The Tax Institute

Tax Update

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LAWYERS

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Contents

Our tax training notes are prepared by Marianne Dakhoul, Jane Harris, Matthew McKee, Gillian Tam, Hayden Rudd, Aritree Barua, Emily Halloran, Amy Burriss, Luke Hermez, Samiksha Vaidya and Aaditya Kadam.

1. Tax Update Pitstop

The Tax Update Pitstop provides a quick reference to the top 5 tax matters from the month as determined by our experts.

Tax Update Matter	**Impact Summary**	**Further Detail**
Item 2.1 Morton	The Federal Court has found that land remained on capital account for the landowner, despite substantial subdivision activities being undertaken on the land over an extended period of time. The Court considered that the development activities on the land were being undertaken by the developer and not the landowner and, therefore, the character of the land did not change for the landowner.	Page 7
Item 2.2 Kirtlan	The Administrative Review Tribunal has held that a taxpayer did not engage in fraud or evasion where he relied upon advice given by his tax agent. The effect of this was that Commissioner was precluded from amending the taxpayer's income tax assessment on the basis that had been a resident of Australia in the relevant years.	Page 10
Item 2.3 Merchant	The Full Federal Court has upheld a finding that an arrangement entered into by Gordan Merchant and his related entities for the sale of shares in Billabong Limited to a related superannuation fund was a scheme entered into or carried out for the dominant purpose obtaining a tax benefit, where the sale realised a capital loss on the shares that was used to offset a capital gain made from other assets in the same year.	Page 28
Item 8.5 ATO views on Bendel decision	The Australian Taxation Office has commented further on its approach to UPEs to private companies pending its appeal to the High Court in the *Bendel* litigation. The ATO's comments include its approach to the exercise of the section 109RB discretion in the event that the appeal is successful.	Page 55
Item 8.7 ATO Small Business Focus Areas	On 9 May 2025, the ATO updated its webpage on Small Business Focus Areas, outlining key areas of compliance attention for the 2025–26 financial year.	Page 58

2. Detailed case summaries

2.1 Morton – capital vs revenue

Facts

In the mid-1950s, Colin Morton purchased approximately 344 acres of land in Tarneit, Victoria, later joined by a 40-acre parcel owned by his wife, Alison. This combined holding became known as the Morton Farm, which Colin farmed initially with sheep, and later with cattle.

In 1973, Colin subdivided a 10-acre portion from his land, later referred to as "Dave's Block." In 1980, Colin's son David purchased Dave's Block from Colin for $13,500.

In 1996, Colin passed away. From that point until 2015, David continued farming operations across the Morton Farm, now including crops like wheat and barley. He resided in Swan Hill but regularly travelled to the property.

In 2008, the Victorian government released a planning update suggesting an expansion of Melbourne's Urban Growth Boundary. David anticipated that Dave's Block would be rezoned, which spurred interest from developers and conversations within the family about subdividing the farm for sale.

In 2010, Dave's Block was formally brought within the Urban Growth Boundary and rezoned as residential land. Increased taxes and reduced farming viability followed.

On 23 November 2012, David entered into a development agreement with Tarneit East Development Project Pty Ltd concerning Dave's Block. This agreement granted exclusive rights to subdivide and develop the land. Under clause 15.8 of that agreement, David agreed to appoint the developer (and its officers or agents) as his attorney to carry out actions necessary for the development that, by law, had to be done by the landowner and could not be executed by the developer independently. This was framed as a 'general power of attorney' and included executing documents and performing obligations related to planning, permits, and sales. Clause 38 of the agreement clarified that this power did not create a broader agency relationship or joint venture.

On the same day, additional development agreements were executed the same day for other parts of the Morton Farm held on trust by David and his brother, Peter Morton, for their respective family trusts.

Between 2014 and 2017, three deeds of variation were executed, progressively altering the developer's fee structure, granting the Morton family greater control over englobo land sales, and enabling the developer to secure project funding by lodging caveats over the land.

On 13 November 2014, the Minister for Planning approved a relevant planning scheme amendment applying to Dave's Block.

On 25 January 2016, Wyndham City Council issued a planning permit for Dave's Block. It included conditions linked to a nearby broiler farm ceasing operations.

On 11 January 2016, construction began on stage 1 of the broader Morton Farm development.

On 16 June 2016, conditional contracts for subdivided lots on Dave's Block were executed.

On August 2017, bulk earthworks commenced on Dave's Block. Construction officially began in September 2017 but was interrupted by funding issues.

On January 2018, work resumed and was completed by November 2018, including roads, parks, utilities, footpaths, and lighting.

On 18 January 2019, a statement of compliance was issued by Wyndham City Council. On 5 February 2019, the subdivision plan was registered.

Dave’s Block itself was a 10-acre parcel that was subdivided into 48 residential lots and two commercial lots. However, the development was part of the much larger Morton Farm project, which was conceptually divided into at least 31 stages and ultimately resulted in the creation of approximately 1,632 lots across the entire estate.

On February and March 2019, settlements occurred for the 48 residential lots on Dave's Block. One commercial lot for a service station settled on 19 October 2020 and another for a childcare centre on 2 July 2021.

On 2 August 2022, the Commissioner issued amended tax assessments to David for the 2019 and 2021 income years, treating sale proceeds as income.

On 30 September 2022, David lodged objections. On 7 June 2023, the Commissioner disallowed the objections.

David appealed to the Federal Court for review of the objection decisions.

The Commissioner argued that the proceeds David received from the sale of subdivided lots on Dave’s Block were assessable income under section 6-5 of ITAA 1997, on the basis that David was carrying on a business of property development and the land constituted trading stock within the meaning of section 70-10 of the ITAA 1997. Alternatively, the Commissioner contended that the proceeds were statutory income under section 6-10 of the ITAA 1997, as profits from a profit-making undertaking or scheme under section 15-15 of the ITAA 1997. The Commissioner relied on the scale and complexity of the project, the formal development agreement David entered into in November 2012, and his involvement in approving budgets and monitoring progress, as evidence that he was engaged in commercial activity beyond the mere realisation of a capital asset. The Commissioner maintained that Dave’s Block became trading stock, or was committed to a profit-making scheme, from the date the development agreement was executed.

David argued that the proceeds from the sale of subdivided lots on Dave’s Block were capital receipts, not assessable income, because he was not carrying on a business nor undertaking a profit-making scheme. He submitted that he acquired the land in 1980 for farming, had used it for that purpose for many years, and only chose to develop it after it became unviable due to rezoning and increasing urban encroachment. He relied on section 104-10(5)(a) of the ITAA 1997, which disregards capital gains on pre-CGT assets, on the basis that the sales were a realisation of a capital asset and not income under sections 6-5 or 15-15 of the ITAA 1997.

David emphasised that he played a passive role in the development process, did not contribute capital or take on financial risk, and specifically avoided involvement in the commercial operations of the developer. He pointed to the terms of the development agreement, which gave the developer full control and confirmed that David had no interest in the development beyond his ownership of the land. He also argued that seeking to maximise the sale price of a capital asset did not in itself establish a business or scheme. In the alternative, if the proceeds were found to be assessable, David contended that the land should not be treated as trading stock from the date of the development agreement in 2012, but from a later point when the land was actually subdivided or when planning permits were issued.

Issue

Was the gain made by David on the sale of subdivided lots on Dave’s Block assessable income under sections 6-5 or 15-15 of the ITAA 1997, or was it disregarded as a capital gain from the mere realisation of a pre-CGT asset?

Decision

The Court considered the long-established principles distinguishing a mere realisation of a capital asset from business or profit-making activity. It relied on the foundational test in *Californian Copper Syndicate (Ltd and Reduced) v Harris* (1904) 5 TC 159, which asks whether the gain was from realising an investment or from carrying out a business. The Court also drew support from *Scottish Australian Mining Co Ltd v Federal Commissioner of Taxation* (1950) 81 CLR 188, where land sales following the cessation of mining were held to be a realisation of capital, despite significant subdivision work.

David's case was found to be closely aligned with decisions like *Statham v Federal Commissioner of Taxation* (1988) 20 ATR 228 and *Casimaty v Federal Commissioner of Taxation* (1997) 37 ATR 358, which affirmed that extensive development activity can still amount to a mere capital realisation, particularly where the taxpayer is not actively engaged in the development business and lacks commercial risk. The Court also adopted the guidance in *Federal Commissioner of Taxation v Williams* (1972) 127 CLR 226, which highlighted the significance of passive ownership and minimal taxpayer involvement.

<u>No business or profit-making scheme</u>

The Court held that David had acquired and held Dave's Block for farming purposes, not for sale at a profit. Although he later engaged a developer to subdivide and sell the land, this was not done in the course of a business. The development was driven by external changes, including rezoning and the declining viability of farming, rather than any entrepreneurial land-trading activity by David.

The Court accepted that David's involvement in the development was limited and mostly passive. He did not fund the project, did not assume commercial risk, and delegated responsibility to the developer. While he sought to maximise the sale price of the land, the Court held that doing so was consistent with prudent asset management, not indicative of a business.

<u>Developer acted independently</u>

The Court placed weight on the development agreement, which made clear that the developer (Tarneit East) operated independently, was not in partnership or joint venture with David, and acted in its own commercial interest. The agreement explicitly stated that David had no interest in the development beyond land ownership.

Although David granted the developer a power of attorney and some administrative oversight, such as budget approvals, the Court found this was not enough to establish that the developer's commercial activities could be attributed to David as a business operation carried on for his benefit.

<u>Magnitude not determinative</u>

The Court acknowledged the large scale of the project but emphasised that the mere magnitude of a development does not convert a capital realisation into a business. The development's scope was seen as a practical response to zoning changes and market conditions rather than evidence of an ongoing trade.

<u>Timing (in the alternative)</u>

In the alternative, the Court addressed the Commissioner's argument that Dave's Block became trading stock on 23 November 2012 when the development agreement was signed. The Court agreed that, if the land had been ventured into a business or scheme, that would have been the operative date. However, since the primary conclusion was that no business or scheme existed, this issue did not affect the outcome.

<u>Conclusion</u>

The Court held that the proceeds David received from the sale of subdivided lots on Dave's Block were not assessable income. The Court concluded that David had not carried on a business of land development, nor had he undertaken a profit-making scheme. Accordingly, the amended tax assessments for the 2019 and 2021 income years were found to be excessive and were varied.

Citation *Morton v Commissioner of Taxation* [2025] FCA 336 (Wheelahan J, Melbourne)
w https://www.austlii.edu.au/cgi-bin/viewdoc/au/cases/cth/FCA/2025/336.html

2.2 Kirtlan – residency and fraud or evasion

Facts

On 1 February 2000, Robert Kirtlan launched his own corporate advisory firm, Ark Securities, operating through a family trust and participating actively in several ASX-listed companies.

In late 2004, Robert and Angela Kirtlan bought a home in Mosman Park, Perth, intending to live there. However, they soon relocated to the UK and leased the property to its previous owner.

On 1 April 2005, the Kirtlan family moved to the UK to support Robert's business ambitions. After a short stay in South Kensington, they rented a house in Chiswick in May 2005. Robert's move was framed as a long-term relocation to expand his business connections in Europe.

On 1 November 2005, Angela and their daughter Portia returned to Australia due to dissatisfaction with life in London. They moved back into the Mosman Park house in December 2005 or January 2006.

On 1 February 2006, Robert returned to London and resumed business activities, renting a flat for his stays and hosting his family during their visits.

Between July 2005 and June 2008, Robert made numerous trips to Australia, spending 173 days in the 2006 financial year, 187 in 2007, and 249 in 2008. These stays were primarily with his family in Perth, while also maintaining business travels to Africa and Asia.

In August 2007, Robert leased a new London flat, indicating a continued intention to live there despite his family being in Australia.

On 1 May 2008, Robert surrendered his London lease and returned to Australia permanently following the global financial crisis and declining business opportunities in the UK. He moved back in with his family and has remained in Australia since.

Throughout 2006 to 2008, Robert had lodged his Australian income tax returns on the basis that he was not a resident of Australia and his UK returns on the basis that he was not a UK resident. Consequently, the significant UK-sourced income derived by Robert was not brought to account in either jurisdiction. His accountant, Kathal Spence, who had advised him since the 1990s, prepared the Australian returns and advised that Robert was not an Australian resident for tax purposes. Kathal based his advice on Robert's assertions about long-term plans and personal circumstances.

On 24 September 2021, the Commissioner disallowed Robert's objections to the amended assessments, which included substantial tax shortfalls totalling approximately $3.79 million and penalties of approximately $1.89 million. These assessments had been issued in 2018, well beyond the standard amendment period, on the basis that Robert had engaged in tax evasion.

Robert applied to the ART for review of the objection decisions.

Robert argued that the Commissioner should not have formed the opinion that his tax shortfalls were due to evasion, which was necessary to justify the amended assessments issued in 2018 for the 2006 to 2008 income years. He claimed he genuinely believed he was not an Australian resident during that period and relied on advice from his long-time accountant, Kathal Spence, who prepared or approved his tax returns on that basis.

Robert submitted that Kathal, having a deep understanding of his personal and business affairs, gave informed advice and that he acted in good faith when following it.

Robert highlighted that his move to the UK in 2005 was genuine, citing long-term leases, integration into UK life, and business activities based there. Although his wife Angela and daughter returned to Australia later that year, Robert remained in London until 2008, only returning due to the global financial crisis and family reasons. He acknowledged inconsistencies in his UK tax returns but attributed them to oversight and reliance on professionals. Overall, he argued that while his returns may have been incorrect, they were not dishonest and did not amount to evasion.

The Commissioner argued that Robert's conduct amounted to evasion, justifying the amended assessments issued outside the usual time limits. He claimed Robert knew he was an Australian resident between 2006 and 2008 but deliberately excluded UK-sourced income from his tax returns, allowing significant income to go untaxed in both Australia and the UK.

Key points included Robert's substantial time spent in Australia, the retention of a family home in Perth, and the ongoing presence of his wife and daughter there, all pointing to continued Australian residency. The Commissioner also highlighted conflicting statements in Robert's UK tax returns, including identifying Australia as his country of residence and describing his UK stay as temporary.

While Robert said he relied on advice from his accountant Kathal, the Commissioner argued that Kathal's advice was not based on full or accurate information and lacked ongoing confirmation. Overall, the Commissioner maintained that Robert's actions were blameworthy and intended to avoid tax, meeting the legal standard for evasion.

Issues

1. Was the Commissioner's formation of the opinion that Robert Kirtlan engaged in evasion lawful under section 170(1) of the ITAA 1936?
2. Were the amended income tax and penalty assessments invalid because they were made outside the limitation period and, therefore, excessive under section 14ZZK of the TAA?

Decision

<u>Evasion finding</u>

The ART considered whether the Commissioner was justified in forming the opinion that Robert's conduct constituted evasion under section 170(1) of the ITAA 1936, which would permit assessments beyond the usual amendment period.

The ART considered whether Robert's conduct, viewed in light of his belief that he was not an Australian resident and his reliance on professional advice, excluded a finding of evasion as required for the Commissioner to issue amended assessments outside the limitation period under section 170(1) of the ITAA 1936. Although Robert spent substantial time in Australia and maintained a home there, the ART accepted that he took genuine steps to establish residence in the United Kingdom from 2005, including entering into leases, enrolling his daughter in school, and conducting business abroad. His return to Australia in 2008 was attributed to market disruptions and personal reasons, not an intent to maintain Australian residence.

The ART found that Robert's long-standing accountant, Kathal, genuinely and independently advised that Robert was not a resident, having been well informed of his personal and financial circumstances, with no evidence of collusion. Although there were inconsistencies in Robert's UK tax returns and omissions of foreign income from his Australian returns, the ART held that these did not amount to the type of blameworthy conduct required to establish evasion. Accordingly, the ART concluded that Robert's belief and reliance on informed professional advice provided a credible explanation that excluded evasion under section 170(1). The Commissioner's opinion was not lawfully formed.

Limitation

The ART noted that under section 14ZZK of the TAA, Robert bore the burden of proving that the amended assessments were excessive. Because the assessments were issued in 2018, well after the statutory amendment periods for the 2006, 2007 and 2008 income years, their validity depended entirely on whether evasion had occurred. Having concluded that there was no evasion, the ART held that the amended assessments were time-barred. As a result, Robert had successfully discharged his burden under the TAA and the assessments, including the associated penalties, were found to be both excessive and invalid.

COMMENT – this is a rare case where the taxpayer was able to successfully challenge a fraud or evasion finding without challenging the Commissioner's reasons for seeking to amend the assessments.

COMMENT – when providing advice, it is important to ensure that files reflect not only the conclusion but also the factual basis for it. While the ART in *Kirtlan* accepted that deep and ongoing familiarity with a client's affairs could support an inference of adequate information, this was a rare case involving a long-term, well-documented relationship. In most situations, the absence of a clear, contemporaneous record of the client's relevant circumstances and reasoning will weaken the weight of the advice if is later scrutinised. Further, under section 30 of the Tax Agent Services (Code of Professional Conduct) Determination 2024 (Cth), written records must be kept that:

> *…*
> *(d) reference information reasonably considered in the provision of the tax agent service; and*
> *(e) include all advice received from the client; and*
> *(f) include all advice provided to the client, and for more complex matters: the relevant facts, assumptions and reasoning underpinning any advice provided (including the basis on which, and the method by which, any calculations, determinations, or estimates used, have been made)*

Citation *Kirtlan and Commissioner of Taxation (Taxation)* [2025] ARTA 539 (Senior Member R Olding, Brisbane)
w https://www.austlii.edu.au/cgi-bin/viewdoc/au/cases/cth/ARTA/2025/539.html

2.3 Charles Apartments – interest deductions

Facts

On 1 February 2002, Charles Apartments Pty Limited, together with Demian Holdings, purchased three adjoining properties at 6, 8 and 10 Charles Street, Parramatta for $3,125,000. Charles Apartments had been created a few months earlier as a special purpose vehicle to acquire and develop these sites. The acquisition was financed through a $3 million loan from St George Bank.

On 23 June 2003, St George Bank notified Charles Apartments that its loan facility would expire at the end of that month. In response, the Demian Group sought consolidated refinancing and secured a $27 million loan from Suncorp. By 24 December 2003, this facility was finalised, the St George loan was repaid, and Suncorp took a mortgage over the properties. Charles Apartments became a guarantor under this arrangement and entered into a Deed of Guarantee and Indemnity with Suncorp. The funds used to repay St George Bank had been provided through an intragroup loan from a treasury company within the Demian Group.

On 9 June 2009, due to the default of West Apartments Pty Ltd, the lead borrower within the Demian Group, Charles Apartments entered into a Deed of Forbearance with Suncorp. This agreement acknowledged Charles Apartments' broader liability for the Group's outstanding debts under the Suncorp facility.

On 12 May 2010, following discussions with Suncorp, Mr Demian received verbal consent to proceed with the sale of the three properties. Three separate contracts of sale were executed shortly after. The first was signed on 18 May, the second on 2 June and the third on 7 June 2010. All three contracts were conditional on simultaneous settlement, which ultimately occurred. The total sale price was $5 million including GST.

On 7 June 2010, a fourth contract, styled as a deed of agreement, was entered into between Advanced Communications (another Demian Group company) and the purchaser of the three properties. This contract transferred for the right, title and interest in relation to certain documents, defined as the D.A. Documents, for the sum of $3,850,000 plus GST. The D.A. Documents were defined as "All plans, reports, council approvals, submissions" for three sites, for a price of $3.85 million plus GST. This was not disclosed to Suncorp. Charles Apartments did not receive any portion of the payment under this fourth contract and did not include it in its tax return.

On 13 August 2010, the full net sale proceeds of $4,870,223 from the three property contracts were remitted directly to Suncorp. Of this, $3 million was attributed to the repayment of principal and the balance of $1,870,223 was treated as interest under the terms of the intragroup loan. According to these terms, Charles Apartments was not liable to pay interest as it accrued, but instead would pay the capitalised interest out of the sale proceeds when it sold the properties, capped to the amount of the sale proceeds after repaying the principal.

In its tax return for the year ending 30 June 2011, Charles Apartments returned the $5 million from the three sales as assessable income.

The Commissioner amended the assessment, attributing a portion of the fourth contract proceeds to Charles Apartments, increasing its taxable income from $5,000,000 to $5,946,000 and imposing penalties. The Commissioner contended that, having regard to all four contracts, Charles Apartments or entities associated with Charles Apartments derived more from the sale of the properties than Charles Apartments reported in its tax return, and it was appropriate to treat a portion of the proceeds of sale under the fourth contract as the balance of the purchase price for the properties.

The Commissioner also disallowed certain claims for deduction of interest expenses and construction costs, on the basis that those expenditures were not allowable deductions under section 8-1 of the ITAA 1997.

Charles Apartments appealed the Commissioner's decision in the AAT, on the basis that no sale proceeds from the fourth contract should be attributed to Charles Apartments and that it was entitled to the deductions. This decision was reported as *WCVB and Commissioner of Taxation (Taxation)* [2024] AATA 1259 (see our June 2024 Tax Training Notes).

The AAT accepted that Charles Apartments did not receive the $946,000 but found that this amount was still assessable due to its commercial connection with the other sales. The AAT accepted the Commissioner's submission that it can be inferred that the fourth contract was an implied direction from Charles Apartments to the purchaser to pay to Advanced Communications that portion of the proceeds of sale under the fourth contract which related to the properties.

It also accepted that Charles Apartments had incurred interest of $1,870,223, but declined to allow any greater deduction on the basis that the taxpayer's liability was limited to the available sale proceeds.

Charles Apartments appealed to the Federal Court.

Charles Apartments submitted that, because the AAT had held $946,000 from a fourth contract was assessable income, it was required to consider a corresponding increase in the allowable interest deduction under section 8-1 of the ITAA 1997. This was described as the "consequential step" argument. Charles Apartments contended that under the intragroup loan arrangement, further interest had accrued, and since this additional income formed part of its assessable income, a nexus existed to support a larger deduction.

Charles Apartments also argued that the AAT erred by limiting its consideration of the interest deduction to $1,870,223.34. It contended that a higher amount should have been taken into account, relying on an interest calculation summary which indicated that approximately $3.4 million in interest had been capitalised. While Charles Apartments acknowledged at the hearing that the AAT did not find this full amount had accrued or was deductible, it maintained that the AAT had effectively accepted the larger calculation but restricted its findings to the $1.87 million figure because that was the maximum surplus available from the property sales under the terms of the intragroup loan.

The Commissioner responded that Charles Apartments itself had confined its claim to this maximum amount. This position was evidenced through multiple aspects of the taxpayer's case before the AAT, including amendments to its Statement of Facts, Issues and Contentions, opening and closing written submissions, and oral argument. Each of these reflected a consistent cap on the claimed deduction at $1,870,223.34. Earlier references to a larger interest figure, such as $2.84 million or $3.4 million, were either historical or framed as calculations not submitted as evidence. A representative for Charles Apartments had described the larger figure as an illustrative aide-memoire, not proof of an actual liability.

The Commissioner also raised two grounds of cross-appeal. The Commissioner argued that the AAT wrongly applied a "but for" test when assessing deductibility under section 8-1 of the *Income Tax Assessment Act 1997*. Specifically, the AAT found that the taxpayer would not have derived assessable income unless it agreed to pay the net proceeds of sale to Suncorp, and therefore the interest was deductible. The Commissioner contended this was legally incorrect, as it focused on the conditions for earning income rather than the required nexus between the interest expense and income-producing activities.

Instead, the Commissioner maintained that the AAT should have applied the established refinancing principle from *Commissioner of Taxation v Roberts; Commissioner of Taxation v Smith* (1992) 37 FCR 246, which requires examining the use of borrowed funds. The AAT's reasoning did not trace the funds or assess how they were used, and its approach denied the parties procedural fairness, as neither party had the opportunity to address the "but for" test.

Issues

1. Did the AAT err by failing to consider whether Charles Apartments was entitled to a further interest deduction corresponding to the additional assessable income from the fourth contract?
2. Did the AAT err by limiting the allowable interest deduction to $1,870,223, despite evidence suggesting a higher amount of accrued interest?
3. Did the AAT apply an incorrect legal test when determining deductibility under section 8-1 of the ITAA 1997 by reasoning that Charles Apartments would not have derived assessable income "but for" its agreement to pay the net proceeds of sale to Suncorp?

Decision

<u>No additional interest deduction for income from fourth contract</u>

The taxpayer's construction of section 8-1 of the ITAA 1997 was grounded in the High Court's reasoning in *Fletcher v Federal Commissioner of Taxation* (1991) 173 CLR 1. In *Fletcher*, the High Court confirmed that the phrase "the assessable income" in the predecessor provision (former section 51(1) of the ITAA 1936) should not be read narrowly as referring only to income actually derived in a given income year. Instead, it encompasses income that a relevant outgoing would be expected to produce, taking a prospective and commercial view of the nexus. The taxpayer argued that this principle applied equally under section 8-1 of the ITAA 1997, which uses the phrase "your assessable income", and therefore that the inclusion of $946,000 as additional assessable income from the fourth contract necessitated a corresponding increase in the deductible interest.

The AAT, however, had found that the liability of Charles Apartments to pay interest under the relevant intragroup loan was conditional. The evidence of Mr Demian, accepted by the AAT, was that interest accrued on the loan but became payable only upon the sale of the properties, and then only to the extent of any available surplus. The AAT concluded that the maximum interest payable by the taxpayer was $1.87 million, which precisely matched the amount available from the net sale proceeds after repaying the principal loan of $3 million. The additional income from the fourth contract, which related to the sale of planning and development documents, was not received by Charles Apartments, was not disclosed to Suncorp, and was not treated as proceeds from the sale of the properties.

The Court accepted the continuing relevance of *Fletcher* in interpreting section 8-1, but it rejected the submission by Charles Apartments that the presence of additional assessable income automatically gives rise to a further deduction. It held that the nexus required under section 8-1 must still be established in fact and on the terms of the legal arrangement. The intragroup loan did not impose liability based on constructive receipt or legal entitlement, but solely on the actual availability of sale proceeds. As the fourth contract did not contribute to those proceeds and was not within the contemplation of the loan agreement, no additional deduction could arise.

Accordingly, the Court concluded that the AAT had not erred in its construction of section 8-1, and that no legal error arose from its refusal to allow a further interest deduction.

<u>Limitation of deduction</u>

The Court found that Charles Apartments had clearly narrowed its case before the AAT. Although its position evolved during the lead-up to the hearing, it ultimately confined its claim to the $1.87 million figure. The AAT responded appropriately to the arguments advanced and did not err in concluding that no greater amount was claimed or substantiated. The Court observed that Charles Apartments had chosen not to argue in the alternative and did not put forward a case for deductibility beyond the surplus amount. As such, there was no legal error in the AAT's treatment of the claimed deduction.

<u>Use of "but for" test</u>

The Federal Court found that the AAT had erred in its application of section 8-1 of the ITAA 1997. In particular, the AAT's reasoning at paragraph [139] was found to rely on a "but for" test, which is not the correct legal standard for determining deductibility under section 8-1. The AAT concluded that the taxpayer would not have derived assessable income unless it had agreed to pay the net proceeds of sale to Suncorp, and therefore the interest payment was deductible. However, the Court held that this reasoning improperly focused on the conditions for earning income, rather than the proper enquiry required under section 8-1, which is whether the loss or outgoing was incurred in gaining or producing assessable income, or necessarily incurred in carrying on a business for that purpose.

The correct approach, as established in *Commissioner of Taxation v Roberts; Commissioner of Taxation v Smith* (1992) 37 FCR 246, is to determine the character of the expense by examining the use of the borrowed funds. The AAT failed to properly trace the original borrowings and the subsequent refinancing through the intragroup loan and instead concentrated on the use of the sale proceeds, which the Court found to be an error of law.

In addition to applying the wrong legal test, the Court found that the AAT had denied the parties procedural fairness. The AAT introduced the "but for" reasoning without giving the parties any opportunity to make submissions on that approach. This was a critical part of the decision, directly affecting the nexus analysis under section 8-1 and the taxpayer's entitlement to the interest deduction.

The Commissioner argued, and the Court accepted, that had the parties been invited to address the AAT's reasoning, they would have presented further submissions. The Commissioner, in particular, would have argued that the entire amount paid to Suncorp was to satisfy obligations under the Guarantee, and therefore was of a capital nature, not deductible on revenue account. The Court concluded there was a realistic possibility that the outcome could have been different had the parties been heard on this issue.

Conclusion

The Federal Court dismissed the appeal brought by Charles Apartments and allowed the Commissioner's cross-appeal. As a result, the Court set aside the decision of the AAT and affirmed the Commissioner's original objection decision, which had disallowed any deduction for interest. The Court confirmed that the proper characterisation of the payment to Suncorp of the net sale proceeds was one under the Guarantee and the payment to Suncorp would be on capital account and hence not deductible.

Citation *Charles Apartments Pty Limited v Commissioner of Taxation* [2025] FCA 461 (Wheatley J)
w https://www.austlii.edu.au/cgi-bin/viewdoc/au/cases/cth/FCA/2025/461.html

2.4 Aitkin – CGT events and calculating market value

Facts

AgriWealth Capital Limited was the manager of the 'AgriWealth 2011 Softwood Timber Project', which was a registered forestry managed investment scheme, being a scheme for establishing and tending trees for felling. The project was formally established by AgriWealth on 19 June 2011.

Michael Aitken was an initial participant in the project.

On 30 June 2011, Michael applied to invest $10,143,700 to acquire 337 'timberlots' in the project, being each an area of half a hectare of planted land, to which a 'forestry interest' attaches to. Under the project, a forestry interest comprised of a right in timber as well as a right in carbon sequestration and salinity rights and credits. As part of the purchase, Michael also acquired corresponding put options which entitled him to sell the timberlots back to AgriWealth at $14,000 per timberlot, totalling $4,718,000.

Michael claimed a full deduction of $9,082,150, to which he was entitled, in the financial year ended 30 June 2011.

On 1 July 2015, Michael exercised his put option. That same day, rather than proceeding to completion of the sale contract that arose from that exercise, Michael entered into a novation deed with AgriWealth. Pursuant to the novation deed:

1. Michael transferred only the timber component of his forestry interest while expressly retaining the carbon sequestration and salinity rights and credits; and
2. the consideration payable was $4,718,000, which was identical to the amount under the Put Option. This amount was not paid to Michael directly but instead applied to discharge outstanding loans he owed to AgriWealth.

On 6 July 2017, Michael lodged his income tax return for the income year ended 30 June 2016. Michael did not include the full amount of the consideration payable as his assessable income but instead relied on a valuation report prepared by Mr Halligan, a valuation expert, which estimated the novated forestry interest to be worth approximately $300,000.

The valuation only considered the novated timber component of Michael's forestry interest. In conducting his valuation, Mr Halligan deliberately excluded any attempt to value the carbon sequestration and salinity rights and credits, and he did not account for the existence and exercise of the put option.

Following an audit of Michael’s tax affairs, on 13 January 2021, the Commissioner issued an amended assessment for the income year ended 30 June 2016. This amendment increased Michael's assessable income to $4,718,000. This was done pursuant to section 394-25 of the ITAA 1997, which deals with CGT events happening in relation to forestry interests in forestry managed investment schemes.

Section 394-25 of the ITAA 1997 applies if:

1. the taxpayer holds a forestry interest in a forestry managed investment scheme as an initial participant: section 394-25(1)(a) of the ITAA 1997;
2. the taxpayer can deduct or has deducted an amount for an income year under section 394-10 in relation to the forestry interest: section 394-25(1)(b) of the ITAA 1997; and
3. a *"CGT event happens in relation to the forestry interest, other than a CGT event that happens in respect of thinning"*: section 394-25(1)(c) of the ITAA 1997.

Pursuant to section 394-25(2) of the ITAA 1997, a taxpayer's assessable income, for the income year in which a CGT event happens, includes:

> *(a) if, as a result of the CGT event, you no longer hold the forestry interest--the market value of the forestry interest (worked out as at the time of the event); or*
>
> *(b) otherwise--the decrease (if any) in the market value of the forestry interest as a result of the CGT event.*

The Commissioner argued that two CGT events occurred on 1 July 2015, being:

1. the exercise of the put option, which was CGT event C2 in relation to the forestry interest. This triggered section 394-25(2)(b) of the ITAA 1997; and
2. the execution of the novation deed, which was also CGT event C2. This triggered section 394-25(2)(a) of the ITAA 1997.

To support the argument that section 394-25 of the ITAA 1997 applies to multiple CGT events involving a forestry interest, the Commissioner relied on the broad statutory language, particularly the phrase *"in relation to"* that is used in section 394-25(1)(c) of the ITAA 1997. The Commissioner referred to the case of *HP Mercantile Pty Ltd v Commissioner of Taxation* (2005) 143 FCR 553 which supported that such language should capture events or transactions with a sufficient connection to the subject matter.

The Commissioner also strongly criticised Michael's valuation methodology. The fact the valuation deliberately excluded the influence of the put option was an error that, in the opinion of the Commissioner, rendered the report fundamentally flawed. The Commissioner also argued that the highest and best use of Michael's forestry interest was to sell each timberlot for $14,000 by exercising the put option. Accordingly, the market value immediately prior to exercise should be $14,000 per timberlot, as set out in the put option deed, which renders an expert valuation unnecessary.

Michael argued that only a single CGT event occurred, based, at least in part, on the use of the singular “event” in section 394-25(1)(c) of the ITAA 1997. Michael contended that only the execution of the novation deed was relevant and that the earlier exercise of the put option was not itself a CGT event affecting the forestry interest.

In support of his valuation, Michael emphasised that the novation deed did not transfer the entirety of his forestry interest.

Michael also sought to rely on PR 2011/12, being the product ruling concerning the project that the Commissioner issued on 11 May 2011, to support his arguments.

The Commissioner argued that PR 2011/12 was not binding in Michael's case because Michael had materially departed from the scheme described in the ruling in two respects, being Michael's finance arrangements and the novation deed excluding carbon sequestration and salinity rights.

On 5 March 2021, Michael objected to the amended assessment.

On 31 August 2023, the Commissioner disallowed the objection but reduced the penalties from 25% to 5%.

Issues

1. Did more than one CGT event occur in relation to Michael's forestry interest?
2. What was the market value of the Michael's forestry interest?
3. Can Michael rely on Product Ruling PR 2011/12?

Decision

Justice Bromwich confirmed that both the exercise of the put option and the subsequent novation were CGT events relevant to Michael's forestry interest. In reaching this conclusion, Bromwich J held that the term "in relation to" in section 394-25(1)(c) of the ITAA 1997 should be interpreted broadly to include events that are sufficiently connected to the forestry interest. Justice Bromwich also noted that the two CGT events could have happened years apart but, on the facts, happened on the same day.

Justice Bromwich rejected Michael's valuation methodology and was unable to accept Mr Halligan's evidence as to market value. His Honour found that the valuation of the forestry interest *"… was conducted without regard to reality"*. Justice Bromwich also noted that the valuation did not take account of the fact that the hypothetical sale occurred in a market where every single potential vendor of forestry interests had the benefit of the same put option and the same right to be paid the same strike price, and *"Put more bluntly, no sane Grower was going to accept anything less than the price obtainable by the exercise of the Put Option"*. Accordingly, his Honour held that Michael had not established that the Commissioner's amended assessment was excessive by including $4,718,000 as the market value.

The Court also held that Michael had materially departed from the terms of PR 2011/12 and, as a result, Michael could not rely on the ruling, and the Commissioner was not bound by it. However, Bromwich J was satisfied that whether or not PR 2011/12 was binding, the result would have been the same.

The appeal was dismissed.

Citation *Aitken v Commissioner of Taxation* [2025] FCA 372 (Bromwich J) w https://www.austlii.edu.au/cgi-bin/viewdoc/au/cases/cth/FCA/2025/372.html

2.5 Association Specialists – late payment of payroll tax and penalty

Facts

The Association Specialists Pty Ltd is a company that provides association management and conference management services. With a team of approximately 40 staff predominantly based in Sydney, the business supports professional and industry associations by handling their administrative operations and organising events.

On 8 April 2024, the long-standing financial controller of The Association Specialists gave notice of resignation, with his final working day set for 7 May 2024. On 6 May 2024, the company appointed a new financial controller, allowing for only one day of handover.

On 10 May 2024, Revenue NSW contacted the company regarding unpaid payroll tax for April 2024. The company paid the April tax on 13 May 2024. On 12 June 2024, the payroll tax for May 2024 was also paid. That same day, Revenue NSW reminded the company that its annual payroll tax return was due by 28 July 2024.

On 18 July 2024, the company's tax agent lodged the annual payroll tax return for the year ending 30 June 2024. The payroll tax for June was paid on 25 July 2024.

On 12 August 2024, Revenue NSW sent correspondence concerning unpaid payroll tax for July 2024. The company later stated that it did not receive this letter.

On 12 September 2024, Revenue NSW issued a payroll tax estimate assessment for the month of August 2024, which included $1,743.73 in penalty tax. The company paid this amount on 19 September 2024.

On 10 October 2024, Revenue NSW issued another assessment notice for July 2024 with $1,701.79 in penalty tax, as well as an assessment for September 2024 including $2,073.07 in penalty tax. The company paid the September amount on the same day, and Revenue NSW later reissued a revised assessment for September excluding the penalty tax.

On 15 October 2024, Revenue NSW emailed a copy of the July assessment again and updated its records to include the new financial controller as the contact. A new assessment for September 2024 without penalty tax was issued that day.

On 21 October 2024, the company formally requested a remission of the July penalty tax. It made a partial payment of the assessment on 31 October 2024, with the balance paid on 13 November 2024.

On 11 November 2024, Revenue NSW rejected the remission request. The company filed an objection on 12 November 2024, which was disallowed on 19 November 2024.

On 2 January 2025, the company filed an application with the NCAT seeking administrative review of the decision concerning the July penalty tax. On 21 January 2025, the company lodged a separate objection to the August 2024 penalty tax, which was disallowed on 29 January 2025.

On 4 March 2025, the NCAT allowed the administrative review application to be amended to include the decision regarding the August 2024 penalty tax.

The Association Specialists argued that it had taken reasonable care to comply with its payroll tax obligations, despite the timing of its financial controller's resignation and replacement. It emphasised that the new financial controller, who started on 6 May 2024, had only one day of handover and faced a significant workload in familiarising himself with the company's manual compliance systems. The company submitted that these transitional difficulties, which it viewed as beyond its control, were the sole cause of the tax defaults and should exempt it from penalty tax under section 27(3)(b) of the *Taxation Administration Act 1996 (NSW)* (**TAA (NSW)**). It also contended that the Chief Commissioner failed to follow his own stated commitments to act "with empathy," as promised in a document titled *Revenue NSW Customer Strategy 2022–2032*., The Association Specialists also referred to a previous occasion where penalty tax had been waived, suggesting that failure to do so in this instance constituted inconsistent treatment. Finally, it challenged the accuracy and fairness of the objection determination, claiming it contained unjustified implications about the company's honesty.

Issues

1. Was The Association Specialists entitled to a determination under section 27(3)(a) of the TAA (NSW) that no penalty tax was payable on the basis that it took reasonable care to comply with its taxation obligations?
2. Was The Association Specialists entitled to a determination under section 27(3)(b) of the TAA (NSW) that no penalty tax was payable on the basis that the tax defaults occurred solely because of circumstances beyond its control?

3. Should the Chief Commissioner's decision not to remit penalty tax under section 33 of the TAA (NSW) be set aside or varied on the basis that the discretion should have been exercised differently?

Decision

Reasonable care

The NCAT examined whether The Association Specialists Pty Ltd had taken reasonable care to comply with its payroll tax obligations during the period in question. It found that although the company acted promptly in appointing a new financial controller, there was no evidence of any structured handover process or steps taken to ensure continuity of compliance. The new financial controller received only one day of handover, was not provided with briefing materials or documentation about his payroll tax responsibilities, and no alternative compliance measures were put in place despite the availability of six accountants. Furthermore, no direct evidence was provided from the new financial controller to explain the delays, and an email he sent acknowledged that he was working with little knowledge of the company. These deficiencies indicated that the company had failed to implement reasonable systems to manage its tax obligations. The NCAT concluded that The Association Specialists had not taken reasonable care and was not entitled to a determination under section 27(3)(a) of the TAA (NSW).

Circumstances beyond control

In assessing whether the tax defaults occurred solely because of circumstances beyond the company's control, the NCAT accepted that the resignation of the financial controller was not within the company's control. However, it found that this alone was not sufficient. The critical failure lay in the company's lack of follow-up actions to mitigate the risk of non-compliance. The company did not assign alternative staff to manage payroll tax, failed to provide the new financial controller with the necessary support, and maintained a manual system that relied heavily on individual intervention. These were matters within the company's control. The legislative requirement under section 27(3)(b) is that the default must be caused solely by external factors. The NCAT concluded that The Association Specialists was not entitled to a determination under section 27(3)(b) of the TAA (NSW) because the defaults were not solely due to circumstances beyond its control.

Remission

The NCAT considered whether the Chief Commissioner's refusal to remit penalty tax under section 33 involved an improper exercise of discretion. It acknowledged that this provision grants a broad discretion but emphasised that the discretion should not undermine the statutory objectives of the penalty regime. In this case, the company had not demonstrated either reasonable care or circumstances entirely beyond its control. The NCAT found no "special circumstances" justifying a discretionary remission and rejected the company's argument that the Chief Commissioner had acted inconsistently or unfairly. It noted that the Commissioner's "commitments" document had no legal force and that an isolated past instance of remission did not establish a precedent. The NCAT concluded that there was no basis to disturb the exercise of discretion under section 33 of the TAA (NSW), and the penalty tax should not be remitted.

Citation *The Association Specialists Pty Ltd v Chief Commissioner of State Revenue* [2025] NSWCATAD 91 (EA MacIntyre, Senior Member)
w https://www.austlii.edu.au/cgi-bin/viewdoc/au/cases/nsw/NSWCATAD/2025/91.html

2.6 Zonadi – primary production land tax exemption

Facts

Zonadi Holdings Pty Ltd as trustee for the Wombat Investment Trust owned land in Pokolbin, NSW, during the 2020 to 2024 land tax years. The land was used for the production of wine grapes, including varieties such as Shiraz, Semillon, and Chardonnay.

Approximately 38% of the 11-hectare property was planted with vines. Open areas of the property not directly under vine were used for essential vineyard operations. These included turning areas for tractors, internal roads for machinery access, and designated spaces for storing vineyard materials such as posts, wires, compost, and mulch.

The remaining land included:

1. two unused areas consisting of trees (approximately 1.3 hectares);
2. a paddock (approximately 1.1 hectares);
3. tourist accommodation (approximately 660m^2);
4. a residence with an office and swimming pool, that was used on weekends by a director of Zonadi Holdings; and
5. cellar door, wine storage, and surrounding curtilage.

The total area of the tourist accommodation, residence, cellar door, cellar storage and surrounding area and curtilage was approximately 1.56 hectares.

The wine was produced offsite using only grapes cultivated on the land. The final product was returned to the property for sale and tasting at the cellar door, which was open on certain days and weekends. This activity was marketed as a “paddock to glass” operation.

Zonadi Holdings generated income through the sale of wine grapes, sale of wine (made from the grapes grown on the land), sale of other goods, and rental of tourist accommodation (available only to wine club members).

Evidence presented included tonnage of grapes sold versus used internally, revenue and profit breakdowns for grape and wine sales, and operational details around how grape sales were conducted. During the relevant years, wine sales consistently accounted for the majority of gross revenue, ranging from 80 to 94 percent annually, while income from grape sales and accommodation was comparatively minor.

On 31 August 2023, the Chief Commissioner notified Zonadi Holdings the land might be subject to land tax. On 22 January 2024, land tax assessments were issued for the 2020 to 2024 land tax years. Zonadi Holdings lodged objections to the land tax assessments on 15 March 2024, which were disallowed on 29 April 2024.

On 7 June 2024, Zonadi Holdings applied to the NCAT for review of the assessments.

The Chief Commissioner argued that Zonadi Holdings was not entitled to the land tax exemption under section 10AA(3)(a) of the *Land Tax Management Act 1956* (NSW) (**LTMA**) because the dominant use of the land was not the cultivation of grapes for the purpose of selling them. Instead, the Commissioner contended that the dominant use was cultivation for the purpose of making wine, which amounted to secondary production and, therefore, fell outside the scope of the statutory exemption for primary production.

The Commissioner submitted that section 10AA(3)(a) of the LTMA requires that cultivation must be for the purpose of selling the produce of the cultivation in its original form. In this case, the grapes grown by Zonadi Holdings were primarily used to produce wine, and that wine was then sold at the cellar door. The grapes themselves were not sold, and the Commissioner argued that when grapes are processed into wine, the resulting product is materially different from the original agricultural produce. Therefore, the use of the land for growing grapes that are later processed into wine could not satisfy the test of being cultivation for the purpose of selling the produce of the cultivation.

Further, the Commissioner referred to financial evidence showing that most of the revenue generated from the land came from wine sales, not from the sale of wine grapes.

Zonadi Holdings argued that it was entitled to a land tax exemption because the dominant use of its land was the cultivation of wine grapes for sale. The land was rural and largely devoted to viticulture, with around 38 percent planted with vines and other areas supporting vineyard operations.

While acknowledging that some grapes were used to make wine, Zonadi Holdings maintained that a significant portion of the grapes was sold each year. It submitted that the law required cultivation for the purpose of sale, not actual sale in every instance. Seasonal challenges and market conditions, it argued, occasionally limited sales but did not alter the land's intended and ongoing use.

Zonadi Holdings also claimed that its internal accounting showed greater profit from grape sales than from wine sales. It argued that profit, not gross revenue, should guide the assessment of dominant use. It asked the NCAT to recognise that its primary activity was growing grapes for sale and to overturn the land tax assessments.

Issues

1. Was the cultivation of the land for the purposes of producing wine grapes to make and sell wine a “primary production use” for the purposes of section 10AA(3)(a) of the LTMA?
2. Was the cultivation of the land for the purposes of selling wine grapes the “dominant use” of the land?

Decision

<u>Cultivation and winemaking</u>

Under section 10AA(3)(a) of the LTMA, for land to qualify for a primary production exemption, the cultivation must be for the purpose of selling the produce of the cultivation.

The Courts have clarified that this means the product grown must be the same as the product sold. The Court of Appeal in *CDPV Pty Ltd v Commissioner of State Revenue* [2017] VSCA 89 confirmed that if grapes are grown and then used to make wine (which is later sold), this does not meet the requirement, as wine is a processed product and not the same as the produce of cultivation.

Similarly, in *Caruana v Chief Commissioner of State Revenue* [2011] NSWADT 183, the Administrative Decisions Tribunal distinguished primary production (e.g., growing grapes) from secondary production (e.g., making and selling wine), noting that processing a crop into a different form breaks the direct connection between cultivation and sale.

In this case, the NCAT found that although Zonadi Holdings cultivated wine grapes, which qualifies as primary production, it retained ownership of the grapes and used them to make wine for its own business. These grapes were not sold as grapes. Instead, they were sold as wine, which is a processed product.

Since the sale involved wine, not grapes, this did not satisfy the requirement in section 10AA(3)(a). The NCAT found that the wine is considered a result of secondary production, and therefore, in respect of the grapes used to produce wine, there had been no cultivation of land for the purpose of selling the produce of that cultivation within the meaning of section 10AA(3)(a).

Dominant use

For land to be exempt from land tax under s 10AA(3)(a) of the LTMA, cultivation must be for the purpose of selling the produce of cultivation, and that purpose must be the dominant use of the land.

While most of the land was physically used for cultivation and required significant investment and labour, the purpose behind that cultivation was split. The NCAT assessed dominance based on several factors, including:

1. land area used for each purpose. The NCAT accepted that most of the land including the open areas used for activities related to cultivation was used for cultivation;
2. labour and investment intensity. Given that most of the land was used for cultivation, the NCAT accepted that this also attracted significant investment and labour compared to other uses; and
3. revenue generated from each activity.

Over each relevant land tax years, the overwhelming majority of revenue came from wine sales. Even in years where a higher tonnage of grapes was sold than used for wine, the financial return from winemaking far exceeded that from grape sales.

The evidence did not include any calculation of the net revenue derived from each activity carried out on the land, when costs attributable to each activity were deducted from gross revenue. Zonadi Holdings was given the opportunity at the hearing to make further submissions on this issue but declined to do so.

The NCAT held that hypothetical or intended sales were insufficient to displace the actual financial outcomes of land use. There was no credible evidence to establish what grape sales would have been under different conditions.

Having regard to the proportionate land area used for cultivation, the level of investment and labour deployed to cultivate the land and the resulting intensity of that use, the NCAT accepted that the cultivation of the land, taken as whole, was the most important use of the land. However, the NCAT stated that the determination of what is the dominant use of the land will turn substantially on the relative financial gains from each use. The weight attaching to the significantly higher financial gain from making and selling wine allowed the NCAT to find that the dominant use of the land was the cultivation of wine grapes for making and selling wine

Although cultivation was clearly the dominant physical use, the NCAT held that the dominant purpose of that cultivation was found to be producing grapes to make and sell wine, based on the revenue and investment patterns.

As a result, the NCAT concluded that Zonadi Holdings did not satisfy section 10AA(3)(a) of the LTMA because the cultivation was not primarily for the purpose of selling the produce of cultivation. The dominant use was cultivation for winemaking. The Chief Commissioner’s assessment was confirmed.

COMMENT – the weight given to financial return in this case as a key factor in determining dominant use contrasts with the weight given to that factor in *Godolphin Australia v Chief Commissioner of State Revenue* [2024] HCA 20, where the High Court found that dominant use could be established based on land use and investment, even where that activity operated at a loss. The NCAT in this case did emphasise that determining dominant use requires a holistic, fact-specific assessment considering land area, intensity of use, time and labour, resources, and financial gain.

Citation *Zonadi Holdings Pty Ltd ATF Wombat Investment Trust v Chief Commissioner of State Revenue* [2025] NSWCATAD 84 (EA MacIntyre, Senior Member)
w https://www.austlii.edu.au/cgi-bin/viewdoc/au/cases/nsw/NSWCATAD/2025/84.html

2.7 VBNX – serious hardship

Facts

In 1989, VBNX permanently relocated to Australia from Lebanon. In 2001, he sold his family home and used the proceeds of sale to start a restaurant business. In 2002, there was a fire at VBNX's restaurant causing serious injury to VBNX.

From 2002 onwards, VBNX started receiving income protection insurance payments which were taxable. In 2009, VBNX divorced his wife and moved back to Lebanon. A short while after, the rest of his family including his ex-wife and children moved back to Lebanon and resided with VBNX.

In 2021, VBNX and his family returned to Australia due to unsafe circumstances in Lebanon. Between 2002 to 2021, VBNX accumulated $528,307.08 in tax debt including income tax, penalties for late lodgment, PAYG liabilities and general interest charge.

In April 2021, VBNX and his family returned to Australia, citing unsafe conditions in Lebanon. He claimed to have borrowed between US$20,000 and US$31,000 for the return and repaid these loans. VBNX resumed efforts to manage his tax affairs, signed up to MyGov, and engaged a tax agent to assist with overdue returns.

On 16 June 2021, the ATO issued a letter stating that $157,386.25 of VBNX's debt was "uneconomical to pursue," which VBNX mistakenly interpreted as a release from that debt. A small amount of interest was remitted, but the principal remained.

On 25 November 2022, VBNX formally applied to the ATO for release from his tax debts, citing serious hardship. This request was refused on 18 April 2023. He objected on 14 June 2023 and supplemented that objection on 6 September 2023. The ATO disallowed the objection on 13 November 2023.

On 25 November 2022, VBNX requested to be released from the relevant tax debt due to serious hardship, however, this request was refused by the Commissioner. VBNX objected to the refusal and supplemented his objection, however, the objection was also disallowed by the Commissioner. This led to VBNX filing an application with the ART on 13 December 2023.

In the interim, he continued receiving $8,019 per month from income protection insurance, supplemented by approximately $2,000 from family contributions, mainly from his ex-wife, who was on a sickness benefit. He paid about $3,336 per month in rent and other living expenses, and while he made some PAYG instalments, these were insufficient to meet current tax liabilities.

By March 2025, VBNX's tax debt had reached over $528,000, with approximately $148,000 in interest. He claimed to have only a modest surplus of $177 per month after expenses, and further debts such as medical costs and child support loomed. Despite his assertions, he had made no repayments toward older debts and continued discretionary spending on items like lottery tickets and vape products.

VBNX submitted that his mental and physical health and the associated dysfunction had not been considered by the Commissioner or, alternatively, not given enough weight. VBNX explained that, as a result of his physical and mental condition, he was not able to work and required ongoing medication with debilitating side effects exacerbated by the stress of his tax debts. VBNX submitted that his diminished responsibility should be considered when assessing the failure to meet his taxation obligations.

Issues

1. Was VBNX in "serious hardship"?
2. Should the Commissioner's discretion under section 340-5 of Schedule 1 of the TAA be exercised in light of all circumstances, including fairness and administrative justice?

Decision

Serious hardship

The ART clarified that the law does not state that tax is relieved if there is an illness and states that there is no defence of "diminished responsibility" at taxation law therefore the tax liabilities of VBNX remain regardless of his health condition.

The term "serious hardship" is not defined in legislation and the ART must exercise its judgement when evaluating the evidence to make a determination.

The ART found that VBNX was in serious hardship and accepted that he was unable to pay his tax liabilities without severe financial consequences. His limited income, inability to work due to medical issues, dependants, and lack of assets were all factors supporting this finding, despite some shortcomings in household financial disclosures.

Exercise of discretion

The ART applied the three tests outlined in *Practice Statement Law Administration 2011/17* to determine whether the discretion under section 340-5 of Schedule 1 of the TAA should be applied. The three tests are:

1. the income/outgoing test: The ART considered that the VBNX 's monthly income of approximately $8,000 came from his income protection insurance where a significant proportion of that amount was contributed to his rent, utilities, groceries and other essential items. There was also some discretionary spending towards tobacco and lotto which only led to a surplus of $177 each month. The ART agreed that payment the tax debt would place VBNX in even greater financial debt or even bankruptcy but believed that adjustments could be made by the VBNX's lifestyle so that contributions, even if marginal, could be made towards the tax debt such as downsizing from a 4-bedroom 4-bathroom home and having other members of the household could contribute more towards the monthly expenses;
2. the assets/liabilities test: the ART concluded that VBNX had little to no assets which could be liquidated to meet his tax liabilities; and
3. other relevant factors: The ART found that VBNX had completely failed to make any payments toward his tax debt over an extended period, showing a lack of seriousness and a disregard for his legal obligations. His tax compliance history was extremely poor, with tax debts accumulating for about 20 years and consistently failing to lodge returns on time. Despite knowing these obligations, he remained in arrears and did not take any action to resolve them, including underpaying his current PAYG instalments. VBNX attempted to shift responsibility to the Commissioner, arguing that payments would have been made if a payment plan had been accepted, and that he did not receive notices while overseas. However, the ART rejected these claims. The ART accepted that the Commissioner had attempted to engage with VBNX before his departure to Lebanon in 2009, and that VBNX's decision to ignore those communications and repay other debts instead of his tax liabilities contributed to the growth of his debt. While the ART acknowledged VBNX had received substantial income from insurance payments over the years, it also recognised VBNX's current and future financial and health hardships.

Balancing these competing considerations, the ART concluded that while a full release of the debt was not appropriate due to VBNX's history of non-compliance, a partial release was justified to reflect his serious hardship and lack of realistic ability to repay the full debt. The decision aimed to give VBNX a chance to move forward and fulfil his obligations like any other taxpayer.

The ART exercised the discretion to partially release VBNX from the tax debt by reducing the income tax liability to $250,000 and cancelling all GIC accrued to the date of judgment.

TRAP – the serious hardship relief under Division 340 is only available for individuals and it only applies to certain liabilities. It does not cover GST debts or associated interest charges. It is generally limited to income tax, PAYG instalments, and related penalties and interest, so practitioners should always check section 340-10 of the TAA and ATO guidance to confirm eligibility.

TIP – When preparing an application for release from tax debt on grounds of serious hardship, it is essential to align the submission with the three-pronged approach outlined in *Practice Statement Law Administration PS LA 2011/17*. This includes clearly addressing: (1) the income/outgoings test, showing the taxpayer cannot meet essential living costs while repaying the debt; (2) the assets/liabilities test, demonstrating that available assets are insufficient or inappropriate to liquidate; and (3) other relevant factors, such as compliance history, medical conditions, and efforts to address debts. Tailoring the evidence and arguments to these criteria can significantly strengthen the case and pre-empt common objections from the Commissioner.

Citation *VBNX v Commissioner of Taxation (Taxation and business)* [2025] ARTA 374 (General Member J Dunne, Melbourne) w https://www.austlii.edu.au/cgi-bin/viewdoc/au/cases/cth/ARTA/2025/374.html

3. Cases in brief

3.1 XRXR – objection to private ruling

XRXR was a senior employee and director at the Australian arm of a foreign company. Tensions arose in the workplace, primarily over disagreements concerning transfer pricing compliance, which XRXR believed was being mishandled. These tensions led to allegations that XRXR was being excluded, had his reputation damaged, and was being pressured to resign. In June 2023, he filed a General Protections Application with the Fair Work Commission, claiming coercion and undue pressure, particularly in relation to his efforts to uphold legal standards. On 20 June 2023, his employer formally notified him that he had been removed from all director roles, stripped of official communication access, placed under investigation, and directed not to contact colleagues or clients. A conciliation conference on 26 June 2023 resulted in a settlement and the signing of a Deed of Release. Under this Deed, XRXR agreed to resign and waive all claims in return for a payment of $259,000, comprising $189,000 for 12 months' pay in lieu of notice and a $70,000 ex-gratia amount. The employer's income statements recorded the full payment as a taxable employment termination payment.

XRXR later sought a private ruling from the ATO to determine whether the payment qualified for concessional treatment as an "excluded payment" under section 82-130(1)(d) of the ITAA 1997. The ATO's first ruling classified the amount as an employment termination payment but did not address whether it was excluded. After XRXR objected, the ATO agreed to issue a second ruling focused on this issue. In the second ruling, the Commissioner determined that the payment did not qualify as an excluded payment. This was based on the Deed's language, which referred to the payment as being in lieu of notice, lacked any admission of liability, described the payment as a termination payment, and indicated a voluntary resignation. XRXR objected again, arguing that the ATO had placed too much emphasis on the Deed while ignoring key facts, such as his experiences of harassment and the Fair Work claim. When the objection was disallowed, XRXR sought a review with the ART.

A preliminary issue was whether the ART had jurisdiction to hear the review given that a tax assessment had already been issued for the same income year. This raised a legal question under section 359-60 of Schedule 1 to the TAA which states that a taxpayer cannot object to a private ruling if there is already an assessment on foot for the same year concerning the same matter. Because both the objection and the application for review were lodged before the assessment, the ART concluded that section 359-60 did not apply to bar the review.

The second issue was whether the ART could consider additional evidence beyond what was in the scheme outlined in the private ruling. The ART concluded it was bound by the scheme, which did not include details about the alleged harassment, reputational damage, and pressure to resign, meaning such evidence could not be taken into account. These omissions limited the ART's ability to consider the broader context.

On the substantive issue of whether the termination payment was "excluded", the ART found that within the scheme of the ruling, there was insufficient evidence to conclude that the payment was made principally for harassment or discrimination. Although some indications of workplace mistreatment existed, they were not shown to be the main reason for the payment. Instead, the payment appeared to serve other purposes, such as facilitating a resignation, and followed the language of the Deed, which stated it was in lieu of notice. There was no suggestion that the Deed was signed under duress or misrepresented the parties' true agreement. The ART ultimately found that the payment was made in connection with the termination of employment, consistent with its classification as an employment termination payment. The Commissioner's decision was upheld.

COMMENT – The ART in this case expressed concern that by omitting facts or categorising them as "contentions" rather than part of the scheme, the Commissioner may improperly limit review. The ART recommended that the Commissioner adopt a better practice of providing draft schemes to taxpayers for review before finalising private rulings, due to the legal consequences of how the scheme is framed.

Citation *XRXR v Commissioner of Taxation (Taxation and business)* [2025] ARTA 357 (General Member J Dunne, Melbourne)
w https://www.austlii.edu.au/cgi-bin/viewdoc/au/cases/cth/ARTA/2025/357.html

3.2 Merchant – dividend stripping and Part IVA

The taxpayer has been largely unsuccessful in its appeal from the decision in *Merchant v Commissioner of Taxation* [2024] FCA 498 (see our June 2024 Tax Training Notes for a full summary of the facts in the case).

In September 2014, Gordon Merchant (No 2) Pty Ltd (**GM2**), as trustee of the Merchant Family Trust (**MFT**), transferred approximately 10 million shares in Billabong International Ltd (**BBG**) to GSM Superannuation Pty Ltd (**GSMS**) the trustee of the Gordon Merchant Superannuation Fund (**Fund**), realising a capital loss of over $56 million.

This transaction generated a capital loss of over $56 million.

In April 2015, GM2 sold shares it held in Plantic Technologies Pty Ltd to a Japanese company (**Kuraray Co Ltd**), generating a capital gain of approximately $85 million.

As part of the Plantic sale to Kuraray, intra-group loans totalling approximately $55 million from Tironui Pty Ltd and GSM Pty Ltd, companies in the Merchant group, were forgiven.

The forgiveness enhanced the sale value of Plantic shares, indirectly benefiting GM2 and associated entities.

The Commissioner asserted that the BBG share transfer was part of a tax avoidance scheme to offset the expected capital gain on Plantic shares, invoking section 177D of the ITAA 1936 on the basis that the scheme had the dominant purpose of securing a tax benefit.

The capital loss was disallowed, significantly increasing MFT's net income (from $5,482,423 to $28,111,179) and the tax payable by GSM Pty Ltd (by $12,877,000.90), as the beneficiary presently entitled to the income of the MFT for the year. A 50% penalty (of $6,438,500.45) was also imposed on GM2 as the trustee of the MFT.

The Commissioner also contended that the forgiveness of loans constituted dividend stripping schemes under section 177E, as profits of Tironui Pty Ltd and GSM Pty Ltd were extracted tax-free.

The Commissioner included the forgiven amounts in Gordon's assessable income, as the sole shareholder of GSM Pty Ltd and Tironui Pty Ltd, and sought to tax them accordingly.

Gordon had also claimed deductions for the expiration of rights to Milestone and Earn-Out payments from the Plantic sale in 2017 and 2018. These rights were contingent on post-sale business performance.

A further dispute concerned whether the expiration of certain future payment rights (Milestone and Earn-Out Amounts from the Plantic sale) in the 2017 and 2018 income years gave rise to deductible losses under the Taxation of Financial Arrangements (**TOFA**) provisions. These rights were contingent on certain sales targets being met, and expired when those targets were not achieved. The primary judge held that the TOFA provisions did not apply because a statutory exception was satisfied. Although it was not essential to the outcome, the judge also found that these rights constituted financial arrangements.

BBG Share Scheme

At first instance, the primary judge upheld the Commissioner's determination, finding the transaction lacked commercial substance and served no legitimate purpose.

Gordon contended that the primary judge applied a subjective test rather than the objective one required by section 177D(2) of the ITAA 1936.

The majority of the Full Court held that the judge correctly applied an objective analysis, reviewing events in a chronological and evidentiary manner.

The majority of the Full Court noted the following factors for the purpose of 177D(2):

1. No change in control or economic ownership: The Court emphasised that the BBG share sale did not alter the control or economic ownership of the shares within the Merchant Group. Despite the sale, the risk of ownership and the benefits of being a shareholder remained unchanged. The Court supported the view that the scheme was primarily aimed at obtaining a tax benefit, not altering ownership or control;
2. timing of the sale: The Court found that the sale was reasonably timed to coincide with the possibility of selling Plantic to Sealed Air. The likelihood of the Plantic sale happening by September 2014 made it logical to proceed with the BBG share sale at that time. Gordon did not provide a compelling reason for why the sale timing needed to be different;
3. inconsistent with the fund's investment strategy: The Court noted that the transfer of BBG shares to the Fund contradicted the Fund’s documented investment strategy. The strategy aimed for high growth and diversification, but the acquisition of non-dividend-paying BBG shares significantly reduced the Fund's income, which was inconsistent with the Fund's objectives; and
4. tax benefits and financial position: The Court concluded that the BBG share sale resulted in crystallising significant capital losses, which could be offset against the anticipated gains from the sale of Plantic. This provided a substantial tax benefit, improving the MFT’s financial position without immediate tax consequences.

The majority of the Full Court confirmed that the dominant purpose of the BBG share sale arrangement was to obtain a tax benefit.

Debt forgiveness arrangements

The majority of the Full Court reiterated that for an arrangement to be caught as a dividend stripping arrangement under section 177E to apply the following must be satisfied:

1. there must be a scheme by way of or in the nature of dividend stripping;
2. the scheme must have a dominant tax avoidance purpose; and
3. the scheme must have the substantial effect of dividend stripping — i.e. substitution of a non-taxable capital benefit for a taxable dividend.

<u>Scheme 1: Tironui Loan Forgiveness</u>

The majority of the Full Court noted that the forgiveness depleted almost all of Tironui’s retained earnings and enabled the MFT (being an entity associated with Gordon) to receive capital proceeds without tax. The capital gains were sheltered by available capital losses, including those from the BBG share scheme.

The majority held that this had the substantial effect of dividend stripping as it enabled Gordon's associate to receive untaxed capital proceeds while avoiding potential tax on distributions of profits

<u>Scheme 2: GSM Loan Forgiveness</u>

This involved forgiveness of approximately $50 million, but GSM had retained earnings of over $218 million.

The capital gain arising could not be entirely offset due to the cancellation of the BBG loss as a result of the application of section 177D.

GSM was assessed on a $33.91 million capital gain but with no corresponding entitlement to the income under trust law.

The majority held that the arrangement did not to have the substantial effect of dividend stripping, as the cancellation of the BBG loss prevented the arrangement from operating as intended and, therefore, it did not have a substantial dividend stripping effect.

The majority noted that a dividend stripping analysis involves examining purpose, effect, and content.

The majority considered that the adopted a rigid “all or nothing” approach — there was no explanation for failing to consider partial adjustments under section 177F(1) or (3).

The majority made it clear court that section 177E does not override the need for a substantial dividend stripping effect, despite the Commissioner’s discretion under section 177F(1) to make partial adjustments.

TOFA deductions claim

The primary judge found that the TOFA exception applied. This exception covers rights arising from the sale of a business (or shares in a company operating a business) that are contingent only on the economic performance of the business after the sale (section 230-460(13) of the ITAA 1997. The majority Full Federal Court accepted that the exception under section 230-460(13) applied such that the TOFA provisions did not apply to the expired rights. This meant the MFT was not entitled to TOFA deductions, but rather the losses were to be treated as capital losses.

Citation *Merchant v Commissioner of Taxation* [2025] FCAFC 56 (Logan, McElwaine and Hespe JJ, New South Wales)
w https://www.austlii.edu.au/cgi-bin/viewdoc/au/cases/cth/FCAFC/2025/56.html

3.3 Evans – input tax credits

Anthony Evans claimed to be the public officer for ‘ANTHONY WILLIAM EVANS, a non-resident unincorporated association identified by a TFN. This "entity" sought over $30 million in GST refunds based on input tax credit claims allegedly in relation to acquisitions made by the entity from Anthony.

The Commissioner denied the credits, cancelled the "entity’s" GST and ABN registrations, and issued administrative penalties nearing $28 million. Anthony objected to these decisions, but the Commissioner disallowed the objections. When Anthony applied to the ART to review these decisions, the Commissioner sought dismissal, arguing the applications were baseless and an abuse of process. The ART agreed in part, finding there was no credible basis to establish the alleged entity as distinct from Anthony himself. As a result, the applications concerning the GST and ABN cancellations and the input tax credit claims were dismissed.

However, the ART declined to dismiss the application related to the administrative penalties, noting the seriousness of the penalties and the need for a proper hearing to assess whether Anthony intentionally disregarded the law or whether any remission might be justified. The ART ordered the parties to submit programming directions for preparing that remaining issue for hearing.

TRAP – the ART noted that that the Full Federal Court in *Dixon v Commissioner of Taxation* [2008] FCAFC 54 held that the fact that the Commissioner did not pay the ITC refunds is not relevant to whether administrative penalties should be remitted. A "shortfall" refers to the difference between the tax properly payable and the amount reported by the taxpayer. If a taxpayer incorrectly claims ITCs to which they are not entitled, the overstated credit results in a shortfall in the amount payable, regardless of whether the Commissioner issues the refund. Therefore, the penalty regime can still apply because the legal focus is on entitlement and accuracy of reporting, not the disbursement of funds.

Citation *Evans and Commissioner of Taxation (Practice and procedure)* [2025] ARTA 545 (Senior Member R Olding, Brisbane)
w https://www.austlii.edu.au/cgi-bin/viewdoc/au/cases/cth/ARTA/2025/545.html

3.4 Sim – exemption from duty for transfer to spouse

On 22 February 2019, Ms Dan Sim, a citizen of South Korea purchased a property in Alphington, Victoria.

At the time of the purchase, Dan was living in Australia on a Partner (Temporary) (class UK) (subclass 820) visa, sponsored by Mr Alan Sam, her Australian partner. Dan was the sole registered proprietor of the property and duty was originally imposed on the transfer at the general rate.

In November 2021, the Commissioner of State Revenue re-assessed the transfer and imposed Foreign Purchaser Additional Duty in the amount of $74,653.25, being 7% of the purchase price. Penalty tax of 20% and market interest was also imposed.

Dan objected to the reassessment on the basis that the transfer was made solely to her because of the advice she and Alan received from their accountant that it would be better for the property to be in Dan's name due to Alan's business interests, noting that they had encountered some difficulties. While the objection was denied, the Commissioner remitted penalties and interest entirely.

Dan applied to the VCAT to review the decision, relying on a new ground being that an exemption from Foreign Purchaser Additional Duty under section 69AJ of the Duties Act applied. The exemption applies where:

(a) *the foreign purchaser is a foreign natural person who is the spouse or domestic partner of a natural person who is not a foreign natural person; and*

(b) *the land-related interest in residential property is transferred jointly to the foreign purchaser and the foreign purchaser's spouse or domestic partner; and*

(c) *subject to section 69AK, the foreign purchaser occupies the residential property as the foreign purchaser's principal place of residence for a continuous period of at least 12 months commencing within the 12 month period immediately after the foreign purchaser becomes entitled to possession of the residential property.*

The Commissioner accepted that the requirements set out in (a) and (c) were met but did not accept that requirement (b) had been met i.e. that the land-related interest was 'transferred jointly' to Dan and Alan.

Dan argued that Alan acquired an equitable interest in the property under a purchase price resulting trust. This was based on the fact that Alan was the named purchaser in the contract of sale (Dan was later nominated to take the transfer), Alan paid majority of the deposit, the balance of loan was secured by way of a joint mortgage, and the parties intended for Alan to have an equitable interest.

The Commissioner argued it was irrelevant whether the property was held on a resulting trust, because the fee simple estate (i.e. the related land-interest) was not "*transferred jointly*" to Alan and Dan. Simply, the fee simple was transferred solely to Dan – there was no joint transfer.

The VCAT found in favour of the Commissioner. The requirement of section 69AJ(b) of the Duties Act was not met as the land was transferred solely to Dan and was not transferred to Dan and Alan jointly. The VCAT agreed with the Commissioner's submission that even if Alan held an equitable interest in the property via a resulting trust, there was no legal transfer of title to Alan.

Citation *Sim v Commissioner of State Revenue (Review and Regulation)* [2025] VCAT 349 (Senior Member Reynah Tang AM, Melbourne)
w https://www.austlii.edu.au/cgi-bin/viewdoc/au/cases/vic/VCAT/2025/349.html

3.5 Sar – remission of interest

Eng Huat Sar is a citizen of Malaysia and Singapore and has been a holder of an Australian permanent resident visa since 1999. In 2004, his place of employment was transferred from Australia to Singapore, where he worked while his family remained in Australia. On 30 June 2018, Eng Huat entered into a contract to purchase a residential property in St Marys, NSW (**Property**).

On 17 August 2018, Eng Huat completed a 'Purchase/Transferee Declaration' form and indicated he was ordinarily resident in Australia and not a foreign person. He also indicated that he was an exempt permanent resident who would occupy the Property as his principal place of residence for a continuous period of 200 days within the first 12 months after the 30 June 2018 contract date.

Eng Huat's wife and her son moved into the property on 2 December 2018, when the vendors vacated the property, and Eng Huat resigned from his job in Singapore on 7 December 2018. However, Eng Huat remained in Singapore until 24 December 2018 in order to maximise the entitlements he was due to receive from his employer at the time of his actual departure from employment. Eng Huat subsequently used and occupied the Property as his principal place of residence from 24 December 2018 onward. However, his use and occupation of the property was 22 days short of the required 200 days requirement in the 12-month period since the 30 June 2018 contract date.

On 6 October 2022 the Chief Commissioner issued a Notice of Investigation to Eng Huat. Eng Huat declared that he had occupied the Property as his principal place of residence since 2 December 2018, on the basis that his wife and her son had moved into the property on that date. The Chief Commissioner issued a Notice of Assessment on 29 March 2023 to Eng Huat which confirmed that he did not meet the residency requirement and was liable for surcharge purchaser duty.

In April 2023, Eng Huat paid all outstanding tax and interest in relation to the surcharge purchaser duty. Subsequently, Eng Huat filed an application for review against the Chief Commissioner seeking the remission of interest.

The NCAT referred to the discretionary nature of the Chief Commissioner's power to remit interest in its review of Eng Huat's application. Eng Huat did not assert that the Chief Commissioner had contributed to his tax default. The NCAT had previously found that he had not commenced using and occupying the Property as his principal place of residence when his wife moved in. Further, his reasons for remaining out of Australia were in order to maximise his employment entitlements, rather than because of any delay or circumstances that were beyond his control. Accordingly, the NCAT held that there were no circumstances, let alone exceptional circumstances, that would justify any remission of general interest under the Chief Commissioner's discretionary power per section 25 of the *Taxation Administration Act 1966* (NSW).

Additionally, the NCAT noted, with reference to the judgments in *Chief Commissioner of State Revenue v Incise Technologies Pty Ltd* [2004] NSWADTAP 19 and *Golden Age and Hannas the Rocks Pty Ltd v Chief Commissioner of State Revenue* [2024] NSWSC 249, it is relevant to the exercise of the Chief Commissioner's discretion in section 25 (being the remission of the premium component of interest) whether the taxpayer has taken reasonable steps to comply with taxation law. As Eng Huat provided no submissions to the NCAT regarding what steps, if any, he took to comply with the taxation law, the NCAT found no basis to exercise the discretion to remit the premium component of interest.

Citation *Sar v Chief Commissioner of State Revenue (No 2)* [2025] NSWCATAD 97 (Senior Member S Higgins, New South Wales) w https://www.austlii.edu.au/cgi-bin/viewdoc/au/cases/nsw/NSWCATAD/2025/97.html

3.6 Appeal updates

Shaw

The Commissioner has appealed to the Federal Court from the ART decision in *Shaw v Commissioner of Taxation* [2025] ARTA 224 (see our April 2025 Tax Training Notes). The decision concerned whether a long-haul truck driver was entitled to deduct meal expenses under section 8-1 of the ITAA 1997. The ART held there was a sufficient link between the expenditure on driver's bank statements and his work, and that the substantiation provisions in sections 900-50 and 900-200 of the ITAA 1997 applied.

Agrinova

Agrinova Pty Ltd appealed to the Appeal Panel from the NCAT decision in *Agrinova Pty Ltd v Chief Commissioner of State Revenue* [2024] NSWCATAD 170 (see our July 2024 Tax Training Notes). The decision concerned whether section 90 of the *Family Law Act* applied to exempt transfers of land from duty. The Appeal Panel dismissed the appeal.

3.7 Other tax and super related cases published from 10 Apr 2025 to 13 May 2025

Citation	Date	Headnote	Link
Hyder v Commissioner of Taxation [2025] FCA 337	10 April 2025	PRACTICE AND PROCEDURE – applications for leave to appeal from exercise of costs discretion – applications dismissed	https://www.austlii.edu.au/cgi-bin/viewdoc/au/cases/cth/FCA/2025/337.html
GWP v Chief Commissioner of State Revenue [2025] NSWCATAD 88	22 April 2025	TAXES AND DUTIES – transfer duty – purchase of property off the plan - tax default – discretion to remit market and premium interest – exceptional circumstances – reasonable care	https://www.austlii.edu.au/cgi-bin/viewdoc/au/cases/nsw/NSWCATAD/2025/88.html
Haines and Commissioner of Taxation (Practice and procedure) [2025] ARTA 461	24 April 2025	PRACTICE AND PROCEDURE – reinstatement of application for review by Tribunal of objection decision – application for review previously dismissed when applicant withdrew – whether appropriate to reinstate – factors to be considered - reinstatement application made more than 28 days after dismissal – whether special circumstances exist – application for reinstatement granted	https://www.austlii.edu.au/cgi-bin/viewdoc/au/cases/cth/ARTA/2025/461.html
Djuric and Commissioner of Taxation (Practice and procedure) [2025] ARTA 469	29 April 2025	PRACTICE AND PROCEDURE – Applicant failed to meet Tribunal directions within a reasonable time – Proceedings dismissed under section 100 of the Administrative Tribunal Act 2024 (Cth) – Reinstatement application under section 102 granted as “appropriate” to do so - accompanying orders – warning to Applicant	https://www.austlii.edu.au/cgi-bin/viewdoc/au/cases/cth/ARTA/2025/469.html
Alcoa of Australia Ltd and	30 April 2025	TAXATION – transfer pricing and arm’s	https://www.austlii.edu.au/c

Citation	Date	Headnote	Link
Commissioner of Taxation (Taxation and business) [2025] ARTA 482		length consideration provisions – Division 13 of the Income Tax Assessment Act 1936 (Cth) – interpretation of s 136AD(1) – burden of proof - sales of alumina to independent parties overseas – no profit shifting within the taxpayer group of companies – relevance of bribery and corruption admissions in United States proceedings as to whether the parties were dealing at arm's length – relevance of price negotiations to whether the parties were dealing at arm's length – tripartite international agreement under s 136AC – consideration of what property was supplied under an international agreement for the purposes of s 136AD(1)(a)) – whether satisfied, having regard to any connection between 2 or more of the parties or to any other relevant circumstances, that the parties to the agreement were not dealing at arm's length with each other in relation to the supply for the purposes of s 136AD(1)(b) – relevance of supply of property to another party – whether consideration received by the taxpayer was less than arm's length consideration under s 136AD(1)(c) – extent of depersonalisation required for a hypothesised agreement for the purpose of determining arm's length consideration under s 136AA(3)(c) – where experts adopted different approaches – whether to determine that s 136AD(1) applies in relation to the taxpayer – finding that Tribunal not satisfied parties were dealing at arm's length with each other in relation to the supply but satisfied the consideration received by the taxpayer was not less than arm's length consideration in respect of the supply – decision to set aside the decision of the Commissioner disallowing taxpayer's objections against assessments and substitute it with a decision allowing each of the applicant's objections in full	gi-bin/viewdoc/au/cases/cth/ARTA/2025/482.html
Nguyen v Chief Commissioner of State Revenue [2025] NSWCATAD 99	6 May 2025	TAXES AND DUTIES – surcharge purchaser duty – principal place of residence exemption – remission of market rate of interest – remission of premium rate component of interest	https://www.austlii.edu.au/cgi-bin/viewdoc/au/cases/nsw/NSWCATAD/2025/99.html
Sun v Chief Commissioner of State Revenue [2025] NSWCATAD 103	7 May 2025	ADMINISTRATIVE LAW – administrative review – assessment - objection – review by Civil and Administrative Tribunal	https://www.austlii.edu.au/cgi-bin/viewdoc/au/cases/nsw/

Citation	Date	Headnote	Link
		STATE TAXES - land tax - surcharge land tax - exemption - whether exemption under Land Tax Act 1956 applies to surcharge land tax - permanent resident - statutes read and construed together - unfairness	NSWCATAD/2025/103.html
Deputy Commissioner of Taxation v Peever [2025] FCA 460	9 May 2025	PRACTICE AND PROCEDURE — Principle of open justice – Suppression or non-publication order – Where a non-party request was made by the media under r 2.32 of the Federal Court Rules 2011 (Cth) – Access was sought to submissions — Whether order necessary to prevent prejudice to the proper administration of justice — Federal Court of Australia Act 1976 (Cth), Part VAA, ss 37AE, 37AF, 37AG and 37AJ — non-publication order made, in part.	https://www.austlii.edu.au/cgi-bin/viewdoc/au/cases/cth/FCA/2025/460.html
Tong v Chief Commissioner of State Revenue [2025] NSWCATAD 105	12 May 2025	ADMINISTRATIVE LAW - administrative review - assessment - objection - review by Civil and Administrative Tribunal STATE TAXES - surcharge land tax - foreign person - ordinarily resident - 200 days - exemption - discretion – unfairness	https://www.austlii.edu.au/cgi-bin/viewdoc/au/cases/nsw/NSWCATAD/2025/105.html

4. Federal Legislation

4.1 Progress of legislation

Title	Introduced House	Passed House	Introduced Senate	Passed Senate	Assented
Superannuation (Better Targeted Superannuation Concessions) Imposition Bill 2023	30/11	9/10	10/10		
Treasury Laws Amendment (Better Targeted Superannuation Concessions and Other Measures) Bill 2023	30/11	9/10	10/10		

5. State legislation

5.1 WA – duty concession for first home buyers

On 9 April 2025, the *Duties Amendment Bill 2025* (WA) was introduced to the Parliament of Western Australia to expand the duty concessions for off-the-plan constructions, and for first home buyers. The amendments were set out in our April 2025 Tax Training Notes.

To be eligible for the first home owner duty concession, the purchaser must:

1. qualify for the first home owner grant under the *First Home Owner Grant Act 2000* (WA), or
2. have qualified for the grant if they had purchased a new home, or paid consideration for the transaction.

The Bill also introduces a higher concessional threshold for homes purchased and constructed outside of the Perth and Peel regions.

The off-the-plan duty concession has been extended from 30 June 2025 until 30 June 2026. Dwellings on survey-strata plans will not be eligible for the concession.

The revised duty concessions will apply to transactions entered into on or after 21 March 2025.

w https://www.parliament.wa.gov.au/parliament/bills.nsf/BillProgressPopup?openForm&ParentUNID=D83AFDAC0B9A49D248258C67000BE0FE

5.2 Guidelines for approving shares equity schemes made (NSW)

New guidelines have been issued by the Treasurer, under section 281 of the *Duties Act 1997* (NSW), as Statutory Instrument 2025-184.

Section 281 of the Duties Act provides for the Chief Commissioner of State Revenue to approve a shared equity scheme for the purposes of transfer duty and land tax. A shared equity scheme is where a home buyer jointly purchases a property with an equity partner, such as government or private entity. The home buyer has the exclusive right to occupy the property, and equity partner contributes finance for the purchase as a mortgagee.

The guidelines are designed to allow flexibility in the development of shared equity schemes and to encourage innovation to better meet the needs of homebuyers.

If the scheme is approved:

1. the buyer may access, subject to normal eligibility rules, first home buyer benefits (such as grants and duty exemptions) and land tax exemptions (such as the principal place of residence); and
2. if the buyer later increases their share in the ownership of the property, no additional transfer duty applies.

The guidelines commenced on 24 April 2025.

w https://legislation.nsw.gov.au/view/pdf/asmade/sl-2025-184

6. Rulings

6.1 Thin cap rulings withdrawn

The ATO has withdrawn *Taxation Ruling* IT 2479W *Income tax: application of thin capitalisation rules* with effect from 10 April 2025. The withdrawal has been made as the ruling no longer reflects the current thin capitalisation rules.

Former Division 16F of th ITAA 1963 was repealed in 2001, and replaced by Division 820 of the *Income Tax Assessment Act 1997*. The thin capitalisation rules in Division 820 have since again been amended by the *Treasury Law Amendment (Making Multinationals Pay Their Fair Share — Integrity and Transparency) Act 2024*, for income years commencing on or after 1 July 2023, with the exception of new integrity rules (debt deduction creation rules) which apply in relation to assessments for income years starting on or after 1 July 2024.

ATO reference *IT 2479W*
w https://www.ato.gov.au/law/view/document?docid=ITR/IT2479/NAT/ATO/00001

6.2 Queensland – Updates to duties practice directions and rulings

On 1 May 2025, the Queensland Revenue Office updated its duty guidance by issuing three practice directions to and updating three other public rulings. A summary of the updated practice directions and rulings is below.

Practice Direction DA085.1.1 Transfer Duty – Relief for certain vacant land concession beneficiaries

This practice direction replaced *Public Ruling* DA085.2.3 *Transfer duty—relief for certain vacant land concession beneficiaries*. It sets out the circumstances under which ex gratia relief may be provided to extend the benefit of the first home concessions and the first home vacant land concession. It applies in cases where the vacant land concession applied, but later the transaction had to be reassessed because either the home was not built in time or the land was disposed of before the construction of the home.

Practice Direction DA085.2.1 Concession for homes and first homes—in specie distributions of residential land

This practice direction replaced *Public Ruling* DA085.3.1 *Concession for homes and first homes—in specie distributions of residential land*. It sets out the circumstances when the concessions available to homes will apply to in specie distributions of residential land from the trustee of a trust to the beneficiaries of the trust where the distribution is not otherwise eligible for an exemption under the *Duties Act 2001* (Qld).

Practice Direction DA087.1.1 Transfer duty concession for homes and first homes—residential purposes

This practice direction replaced *Public Ruling* DA087.1.4 *Transfer duty concession for homes and first homes—residential purposes*. It clarifies the Commissioner's view regarding land used for 'residential purposes' in relation to the transfer duty concessions which are available to homes.

Public Ruling DA085.1.12 Concession for homes and first homes—occupancy requirements

This public ruling clarifies the Commissioner’s interpretation of the Duties Act regarding the transfer date and occupation date, particularly the meaning of "principal place of residence," and outlines the circumstances in which a reassessment may be issued.

Public Ruling DA086A.1.5 Inclusion of chattels in the acquisition of a home or first home

This public ruling explains when chattels will be considered part of a home acquisition and eligible for the applicable concession.

Public Ruling TAA060.3.8 Penalty tax—home concessions

This public ruling sets out the principles the Commissioner uses to determine whether to remit penalty tax following a reassessment of a home concession, including the extent of any remission, and provides guidance on the application of these principles.

Queensland Revenue Office reference DA085.1.1, DA085.2.1, DA087.1.1, DA085.1.12, DA086A.1.5 and TAA060.3.8 w https://qro.qld.gov.au/2025/05/updated-rulings-on-home-concessions/

7. Private rulings

7.1 GST – partnership

Facts

A partnership acquired a property and recorded the asset in its accounts as a non-current asset under land and buildings. The property was used to operate a business carried on by the partnership in the names of the individual partners. During the period the business was active, the partnership did not pay rent for the use of the property.

The partnership was registered for GST. After the business ceased operations, the property was transitioned to a new use and is now subject to a lease agreement with an unrelated third party. The annual rental income specified in the lease does not exceed a certain (unspecified) amount.

While operating the business, the partnership claimed deductions for typical outgoings related to the property, including council rates, water rates, insurance, and repairs, which were expensed in the accounts. No deductions were claimed for capital works under Division 43 of the ITAA 1997, but depreciation deductions were taken for plant and equipment such as air-conditioners, shelving, and an alarm system.

Questions

1. Is the partnership liable for GST in relation to the income received from leasing the property, in accordance with section 9-5 of the GST Act?
2. If the GST registration of the partnership is cancelled, will a GST adjustment be required in relation to the property?
3. If the property is sold, do any GST implications need to be considered?

Ruling

<u>Leasing income</u>

The ATO determined that the lease of the property constituted a taxable supply under section 9-5 of the GST Act. The supply met all criteria: it was made for consideration, in the course or furtherance of the partnership's enterprise, and the partnership was registered for GST. Although the rental amount was below a certain threshold, the low value of consideration did not alter the nature of the supply. Furthermore, as the property was not residential premises, the supply was not input taxed under Division 40. On this basis, the ATO concluded that the lease of the property was a taxable supply, and the partnership was liable to remit GST on the rental income.

<u>No adjustment on deregistration</u>

The ATO examined whether a decreasing adjustment was required under section 138-5 of the GST Act upon cancellation of the partnership's GST registration. A decreasing adjustment is triggered when an entity ceases to be registered and holds an asset acquired or applied for a creditable purpose, if that asset is subsequently applied for a non-creditable purpose. However, in this instance, the ATO found that no such adjustment was necessary. The property had been acquired and used in carrying on the enterprise of the partnership, and following deregistration, there was no ongoing creditable use. Since the asset was not being applied for private or domestic purposes, and no further input tax credits would be claimed, the ATO concluded that no adjustment under Division 138 was required upon deregistration.

Implications on sale

The ATO declined to make a definitive ruling regarding the GST implications of a future sale of the property, citing the hypothetical nature of the question. It noted that the GST treatment of a sale would depend on several factors, including whether the partnership was registered or required to be registered for GST at the time of the transaction, whether the sale was made in the course or furtherance of an enterprise, and the nature of the property being sold (e.g., whether it constituted commercial premises or residential premises). The application of concessions such as the margin scheme or going concern provisions could also affect the outcome. Accordingly, the ATO concluded that it could not express a view on the GST consequences of a future sale due to the uncertainty of relevant facts at the time of the potential transaction.

ATO reference *Edited Private Advice Authorisation No. 1052368324476*
w https://www.ato.gov.au/law/view/document?docid=EV/1052368324476

7.2 GST – adjustment events

Facts

Entity A is a property investment entity wholly owned by Entity C as trustee for Entity B. Entity A is registered for GST, using the accounting method basis and reports on a lodgement cycle basis. Its principal activity is investing in Australian real property, with a focus on Build to Rent projects involving the acquisition, development and leasing of real estate.

On a specified date, Entity A entered into a contract to purchase a commercial office property (**Property**) from Entity D (**Vendor**). The sale price included GST, and a tax invoice was issued to Entity A's trustee. The contract required that Entity A, as purchaser, grant a lease to the Vendor to commence the day after settlement.

Accordingly, on the day following completion, Entity A leased the Property back to the Vendor under an office lease with standard commercial terms, a fixed annual rent (plus GST), and a defined expiry date unless otherwise agreed. Settlement of the purchase occurred as scheduled, and the parties did not treat the sale as a GST-free supply of a going concern.

Subsequently, Entity A entered into a development management agreement (**DMA**) with a Development Manager to undertake a new development on the Property. Under this agreement, the Development Manager is responsible for activities relating to the development, and Entity A must grant them access to the site. However, the Development Manager will not begin work or exercise access rights until after the office lease expires.

The planned development will involve constructing a multi-storey residential community designed for long-term rental housing, with various unit types and shared amenities. Practical completion is anticipated in a specified month and year, with residential leases expected to commence shortly thereafter. All residential leases are intended to be for terms of less than 50 years.

Questions

1. Did the taxpayer acquire the Property for a fully creditable purpose as defined in section 11-15 of the GST Act?
2. Will Division 129 of the GST Act apply in respect of the taxpayer's acquisition of the Property?
3. If Division 129 of the GST Act will apply, what is the date the first adjustment period (1st Adjustment Period) ends and how many adjustment periods will apply pursuant to section 129-20 of the GST Act?
4. Is the taxpayer required to make an adjustment pursuant to Division 129 of the GST Act in the first Adjustment Period?

5. Is the taxpayer required to make adjustments pursuant to Division 129 of the GST Act in the following nine Adjustment Periods?

Ruling

Acquisition for a creditable purpose

The ATO assessed whether the taxpayer acquired the property for a fully creditable purpose under section 11-15 of the GST Act. A fully creditable purpose exists where the acquisition is made in carrying on an enterprise and the input is not used to make input taxed supplies. Although the taxpayer is engaged in a Build to Rent project and intends to use the property for residential leasing, the initial use of the property was to lease it back to the vendor under a commercial lease. While commercial leasing is generally a taxable supply, in this context the taxpayer's broader intention included future residential use, which is input taxed. As the property was initially used solely for input taxed supplies, the acquisition was not considered to be for a fully creditable purpose. The ATO concluded that the taxpayer did not acquire the property for a fully creditable purpose under section 11-15 of the GST Act.

Division 129 adjustments

Division 129 of the GST Act permits adjustments to input tax credits if there is a change in the extent of creditable purpose after acquisition. Although the taxpayer did not initially acquire the property for a fully creditable purpose due to its input taxed leasing use, the planned redevelopment and future use of the property introduced a potential for a different use profile. This change in use, even from one input taxed purpose to another, may be significant enough to require an adjustment under Division 129, depending on how the use evolves over time and the nature of supplies made. The ATO determined that Division 129 of the GST Act applies to the taxpayer's acquisition of the property.

First adjustment period

Under section 129-20 of the GST Act, the number and timing of adjustment periods are determined based on the nature of the acquisition. As the property acquired is real property, ten adjustment periods apply. The first adjustment period ends at the end of the tax period that commences at least 12 months after the date of acquisition. This is consistent with the rules applicable to longer-term capital assets. The ATO determined that the first adjustment period ends on a specified date and that ten adjustment periods apply to the taxpayer's acquisition of the property.

Adjustment in first period

To determine whether an adjustment is required in the first adjustment period, it must be established whether the extent of creditable purpose has changed since acquisition. During this period, the property remained leased under the original Office Lease, which constitutes input taxed use. Since the development activity had not yet commenced, there was no evident shift in the extent of creditable use. However, without more definitive factual information about whether any development activities or alternative uses had begun during the period, the ATO was unable to reach a conclusive position. The ATO was unable to provide a definitive answer as to whether an adjustment is required in the first adjustment period under Division 129 of the GST Act.

Adjustments in subsequent periods

The application of Division 129 in future periods depends on whether the extent of creditable purpose changes. Although the future use of the property will be residential leasing—which is also input taxed—the redevelopment may involve different activities or mixed-use elements, such as commercial tenancies or short-term accommodation, which could alter the creditable use proportion. Adjustments may therefore be necessary if there is a material change in the nature or extent of use. The ATO determined that the taxpayer may be required to make adjustments in subsequent adjustment periods under Division 129 of the GST Act, depending on how the extent of creditable purpose changes over time.

ATO reference *Edited Private Advice Authorisation No. 1052202462935*
w https://www.ato.gov.au/law/view/document?docid=EV/1052202462935

7.3 Employee share scheme and change of residency

Facts

On the specified date, the taxpayer arrived in Australia on a temporary work visa and commenced employment with a company that is a subsidiary of an international company listed on the stock exchange.

As part of the taxpayer's remuneration, the taxpayer received discounted shares through an Employee Share Scheme (ESS), all related to the taxpayer's Australian employment.

The ESS interests had a deferred taxing point.

The taxpayer received shares in multiple financial years, each with an ESS value of $Y, and paid no income tax or Division 293 tax on them.

On the specified date, the taxpayer became an Australian tax resident upon obtaining permanent residency.

On the same specified date, the taxpayer ceased employment with the company and sold the ESS shares.

Since the time of the taxpayer's residency status change, the market value of the shares decreased by approximately Y%.

The taxpayer provided two cost base calculations related to the ESS shares, both showing a value of $Y:

1. Market-based cost base (at residency change): $Y
2. ESS value-based cost base (from tax returns): $Y

Question

On the disposal of ESS grant shares, will the cost base of the shares be the market value at the time when they taxpayer became an Australian resident?

Ruling

The ATO ruled no.

As taxpayer's ESS shares were acquired when the taxpayer worked as an Australian employee, they are treated as income from sources in Australia and will be taxed in accordance with the ESS rules.

Therefore, as the ESS interests had a deferred taxing point. The cost base will be the market value at the deferred taxing point under subsection 83A-110 (1) of the ITAA 1997.

ATO reference *Edited Private Advice Authorisation No. 1052368535331*
w https://www.ato.gov.au/law/view/document?docid=EV/1052368535331

7.4 Vested and indefeasible interest

Facts

A unit trust has a number of unitholders, each of whom holds an interest in the income and capital of the Trust in proportion to their unit holdings. The Trust is not publicly listed, is not widely held, and currently has only one class of ordinary units on issue. No different classes of units or partly paid units have ever been issued, nor are there any plans to do so. Units are only transferred or redeemed at the request of a unitholder, and the redemption or issue price is not linked to the Trust’s net asset value based on Australian accounting principles.

The Trust Deed empowers the trustee, with unitholder consent, to amend the Trust or create and issue additional units. However, there is no intention to amend the Deed during the ruling period in a way that could defeat a unitholder’s interest in the Trust's income or capital. The trustee has never exercised such power and does not intend to.

The Trust is the sole shareholder of a company, which is expected to pay fully franked dividends to the Trust over the coming income years. These dividends will carry significant franking credits. The Trust will distribute its net income, including the franked income, to its unitholders proportionately.

All units carry equal rights to income, capital, and voting. The trustee deals with unitholders at arm’s length and the Trust undergoes annual audits by an independent auditor.

No arrangements are or will be in place that would result in related payments under former section 160APHN of the *ITAA 1936*, or cause the Commissioner to apply provisions under paragraph 177EA(5)(b) of the *ITAA 1936* or paragraphs 207-150(1)(c) to (h) of the *ITAA 1997*. Additionally, no unitholder's exposure to risks of loss or opportunities for gain is diminished below the stipulated threshold, ensuring genuine ownership interests are maintained.

Questions

1. Do the Unitholders under the Deed of Trust have a vested and indefeasible interest in the income and capital of the Trust as required under former subsection 160APHL(11) of the ITAA 1936 for the purposes of the qualified person requirement under section 207-145 of the ITAA 1997?
2. If the answer to question 1 is no, can and will the Commissioner exercise the discretion under former subsection 160APHL(14) of the ITAA 1936 to treat the Unitholders' interests in the Trust as vested and indefeasible for the purposes of the qualified person requirement under section 207-145 of the ITAA 1997?
3. If the answer to question 2 is no, will the proposed amendments to the Deed of Trust result in the Unitholders having a vested and indefeasible interest in the income and capital of the Trust as required under subsection 160APHL(11) of the ITAA 1936 for the purposes of the qualified person requirement under section 207-145 of the ITAA 1997?
4. If the answer to question 3 is yes, will the proposed amendment to the Deed of Trust trigger a resettlement of the Trust as considered in Taxation Determination TD 2012/21?

Ruling

<u>Vested and indefeasible interest</u>

In determining whether the unitholders in the Trust have a vested and indefeasible interest in the income and capital of the Trust under former subsection 160APHL(11) of the ITAA 1936, the ATO considered both statutory requirements and relevant judicial interpretations. Under Division 207 of the ITAA 1997, the entitlement to franking credit benefits depends on being a "qualified person", which in the case of a trust requires unitholders to hold a vested and indefeasible interest in the trust corpus.

The concepts of "vested" and "indefeasible" are not defined in the tax legislation, but the courts have interpreted them in several cases. In *Dwight v Federal Commissioner of Taxation* (1994) 92 ATC 4192, Hill J distinguished "vested" from "contingent", clarifying that a vested interest is a present fixed right, even if enjoyment is deferred. Applying this, the ATO accepted that the unitholders are vested in interest since their rights to income and capital are fixed proportionally to their unit holdings.

However, the issue turned on whether these interests were also "indefeasible". As explained in Dwight and *Colonial First State Investments Limited v Commissioner of Taxation* \2011] FCA 16, an interest is indefeasible if it cannot be annulled or invalidated. The ATO identified three relevant powers in the Trust Deed of Trust: the trustee's ability to issue further units, to redeem units, and to amend the Trust Deed itself with unitholder consent. According to former subsection 160APHL(12) of the ITAA 1936, an interest is deemed defeasible if it can be reduced by the issue of further units or if redemption can occur below value. The exception in subsection 160APHL(13), that such actions will not render the interest defeasible if carried out at market value or net asset value, did not apply, as the Trust does not price units on the basis of net asset value.

Moreover, the ability to amend the Trust Deed in a manner that could extinguish or diminish a unitholder's entitlement also pointed towards the interest being defeasible. In Colonial, Stone J held that even where members consent to changes by special resolution, the possibility of terminating rights to capital or income renders such interests defeasible.

Therefore, due to these embedded powers in the Trust Deed, particularly the discretionary pricing of units and the trustee's ability to amend the Trust, the ATO concluded that the unitholders' interest is not indefeasible. Accordingly, the unitholders do not hold a vested and indefeasible interest in the corpus of the Trust for the purposes of former subsection 160APHL(11) and are not qualified persons under section 207-145 of the ITAA 1997 based solely on the current terms of the Trust Deed.

<u>Exercise of discretion</u>

Having determined that the unitholders' interest in the Trust was not indefeasible under former subsection 160APHL(11) of the ITAA 1936, the ATO next considered whether to exercise its discretion under former subsection 160APHL(14) to treat the interest as if it were vested and indefeasible. This provision allows the Commissioner to treat a defeasible or non-vested interest as meeting the requisite standard, provided certain conditions are met and having regard to various contextual factors.

First, the ATO confirmed that the unitholders do indeed have an interest in the corpus of the Trust and that, but for the exercise of this discretion, that interest is defeasible. The circumstances in which defeasance could occur were again noted: the trustee's power to issue additional units, unitholder rights to redeem units, and the trustee's ability to amend the Deed (with unitholder consent). These mechanisms technically allow for the unitholder's rights to be altered or diminished.

However, the likelihood of these powers being exercised in a way that would actually defeat a unitholder's interest was considered low. The trustee had advised the Commissioner that it would not amend the Deed to undermine unitholder rights during the ruling period, did not intend to exercise such powers, and had a consistent practice of issuing only ordinary units with uniform rights. No units had ever been compulsorily redeemed, and all dealings with unitholders occurred on an arm's length basis.

The ATO also considered the broader nature of the Trust: it is a private, unlisted unit trust that is independently audited annually. These characteristics support the conclusion that the Trust operates transparently and with commercial integrity.

Finally, the ATO evaluated the issue in light of the policy intent behind the franking credit integrity rules. As outlined in the Explanatory Memorandum to the *Taxation Laws Amendment Bill (No. 2) 1999*, these rules aim to prevent the use of franking credits by parties who are not true economic owners of the relevant shares. Here, the unitholders were found to bear the real economic risks and benefits associated with the Trust's shareholding in the underlying company. No related payment arrangements, risk-diminishing schemes, or other avoidance structures were present that might otherwise justify denying access to the franking credits.

Given these findings, and to avoid undermining the purpose of the integrity measures while recognising the commercial and equitable operation of the Trust, the ATO concluded that it was appropriate to exercise the discretion under former subsection 160APHL(14). The unitholders' interest was therefore treated as vested and indefeasible for the purposes of the qualified person rule in section 207-145 of the ITAA 1997.

Remaining questions

Given the answer to question 2, the ATO considered it was not necessary to answer questions 3 and 4.

ATO reference *Edited Private Advice Authorisation No. 1052364597044*
w https://www.ato.gov.au/law/view/document?docid=EV/1052364597044

7.5 Income protection payments

Facts

The Company was incorporated by A in 1999 to operate a business in which A was the principal professional as a medical practitioner. A has always been the sole director and sole shareholder of the Company. A was additionally one of a number of employees of the Company working in the business; the other employees including reception staff and other professionals.

There was no formal contract of employment, nor any official employment policies regarding employee benefits between the Company and A. A has been paid a salary by the Company since it commenced the business.

In 2011, the Company (as policy owner) acquired an income protection insurance policy in respect of the life of A (**Policy**). Under the Policy, the Company is entitled to a 'monthly amount insured' determined by reference to A's annual income at the time of acquisition and payable upon A's total disablement due to illness or injury.

A suffered significant injury in an accident in the 20XX income year and has subsequently been assessed as totally disabled and is not working in any gainful occupation, and is unable to perform one or more duties necessary to produce income from their regular occupation. As a result, the Company has been paid the monthly amount insured by the insurance company since 2015.

The monthly amount insured has been utilised by the Company to pay A's salary since their injury, as well as fund dividends paid by the Company to A. All of the insurance proceeds received by the Company under the Policy since 20XX have been included in the assessable income of the Company in the year of receipt.

The Company business was sold in 20XX pursuant to a Contact of Sale to an unrelated party.

The Company proposed to invest some or all of the monthly amount insured it received under the Policy (e.g. in term deposits) rather than pay the insurance proceeds immediately as dividends (or some other payment form) to A (**Proposed Scheme**).

Questions

1. Are the income protection benefit payments received by the Company under the insurance policy personal services income of A within the meaning of section 84-5 of the ITAA 1997?
2. Are the income protection benefit payments received by the Company under the insurance policy base rate entity passive income within the meaning of section 23AB of the Income Tax Rates Act 1986 (ITRA)?

3. If the funds from the income protection benefit payments received by the Company under the insurance policy are retained and invested by the Company rather than paid out as dividends or benefit payments to A, will the Commissioner determine under section 177F of the ITAA 1936 that the whole or a part of those income protection benefit payments are assessable income of A?

Ruling

The income protection benefit payments received by the Company under the insurance policy were deemed not to be personal services income or base rate passive income per the statutory definitions. The Proposed Scheme to invest some or all of the benefits received by the Company was determined to not be assessable income under section 177F of the ITAA 1936 on the basis that the Proposed Scheme was not entered into with the dominant purpose of obtaining a tax benefit in relation to assessable income.

Personal services income

Section 84-5 of the ITAA 1997 defines personal services income (**PSI**) as ordinary income which is mainly a reward for personal efforts or skills (or would mainly be such a reward if it was your income). This reference to ‘or would mainly be such a reward if it was your income' applies to situations where the income is legally derived by a personal services entity (PSE) and not the individual.

The meaning of 'mainly' in this section is explained at paragraph 37 of TR 2022/3 to mean 'chiefly', 'principally' or 'primarily' a reward for the provision of the personal efforts of exercise of the skills of an individual – i.e. more than half of the ordinary income received.

As A is no longer capable of performing their duties as a medical practitioner due to their injury, the benefits are merely paid to the Company pursuant to its contract of insurance with the insurance company; rather than being paid to the Company as a reward for A's personal efforts or skills. Therefore, the benefits do not qualify as PSI under section 84-5 of the ITAA 1997.

Passive income status

Base rate entity passive income (**BREPI**) is defined in section 23AB of the *Income Tax Rates Act 1986* (Cth) (**ITRA**). It includes assessable income that is a distribution; franking credit; non-share dividend; payment of interest; royalties or rent; a gain on a qualifying security; a net capital gain; or assessable income of a partner in a partnership or a beneficiary in a trust.

As the benefits paid to the Company by the insurance company under the Policy are not a payment of a type which falls under any of the categories of income specified in section 23AB; they are not BREPI.

Scheme for obtaining a tax benefit

Part IVA of the ITAA 1936 applies to an arrangement where the following elements exist:

1. there is a scheme as defined in subsection 177A(1) of the ITAA 1936;
2. there is a tax benefit in relation to assessable income which is defined in subsection 177C(1)(a) of the ITAA 1936 as an amount not included in the assessable income of the taxpayer, which would have been included or been expected to be included in the assessable income if not for the scheme;
3. having with regarding to the 8 objective matters identified in subsection 177D(2) of the ITAA 1936, it would be concluded by a reasonable person that the taxpayer entered into the scheme for the dominant purpose of obtaining a tax benefit in connection with the scheme; and
4. the Commissioner makes a determination under subsection 177F(1)(a) of the ITAA 1936 that the whole or part of the amount shall be included in the assessable income of the taxpayer.

As discussed above, the benefits received by the Company under the Policy were not deemed to be assessable income, as defined in subsection 177C(1)(a).

The Proposed Scheme would result in A receiving less income or no income; as the Company would retain and invest the benefits received under the Policy instead of paying them to A in the form of a dividend or any form of assessable income. Therefore, with regard to the matters in subsection 177D(2) of the ITAA 1936, the Commissioner determined that the Proposed Scheme was not entered into or carried out for the dominant purpose of enabling A or the Company to obtain a tax benefit.

ATO reference *Edited Private Advice Authorisation No. 1052368207163*
w https://www.ato.gov.au/law/view/document?docid=EV/1052368207163

7.6 Deductions for payments to overseas contractors

Facts

The taxpayer registered for an ABN as a sole trader on XX March 20XX and registered the business on X April 20XX.

The taxpayer operates as a Research Specialist and Service Designer, performing complex tasks such as research design, synthesis, strategy reporting, and stakeholder engagement.

In the 20XX income year, the taxpayer was engaged by multiple companies under employment contracts as follows:

1. Employer A: Received a salary, worked prescribed hours at the employer's office under supervision.
2. Employer B: Fixed-term contract extended during the year; salary and terms unchanged.
3. Employer C: Fixed salary, full-time (5 days/week), worked both on-site and from home; entitled to leave and superannuation.
4. Employer D: Fixed annual salary, worked on-site, reported to a supervisor; entitled to leave and superannuation.

The taxpayer also operated a sole trader consultancy and provided research services to Company E, earning business income.

To manage workload and maintain output quality, the taxpayer engaged overseas research consultants due to specialised expertise not being readily available in Australia, volume management and quality control, and operational efficiency in handling complex research tasks.

Invoices from subcontractors in the relevant year included:

1. Company F:
   (a) First invoice: 95% of work supported taxpayer's duties with Employer A; 5% was for taxpayer's consultancy business.
   (b) Second invoice: 90% related to Employer A, 5% to Employer B, and 5% to the taxpayer's consultancy work.
2. Company G:
   (a) First invoice: 90% related to Employer C; 10% to the taxpayer's consultancy project for Company E.
   (b) Second invoice: 90% for Employer C; 10% for consultancy work with Company E.

Question

Is the taxpayer entitled to a deduction for engaging overseas contractors under section 8-1 of the ITAA 1997 in the course of taxpayer's employment?

Ruling

The ATO ruled no.

Under section 8-1 of the ITAA 1997, a deduction is allowed for expenses incurred in gaining or producing assessable income, unless the expenses are capital, private, domestic, or related to exempt income. The ATO stated that the courts have stablished that expenses must be income-producing in character, there must be a clear nexus between the expense and income generation, and the expense must be directly linked to the operations by which income is earned.

The taxpayer engaged overseas research consultants to complete work that the taxpayer was contractually required to perform as an employee. This constituted a delegation of employment duties, differing from *Frisch v Federal Commissioner of Taxation* [2008] AATA 462, where the taxpayer retained core responsibilities.

The subcontractors performed tasks for which the taxpayer received a salary. Therefore, to the extent the expenses were incurred in outsourcing the taxpayer's tasks as an employee to overseas subcontractors, they were not considered a cost of deriving the income. The expenses were not incurred in gaining or producing the taxpayer's employment income and were considered private and domestic in nature. The expenses were not deductible under section 8-1.

COMMENT – the reasoning in the ruling appears at odds with orthodox principles for ascertaining whether there is a sufficient nexus under section 8-1 of the ITAA 1997. It is difficult to understand why the fact that the delegation may not have been permitted under the employment contract means that the occasion of the expenditure was not the taxpayer's income earning activities.

The conclusion that the outgoings were private or domestic in nature is plainly incorrect.

While the facts in *Frisch* were different, the reasoning of the AAT in that case should have resulted in the outgoings being held to be deductible.

ATO reference *Edited Private Advice Authorisation No. 1052351121003*
w https://www.ato.gov.au/law/view/document?docid=EV/1052351121003

7.7 Tax treatment of settlement adjustment amount

Facts

The taxpayer owned a rental property located at X Street, in an unspecified state. This property was held as a long-term investment for the purpose of generating rental income. In the relevant income year, the property was sold while still subject to an existing lease agreement.

The purchaser was an unrelated third party, with no association or connection to the taxpayer. Under the terms of the existing lease, the landlord (the taxpayer) was required to make monthly rent abatement payments of $X plus GST to the tenant over the initial seven-year lease period, provided the tenant met certain conditions. If these conditions were satisfied throughout the lease, the total rent abatement payable would amount to $X.

The contract of sale for the property listed a purchase price of $X, which included a deposit of $X. However, after the contract was signed and before settlement, both parties agreed to insert a special condition into the contract. This condition stipulated that an adjustment would be made at settlement to account for the rent abatement.

This special condition reflected a prior understanding during sale negotiations: the purchaser would not assume liability for any loss arising from the rent abatement. Because the original signed contract did not include a clause to this effect, the taxpayer agreed to the insertion of the special condition to ensure the sale would proceed, despite receiving a reduced amount from the nominal contract price.

Settlement was completed in the relevant year. Up to the date of settlement, the taxpayer paid the tenant $X in rent abatement. At settlement, the purchase price was adjusted in the purchaser's favour by an amount of $X to reflect this liability. Additional adjustments to the purchase price were also made.

In total, the taxpayer received $X from the deposit prior to settlement and a further $X at settlement.

Questions

1. Is the taxpayer entitled to a deduction under section 8-1 of the ITAA 1997 for the settlement adjustment amount of $X?
2. If the answer to question 1 is no, pursuant to subsection 116-20(1) of the ITAA 1997, is the amount of the capital proceeds from the sale of the property $X?
3. If the answer to question 2 is yes, are the capital proceeds from the sale of the property replaced with the market value of the property under subsection 116-30(2) of the ITAA 1997?

Ruling

<u>Deduction under section 8-1</u>

The ATO considered whether the taxpayer was entitled to a deduction under section 8-1 of the ITAA 1997 for the adjustment amount paid at settlement in respect of the rent abatement arrangement. Under section 8-1, a deduction is allowable for losses or outgoings to the extent they are incurred in gaining or producing assessable income or are necessarily incurred in carrying on a business for that purpose. However, a deduction is not available where the expense is capital, private or domestic in nature, or incurred in relation to earning exempt income.

In this case, the ATO determined that the settlement adjustment amount was not incurred in the course of gaining or producing rental income. Instead, it was a capital expense associated with the disposal of the rental property, which is a capital asset. The payment was not made as part of the ongoing lease arrangement but arose from the contractual sale negotiations, particularly to adjust the sale price to reflect the purchaser's exclusion from liability for future rent abatements.

As the adjustment was directly connected to the sale and thus capital in nature, it was not deductible under section 8-1. Accordingly, the ATO concluded that the taxpayer was not entitled to a deduction for the settlement adjustment amount.

<u>Adjustment to capital proceeds</u>

The ATO next considered whether the amount of capital proceeds from the sale of the property should be reduced by the settlement adjustment amount. Subsection 116-20(1) provides that capital proceeds from a CGT event include the money and market value of any other property received or entitled to be received in respect of the event.

Here, while the original contract listed a higher nominal purchase price, the parties subsequently amended the agreement through a special condition that explicitly reduced the amount payable at settlement by the adjustment amount. As this condition formed part of the final legally binding agreement under which the sale was completed, the ATO accepted that the reduced amount actually received was the true consideration.

Therefore, the ATO determined that the capital proceeds were equal to the reduced amount, being the sum actually received by the taxpayer at settlement plus the deposit, consistent with subsection 116-20(1).

Market value substitution

Finally, the ATO considered whether the market value substitution rule under subsection 116-30(2) of the ITAA 1997 should apply. This provision requires the market value of the CGT asset to be substituted for the capital proceeds if the parties were not dealing at arm's length and the capital proceeds are less than market value.

Although the final proceeds were lower than the initial contract price, the ATO found that the parties were dealing at arm's length. The purchaser was unrelated and unaffiliated with the taxpayer, and the adjustment to the price reflected genuine commercial negotiations. The change was not artificial or contrived to produce a tax benefit, but rather addressed a previously overlooked allocation of risk relating to the rent abatement.

As a result, the ATO determined that the market value substitution rule did not apply.

ATO reference *Edited Private Advice Authorisation No. 1052366754830*
w https://www.ato.gov.au/law/view/document?docid=EV/1052366754830

7.8 CGT look through to asset

Facts

Group X, a tax consolidated group, was established prior to 1985 by Person A and Person B, the parents of Person X and Person Y. Company X, which became the head entity of Group X, is equally owned by Person X and Person Y. Person X holds D class X% non-cumulative redeemable preference shares and one X% non-cumulative preference share, all of which were acquired after 19 September 1985 (post-CGT assets). Person Y holds C class X% non-cumulative redeemable preference shares and one X% non-cumulative preference share, all acquired before that date (pre-CGT assets).

In 19XX, Person X, Person Y, and Person B entered into an agreement (the **19XX Agreement**) concerning a future arrangement for distributing Company X's assets. This agreement provided that, if Person B did not exercise certain share options before the expiry date, Person X and Person Y would wind up Company X and ensure that, after payment of capital gains tax, the net assets were distributed equally between Person X, Person Y, and Person B. They also agreed to incorporate this commitment into their wills.

Initially, Person A managed Group X, but in 20XX, Person B assumed control. Person B later withdrew from management due to a health condition.

On X/XX/20XX, Person B and Company X entered into a Share Option Agreement granting Person B the right to acquire 10 'E' Class X% redeemable preference shares in Company X, exercisable by X/XX/20XX. If unexercised, the company was to be wound up within a specified period. An explanatory statement was prepared at the time to clarify that the intention behind both the Share Option Agreement and the 19XX Agreement was to secure Person B's financial position by providing them one third of Company X's post-tax value.

Following the death of Person A on X/XX/20XX, a dispute arose between Person X and Person Y regarding Person X's role in the business. As a result, on X/XX/20XX, the Court made orders by consent (**Month A Orders**) for the sale of Group X's assets and the winding up of the group. Although consent orders were made, further disputes between the parties delayed the sale and liquidation process.

Subsequently, on X/XX/20XX, Person X and Person Y, acting in their personal capacities and as attorneys for Person B, signed a deed (**Option Exercise Deed**) confirming that the options would not be exercised. This deed updated clause 3.1 of the 19XX Agreement to reflect the anticipated winding up of the company following the sale of assets under the Month A Orders, ensuring the equal distribution of net assets among Person X, Person Y, and Person B.

On X/XX/20XX, Person X and Person Y jointly applied to the Court, in their roles as Person B's attorneys, seeking confirmation that it was appropriate not to exercise the options. The Court made orders on X/XX/20XX (**Month B Orders**) requiring completion of the asset sale and liquidation by a specified date.

Person B died on X/XX/20XX. Under Person B's will, Person X and Person Y were appointed joint executors and named as equal beneficiaries, aside from a few minor bequests. On X/XX/20XX, with the consent of both parties, the Court appointed administrators for Person B's estate, who received letters of administration on X/XX/20XX.

In line with the agreements, and because Person X held post-CGT shares while Person Y's shares were pre-CGT, Person Y was required to make a Tax Equalisation Payment to cover half of the income tax liability incurred by Person X from the liquidation of Company X.

The liquidation of Group X proceeded as a members' voluntary winding up on X/XX/20XX. The Liquidator has since made several equal distributions to both shareholders:

1. an initial distribution on X/XX/20XX, fully funded from pre-CGT reserves;
2. further distributions on X/XX/20XX and X/XX/20XX, also sourced entirely from pre-CGT reserves; and
3. a final distribution on X/XX/20XX, again sourced from pre-CGT reserves, part of which was paid directly to the ATO on behalf of Person X. This included an amount paid by Person Y as a Tax Equalisation Payment.

The Liquidator has retained further funds for additional equalisation payments. Person X's tax liability from the distributions, relating to net capital gains, arose during the 20XX and 20XX income years. It is assumed that the obligation to allocate one-third of the net assets to Person B ceased upon their death.

Under the Option Exercise Deed and the 19XX Agreement, Person X had the rights to:

1. receive one third of the net assets of Company X upon its winding up, after payment of any capital gains tax assessed on the distributions received; and
2. be compensated by Person Y (via a Tax Equalisation Payment) for half of the CGT liability incurred due to Person X's post-CGT shareholding status, since Person Y's shares are pre-CGT and not subject to capital gains tax.

Person X contended it would be appropriate to apply a 'look-through' approach to the payment of the Tax Equalisation Payments because the discharge of the Person X Rights is merely facilitating the real transaction, being a gift from Person Y to Person X. This was based on the submission that:

1. as a general principle the CGT provisions address what is the most relevant transaction to be considered
2. in determining what the most relevant asset or transaction is, it is often appropriate to adopt a 'look-through' approach to the transaction or arrangement;
3. it is sometimes appropriate to regard the capital proceeds as being in respect of an 'underlying asset' rather than a more proximate 'right' to payment; and
4. in the case of an unpaid present entitlement to income of a trust, on payment of that income, the Commissioner's position has been that it is appropriate to look through the legal rights incidentally created and discharged/satisfied when they are merely facilitating the real transaction, being the distribution of income from a trust to a beneficiary.

Questions

1. Will the Commissioner accept that a 'look-through' approach applies to the payment of the Tax Equalisation Payments, thereby disregarding the application of CGT event C2 to the ending of the Person X Rights?
2. If the answer to Question 1 is no, will the Commissioner accept that the disposal of the Person X Rights will not give rise to a capital gain in the hands of Person X under the CGT provisions of the ITAA 1997?

Ruling

'Look-through' approach

The ATO determined that the Tax Equalisation Payments made by Person Y to Person X do not qualify as gifts. This is because the payments were made under a binding obligation set out in the Option Exercise Deed and the 19XX Agreement, which required Person Y to compensate Person X to ensure equal net receipts after tax. The ATO considered that if Person Y had not made the payments, Person X could have enforced their rights under the agreements through legal action. As such, the payments were not made voluntarily, which is a necessary condition for a gift under paragraph [13] of *Taxation Ruling* TR 2005/13.

The ATO determined that the 'look-through' approach does not apply to disregard the application of CGT event C2 to the ending of the Person X Rights. The ATO reasoned that CGT event C2 occurs when an entity's ownership of an intangible asset, such as contractual rights, ends due to expiration, cancellation, or similar events. In this case, the Tax Equalisation Payments did not change the fact that Person X's rights were extinguished, triggering CGT event C2 under the provisions of the ITAA 1997. The ATO emphasised that the CGT provisions must be applied in accordance with the substance of the transaction, meaning the expiration of the rights remained a separate CGT event regardless of any underlying commercial arrangements.

The ATO concluded that a 'look-through' approach is not appropriate for the Tax Equalisation Payments received by Person X. While the Commissioner accepted in *Commissioner of Taxation v Dulux Holdings Pty Ltd & Ors* [2001] FCA 1344 that incidental legal rights may be disregarded when they merely facilitate a real transaction, that principle does not apply here. The Person X Rights to receive the Tax Equalisation Payments represent a specific and material entitlement arising from detailed historical negotiations and formal agreements. These rights are not incidental and cannot be ignored or re-characterised as gifts.

The ATO further determined that the Agreements require Person X and Person Y to receive equal net distributions from Company X, after accounting for tax. Since only Person X is subject to capital gains tax due to their post-CGT shares, the Agreements require Person Y to gross-up Person X's receipts by paying an amount equal to half of Person X's tax liability.

As these payments are made for Person X's benefit and reduce their tax liability, they must be included in Person X's assessable income under the constructive receipt provisions in subsection 6-5(4) for ordinary income or section 103-10 of the ITAA 1997 for capital proceeds. The ATO rejected the notion that these amounts can be excluded from income merely because they were paid directly to the ATO. Doing so would result in a tax credit without corresponding income, leading to a tax advantage.

Taxable capital gain

Furthermore, the ATO ruled that the ending of the Person X Rights resulted in a taxable capital gain. Under section 104-25 of the ITAA 1997, a capital gain arises when the capital proceeds from a CGT event exceed the asset's cost base.

The Person X Rights originated from the 19XX Agreement and were later modified by the Option Exercise Deed and the decision by Person B's executors not to exercise the options. The ATO considered whether Person X had any cost base for these rights under section 110-25. While Person X originally agreed to transfer one third of Company X's net assets to Person B, this obligation was ultimately not enforceable due to the variation of the agreement and the contingent nature of the payment.

Referring to *Dingwall, K. v Commissioner of Taxation* [1995] FCA 431, the ATO reiterated that a cost base must involve an actual or presently enforceable obligation to pay. Since Person X was never under a binding obligation to pay a defined amount in order to acquire the rights, the Commissioner concluded that there was no cost base attributable to the Person X Rights.

As a result, the ATO determined that the entire capital proceeds received in respect of the ending of the Person X Rights are assessable as a capital gain.

TIP – under section 112-20(1)(a)(i), the market value substitution rule for cost base does not apply to rights acquired as a result of CGT event D1 (creation of a contractual right or other legal or equitable right in another entity).

COMMENT – this has long been recognised as a technical problem for unpaid present entitlements from trusts. No amount is paid to acquire the right to be paid the distribution (the creation of which triggers CGT event D1) and the right comes to an end upon payment (which triggers CGT event C2). The ATO has an administrative approach, as referred to in the taxpayer's submissions in this ruling, of 'looking through' to the underlying transaction (being the distribution from the trust) and disregarding the CGT event C2.

ATO reference *Edited Private Advice Authorisation No. 1052324499769*
w https://www.ato.gov.au/law/view/document?docid=EV/1052324499769

8. ATO and other materials

8.1 Super rates and thresholds for 2025-26

Several superannuation thresholds for the 2025–26 income year have been indexed in line with Average Weekly Ordinary Time Earnings (AWOTE), leading to increases in limits such as the CGT cap, low rate cap, employment termination payment (ETP) cap, and the general transfer balance cap. These increases reflect ongoing adjustments for inflation and wage growth. The concessional and non-concessional contribution caps remain unchanged at $30,000 and $120,000 respectively, though the non-concessional cap is still subject to a person's total superannuation balance at the end of the previous financial year. The bring-forward rules continue to apply, allowing eligible individuals under age 75 to make up to three years' worth of non-concessional contributions in a single financial year, depending on their total super balance.

The super guarantee (SG) rate increased to 12% from 1 July 2025, marking the final step in the legislated SG rate increase schedule. Interestingly, despite this increase, the maximum super contribution base has decreased slightly, from $65,070 to $62,500 per quarter, likely due to movements in average earnings data. The Division 293 income threshold remains steady at $250,000.

The ATO published the following key superannuation rates and thresholds for the 2025–26 income year:

Threshold	**2025–26**	**2024–25**	**Change**
Non-concessional contributions cap	$120,000	$120,000	No change
Concessional contributions cap	$30,000	$30,000	No change
CGT cap amount	$1,865,000	$1,780,000	Increased by $85,000
Low rate cap amount	$260,000	$245,000	Increased by $15,000
ETP cap (life and death benefit)	$260,000	$245,000	Increased by $15,000
Genuine redundancy and early retirement base limit	$13,100	$12,524	Increased by $576
Genuine redundancy and early retirement per year of service	$6,552	$6,264	Increased by $288
Super guarantee rate	12.00%	11.50%	Increased by 0.5%
Maximum super contribution base (per quarter)	$62,500	$65,070	Decreased by $2,570
Transfer balance cap	$2,000,000	$1,900,000	Increased by $100,000
Defined benefit income cap	$125,000	$118,750	Increased by $6,250
Co-contribution income thresholds	$47,488–$62,488	$45,400–$60,400	Increased by $2,088 each

w https://www.ato.gov.au/tax-rates-and-codes/key-superannuation-rates-and-thresholds

8.2 Fixed rate for work from home running expenses

On 16 April 2025, the ATO published an update to *Practical Compliance Guideline* PCG 2023/1 to reflect the increase in the fixed rate for work from home running expenses from 67 cents to 70 cents per hour, effective from 1 July 2024.

Taxpayers may use the fixed rate method to claim work-related additional running expenses as an alternative to claiming actual expenses. The eligibility criteria and types of expenses covered under the fixed rate method remain unchanged.

ATO reference *PCG 2023/1* w https://www.ato.gov.au/law/view/document?docid=COG/PCG20231/NAT/ATO/00001

8.3 Waiver of tax-related liabilities in proceeds of crime matters

To supplement Division 342 of Schedule 1 of the TAA, *Practice Statement Law Administration 2011/10* provides guidelines on how and when the Commissioner may waive the Commonwealth's right to recover certain tax debts to facilitate criminal confiscation actions under the *Proceeds of Crime Act 2002* (**POCA**).

On 10 April 2025, the ATO updated its Practice Statement to align it with current legislation, operational frameworks, and internal ATO procedures.

Key changes included updated definitions, a revised preamble, and new guidance on the Commissioner's waiver power. This guidance clarifies that the waiver can extend to penalties and interest, outlines the risks of exercising the waiver where POCA outcomes are uncertain, and emphasises the importance of early engagement with relevant authorities. The update also reflects the repeal of the POCA and its replacement by the *Proceeds of Crime Regulations 2019* and strengthens alignment with the wording and objectives of both the TAA and POCA.

ATO reference *PS LA 2011/10* w https://www.ato.gov.au/law/view/document?DocID=PSR/PS201110/NAT/ATO/00001

8.4 ATO views on Bendel decision

On 28 April 2025, the ATO published a webpage in which Deputy Commissioner Louise Clarke discussed the Federal Court's decision in *Bendel v Commissioner of Taxation* 2023] FCA 105 (see our February 2025 Tax Training Notes) and its implications for the administration of Division 7A of the ITAA 1936.

The *Bendel* decision concerned a trust that had made a present entitlement of income to a corporate beneficiary, while retaining the funds within the trust. The Federal Court found that this arrangement did not constitute a "loan" for the purposes of section 109D(3) of the ITAA 1936 and therefore did not result in a deemed dividend under Division 7A. This outcome diverged from the ATO's established view, as reflected in Taxation Determination TD 2022/11 and Practical Compliance Guideline PCG 2010/4.

The Deputy Commissioner stated that the ATO "*does not agree with the decision in Bendel*" and confirmed that the Commissioner has appealed the decision to the Full Federal Court. She said:

> *Until the outcome of the appeal is known, the ATO will continue to administer the law in accordance with our existing public advice and guidance, including TD 2022/11.*

She further clarified that no changes will be made to the ATO's guidance at this time:

> *We won't be revising TD 2022/11 at this time, but we'll continue to monitor the need for further advice or guidance.*

No blanket deferral for lodgment

The Deputy Commissioner has confirmed that no blanket deferral will be granted for the lodgment of tax returns by private companies affected by the *Bendel* decision while the High Court considers the Commissioner's special leave application. She stated that it is not usual practice to allow lodgment deferrals while a matter progresses through the courts.

The Deputy Commissioner acknowledged that some private company taxpayers will need to decide how to treat unpaid present entitlements (**UPEs**) when preparing their 2024 tax returns. She referred to the published Interim Decision Impact Statement, which explains that the Commissioner is maintaining the view expressed in TD 2022/11 while the special leave application is pending.

She also noted that how private company beneficiaries deal with UPEs may have implications under other integrity provisions in the tax law, including section 100A and subdivision EA. These provisions operate independently of the *Bendel* appeal process. As such, the Deputy Commissioner indicated that there is a "clear pathway" for taxpayers who wish to avoid potential exposure to those provisions, irrespective of the outcome of the current High Court proceedings.

No blanket exercise of 109RB discretion

The Deputy Commissioner has confirmed that there will be no blanket exercise of the discretion under section 109RB in circumstances where a group has arranged its affairs in reliance on the *Bendel* decision, and a deemed dividend has arisen, even if the Commissioner is ultimately successful in the High Court.

She explained that section 109RB allows the Commissioner to disregard the operation of Division 7A or permit a deemed dividend to be franked where the dividend arose due to an honest mistake or inadvertent omission. However, the discretion can only be exercised on a case-by-case basis, and only where a deemed dividend has actually arisen, with each matter assessed on its individual facts and circumstances.

Current ATO approach

The Deputy Commissioner acknowledged the uncertainty arising from the decision and the interest it has generated within the profession:

> *We understand this is a significant area for practitioners and private groups and will provide updates as appropriate.*

She confirmed that the ATO's position remains that a UPE to a corporate beneficiary, where the amount is retained in the trust and made available for its use, may constitute a loan for Division 7A purposes. The ATO will continue to administer the law on that basis unless and until the outcome of the appeal determines otherwise.

The Deputy Commissioner concluded that the ATO will consider issuing further practical guidance once the appeal has been resolved.

w https://www.ato.gov.au/businesses-and-organisations/business-bulletins-newsroom/deputy-commissioner-louise-clarke-discusses-bendel-decision

8.5 New NSW land tax website

Revenue NSW launched a redesigned land tax website on 5 May 2025. The updated site is intended to improve user experience by offering clearer explanations of land tax calculations, practical examples, and simplified step-by-step instructions for key tasks such as lodging returns, accessing assessment notices, and setting up payment plans.

Key features include:

1. streamlined navigation and reorganised content for easier access;
2. a quick access button on the homepage linking directly to Land Tax Online;
3. plain English content with practical examples to illustrate key concepts;
4. step-by-step guidance for managing land tax obligations; and
5. continued functionality for existing bookmarks.

Revenue NSW has also updated its customer correspondence, including assessment notices and new client letters, to make them easier to understand and respond to effectively.

Users are encouraged to explore the updated website and provide feedback through the on-site survey to support further enhancements.

w https://www.revenue.nsw.gov.au/news-media-releases/new-land-tax-website-launching-monday-5-may
w https://www.revenue.nsw.gov.au/taxes-duties-levies-royalties/land-tax

8.6 ATO to focus on deduction claims

On 7 May 2025, the ATO revealed some "wild" and "unbelievable" tax deduction attempts it saw last year.

Some of the attempts included:

1. a mechanic tried to claim an air fryer, microwave, two vacuum cleaners, a TV, gaming console and gaming accessories as work-related. The claim was denied as these expenses are personal in nature;
2. a truck driver tried to claim swimwear because it was hot where they stopped in transit and they wanted to go for a swim. The claim was denied as these expenses are personal in nature; and
3. a manager in the fashion industry tried to claim well over $10,000 in luxury-branded clothing and accessories to be well presented at work, and to attend events, dinners and functions. The clothing was all conventional in nature and was not allowed.

In this announcement, the ATO also reminded taxpayers of the following:

1. the 'myDeductions tool' on the ATO app. The tool allows taxpayers to keep records of work and general expenses which can be easily shared with a registered tax agent or uploaded to 'myTax'; and
2. to declare all sources of income, including amounts earned from additional jobs or services outside regular employment.

w https://www.ato.gov.au/media-centre/ato-unveils-wild-tax-deduction-attempts-and-priorities-for-2025

8.7 ATO small business focus areas

On 9 May 2025, the ATO updated its webpage on Small Business Focus Areas, outlining key areas of compliance attention for the 2025–26 financial year. The update highlights the ATO's ongoing scrutiny in the following areas:

1. **Lodgment**: Ensuring small businesses meet their obligations to lodge tax returns and activity statements on time.
2. **Cash Economy**: Monitoring businesses that may be underreporting income by dealing in cash.
3. Superannuation Guarantee: Focusing on correct and timely payment of super to employees, especially using Single Touch Payroll data.
4. **GST Obligations**: Addressing incorrect or inconsistent GST reporting, particularly regarding registration and reporting thresholds.
5. **Related-party Transactions**: Examining business arrangements that may result in income shifting or artificial deductions.
6. **Profitability**: Comparing reported income to benchmarks to identify underperformance or anomalies suggesting non-compliance.

w https://www.ato.gov.au/businesses-and-organisations/corporate-tax-measures-and-assurance/our-focus-areas-for-small-business/small-business-focus-areas