, including the decisions in *Harding v Commissioner of Taxation* [2019] FCAFC 29, *Pike v Commissioner of Taxation* [2019] FCA 2185 (**Pike**) and *Addy v Commissioner of Taxation* [2019] FCA 1768 (**Addy**).

The draft Ruling notes that there are four tests for residency of individuals, being the ordinary concepts test, the domicile test, the 183-day test and the Commonwealth superannuation fund test.

The draft Ruling covers the residency tests for individual other than the Commonwealth superannuation fund test.

Ordinary concepts test

The ATO notes that this test considers where a person resides within the ordinary meaning and that the question is whether a person's presence in Australia is usual and settled in contrast to temporary and casual.

The ATO notes that in determining this, the following factors are relevant and that all factors need to be considered:

- period of physical presence in Australia – the ATO notes that the length of time is relevant but not determinative as there is a distinction between staying in Australia (which is normally insufficient) and residing here. The ATO notes that ordinarily a stay of less than 6 will not be sufficient to establish residency;

- intention or purpose of presence – the ATO notes that the question is whether a person has a settled presence in Australia and that staying for work for a short period is not usually sufficient. The ATO notes that objectively observable evidence, such as passenger cards and visa documents, are relevant but not determinative. In terms of subjective intention, the ATO states as follows:

  > *35. Importantly, subjective intention is not decisive and its significance and weight will depend on the circumstances. Residency is not established merely by asserting an intention to live in Australia permanently. Similarly, residency is not shed when departing Australia, merely asserting an intention to never live in Australia again.*

  The ATO also notes that your future intention to reside overseas will not cause you to cease residing in Australia. The ATO cites a transition arrangement as an example of this where the family stays in Australia while one spouse starts spending time overseas with the intention that whole family will move eventually;

- behaviour while in Australia – the ATO notes that it is relevant whether your behaviour indicates that intention to stay here as part of the regular order of live. For example, enrolling kids in school and taking up long-term accommodation;

- family, and business or employment ties – on this point, the ATO notes as follows:

  > *47. Generally speaking, working overseas but returning to Australia at intervals to resume a pre-existing, established family and social life will often mean you are still residing in Australia.[29] This is the case even if you spend more time overseas than in Australia in any given income year.*

- maintenance and location of assets – on this point the ATO notes as follows:

  > *Australian bank accounts held open while you are located overseas could be consistent with maintaining a continuity of association with Australia but could also be the result of there being no pressing reason to close them.*

- social and living arrangements.

Domicile test

The ATO notes that under the domicile test, a person a resident unless the Commissioner is satisfied the person has a permanent place of abode outside of Australia.

The ATO notes that a person's domicile will be their domicile of origin unless they have made a domicile of choice, which requires both lawful physical presence in a foreign country and an intention to make a home indefinitely in that country.

The ATO notes that even living outside of Australia for a substantial period may not be sufficient to acquire a domicile of choice if a person intends to return to Australia on an event happening, such as an employment contract ending.

In terms of permanent place of abode, the ATO notes as follows:

1. permanent does not mean everlasting or forever but is in contrast to temporary or transitory;
2. a permanent place of abode is not based on a particular dwelling but refers to the location of where a person lives i.e. a town or country;
3. for practical purposes, a person must intend to reside in a place for 2 or more years for it to be their permanent place of above but whether that is sufficient depends upon the circumstances;
4. a nature of a person's accommodation is relevant as it indicates whether the presence is permanent; and
5. retaining accommodation in Australia is relevant but it will depend what use is made of the accommodation. It will have reduced significant if the home is rented out to arm's length parties. If the home remains available, it will assume significance.

183-day test

The ATO notes that the 183-day test provides that a person is a resident if they have been present in Australia for 183 days or more in an income year, unless the Commissioner is satisfied that both the usual place of abode of the person is overseas and the person does not intend to take up residency in Australia.

The ATO accepts that a person could be in Australia for more than 183-days in a number of continuous income years if they have a usual place of abode outside of Australia and do not intend to take up residence as 'intend to take up residence' does not simply mean an intention to stay for a long time.

Part year residency

The ATO notes that a person is not necessarily a resident for the entire income year if they only spend part of the year in Australia

The Draft Ruling provides a number of examples on the ATO's view as to the application of the three residency tests.

Self-assessment

The exceptions in the domicile test require that the "Commissioner be satisfied". In *Addy,* it was held that this required the Commissioner to have the requisite state of mind. However, the ATO considers that in certain circumstances taxpayers can self-assess the availability of the exclusions. For example, if a person is in Australia on a holiday for more than 183 days, they can self-assess whether they have a usual place of abode outside of Australia and that they do not intend to become a resident.

Further, if a person has an Australian domicile but has indefinitely abandoned Australia to live in an overseas country or town, they can self-assess that they have a permanent place of abode outside of Australia.

The Draft Ruling is open for comments until 25 November 2022.

ATO reference *Draft Taxation Ruling* TR 2022/D2
w https://www.ato.gov.au/law/view/document?docid=DTR/TR2022D2/NAT/ATO/00001

3.3 Non-contingent liabilities and cost base

The ATO has finalised a Taxation Determination on the following question:

> *If a non-contingent liability to pay a specified amount is included in the cost base of your CGT asset under either subsection 110-25(2) or section 112-35 of the ITAA 1997 and you deduct or can deduct that amount, does subsection 110-45(2) of the ITAA 1997 apply?*

Section 110-45(2) of the ITAA 1997 provides as follows:

> *Expenditure (except expenditure excluded by subsection (1B)) does not form part of the cost base to the extent that you have deducted or can deduct it for an income year, except so far as …*

The ATO answers that yes, to the extent that a contingent liability has been deducted or can be deducted, the amount will not form part of the cost base of the assets, unless it falls within one of the exceptions.

The ATO does note that a 'contingent liability' includes a loan or other debt but does not include an inchoate liability subject to a variety of contingencies, such as a contractual obligation to pay a person an amount based on future market values when an event occurs.

ATO reference *Taxation Determination* TD 2022/14
w https://www.ato.gov.au/law/view/document?docid=TXD/TD202214/NAT/ATO/00001

3.4 Games and sports exemption

The ATO finalised Taxation Ruling TR 2022/2 on 14 September 2022 which applies to societies, associations or clubs seeking to determine whether they are exempt from income tax under table item 9.1(c) of section 50-45 of the ITAA 1997. The ATO refers to the exemption as the 'games and sports exemption'.

The Ruling was released as draft ruling TR 2021/D6 which was covered in our October 2021 Tax Training Notes. The Ruling has been finalised with only minor changes from the draft ruling and clarifies some examples.

The Ruling provides that a society, association or club will qualify for the games and sports exemption where it:

1. is established for the main purpose of the encouragement of a game or sport;
2. is not carried on for the purposes of its individual members' profit or gain, and
3. meets other special conditions under section 50-70 ('in Australia' or DGR test).

The Ruling clarifies the meaning of the encouragement of a game or sport, and does not deal with the other special conditions, which are dealt with in *Taxation Ruling TR 2015/1 Income tax: special conditions for various entities whose ordinary and statutory income is exempt* and *Taxation Ruling TR 2019/6 Income tax: the 'in Australia' requirement for certain deductible gift recipients and income tax exempt entities*.

Society, association or club

The ATO adopts the ordinary meaning of a 'society, association or club.' An essential requirement is that it must be a voluntary organisation of people associated together for a common or shared purpose. The ATO example considers that a trust will not qualify as a 'society, association or club'.

Non-profit

A society, association or club must not be carried on for the purposes of individual members' profit or gain, either while the club is operating or on its winding up. The most common way this requirement is met is by the

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society, association or club including a not-for-profit clause in its governing documents. If a society, association or club is prohibited from profiting members by statute, it will meet this requirement.

Game or sport

The meaning of game or sport is not defined in legislation and takes on their ordinary meaning. The ATO considers that a common feature of a sport is that there are a set of conventions, expectations and rules.

The meanings of game or sport also extend to:

1. non-athletic activities, such as chess or bridge
2. activities where people use machines to participate, such as motor racing, and
3. non-competitive activities, such as mountaineering.

The ATO notes that a game or sport often involves a competition but that will not necessarily be the case. To qualify as a game or sport, participants must share a common understanding that the activities they perform are the activities of a particular game or sport.

The ATO considers a game or sport can be contrasted with an activity where a thing, object or animal is the essential focus, or the activity is merely a means to an end.

The following examples are considered by the ATO and not being a game or sport:

1. bird-raising, bird-keeping and bird-watching;
2. bodybuilding;
3. car owners' clubs/associations;
4. dancing as a social activity (including ballroom dancing, line dancing, square dancing and Highland dancing);
5. modelling of railways;
6. stamp and coin collecting;
7. playing of gaming or gambling machines and gambling generally, and
8. breeding and showing of animals.

Main purpose established for the encouragement of a game or sport

The main purpose of a society, association or club in the relevant income year must be the encouragement of a game or sport.

Determining the main purpose requires an objective evaluation of all material facts and circumstances.

Relevant considerations include:

1. subjective motives or intentions of the founders or members of the club;
2. stated purpose of a club;
3. the activities and history of the club;
4. how the club is controlled.

It is the main purpose of the club in the year under examination that is the relevant consideration, and not in the year of formation, as the main purpose may have changed over time.

A club that has both sporting and non-sporting purposes will not qualify for the games and sports exemption unless the non-sporting purpose is:

1. merely ancillary and incidental to its sporting purpose; or
2. secondary to its sporting purpose (that is, a purpose that is independent to, but less important than, the sporting purpose).

Direct or indirect activities that indicate the encouragement of a game or sport can include:

1. forming, preparing and entering teams and competitors in competitions in the game or sport;

2. coordinating activities;
3. organising and conducting tournaments;
4. improving the abilities of participants;
5. improving the standard of trainers and coaches;
6. providing purchased or leased facilities for the activities of the game or sport for the use of club members and visitors;
7. encouraging increased and wider participation and improved performance;
8. marketing;
9. initiating or facilitating research and development, and
10. facilitating such activities listed in by making a financial or in-kind contribution to an organisation that performs them.

The Ruling provides various examples of clubs with differing factors.

The Ruling replaces *Taxation Ruling* TR 97/22 which has been withdrawn. The Ruling applies for income year before and after the date of issue.

ATO reference *Taxation Ruling TR 2022/2 Income tax: the games and sports exemption*
w https://www.ato.gov.au/law/view/document?docid=TXR/TR20222/NAT/ATO/00001

3.5 Australian interest income derived by US or UK financial institutions

The ATO has published a draft addendum to Taxation Ruling TR 2005/5 which sets out the circumstances under which US or UK residents will not be subject to tax in Australia on interest income arising in Australia, within the meaning of Article 11(7) of the Australia - United States Double Taxation Agreement or the Australia - United Kingdom Double Taxation Agreement.

The reason for the addendum is to clarify aspects of the definition of 'financial institution' in the DTAs.

The draft addendum is open for consultation with a due date specified as 11 November 2022.

ATO reference *Taxation Ruling* TR 2005/5DC2
w https://www.ato.gov.au/law/view/document?docid=DTC/TR20055DC2/NAT/ATO/00001

3.6 Victorian Duty – economic entitlements in relation to land

The Victorian State Revenue Office has issued *Draft Revenue Ruling* DA-065 to provide clarification on the application of the economic entitlement provisions to ordinary fees for service.

Where a person acquires an 'economic entitlement' in land, the person is taken to have acquired beneficial ownership in the land and duty is chargeable under Chapter 2 of the *Duties Act 2000* (Vic). The interest in the land taken to be beneficially owned under the economic entitlement provisions is also a land holding for the purpose of the landholder provisions in Part 2 of Chapter 3 of the *Duties Act*.

The draft Revenue Ruling confirms that the intention of the economic entitlement provisions is to impose duty on arrangements where a person, without acquiring an ownership interest in land, nevertheless obtains rights and benefits relating to the land that are economically equivalent to ownership interests.

It follows that ordinary fees for service such as real estate agent fees are not considered to be an economic entitlement. The Commissioner considers that these are a genuine fee for service and not a benefit normally reserved for the owner of the land. Other examples of fees for service include architect fees, project managers, planning consultants, private advisory firms and lenders and financiers.

Therefore, where a person providing a genuine service in relation to land:

1. is normally engaged in a full-time capacity in providing those services;
2. the agreed fee/rate is within industry parameters; and
3. the person is unconnected to any other person who has an economic entitlement in relation to the land,

then it is unnecessary for the service agreement to be disclosed to the Commissioner by the service provider.

Where the service provider is associated with a person who has acquired an economic entitlement in relation to land, the draft Revenue Ruling clarifies that the fee for service must be disclosed to the Commissioner, and evidence is to be provided that the service fee was a genuine fee for service.

In relation to the acquisition of shares and units, where the entitlement to income, rents, profits, capital growth or proceeds of sale is general in nature and not specific to particular land held by the entity, the economic entitlement provisions in relation to land would not apply.

The draft Revenue Ruling is closed for consultation and is in the process of being reviewed.

SRO Reference *Draft Revenue Ruling* DA-065 (Vic), *Land transfer duty – Acquisition of economic entitlements in relation to land (service fees)*
w https://www.sro.vic.gov.au/land-transfer-duty-acquisition-economic-entitlements-relation-relevant-land-service-fees

4. Private Binding Rulings

4.1 Income from sportsperson as PSI, subject to income averaging

Facts

A sportsperson has generated income by partaking in competitions and winning prize money, making guest appearances, attending speaking engagements, providing interviews on TV and radio, and through sponsorship endorsements.

The sportsperson had previously established a trust.

Since settlement, all income earning activities have been conducted through the trust, and the Trust distributes all income to the sportsperson. No salary or wages are paid by the trust to the sportsperson.

The Trust did not meet the requirements to be considered to be a personal services business.

Question

Do the income averaging rules under Division 405 of the ITAA 1997 apply to the taxpayer in relation to the assessable professional income earned?

Decision

Ordinary or statutory income of another entity that is mainly a reward for the taxpayer's personal efforts or skills will be the taxpayer's personal services income under subsection 84-5(1) ITAA 1997. The ATO ruled that in the present circumstances, the income earned by the trust is mainly a reward for the sportsperson's personal effort or skills and will be classified as PSI.

The ATO ruled that a trust meets the definition of a personal services entity under subsection 86-15(2). Unless the personal services entity is conducting a personal services business, the income it derives must be included in the individual's assessable income.

Income averaging

As the personal services entity was not conducting a personal services business, the PSI alienation rules will apply under Division 86 of the ITAA 1997. The ATO determined that to the extent that the income derives is PSI, it will be attributed to the sportsperson in their individual tax return under 86-15(1) of the ITAA 1997.

Division 405 of the ITAA 1997 allows special tax rates to apply to certain above average special professional income. A sportsperson falls within the definition of a special professional under section 405-25(1). Therefore, the sportsperson's assessable professional income, defined under section 405-50 including prize money and income from promotions or commentary (such as guest appearances, speaking engagements and interviews on TV and radio), will be taxed at the special rates under Division 405.

ATO reference *Private Binding Ruling* Authorisation Number 1051991200162
w https://www.ato.gov.au/law/view/document?docid=EV/1051991200162

4.2 Assessability of gains derived from holding revenue assets

Facts

Company X is a resident for tax purposes and is listed on the ASX. Company X carries on a business and its main activities are the investment of cash and securities for short term trading, profit making ventures, holding securities for long term capital appreciation and dividend returns and generating an on-going return.

Regarding its revenue assets (other than trading stock), Company X invests in:

1. units in unit trusts in which Company X receives tax deferred distributions not assessable to Company X under section 97 of the ITAA 1936; and
2. shares in companies in which Company X receives return of share capital, which is not assessable to Company X under section 44 of the ITAA 1936.

To date, Company X has treated the tax deferred distributions and capital returns as ordinary income and assessable under section of 6-5 of the ITAA 1997 at the time of receipt. The initial cost of the investments is taken into account in working out the gain or loss on disposal of the units or shares.

Question

Will the tax deferred distributions and capital returns received by the Company X be assessable to the Company X under section 6-5 of the ITAA 1997?

Decision

Section 6-5(1) provides that the assessable income of a resident entity includes income according to ordinary concepts. The ATO noted that what constitutes 'income according to ordinary concepts' has been developed through caselaw. In *Scott v Federal Commissioner of Taxation [1966] HCA 48* Windeyer J said that whether or not a particular receipt is income depends upon its quality in the hands of the recipient.

In *Federal Commissioner of Taxation v Myer Emporium Ltd* [1987] HCA 18 the High Court noted:

> *Because a business is carried on with a view to profit, a gain made in the ordinary course of carrying on the business is invested with the profit-making purpose, thereby stamping the profit with the character of income. But a gain made otherwise than in the ordinary course of carrying on the business which nevertheless arises from a transaction entered into by the taxpayer with the intention or purpose of making a profit or gain may well constitute income*

The ATO referred to its *Taxation Ruling* TR 92/3 where the Commissioner ruled that if a taxpayer carrying on a business makes a profit from a transaction, that profit is income if the transaction is in the ordinary course of the taxpayer's business. TR 92/3 also provides that profits or gains made in the ordinary course of carrying on a business could be either a profit or gain arising from a transaction which is itself a part of the ordinary business of the taxpayer, or a profit or gain arising from a transaction which is an ordinary incident of the business activity of the taxpayer.

The ATO also referred to its Taxation Ruling TR 96/4 and the cases of *Colonial Mutual Life Assurance Society Ltd v Federal Commissioner of Taxation* [1946] HCA 60 and *Chamber of Manufacturers Insurance Ltd v The Commissioner of Taxation of the Commonwealth of Australia* [1984] FCA 119, which all share the principle that in instances where the investments such as shares are held by banks, the shares held are generally considered to be revenue assets, but not trading stock.

The ATO determined that Company X is an active investment company with one of its main activities being investment for profit. There is clearly a profit-making purpose, being an ordinary incident in the carrying on of its investment business. Therefore, the tax deferred distributions and capital returns are characterised as being on revenue account and should be included in Company X's assessable income under section 6-5.

TIP – if the tax-deferred amounts trusts are not ordinary income they would cause CGT event E4 to occur. If the capital amounts from companies are not ordinary income they would cause CGT event G1 to occur, which has the same effect as CGT event E4.

ATO reference *Private Binding Ruling* Authorisation number 1051980050896
w https://www.ato.gov.au/law/view/document?docid=EV/1051980050896

4.3 Deductions for foreign rental property

Facts

The taxpayer is a tax resident of Australia. The taxpayer owns a rental property in a foreign country and has derived income from the property.

A valuation report was prepared by a foreign professional practice in the foreign country for the whole of the building. The purpose of the report was to estimate construction costs of the building for depreciation purposes.

The cost of the valuation was able to be apportioned. The taxpayer incurred expenses for the taxpayer's share of the valuation.

Question

Is the taxpayer entitled to deduct the share of the expenses incurred in obtaining a valuation report for the foreign property?

Decision

The ATO ruled no. The purpose of the valuation was to determine the quantum of construction costs. The expenditure does not have a sufficient nexus to the gaining of assessable income. The taxpayer is not entitled to a deduction for the expenses under section 8-1 of the ITAA 1997.

The taxpayer is also not entitled to a deduction under section 25-5 of the ITAA 1997 for the costs of managing their tax affairs. Section 25-5(2)(e) of the ITAA 1997 provides that expenditure relating to advice about the operation of a tax law must be provided by a recognised tax adviser to be deductible.

The ATO stated that Australian quantity surveyors are required to register with the Tax Practitioners Board in order for their fees relating to depreciation and capital works deductions to be deductible. The foreign professional practice is not registered with the Tax Practitioners Board.

COMMENT – it is difficult to understand how a valuation report is considered to be advice about the operation of a tax law, so that the costs here should be deductible under section 25-5.

ATO Reference *Private Binding Ruling* Authorisation Number: 1051974941962
w https://www.ato.gov.au/law/view/document?docid=EV/1051974941962

4.4 Downsizer eligibility for land more than 2 hectares

Facts

The taxpayer acquired the Property with their spouse in 19XX.

The Property was the main residence of the taxpayer since 19XX. The Property comprises XX acres of land and the farming area was used in a primary production business to produce assessable income.

The Taxpayer sold the Property and the interest in the Property is sufficient to fund the maximum downsizer contribution of $XXX. The proceeds from the sale of the Property were exempt or partially exempt from capital gains tax under the main residence exemption.

The following assumptions were applied:

1. the Taxpayer has not previously made a downsizer contribution;
2. the Taxpayer will make the downsizer contribution within the prescribed time; and
3. the Taxpayer will provide the relevant complying superannuation fund with the Downsizer contribution into super form either before or at the time of making the downsizer contribution.

Question

Is the Taxpayer eligible to make a downsizer contribution into superannuation utilising the proceeds from the sale of the Property which exceeds the value attributable to the principal residence and surrounding area of 2 hectares?

Decision

The ATO has published Law Companion Ruling 2018/9 - H*ousing affordability measures: contributing the proceeds of downsizing to superannuation* (**LCR 2018/9**) which describes how the Commissioner will apply the downsizer requirements in section 292-102 of the ITAA 1997.

Paragraph 50 of LCR 2018/9 states that for the purpose of making a downsizer contribution, it is not relevant how the main residence exemption is calculated or apportioned. The downsizer contribution amount available relates to the proceeds from the disposal of the interest in a dwelling and does not depend on the extent to which the amount is exempt as a main residence for CGT.

Given that the Property was subject to the partial main residence CGT exemption as it exceeded 2 hectares and was the main residence of the Taxpayer, the entire sale proceeds from the disposal of the Property can be utilised to finance the downsizer contributions.

The maximum amount of the contributions is the lesser of either $300,000, or the proceeds from the sale of the interests in the dwelling. The Taxpayer was therefore eligible to make a downsizer contribution up to the maximum amount of $300,000 provided that the other conditions in section 292-102 of the ITAA 1997 are met.

ATO reference *Private Binding Ruling* Authorisation Number 10519993261061
w https://www.ato.gov.au/law/view/document?docid=EV/1051993261061

4.5 GST and loyalty programs

Facts

A Loyalty Program Operator operates a Loyalty Program that meets the criteria set out in paragraph [7] of GSTR 2012/1.

Customers who sign up to become members of the Loyalty Program agree to Terms and Conditions by completing a membership application form.

After becoming a member, customers earn points on eligible purchases from Participating Retailers (retailers where the member may earn points and use Loyalty Dollars (L$)) and other business partners (retailers where the Member may earn points but not use L$) on every dollar they spend and via special promotions offered. The points earned are credited to the individual member's account.

The Participating Retailer and the Loyalty Program Operator are registered for GST.

The Taxpayer has joined as a Participating Retailer to the Loyalty Program.

The points earned by Members and credited to their account do not have any monetary value and do not give the right to any rewards until such time as the points are redeemed.

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Participating Retailers and other business partners are required to pay the Loyalty Program Operator for the points earned by members on eligible purchases at the Participating Retailer or business partner. The Loyalty Program Operator uses these funds to purchase the rewards to be provided to Members redeeming their points.

Members then use their points to redeem rewards.

Members can choose to redeem their points for L$. Members can convert points to L$ in multiples.

L$ can currently be used to pay for purchases at many Participating Retailers. Where a member wishes to use L$ at Participating Retailers, the member must log into their account and redeem their chosen number of points for a certain value of L$. The L$ are then credited to the member's Loyalty card.

To redeem their L$ the member swipes their card at point of sale and enters the amount of L$ that they want to use in the transaction. The Loyalty card is protected by a PIN which the customer must enter in order to access and redeem the L$.

As an example, a customer with $10 of L$ has scanned $22 of shopping at the register and then elects to pay for the shopping with $12 cash and redeeming $10 of L$. The Participating Retailer must accept the L$ and only Charge the Member the discounted price.

Redemption payments to Participating Retailers

Under the terms of the Participation Agreement between Loyalty Program Operator and the Participating Retailer the Participating Retailer must accept L$ and only charge the member the discounted price.

In turn, Loyalty Program Operator agrees that where points are redeemed by members for a 'money off' reward at the Participating Retailer, the Loyalty Program Operator will pay that Participating Retailer an amount (a **Redemption Payment**) to compensate the Participating Retailer for redeeming the L$.

The exact amount of the Redemption Payment from Loyalty Program Operator to the relevant Participating retailer will depend upon the rate negotiated between the Participating Retailer and Loyalty Program Operator.

Questions

1. Is the consideration for the goods or services supplied by a Participating Retailer to a member using a 'money off' reward limited to the discounted price?
2. Does the Participating Retailer make a taxable supply to Loyalty Program Operator for the Redemption Payment?
3. If the answer to question 2 is yes, is the character of the supply by the Participating Retailer to Loyalty Program Operator the same as the character of the supply to the member?

Decision

Question 1

The ATO ruled yes.

Where the member is using its Loyalty points to obtain 'money off' - whether by using L$ loaded on their Loyalty card or swiping their Loyalty card for $10 off at POS - the reward they are getting is a discount for the goods or services being purchased.

In such circumstances, the ATO considers that the consideration that the Participating Retailer receives from the member is limited to the cash payment that is received from the member. There is no other payment or valuable right received by the Participating Retailer.

Question 2

The ATO ruled yes.

The Participating Retailer and Loyalty Program Operator are parties to the Participation Agreement under which they have agreed to make a number of supplies to each other.

One such supply is the Participating Retailers' agreement to accept 'money off' rewards by only charging members the discounted price. In consideration for having done so, the Loyalty Program Operator will pay the Participating Retailer a Redemption Payment.

As a result of the contractual agreement and the actions of the parties, there is both a supply and consideration in the Participating Retailer accepting the 'money off' reward.

Such supply will be a taxable supply as the requirements of a taxable supply in section 9-5 of the GST Act are met.

The ATO position is that whilst Loyalty Program Operator's payment to the Participating Retailer is in the context of a supply to the member, the ATO does not consider this to be 'third party consideration' because:

1. there is a commercial agreement in place - the Participation Agreement - between Loyalty Program Operator and the Participating Retailers that creates binding obligations;
2. the one set of acts - supplying the goods or services and accepting the 'money off reward' can give rise to two supplies;
3. the Participation Agreement has binding obligations, so is even more conclusive than the 'pre-existing framework' factors of the *Commissioner of Taxation v Secretary to the Department of Transport (Vic)* [2010] FCAFC 84 (the *Department of Transport*) case and paragraphs 221A-221G of GSTR 2006/9.

Question 3

The ATO ruled yes.

It is considered that the character of the supply by the Participating Retailer to Loyalty Program Operator is the same as the character of the supply to the Member. This is consistent with the decision in *Department of Transport*. In that case, the single action of transporting an eligible taxi passenger was taken to be a supply to both the passenger (who paid a discounted fare) and the Department (who paid an amount equal to the remaining fare). Both supplies had the same character of transport services.

COMMENT – it is not clear how far you take the 'same character' approach. For example, would be it be the case that, if the supply to the Loyalty Program Operator otherwise met the conditions to be GST-free in section 38-190 of the GST (export supplies), the supply would not be GST-free?

ATO reference *Private Binding Rule Authorisation* Number 1051994171600
https://www.ato.gov.au/law/view/document?docid=EV/1051994171600

5. ATO and other materials

5.1 100A further green zone examples

The ATO has indicated that it intends to finalise the draft public advice on section 100A before the end of 2022. A compendium of feedback will also be published when the advice is finalised. In the meantime, the ATO has released an update to PCG 2022/D1 to include extra green zone examples.

The ATO confirms that the final advice will make clear that section 100A does not apply where there is no agreement, or where the beneficiary simply receives and enjoys the benefit of the distribution, which they are liable to be taxed on.

The ATO is intending to make changes to PCG 2022/D1 which include:

1. expanding the green zone scenarios to which the ATO does not intend to apply compliance resources;
2. removing the blue zone for which more information was required to determine if there was a risk; and
3. including more practical examples to illustrate the operation of the green and red zone.

The new green zone examples include:

1. a loss trust or loss company beneficiary is presently entitled to trust income and those beneficiaries are members of the same family group as the distributing trust. Where there is a loss beneficiary, it must continue to be solvent, particularly if the loss beneficiary uses the trust entitlement to fund an equity distribution;
2. there is a time lag between when a beneficiary becomes entitled to trust income and that entitlement being satisfied, provided the lag does not exceed two years (e.g. it takes two years for a beneficiary's entitlements to be paid to it and in that time the funds were retained by the trustee as part of the investment portfolio of the trust);
3. there is a testamentary trust that is maintained for the benefit of an individual where the trustee reinvests income to which the individual is presently entitled; and
4. there is a business carried on by a trust where two generations of the same family manage that business (e.g., a farming business).

w https://www.charteredaccountantsanz.com/member-services/technical/tax/tax-in-focus/open-consultations-australia

5.2 Letters to clients with debts on hold

The ATO wrote to clients regarding their debts on hold in May 2022 and again on 20 September 2022.

The ATO is reminding clients that:

1. any refunds and credits may be offset against on-hold debt;
2. the refund amount clients receive may be less than expected; and
3. the ATO may use credits received by clients from other government agencies to pay off the tax or super debt of clients.

Offset transactions can be viewed in 'online services for agents'. Clients will also receive a statement of account which can be accessed in 'online services for agents' under 'communication history'.

Debts on hold can be viewed by following the steps outlined in 'debts on hold'.

Clients with residual debt after offsets can avoid further general interest change by paying in full. If the amount cannot be paid in full, the client may be able to set up a payment plan.

w https://www.ato.gov.au/Tax-professionals/Newsroom/Income-tax/Letters-to-clients-with-debts-on-hold/

5.3 GST and residential colleges

The ATO has released its draft *Practical Compliance Guideline* PCG 2022/D3 in relation to goods and services tax and residential colleges. It sets out the ATO's compliance approach for universities and residential colleges supplying accommodation, meals, tertiary residential courses and religious services to resident students, and claiming input tax credits.

It is intended that the PCG, once finalised, will apply from 1 January 2023.

A residential college is defined as an accommodation facility that is generally located on or close to a university, and is usually fully furnished. Services provided by residential colleges to students will vary. All provide accommodation, but may differ in terms of providing meals.

For GST purposes, an endorsed charity is a charity that has an Australian business number (ABN) and is registered with the Australian Charities and Not-for-profits Commission (ACNC) and endorsed for GST concessions by the Commissioner. Endorsed charities are eligible for various GST concessions, such as treating certain supplies as GST-free rather than taxable or input taxed. This requires satisfaction of section 38-250 of the GST Act.

The Commissioner has prepared the PCG to assist residential colleges that are endorsed charities in determining how GST applies to supplies they make under resident student contracts.

For endorsed charities, section 38-250 of the GST Act provides that supplies are GST-free if the supply is:

1. a supply of accommodation for less than 75% of the GST-inclusive market value of the supply (accommodation market value test);
2. a supply other than a supply of accommodation for less than 50% of the GST-inclusive market value of the supply (non-accommodation market value test);
3. a supply of accommodation for less than 75% of the cost to the supplier of providing that accommodation (accommodation cost test); or
4. a supply other than a supply of accommodation for less than 75% of the consideration the supplier provided, or was liable to provide, for acquiring the thing supplied (non-accommodation cost test).

The guideline considers the accommodation market value test and the non-accommodation market value test.

Difficulties that arise in determining how the GST law applies are set out as including:

1. determining the apportionment of fees where a contract with a student contains multiple supplies (or components) for a single fee;
2. comparing that apportioned fee for each component to the relevant market value of the relevant supply to determine if section 38-250 is satisfied;
3. determining the GST classification of each component and any GST payable;
4. where some supplies are input taxed, determining the extent of creditable purpose where an acquisition relates to supplies that are both input taxed and GST-free or taxable.

The Commissioner has developed the ATO charity benchmark market values for use by certain charities in certain circumstances in applying section 38-250. The purpose of these 'proxy' values is to reduce compliance costs for relevant charities, and provide assurance that the Commissioner will not allocate compliance resources to review GST outcomes for accommodation and meals where the ATO charity benchmark values has been correctly applied.

Residential colleges may, but are not required to, use the ATO charity benchmark market values. If a residential college chooses to apply the ATO charity benchmark market values, it must do so in accordance with the Commissioner's guidance in *GST and supplies by charities benchmark market values*.

The draft PCG considers how the ATO charity benchmark market values can be applied in relation to accommodation and meals.

The draft PCG provides guidance that where a rate of no more than 2% has been attributed to GST-free tertiary residential college courses, the Commissioner will not allocate compliance resources. The PCG also set out what will qualify as a tertiary residential college course, and therefore be a GST-free supply.

Similarly, where a residential college attributes no more than 2% of the mandatory charges to GST-free religious services, the Commissioner will not allocate compliance resources.

The draft PCG also sets out a guide for apportionment of fees for components in the student contract and provides several examples.

The Commissioner accepted comments on the draft up until 30 September 2022.

ATO reference *Draft Practical Compliance Guideline PCG 2022/D3*
w https://www.ato.gov.au/law/view/document?docid=DPC/PCG2022D3/NAT/ATO/00001

5.4 Market valuation for tax purposes

The ATO has a guide to assist in understanding the Commissioner's expectation on market valuation for tax purposes. The guide also includes information on what market value means for tax purposes and the evidence and processes generally expected in a valuation.

The guide defines the term 'asset' to mean:

1. real property;
2. plant and equipment;
3. businesses;
4. goodwill;
5. shares;
6. units;
7. liabilities;
8. benefits provided; and
9. financial instruments.

The guide discusses in detail each asset class and the relevant professional required to conduct the valuation for that particular asset class.

Importantly, the guide notes that if the ATO undertakes a market valuation review, the onus for providing a defensible valuation remains with the taxpayer, even if a professional has been engaged to provide the valuation. The taxpayer is responsible for ensuring that the professional is suitably experienced and knowledgeable, receives appropriate instructions, remains objective, has no limitations to prohibit them carrying out the valuation and provides a reasonable market value supported by credible evidence and a recognised valuation methodology.

The guide explains the valuation standards and the fundamentals for tax compliance and confirms if the guide is followed, the tax risks associated with valuations should be reduced.

w https://www.ato.gov.au/law/view/document?docid=SGM/market_val

5.5 Extending the 2-year period to dispose of dwellings acquired from a deceased estate

On 30 September 2022 the ATO updated its *Practical Compliance Guideline* PCG 2019/5. The PCG provides the ATO's compliance approach as to how the CGT main residence exemption may apply when you are disposing of a dwelling when it has been passed to you either as an individual beneficiary or a trustee of a deceased estate.

Generally, if you dispose of an ownership interest in a dwelling that passed to you as an individual beneficiary or as the trustee of the deceased estate within 2 years of the deceased's death, any capital gain or loss you make on the disposal is disregarded. The Commissioner has a discretion to extend the 2-year period. The PCG outlines a safe harbour approach that taxpayers can rely upon, as if the Commissioner had exercised that discretion, to manage their tax affairs.

The PCG provides that, if the delay is within 18 months after the 2-year period from the deceased's death, taxpayers can disregard the capital gain as if the Commissioner had exercised his discretion if they meet the conditions for the safe harbour. If the delay is over 18 months from the 2-year time period, then a taxpayer is required to apply for the Commissioner to exercise his discretion.

The PCG sets out what is required to qualify for the safe harbour, being the following conditions:

1. during the first 2 years after the deceased's death, more than 1 month was spent addressing one or more of the circumstances described in paragraph [12] of the Guideline;
2. the dwelling was listed for sale as soon as practically possible after those circumstances were resolved (and the sale was actively managed to completion);
3. the sale was completed (settled) within 12 months of the dwelling being listed for sale;
4. if any of the circumstances described in paragraph 13 of this Guideline were applicable, they were immaterial to the delay in disposing of your interest; and
5. the longer period for which you would have otherwise need the discretion to be exercised is no more than 18 months.

The circumstances in paragraph [12] are as follows:

1. the ownership of the dwelling, or the will, is challenged;
2. a life tenancy or other equitable interest given in the will delays the disposal of the dwelling;
3. the complexity of the deceased estate delays the completion of administration of the estate;
4. settlement of the contract of sale of the dwelling is delayed or falls through for reasons outside of your control; or
5. restrictions on real estate activities imposed by a government authority in response to the COVID-19 pandemic.

Paragraph [13] states that in order to qualify for the safe harbour, none of the following may have been material to the delay of disposal:

1. waiting for the property market to pick up before selling the dwelling;
2. waiting for refurbishment of the dwelling to improve the sale price;
3. inconvenience on the part of the trustee or beneficiary to organise the sale of the dwelling; or
4. unexplained periods in inactivity by the executor in attending to the administration of the estate.

If the Commissioner's discretion is required, the PCG confirms that the ATO will consider the same factors as the safe harbour in addition to, but not limited to, the following factors:

1. the sensitivity of your personal circumstances and of other surviving relatives if the deceased;
2. the degree of difficulty in locating all beneficiaries require to prove the will;
3. any period the dwelling was used to produce assessable income; and
4. the length of time you held the ownership interest in the dwelling.

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The updated PCG clarifies that references to 'you' throughout the ruling include individuals, whether as a beneficiary or a trustee.

The PCG also includes a diagram to illustrate how the safe harbour can be relied upon.

The PCG also includes information and examples relating to how the Guideline applies to situations impacted by COVID-19.

The PCG will apply before and after its date of issue.

ATO reference *Practical Compliance Guideline PCG 2019/5*
w https://www.ato.gov.au/law/view/document?docid=COG/PCG20195/NAT/ATO/00001

5.6 ATO guidance – getting CGT right for foreign residents

The ATO has modified its guidance regarding how CGT applies to foreign residents.

Foreign residents and main residence exemption

If a foreign resident sold property after 30 June 2020, they are not entitled to the main residence exemption unless they meet the requirements of the life events test.

Foreign residents who sold property prior to 30 June 2020 may be eligible for the main residence exemption in the usual way.

Foreign residents and the 50% CGT discount

The 50% CGT discount can only be applied to part of a capital gain arising from a foreign or temporary resident selling Australian property if they acquired the property on or before 8 May 2012, or they had a period of Australian residency after 8 May 2012.

If either of these applies, foreign residents may pro rata apportion of the discount for the number of days they were an Australian resident after 8 May 2012.

If property is purchased after 8 May 2012 and the buyer remains a foreign or temporary resident for the entire time they own the property, they are not entitled to any CGT discount upon disposal of that property.

w https://www.ato.gov.au/Tax-professionals/Newsroom/Income-tax/Getting-CGT-right-for-foreign-residents/

5.7 Crypto asset investments and tax

The ATO website sets out three steps to help taxpayers manage their crypto asset tax responsibilities, being:

1. report the disposal of crypto ('disposal' does not simply mean sale, but also includes exchanging one crypto asset for another and converting crypto to a fiat currency);
2. work out any CGT (in order to calculate whether a capital gain or loss has been made, the value of crypto purchases and sales in Australian dollars needs to be determined); and
3. keep records of all transactions associated with buying, holding and disposing of crypto assets for at least five years after the disposal of any crypto (the ATO has included a useful table of the records that should be kept by taxpayers).

The ATO has also confirmed that some capital gains or losses from disposing of crypto assets that are personal use assets may be disregarded. Crypto assets that are kept or used mainly as an investment, in a profit-making scheme or in carrying on a business are not personal use assets.

w https://www.ato.gov.au/General/Other-languages/In-detail/Information-in-other-languages/Crypto-asset-investments-and-tax/

5.8 Staking rewards and airdrops

The ATO has updated its website guidance in relation to the tax implications of receiving cryptocurrency staking rewards and airdrops.

Staking rewards

The ATO is of the view that rewards from staking, including rewards for maintaining the network, rewards for participating in 'proxy staking' and rewards for voting tokens in a consensus mechanism, are ordinary income. The monetary value of the tokens at the time they are received should be declared in the tax return as 'other income'.

Airdrops

The ATO describes airdrops as marketing tools 'that distribute crypto assets through a group of people to build their use and popularity. Some projects 'airdrop' new tokens to existing token holders as a way of increasing the supply of tokens.

The monetary value of a token received by airdrop by an existing token holder is ordinary income at the time it is received and should be declared in the tax return as 'other income'.

Initial allocation airdrops

The ATO states that tokens received in an initial airdrop do not constitute ordinary income. An initial airdrop is described as being the very first distribution of tokens where there has been no trading in the tokens prior to the airdrop.

The ATO provides the following example:

> *Example: capital gain and CGT discount on initial airdrop token*
>
> *Cswap launched its own native protocol token, CX through a community airdrop.*
>
> *Josh is an eligible account holder of the Cswap protocol and received an initial allocation of 800 CX tokens on 16 September 2021.*
>
> *Josh does not derive ordinary income or make a capital gain as a result of the receipt of the 800 CX.*
>
> *On 25 May 2023, Josh sold the 800 CX for $4,000. Because the cost base of the CX tokens was zero, Josh makes a total capital gain of $4,000 in the 2022–23 income year from the sale of the CX.*
>
> *Josh is also eligible to reduce his total capital gain using the CGT discount, as he held his CX for more than 12 months.*

The ATO is of the view that these tokens have no market value because they have not previously been traded. If the tokens are provided for free, they have a cost base of $0. If the tokens are not free, the cost base will be the amount paid to acquire them.

w https://www.ato.gov.au/Individuals/Investments-and-assets/Crypto-asset-investments/Transactions---acquiring-and-disposing-of-crypto-assets/Staking-rewards-and-airdrops/

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5.9 Review of Taxpayers' Charter

The ATO is reviewing the Taxpayers' Charter. The Taxpayers' Charter sets out a taxpayer's rights and obligations when interacting with the ATO as well as what can be expected from the ATO as it administers the tax and superannuation systems.

The ATO has asked for feedback on the following questions:

1. How well does the Charter meet your expectations about we should interact with taxpayers when administering the tax, super and registry systems?
2. Does the Taxpayers' Charter provide enough clear information about:
   - your rights and obligations when interacting with us
   - what we should do to support your rights and treat you fairly and reasonably
   - your right to request a review of your situation or to make a complaint?
3. Considering recent difficulties such as COVID-19 and natural disasters, is there any additional content that needs to be included in the Taxpayers' Charter? If yes, what, and why?
4. Is there anything in the Charter that you think is out of date or unnecessary?
5. Do you think we are behaving as required by the Charter?
6. If you have used the Charter for guidance when dealing with us, what sections of the Charter and in what role did you use it (for example, as a taxpayer, a tax practitioner or a taxpayer representative)?

Feedback should be sent to taxpayerscharter@ato.gov.au by 24 October 2022,

w https://www.ato.gov.au/About-ATO/Commitments-and-reporting/Taxpayers--Charter/Taxpayers--Charter-review/

5.10 ATO Top 1,000 combined assurance review program for large super funds

The ATO has established the combined assurance review program (**CAR**) for large superannuation funds. The CAR program aims to ensure that large superannuation funds comply with their tax and data governance obligations.

Particular areas of focus include the treatment of third-party data and GST and member reporting. The CAR program also seeks to identify areas of risk regarding income tax and GST.

Superannuation funds that were part of the Top 1,000 Streamlined Assurance Review (**SAR**) program should review their Streamlined Tax Assurance Report and ensure that any recommendations from previous reviews have been addressed.

w https://www.ato.gov.au/Business/Business-bulletins-newsroom/Large-business/Top-1,000-combined-assurance-review-program-for-large-super-funds/

5.11 Granny flats for rent in Queensland

The Deputy Premier of Queensland announced that under emergency planning changes, Queensland home owners who have granny flats will be allowed to rent them out to people other than immediate family members for the next three years in an attempt to address Queensland's housing crisis.

The emergency planning changes will be reviewed after three years.

w https://statements.qld.gov.au/statements/96181

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