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The Tax Institute

Taxation *in* Australia

Section 99B: implications for Australian beneficiaries
George Psarrakos, CTA

Self-coaching your way to bust your busyness
Karen Stein

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Invitation to write

We welcome original contributions that are of interest to tax professionals, lawyers, academics and students.

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Insights from the Institute

Regular columns

Tax News – at a glance

by TaxCounsel Pty Ltd

September – what happened in tax?

The following points highlight important federal tax developments that occurred during September 2023. A selection of the developments is considered in more detail in the "Tax News – the details" column on page 174 (at the item number indicated).

More amending legislation

The Treasury Laws Amendment (Support for Small Business and Charities and Other Measures) Bill 2023, which was introduced into parliament on 13 September 2023, contains amendments that, when enacted, will give effect to several previously announced measures. **See item 1.**

Connected entities: Commissioner's control discretion

The Commissioner has released a final determination that provides guidance on the administration of the discretion conferred on him by s 328-125(6) of the *Income Tax Assessment Act 1997* (Cth) to disregard, when working out an entity's aggregated turnover, that entity's control of another entity where the control percentage is at least 40% but less than 50% (TD 2023/5). **See item 2.**

Commissioner's Tax Summit address

With about six months to go until his term of office expires, and determined not to take his foot off the pedal, the Commissioner of Taxation (Mr Chris Jordan) gave his last address at The Tax Institute's Summit on 6 September 2023. **See item 3.**

And for no other purpose

A majority of the Full Federal Court (Wheelahan and Hespe JJ; Logan J dissenting) has affirmed a decision of Thawley J at first instance that the appellant taxpayer was liable for GST and luxury car tax for the tax periods from June 2016 to November 2017 in respect of some 40 cars acquired by the taxpayer and displayed at the Gosford Classic Car Museum which was owned and operated by the taxpayer (*Automotive Invest Pty Ltd v FCT* [2023] FCAFC 129). **See item 4.**

Family trust election issues

In a recent decision, the Full Federal Court (Logan, Wheelahan and Hespe JJ) has unanimously dismissed an application by the taxpayers for leave to appeal from an interlocutory decision of Wigney J in which his Honour rejected their contentions that there were grounds for ordering that moneys paid by them into court following the making of freezing orders should be repaid to them (*Widdup v DCT* [2023] FCAFC 145). **See item 5.**

One-off government payment not income

The AAT has held that a payment received by a taxpayer from a fairness fund that had been established by the Victorian Government in connection with changes to the regulation of the taxi industry was not income according to ordinary concepts (*Bains and FCT* [2023] AATA 2477). **See item 6.**

Property development profits

The Federal Court (Charlesworth J) has rejected a taxpayer's challenge to amended assessments made by the Commissioner on the basis that profits from the disposal of subdivided and developed land were assessable income (*Makrylos v FCT* [2023] FCA 971). **See item 7.**

When employee bonus derived

The AAT has held that an employee bonus that fell due for payment to the taxpayer while he was a resident of Kuwait (and not of Australia), but was paid to him in later income years after he became a resident of Australia, was assessable income of the taxpayer in the income years in which it was paid (*Tawfik and FCT* [2023] AATA 2541).

President's Report

by Marg Marshall, CTA

Local engagement, local connections

President Marg Marshall reflects on local connections and an improving Institute.

The tax profession is a diverse and broad discipline – from legal to academic, sole practitioner to large, multinational corporations, you'll find tax practitioners working in almost every corner of our economy.

The Tax Institute is a national organisation and we are proud to have members from across the tax profession and from all around Australia. That kind of reach means that we are able to have influence in important conversations and draw on the insight and expertise of practitioners from all walks of life. Our incredible volunteer community is testament to the broad and inclusive nature of our membership.

However, even as we look to grow and expand, the value of small, local connections cannot be understated. How wonderful is it to know the practitioners working in your area? To share ideas, successes and challenges with like-minded professionals?

Our Local Tax Clubs, a series of events that run in many parts of the country, are a key opportunity to start building your network in your own backyard. These are events that deal with issues of immediate importance and allow you time to discuss day-to-day challenges with those who understand your work.

There are two sessions left for the year for most of our Local Tax Clubs. If you haven't already, I encourage you to register and head along to your local gathering to talk tax and get to know your fellow members.

We continue to work to maintain those local networks in this and other ways. Local engagement allows us to tailor our membership experience to what is relevant to you. In future, we hope to engage directly with members on an even more personal level. One of the best things about our community is the sense of camaraderie built among members, and whether you've been with us for one year or one decade, I hope you are finding your place in our community.

Growing as an Institute

This year, we have made significant investments in our events, membership experience, advocacy and resources. As always, we are working towards the goal of continually improving the professional lives of our members.

This process of growth and improvement is not finished (is growth ever really finished?). We continue to work on new ways of bringing value to you. We appreciate your feedback and patience as we evolve and encourage you to engage with local Institute representatives to ensure that your voice is heard as we work to better our community.

What our future looks like

As the end of the year approaches and we turn our thoughts to 2024, the Institute is in a position to flourish. The foundations we have laid and the investments we have made provide stability for the future. They mean that we can focus on the important business of educating tax practitioners and improving the professional lives of our members.

We will hold our Annual General Meeting soon, which is another opportunity for you to be involved in the direction of the Institute. All voting members are invited to attend and I encourage you to take up this invitation.

As always, our future is guided by the needs of our members. Please continue to engage with us and be involved in the process as we move forward together.

CEO's Report

by Chair and Acting CEO, Clare Mazzetti

The path towards our goals

Acting CEO Clare Mazzetti on how the Institute is planning and prioritising future goals.

In June this year, I wrote to you about how, in my role as Acting CEO, I would be working with the Board to put the Institute on a clear path towards its strategic goals. We knew then that there was much change ahead for the Institute. We are still in the midst of change and, as I wrote then, the interests of our members, volunteers and the tax community continue to take centre stage in all that we do.

We, like many organisations, are working to make our operating model more efficient and effective. In doing so, I have had opportunity to reflect on the practice of goal-setting.

In the professional world, we are all familiar with the importance of setting goals to work towards. It helps to focus your energy, prioritise your time, and appreciate the value of your work.

When a goal seems particularly hard to reach, I find it is often that we've forgotten to consider the method of reaching it. Processes, priorities and planning, though far less glamorous than big ticket goals, are just as important, if not more so, as the goal itself. Knowing your destination is important – but that's not what gets you there.

For the Institute, a big part of this is ensuring that our methods align with our member expectations and our internal values of accountability, community spirit, exploring possibilities, making an impact, and working to be the best version of ourselves.

In recent months, we have been focused on investing in the systems, processes and foundation that will allow us to reach future goals. Those goals include cementing our place as the home of tax education, continuing our advocacy work, and delivering an upgraded, modern digital experience to members. Many of our more ambitious goals remain works-in-progress. Some, such as digital transformation, are an ongoing journey of improvement, rather than a set destination.

To achieve these things, we are evaluating the way we work, our financial sustainability, our culture and much more.

These things contribute to the "how" of reaching our goals as an Institute. I know I speak on behalf of the whole team at the Institute when I say we hope that the foundations we are laying now will have significant benefits for your tax career for years to come.

What's next

As we round out the year, it is time to start thinking ahead to what our next goals look like and the ways we may have to grow or adapt to reach them.

In coming months, we hope to announce the appointment of a new CEO, who will bring their own ideas, perspective and goals to the table. I have been working with a number of wonderful candidates to identify a leader who aligns with our values and understands our vision. Our recent work, as mentioned above, also sets the stage for a new CEO to hit the ground running.

I am confident that the next steps for our organisation, be it appointing a new CEO, continuing our work in the digital space, or launching new learning options, will be of great benefit to our community. I look forward to taking that journey with you.

Senior Tax Counsel's Report

by Julie Abdalla, FTI

Interpretation of tax law

We trace the evolution of tax law interpretation by the High Court of Australia pre- and post-introduction of s 15AA of the *Acts Interpretation Act 1901* (Cth).

Australia's legal system is underpinned by the doctrine of the separation of powers. That is, the legislature makes the law; the executive administers the law; and the judiciary interprets the law. Most significant taxes, such as income tax, superannuation-related taxes, customs and excise duties, and goods and services tax, are levied under the authority of the Commonwealth legislation (ie at the federal level).

Interpretation of Commonwealth legislation and instruments made under Commonwealth Acts is subject to the *Acts Interpretation Act 1901* (Cth) (the Interpretation Act). Part 5 of the Interpretation Act contains the general interpretation rules. Section 15AA of the Interpretation Act was introduced by the *Statute Law Revision Act 1981* (Cth). It is noteworthy as it provides guidance on purposive interpretation and indicates that this is to be preferred to other kinds of interpretation.

Tax law interpretation pre-1980s

The earliest High Court case that dealt with the interpretation of tax law is *Anderson v Commissioner of Taxes (Vic)*[1] (*Anderson*) where Latham CJ supported the strict interpretation of tax legislation by reference to the letter of the law.[2]

Further, in *Anderson*, Rich and Dixon JJ approved the approach of strict interpretation of tax law, referring to case law and indicating that the intention to impose tax must be demonstrated by "clear and unambiguous language and cannot be inferred from ambiguous words".[3] Their Honours referred to Lord Buckmaster's view in *Ormond Investment Co v Betts*[4] of this rule as a cardinal principle and referred to his comments that:[5]

> "It is well established that one is bound, in construing Revenue Acts, to give a fair and reasonable construction to their language without leaning to one side or the other, that no tax can be imposed on a subject by an Act of Parliament without words in it clearly showing an intention to lay the burden upon him, that the words of the statute must be adhered to, and that so-called equitable constructions of them are not permissible."

One of the last cases to clearly support strict interpretation based on the letter of the law was *FCT v Westraders Pty Ltd*,[6] where Barwick CJ observed that parliament must specify the circumstances that will lead to the payment of tax, and the role of the court is to merely interpret the words of the parliament and assess the applicability of the circumstances to the taxpayer.

Tax law interpretation post-1980s

We start to see a shift in the early 1980s towards a more purposive approach to statutory interpretation. In *Cooper Brookes (Wollongong) Pty Ltd v FCT*,[7] Mason and Wilson JJ, in relation to the interpretation of tax law, noting that the literal interpretation of the provision in question was capricious and irrational, favoured purposive interpretation.[8] Their Honours also observed that taxing statutes are not to be given special status as they are not immune from the general principles governing the interpretation of statutes.[9]

In *Austin v The Commonwealth of Australia*,[10] Kirby J stated that the purposive rule of interpretation is supported by provisions of the Interpretation Act and acknowledged that the courts in recent times have departed from interpreting tax laws narrowly and literally, in favour of an interpretation that seeks to achieve the purpose or object of the legislation.[11]

Conclusion

There has been a gradual shift in the approach to the interpretation of tax law from the strict interpretation of the letter of the law in the early 1980s towards a more purposive approach. This is also supported by the introduction of s 15AA to the Interpretation Act in 1981.

With the increase in principles-based drafting in tax law formulation, purposive interpretation is all the more important. This approach also needs to be consistently followed through in the administration of the law but that is a topic for another day.

References

1 [1937] HCA 24.

2 *Inland Revenue Commissioners v Duke of Westminster* [1936] AC 1 at 24-25 and *Partington v Attorney-General* (1869) LR 4 HL 100 at 122, cited in *Anderson v Commissioner of Taxes (Vic)* [1937] HCA 24.

3 *Brunton v Commissioner of Stamp Duties for New South Wales* [1913] AC 747 at 760, cited in *Anderson v Commissioner of Taxes (Vic)* [1937] HCA 24. See also *Attorney-General v Milne* [1914] AC 765 at 781.

4 [1928] AC 143 at 151, cited in *Anderson v Commissioner of Taxes (Vic)* [1937] HCA 24.

5 *Ormond Investment Co v Betts* [1928] AC at 162, cited in *Anderson v Commissioner of Taxes (Vic)* [1937] HCA 24.

6 [1980] HCA 24.

7 [1981] HCA 26.

8 [1981] HCA 26 at [28].

9 [1981] HCA 26 at [33].

10 [2003] HCA 3.

11 [2003] HCA 3 at [251].



Tax News – the details

by TaxCounsel Pty Ltd

September – what happened in tax?

The following points highlight important federal tax developments that occurred during September 2023.

Government initiatives

1. More amending legislation

The Treasury Laws Amendment (Support for Small Business and Charities and Other Measures) Bill 2023, which was introduced into parliament on 13 September 2023, contains amendments that, when enacted, will give effect to several previously announced measures. The more important of these measures are noted below.

Instant asset write-off: small business entities

Proposed amendments to the *Income Tax (Transitional Provisions) Act 1997* (Cth) will increase the instant asset write-off threshold (the threshold below which amounts can be immediately deducted under the simplified depreciation rules) from $1,000 to $20,000. This will allow small businesses (with an aggregated annual turnover of less than $10m) to immediately deduct the full cost of eligible depreciating assets costing less than $20,000 that are first used or installed ready for use for a taxable purpose in the period from 1 July 2023 until 30 June 2024.

Small business energy incentive

Other proposed amendments to the *Income Tax (Transitional Provisions) Act 1997* will provide small and medium businesses (with an aggregated annual turnover of less than $50m) with access to a bonus deduction equal to 20% of the cost of eligible assets or improvements to existing assets that support electrification or more efficient energy use.

This is a temporary measure to support small and medium businesses to electrify, improve their energy efficiency, and save on their energy bills. The bonus deduction applies to the cost of eligible assets and improvements up to a maximum amount of $100,000, with the maximum bonus deduction being $20,000.

The amendments will apply to eligible assets first used or first installed ready for use, and eligible improvement costs incurred, from 1 July 2023 until 30 June 2024.

New class of deductible gift recipients

Other amendments when enacted will facilitate certain community charities (community charity trusts and community charity corporations) achieving deductible gift recipient status in recognition of their valuable contribution to their communities and Australian society. A new pathway is being created to enable these charities to apply for deductible gift recipient endorsement by the Commissioner of Taxation.

Accounting standards: general insurance contracts

Amendments to the income tax law with respect to general insurance will provide broad alignment with the new accounting standard, AASB 17.

The amendments will reduce the income tax compliance burden on the general insurance industry caused by the misalignment between the income tax law and the adoption of the new AASB 17. The amendments are to apply to income years starting on or after 1 January 2023.

The Commissioner's perspective

2. Connected entities: Commissioner's control discretion

The Commissioner has released a final determination that provides guidance on the administration of the discretion conferred on him by s 328-125(6) of the *Income Tax Assessment Act 1997* (Cth) (ITAA97) to disregard, when working out an entity's aggregated turnover, that entity's control of another entity where the control percentage is at least 40% but less than 50% (TD 2023/5).[1]

An entity may need to aggregate its annual turnover with that of other entities to determine its eligibility for certain tax concessions or other tax treatment. For example, an entity's aggregated turnover is relevant when determining whether it is a small business entity for an income year and able to access a range of concessions, including CGT concessions, shorter periods of review, and exemption from FBT for car parking fringe benefits.

The aggregation issues have taken on added significance following the introduction of tax incentives with higher aggregated turnover thresholds, thereby extending their relevance beyond the small business market. This includes temporary measures introduced in 2020 in response to the COVID-19 pandemic, such as full expensing of depreciating assets, and the corporate loss carry back rules.

Aggregation will be necessary where there is a connection between the entities based on "control". Subsections 328-125(2) and (4) ITAA97 set out the primary tests of control for this purpose. These subsections provide for the calculation of a "control percentage" and, where an entity (the first entity) holds a percentage of at least 40% of the relevant interests in another entity (the test entity), the first entity is considered to control the test entity for the purposes of s 328-125 ITAA97.

Where the first entity has a control percentage of at least 40% but less than 50%, s 328-125(6) ITAA97 provides the Commissioner with a discretion to determine that it does not control the test entity. To make that determination, the Commissioner must think that the test entity is controlled by an entity or entities (the third entity or entities) that is not, or does not include, the first entity or any of its affiliates.

Diagram 1 sets out the scenario in which the question of the Commissioner's exercise of the discretion can arise.

If the Commissioner were to exercise the discretion, the test entity's annual turnover would not be counted when determining the aggregated turnover of the first entity.

The statutory condition for exercising the Commissioner's discretion requires that the Commissioner positively conclude that there is actual control of the test entity by a third entity or entities. It is not sufficient to merely show that the first entity does not have actual control of the test entity.

The principal concern of TD 2023/5 is to provide guidance on the following specific issues relating to the concept of "control" which the ATO has had to consider when administering the Commissioner's discretion:

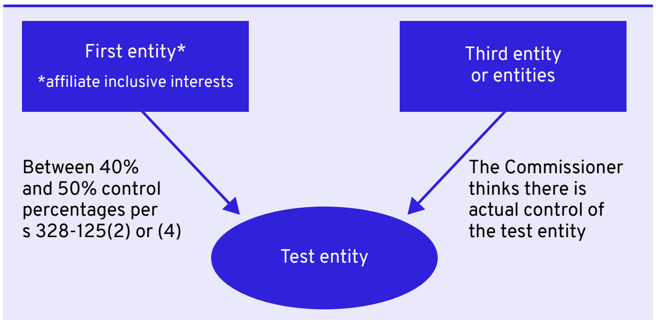
- requests for the Commissioner's discretion to be exercised where a third entity has sole or primary responsibility for day-to-day management of the affairs of the test entity, but holds relatively insignificant or no interests in the income or capital of the test entity, or in shares carrying voting rights (if the test entity is a company); and
- applicants suggesting that their control percentage of between 40% and 50% should be disregarded because the remaining holders of interests in the test entity will together necessarily control the entity, irrespective of their number or relationship to each other.

Some points considered in TD 2023/5 are:

- the relevance of who has responsibility for managing day-to-day business;
- whether the third entity can hold less than a 40% interest; and
- the position where there is control by more than one "third" entity.

TD 2023/5 does not seek to deal comprehensively with the concept of "control" for the purposes of considering the Commissioner's discretion, nor the wide range of circumstances in which it will be relevant for the exercise of the Commissioner's discretion. The Commissioner's conclusion on control in a given case will turn on its specific facts and circumstances. General statements on the concept, supported by generic examples with narrow fact patterns, would be of limited assistance as guidance for individual cases and may even mislead. Additional public guidance may be considered in future if there is a need to clarify the Commissioner's views on further discrete issues arising from the ongoing administration of the Commissioner's discretion.

Diagram 1. Commissioner's discretion scenario



3. Commissioner's Tax Summit address

With about six months to go until his term of office expires, and determined not to take his foot off the pedal, the Commissioner of Taxation (Mr Chris Jordan) gave his last address at The Tax Institute's Summit on 6 September 2023.

Some points of interest from the Commissioner's Summit address are:

- his key priority as the Commissioner has been to consistently build trust and confidence in the ATO's professionalism, reliability and fairness;
- the Tax Avoidance Taskforce, which commenced in 2016, has helped secure more than $26b in additional tax revenue up to 30 June 2023;
- locking in tax outcomes for the future has become an important feature of the ATO's settlements with multinationals. It provides the ATO, taxpayers and the community with certainty that multinationals are meeting their tax obligations and avoiding disputes into the future;
- while publicly disclosed information in relation to settlements will typically show significant payments being made for the finalisation of the dispute, these amounts do not reflect the additional revenue that will often be payable in future years as a result of locking in tax outcomes;
- using the momentum from the legal precedent established in the *Chevron* case,[2] the ATO has been able to resolve a range of disputes, removing more than $40b in excessive interest charges from related party dealings which would have otherwise been deducted;
- since 2013, the ATO is now an international leader in championing effective global multinational tax compliance at the OECD's Forum of Tax Administration;
- the ATO is cracking down on deliberate attempts to defraud the Australian taxpayer. In response to increasing fraud attempts, the ATO is embedding fraud prevention methods into its systems, and increasing its detection capabilities. A Fraud and Criminal Behaviours Group has been established, with 500 dedicated staff;
- also front of mind is addressing collectable debt. Most collectable debt is self-assessed. It includes GST that a business has collected and received credits for but has not remitted, and it includes unpaid pay-as-you go withholding and superannuation guarantee charge that has a direct impact on employees; and
- small businesses continue to be over-represented in the ATO debt book, owing over $33b of the $50.2b of collectable debt. Of that, $23b is unpaid business activity statement debt. Although small business is

overrepresented here, the ATO is very focused on every group in the tax system.

As to the future, the Commissioner said that, if a tax professional's business model is high-volume, simple tax returns with no value add and low margins, such a business will not be viable in three to five years. The role of tax agents and other intermediaries is already changing and the reality is that the opportunities need to be embraced.

While pleased with the ATO's progress so far, the Commissioner said that there was always more to do. There needs to be an increased uptake of the ATO's digital services – it is 2023 and the ATO was still receiving close to 1 million paper activity statements and sending out cheques.

In the future, there should be fewer calls from tax professionals coming into the ATO call centres. Today, more than one in five of the 1.4 million calls answered by the ATO this financial year have been from tax professionals, and many of the calls are for things that professionals can be self-serving through the ATIO's online services.

The Commissioner acknowledged that the onus will be on the ATO to make sure that easy access is provided to clear, helpful information and guidance. A whole new ATO website is coming later this year, with a much better look and feel which will make it easier for people to find the answers they need.

Recent case decisions

4. And for no other purpose

A majority of the Full Federal Court (Wheelahan and Hespe JJ; Logan J dissenting) has affirmed a decision of Thawley J at first instance that the appellant taxpayer was liable for GST and luxury car tax for the tax periods from June 2016 to November 2017 in respect of some 40 cars acquired by the taxpayer and displayed at the Gosford Classic Car Museum (the museum) which was owned and operated by the taxpayer (*Automotive Invest Pty Ltd v FCT*[3]).

The taxpayer's liability turned on whether it used the cars for a purpose other than a "quotable purpose", as defined in the *A New Tax System (Luxury Car Tax) Act 1999* (Cth) (LCT Act). The Commissioner conceded that each of the cars was held by the taxpayer as trading stock and this meant that the issue was whether the taxpayer had the intention of using each car for no other purpose.

Before Thawley J, the parties accepted that the LCT Act issue turned on whether, by being displayed in the museum, each of the 40 cars was used for a purpose other than holding the car as trading stock, for the purposes of s 9-5(1) LCT Act. The parties also accepted that, on the facts of the present case, the GST issue was to be resolved on the same basis, notwithstanding that the GST issue was concerned with the entitlement to quote which was to be determined by the intended use at the time of quoting, rather than actual use.

Thawley J concluded that each car was not used for no purpose other than holding the car as trading stock. Each car was also used for the purpose of displaying the car, together with other cars, as exhibits in a museum, being operated commercially as a museum.

In dismissing the taxpayer's appeal from the decision of Thawley J, the majority of the Full Court, in a joint judgment, said that they did not accept the taxpayer's construction of "and for no other purpose" as requiring the other purpose to be exclusive or alternative to the purpose of holding the cars as trading stock. That construction was not consistent with the ordinary reading of the phrase. It was not consistent with the use of the conjunctive "and". Most importantly, it rendered the phrase "and for no other purpose" otiose. The phrase "and for no other purpose" was to be read as "solely" or "only".

Their Honours said that the presence of the phrase "other than … for hire or lease" to qualify the concept of trading stock did not require the phrase "and for no other purpose" to be read otherwise than as "solely". The question was not whether the use of each of the cars as part of a display at the museum was a subsidiary or an ancillary purpose, or collateral to the purpose of holding each car as trading stock. Rather, the question was whether the use of each of the cars as part of such a display was an incident of holding that car as trading stock, such that its display was part of its use as trading stock and was part of a singular purpose. The issue was therefore one of fact and degree.

Their Honours went on to say that it may readily be accepted that displaying an item for sale is an incident of holding that item as trading stock. An item of trading stock is not held for an additional purpose merely because it is displayed on a shop shelf or in a shop window, rather than held in the shop's storage room. A car does not cease to be used solely as trading stock merely because it is displayed in a car dealership showroom. It may also be accepted that the mere deployment of a novel (as opposed to conventional) manner of displaying cars does not result in any particular car being held for a purpose other than as trading stock.

However, the nature of and manner in which the cars in the present case were displayed went much further than simply displaying the cars as for sale in a showroom in a novel way to appeal to a niche market. Their Honours said that the display of the cars achieved a commercial end in and of itself by attracting as many visitors as possible. The nature of the display was that of an exhibition marketed to visitors as a destination in and of itself. The entrance fee charged was more than nominal. Adults were charged $20 each and $12 for each child. Family tickets were $55. About one year after it opened, the museum attracted its 100,000th visitor, and the display of the cars by the museum generated in excess of $1.32m in admission fees in its first full financial year of operation. Fees were also charged for external parties to stage events such as corporate functions at the museum.

After saying that the purpose for which the cars were used was to be ascertained by an objective consideration of the totality of the facts and circumstances, the majority went on:

> "110. … Although, on their own, the provision of facilities such as a café or an outlet offering memorabilia do not and cannot determine the purpose for which each of the cars was used by the appellant, the existence of those facilities in conjunction with the charging of a real and not a token entrance fee, the engagement of employed

> and volunteer staff to provide guidance and information to visitors, and the marketing of the exhibited collection of cars as a tourist or visitor destination is not consistent with a conclusion that the cars were used for the purpose of being held as trading stock and for no other purpose. Whatever Mr Denny as the controlling mind of the appellant thought he was doing, or whatever character might be attributed to the use of the premises for local government purposes, and irrespective of whether the premises constituted a museum *stricto sensu*, the scale and nature of the appellant's activities resulted in each of the cars being held as more than trading stock."

5. Family trust election issues

In a recent decision, the Full Federal Court (Logan, Wheelahan and Hespe JJ) has unanimously dismissed an application by the taxpayers for leave to appeal from an interlocutory decision of Wigney J in which his Honour rejected their contentions that there were grounds for ordering that moneys paid by them into court following the making of freezing orders should be repaid to them (*Widdup v DCT*[4]).

On 21 June 2022, the Deputy Commissioner issued Mr Julian Widdup and Mrs Cecilia Widdup with a number of notices under various provisions in the *Income Tax Assessment Act 1936* (Cth) (ITAA36). Those notices included: (1) notices of liability under s 271-90 of Sch 2F ITAA36 to pay family trust distribution tax of $3,599,409 for which Mr and Mrs Widdup were said to have been liable since 20 July 2018 (the FTDT notices); (2) notices of liability to a general interest charge of $1,210,907 (accrued as at 21 June 2022) in respect of the family trust distribution tax liability; (3) notices of amended assessment to income tax under s 170(1) ITAA36 which assessed Mr and Mrs Widdup to each be liable for income tax of $1,785,073 for the income year ended 30 June 2018; and (4) notices of assessment of shortfall interest of $249,943 in respect of the assessed income tax shortfall.

It should be noted that a crucial underlying issue in relation to the FTDT notices, which it was unnecessary to decide for the purposes of the interlocutory proceedings and will only arise for decision if the substantive objection proceedings go to trial, was whether or not a family trust election had been made and, more particularly, whether an election could be made without the written election being given to the Commissioner. While, as noted, not called on to make a decision on the issue, Wigney J and the Full Court did in fact canvas the issue. The Full Court said:

> "40. We are satisfied that there is an arguable case that the form published by the Commissioner for the making of a family trust election does not need to be given to the Commissioner and that it is sufficient if the Commissioner is notified that a family trust election in the approved form has been made. Particularly in the context of a self-assessment regime, there is an arguable case that by completing the tax return forms published by the Commissioner in a manner consistent with the making of a family trust election, the Commissioner may be notified that a family trust election in the approved form has been made by a trustee."

6. One-off government payment not income

The AAT has held that a payment received by a taxpayer from a fairness fund that had been established by the Victorian Government in connection with changes to the regulation of the taxi industry was not income according to ordinary concepts (*Bains and FCT*[5]).

Before he exited the Victorian taxi industry, the taxpayer held three taxi licences. The industry had undergone significant changes and reforms adversely affecting taxi licence holders. One such change was the emergence of Uber services. Another involved reforms to Victorian laws which had the effect of revoking existing tradeable taxi licences, for which licence-holders had paid significant sums, and replacing those licences with non-tradeable licences.

To address the disruption caused by the reforms, the Victorian Government provided various forms of financial relief, including the Victorian taxi reform hardship fund and transitional assistance payments, which were tailored to provide some relief against particular consequences of the reforms.

Additionally, the Victorian Taxi Reform Fairness Fund (the fund) was set up to provide support to persons facing significant financial hardship as a result of the reforms. On 6 March 2018, the taxpayer received a payment of $250,000 from the fund (the payment). He exited the taxi industry in or around June 2018. The taxpayer's first licence was revoked on 9 October 2017. If not revoked sooner, the remaining licences would have been revoked by statute with effect from 1 July 2018. The AAT said that the sole issue for determination was whether the payment was subject to income tax as income according to ordinary concepts.

After considering the contentions of the parties, the AAT said that the balance favoured the view that the payment was a one-off discretionary payment which was paid as a matter of public policy for the relief of unfair financial hardship, rather than a product of the taxpayer's remaining taxi business, such as it was at the time, or as a substitute for or estimate of income forgone.

Although the only issue regarded by the parties and, hence, the AAT as requiring decision was whether the payment from the fund was income, it is not clear that this was necessarily the case. It is submitted that there may have been a question of whether CGT event H2 (receipt for an event relating to a CGT asset), which is what may be called "the residual CGT event", had happened. It is not possible to canvass in any detail the construction and application of the CGT event H2 provisions, but a few points may be noted.

Broadly, CGT event H2 can only happen if no other CGT event happens in the particular circumstances. The event happens if an act, transaction or event occurs in relation to a CGT asset that the taxpayer owns, and the act, transaction or event does not result in an adjustment being made to the asset's cost base or reduced cost base (s 104-155 ITAA97). It is well established that the words "in relation to" are words of potentially wide import and, depending on the context, are capable of referring to any relationship between two subject-matters.[6] It is suggested that it is arguable that the making of the payment that was in issue in the *Bains* case constituted an act (if not also a transaction or an event) that occurred before the taxpayer exited the taxi industry.

A capital gain is made from the happening of CGT event H2 if the capital proceeds, because of the CGT event, are more than the incidental costs the taxpayer incurred that relate to the event. A capital loss is made if those capital proceeds are less (s 104-155(3) ITAA97).

For the purposes of working out a capital gain or capital loss from the happening of CGT event H2, the capital proceeds are the money or other consideration that the taxpayer received, or is entitled to receive, because of the act, transaction or event (s 116-20(2) ITAA97).

7. Property development profits

The Federal Court (Charlesworth J) has rejected a taxpayer's challenge to amended assessments made by the Commissioner on the basis that profits from the disposal of subdivided and developed land were assessable income (*Makrylos v FCT*[7]).

On 30 June 2006, the taxpayer (a Mr Michael Makrylos) signed a contract for the purchase of 7,060 square metres of land situated at 125 Dick Ward Drive in the Darwin suburb of Coconut Grove (the property). The purchase price was $825,000 and settlement of the contract occurred on 17 August 2006 (the acquisition date).

The land was later rezoned, subdivided, developed and sold pursuant to a joint venture agreement between the taxpayer and corporate entities associated with him. In the income years ending 30 June 2013 and 30 June 2014, 15 of the 16 developed parcels sold for a total of $11,995,000.

The taxpayer lodged tax returns for the 2013 and 2014 income years, claiming his assessable income to be $93,473 and $59,775, respectively, and his resultant tax liabilities to be $22,532 and $10,973, respectively. The Commissioner originally assessed the taxpayer on the basis of the returns as lodged by him. The tax returns treated the property as the taxpayer's main residence for a period of time after its acquisition, and from 18 May 2011, as trading stock held in the course of a business. The taxpayer first received assessments that accorded with the returns as lodged.

Following an audit, the Commissioner issued amended assessments to the taxpayer for the 2013 and 2014 income years on the basis that the taxpayer held the property as trading stock from the acquisition date. The effect of the amended assessments was that the taxpayer had a personal tax liability of $1,353,656 and $487,008 for the respective income years. The taxpayer lodged objections with respect to both income years. The basis of the taxpayer's objection was that he did not commence to hold the property as trading stock until on or about 18 May 2011, with the result that his assessed tax payable should be calculated by reference to (among other things) the value of the property as at that date.

On 27 May 2021, the Commissioner allowed the objection in relation to the 2013 income year only in part and otherwise disallowed the objection. By the objection decision, the Commissioner concluded that the property was held as trading stock from the acquisition date. The taxpayer appealed to the Federal Court from the Commissioner's objection decision. Charlesworth J has now dismissed the taxpayer's appeal.

The tax returns submitted by the taxpayer claimed deductions on the basis that the property converted to trading stock on 18 May 2011 and therefore had a deemed value as at that date, calculated in accordance with s 70-35(1) ITAA97.

By the objection decision, the Commissioner concluded that the property was held as trading stock from the acquisition date. That conclusion had the consequence that fewer deductions could be claimed in the 2013 and 2014 income years than those claimed by the taxpayer.

On appeal, the taxpayer maintained that the date on which the property first came to be held as trading stock was 18 May 2011 and, in the alternative, alleged that the property was first held as trading stock "some time in April 2010".

The taxpayer contended that, as at the acquisition date, he intended to construct his primary family dwelling on the property and that that intention persisted for some years. He asserted that he did not hold the property as "trading stock" until 18 May 2011, the date on which he became legally obliged to commit the property to a joint venture on the fulfilment of the condition precedent in the applicable joint venture agreement.

Charlesworth J said that, as a question of law, it was correct to say that the signing of a contract for the purchase of land for a family home does not constitute the carrying on of a business. However, as a question of fact, the taxpayer had not proven to the requisite standard that he purchased the property for a family home.

In addition, her Honour was not satisfied that the business of property development undertaken by the "Makrylos Group" was a business conducted only by the corporate entities that she had identified. The evidence supported a conclusion that the taxpayer personally was a participant among a group of entities whose affairs were so integrated that the business of property development could not be said to be owned and operated by any one of them in isolation from the other. The taxpayer had not shown that the property was held in his own name for reasons independent of the property development business conducted by the "Makrylos Group".

The facts of the present case were that the taxpayer ventured real property legally held in his own name into a joint venture, and that its ultimate sale was undertaken in the ordinary course of a property development business. The relevant question was when the purpose for holding the property for that future purpose first arose. That purpose may arise without the person having certainty as to the terms on which the thing might be sold, to whom it might be sold and the form it might take at the time of its sale.

After referring to the definition "trading stock" in s 70-10(1) ITAA97 (anything produced, manufactured or acquired that is held for purposes of manufacture, sale or exchange in the ordinary course of a business), Charlesworth J said that the phrase "held for the purposes of sale" was not to be equated with "held in the ordinary course of a business". A person may hold land for the purpose of a sale intended to occur some time in the future. The item held will be trading stock if the sale in the person's contemplation is a sale that is to occur in the ordinary course of a business at an undetermined date in the future.

The particular business envisaged may change, without altering the purpose for which the item is held. Charlesworth J said that she found that the taxpayer held the property for that purpose well before April 2010. Her Honour said that, even if the purpose first arose in 2008, the taxpayer's appeal must be dismissed because there was insufficient valuation evidence to show that the assessments were excessive or to show what they should have been.

Charlesworth J said that, for similar reasons, the submission that the requisite purpose could not have come into existence until the taxpayer became legally obliged to sell the land (that is, on 18 May 2011) should be rejected. On the facts, the taxpayer held the land for the defined purpose well before he was contractually obliged to proceed with its sale. As a question of law, an item may be held for the purpose of sale in the ordinary course of a business whether or not the person has, in their contemplation, the form that the item may take when it is sold, to whom it will be sold, at what price, and on what conditions.

The Commissioner also contended that, because the taxpayer acquired the property as part of a profit-making scheme, the taxpayer would only have been entitled to a general deduction pursuant to s 8-1 ITAA97 for outgoings in the nature of acquisition costs in the income year of the acquisition and not in either the 2013 or 2014 income year.

Unlike the purpose referred to in the "trading stock" definition, for a profit-making scheme to arise, it was necessary for the taxpayer to have an intention to derive a profit from the relevant property at the time of its acquisition. Her Honour said that, if it were necessary to determine the question, she would have concluded on the whole of the evidence that the taxpayer entered into the contract for the acquisition of the property with the purpose of developing it in a multi-dwelling subdivision, and selling the units within the development with a view to gaining a profit in a commercial venture.

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References

1 The draft determination is TD 2023/D2 and was considered in the August 2023 Tax Tips column of this journal at p 70.

2 *Chevron Australia Holdings Pty Ltd v FCT* [2017] FCAFC 62.

3 [2023] FCAFC 129.

4 [2023] FCAFC 145.

5 [2023] AATA 2477.

6 *First Provincial Building Society Ltd v FCT* [1995] FCA 1101.

7 [2023] FCA 971.

Tax Tips

by TaxCounsel Pty Ltd

Contract timing issues

The time when a contract is made can have significant taxation implications.

Background

Whether and, if so, when a contract is entered into will frequently have potential implications, not only for the commercial interests of the parties involved, but also for their taxation positions.

For example, as discussed below, the time when a contract for the acquisition or disposal of an asset is entered into will be relevant for the purposes of CGT in a range of situations.

Further, the time of the acquisition of an asset under a contract may be relevant for the purpose of qualifying for a concession, such as an investment allowance or an accelerated or instant asset write-off.[1]

Delving back into history a little, the first limb of the former s 26(a) of the *Income Tax Assessment Act 1936* (Cth) (ITAA36) (which operated to bring into a taxpayer's assessable income the profit arising from the sale of property that was acquired by the taxpayer for the purpose of profit-making by sale) required regard to be paid to the purpose of the taxpayer at the time of the acquisition of the property. In the case of an acquisition of property under a contract, this time was the date of the contract.[2]

The time of the making of a contract may also be relevant when determining whether a loss or an outgoing has been incurred for the purposes of applying the general deduction provision of the *Income Tax Assessment Act 1997* (Cth) (ITAA97).[3]

In the absence of a special provision to the contrary in the relevant legislation, for taxation purposes the determination of whether there is a binding contract in any case is determined by reference to the same principles as apply for the purposes of contract law generally and have evolved over the years. The application of these principles in particular situations has given rise to a very substantial body of case law.

This article briefly considers the recent decision of Cheeseman J in *Moss v Contracoin Pty Ltd*[4] in which her Honour outlined the issues that arise when determining whether a contract has been entered into.

The article also considers the issues raised by the special CGT discount capital gain provision that applies where a CGT event happens to a CGT asset that was acquired 12 months or more after the acquisition of a CGT asset but the event happens under an agreement made within that 12-month period.

Contract timing: CGT relevance

For CGT purposes, the potential relevance of the time when a contract is entered into may be illustrated by the following.

CGT event A1

The time a contract is entered into is relevant for the purposes of applying various CGT events.

The most frequently encountered CGT event is CGT event A1 which happens if a taxpayer disposes of a CGT asset that was not acquired before 20 September 1985.[5] A taxpayer disposes of a CGT asset if a change of beneficial ownership occurs from the taxpayer to another entity, whether because of some act or event or by operation of law.[6]

The time of the happening of CGT event A1 is:

- when the taxpayer enters into the contract for the disposal of the asset; or
- if there is no contract, when the change of ownership occurs.[7]

Where CGT event A1 happens, the time when the event is taken to happen determines the time when the other party to the contract is taken to have acquired the asset.[8]

CGT event D1

Another example in the context of the CGT events where the time of the making of a contract will be relevant to the happening of a CGT event is provided by CGT event D1. That event happens if a taxpayer creates a contractual right or other legal or equitable right in another entity,[9] for example, a restrictive covenant or an easement.

If the right is created by a contract, the time of the happening of CGT event D1 is when the contract is entered into.[10]

Discount capital gain issues

One requirement that must be met for a taxpayer to be eligible to claim the CGT discount capital gain concession provided for by Div 115 ITAA97 is that the particular capital gain must result from a CGT event happening to a CGT asset that was acquired by the entity making the capital gain at least 12 months before the CGT event.[11]

However, the effect of s 115-40 ITAA97 is that a capital gain on a CGT asset from a CGT event is not a discount capital gain if the CGT event occurred "under an agreement" that the taxpayer made within 12 months of acquiring the CGT asset. This provision is clearly intended to operate as an anti-avoidance provision.

The explanatory memorandum to the New Business Tax System (Integrity and Other Measures) Bill 1999 states:

> "11.29 If a taxpayer makes a capital gain from a CGT event happening to a CGT asset acquired by the taxpayer

more than 12 months before the CGT event, under an agreement entered into within that 12 month period, the capital gain does not qualify for the CGT discount *[item 13, section 115-40]*. This rule will prevent taxpayers inappropriately taking advantage of the CGT discount by seeking to extend artificially the period of ownership of the asset that produces the capital gain."

There is no definition of "agreement" for this purpose. This contrasts with the somewhat elaborate provisions in the former s 26AAA ITAA36[12] which were aimed at the situation where a sale of property occurred more than 12 months after it was purchased and the sale was made in pursuance of an option granted, or an agreement entered into, during the 12 months. For that purpose, the reference to an agreement or option included an agreement or option that was not enforceable by legal proceedings, whether or not it was intended to be enforceable. Further, an arrangement or understanding, whether formal or informal and whether express or implied, was deemed to be an agreement.[13]

There does not appear to be any decision of the Federal Court or the AAT in which this discount capital gain provision has been considered, and the Commissioner has not issued a ruling to explain his views as to its operation.

It is important to keep in mind that, if the Commissioner were to make an assessment on the basis that s 115-40 applied, the taxpayer would bear the onus of establishing that the assessment was excessive. In this regard, if there were a contract for the sale of a CGT asset that is entered into shortly after the expiration of the 12-month period, this may, in some circumstances, prompt the Commissioner to assess on the basis that there was an agreement within the 12-month period, particularly if the amount of the capital gain were large.

The lack of guidance is unfortunate because, literally, the provision could have a potentially wide operation. For example, what would be the situation if a taxpayer were to acquire factory premises which the taxpayer intends to lease in order to derive rental income and leases the premises six months after their acquisition, with the lease granting to the lessee an option to acquire the premises at the end of the term of the lease? In that situation, would the option be a relevant "agreement"?

At the other end of the spectrum, if a taxpayer were to acquire property and, within 12 months of the acquisition, a put option and a call option were to be granted in respect of the property that was exercisable outside the 12-month period, this presumably would potentially activate the provision under discussion.

There will be a range of circumstances to consider, including the extent to which unenforceable agreements can be relevant.

The existence of a contract: general principles

For the purposes of revenue law, the question of whether the parties have entered into a contract will depend on the application of the ordinary principles of contract law. The cases in which these principles have been considered and applied form an ever-growing area of the law.

While, in the vast majority of cases, it will be clear whether there is a contract for the disposal of a CGT asset and when that contract was entered into, there are circumstances in which difficulties may arise.

The applicable principles that are relevant when determining whether there is a binding contract in particular circumstances were recently set out by Cheeseman J in *Moss v Contracoin Pty Ltd*.[14] Her Honour said that those principles were well established and referred to *Archer Capital 4A Ltd as Trustee for the Archer Capital Trust 4A v Sage Group Plc*[15] where Farrell J made these points:

- when determining whether the parties have reached a binding agreement, the court must ascertain the "objective intention" of the parties. It is not enough that the parties reached a consensus; they must have intended that the consensus arrived at will be legally binding and enforceable by a court;
- determining objective intention is a fact-based inquiry. Although judges are wont to formulate guiding "principles" or "propositions", those "principles" and "propositions" are subservient to the fact-specific objective finding of the parties' intention;
- intention may be found in a series of communications or a single document. It is the intention that a reasonable person would discern that the parties had concerning the subject-matter of the alleged contract if that reasonable person had the parties' knowledge of the words and actions communicated to each other and of the surrounding circumstances;
- it is uncontroversial that labelling a document "subject to contract" is not determinative of whether the parties intended to be bound before the execution of a formal agreement. However, the use of the phrase usually creates a presumption that the parties did not intend that document to be binding, but rather the basis for a future contract; and
- the conduct of the parties after the time the alleged contract arose may be relevant for the purpose of casting light on the meaning of communications and whether the parties intended to be legally bound.

Masters v Cameron

Cheeseman J also referred to the leading decision of the High Court in *Masters v Cameron*[16] and, in particular, to the following passage from the High Court's judgment:

> "9. Where parties who have been in negotiation reach agreement upon terms of a contractual nature and also agree that the matter of their negotiation shall be dealt with by a formal contract, the case may belong to any of three cases. It may be one in which the parties have reached finality in arranging all the terms of their bargain and intend to be immediately bound to the performance of those terms, but at the same time propose to have

the terms restated in a form which will be fuller or more precise but not different in effect. Or, secondly, it may be a case in which the parties have completely agreed upon all the terms of their bargain and intend no departure from or addition to that which their agreed terms express or imply, but nevertheless have made performance of one or more of the terms conditional upon the execution of a formal document. Or, thirdly, the case may be one in which the intention of the parties is not to make a concluded bargain at all, unless and until they execute a formal contract.

10. In each of the first two cases there is a binding contract: in the first case a contract binding the parties at once to perform the agreed terms whether the contemplated formal document comes into existence or not, and to join (if they have so agreed) in settling and executing the formal document; and in the second case a contract binding the parties to join in bringing the formal contract into existence and then to carry it into execution. Of these two cases the first is the more common. Throughout the decisions on this branch of the law the proposition is insisted upon which Lord Blackburn expressed in *Rossiter v Miller* (1878) 3 App Cas 1124 when he said that the mere fact that the parties have expressly stipulated that there shall afterwards be a formal agreement prepared, embodying the terms, which shall be signed by the parties does not, by itself, show that they continue merely in negotiation. His Lordship proceeded: '… as soon as the fact is established of the final mutual assent of the parties so that those who draw up the formal agreement have not the power to vary the terms already settled, I think the contract is completed' (1878) 3 App Cas, at p 1151: see also *Sinclair, Scott & Co. Ltd. v. Naughton* [1929] HCA 34; (1929) 43 CLR 310, at p 317. A case of the second class came before this Court in *Niesmann v. Collingridge* [1921] HCA 19; (1921) 29 CLR 177 where all the essential terms of a contract had been agreed upon, and the only reference to the execution of a further document was in the term as to price, which stipulated that payment should be made 'on the signing of the contract'. Rich and Starke JJ. observed (1921) 29 CLR, at pp 184, 185 that this did not make the signing of a contract a condition of agreement, but made it a condition of the obligation to pay, and carried a necessary implication that each party would sign a contract in accordance with the terms of agreement. Their Honours, agreeing with Knox C.J., held that there was no difficulty in decreeing specific performance of the agreement, 'and so compelling the performance of a stipulation of the agreement necessary to its carrying out and due completion' (1921) 29 CLR, at p 185: see also *O'Brien v. Dawson* [1942] HCA 8; (1942) 66 CLR 18, at p 31.

11. Cases of the third class are fundamentally different. They are cases in which the terms of agreement are not intended to have, and therefore do not have, any binding effect of their own: *Governor & c. of the Poor of Kingston-upon-Hull v. Petch* [1854] EngR 995; (1854) 10 Exch 610 (156 ER 583). The parties may have so provided either because they have dealt only with major matters and contemplate that others will or may be regulated by provisions to be introduced into the formal document, as in *Summergreene v. Parker* [1950] HCA 13; (1950) 80 CLR 304 or simply because they wish to reserve to themselves a right to withdraw at any time until the formal document is signed. These possibilities were both referred to in *Rossiter v. Miller* [1877] UKLawRpCh 168; (1878) 3 App Cas 1124. Lord O'Hagan said: 'Undoubtedly, if any prospective contract, involving the possibility of new terms, or the modification of those already discussed, remains to be adopted, matters must be taken to be still in a train of negotiation, and a dissatisfied party may refuse to proceed. But when an agreement embracing all the particulars essential for finality and completeness, even though it may be desired to reduce it to shape by a solicitor, is such that those particulars must remain unchanged, it is not, in my mind, less coercive because of the technical formality which remains to be made' (1878) 3 App Cas, at p 1149. And Lord Blackburn said: 'parties often do enter into a negotiation meaning that, when they have (or think they have) come to one mind, the result shall be put into formal shape, and then (if on seeing the result in that shape they find they are agreed) signed and made binding; but that each party is to reserve to himself the right to retire from the contract, if, on looking at the formal contract, he finds that though it may represent what he said, it does not represent what he meant to say. Whenever, on the true construction of the evidence, this appears to be the intention, I think that the parties ought not to be held bound till they have executed the formal agreement' (1878) 3 App Cas, at p 1152. So, as Parker J. said in *Von Hatzfeldt-Wildenburg v. Alexander* [1911] UKLawRpCh 90; (1912) 1 Ch 284, at p 289 in such a case there is no enforceable contract, either because the condition is unfulfilled or because the law does not recognize a contract to enter into a contract."

Cheeseman J went on to say that the authorities have subsequently recognised an additional or fourth category of agreements to contract which is where the parties intend to be bound immediately and exclusively by the terms which they had agreed on while expecting to make a further contract in substitution for the first contract, containing, by consent, additional terms.

Perri v Coolangatta Investments

Cheeseman J also referred to the decision of Mason J in *Perri v Coolangatta Investments Pty Ltd*:[17]

"17. Generally speaking the court will tend to favour that construction which leads to the conclusion that a particular stipulation is a condition precedent to performance as against that which leads to the conclusion that the stipulation is a condition precedent to the formation or existence of a contract. In most cases it is artificial to say, in the face of the details settled upon by the parties, that there is no binding contract unless the event in question happens. Instead, it is appropriate in conformity with the mutual intention of the parties to say that there is a binding contract which makes the stipulated event a condition precedent to the duty of one party, or perhaps of both parties, to perform. Furthermore, it gives the courts greater scope in determining and adjusting the rights of the parties. For these reasons the condition will not be construed as a condition precedent to the formation of a contract unless the contract read as a whole plainly compels this conclusion."

Contracts for sale of land

In *McDonald v FCT*,[18] the taxpayer contended that there was a binding oral contract for the sale of real property that was entered into before 20 September 1985 and was relevant for CGT purposes, rather than the contract that resulted from the subsequent exchange of contracts.

The Full Federal Court rejected this contention. Stone J (Beaumont J agreeing) said that, in *Allen v Carbonel*,[19] the High Court commented that the "usual method of selling real estate in New South Wales is by means of the signing and exchange of contracts in the form approved by the Real Estate Institute of New South Wales". The High Court relied on this practice to support an inference that the parties did not intend an informal agreement for the sale of the property to be binding. Stone J went on:

"18. … In *GR Securities Pty Ltd v Baulkham Hills Private Hospital Pty Ltd* (1986) 40 NSWLR 631, McHugh JA in the NSW Court of Appeal referred to the method of exchange … and stated that 'even though the parties agree in writing that real estate is sold for a specified price, the presumption is that no binding contract exists until "contracts" are exchanged'. This presumption or expectation has been accepted in many other cases …"

Stone J said that neither her comments nor the authorities cited should be taken as denying that it is possible for a contract for the sale of land in New South Wales to be effected other than by exchange of contracts. Stone J then went on:

"20. … Ultimately, the intention of the parties as to whether they enter into binding obligations is decisive; *Masters v Cameron* [1954] HCA [72] … In reaching the point from which they intend to be bound, they may agree that one of the terms of the contract is that certain obligations under it are to be retrospective to a specified date. However, the date of the formation of the contract is a matter of law and the parties cannot, by backdating the written document, rewrite history with the effect that a binding contract existed from the specified date.

21. No special form of words is necessary to ensure that an agreement is binding or not binding. However, the practice in New South Wales of proceeding by exchange of contracts is so entrenched that a party contending for an intention to proceed other than in accordance with the established procedure will need clear evidence to support the contention."

Observations

It will be appreciated that the question when a contract is entered into can arise in a number of contexts. While the answer is often clear, difficulties can arise and, in a taxation context, there may be provisions that seek to prevent arrangements that attempt to get around a provision (as in the case of the discount capital gain provisions).

The issues discussed are fundamental and the parties' legal advisers should, to the extent possible, seek to draft a document that clearly indicates its status. The potential for problems is illustrated by the number of reported cases in which the principles enunciated by the High Court in its decision in *Masters v Cameron* have been applied.

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References

1 See, for example, *Kearney v FCT* 84 ATC 4295 and *W & J Investments Pty Ltd v FCT* [1989] FCA 415.

2 *Annalong Pty Ltd v FCT* [1972] HCA 45.

3 S 8-1 ITAA97.

4 [2023] FCA 976.

5 S 104-10(1) ITAA97.

6 S 104-10(2) ITAA97.

7 S 104-10(3) ITAA97.

8 S 109-5 ITAA97.

9 S 104-35(1) ITAA97.

10 S 104-35(2) ITAA97.

11 S 115-25(1) ITAA97.

12 Assessable income from property purchased and sold within 12 months (on or before 25 May 1988.

13 See former s 26AAA(1)(b) and (c) and (2) ITAA36.

14 [2023] FCA 976. For other recent decisions, see *Re Sparkling Beverages Pty Ltd (No. 2)* [2023] VSC 419 and *Al-Freah v Thompson* [2023] QCA 175.

15 [2015] FCA 960.

16 [1954] HCA 72.

17 [1982] HCA 29.

18 [2001] FCA 305. There may be an issue of the enforceability of such a contract. The general rule is that, to be enforceable, a contract for the sale or other disposition of land (or any interest in land) must be evidenced in writing and signed by the party to be charged or by some other person thereunto lawfully authorised by that party. See, for example, s 54A of the *Conveyancing Act 1919* (NSW). For a decision in which the operation of this section was considered, see *Khoury v Khouri* [2006] NSWCA 184.

19 [1975] HCA 14.

Mid Market Focus

by Nilan Gandhi, ATI, HLB Mann Judd

Last chance to claim loss carry back tax offset

A timely reminder for eligible entities that the 2023 income tax return provides them with the last opportunity to claim the loss carry back tax offset.

Introduction

The Treasury Laws Amendment (A Tax Plan for the COVID-19 Economic Recovery) Bill 2020 (the Bill) was first introduced into parliament on 7 October 2020 and was enacted as law later that month on 14 October 2020.

The Bill amends the income tax regime to allow eligible entities with an aggregated turnover of less than $5b to carry back a tax loss in the 2019–20, 2020–21 or 2021–22 income year and apply it against tax paid in a previous income year as far back as the 2018–19 income year.[1]

This measure provides eligible entities with the opportunity to claw back income tax paid in an earlier income year with tax losses incurred in the current income year. To do so, the eligible entity applies for a refund for the income tax paid in an earlier income year (for example, the 2020–21 income year), as a refundable tax offset, where the eligible entity has incurred a tax loss in a more recent income year (for example, the 2022–23 income year).

As this offset is a refundable tax offset, eligible entities will receive cash refunds which will be significantly important for their cash flow.

It is important to note that these refunds will represent the income tax paid in an earlier income year which has been returned to the taxpayer through the loss carry back tax offset.

Eligible entities

Only a corporate tax entity is eligible to claim this offset, which means that the following types of entities will be eligible:[2]

- companies;
- corporate limited partnerships; and
- public trading trusts.

Entities that are in a trust structure will not be eligible for this loss carry back tax offset.

In addition, a corporate tax entity must satisfy the following requirements to be eligible to claim the loss carry back tax offset:

1. the entity has carried on a business with an aggregated turnover of $5b or less in the income year that it has incurred the tax loss;
2. the entity has remained as a corporate tax entity throughout the period when the entity made the tax loss to the income year it is applying the tax loss to; and
3. the corporate tax entity must have lodged an income tax return for the current income year and each of the five years preceding the current income year. Some exceptions apply where the corporate tax entity is not required to lodge a tax return for an earlier income year.

Claiming the loss carry back tax offset

The eligible entity must make the choice to claim the tax offset on the income tax return for the income year in which it has made the tax loss. The application for this tax offset is made when the tax return for that loss income year is lodged with the ATO.

When claiming the tax offset on the income tax return, the eligible tax entity must be aware of the following:

- the amount of the tax offset that it is claiming, and this must be completed at the appropriate labels on the income tax return;
- all labels on the income tax return for this loss carry back tax offset must be completed; and
- the franking account balance must be completed.

Calculating the loss carry back tax offset

A corporate tax entity's entitlement to the tax offset is determined by working through the following steps:

1. calculating the amount of tax loss that the entity is carrying back to an earlier income year;
2. if the entity has net exempt income, the loss carry back amount will need to be adjusted or reduced by any utilised net exempt income that the entity had in the income year in which the loss is being applied to;
3. the loss carry back remaining after applying unutilised net exempt income is then multiplied by the entity's corporate tax rate in the year of loss:
   a. where the entity is a base rate entity, the corporate tax rate in the loss year will vary between 27.5% and 25% for the 2019–20 to 2022–23 income years; and
   b. where the entity is not a base rate entity, the corporate tax rate will be 30% in the loss year; and
4. where the entity is claiming the offset, the offset is limited to:
   a. the amount of income tax paid by the entity in the earlier income year in which it is applying the loss to;

b. the maximum amount of refund that the entity can obtain under this offset is equivalent to the income tax paid in the earlier income year; and

c. the balance of the entity's franking account at the end of the income year.

The ATO has an online calculator which can be used to determine the loss carry back tax offset.

The loss carry back tax offset is a refundable tax offset. However, the Commissioner's usual practice is to apply any refund amount arising from an offset towards paying another amount that the entity owes to the Commissioner before an actual refund is paid.[3]

Ineligible tax losses

A corporate tax entity cannot claim carry back tax losses that have been transferred to the entity through:

- Div 170 ITAA97 (that is, transfers between companies in the same foreign banking group);
- transfers to the head company of an income tax consolidated group; or
- tax losses that exist in the entity through excess franking offsets.

Other considerations

A corporate tax entity will need to be aware of other considerations when applying for the loss carry back tax offset, including:

1. the integrity rules:
   a. the similar business test or the continuity of ownership test;
   b. Where the entity fails the similar business test and the continuity of ownership test, the losses can still be carried forward and applied against taxable income in the future income years; and
2. where an entity has claimed the loss carry back tax offset, the entity must note that this will impact the following:
   a. the ability to pay franked dividends in the future as the franking account will be impacted by this offset; and
   b. the ability to carry forward tax losses to offset taxable income in future income years.

Summary

The 2023 income tax return provides a last opportunity for businesses in a corporate tax entity structure to claim the loss carry back tax offset. This refundable tax offset will assist businesses in boosting their cash flow by recovering some of the income tax paid in an earlier income year if they are eligible to do so.

Nilan Gandhi, ATI
Manager – Business & Tax Advisory
HLB Mann Judd

References

1 Ch 2.1 of the explanatory memorandum to the Treasury Laws Amendment (A Tax Plan for the COVID-19 Economic Recovery) Bill 2020.

2 S 960-115 of the *Income Tax Assessment Act 1997* (Cth) (ITAA97).

3 Para 2.36 of the explanatory memorandum to the Treasury Laws Amendment (A Tax Plan for the COVID-19 Economic Recovery) Bill 2020.

Higher Education

Enhancing problem-solving skills

The dux of Tax for Trusts for Study Period 1 2023 shares how the subject helped to improve her approach to client advice and communication.

Yuxi Dedic
Supervisor, Martin and Martin Consulting Pty Ltd, Victoria

How did you get started in tax?

I started my full-time professional role as an SMSF auditor and later developed an interest in general accounting and taxation. After immersing myself in SMSF auditing for about a year, I moved to my current firm where I have been for the last five years. I prepare annual financial statements and income tax returns for companies, trusts, partnerships, superannuation funds, and individuals/sole traders. I also prepare monthly, quarterly and annual GST/BAS/IAS and annual FBT returns.

What made you select the subject "Tax for Trusts: from an SME perspective"?

I chose the subject mainly because of my strong interest in trusts. Almost 100% of my clients have trusts as a part of their group entities. Studying Tax for Trusts with The Tax Institute helped me build a solid knowledge base to assist my clients.

I would say that 80% of the subject content covered what I do daily in the office, such as the loss of trust estate and other relevant tests, the streaming of trust distributions, and Div 7A. The other 20% covered areas that I do not regularly practice, such as trust vesting, disclaimer of trust entitlements, and capital gains distributions to non-residents, so this part of the subject content which helped to build my overall knowledge in trusts.

Have you applied this new knowledge in your work?

Definitely. Taking trust vesting as an example, now, when I review the trust deed of a discretionary trust, I pay closer attention to the trust vesting date and advise trustees to extend the vesting date if permitted by the deed in order to avoid the situation where trustees lose their discretionary power to distribute.

What has been your experience studying at The Tax Institute Higher Education?

I would say that the benefits are massive. Compared to my previous study experience, the materials provided by The Tax Institute are well-structured and relevant to my day-to-day work. In addition, the lecturers are experts in the subjects that they are teaching, and they all have solid practical knowledge. I benefitted a lot from the Q&A sessions with lecturers because they not only helped with the questions that I had about study materials, but also with issues that I regularly encounter in my work.

What's the secret to your academic success?

I guess the trick is to be organised and to have a routine. I allocated two nights of study during the week and 2–3 hours per day during weekends. This allowed enough time to go through study materials more than once and to prepare for assignments and exams.

Where to now for you when it comes to continuing tax education?

I am a CPA and, once I have completed the CTA3 Advisory subject, I will obtain the CTA qualification and the Graduate Diploma of Applied Tax Law. I love refreshing my tax knowledge and building on it and, with the ever-changing tax law, I cannot see myself stopping tax education any time soon.

What advice do you have for other tax professionals considering studying?

I advise other tax professionals to start studying with The Tax Institute. I developed a deeper understanding of what I do daily in the office after I started the CTA program and the Graduate Diploma of Applied Tax Law.

Section 99B: implications for Australian beneficiaries

by George Psarrakos, CTA, Tax Partner, Mutual Trust

There is limited guidance on the application of s 99B of the *Income Tax Assessment Act 1936*. Its extreme breadth seems to catch common situations involving Australian beneficiaries of both resident and non-resident trusts. With the potential for "throwback" interest, the outcome for unwary beneficiaries can be punishing. This article explores s 99B in detail and considers many of the unanswered questions around its application in practice. For foreign trustees and executors, or Australian inheritors, beneficiaries or migrants, there are warnings of the potential dangers and the available, albeit limited, solutions.

Introduction

More millionaires have migrated to Australia in the last 20 years than (almost) any other country in the world. This is in addition to returning expats, inheritors and beneficiaries of overseas wealthy families.

It is shocking for these clients to learn that close to half of their funds (or more) could be wiped out by Australian tax. The application of s 99B of the *Income Tax Assessment Act 1936* (Cth) (ITAA36) is often met with disbelief by clients. It has the potential to capture amounts which a lay person might otherwise consider to be tax-free.

I say this because s 99B applies at the point an amount of trust property is paid or applied for the benefit of an Australian resident beneficiary. However, the source of the amount could be foreign income derived by a foreign trustee while the beneficiary was a non-resident (even decades ago).

In addition to the primary tax (and, if relevant, interest and penalties), there is also the potential for "throwback interest" which has a punitive impact on the unwary beneficiary.

Despite s 99B having been introduced 45 years ago, its interpretation and scope are not always fully understood.

In today's environment, s 99B can apply to common situations, such as:

- previous foreign employment earnings;
- pre-migration wealth;
- foreign gifts and inheritance; and
- inter-generational wealth transfers.

This article explores the scope of s 99B and useful strategies to manage the implications for Australian resident high net wealth individuals and wealthy families. This includes accounting treatment, record-keeping and other practical and technical considerations.

References to "the Tax Act" are to the *Income Tax Assessment Act 1936* and the *Income Tax Assessment Act 1997* (collectively).

Origin story

Like all good heroes and villains, s 99B has an interesting origin story.

In 1969, the High Court in *Union Fidelity Trustee Co of Australia Ltd v FCT* (*Union Fidelity*) determined that Div 6 of Pt III ITAA36, as it was then written, did not capture foreign-sourced income. This was problematic as the foreign-sourced income of a foreign trustee (or potentially even a resident trustee) could escape Australian tax unless it was paid as income to the Australian resident beneficiary.[1] The trust income could also be tax-free or lightly taxed in the source jurisdiction.

This loophole was identified in the 1975 Asprey report.[2]

To combat this, from 1 July 1978, s 99B and its sidekick, s 99C ITAA36, were introduced by the Income Tax Assessment Amendment Bill (No. 5) 1978[3] (the 1978 Bill) to capture the accumulated untaxed income of foreign trusts.

Along with a re-write of Div 6, the 1978 Bill formed the basis for the current "modern" system of taxing trust income, which, along with some further modernisation, band-aid fixes, and an attribution regime, now consists of:

- the trust's tax law income (or "net income", used interchangeably) is calculated on the basis that the trustee was a hypothetical resident, referred to as the "residency assumption" (ie worldwide income);
- a resident trust estate is one where, at *any time* during the year of income, *a* trustee of the trust was a resident of Australia, or the central management and control of the trust was in Australia;
- where a beneficiary was "presently entitled" or "deemed presently entitled"[4] to a "share" of the income of the trust estate (accounting or distributable income), its "share" of the trust's tax law income[5] is included in the beneficiary's assessable income and taxed at the beneficiary's tax rate[6] – with an apportionment of source for periods of non-tax residency;
- where there was no present entitlement to all or part of the trust income, the trustee is taxed at a flat 47% on the trust's tax law income. A foreign trustee is only taxed

on the trust's Australian-sourced income, but not on its foreign-sourced income[7] (hence the need for s 99B); and

- s 99B which operates as a "catch-all" for *all* trust amounts, with a carve-out for amounts previously subject to tax or otherwise exempt under the provisions above (or taxed under the transferor trust attribution regime).

So, when unleashed, s 99B had the potential to apply to both foreign and resident trusts.[8]

In 1991, the "extreme width" of s 99B was recognised by Hill J's judgment in *Traknew Holdings Pty Ltd v FCT*.[9] As such, it is sometimes stated that s 99B should be limited to the perceived legislative purpose for its enactment (ie accumulated foreign income of a foreign trust).

In 2011, concerns regarding s 99B were raised in the Treasury discussion paper *Modernising the taxation of trust income – options for reform*, in particular, the uncertainty from the "expansive wording" of s 99B and its application to resident trusts.

In 2011, the ATO released ATO ID 2011/93 which outlined that under:

> "… section 99B of the ITAA 1936, and by inference from subsection 102AAM(5) of the ITAA 1936, that there is no apportionment of the amount included in assessable income by reference to the residency status of the beneficiary as at the time the income was derived by the trust. Rather, the only explicit condition concerning residency is that the beneficiary be a resident at some time during the year of income in which the trust property is paid to them or applied for their benefit."

In 2012, *Howard v FCT*[10] considered s 99B where there was a share buy-back and a successive distribution through interposed foreign trusts to an Australian resident.

In 2017, the ATO finalised TD 2017/24 and TD 2017/23 which addressed the interaction of s 95(1) ITAA36 net income and s 855-10 of the *Income Tax Assessment Act 1997* (Cth) (ITAA97), with the conclusion that such capital gains from a foreign trust are caught to the beneficiary under s 99B and are not eligible for the CGT discount nor offset against capital losses in the beneficiary's hands.

In 2019, the burden of proof in relation to s 99B was addressed in *Campbell and FCT*.[11]

In 2021, the ATO released TA 2021/1 which briefly discussed s 99B, among other provisions. It states that "genuine gifts or loans" may be caught by s 99B "if the amounts are paid by or through trusts".

The ATO's website (last modified on 1 December 2021) contained guidance on s 99B which outlined three simple questions:[12]

> "• Whether you are a beneficiary of the foreign trust.
>
> • Where the foreign trust obtained the money. This will assist in determining the source of the money.
>
> • Why the money was paid to you; for example, is it payment for services, a gift, a distribution, or a loan. This will assist in understanding the nature of the payment."

The 8 June 2023 key messages from the ATO's Private Groups Stewardship Group stated that there would be practical guidance issued on s 99B.

And here we are today!

The gateway: s 99B(1)

Section 99B(1) operates as a "basic rule" to include an amount in a beneficiary's "assessable income":

> "**Receipt of trust income not previously subject to tax**
>
> (1) Where, at any time during a year of income, an amount, being property of a trust estate, is paid to, or applied for the benefit of, a beneficiary of the trust estate who was a resident at any time during the year of income, the assessable income of the beneficiary of the year of income shall, subject to subsection (2), include that amount."

The title of s 99B (which forms part of the ITAA97 under s 950-100(1)) clearly states its objective to capture a receipt of untaxed trust income. There is no mention of "foreign trustee" or "foreign-sourced accumulated earnings".

For s 99B to be enlivened, trust property needs to be paid to, or applied for the benefit of, a resident beneficiary.

An amount of trust property of the trust estate

It is the "property" which is the subject of the trust relationship and this is the relevant starting point for the enquiry.

"Property" (unlike "CGT asset") is not defined for tax purposes. Its ordinary meaning is something which is capable of ownership, whether real or personal, tangible or intangible.[13] Section 99B therefore applies to not only a payment or an application of money, but also to any application of a trust asset.

Perhaps "property of the trust estate" can be contrasted to "income of the trust estate" which is the "surplus" income or "distributable" income ascertained by the trustee according to appropriate accounting principles and the trust instrument.[14] Therefore, its target is (prima facie) accumulated trust income (see discussion below on "corpus of the trust estate").

There is no enquiry as to the nature or character of the "property", that is, whether it is "income", "net income", gains, reserves, corpus or some other amount for accounting, tax or trust law purposes. Nor is there any enquiry of the source or situs of the relevant property.

There is no enquiry of the residence of the trust, the trustee or any other reference to domicile, settlor, transferor, controller or grantor.

In addition, the term "trust estate" is also not defined for tax purposes. The term "trustee" has an extended definition in s 6(1) ITAA36 for tax purposes. Generally, for Div 6 purposes, the term applies where the legal ownership of assets is vested in a person with some proprietary right by which the income arises, even though they may not be a trustee in the "proper sense" (eg executors and deceased estates but not liquidators).[15]

Finally, the word "amount" implies that the property being paid or applied must be quantified in some sense.[16] There is no guidance on how this is to be measured or valued.

An amount of money paid (including expenditure or cost) may be easily quantifiable, but the giving of property, or a non-cash benefit, might be its market value.[17] There is no mention of an "arm's length dealing". This raises some interesting questions where the property is a loan or an intangible benefit under s 99C (see later discussion).

If the amount is in foreign currency, it would be translated into Australian currency[18] when the amount is included in assessable income (on the basis that it is statutory income outside of the CGT provisions).[19]

Section 10-5 ITAA97 lists s 99B amounts as "statutory income".

Is paid to or applied for the benefit of

"Paid" is not generally defined in the Tax Act (although it may be defined for some purposes, such as for dividends or for withholding tax purposes).

The composite expression "paid *to*" implies a direct receipt of funds by the beneficiary.

"Applied for the benefit of" is similarly not defined in the Tax Act. It may imply an indirect payment, where the amount is dealt with by the trustee in some other way by which the beneficiary could benefit. It could include a payment to a third party, a payment in satisfaction of an amount owed by the beneficiary, a payment at the direction of the beneficiary, or a crediting of an amount (entitlement) to the beneficiary account with the trustee.

Section 99C expands the meaning of "applied for the benefit of a beneficiary of the trust estate".

A beneficiary of the trust estate

For s 99B to apply, it appears that the recipient of the trust property must be an actual beneficiary of the trust estate. Accordingly, someone who is not a beneficiary of the trust under the deed may not be caught under s 99B.

A beneficiary for tax purposes is generally accepted to be a person entitled to due administration by the trustee, that is, a mere object and not just someone who is entitled.[20]

The interest of the beneficiary in the trust is also not explored in s 99B(1) — only that the property is paid to or applied for their benefit.

The wording also seems to imply that the payment or application of the trust property must actually benefit (betterment) the person in their capacity as a beneficiary of the trust. There is no express wording in s 99B to that effect (as there is for shareholders/creditors in the s 6(1) definition of a "dividend"), and under s 99C, it appears that it could apply in broader situations.

Who was a resident at any time during a year of income

The jurisdictional nexus in s 99B is that the recipient beneficiary is an Australian tax resident "at any time" during an income year.

The "income year" means the period of 12 months beginning on 1 July,[21] unless the Commissioner allows a substituted accounting period.[22] It is unlikely that the Commissioner would allow a substituted accounting period for an individual as their circumstances would not be outside the "ordinary run" (see PS LA 2007/21).

The assessable income of the beneficiary shall … include that amount

Once the requisite connection between the payment or application of trust property and a resident beneficiary has been made, the "amount" of trust property is included in the beneficiary's assessable income.

As s 99B operates on an assessment basis, the assessable amount is included in the beneficiary's tax return. Given the trustee is a foreign entity, a trustee withholding mechanism would be impractical.

The amount is taxed at the beneficiary's marginal tax rate (assuming the beneficiary is not tax exempt), including any entitlement to the tax-free threshold (or pro rata) and the Medicare levy etc.

Subject to s 99B(2)

Section 99B(2) includes a number of items which reduce the amount included in the resident beneficiary's assessable income under s 99B(1) (see later discussion).

Interestingly, as it is the amount of the payment (property) which is included in the beneficiary's assessable income under s 99B(1), in the context of capital gains, it would be the payment of the capital proceeds which would be caught, not the net gain, if it were not for the reductions under s 99B(2).

Planning considerations under s 99B(1)

There are a number of planning considerations that arise around s 99B(1), as discussed below.

Is it a trust?

First, it is necessary to consider whether the foreign entity is a "trust" for Australian tax law purposes (eg a foreign foundation under civil law). This will depend on the entity's constituting documents (whether a deed, regulations or articles of association etc) and how the entity is recognised under the foreign law.[23]

In general, where the legal ownership of the assets vests in one entity, with an obligation to hold the assets for the benefit of another entity, the entity is likely to be considered a trust by the ATO for Australian tax purposes.[24]

Location, location, location

It is very easy for a foreign trust to become a resident. However, the location of the trustee or the trust estate's central management may not be of assistance. Payments from the accumulated income of the now resident trust would still be captured under s 99B(1).

On the other hand, this inquiry will be relevant from an administrative perspective and for dealing with current year trust income under s 97 or 99A ITAA36. Additionally, the transferor trust rules cease to have practical effect once the trust estate is a resident (ie attributable income is "nil").[25]

Similarly, the location of the trust assets would not matter. Australian-sourced income and taxable Australian property (TAP) of a foreign trustee falls within Div 6 or the withholding provisions (with some exceptions). It is only the location of the beneficiary that is important for s 99B purposes (see later for resident transferors).

Timing is everything: inbound beneficiaries

Section 99B can have no application where the beneficiary is not an Australian tax resident for the *entire* income year. Proactive advice and dealing with trust payments and property in the year ended 30 June *before* the beneficiary becomes an Australian tax resident is a simple solution.

Leaving a 12-month (full income year) buffer between payment and establishing an Australian footprint is an easy safeguard, given there is no (current) bright line threshold under the "resides test".

Leave the country: outbound residents and transitory beneficiaries

Another solution might be to simply leave the country 12 months (a full income year) before an "impending" foreign trust payment (subject to the application of s 99C). This, of course, is easier said than done and should be undertaken with extreme caution.

The resides test is a question of fact and degree and a "continuing association with Australia" will be unhelpful.

The domicile and the 183-day tests require that you have established a permanent or a usual place of abode (respectively) outside Australia — both require the Commissioner to be satisfied that this is in fact the case.[26]

Tax residency is easy to make and hard to break.

Love can be taxing: temporary residents

Generally, a taxpayer on a temporary Australian visa who does not have an Australian spouse would not be assessable on foreign-sourced ordinary income and statutory income derived[27] when they were a temporary resident (except for remuneration and personal services income).

Source tracing for s 99B is provided by s 6B(2A)(a)(ii) ITAA36 which considers that "for the purposes of this Act"[28] an amount of income derived by a person shall be deemed to be income derived from a particular source if the person derived the amount of income as a beneficiary of a trust estate and the amount of income can be attributed, directly or indirectly, to income derived from that source (or to an amount deemed by s 6B to be income derived from a source).

Accordingly, s 99B amounts should be non-assessable non-exempt income of a temporary resident (assuming they are not from an Australian source).

Section 768-910(2) ITAA97 should also cover an amount paid or applied at the time the person is a temporary resident, notwithstanding that they may not be a temporary resident for the full income year (as compared to the inbound/outbound scenarios above).

The transferor trust rules are also "switched off" for temporary residents (s 786-970 ITAA97).

Can a double tax agreement help?

Where a trustee is a dual tax resident, a double tax agreement (DTA)[29] is likely to allocate residency to the jurisdiction in which the trust has its "place of effective management". This may provide some insight as to how the trust should be administered for tax purposes from an Australian perspective. However, it is the beneficiary who is taxed under s 99B and not the trustee.

Where the Australian beneficiary is a dual tax resident but a foreign resident for DTA purposes, relief might be available.

Trust distributions are likely to be covered under the "other income" article in the DTA[30] when considering trust distributions. Under the OECD *Model Tax Convention on Income and on Capital*, exclusive taxing rights is given to the state of residence.

Therefore, a resident under Australia's domestic laws, but a foreign resident for DTA purposes, is likely to escape the impact of s 99B. However, an Australia resident for DTA purposes is likely to have no such luck and instead would look for relief from double tax by tax credit.

Section 3(4) of the *International Tax Agreements Act 1953* (Cth) also deems source by way of a look-through for trust income.

Foreign currency

As an amount of statutory income (but not a capital gain), an amount under s 99B denominated in foreign currency is converted for tax purposes to the equivalent Australian currency at the exchange rate applicable at the earlier of the time of receipt or when the requirement first arose to include it in the taxpayer's income".[31]

If an entitlement arises prior to satisfaction, or the amount remains in foreign currency, a foreign currency realisation event or a CGT event may arise.

A (trustee of a) foreign trust is not able to make a functional currency election under Subdiv 960-D ITAA97 (unless it is a "transferor trust" or has a CGT event from an interest in indirect Australian real property).

Tax rates

For a resident individual, it makes no difference if they are taxed under s 97 or 99B as both apply resident marginal tax rates. This assumes that the amount captured under both of these sections is the same and ignores throwback interest (discussed later).

For a company beneficiary, it will depend on whether the amount is referable (either directly or indirectly) to the "base rate entity passive income" of the foreign trustee.

Accumulated trust income captured under s 99B should not be "excepted trust income" for the purposes of Div 6AA ITAA36, so it would be taxed at punitive rates to minor beneficiaries.

Read the deed

Reading the deed (assuming you can access a copy in English) to understand whether the recipient is actually a beneficiary, and whether they are entitled to receive the trust amounts, will be relevant. If someone is not a beneficiary or not entitled to receive an amount as a beneficiary (eg breach of trust), s 99B might not apply.

For the purposes of the reductions in s 99B(2) or the timing under s 99C, the nature of the beneficiary's interest and their entitlements to trust income or corpus will be relevant.

Period of amendment

The usual four-year time limit appears to apply for s 99B purposes, subject to there being no fraud or evasion.

Rulings and voluntary disclosure

If an assessable amount under s 99B has been overlooked, a voluntary disclosure should be prepared to mitigate the risk of penalties. If there is uncertainty on the application of s 99B, a ruling may be beneficial.

Practically, amounts caught under s 99B would be brought to the Commissioner's attention by data-matching information with the Australian Transaction Reports and Analysis Centre.

The escape door: s 99B(2)

The extreme breadth of s 99B(1) is reined in by s 99B(2):

"(2) The amount that, but for this subsection, would be included in the assessable income of a beneficiary of a trust estate under subsection (1) by reason that an amount, being property of the trust estate, was paid to, or applied for the benefit of, the beneficiary shall be reduced by so much (if any) of the amount, as represents:

(a) corpus of the trust estate (except to the extent to which it is attributable to amounts derived by the trust estate that, if they had been derived by a taxpayer being a resident, would have been included in the assessable income of that taxpayer of a year of income);

(b) an amount that, if it had been derived by a taxpayer being a resident, would not have been included in the assessable income of that taxpayer of a year of income;

(ba) an amount that is non-assessable non-exempt income of the beneficiary because of section 802-17 of the *Income Tax Assessment Act 1997*;

(c) an amount:

(i) that is or has been included in the assessable income of the beneficiary in pursuance of section 97; or

(ii) in respect of which the trustee of the trust estate is or has been assessed and liable to pay tax in pursuance of section 98, 99 or 99A; or

(iii) that is reasonably attributable to a part of the net income of another trust estate in respect of which the trustee of the other trust estate is assessed and is liable to pay tax under subsection 98(4);

(d) an amount that is or has been included in the assessable income of any taxpayer (other than a company) under section 102AAZD; or

(e) if the beneficiary is a company – an amount that is or has been included in the assessable income of the beneficiary under section 102AAZD.

(2A) An amount that is not included in a beneficiary's assessable income because of paragraph (2)(d) or (e) is not assessable income and is not exempt income.

(3) In paragraphs (2)(d) and (e):

'company' means a company other than a company in the capacity of a trustee."

Section 99B(2) makes it clear that it is intended to reduce the "amount" that is assessable under s 99B(1). This limits the amounts initially caught under s 99B which may have otherwise been tax-free or subject to Australian tax.

The reduction is "by so much of the amount, as represents" the listed exclusions. This implies that some type of quantifiable "trust law" tracing, attribution or sourcing is required. There is no specific tracing rule or formula provided for in s 99B(2).

"Represent" is not defined for tax purposes. It can be defined as "to stand as an equivalent; correspond to or to act as a substitute or proxy".[32] This means that a direct connection or tracing is allowed, otherwise the provisions may have stated "is" corpus (rather than "represents" corpus).

How exact the sourcing needs to be is unclear (eg to its "origin"), especially where trust funds have been intermingled and reinvested over many years. Again, it may not need to be exact, provided it has been correctly accounted for in the books of the trust (or documented in the trust records).

Although "attributable" is also not defined for tax purposes, it can be defined as "to regard as belonging to, produced by or resulting from"[33] but it seems to require a closer connection.

It is noted that the term "attributable" is used for the corpus reduction and "reasonably attributable" when tracing through a trust for s 98(4) ITAA36 amounts.

Corpus reduction

Represents corpus of the trust estate

"Corpus of the trust estate" is not defined in the Tax Act. Its ordinary meaning is the "capital of a fund, as contrasted with the income".[34] Depending on the terms of the trust deed, it could constitute the initial settled sum, voluntary transfers and income not distributed but accumulated by the trustee.

For the reduction under s 99B(2)(a), it must be capable of being appointed to the capital beneficiaries under the terms of the trust instrument and in conformity with trust law.

Quantifying the amount of corpus and whether "so much of" a distribution is "represented" by corpus might be a system of accounting or bookkeeping, with debits and credits in the books of the trust. This will not always be the case, as not all entries will impact the equity section of the balance sheet (especially under s 99C).

Similar concepts can be found in relation to s 47 ITAA36,[35] where the Archer Brothers principle[36] is relied on to determine the extent to which a liquidator's distributions "represent" income or a loss of paid-up capital (see TD 95/10).

Comparably, the s 6(1) ITAA36 definition of a "dividend" is explicit when it states that an "amount of value debited against an amount standing to the credit of the share capital account of the company" is not a dividend.

The amount of corpus and any subsequent debits would be calculated in foreign currency and only the final assessable amount of the distribution converted to Australian dollars.

Except to the extent to which it is attributable to amounts where otherwise assessable to a hypothetical resident

To avoid foreign trusts accumulating income as trust capital and distributing it as tax-free trust corpus under the above reduction, a "parenthetic exclusion" is provided for amounts which would have been assessable if they had been derived by a hypothetical resident. This includes amounts which are assessable income for tax purposes but capital for trust law purposes (such as a deemed dividend under a share buy-back[37] or a liquidator's distribution under s 47).

In *Howard's* case, there was a chain of trusts and a distribution from the vesting of one trust to another, which was not automatically an amount of corpus. Section 99B was required to be applied at each layer of trust, from the level of the deepest trust and cascaded through successive trusts[38] back up to the original trust (genuine) resident taxpayer.[39]

A hypothetical resident taxpayer

Both *Howard's* case and *Union Fidelity* support a view that the hypothetical taxpayer is not the trustee or the beneficiary[40] but "a" separate, entirely fictional or abstract entity (especially in light of the diverse range of taxpayers and their differences, such as the application of CGT discount, losses etc). That is, ignore the "taxpayer attributes" of both the trustee and the beneficiary.

For income, the Commissioner may "generically" look at whether the income is of "a class" that would "ordinarily" be included in the assessable income of a resident taxpayer.[41] Possibly, this might mean only considering provisions that apply to all taxpayers "generally". For capital gains, the Commissioner takes that view that s 99B should not apply to gains that are disregarded by any resident taxpayer.[42] How far this goes is not known. If an amount of income could only ever be derived by a trustee or an individual and not by a company, the hypothesis must logically assume that it is a natural person taxpayer.

Additionally, in some contexts, it might make sense to consider that "an amount" means a "class" or "type" of income rather than a specific quantity (see later discussion).

Whether the "amount" needs to be calculated in accordance with Australian tax rules is not clear. Section 99B refers to "an amount being derived" and the gross concept of "assessable income", rather than to a "net" amount (although the situation may be different for capital gains, see below).

Practically, for an amount to be paid to a beneficiary, it would be the net (cash) amount after actual expenses and losses[43] that would be available for distribution (ie a reduction to available corpus or debt). However, this would depend on the actual context (eg a payment of net rent to the beneficiary compared to an application of gross rent towards the beneficiary's expenses). Notional expenses might simply mean that there is more cash or corpus available for distribution.

For capital gains, the approach is more interesting. Both s 99B(2)(a) and (b) refer to a hypothetical taxpayer (see below).

Otherwise not assessable income reduction

For amounts which may not be added to corpus, a further reduction is available under s 99B(2)(b) where an amount would have been non-assessable income to a hypothetical resident taxpayer. This could include amounts which result in an accretion to the trust (say, a "reserve") but not assessable income for tax purposes, such as a debt forgiveness amount, the release of an unpaid present entitlement, or the excess of accounting income[44] over net income.[45]

It would also include pre-CGT gains/reserves and, presumably, the cost base amount from a capital gain (noting that s 99B(1) would initially include the entire capital proceeds as assessable income).

Notional accounting income (such as revaluation gains or other unrealised gains), which is not assessable income, may not be represented by cash and therefore not property available to be paid or applied to the beneficiary. Alternatively, a foreign trustee could borrow to fund such amounts, with the funds borrowed similarly representing amounts not otherwise assessable to a hypothetical resident taxpayer.

A hypothetical resident taxpayer: capital gains

It would appear that the hypothetical resident taxpayer approach should allow "asset attributes" when quantifying, calculating or computing capital gains or other amounts for tax purposes (eg capital allowances) in order to quantify the "amount". This would include acquisition dates, proceeds, cost base, pre-CGT status, and so on.

Presumably, this means that the assessable/non-assessable amount is calculated under Australia's tax rules,[46] including the application of the market value substitution rule[47] when calculating the cost base of the asset held by the foreign trustee. Provisions such as those relating to CGT event K6 and Div 149 ITAA97 should similarly also be applied.

> "… s 99B is self-executing. That is, no tax avoidance or tax reduction purpose is necessary for s 99B to operate."

Interestingly, the cost base amount in the calculation of a capital gain would be non-assessable to a resident beneficiary and, therefore, it reduces the assessable amount under s 99B(2)(b). However, if the cost base (ie acquisition of the assets) was funded by accumulated earnings of the trust, this seems to escape the rules.

Current and prior year capital losses are available to taxpayers "generally" when working out their net gain, and therefore the assessable income "amount" under s 102-5.

Section 99B was written prior to the introduction of CGT and never updated. The explanatory memorandum to the 1978 Bill (the 1978 EM) acknowledges that capital gains remain tax-free under s 99B. As such, a gain may retain its pre-CGT status for one asset under s 99B (as an "asset attribute") but would not get the benefits of the non-assessable component of the CGT discount for another asset (as it is a "taxpayer attribute").

Section 95 ITAA36 and Div 855 ITAA97

A further complication arises for current year capital gains of the foreign trust. Ordinarily, where an Australian beneficiary is presently entitled to a trust's capital gain (which is included in its "net income" by way of the residency assumption in s 95(1) ITAA36), s 97 and the CGT rules would operate to allow the CGT discount to the beneficiary.[48]

In the Commissioner's view in TD 2017/23, under the rules of statutory interpretation, where there is conflict between general and specific provisions, the specific provision prevails, that is, s 855-10 ITAA97 prevails over the residency assumption in s 95(1) and non-TAP gains are excluded from the trust net income. Accordingly, such amounts do not flow to the beneficiary under s 115-215 ITAA97[49] (or to the trustee under s 115-220 or 115-222 ITAA97) and are instead included in the beneficiary's assessable income under s 99B without the benefit of the CGT discount or capital losses (see TD 2017/24).

Conduit foreign income flow-through reduction

Non-assessable non-exempt conduit foreign income amounts received by an Australian trust from an Australian company can flow through the trust to a foreign beneficiary tax-free (s 802-17 ITAA97). Therefore, they are excluded from s 99B(1) by s 99B(2).

Conduit foreign income is non-assessable foreign income of an Australian company which is unfranked and declared to be conduit foreign income in the company's distribution statements on or before the day of distribution. It is free of Australian corporate tax and dividend withholding where its final destination (including through a chain of interposed trusts) is a foreign resident beneficiary.

It would seem that a non-portfolio dividend via a foreign trust to an Australian corporate beneficiary may not be caught under s 99B where the conditions in s 768-5(2) ITAA97 are met (see TD 2017/22).

Assessable under ss 97 to 99A reductions

Section 99B(2)(c) is what gives s 99B its residual operation as it carves out amounts dealt with under ss 97, 98 and 98(4) (where there is present entitlement) and ss 99 and 99A (where there is not a present entitlement). This means that where, under the terms of the trust deed, it is possible to create a present entitlement to the annual income of the trust estate (being in the income year it is derived), ss 97 and 98 should take primacy[50] (with the exception of non-TAP capital gains, discussed above).

It is interesting to note that s 99B(2)(c)(i), which deals with s 97 amounts, only requires that the amount "is or has been included" in *the* beneficiary's assessable income, not that the beneficiary has paid tax on it (or that another person has been taxed). However, the requirement under the other subparas in 99B(2)(c) is that the amount "is or has been assessed and liable to pay tax" (by the trustee). This may be relevant where the four-year period of amendment has expired.

Assessable under transferor trust reduction

Where an amount has been included in assessable income under the transferor trust rules, the amount should not be taxed again under s 99B. As such, where the payment or application under s 99B can be sourced back to an amount of “attributable income” assessable to a resident transferor (“attributable taxpayer”), the s 99B amount is reduced accordingly.

Very broadly, a transfer of property or services by an Australian resident (directly or indirectly) to a foreign discretionary trust is generally caught in the transferor trust rules unless it was in the ordinary course of carrying on business and under an arm’s length transaction.

The attributable income of a foreign trust in an unlisted jurisdiction is the trust’s net income and the eligible designated concessional income[51] for a foreign trust in a listed jurisdiction.[52]

It is possible that mismatches could arise between the assessable amount under the transferor trust rules and for s 99B purposes (see later discussion regarding the CGT discount).

Planning considerations under s 99B(2)

There are a number of planning considerations that arise around s 99B(2), as discussed below.

Financial accounts and burden of proof

Sourcing or tracing the payment to tax-free corpus or a non-assessable amount may initially start with a good set of accounts, with appropriate debits and credits and a dissection of the amounts in the equity section.

Some foreign trusts do not maintain financial accounts, so a forensic reconstruction of historical data (if possible) may be required.

Other documents, such as the requirements of the trust deed (including whether the beneficiary can be entitled to corpus) and trustee resolutions, will also be important to support the accounting treatment adopted.

Accounting and trustee requirements in the foreign jurisdiction may also impact the records.

Corroborating verbal evidence by knowledgeable parties could also be helpful in the absence of other or contradictory documents (see *Campbell’s* case). An uncooperative foreign trustee could make things difficult.

If maintained in a foreign language, the information should be translated and maintained in English.

Finally, as a practical matter, where the annual income of the trust has been applied against expenses of the trust and the remaining trust net income has historically been paid to or for the beneficiaries, it may be implied that a residual payment could only have been sourced from corpus.

Migrate the trust to Australia

Migrating the trust to Australia means that each CGT asset of the trust is deemed to be acquired, at that time, for its market value (except for pre-CGT assets and TAP) under s 855-50 ITAA97. As such, s 99B should not apply to the uplift in cost base amount when the assets are realised. The hypothetical resident taxpayer is now an actual resident taxpayer, and the amount when derived is not assessable to that resident taxpayer. That is, the gain is included in the resident trust’s s 95(1) net income and dealt with under ss 97 to 99A and the CGT rules. The CGT discount should similarly be available (with the 12 months starting from the time the trust became resident).

A discrepancy arises here, as the “amount” of capital gain under ss 97 to 99A (and s 102-5 due to the cost base uplift) will be different to the “amount” paid or applied to the resident beneficiary. Therefore, there is still the possibility that any difference in the amounts may be caught by s 99B(1) and not excluded by s 99B(2). In this case, taking a view that it is the “class” (type or character) of income that is relevant (rather than a specific quantum) seems to align the outcome with the purpose of Subdiv 855-B ITAA97.

Of course, the above assumes that the trust is not already a “controlled foreign trust” under s 342(a) ITAA36 which can have broad application and might be a trap if not read closely. This adds further integrity to the rules for inappropriate uplifts in cost base.

A roll-over of the trust assets to a resident company could then also be available under Subdiv 122-A ITAA97.

Finally, the above ignores any foreign exit taxes or ongoing tax implications in the foreign jurisdiction.

Is someone else assessable under the transferor trust rules?

Given the breadth of the transferor trust rules, it is possible that another taxpayer in another income year was assessable on the amount. Under s 99B(2)(d), the amount has to be “included in the assessable income of *any* taxpayer”.[53]

Given the breadth of the transferor trust rules, it is generally more likely that they apply before s 99B.

Unlike s 99B, amounts attributed under the transferor trust rules are eligible for the CGT discount[54] so may provide a more favourable tax outcome.

This assumes that the “amount” referred to in s 99B(2)(d) includes both the gross and discounted portions of a capital gain, which are all factored into the calculation of the final net/discounted “amount” included in the assessable income of the resident transferor under s 102AAZD ITAA36. Otherwise, s 99B would capture any difference in the amounts (being the discounted portion) paid to or applied for the resident transferor or any other resident beneficiary.

Death of transferor

Where a transferor dies, it does not appear that the trust income is attributed to their deceased estate. Section 99B might instead apply to those amounts from such trusts.

Post-marital and family relief foreign trusts

Non-resident family trusts (post-marital and family relief trusts) which are excluded from the transferor trust rules require that the beneficiaries are foreign residents and therefore would fall outside s 99B (which requires a resident beneficiary).

Pre-residency trusts (migrant transferors)

An individual who first became an Australian resident after 12 April 1989 will not be subject to the transferor trust measures if they transferred property or services to a non-resident trust estate before becoming a resident and they were not in a position to control the trust estate. Section 99B might instead apply to those amounts from such trusts.

Offshore estates and testamentary trusts

Transfers from a resident deceased according to the directions in the deceased's will, codicil or court order (but not by testamentary trustee discretion) are excluded from the transferor trust rules (s 102AAL ITAA36). Section 99B might instead apply to those amounts from such trusts.

Foreign deceased estate: distribution of assets existing at date of death

Whether a deceased estate is a foreign trust does not depend on the residency status of the deceased but rather the residency status of the executor(s) or the place of central management and control of the administration.

Theoretically, an Australian resident could create a foreign deceased estate when they die if the executor of their will is overseas, although the usual CGT cost base rules and CGT event K3 should still apply (as relevant).

When a foreign person dies, their assets at the time of death form part of the corpus of the trust at their market value, so cash or assets sourced from these amounts should be tax-free to the Australian beneficiaries,[55] although another view could be that a hypothetical resident would acquire the assets of a foreign resident deceased at their market value (apart from TAP).

For in-specie distributions, the beneficiary should obtain a market value cost base in Australian dollars on the date of death of the deceased, with the acquisition date for the CGT discount backdated to the time the foreign deceased acquired the asset (item 4 of the table in s 115-30(1) ITAA97).

Finally, it does not appear that a tax credit should be available from the payment of foreign inheritance/estate taxes (ss 770-10 and 770-15 ITAA97), although careful reading of any relevant DTA is prudent.

Foreign deceased estate: accumulation during administration

Income or realised gains (in excess of the market value on death) accumulated during the administration period, where a present entitlement cannot yet be created in favour of a beneficiary (see IT 2622), would be assessable to a resident beneficiary under s 99B when later paid.

Modifications may arise for gains on assets such as collectibles, personal-use assets, motor vehicles, trading stock and main residence.

Foreign pension funds: lump sum withdrawal of foreign employment earnings

Where the foreign fund does not meet the definition of "foreign superannuation fund" in s 995-1 ITAA97, a lump sum payment will be dealt with under s 99B[56] rather than Subdiv 305-B ITAA97.

Subdivision 305-B allows a lump sum withdrawal from a foreign superannuation fund to be tax-free[57] within six months of establishing Australian tax residency. After that time, the "applicable fund earnings" are assessable to the individual from the time they became a resident (ie "grandfathered").

Many foreign funds may not qualify for this as they allow withdrawals for purposes other than retirement, invalidity or death (such as education, home ownership, emigration, medical expenses, college tuition, and funeral expenses) and therefore do not meet the "sole purpose test".[58] [59]

Post-tax contributions to the fund would constitute corpus. Earnings on that corpus which are withdrawn as a lump sum would be assessable under s 99B. Deferred pre-tax contributions may not be tax-free corpus.

Roll-overs from one foreign fund to another foreign fund, at the direction of the beneficiary (or as "beneficial owner"), would be applied for the benefit of the beneficiary and therefore caught under s 99B at the time of the roll-over.

The decision to withdraw a lump sum amount may also depend on foreign taxes on withdrawal and any foreign inheritance tax exemptions for foreign domiciled persons.

As a foreign fund is not a "complying superannuation plan", lump sum death benefits paid to a dependent would not be tax-free under Subdiv 302-B ITAA97.

Foreign life insurance, life assurance, insurance bonds and endowment policies

Lump sum payments (including reversionary bonuses)[60] under a foreign life insurance policy,[61] an assurance policy or an insurance bond can be distributions from a foreign trust. Similar rules to the above apply if considering whether the fund is a foreign superannuation fund. Such payments are not ordinary income and are dealt with as statutory income under s 26AH ITAA36 (see IT 2504 and IT 2346), except where the policy was held for more than 10 years.

Sections 118-300 and 118-305 ITAA97 also disregard capital gains or losses made from a CGT event happening in relation to an interest under an insurance policy or a capital amount from a foreign superannuation fund. As these amounts would not be assessable to a hypothetical resident taxpayer, they would be "carved out" of s 99B.

Broadening the net: s 99C

The Asprey report recognised that, in some cases, instead of paying amounts to the beneficiary, the trustee may apply the foreign source income for the benefit of the beneficiary and the application may not give rise to a receipt of an entitlement so as to constitute a derivation of income by the beneficiary.

The 1978 EM (at p 28) explains that:

> "… section 99C is complementary to section 99B and is designed to ensure that a beneficiary will not escape

the provisions of section 99B where indirect or artificial means are used to provide the beneficiary with the benefit of accumulated trust income."

The general rule

Section 99C(1) is the general rule that states:

> **"Determining whether property is applied for benefit of beneficiary**
>
> (1) In determining for the purposes of section 99B whether any amount has been applied for the benefit of a beneficiary of a trust estate, regard shall be had to all benefits that have accrued at any time to the beneficiary (whether or not the beneficiary had rights at law or in equity in or to those benefits) as a result of the derivation of, or in relation to, that amount, irrespective of the nature or form of the benefits."

This rule (or guidance to "determining") is incredibly broad. It appears that a connection is required between the derivation (or sourcing) of an amount and its accrued benefit for a specific identifiable beneficiary.

Section 99C(2) reinforces the general rule above by setting out a number of examples where an amount is deemed to having been applied for the benefit of the beneficiary under s 99C(1).

The Commissioner has observed[62] that s 99C(1) provides that regard should be had to all benefits that have accrued at any time to the beneficiary and therefore the application of an amount in a particular income year is not affected by:

- the passage of time between benefits being provided;
- the provision of different benefits to the beneficiary; and
- whether there is a series of transactions resulting in indirect benefits.

Specific examples

The examples in s 99C(2) are listed as follows:

> "(2) Without limiting the generality of subsection (1), an amount shall be taken, for the purposes of section 99B, to have been applied for the benefit of a beneficiary if:
>
> (a) whether by re-investment, accumulation, capitalization or otherwise, and whether directly or indirectly, the amount has been so dealt with that it will, at a future time, and whether in the form of income or not, enure for the benefit of the beneficiary;
>
> (b) the derivation of the amount has operated to increase the value to the beneficiary of any property or rights of any kind held by or for the benefit of the beneficiary;
>
> (c) the beneficiary has received or become entitled to receive any benefit (including a loan or a repayment, in whole or in part, of a loan, or any other payment of any kind) provided directly or indirectly out of that amount or out of property or money that was available for the purpose by reason of the derivation of the amount;
>
> (d) the beneficiary has power, by means of the exercise by the beneficiary of any power of appointment or revocation or otherwise, to obtain, whether with or without the consent of any other person, the beneficial enjoyment of the amount; or
>
> (e) the beneficiary has directly or indirectly assigned to another person his or her interest in the amount or is able, in any manner whatsoever, and whether directly or indirectly, to control the application of that interest."

The 1978 EM lists the following as examples[63] (or deemed amounts) or descriptions of the nature and form of benefits as having been applied for the benefit of a beneficiary of the trust estate:

- the amount will in any form enure for the beneficiary's benefit;
- the derivation of the amount increases the value of the beneficiary's property;
- the beneficiary receives a loan or other benefit provided out of the amount;
- the beneficiary has power to obtain the beneficial enjoyment of the amount; and
- the beneficiary assigns his interest in the amount or is able to control its application.

Section 99C(2) is explored in the situations below.

Planning considerations under s 99C

What interest does the beneficiary have?

A present entitlement to current year trust income by a resident beneficiary would be dealt with under s 97. Therefore, s 99C is directed at interests which are less than a present entitlement for a resident beneficiary.

Different outcomes may arise if the interest to trust income or capital is vested in possession or vested in interest and whether that interest is defeasible or indefeasible. If the entitlement is contingent or defeasible, it seems unusual to say that the amounts "accrue" or "enure" to a beneficiary.

A purely discretionary object of a trust should not be caught under the general rule merely by the accumulation and reinvestment of income by the foreign trustee.

A trust would be akin to an Australian discretionary trust where, under the deed, there is trustee discretion as to when any payments from the trust fund will be made, how they will be distributed between the named beneficiaries (or class of beneficiaries), and how much the payments will be.

Debt forgiveness and release of unpaid present entitlements

Where a foreign trustee releases a beneficiary from a debt, the forgiven amount may be caught under 99C(2). However, s 99B(2) might operate to reduce the assessable amount as being sourced from either non-assessable trust income or corpus.

Loans, payments, repayments and source of finance

It sounds unusual that a loan might be a "benefit" under s 99C(2)(c) given there is a corresponding obligation by the beneficiary to pay back the funds.[64] Understandably, this would make sense for a "non-genuine"[65] loan that is never intended to be repaid (ie it is in substance a "disguised" trust distribution).

For an interest-free or low interest loan, it might be argued that the "benefit" to the beneficiary is only the interest component and this is the amount that should be caught under s 99C(2). However, there is no such guidance in the provisions or in the 1978 EM, so it appears that the entire loan principal may be assessable.[66]

Even if the loan is on genuine "arm's length" terms, the Commissioner is still of the view that the entire amount of principal is assessable under s 99B.[67] The Commissioner relies on the 1978 EM to support this view (notwithstanding that the 1978 EM also states that s 99C is intended to apply to "indirect or artificial means"). There is merit to the Commissioner's view, as s 99C(2) is worded as a deeming provision (ie "shall be taken").

However, it is difficult to reconcile the concept that an "arm's length dealing"[68] by a trustee with a beneficiary (in a different capacity), where commercial consideration is provided,[69] is being "applied" "for the benefit" of a "beneficiary".

It also seems punitive when compared to s 99B's corporate siblings, in Div 7A and s 47A ITAA36, which at least exclude s 109N complying loans or "arm's length" loans, respectively.

Section 99C(2)(c) also extends to any payments and even repayments of loans owed by the trustee to the beneficiary.[70] As such, loans (or prior trust entitlements[71]) owed to the beneficiary by the foreign trust should be repaid prior to establishing Australian tax residency.

If the loans from the trust are sourced from non-assessable corpus or other debt, a reduction might be available under s 99B(2). However, the ATO takes the view that, once the corpus exception has been claimed for the loan, it is no longer available for other applications under s 99B(1) payments.[72]

This is interesting from an accounting perspective as the accounting entries for advancing and repayment of the loan (Dr Loan Receivable/Cr Cash) would never impact the equity section of the balance sheet. Presumably, under this logic, a repayment of the loan (Dr Cash/Cr Loan Receivable) would "make good" the corpus amount or be treated as a "non-assessable amount".

Finally, this raises some interesting issues in the context of resident trusts, as loans, payments and the satisfaction of trust entitlements would be caught by s 99C. However, a resident trust would be unlikely to have accumulated untaxed earnings and therefore section 99B(2) would apply to reduce the amount assessable to the resident beneficiary.

Back-to-back amounts

Section 99C(2)(c) uses the expression "the beneficiary has received … any benefit[73] (including … any other payment of any kind) … provided *directly or indirectly* out of *that* amount …".

One view is that this expression would trace a loan or payment made from the foreign trust to an interposed foreign beneficiary who on-lends, pays or gifts[74] the amount to an Australian (target) entity (who would also have to be a beneficiary under the trust deed). This makes sense in an artificial arrangement, especially where the foreign trustee is a knowing participant or facilitator of the benefit to the end "target" entity.[75]

Another view might be that it is not a tracing of the recipients, but rather a tracing of the source of the amount (property or money).

Arguably, if the first amount from the trust is *genuinely* applied for the benefit of that beneficiary, the enquiry should end there (in fact, s 99B(1) would catch the payment and s 99C would not be required). If that beneficiary independently chooses to apply those funds for a subsequent purpose (eg for an Australian relative), this should not change the nature of the trust payment.

Foreign gift tax and taxes paid by the foreign beneficiary should be considered.

Beneficial enjoyment of trust property

If the beneficiary "has the power" to obtain the "beneficial enjoyment" of an amount, this could also be caught under s 99C(2)(d). In this example, "amount" presumably refers to the beneficial enjoyment of some trust property or income.

How this amount is quantified or valued in order to be included in the beneficiary's tax return is unclear (ie is it the entire value of the property or just the "annual" enjoyment). The payment of consideration, or offsetting of expenses, does not appear to reduce the "amount" and may even add to the trust's accumulated income.

Assignment of interest in accumulated income of trust

If an Australian resident has an interest in the accumulated income of a trust which they assign to a foreign beneficiary (who would not be caught under s 99B), s 99C(2)(e) would capture it (so could CGT event E8 or A1).

In-specie distributions

In addition to s 99B applying to an in-specie distribution from a foreign trust to a resident beneficiary, CGT events E4 to E8 (and maybe even CGT events A1, C2 and H2) could also apply in relation to the beneficiary's interest in the trust, giving rise to a further (discountable) CGT event.

The anti-overlap rule in s 118-20 ITAA97 should reduce the gain on the basis that, "because of the event" (being the trust payment and its impact on the trust interest), the gain is assessable income under another provision of the Tax Act (ie s 99B).

Throwback interest[76]

To compensate for the deferral of tax on amounts accumulated by a foreign trustee, an amount included in the beneficiary's assessable income under s 99B is subject to an interest charge[77] where the amount was derived from profits in a year where:[78]

- the trust was a resident in a listed country[79] – income was eligible designated concessional income;[80] or
- the trust was a resident in an unlisted country – income was not subject to (full) tax.

Amounts that cannot be proven otherwise are deemed to be eligible designated concessional income (s 102AAM(1A)(a) ITAA36).

The interest accrues on the amount of the s 99B distribution grossed up for any foreign tax credits, under the following formula:

$$\text{Amount on which interest is payable} = (\text{Distributed amount} \times \text{Applicable rate of tax}) - \text{Foreign income tax offset}$$

The applicable tax rate is the general company tax rate (ie not a "base rate entity") in the year of distribution or the maximum marginal tax rate of any other taxpayer.

The interest charge accrues from the start of the year following the income derivation[81] to the end of the income year in which the amount was included in the beneficiary's assessable income.[82] The amount of interest is capped at the after-tax amount of the distribution.[83]

The current interest rate is the general interest charge under s 8AAD of the *Taxation Administration Act 1953* (Cth) (TAA53) less seven percentage points (ie the base interest rate, being the RBA's published 90-day average yield bank accepted bill).

The relevant interest rate depends on the relevant period (see Table 1).

Table 1. Applicable interest rates for s 102AAM

Period	Rate
From 14 September 2006	Rate applying under s 8AAD TAA53
From 1 July 1999 until 14 September 2006	Rate applying under s 214A ITAA36
From 1 July 1994 until 30 June 1999	Rate applying under s 214A ITAA36 less four percentage points
Before 1 July 1994	Rate applying under s 10 of the *Taxation (Interest on Overpayments and Early Payments) Act 1983* (Cth)

Foreign deceased estate: interest charge

Distributions from deceased estates to beneficiaries within three years of death are excluded from the interest charge.[84] It does not appear that a testamentary trust will qualify for this exception.

Deductibility of interest charge

A tax deduction to neutralise the impact of the throwback interest does not appear to be available. Section 8-1 ITAA97 may be of no assistance as the interest was not incurred "in" gaining or producing assessable income.

Section 25-5 ITAA97 for tax-related expenses only provides a deduction for a general interest charge, being a charge worked out under Pt IIA TAA53 (see s 995-1 ITAA97) where the above charge is calculated under s 102AAM (with reference to the general interest charge provisions).

Foreign income tax offsets

Division 770 ITAA97 allows a gross-up and tax credit (up to the foreign income tax offset limit) for foreign taxes appropriately levied and paid on amounts included in assessable income. A DTA may also allow a credit or an exemption.

Section 770-130 ITAA97 deems the taxpayer to have paid an amount of foreign tax "in respect" of a taxed amount that is all or part of an amount included in the taxpayer's ordinary or statutory income where the amount is:

- **paid by another entity under an arrangement with the taxpayer or under the law relating to the foreign income tax:** an arrangement could be an amount paid by the taxpayer's representative, by a partner in a partnership, or a trustee on behalf of a beneficiary or a spouse (apportioned as appropriate). Alternatively, it could be where a foreign law requires payment on your behalf such as deduction or withholding.

  In both cases, it is the taxpayer who bears the economic burden of the foreign tax (ie it is the tax liability of the taxpayer) and a material connection or nexus is required between the amount included in the taxpayer's assessable income and the foreign tax. This is the case for "flow-through" entities (or by election) but not for non-flow through entities, such as a company paying underlying corporate tax in its own right or a foreign pension fund (see TR 2005/3(W)).

  In addition to apportionment, the words "in respect of" allow a slicing of foreign income tax for conduit or flow-through entities such as trusts or partnerships; or
- **paid for the beneficiaries of a trust estate:** where the foreign tax is not paid by the trust itself, the character and source of the income (via s 6B) flows through the trust to the beneficiary. This could be whether the trust income is subject to deduction or tax paid by an earlier trust. For example, withholding taxes by a company on a dividend paid to a trust.

Section 770-190 ITAA97 varies the usual amendment period in s 170 ITAA36 where an "amendment event" occurs in relation to foreign taxes paid.

Foreign income tax offset mismatches

Although conceptually a credit should be allowed for amounts assessable under s 99B, it may be the case that a foreign income tax offset is not available where:

- the trust is not considered flow-through in the foreign jurisdiction and is taxed in its own right;
- the foreign jurisdiction taxes another taxpayer, such as a grantor or another beneficiary;
- a nexus (or evidence) cannot be established between the foreign income and the tax paid;
- it is Australian withholding tax on Australian income taxes to a foreign trustee or beneficiary; or
- the tax is not on income (eg inheritance or gift tax).

In such cases, only tax relief by deduction might be available (ie the net after-tax amount is taxed in Australia).

Other considerations

Section 102

It is not unusual for a foreign trust to be revocable by the person that established it or for it to be established for the purpose of a minor beneficiary. Section 102 ITAA36 gives the Commissioner the power to tax the trustee (and not the beneficiary) on the trust's net income to the extent that it is not included in the "creator's assessable income". This rule excludes foreign income derived during the periods the creator was a foreign resident. Section 99B could capture such amounts later paid to a resident beneficiary (assuming that the person can benefit under the trust deed).

Section 100A

Section 100A ITAA36 does not look at the residency of the trustee or the beneficiary. It is an anti-avoidance provision that *taxes a trustee* under s 99A where a present entitlement arises to a beneficiary but a benefit has been provided to someone other than (or jointly to) the beneficiary.

Section 99B *taxes the beneficiary* where the benefit is actually paid or applied to a resident beneficiary and the amount has not been taxed to the trustee. As such, the two provisions are in some respects inverse.

Section 100A also requires a "tax reduction purpose", whereas s 99B is self-executing. That is, no tax avoidance or tax reduction purpose is necessary for s 99B to operate. Nor is there an exclusion in s 99B for "an arrangement entered into in the course of ordinary family or commercial dealing".

Family trust elections

A foreign trust could make a family trust election, for example, to satisfy the continuity of ownership test of an Australian loss company. Where this arises, the Commissioner can give notice to the foreign trust to collect information about its distributions to both resident and foreign resident beneficiaries.

Conclusion

Section 99B was clearly written for a different time and place. In its historical context, it was meant to apply to Australian residents who benefitted from accumulating tax-free income in a foreign trust. However, its application to resident trusts has not been settled.

The existence of throwback interest implies that the Australian beneficiary had some role to play in accumulating the income offshore.

Section 99B operates without regard to a commercial or family purpose and penalises common, legitimate and, in some cases, even arm's length arrangements of former foreign residents and Australian beneficiaries of overseas relatives. In a today's globalised environment, s 99B seems out of place (an "overreach") and once a person has established tax residency, there may be little that can be done to reverse the impact of it.

Be prepared.

George Psarrakos, CTA
Tax Partner
Mutual Trust

This article is an edited and updated version of "Foreign family offices, trustees and foundations: the scope of s 99B and implications for Australian beneficiaries" presented at The Tax Institute's Local Tax Club Series held in Melbourne on 27 July 2023 and Geelong on 28 July 2023.

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References

1. The trust income could be accumulated and later paid to the Australian beneficiary as a non-assessable amount, such as trust corpus. Former ss 26(b) and 25(1) ITAA36 would capture ordinary income paid to a beneficiary.
2. Commonwealth Taxation Review Committee and Justice K Asprey (Chairman), *Full report*, 31 January 1975, Australian Government Publishing Service, Canberra, 1975.
3. Enacted by the *Income Tax Assessment Amendment Act 1979*.
4. Under s 95A or 101 ITAA36 for discretionary trusts.
5. Also a share of the trust's exempt or non-assessable non-exempt income.
6. Trustee taxation arises for minor beneficiaries ("under a legal disability") and foreign beneficiaries (or foreign trustee beneficiaries) with credit mechanisms for the beneficiary.
7. See later discussion regarding capital gains.

8 Although it can apply to both, the focus of this article is on foreign trusts.

9 [1991] FCA 129.

10 [2012] FCAFC 149.

11 [2019] AATA 2043.

12 Australian Taxation Office, *Receiving payments or assets from foreign trusts*. Available at www.ato.gov.au/General/Trusts/In-detail/Distributions/Receiving-payments-or-assets-from-foreign-trusts/#.

13 M Woodley (ed), *Osborn's concise law dictionary*, 10th edition, Sweet & Maxwell, 2005.

14 See *FCT v Bamford* [2010] HCA 10 and *Zeta Force Pty Ltd v FCT* [1998] FCA 728.

15 See *FCT v Australian Building Systems Pty Ltd (in liq)* [2015] HCA 48.

16 Practically, the "amount" must be quantified so it can be included in the beneficiary's tax return (assessable income).

17 Which, for tax purposes, is usually its ordinary meaning as affected by Subdiv 960-S ITAA 97 (s 995-1 ITAA97). Section 21 ITAA36 may have limited application as a dealing within the context of s 99B is unlikely to involve "consideration". Section 103-5 ITAA97 deals with amounts under the CGT rules.

18 S 960-50(1) ITAA97.

19 Item 4 of the table in s 960-50(6) ITAA97.

20 See *Kafataris v DCT* [2008] FCA 1454 and *Yazbek v FCT* [2013] FCA 39.

21 S 995-1 ITAA97.

22 S 18 ITAA36.

23 For further discussion, see N Brydges, "Australian residents, foreign trusts and foreign funds – the new black!", paper presented at The Tax Institute's Vic 7th Annual Tax Forum on 17 October 2019, including the four elements of a trust (*Harmer v FCT* [1989] FCA 432), *Mulherin v FCT* [2013] FCAFC 115 (Liechtenstein Foundation) and various private rulings.

24 See, for example, PBR 1012616654481.

25 S 102AAU(2) ITAA36.

26 Notwithstanding that the Commissioner expects you to self-assess (see paras 109 and 110 of TR 2023/1).

27 Statutory amounts can be "derived". See *Allen (Trustee), in the matter of Allen's Asphalt Staff Superannuation Fund v FCT* [2011] FCAFC 118 and *SCCASP Holdings Pty Ltd as trustee for the H&R Super Fund v FCT* [2013] FCAFC 45.

28 See *Gibb v FCT* [1966] HCA 74. This means both ordinary and statutory income.

29 Assuming that a trust is a "person" covered by the DTA. Also, the multi-lateral instrument should be considered (eg optional art 3 that deals with transparent entities to access treaty benefits).

30 Noting that some articles look at the "beneficially owner of the income".

31 Item 7 in the table in s 960-50(6) ITAA97.

32 *Collins Australia Dictionary*, 6th concise edition.

33 *Collins Australia Dictionary*, 6th concise edition

34 M Woodley (ed), *Osborn's concise law dictionary*, 10th edition, Sweet & Maxwell, 2005.

35 "to the extent to which [distributions] represent income … replace loss of paid-up share capital".

36 *Archer Bros Pty Ltd v FCT* [1953] HCA 23.

37 *Howard v FCT* [2012] FCAFC 149.

38 Including simple trusts, such as nominee arrangements.

39 A similar approach was taken in the context of a series of s 47 liquidation in *FCT v Brewing Investments Ltd* [2000] FCA 920.

40 Otherwise, it might be argued at the time the amount was assessable to a resident trustee under s 99A and therefore not assessable to the beneficiary.

41 See PBR 1051630967428.

42 See para 21 of TD 2017/24.

43 *Sole Luna Pty Ltd as Trustee for the PA Wade No. 2 Settlement Trust v FCT* [2019] FCA 1195 dealt with the application of the statutory fiction of a foreign trust's "net income" under s 95 (where there were foreign exchange losses) as the first step in ss 97 to 99A (but not s 99B).

44 Which could be affected by the application of certain accounting principles and standards.

45 Noting the ATO's view in IT 2512 that Div 6 ITAA36 (including s 99B) is not an exclusive code for the beneficiaries.

46 See PBR 1051693349071.

47 See PBR 1051970330207 regarding shares under a demutualisation and PBR 1051910296871 for an inherited investment-linked life assurance bond.

48 This seems to still be the case for gains of a foreign trustee which are TAP.

49 This was also identified in para 6.17 of the Board of Taxation's report to the Treasurer on *International Taxation Arrangements* in February 2003.

50 The framework of Div 6 gives priority to s 97 only by reason of s 99B(2)(c)(i).

51 S 317 ITAA36 and reg 17 of the *Income Tax Assessment (1936 Act) Regulation 2015* (Cth).

52 S 320 ITAA36.

53 See ATO ID 2010/211 regarding the amendment period.

54 S 102AAZB ITAA97.

55 See PBR 1051630967428.

56 Assuming that the former foreign investment fund rules did not tax the amount already (s 23AK ITAA36).

57 If the taxpayer chooses, they could contribute the withdrawn amount as a "non-concessional" contribution to an Australian superannuation fund.

58 See *Scott v FCT (No. 2)* (1966) 10 AITR 290, *Mahoney v FCT* (1967) 41 ALJR 232 and *Barker v FCT* [2015] QCA 215.

59 See PBR 1051618374747.

60 S 15-75 ITAA97.

61 See the definition of "life policy" in s 995-1, and s 9 of the *Life Insurance Act 1995* (Cth).

62 See PBR 1052059680727.

63 Modelled on the former s 24H ITAA36.

64 Consider the application of s 59-30 ITAA97 which makes amounts that you must repay non-assessable and non-exempt income. An unlimited amendment period is available in these circumstances under item 22 of the table in s 170(10AA) ITAA36.

65 This is a colloquial term. For ATO guidance on evidencing "genuine loans", see www.ato.gov.au/Business/Privately-owned-and-wealthy-groups/Tax-governance/Tax-governance-guide-for-privately-owned-groups/Gifts-or-loans-from-related-overseas-entities/#.

66 See PBR 1051830400148.

67 See PBR 1052059680727.

68 Possibly excluded under the transferor trust rules.

69 In the event that the supply was connected with the indirect tax zone (eg goods imported on a non-free on board basis), it may be in the course of furtherance of an enterprise (see GSTD 2009/1).

70 Although a forgiveness of the loan by the beneficiary could be later paid out as a non-assessable amount

71 See ATO ID 2004/66.

72 See PBR 1052059680727.

73 Benefits from a trustee to a beneficiary would be non-assessable non-exempt income if they are fringe benefits under s 23L ITAA36.

74 For ATO guidance on evidencing "genuine gifts", see www.ato.gov.au/Business/Privately-owned-and-wealthy-groups/Tax-governance/Tax-governance-guide-for-privately-owned-groups/Gifts-or-loans-from-related-overseas-entities/#.

75 How far a tracing exercise should go to the "end" recipient is unclear. Presumably, some causal nexus is required rather than a mere remote connection.

76 Parts of this section of the article have been loosely adapted from ATO, *Foreign income return form guide 2021*, pt 2, s 2. Available at www.ato.gov.au/law/view/document?DocID=SAV%2FFIRFG%2F00003.

77 As individuals are not full self-assessment taxpayers (see ss 6(1) and 161AA ITAA36), it is the Commissioner that "must" make the assessment for the interest payable.

78 Theoretically, this could also apply to a resident trust which was previously a foreign resident.

79 S 320 ITAA36.

80 S 317 ITAA36 and reg 17 of the *Income Tax Assessment (1936 Act) Regulation 2015* (Cth).

81 Or from the 1990–91 income year for amounts accumulated before then.

82 Where the beneficiary first became a resident after the 1990–91 income year, the accrual seems to start from the next income year after establishing residency (s 102AAM(5) ITAA36).

83 S 102AAM ITAA36.

84 S 102AAM(1C) ITAA36.

Self-coaching your way to bust your busyness

by Karen Stein, Professional Certified Executive Coach

Being busy has become the workplace norm. It is too often the response to how people describe themselves. Yet it is also too often accepted as being an accepted state which has to be endured. By drawing your attention to the consequences and unintended consequences of being busy, it becomes easier to contemplate the importance of better managing your time. There are a number of strategies which can be adopted to support you in busting your busy ways, so that you are more mindful and enabled to respond to how you use your time. This article provides a number of self-coaching strategies in support to better lead your way.

As lodgment deadlines closed in, Nathan's workday became longer. He found himself working 12 to 14-hour days. This seemed only a small stretch from his usually busy days of late. His diary was filled with back-to-back meetings and his desk was heaving with files and worksheets. Nathan prided himself on juggling numerous priorities and delivering high-quality outputs, yet he noticed his mental load and energy consumption increasing as he tried to maintain his planful approach to work. He also found things were taking longer than usual.

Nathan described himself as "busy"! In fact, he was so busy that Nathan rarely got to do the things that were most important to him – ideating and innovating, investing in stronger client relationships, and building the skills of his team.

His colleagues heard this in his language as he referred to himself as stretched, time-poor, swamped, hectic, at capacity, and neck-deep in all that he had to get done. His physical state mirrored this, with Nathan looking tired, overwhelmed and stressed. He had bypassed his exercise routine and healthy eating, and was spiking his energy with snacks, coffee and takeaways.

Nathan was reluctant to ask for help, as he prided himself on always being in-service to his clients. Yet, what Nathan overlooked were the consequences and unintended consequences of his busy ways of working.

Consequences of being busy

Limited perspective

When you, like Nathan, always find yourself being busy, it is common to approach your work holding a limited perspective. Due to your hectic schedule, you may be likely to make assumptions as there is no time to fact-check. Miscommunications and misunderstandings may result, furthering the time required to complete tasks. Data may be incorrectly interpreted as you rush through your work and mistakes can arise. You may find yourself spending more time correcting work, or restating positions with correct data, which could have been avoided had you slowed down and made further inquiries at the outset. Your busy working style may disrupt your quest to consistently deliver work of a high quality.

Time management and productivity

Being busy often involves a significant amount of multi-tasking, where you jump from one task or engagement to another. Many confuse this level of activity with productivity. And often, the busier you are, the busier you get as you try to do more in response to what you have committed to.

Yet research tells us that performance is actually lessened when you are multi-tasking compared to when you complete tasks sequentially. Increased multi-tasking also leads to a significant decrease in accuracy, which can negatively impact your performance. When your performance is of lesser quality and efficiency, the cost of completing your work increases. Your return on investment is diminished and your ability to recover these extra costs is unlikely. Your own physical and emotional cost of investment is also extended with the stress and frustration associated with this way of working.

Burnout

Juggling so many priorities requires tremendous personal resources. The hours you commit to work can become hazardous and disconnected from your wellbeing. The pace of being busy in the workplace leaves little time for much else. Your threading of meetings back-to-back removes the space required to pause, reset and replenish. As a result, stress levels and anxiety can increase. Your feelings of being overwhelmed can build, and your emotional resources may become depleted in support of your best self. Burnout sits close by. Burnout is a reaction to prolonged or chronic stress that can lead to exhaustion and other mental and physical reactions.

Unintended consequences of being busy

As well as the more obvious consequences of being busy, there are a number of unintended consequences which are often overlooked, until they play out.

Team engagement

As in Nathan's case, when you are too busy to share the workload or seek support, you can unintentionally have a negative leadership impact on the team. Being too busy to delegate to or empower your team members creates feelings within the team of frustration, of not mattering, or of feeling untrusted or of little value. The disconnect which arises leads to disengagement and low morale, which can lower retention. Team culture can be impacted, and when you finally reach out to seek support or engage with your team, it may be too little, too late.

Poor collaboration

It is very easy to get on with things and do it your way when you are busy, just as Nathan does. After all, there is no time to stop and consult with others! Yet, adopting this perspective has unintended consequences. Your connection with others is reduced and it may be that you are overlooked for opportunities which could be of great interest to you. Your network may make assumptions that you are unavailable or disinterested in participating, given your lesser presence. Your disconnected state may create a lesser number of people willing to make themselves available for you when you finally reach out for help, leaving you having to do more yourself in an isolated manner.

You stop learning and growing

When you are so busy, you will be unlikely to find time to experiment, learn and develop. Your attention to your behaviours, emotions and cognitions will likely be lessened as you deprioritise time for self-reflection and self-coaching. You will be more likely to adopt the status quo without question, which may reduce efficiencies, creativity and innovation. You will be unlikely to try something new with a growth mindset, given your focus on being so busy – you just want to get things done! This may inhibit your professional development and growth.

No time for the things which matter

If, like Nathan, you just keep working and pushing through, you may soon lose time for what really matters to you. You may just keep doing things which are not meaningful or of value. Your impact may lessen.

Nathan found the consideration of his busy state useful, yet he wondered how to respond. The following strategies were shared with Nathan, which you too may apply to alter your busy state.

Self-coaching in support of busting your busy state

Apply the brakes

The first step is to become mindful of what is currently on your plate. As hard and uncomfortable as it may feel to slow down for a moment, take a step to pause to assess your priorities and determine what you can say no to, or share with others. Think of it as a personal time audit. What can you identify in the patterns of the use of your time? What does the data tell you?

List your current workload and pressing priorities and empty them into three buckets: those activities which are most purposeful; those which you must do and cannot delegate to others; and those which can be passed on to your team (see Diagram 1).

By understanding how you are using your time, you can make informed decisions to lead yourself and others more efficiently. You can recognise what will energise, motivate and engage you. You can identify what will be better placed with someone else, and you can consider how efficiently you can do those things which you simply need to tolerate.

Completing this assessment each week can help you to visualise how you are using your time and will support your choices to free up your time and engage in more purposeful activities. It can assist you in establishing what is keeping you busy and whether this is helping or hindering you on your way towards the completion of your goals.

Empower your team

Now that you have classified your current workload, draw your attention to your team, and involve them where you can. Notice your reluctance to delegate and to address the many reasons which have prevented you to date, such as:

- "It will be faster if I do it myself" – while this may be true for the moment, recognise the never-ending cycle of your increased workload if you do not challenge your mindset. How will you further develop and empower your team if you don't allow them the opportunity to engage and learn through your delegation?

Diagram 1. Mindful assessment of how you use your time

Most purposeful	Must do	Pass on
This is your most productive zone and where you will benefit from focusing. Devoting a large amount of time to purposeful goals and tasks leads to your highest motivation, engagement, energy, flow and optimism. These are the goals and tasks you are likely to be most excited about. They matter most to you and provide you with the most fulfilment and meaning.	These are the goals and tasks that need to be completed as part of your role, but that don't align so closely with your purpose. You will have a lower level of motivation and engagement with these goals and tasks. They do however absorb your time, which may take your focus away from your purposeful goals and tasks. How can you work through what can't be delegated quickly and efficiently? What can be done to reframe the goals to align them with your purpose?	This is your least productive zone. These are the things you can more readily delegate, so you can regain your focus elsewhere. Identify who else might be motivated to undertake these goals and tasks. This may in fact align with someone else's purpose, so you may be empowering them through delegation. How can you delegate, expand resources or reprioritise to allow you to focus on more purposeful goals and tasks?

- "I'm too busy to delegate" – and you always will be if you don't pause and delegate. With some discipline, the time you need to allocate to effective delegation will win you back additional time to devote to other priorities.
- "My team is too busy to delegate to" – they may well be busy but be careful about making decisions based on this assumption. People are motivated by different factors. Some may be motivated to engage in the task and be able to make room or use discretionary time to assist. They may find efficiencies elsewhere to benefit from this opportunity to learn and grow. Allow them the chance to assess this possibility, rather than assuming from the outset that they can't.

Improve the governance of your use of time

Set your boundaries around how you use your time. Reflect on the table you have populated above to note what is most purposeful to you. Dial up your curiosity to consider whether what is being asked of you is best suited to you or another colleague.

Recognise the boundaries which you need to set in sharing your time with work and other parts of your life. When you are continuously agreeable to taking on more work and opportunities, notice what you are giving up in response. Rather than overfilling your cup, be intentional about what you can say no to, postpone, reschedule or reassign, to make space in your cup for these additional opportunities.

You may often have greater ability to negotiate deadlines, schedules and team composition than you first realise. Pausing to consider your options and boundaries can assist with the governance of your time.

With some discipline and the adoption of your self-coaching practices, you can improve your engagement, motivation and leadership impact. This will improve your wellbeing and move you away from an uncomfortably busy state to one which is more meaningful and productive.

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A Matter of Trusts

by Will Monotti, Sladen Legal

Lost trust deeds: consequences for trustees

A decision of the Supreme Court of Victoria, in which it was held that a discretionary trust had failed for uncertainty on the basis of its deed being lost, has been overturned.

In the November 2022 issue of *Taxation in Australia*,[1] this column discussed *Mantovani v Vanta Pty Ltd (No. 2)*,[2] a Victorian Supreme Court case which concerned a trust that was being administered despite its deed being lost. Since that article, the Victorian Supreme Court of Appeal has handed down its decision on this matter. The Court of Appeal's decision provides further clarification to trustees facing the issue of a lost deed, and whether a lost deed could result in the trust failing for uncertainty.

The trial decision

A detailed summary of the judgment of McMillan J is set out in the November 2022 article.[1] In brief, the decision related to the Mantovani Family Trust (the trust), a trust established by deed dated 27 July 1976.

The trust's assets included several parcels of real estate located in regional Victoria. This real estate was transferred to the trust by Teresa Mantovani. The directors of the company acting as trustee of the trust were two of Teresa's children, Rocky and Nic Mantovani. The trustee had made distributions from the trust over many years exclusively to Rocky and Nic.

After Teresa's death, the executors of her estate informed another child of Teresa, Giovanni (also known as John), that a property owned by Teresa and occupied by him needed to be sold to enable Teresa's estate to cover its debts. A dispute arose, and during that dispute, John asked to be provided with documentation relating to the trust. It thereafter emerged that the trust deed had been lost, with the only page to have survived being its schedule page. This schedule page listed the name of the trust, the date of its establishment, its settlor, trustee, settled sum, appointor, and beneficiaries, which included, among others, the four children of Teresa.

The matter was brought before McMillan J in the Victorian Supreme Court. Her Honour applied a six-step test in her reasoning, and concluded that the trust had been administered for some time on the basis of mere "guesswork" by the trustee and had failed for uncertainty. Further, McMillan J determined that it was Teresa's estate in which the assets of the trust were to be vested.

The appeal

McMillan J's decision was appealed to the Victorian Supreme Court of Appeal.[3] The three grounds of appeal were:

1. whether the determination that the trust had failed by reason of uncertainty, because its deed had been lost, was in error;
2. whether the determination that the loss of the trust's deed had created a resulting trust was in error; and
3. whether the determination that the trustee of the trust take account and make payment to Teresa's estate was in error.

In its judgment, the Court of Appeal offered further analysis of decisions that were referenced in the trial judgment, including the 1986 NSW case of *Maks v Maks*,[4] and an observation that was made as obiter dicta by McDonald J in the 2019 Victorian case of *Yap v Lee*.[5] These decisions had suggested to McMillan J that, in relation to the evidentiary requirements for certainty, there was a requirement for:[6]

> "… 'clear and convincing proof' of not only the existence, but also the contents of the original document, in the same order as the proof required to establish an entitlement to rectification of a written instrument."

The Court of Appeal examined the provisions of the NSW *Evidence Act 1995*, introduced following the *Maks v Maks* decision. The relevant provisions of this legislation are similarly worded in the corresponding Victorian *Evidence Act 2008*. This legislation does not, in fact, require the application of a "clear and convincing proof" test, but instead provides that, in civil proceedings, a court must find the case of a party proved "if it is satisfied that the case has been proved on the balance of probabilities".[7]

When it came to the determination as to whether the trust was valid and subsisting, the Court of Appeal went back to the most straightforward of trust principles and looked at the "three certainties" test, which confirms that a trust's existence can be determined if there is certainty of intention, subject matter and object. In this case, the Court of Appeal determined that the trust did meet these three certainties, given that:[8]

- the schedule page to the trust deed was available, and this schedule page set out an ascertainable and defined class of beneficiaries;
- there were trust records available, including financial reports, tax reports and records of distributions; and
- the evidence presented indicated the settlor's intention to establish a discretionary trust for the beneficiaries named in the schedule, and Teresa's intention, when transferring the properties that she owned to the company acting as trustee of the trust, that those properties would become assets of the trust.

In effect, the Court of Appeal's conclusion was that the wrong test had been applied by McMillan J and that, with the correct test applied, it could be determined on the balance of probabilities that a trust existed, notwithstanding that the deed had been lost and its terms could not be precisely ascertained.

The Court of Appeal held that to take the step of annulling the trust on the grounds of uncertainty would, rather obviously, result in significant implications for the trust and its beneficiaries. It noted that the Supreme Court had scope to "fill the gap" in instances where there was uncertainty as to the non-essential terms of the trust,[9] and confirmed that:

> "116. … it has been and remains open to Vanta to apply to the Court for judicial guidance as to the administration of the trust notwithstanding the loss of the Deed."

The applicants to the proceeding gave an undertaking that, if the appeal were allowed, they would make application to the Supreme Court for orders as to the effective administration of the trust, pursuant to its rules and s 63 of the *Trustee Act 1958* (Vic), within two months of the issue of the Court of Appeal's decision.[10]

Given that the trust had not failed for uncertainty, it was not necessary for the applicants to make out the additional grounds. However, the Court of Appeal did address those grounds and held that the remedy of the resulting trust should not have been applied, even if the trust had failed. Notwithstanding that Teresa had transferred properties into the trust, she had done so for consideration, with Teresa credited as having a loan account in the books of the trust accordingly. She had not created a settlement by doing so, and so there was no trust that resulted to her on the purported failure of the trust. The Court of Appeal noted:

> "144. There has been no suggestion that the Trust was ineffective or inoperative or had failed at the outset. Accordingly, the former ownership of the properties by Teresa is purely historical and of no relevance following the proper completion of the transaction just described. The notion that something did happen automatically, albeit with retrospective recognition, is entirely inapt. The nature and manner of implementation of the transfers effectively forecloses any notion that, close to half a century later, the events may be retroactively reconfigured to achieve a result that was not only unintended, but is the opposite of what was intended and satisfactorily implemented. The use and enjoyment of the properties by the Trust was clearly intended and that intention was realised."

Given that there was no resulting trust, the Court of Appeal determined that the order for the taking of accounts fell away.

Conclusion

Although the trust in this matter was not found to have failed for uncertainty, the trustee was ordered to seek urgent judicial directions as to its administration, and the Court of Appeal noted that the trustee should have taken these steps some time ago.[11] The decision therefore does provide some relief to the trustees of privately managed trusts in that it confirms that a trust will not necessarily fail if a deed cannot be found. But the decision should not be read as one providing exoneration to trustees from storing trust documents safely and from maintaining trust records. A beneficiary can, at any time, see certain records of the trust on making a request to the trustee, and a trustee should always be ready to answer any such request.

As to the matter of the administration of this particular trust, the Court of Appeal noted that it remained open to John to take whatever steps he deemed appropriate in relation to the actions of the trustee and its directors, including in relation to distributions of trust income. No doubt John and his advisers have been closely reading the Court of Appeal's decision in *Owies*[12] in this regard.

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References

1 W Monotti, "Lost trust deeds", (2022) 57(5) *Taxation in Australia* 283. Available at www.taxinstitute.com.au/resources/journals/taxation-in-australia/2022/a-matter-of-trusts-lost-trust-deeds.

2 [2021] VSC 771.

3 *Vanta Pty Ltd v Mantovani* [2023] VSCA 53.

4 (1986) 6 NSWLR 34.

5 [2019] VSC 743.

6 [2021] VSC 771 at [62].

7 See s 140 of the *Evidence Act 2008* (Vic), as cited in *Vanta Pty Ltd v Mantovani* [2023] VSCA 53 at [68]. A similar provision is included at s 140 of the *Evidence Act 1995* (NSW).

8 [2023] VSCA 53 at [103]–[108].

9 [2023] VSCA 53 at [114].

10 [2023] VSCA 53 at [117].

11 [2023] VSCA 53 at [155].

12 *Owies v JJE Nominees Pty Ltd* [2022] VSCA 142.

Superannuation

by Daniel Butler, CTA, and
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Transfer duty on property investments

Landholder duty may arise where a significant interest is acquired when aggregated with other interests in the landholder by any other person in an "associated transaction".

Overview

Structuring property investments via a company or unit trust may give rise to landholder duty for non-related investors, as highlighted in *Oliver Hume Property Funds (Broad Gully Rd) Diamond Creek Pty Ltd v Commissioner of State Revenue (Review and Regulation)*.[1]

This decision resulted in an additional $151,235 of duty plus interest and penalties payable to the Victorian State Revenue Office (SRO) given the unity of purpose of the 18 unrelated investors undertaking a specific development that constituted an "associated transaction" for the purposes of the *Duties Act 2000* (Vic) (the Duties Act).

Facts

The Oliver Hume Property Funds Group formed a special purpose entity known as Diamond Creek Pty Ltd (Diamond Creek) to purchase land in outer Melbourne, with the objective of developing the site for investment returns.

An information memorandum was distributed to sophisticated investors under s 708(8) of the *Corporations Act 2001* (Cth) to raise capital through the issuing of shares. The information memorandum stated at para 5.3 under a heading of "General Risk Factors":

> "Provided the only dutiable property held by the Company is the Land, the acquisition of Shares by Applicants under this Offer will not attract Victorian transfer duty, unless the landholder duty provisions apply (generally, if the shareholder, or two or more associated shareholders acquire 50% or more shares of the Company)."

On 2 July 2014, $1.8m was raised in the form of 1.8 million shares acquired by 18 investors. Fourteen of these were existing investors from an investment database, two were referred by a consultant, and two were unrelated to the others. A number of SMSF investors were involved. No duty was accessed or paid at the time these investors subscribed for shares.

On 28 February 2019, the SRO informed Diamond Creek that the acquisition of shares in the company had formed substantially one arrangement, one transaction or one series of transactions triggering an assessment of landholder duty.

On 1 July 2020, the SRO issued a notice of assessment in the sum of $168,162.67, including penalty tax and interest.

Landholder duty

In Victoria, where a person or an entity acquires a "significant interest" in a landholder with a total unencumbered land value (ie ignoring any debt, mortgage, etc) of over $1m, a liability to pay duty may arise under s 77 of the Duties Act.

The threshold for a significant interest is 20% for a unit trust scheme and a 50% for a company, as referenced in the information memorandum to the shareholders.

Relevantly in this decision, landholder duty may also arise where a significant interest is acquired when aggregated with other interests in the landholder by any other person in an "associated transaction" (s 78(1)(a)(ii)(C) of the Duties Act).

An "associated transaction" includes where the acquisitions form substantially one arrangement, one transaction or one series of transactions (see the definition in s 3 of the Duties Act).

Decision

Although each individual shareholder was below the threshold for an individual significant interest, the tribunal upheld the Commissioner's assessment that, when aggregated, the share acquisition by the 18 investors formed substantially one arrangement.

The decision noted that an arrangement may be unilateral and that whether a number of acquisitions constituted an arrangement is determined by the actions and motives of the transferor and transferees. When analysing the motives of each party to the transaction, Macnamara J found that there was:

- a clear "unity of purpose" between the investors to become shareholders in Diamond Creek, despite not being acquainted with one another;
- a clear "unity of purpose" from Diamond Creek to enlist shareholders to carry out a development project; and
- a "oneness of purpose" between the investors and Diamond Creek.

This unity of purpose amounted to the 18 unrelated investors forming substantially one arrangement when purchasing shares in Diamond Creek, triggering the landholder duty provisions of the Duties Act.

Revenue Ruling DA 057

The tribunal also found it necessary to address a revenue ruling by the SRO on associated transactions and landholder duty. In Revenue Ruling DA 057, the Commissioner stated:

> "While the term 'associated transaction' is broadly defined in section 3(1) of the Act, the Commissioner has taken the position that he will not regard acquisitions of interests by independent members of the public as an associated transaction if the acquisitions are made in response to a genuine public offer under a product disclosure statement or prospectus lodged with the Australian Securities and Investments Commission."

In this instance, a product disclosure statement or prospectus was not lodged with ASIC. Nonetheless, the tribunal conceded that, subject to restrictions, the information memorandum and share offer could be regarded as an offer to the public at large. However, the tribunal noted that the Commissioner's ruling did not have the force of law (as noted in the ruling itself) and that no provision authorises the Commissioner to offer this concession.

Conclusion

Potential investors must be aware that investments in a company or unit trust that include land or dutiable property may give rise to an extra layer of duty if there is a unity of purpose that results in "associated transaction" with other investors.

It should be noted that most Australian states/territories have some form of landholder duty regime but each with their peculiar differences. Thus, advice should be obtained from a lawyer who is an expert in this area in the particular jurisdiction.

As SMSFs are often investing in companies or unit trusts to acquire and possibly to improve or develop property, SMSF trustees should ensure that, prior to entering such arrangements, they obtain advice from an SMSF and tax perspective, including state/territory taxes. Note that state/territory tax advice may constitute legal advice and non-legally qualified advisers should be mindful of their professional limitations.[2]

Reliance on concessions made in SRO revenue rulings should be exercised with caution as they do not have the force of law.

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References

1 [2023] VCAT 634.

2 See, for example, *Galea v Camilleri; The Estate of Patricia Camilleri* [2023] NSWSC 206.

Events Calendar

Upcoming months

OCTOBER
11–12
Wed–Thu

QLD

Death & Taxes Conference

12 CPD hours

OCTOBER
18–19
Wed–Thu

NSW

National Transfer Pricing Conference

13 CPD hours

OCTOBER
19–20
Thu–Fri

TAS

Tasmanian Convention

12 CPD hours

OCTOBER
25–26
Wed–Thu

NSW

National GST Conference

13 CPD hours

NOVEMBER
1
Wed

Online

Property Intensive

6 CPD hours

NOVEMBER
1–2
Wed–Thu

VIC

National Superannuation Conference

12 CPD hours

For more information on upcoming events, visit taxinstitute.com.au/events.

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