Volume 57(8)
March 2023

The Tax Institute

Taxation *in* Australia

Section 100A: yea or nay?
Elizabeth Allen and John Ioannou, CTA

The life cycle of a tax dispute with the ATO
Adam Ahmed

Hybrid mismatch rules: practical considerations
Ramy Singh, CTA

Contents

Cover article

Feature articles

Invitation to write

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

For details about submitting articles, please see Guidelines for Publication on our website taxinstitute.com.au, or contact publisher@taxinstitute.com.au.

Insights from the Institute

Regular columns

Tax News – at a glance

by TaxCounsel Pty Ltd

February – what happened in tax?

The following points highlight important federal tax developments that occurred during February 2023. A selection of the developments is considered in more detail in the "Tax News – the details" column on page 440 (at the item number indicated).

DGR registers reform

The Treasurer has released exposure draft legislation (and explanatory material) that would transfer to the ATO the administration of four unique deductible gift recipient categories that are currently administered by other government agencies. **See item 1.**

Superannuation funds: non-arm's length expense rules

The government has released a consultation paper which considers options to amend the non-arm's length income provisions which apply to superannuation funds. **See item 2.**

Accessing company profits tax-free

The Commissioner has released a taxpayer alert in relation to arrangements where an individual accesses the profits of a private company in tax-free form (that is, without an additional tax liability for the individual) by arranging for the profits to be passed to the individual through an interposed holding company (TA 2023/1). **See item 3.**

Advice under development

The Commissioner has recently released an update of the advice that is currently being worked on by the ATO. **See item 4.**

Discretionary trust: reimbursement agreements and Pt IVA

In a recent decision, the Full Federal Court (Perry, Derrington and Hespe JJ) has unanimously affirmed a decision of Logan J at first instance that the reimbursement agreement provision in Div 6 of the *Income Tax Assessment Act 1936* (Cth) (ITAA36) (s 100A) had no application in the circumstances, but reversed the decision of Logan J as to the operation of the general anti-avoidance provisions of Pt IVA ITAA36 in relation to one of the income years in question (*FCT v Guardian AIT Pty Ltd ATF Australian Investment Trust* [2023] FCAFC 3). **See item 5.**

AAT: jurisdiction issue

The AAT has held that it did not have jurisdiction to review a decision made by the Commissioner to refuse the taxpayer's request to remit a shortfall interest charge totalling $17,901.55 which related to income tax assessments for the 2017 and 2018 income years (*Dermatis and FCT* [2023] AATA 13). **See item 6.**

Consultation into the objective of superannuation

In a joint media release on 20 February 2023, the Treasurer and the Minister for Financial Services announced the release of a consultation paper that seeks feedback about the benefits, phrasing and implementation of an objective for superannuation. Legislating an objective for superannuation is intended to instil a greater confidence in the superannuation system.

Amending TPB legislation

Amending legislation has been introduced into parliament which, when enacted, will give effect to various recommendations of the final report of the independent review into the effectiveness of the Tax Practitioners Board (TPB) and the *Tax Agent Services Act 2009* (Cth). The recommendations include: the strengthening of the disclosure requirements to require tax practitioners to not employ or use disqualified entities in the provision of tax agent services without approval from the TPB; and converting the three-year registration cycle to annual registration.

The amendments relating to the employment or use of disqualified entities are considered in the Tax Tips column of this issue of the journal (see page 445).

President's Report

by Marg Marshall, CTA

Advocating for our tax system

The Federal Budget presents a major opportunity to have our voice heard on the tax policy matters that affect our members.

At The Tax Institute, we wear a few different hats according to what support our members need. We are educators, event planners, bridge-builders, cheerleaders, and much more. Our advocacy work as representatives of our community is a vital part of what we do. It's driven both by our Tax Policy and Advocacy team and by our volunteer committee members who generously give their time and expertise in a range of specialties.

It's through our advocacy work that we are able to represent your best interests on the public stage, taking your concerns and needs to the regulators and policymakers who can enact change. We have fostered relationships with various government and regulatory bodies in order to have this significant voice in our tax ecosystem. It's so important that, as the major member organisation for tax practitioners, we are part of the development of policy within our tax and transfer systems.

The Federal Budget is an important opportunity for government to demonstrate its priorities and vision for the future of our economy. This year, as in recent years, it is vital that our tax policies allow for certainty when people are making decisions that support and grow their businesses and livelihoods. I have first-hand experience with how important a sense of certainty around tax matters can be for SME clients in particular.

Last month, our team released the Federal Budget 2023–24 submission, outlining our priorities for the upcoming Budget. We worked closely with our national technical committees to develop a submission that includes the most pressing issues facing our members from all sectors of the tax profession.

Some of the issues raised include:

- **Non-arm's length income provisions for superannuation funds:** this ongoing issue has been much discussed at the Institute and among our members. While we welcome the announced consultation on the non-arm's length expense rules for superannuation funds, the issues facing practitioners and their clients are broader than what the proposed consultation covers. Further solutions must be sought;
- **Div 7A reform:** another favourite topic of conversation, Div 7A is a source of significant complexity and compliance costs. While some action has been announced – and consequently deferred – further detailed consultation with the tax community and legislation in this area are needed;
- **Simplification of fringe benefits tax:** FBT is another area of tax law that suffers from complexity and creates a significant cost burden for taxpayers. The Tax Institute's view has long been that the current FBT regime should be abolished and replaced with an approach that more efficiently and fairly meets its policy objectives; and
- **Establishing a pathway to reform:** last, but certainly not least, we have reiterated our view that comprehensive and meaningful reform is vital for Australia's tax and superannuation systems. A good tax system is simple, equitable and efficient. It's the basis on which we can grow economically and socially. This next Budget announcement is a perfect opportunity to announce a vision for reform.

The Federal Budget is still some time away and will likely be announced in early May. As always, our team will be on hand to support you with resources and analysis of the tax measures announced.

Dr Ken Henry at the Financial Services Conference

On the topic of the tax and transfer system and opportunity for reform, I am very excited that Dr Ken Henry, who has chaired multiple tax reviews and was instrumental in bringing us the *Australia's Future Tax System Review*, known as the Henry review, will be joining us later this month at the Financial Services Conference.

Dr Henry's work informs a lot of current thought around our tax system and potential reform opportunities. At the event, he will be discussing whether now, in the midst of significant economic and social change, is the time for real and genuine tax reform in Australia.

It is sure to be an enlightening session and I hope you will all be coming along.

CEO's Report

by Giles Hurst

Your place in the Institute

A career with purpose is about being part of successes bigger than your own – the Institute gives you those opportunities.

Henry Ford once said that coming together is a beginning, staying together is progress, and working together is success. Forging a career with purpose often means more than just doing good work – it means being involved in successes bigger than your own and connecting with others who share your passions.

The Tax Institute has a proud 80-year history of bringing together the best and brightest of the tax profession. We are a vibrant, connected community, and a thriving volunteer force fuels some of our best work. We're proud to offer our members opportunities to build their careers, whether by making connections with other practitioners throughout the profession, or by developing experience that can help them take the next big step.

As 2023 truly gets underway, I'd like to take a moment to remind you of some of the ways you can be involved in working together with fellow members. While you may immediately think of our various committees as the main way to contribute, there are plenty of other avenues for those who are unable to devote time to committee work or who simply prefer to take part in other ways. A few of these opportunities are discussed below.

Engage in professional development events

When it comes to collaboration, nothing beats the value of getting into a room with other tax practitioners. We have an exciting line-up of CPD events planned throughout the year for you to throw yourself into.

If you'd like to be involved in an official capacity, you can join an event organising committee or sign up as a speaker in your area of expertise. Outside of that, I would encourage you to be involved by attending and actively engaging in CPD events that interest you. Many wonderful career moves and professional connections have been forged through enthusiastic participation in a conference or discussion group.

Write for our journals

Our members are some of the most talented tax practitioners working today. Sharing your insight and analysis not only benefits your fellow practitioners, but also helps to build your profile and career. Contributing your ideas in a public forum, like our journals, is also a useful avenue for feedback and collaboration.

As you no doubt know, we publish three academic journals with differing purposes: *The Tax Specialist*, *Australian Tax Forum* and, of course, *Taxation in Australia*. We welcome your submission to any of these.

Write for the TaxVine newsletter

Our *TaxVine* newsletter reaches thousands of members each week and includes the latest in tax news. We welcome feature articles authored by experienced members on trending issues or topics.

If your ideas aren't suited to the style or schedule of our journals, contributing to *TaxVine* is another way to share them with fellow members and start a dialogue. This collaborative spirit is fundamental to who we are as an organisation, and we are keen to facilitate these conversations among members.

Lend your expertise to topical resources

We regularly publish articles and other resources on our website, including both thought leadership and topical issues, to help members stay abreast of the latest developments from around the tax space. While most of these resources are produced by our Tax Policy and Advocacy team, we'd love to hear from you if you have an area of interest that you think fellow members should know more about.

Working together is success – for our organisation and for you in your own career. If you're interested in being involved this year, please reach out to our team.

Associate's Report

by Abhishek Shekhawat, ATI

NALI for superannuation funds

With the long-awaited proposed changes to the non-arm's length income rules being announced, it is necessary to examine whether they are enough to address the underlying concerns.

On 24 January 2023, the government released a consultation paper considering the options to amend the non-arm's length income (NALI) provisions that currently apply to superannuation funds. The consultation follows significant efforts from The Tax Institute, other professional bodies and industry associations to advocate for change regarding how the rules currently operate. However, the changes suggested in the consultation paper do not properly address the underlying concerns, and would benefit from a fresh approach.

Overview of the NALI rules. The NALI rules are contained in s 295-550 of the *Income Tax Assessment Act 1997* (Cth) (ITAA97). Broadly, the provisions were introduced as an integrity provision to deter people from entering into arrangements designed to inflate member balances by allowing the fund to charge excessive amounts of income for entitlements or services provided. The derivation of excessive income was a result of the superannuation fund not dealing with the paying party at arm's length. Any income that is captured by the NALI provisions was taxed at the highest marginal tax rate of 45%.

The NALI rules were amended in 2019 to also cover non-arm's length expenditure (NALE) dealings. The changes were in response to concerns that some superannuation funds were entering into limited recourse borrowing arrangements that charged lower expenditure for services performed by parties for the fund. This also had the effect of artificially inflating the income of a superannuation fund.

Unfortunately, instead of designing a set of rules from the ground up to manage NALE transactions, the government introduced the 2019 changes by making amendments to s 295-550 ITAA97. This had the effect of any breaches of the NALE provisions potentially making the entire income of the superannuation fund, as well as all gains from the disposal of the fund's assets, NALI, and thereby subject to the highest rate of tax.

As demonstrated by the Commissioner's view in LCR 2021/2, the breadth of the NALE provisions could be easily breached for small or inadvertent NALE expenses, disproportionately impacting all of the income of a fund. Such expenses could include book-keeping or audit activities undertaken for little or no expense, or services by wholly owned entities being provided for little to no mark-up. Further, the NALE rules currently apply to all superannuation funds. With the rules being so easy to breach, the rules could have a real impact on many Australian superannuation balances.

Proposed changes. The government has proposed to change the NALI provisions to the extent that they relate to general expenses. Broadly, SMSFs and small APRA-regulated funds will be subject to a factor-based approach. This would set an upper limit on the amount of fund income taxable as NALI due to a general expenses breach. The currently proposed limit is a factor of 5 times the amount of the general NALE amount. If the product of 5 times the breach is greater than all of the fund's income, the entirety of the fund's income will be subject to tax at the highest marginal rate. Meanwhile, large APRA regulated funds would be exempted from the NALI provisions for general expenses.

It should be noted that, where there is a NALE breach for specific expenses by superannuation funds, the current NALI rules would continue to apply. As a result, all of the income of that asset will be NALI and subject to the highest marginal tax rate.

Is this the best way forward? The government's proposed approach, although welcomed by some, is not a permanent or long-term solution to the problems created by the NALI and NALE rules. The proposed changes will not address the key concerns that have been raised by the profession and industry.

For example, the NALI provisions would benefit from a rectification clause that would allow trustees of all superannuation funds to address inadvertent or honest errors. The provisions would also benefit from a re-designed approach that separates NALE from s 295-550 ITAA97, providing for a more proportionate response for NALE breaches. Details of some suggested solutions can be found in the submission to the former government by The Tax Institute and several professional associations and industry bodies in September 2021 and December 2021.

The Tax Institute and several professional associations and industry bodies have also signed an open letter to the government, highlighting the concerns with the proposal and suggesting alternative approaches.

Hopefully, the government will re-assess the need for real, lasting change that will create a fairer and more balanced system while still ensuring that the rules provide our system with the needed integrity. Let us know in The Tax Institute's Community what your thoughts are about the government's proposed NALI changes, and what more could be done to improve the operation of the provisions.

Tax News – the details

by TaxCounsel Pty Ltd

February – what happened in tax?

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

Government initiatives

1. DGR registers reform

The Treasurer has released exposure draft legislation (and explanatory material) that would transfer to the ATO the administration of four unique deductible gift recipient (DGR) categories that are currently administered by other government agencies.

This change is intended to make all DGR categories consistent in administration, reduce red tape imposed on endorsed organisations, and simplify the application process for organisations seeking DGR status.

The four DGR categories that are currently administered by government entities other than the ATO are:

- environmental organisations: administered by the Department of Climate Change, Energy, the Environment and Water;
- harm prevention charities: administered by the Department of Social Services;
- cultural organisations: administered by the Office for the Arts in the Department of Infrastructure, Transport, Regional Development, Communications and the Arts; and
- overseas aid organisations: administered by the Department of Foreign Affairs and Trade.

The explanatory material states that applications for an organisation to be endorsed as a DGR in these categories are typically significantly slower than applications in other DGR categories. It currently takes up to two years for DGR status to be approved for an entity seeking addition to one of the registers. The proposed amendments are intended to streamline the application and reporting requirements and reduce DGR approvals from up to two years to around one month.

2. Superannuation funds: non-arm's length expense rules

The government has released a consultation paper which considers options to amend the non-arm's length income (NALI) provisions which apply to superannuation funds.

While the NALI provisions are operating broadly as intended, the government appreciates that some superannuation industry stakeholders have raised the potential for disproportionately severe outcomes for breaches relating to general expenses.

For the purposes of stakeholder consultation, Treasury has developed potential policy changes to the NALI provisions where they relate to general expenses which have a sufficient nexus to all ordinary and statutory income derived by the fund.

Potential amendments to the NALI provisions for superannuation funds could be adopted as follows:

- self-managed superannuation funds and small Australian Prudential Regulation Authority (APRA) funds would be subject to a factor-based approach which would set an upper limit on the amount of fund income taxable as NALI due to a general expenses breach. The maximum amount of fund income taxable at the highest marginal rate would be 5 times the level of the general expenditure breach, calculated as the difference between the amount that would have been charged as an arm's length expense and the amount that was actually charged to the fund. Where the product of 5 times the breach is greater than all fund income, all fund income will be taxed at the highest marginal rate; and
- large APRA-regulated funds would be exempted from the NALI provisions for general expenses.

The Commissioner's perspective

3. Accessing company profits tax-free

The Commissioner has released a taxpayer alert in relation to arrangements where an individual accesses the profits of a private company in tax-free form (that is, without an additional tax liability for the individual) by arranging for the profits to be passed to the individual through an interposed holding company (interposed company) (TA 2023/1).

In these arrangements, a company is interposed between a private company with retained profits (first company) and its shareholder, and a CGT roll-over is applied to disregard the CGT consequences.

The first company then pays a franked dividend to the interposed company, which uses the proceeds to fund a loan to the individual, on terms which do not comply with the Div 7A loan requirements (s 109N of the *Income Tax Assessment Act 1936* (Cth) (ITAA36)).

The roll-over enables the shareholder to disregard for tax purposes the capital gain that they make on disposal of their shares in the first company. Further, the arrangements are structured so that Div 7A ITAA36 would not apply to treat the loan to the individual as an assessable dividend. That is because the interposition of the company and the subsequent dividend paid by the first company is to ensure that neither company has a distributable surplus for the purposes of Div 7A. As a result, the individual seeks to access, and purports to be able to access, the retained profits of the first company in a tax-free form.

TA 2023/1 applies to arrangements which, when viewed objectively, indicate that the dominant purpose of the arrangements is tax avoidance by enabling the individual to obtain a tax advantage or benefit.

The Commissioner is concerned that individual taxpayers and private companies under their control may be entering into these arrangements under the misapprehension that they are effective in avoiding additional tax being paid by the individual taxpayer. The ATO will closely examine these arrangements, including those where a holding company is interposed between a trustee shareholder and a company as similar concerns apply.

More specifically, aspects of the arrangements that concern the ATO include whether:

- there is any intention for the purported "loan" to the individual to be repaid or whether the amount may be taken to be an assessable dividend paid to the individual pursuant to s 109C ITAA36;
- the arrangements comprise a "dividend stripping" scheme or operation, such that s 177E ITAA36 applies to include the amount of the purported loan in the taxpayer's assessable income and s 207-145 of the *Income Tax Assessment Act 1997* (Cth) (ITAA97) applies to cancel the franking credit on the dividend paid to the interposed company; or
- there is a scheme under s 177D ITAA36 to which the general anti-avoidance provisions of Pt IVA could apply.

4. Advice under development

The Commissioner has recently released an update of the advice that is currently being worked on by the ATO. The following are some issues of interest.

Income tax issues

Capital allowances – composite items. A revised draft ruling is to be issued dealing with the issues that can arise under the capital allowance provisions of identifying the depreciating asset(s) where there is a composite item. The new draft ruling will replace TR 2017/D1 and will take into account subsequent developments.

Division 7A – undue hardship – corporate trustees. A draft determination is to be released which will set out the Commissioner's preliminary view on whether a corporate trustee could suffer undue hardship on payment of a debt owed to a company for the purposes of s 109G(4) ITAA36.

Construction of capital assets. A ruling is to be issued to finalise TR 2019/D6 and to provide clarification of the appropriate treatment of labour and other costs associated with the building and construction of capital assets.

The ATO has received a number of submissions on TR 2019/D6. The ATO does, however, maintain its view that labour costs covered by the draft ruling can be prevented by s 8-1(2)(a) ITAA97 (loss or outgoing of capital, or of a capital nature) from being deductible and there is no presumption that labour costs are always on revenue account.

Royalties and software. Advice on the development and marketing of software was previously provided in TR 93/12 (income tax: computer software). A draft ruling (TR 2021/D4) was issued in June 2021 to provide guidance on modern forms of software distribution, including digital channels and cloud computing. A revised draft ruling is to be issued which will provide the Commissioner's view on the circumstances in which amounts in respect of the licensing and distribution of software will be royalties as defined in s 6(1) ITAA36.

Use of an individual's image. TD 2022/D3 (use of an individual's fame by related entities) is being finalised and the final ruling will set out the Commissioner's view on how s 6-5 ITAA97 (income according to ordinary concepts) applies to arrangements where an individual with fame establishes a connected entity and enters into an agreement with that entity granting it non-exclusive use of their name, image, likeness, identity, reputation and signature.

Connected entities – control discretion. Where the control percentage under the connected entity rules in s 328-125 ITAA97 is at least 40% but less than 50%, the Commissioner has a discretion (under s 328-125(6) ITAA97) to determine that the first entity does not control the other entity if he thinks that the other entity is controlled by an entity other than, or by entities that do not include, the first entity or any of its affiliates.

A draft determination is to be issued which will set out the Commissioner's preliminary view on the meaning of "control" for the purposes of exercising this discretion.

Financial advice fees. A draft determination is to be released which will set out the Commissioner's preliminary view on the deductibility of financial advice fees under s 8-1 (general deductions) or s 25-5 ITAA97 (deductions for tax-related expenses) for individuals who are not carrying on a business.

The determination will broaden and update TD 95/60, which will be withdrawn when the updated determination issues.

GST

Time limits on entitlements to tax credits. A draft miscellaneous taxation ruling is under consideration which will deal with the time limits for claiming an input tax or fuel tax credit and, in particular, will set out the Commissioner's views on when entitlements to input tax credits or fuel tax credits do not cease.

Supply of burial rights by a government agency. GSTD 2021/D2 is being finalised and, when finalised, will set out the Commissioner's view on the GST consequences where an Australian government agency supplies a right of burial in respect of a public cemetery. The ATO is currently reviewing the large number of submissions received in relation to GSTD 2021/D2.

GST treatment of financial supplies. An addendum to GSTR 2002/2 (goods and services tax: GST treatment of financial supplies and related supplies and acquisitions) is being prepared that will update the ruling to reflect changes in the GST law (for instance, changes to the GST legislation applicable to cross-border supplies and in relation to digital currency) and will also contain some proposed changes to modernise parts of the ruling.

GST and retirement villages. A draft practical compliance guideline is being prepared which will set out the Commissioner's proposed compliance approach to assist retirement villages that make minimal taxable supplies to determine the extent of creditable purpose for acquisitions made in constructing and operating a retirement village. The proposed compliance approach will assist in reducing complexity and the costs of compliance.

FBT

Electric vehicles. A draft guideline is to be issued which will provide a methodology to enable users of electric vehicles to determine an approximate cost for the electricity used when charging an electric vehicle at home.

Capital gains tax

Appointment of capital – CGT event E5 or E7. A draft determination is to be issued which will deal with the question of whether CGT event E5 (beneficiary becoming entitled to a trust asset) or CGT event E7 (disposal to beneficiary to end capital interest) happens if the trustee of a discretionary trust appoints an amount of capital to a beneficiary (for example, by special resolution) and later makes a capital distribution in Australian currency in satisfaction of the appointed interest.

Australian currency denominated asset – CGT events E5 to E7. A draft determination is to be issued which will consider the question of whether an asset with a face value in Australian currency (including an Australian currency banknote or coin) can be a CGT asset for the purposes of CGT events E5 to E7.

Unit trust – CGT events E5 to E8. A draft determination is to be issued which will consider the meaning of the term "unit trust" in CGT events E5 to E8 and what the interaction implications are for other CGT events, in particular, CGT events E4 and C2.

Water rights. A draft determination is being prepared which will clarify whether certain CGT assets, such as water access entitlements, are "taxable Australian real property".

Recent case decisions

5. Discretionary trust: reimbursement agreements and Pt IVA

In a recent decision, the Full Federal Court (Perry, Derrington and Hespe JJ) has unanimously affirmed a decision of Logan J at first instance that the reimbursement agreement provision in Div 6 ITAA36 (s 100A) had no application in the circumstances, but reversed the decision of Logan J as to the operation of the general anti-avoidance provisions of Pt IVA ITAA36 in relation to one of the income years in question (*FCT v Guardian AIT Pty Ltd ATF Australian Investment Trust*[1]).

The transactions that gave rise to the tax litigation were carried out in the wider context of the reorganisation of the affairs of Mr Springer who had carried on various businesses through a number of companies and was seeking to transition to retirement. Mr Springer's business structure included the Australian Investment Trust (AIT), which was a discretionary trust that was settled on 25 June 1998 and of which Mr Springer was the "principal". This office conferred on Mr Springer the power to appoint a person to be a beneficiary of the trust. Guardian AIT Pty Ltd (Guardian), of which Mr Springer was the sole shareholder, became the trustee of the AIT on 14 November 1999. The shares in the various companies that carried on the businesses were held by AIT and/or Mr Springer.

On 27 June 2012, Mr Springer incorporated a company (AIT Corporate Services Pty Ltd (AITCS)) and appointed it to be a beneficiary of the AIT. The sole shareholder of AITCS was Guardian in its capacity as trustee.

On 28 June 2012, Guardian as trustee of the AIT appointed the income of the AIT for the 2012 income year that was not in the form of franked dividends ($2,640,209) to AITCS. This distribution was not paid to AITCS, creating an unpaid present entitlement (2012 UPE). On 17 April 2013, AITCS drew on its entitlement to the income of the AIT to discharge its liability to income tax for the 2012 income year of $792,062.

On 1 May 2013, AITCS declared a fully franked dividend in the amount of $1,848,145 payable to the AIT. That dividend was paid by reducing the balance of the 2012 UPE of AITCS to the income of the AIT from $1,848,145 to nil.

On 23 June 2013, Guardian appointed the net income of the AIT for the 2013 income year attributable to franked dividends to Mr Springer. This amount included the fully franked dividend declared by AITCS on 1 May 2013. Mr Springer was a non-resident for the purposes of Australian income tax which meant that the distribution was not subject to withholding or other Australian income tax.

A similar procedure was adopted in relation to each of the 2013 and 2014 income years. The financial statements of the AIT for the 2013 income year disclosed that, as at 30 June 2013, Mr Springer had unpaid beneficiary entitlements (including interest) of $12,546,677.

The Commissioner assessed Guardian for the 2012 to 2014 income years under ss 100A and 99A ITAA36. In the alternative, the Commissioner made determinations under Pt IVA ITAA36 and assessed Mr Springer in each of those income years to the amounts appointed to AITCS.

At first instance, Logan J held that s 100A had no application in any of the income years in question and that Pt IVA did not apply in any of the years on the basis that there was no tax benefit and, if there were a tax benefit, the requisite dominant purpose was not to obtain the tax benefit.

The Commissioner appealed to the Full Federal Court from the decision of Logan J in relation to the operation of s 100A for the 2013 income year and in relation to the application of Pt IVA for the 2012 and 2013 income years. The Full Court dismissed the Commissioner's appeal in relation to the application of s 100A ITAA36 and allowed the Commissioner's appeal in relation to the application of Pt IVA for the 2013 income year.

The judgment of the Full Court was given by Hespe J, with whose reasons Perry and Derrington JJ each agreed.

Section 100A

The Commissioner's case on appeal in relation to s 100A was narrower than the case put before Logan J. On appeal, the Commissioner did not seek to contend that a reimbursement agreement existed as at 28 June 2012, at the time Guardian appointed income to AITCS. The Commissioner on appeal accepted Logan J's conclusion that s 100A did not apply in respect of the year ended 30 June 2012.

Hespe J said that, while it was not necessary that an understanding be enforceable, or that it be intended to be enforceable, in order to constitute an "agreement" for the purposes of s 100A ITAA36, the understanding must nevertheless reflect a common intention, or consensus existing between at least two parties. Each of the terms "agreement, arrangement or understanding" in context implied at least an arrangement to which there is more than one party.

Her Honour said that the inquiry in relation to the existence of a reimbursement agreement in s 100A required the existence of an "agreement" (as defined in s 100A(10) ITAA36) invoking, as it did, a requirement of consensus and adoption. The scope for attribution in that context was far more limited. In the absence of a finding that a communication had been made to Mr Springer or his agent of a plan or recommendation prior to 23 June 2013, it was necessary to find that Ms Burke or Mr Fischer (the personnel in the accounting firm Pitcher Partners who were advising Mr Springer) had authorisation to act on or on behalf of the entities in order to conclude that there was consensus or adoption by Guardian and Mr Springer. No such finding was made by Logan J and, apart from relying on the general practice of Mr Springer to follow the advice of Pitcher Partners, the Commissioner did not press for such a finding on the appeal. Mr Fischer's evidence was that Ms Burke worked under his supervision. There was no evidence that she had authority to act on behalf of Mr Springer or the entities in the Springer group. While the evidence supported a finding that Mr Springer generally followed the advice of Mr Fischer, there was no evidence that Mr Fischer was an authorised representative of Mr Springer or the Springer group.

Hespe J said that it was to be concluded that, although the payment of a dividend by AITCS to the AIT as at 23 June 2013 was not "wholly conjectural", there was no "agreement" as at 23 June 2013 within s 100A(13) ITAA36 which involved the payment of such a dividend and, therefore, there was no "reimbursement agreement" for the purposes of s 100A ITAA36.

This conclusion in relation to s 100A ITAA36 made it unnecessary for the Full Federal Court to consider the issues of purpose and the scope of the phrase "ordinary commercial or family dealing" in the definition of "agreement" in s 100A(13) ITAA36.

Part IVA

In relation to the application of Pt IVA ITAA36, Hespe J said that the entire object of s 177D ITAA36 (schemes to which this Part applies) was to require a conclusion to be drawn in respect of the purpose of a party based on the factors specified in that section. That purpose was not the party's actual subjective purpose but an attributed purpose.

Her Honour said that, on the creation of AITCS's unpaid present entitlement to the income of the 2013 income year on 23 June 2013, the objective circumstances would give rise to an expectation in an objective, reasonable observer that AITCS's unpaid present entitlement would be cleared out in the same way as it was in respect of the entitlement created for the year ended 30 June 2012, enabling Mr Springer to enjoy the benefit of that distribution in the form of a franked distribution paid to him in the following year. This was precisely what happened.

As the chronology of events demonstrated, the manner in which the 2012 related scheme came to be entered into and carried out, and the form which it came to take, were the products of an evolving set of circumstances. By contrast with the 2012 related scheme, the form of the 2013 related scheme was not the product of an evolving set of circumstances, but was the implementation of a strategy that had been developed with the evolution and implementation of the 2012 related scheme.

Other s 100A litigation

It should be noted that an appeal by the taxpayer from the decision of Thawley J in *BBlood Enterprises Pty Ltd v FCT*[2] which raised s 100A ITAA36 issues is due to be heard by the Full Federal Court in March 2023.

6. AAT: jurisdiction issue

The AAT has held that it did not have jurisdiction to review a decision made by the Commissioner to refuse the taxpayer's request to remit a shortfall interest charge totalling $17,901.55 which related to income tax assessments for the 2017 and 2018 income years (*Dermatis and FCT*[3]).

On 1 April 2021, a notice of amended assessment was issued to the taxpayer for the year ended 30 June 2018, which included a tax shortfall amount of $251,985 and a shortfall interest charge of $17,613. On 6 April 2021, a notice of amended assessment was issued to the taxpayer for the year ended 30 June 2017, which included a tax shortfall amount of $2,392 and a shortfall interest charge of $287.

Following requests made via the tax agent portal for the remission of all shortfall interest and general interest charged on the taxpayer's income tax account, the Commissioner notified the taxpayer in writing of the shortfall interest charge remission decision not to remit the shortfall interest charge amount, attaching reasons for the decision.

The Commissioner also advised the taxpayer that he could not object to the shortfall interest charge remission decision as the shortfall interest charge balance payable was equal to or less than 20% of the tax shortfall amount. Further, the taxpayer was advised that, if he did not agree with the Commissioner's decision, he could apply to the Federal Court or the Federal Circuit Court for a review within 28 days of receiving the decision.

On or around 22 November 2022, the taxpayer lodged an application in the AAT seeking review of the shortfall interest charge remission decision (the application). Following an interlocutory hearing, the AAT held that it did not have jurisdiction to consider the application.

After referring to, and quoting from, the joint judgment of the majority of the Full Federal Court in *FCT v Administrative Appeals Tribunal*,[4] the AAT said that it was apparent that the question of jurisdiction was to be determined by reference to the definition of a "taxation decision" that applies for the purposes of the *Taxation Administration Act 1953* (Cth) (TAA53). If a taxpayer does not have the right to object against a decision in accordance with Pt IVC of that Act, it is not a "taxation decision".

In relation to a decision by the Commissioner not to remit an amount of shortfall interest charge, a taxpayer has the right to object against such a decision provided the shortfall interest charge that was not remitted is more than 20% of the tax shortfall amount pursuant to s 280-170, Sch 1 TAA53. Conversely, there was no provision that permitted a review of a decision under Pt IVC where the amount of the shortfall interest charge that was not remitted was less than 20% of the shortfall amount.

The AAT said that the taxpayer in the present case had no statutory right to object to the decision to not remit the shortfall interest charge because the shortfall interest charge amounts for the 2017 and 2018 income years totalling $17,901.55 were less than 20% of the tax shortfall amounts for each of those years. Consequently, as the taxpayer had no right to object, there was no taxation decision that could be the subject of review by the AAT.

TaxCounsel Pty Ltd
ACN 117 651 420

References

1 [2023] FCAFC 3.
2 [2022] FCA 1112.
3 [2023] AATA 13.
4 [2011] FCAFC 37.

Tax Tips

by TaxCounsel Pty Ltd

Tax Practitioners Board developments

There is amending legislation and other recent Tax Practitioners Board developments that should be noted.

Background

Each 1 March marks an anniversary of the establishment of the Tax Practitioners Board (TPB) by the *Tax Agent Services Act 2009* (Cth) (TASA09). That Act received royal assent on 26 March 2009 but significant operative provisions, including those relating to registration, the code of conduct, civil penalties and investigations, commenced on 1 March 2010.

In the ensuing years, there have been considerable developments, including the issue by the TPB of a variety of information products, actions taken by the TPB to enforce compliance with the Act, and decisions, principally of the AAT, that have resulted from such compliance action.

Importantly, significant legislative change to the TAA09 is proposed to further ensure that the regulatory regime is enhanced and operates satisfactorily. In this regard, an amending Bill (the Treasury Laws Amendment (2023 Measures No. 1) Bill 2023) was introduced into parliament on 16 February 2023.

The TPB has been very proactive and its website is clear evidence of the Board's dedication to, on the one hand, providing appropriate assistance and, on the other, ensuring compliance.

This article briefly considers the most recent court decision relating to the way that the compliance provisions are to be applied, several recent enforcement decisions of the TPB, and aspects of the proposed legislative amendments.

The latest court decision

The most recent court decision involving the operation of the TASA09 is the decision of the Federal Court (Charlesworth J) in *Tax Practitioners Board v Williams*.[1]

The issues for decision in this case arose in the context of an individual (a Mr Williams) whose registration as a tax agent had lapsed on 1 December 2018.

After the lapse of his registration, Mr Williams continued to prepare and lodge tax returns for taxpayers in Australia for a fee or other reward. By doing so, he committed multiple contraventions of s 50-5(1) TASA09 (providing tax agent services if unregistered).

On 8 June 2021, the Tax Practitioners Board commenced the present proceedings seeking the imposition of civil penalties and other relief in connection with Mr Williams' contraventions. By its originating application, the Board also sought interlocutory relief in the form of an injunction restraining Mr Williams from preparing and lodging tax returns for taxpayers for a fee or reward while not registered as a tax agent. On 18 June 2021, the Federal Court (the court) granted the interlocutory injunction with Mr Williams' consent.

By a statement of charge dated 29 September 2021, the Board alleged that Mr Williams was in contempt of the injunction by preparing and lodging seven income tax returns for four different taxpayers on 5 July 2021, 22 July 2021 and 23 July 2021.

Mr Williams admitted the conduct constituting the contraventions of the TASA09, as well as the conduct constituting the contempt. On 13 October 2021, Mr Williams was adjudged guilty of contempt as alleged in the statement of charge. He did not contest the question of his guilt.

In the present proceedings, the court was called on to assess the civil penalties and other remedies to be imposed for the civil contraventions, and consider whether a final injunction should be granted and the appropriate punishment for the contempt.

The decision

Charlesworth J held that:

- there would be an order that Mr Williams pay civil penalties in an amount totalling $80,000 for his contraventions of s 50-5(1) TASA09;
- there would be a final injunction in the terms sought by the Board, subject to Mr Williams having liberty to apply to vary or revoke the injunction not earlier than 10 years from 8 February 2023 (the date of the judgment); and
- for his contempt of the court, Mr Williams would be sentenced to a term of imprisonment in a correctional facility for 10 days, such term to commence on a date to be fixed after the expiry of the period in which he could appeal from the court's orders.

Particular aspects of the decision

Some aspects of the judgment of Charlesworth J are noted below.

In relation to the contraventions of s 50-5(1) TASA09, Charlesworth J said that:[2]

> "The importance of s 50-5 hardly needs stating. The prohibition against persons providing tax agent services for fee or reward without being registered as a tax agent is the lynch pin in the regime. It is the requirement to hold a license (in the form of registration) that subjects those who provide taxation services to standards of behaviour contained in the Code and enforceable by the Board. That requirement ensures that defined tax

services are only provided by persons who are fit and proper to provide them. The conditions of fitness and propriety require not only that the registrant holds the necessary knowledge and qualifications, but also possesses personal characteristics that are not inimical to the statutory purpose. Conduct that contravenes s 50-5(1) is conduct that undermines the efficacy of the whole of the regime."

Her Honour said that the purpose of a civil penalty is to protect the public interest by deterring future contraventions of the TASA09 by the contravener and by others.

Charlesworth J then went on:[3]

> "The power to impose a penalty is discretionary. It is cast in relevantly the same terms as that conferred under s 546 of the *Fair Work Act 2009* (Cth), the scope of which was recently discussed by the High Court in *Australian Building and Construction Commissioner v Pattinson* [2022] HCA 13 … As Kiefel CJ, Gageler, Keane, Gordon, Steward and Gleeson JJ there observed, it is 'like any discretionary power conferred by statute on a court, to be exercised judicially, that is, fairly and reasonably having regard to the subject matter, scope and purpose of the legislation' (at [40]). Their Honours emphasised that when imposing a penalty, the Court acts for the purpose of protecting the public interest by deterring future like contraventions: *Pattinson* (at [40]). Retribution has no part to play."

Her Honour went on to say that, when determining the appropriate penalty, the seriousness of the contravention is a relevant consideration. However, it is not to be regarded as a controlling factor.[4] As the majority said in *Australian Building and Construction Commissioner v Pattinson*, "[c]onsiderations of deterrence and the protection of the public interest, justify the imposition of the maximum penalty where it is apparent that no lesser penalty will be an effective deterrent against future contraventions of a like kind".[5] The maximum penalty is not otherwise to be utilised as a "yardstick" or as the uppermost end of a scale by which contraventions may be graded according to seriousness with corresponding monetary penalties.[6]

Charlesworth J then went on:[7]

> "There must be a 'reasonable relationship' between the theoretical maximum and the penalty imposed, however, as emphasised in *Pattinson* (at [56]–[57]), the reasonableness of that relationship is to be established by reference to the circumstances of the contravener as well as the circumstances of the conduct constituting the contravention. Either of those circumstances may have a bearing on the need for deterrence in the particular case. They may overlap, particularly in cases where the contravening conduct is accompanied by a deliberate or strategic state of mind. The seriousness of a contravention and the associated need for deterrence may be assessed not merely by reference to the nature of the physical acts constituting the contravention, but by the accompanying mental attitude: *Pattinson* (at [57]–[58])."

Her Honour said that she assessed the penalty on the basis that the multiple contraventions together formed a part of a course of conduct occurring over a number of months. As emphasised in *Employsure*,[8] it did not follow that the maximum penalty that might otherwise be imposed should be converted to that applicable to a single contravention.

In all of the circumstances, Charlesworth J was satisfied that the penalty should be fixed in an amount that had a considerable financial impact on Mr Williams.[9] There was a need in the present case to impress on Mr Williams that contravening the TASA09 was not a solution to his financial difficulties but would only serve to exacerbate them. The imposition of a financial penalty would of course be a source of additional financial hardship, but that was a consequence contemplated by the TASA09 itself. The circumstance that a civil penalty occasions hardship does not mean that it is imposed for a punitive purpose. After weighing up the arguments of the parties, Charlesworth J considered that a penalty in the amount of $80,000 was more appropriate to bring about the insight necessary to influence Mr Williams' future behaviour.[10]

Charlesworth J said that it was correct to say that an appropriate penalty is one that deters prospective contraveners from regarding non-compliance with the law as a potentially profitable exercise. On that topic, her Honour said that she had had regard to authorities put forward by Mr Williams' counsel indicating the penalties imposed in cases he sought to employ in a comparative way but said that she had derived little assistance from them. Her Honour was not persuaded that penalties should be fixed as a multiple of the financial gain (derived from the contravention) equivalent to a multiple derived mathematically from other cases. To proceed in that way would be to ignore fundamental features of the present case. Moreover, the low amount of financial gain was not the result of a conscious decision of Mr Williams to cease contravening the TASA09. As such, the low financial gain was not a reliable indicator of the need for deterrence.

Contempt

Charlesworth J said that, as a matter of specific deterrence, she considered that the prospect that a term of imprisonment may be imposed in respect of future conduct constituting a contempt of the court was a relevant factor. However, unlike the civil penalty regime in the TASA09, the need to ensure specific deterrence was not the only purpose of the court's power to punish for contempt. In this case, considerations of general deterrence and punishment were significant.

After noting that the conduct constituting the contempt occurred against a background of repeated contraventions of the TASA09 that the threat of civil penalty proceedings had been ineffective to discourage, and that it was not suggested by Mr Williams that he misunderstood the purpose of the injunction (being to cease his contravening conduct), Charlesworth J said:[11]

> "Viewed in context, I consider the conduct constituting the breach of the Injunction to be very serious because it

demonstrates an absolute disregard for the authority of the Court. The explanation for the contempt is the same as that put forward to explain the civil contraventions, namely, straitened financial circumstances and asserted pressure from taxpayers. I reject the assertion that the contempt is explained or justified in any way by pressure asserted by the taxpayers themselves. The motivating factor on Mr Williams' part was to gain money for conduct that, I find, he knew to be in breach of the Court's order. The Court has previously found that the breach of its orders was wilful and there was no application to revisit that finding. To the extent that Mr Williams was ignorant, he was ignorant of the seriousness with which the Court may view the contempt. I do not consider that to be a sufficient reason to avoid imposing upon Mr Williams a penal consequence that is appropriate to punish his knowing breach of the Court's order.

The need for general deterrence in the present case is pressing. The Court has an important role to play in the enforcement of a number of regulatory regimes established by the Parliament. The making of orders to ensure compliance with the regime established by the TAS Act is made plain in s 70-5. An injunction made under that provision is intended to provide for additional consequences for contravening conduct (deriving from the Court's own powers) over and above the civil penalty regime."

In all of the circumstances, her Honour did not consider the imposition of a fine to be an adequate punishment for the contempt, even if the evidence was sufficient to show that Mr Williams had the capacity to pay. Nor did her Honour consider the imposition of a fine to serve the legitimate purpose of general deterrence in the present case. Her Honour went on:[12]

It is true that a fine might be such as to make a breach of the Court's orders a commercially unpalatable risk. But as the present case shows, there is a class of persons (of whom Mr Williams is one) who are prepared to take considerable risks in contravening the law even where the chance of detection is very high. More fundamentally, the purpose of the power to punish for contempt is one that is concerned to protect and maintain the administration of justice more generally by reinforcing the Court's authority. I am satisfied that Mr Williams knowingly ignored and so disrespected the Court's authority, albeit in circumstances where he misjudged the seriousness with which the Court would view his conduct.

I have carefully considered the impact that a term of imprisonment would have in terms of the deprivation of Mr Williams' personal liberty. That impact necessarily varies according to the length of the sentence. The deprivation of personal liberty is a serious consequence and it is for that reason that I consider the term of imprisonment should be short, but nonetheless sufficient to impress upon Mr Williams and others the importance of compliance with orders made under the TAS Act that buttress the regime, and to discourage conduct that undermines the Court's authority more generally.

In the circumstances described I am satisfied that the imposition of a fine is insufficient and that a period of 10 days imprisonment is appropriate."

Charlesworth J made these further points:[13]

- the term of imprisonment was arrived at after careful regard to Mr Williams' degree of cooperation in the proceeding, particularly his conduct in not disputing the facts alleged in the statement of charge and his compliance generally with the procedural orders of the court. Were it not for the significant degree of cooperation by Mr Williams, the term of imprisonment would have been 21 days, more than twice as long as that now contemplated;
- there was a possibility that a custodial sentence may impact negatively on Mr Williams' family relationships;
- a term of imprisonment may be suspended. However, in the present case, the impacts of a short custodial sentence were not such as to warrant suspension; and
- the date on which the term of imprisonment should commence may be deferred so as to reduce the impact that it may have on third persons, including family members.

Some recent TPB enforcement action

Sharing of confidential information

In a media release on 23 January 2023, the TPB announced that a former tax partner at PricewaterhouseCoopers (PwC) had been deregistered as a tax agent for integrity breaches, with a two-year ban on becoming a registered tax practitioner.

An investigation carried out by the TPB revealed that the then tax agent, while a partner of PwC, was part of a confidential consultation by Treasury in relation to improving the tax laws. This included new rules to stop multinationals avoiding tax by shifting profits from Australia to tax and secrecy havens. The then tax agent made unauthorised disclosures of this confidential law reform information to partners and staff of PwC.

The TPB found that the then tax agent had failed to act with integrity, as required under his professional, ethical and legal obligations, and terminated his tax agent registration.

In addition, the TPB investigation determined that PwC had failed to properly manage conflicts of interest when this confidential law reform information was shared with partners and staff in its tax practice. PwC breached its obligations under the law and the Code of Professional Conduct. The TPB ordered PwC to have processes and training in place to ensure that conflicts of interest were adequately managed.

Agent's tax obligations

In a compliance case study released on 10 February 2023, a tax agent failed to meet their obligations by not lodging several personal business activity statements by their due dates. The tax agent also failed to pay or enter into an approved payment arrangement with the ATO for their personal tax debt, despite the Board Conduct Committee previously:

- imposing an order on the agent in 2021 requiring them to do so; and
- requiring the agent to provide the Board with evidence of any commencement, default or cancellation of the payment plan.

It was noted that the ATO had also granted an extension of time to the tax agent to address their outstanding personal tax debt. However, the debt remained outstanding.

The Board Conduct Committee noted the significant period of time that the tax agent's personal tax obligations remained unaddressed, and the agent's failure to comply with the order.

The Board Conduct Committee determined that the tax agent ceased to be a fit and proper person to remain registered. When making this decision, the Board Conduct Committee noted that a tax practitioner's lack of attention to personal tax obligations and their dealings with regulators reflected on their ability to represent the tax affairs of their clients.

The Board Conduct Committee terminated the tax agent's registration and also prohibited the agent from reapplying for registration for a period of two years.

Personal and related entities' tax affairs

In another compliance case study released on 10 February 2023, a tax agent and their related entities had a substantial number of personal tax returns and business activity statements outstanding for over four years. They also had over $1.5m in outstanding tax debt without an approved payment arrangement with the ATO.

The tax agent further failed to disclose these outstanding tax obligations in their renewal application, thereby making a false and misleading statement to the TPB.

The TPB's investigations also showed that the agent had reported incorrect income, tax losses and credits for a related entity, resulting in significant tax shortfalls and penalties imposed by the ATO following an audit. The agent failed to respond to the ATO's formal notice for information.

The tax agent also failed to respond to requests made by the TPB for information.

The TPB Board Conduct Committee determined that the tax agent failed to satisfy that they were a fit and proper person to be registered, and terminated their registration due to their conduct which:

- breached items 1, 2 and 14 of the Code of Professional Conduct;
- showed disregard to the TPB by failing to respond to its requests for information and declaring they had no outstanding tax obligations when they were aware that the TPB had already began an investigation into their conduct;
- demonstrated non-compliance with taxation laws through significant outstanding tax obligations;
- exhibited recklessness and failure to uphold the integrity of the tax system by recording or reporting income and credits incorrectly; and
- showed disregard to the ATO by not complying with a formal notice issued by the ATO.

Taking into account the seriousness and repeated nature of the tax agent's conduct, the Board Conduct Committee further prohibited the agent from reapplying for registration for three years.

The proposed amendments

As indicated, an amending Bill (the Treasury Laws Amendment (2023 Measures No. 1) Bill 2023) has been introduced into parliament which, when enacted, will give effect to various recommendations of the final report of the independent review into the effectiveness of the TPB and the TASA09.

In particular, the recommendations were to:

- amend the object clause of the TASA09 to make it more contemporary and better aligned with the TPB's role and responsibilities (recommendation 2.1);
- enhance the TPB's financial independence by establishing a special account (recommendation 3.1);
- amend the TASA09 to strengthen the disclosure requirements to require tax practitioners to not employ or use disqualified entities in the provision of tax agent services without approval from the TPB (recommendation 4.6);
- convert the three-year registration cycle to annual registration to align with the TPB's administrative annual declaration process (recommendation 4.7); and
- amend the TASA09 to give the relevant Minister the power to supplement the TASA09's Code of Professional Conduct to address emerging or existing behaviours and practices (recommendation 5.1).

Disqualified entities

The most significant of the proposed amendments is that which is to give effect to recommendation 4.6 and which will require tax practitioners to ensure that their employees and associates are not disqualified entities.

The recommendation is intended to deal with an identified gap in the regulation of tax services whereby entities who would not qualify to be registered as a tax practitioner (eg an applicant whose registration application was rejected for not meeting the fit and proper requirements) are nevertheless able to provide tax services under the auspices of a registered tax practitioner.

Recommendation 4.6 is being implemented by introducing the following obligations:

- new obligations under the Code of Professional Conduct for tax practitioners to ensure that:
  - they do not employ or use entities who meet the definition of a "disqualified entity" to provide tax agent services on their behalf, unless approved by the TPB; and
  - they do not enter an arrangement with a disqualified entity in connection with providing tax agent services; and
- an entity who meets the definition of a "disqualified entity" must disclose their disqualified status to the tax practitioner if:
  - they are being employed or used to provide tax agent services on behalf of the tax practitioner; or
  - they are entering an arrangement with a tax practitioner in connection with providing tax agent services.

These amendments are intended to ensure that the entities employed or used by tax practitioners in the provision of tax services, have the appropriate ethical and professional attributes to be employed in the tax profession. The amendments mirror the requirements that currently apply in respect of legal practitioners and their employees and associates in Victoria and New South Wales.

Several points in relation to the amendments in this regard are noted below.

Who is a disqualified entity?

The definition of a "disqualified entity" in the amending legislation is partially based on the objective criteria which are currently utilised to determine whether individuals are "fit and proper" for the purposes of ss 20-15 and 20-45 TASA09.

In addition, it would include anyone who has:

- committed a serious offence (as defined in the *Income Tax Assessment Act 1997* (Cth));
- been subject to sanctions by the TPB;
- had their registration refused, terminated or suspended for reasons other than work experience and qualifications; or
- been found to have breached the Act by the TPB or a court.

Obligations of disqualified entities

A disqualified entity will have the obligation to notify the tax practitioner of their status if:

- they seek or continue employment or engagement to provide tax agent services, or they become a disqualified person in the course of their employment or engagement; or
- they seek or continue an arrangement in connection with a tax practitioner in connection with the provision of tax agent services, or they become a disqualified person in the course of an arrangement.

Following the provision of notice by a disqualified entity, it will be the tax practitioner's responsibility to contact the TPB and seek approval to employ or use the individual or entity to provide tax agent services on their behalf.

If a disqualified entity fails to provide written notice to the tax practitioner, prior to commencing or during the provision of tax agent services or where there is an arrangement with the tax practitioner, the TPB will be able to apply to the Federal Court to seek civil penalties.

Obligations of tax practitioners

Employment or use of a disqualified entity

Registered tax practitioners will be required to comply with a new ongoing obligation under the Code of Professional Conduct. Under this obligation, tax practitioners must not employ or use an entity to provide tax agent services on their behalf if they know or ought to reasonably know that they are a disqualified entity, unless they have received approval from the TPB.

As part of their Code of Professional Conduct obligations, tax practitioners will be required to consider the following:

- who the individuals or entities are who have been employed or used, or seek to be employed or used, by the registered tax practitioner to provide tax agent services on their behalf; and
- whether any of those individuals or entities meet the definition of a "disqualified entity".

Tax practitioners would likely need to assess the following entities who are or will be used in providing tax agent services: employees, associates or contractors. However, this list is illustrative only and depends on the specific facts and circumstances of each tax practitioner and the people and entities they employ or use in their business.

Individuals who only provide peripheral services to assist a tax practitioner will not be included in the scope of the proposed amendments. For example, administrative support staff who are only responsible for the administrative management of client files and data would not be considered as providing tax agent services on behalf of a tax practitioner.

Further, individuals or entities who are included in the scope of those who are "used" to provide tax agent services would be those who would share in the revenue and income received from the services provided under the tax practitioner. This is intended to avoid imposing sanctions on those providing voluntary tax agent services at no cost.

Tax practitioners would be expected to implement new onboarding requirements, information-gathering and employee reporting processes to determine whether their staff and the people they use are disqualified entities and require notification and approval by the TPB.

Application and transitional provisions

The amendments in relation to recommendation 4.6 are to commence from the first 1 January, 1 April, 1 July or 1 October to occur after the day the amending Bill receives royal assent.

The amending Bill contains application and transitional provisions that are intended to appropriately capture both existing and new employees or entities who may be disqualified entities, and provide tax practitioners and regulators with sufficient time to implement the amendments.

A transitional period is being provided for the notification requirements and the delayed application of the Code of Professional Conduct requirement is being allowed to ensure sufficient time for:

- tax practitioners to implement internal processes to confirm whether their existing workforce consists of disqualified entities;
- existing employees and entities to disclose that they are disqualified to the relevant tax practitioner; and
- the TPB to establish the systems and operations necessary for the notification and approval process and administrative guidance.

Observations

It will be apparent that the amendments will mean that registered tax practitioners will need to develop and put in place appropriate mechanisms that will ensure that they are compliant with the amendments.

TaxCounsel Pty Ltd

References

1 [2023] FCA 63.

2 [2023] FCA 63 at [12}.

3 [2023] FCA 63 at [15].

4 *Australian Building and Construction Commissioner v Pattinson* [2022] HCA 13 at [58].

5 [2022] HCA 13 at [50].

6 [2022] HCA 13 at [51].

7 [2023] FCA 63 at [17].

8 *Australian Competition and Consumer Commission v Employsure Pty Ltd (No. 2)* [2021] FCA 1488.

9 [2023] FCA 63 at [81].

10 [2023] FCA 63 at [85].

11 [2023] FCA 63 at [121] and [122].

12 [2023] FCA 63 at [123]–[125].

13 [2023] FCA 63 at [126]–[129].

Higher Education

Accessible way to obtain a postgraduate degree

The dux of Corporate Tax Study Period 1 2022 discusses the practicality of the subject, what he found most interesting, and the fact that there are no shortcuts for great results.

Adrian Flego
Tax Policy Adviser
Treasury

Please provide a brief background of your career in tax.

I have worked for the Australian Public Service for 12 years in various roles, including at the ATO, the Board of Taxation and Treasury, where I am now.

Why did you choose to study with The Tax Institute Higher Education?

The Graduate Diploma of Applied Tax Law seemed like it would impart more practical skills and knowledge for a working professional than a university Masters degree. Also attractive was the accessible cost for an accredited postgraduate qualification.

What was the reason for undertaking the Corporate Tax subject?

Corporate Tax was an elective as part of the Graduate Diploma of Applied Tax Law. I also had a personal interest in developing my technical skills and knowledge in this area.

What skill or knowledge areas have you gained by undertaking this subject?

To provide credible and informed advice on corporate tax matters.

What part of the subject did you find most interesting?

The most interesting aspect of this subject was the interaction of the rules for winding-up/liquidations and the small business CGT concessions. Also of interest was the oddity of the approach to the “restructure” concept in the demerger rules and its interaction with the anti-avoidance framework in s 45B of the *Income Tax Assessment Act 1936* (Cth).

How did you juggle study, work and other commitments?

It required hard work and sacrifice on weekends, and unfortunately, there are no shortcuts. One tip is to keep on top of the content on a weekly basis.

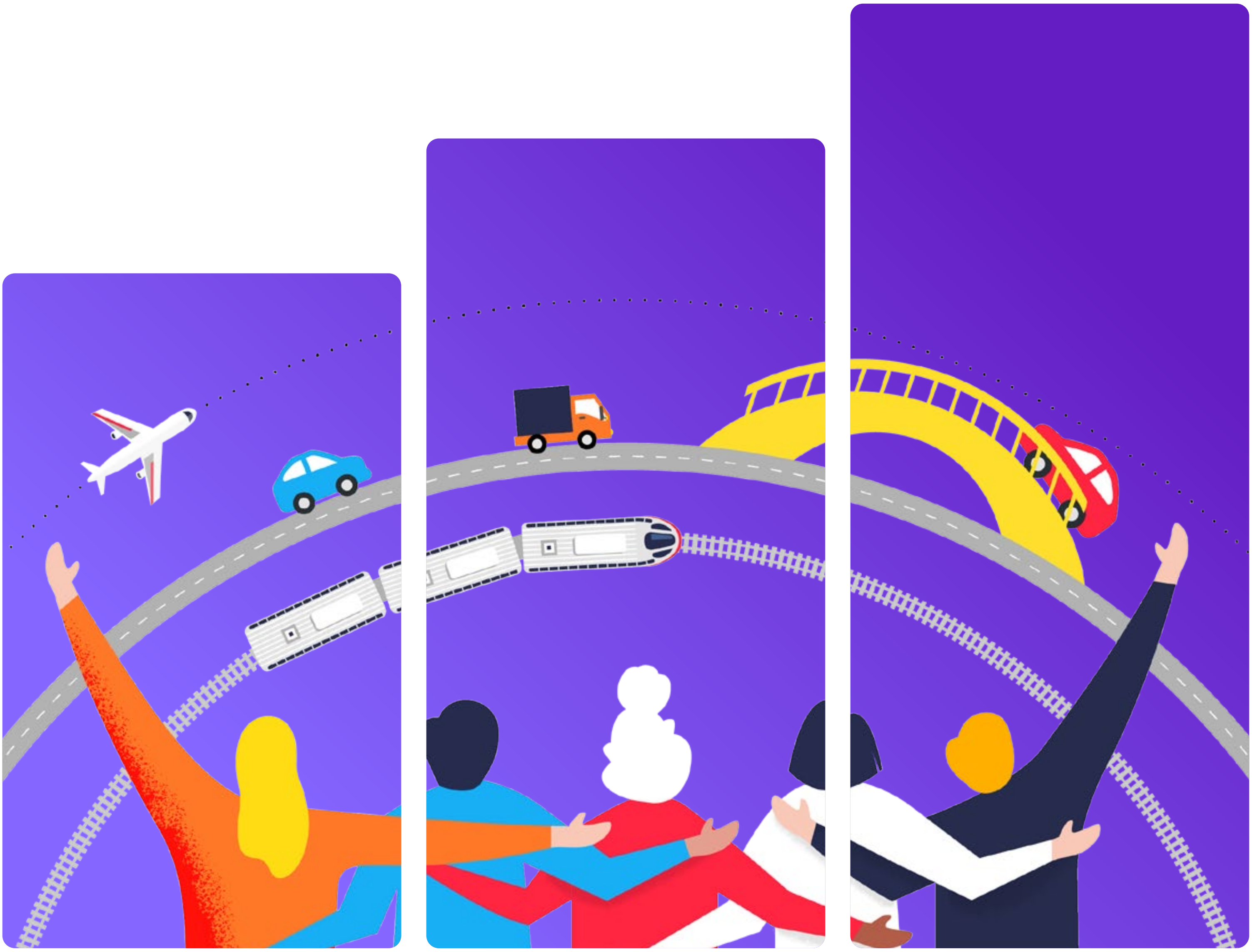
Where to now for you when it comes to continuing tax education?

Finish the Graduate Diploma of Applied Tax Law and gain the Chartered Tax Adviser designation.

What advice do you have for other tax professionals considering the Graduate Diploma of Applied Tax Law?

I’m not a tax practitioner, but as someone involved in tax policy development, I have found the course invaluable for the practical knowledge and application to real-life scenarios and case studies. I would recommend anybody wanting more tangible, practical learning to undertake the course.

Ready to continue your education in tax? Gain the skills, knowledge and expertise you need to succeed in tax with an online accredited tax program.



Section 100A: yea or nay?

by Elizabeth Allen, Special Counsel, and John Ioannou, CTA, Principal Lawyer, Macpherson Kelley

While recent cases on s 100A may provide some comfort to advisers and their clients in respect of how they manage their trust distribution strategies, it is important to keep in mind that overcoming a particular anti-avoidance provision is not a "get out of jail free" card. A review of the cases in the area show that where few succeed, many others often fail off the back of a lack of evidence, quality of evidence, or as a result of other anti-avoidance provisions being deployed.

Introduction

Six primary taxpayers (between them, across some 12 decisions) have sought the court's guidance on how to correctly interpret s 100A of the *Income Tax Assessment Act 1936* (Cth) (ITAA36).

While the intention of this article is to give a summary of the learnings that each court decision provides, we have also sought to distil a set of 10 guiding principles to use as a starting point for s 100A analysis and to help shape your analysis.

These principles ("commandments" if you will) are by no means exhaustive. But they are, at least to the authors' minds, 10 common themes that arise from the courts' interpretation and application of s 100A over the past 45 years, and they are designed to help you answer the question, "s 100A: yea or nay?".

History and context

Two excellent papers, to which the authors are indebted, have already made much of the history and context of s 100A.[1] However, for current readers, suffice to say that the relevant points are as follows:

- until the 1970s, the most significant changes to the Australian tax system were targeted at expanding the revenue base;[2]
- with a top marginal rate of tax sitting between 66% and 60% over the course of the 1970s (and a comparative corporate rate of anywhere between 45% for private companies in 1970 to 46% by the start of the 1980s), tax avoidance had been adopted as somewhat of a national sport;
- between 1974 and 1977, the Commissioner suffered a series of public setbacks in his attempted prosecution of tax avoidance cases[3] under the then s 260 ITAA36. In these cases, Barwick CJ's High Court effectively rendered that section "ineffective as a general 'anti-avoidance' provision";[4]
- concurrently, Australian taxpayers were falling in love with trusts, with a steady growth in popularity as both a business and an investment vehicle emerging from the late 1950s;[5]
- by the 1970s, people had clearly identified the ability to use, in particular, discretionary trusts to stream income to beneficiaries with a preferable rate of tax. Sometimes those distributions would end up benefitting someone else other than the recipient of the distribution;
- by 1978, then Treasurer, the Hon. John Howard AC, had had enough. Over the course of several months, he:
  - announced that the government would be legislating to counter tax avoidance through trust stripping schemes by rendering distributions of income by trustees pursuant to arrangements with a tax avoidance purpose ineffective;[6]
  - introduced the Income Tax Assessment Amendment Bill (No. 5) 1978 (the Bill) to parliament on 23 November 1978; and
  - saw the Bill become law in March 1979;
- while the explanatory memorandum that accompanied the Bill suggested that, at least in the context of s 100A, the key factor that the parliament sought to target was:
  - specifically introduced beneficiaries,
  - with a comparatively low rate of tax (say, either due to their rate of tax or due to the availability of tax losses),
  - coupled with a parallel arrangement comprising an obligation by the beneficiary to pay the distribution elsewhere (the necessary "reimbursement agreement"), and
  - a third party actually receiving that amount in a non-taxable form,

  clearly, given the High Court's approach to the statutory interpretation of anti-avoidance provisions specifically, the parliament had a desire to introduce legislation that would be broad enough to allow interpretation beyond targeting a specific type or series of transactions;
- notwithstanding the big song and dance made when it was first introduced, s 100A has remained largely dormant (at least from the public's perspective), only getting serious consideration by the courts with regard to four taxpayers between 1989 and 2008, namely, *East Finchley*,[7] *Prestige Motors*,[8] *Idlecroft*[9] and *Raftland*;[10]
- fast forward to the mid- to late 2010s, when the tax adviser community was firmly put on notice that the Commissioner had renewed interest in "reimbursement agreements" thanks to:
  - a publication on the ATO's website, *Trust taxation – reimbursement agreement*; and

  - statements by senior members of the ATO at industry events (such as at The Tax Institute's 2018 National Convention and Noosa Tax Intensive) that certain trust arrangements involving apparent reimbursement agreements were attracting the Commissioner's attention;
- as a side note, of course we now know, thanks to the court's timeline of events,[11] that the Commissioner's review and audit of Mr Springer (of *Guardian AIT* fame) was well underway by this point, culminating with amended assessments issuing in late 2017. Similarly, the *BBlood*[12] and associated taxpayer audits were clearly underway around this time, given the first amended assessment issues in August 2019;
- fast forward again to 2021, the first time that a s 100A case comes before the court in some 13 years is in *Guardian AIT* in April of that year before Logan J, and later the *BBlood* hearing before Thawley J in October;
- having ventilated (and tested) his views before the courts over the course of 2021 (and again on appeal in *Guardian AIT* in late 2022), the Commissioner promptly releases (in February 2022) and then finalises (in December 2022) TR 2022/4; and
- most recently, on 24 January 2023, the Full Federal Court released its reasons for the decision in the *Guardian AIT* appeal, in which it held that the taxpayer was wholly successful on s 100A, but fell somewhat short in respect of the general anti-avoidance provisions.

Where to from here?

So where does that leave us in February 2023?

Other than waiting with bated breath to see whether the Commissioner seeks special leave to further appeal *Guardian AIT* up to the High Court, and awaiting the outcome of the *BBlood* appeal (to be heard in March of this year), we, as the taxpayer adviser community, still only have somewhat limited judicial guidance on the application of s 100A (remembering, of course, that the Commissioner's published views are not law).

Section 100A in its own words

In its current form,[13] the operative provisions of s 100A read as follows:

> "**100A Present entitlement arising from reimbursement agreement**
>
> (1) Where:
>
> (a) apart from this section, a beneficiary of a trust estate who is not under any legal disability is presently entitled to a share of the income of the trust estate; and
>
> (b) the present entitlement of the beneficiary to that share or to a part of that share of the income of the trust estate (which share or part, as the case may be, is in this subsection referred to as the ***relevant trust income***) arose out of a reimbursement agreement or arose by reason of any act, transaction or circumstance that occurred in connection with, or as a result of, a reimbursement agreement;
>
> the beneficiary shall, for the purposes of this Act, be deemed not to be, and never to have been, presently entitled to the relevant trust income.
>
> (2) Where:
>
> (a) apart from this section, a beneficiary of a trust estate who is not under any legal disability would, by reason that income of the trust estate was paid to, or applied for the benefit of, the beneficiary, be deemed to be presently entitled to income of the trust estate; and
>
> (b) that income or a part of that income (which income or part, as the case may be, is in this subsection referred to as the ***relevant trust income***) was paid to, or applied for the benefit of, the beneficiary as a result of a reimbursement agreement or as a result of any act, transaction or circumstance that occurred in connection with, or as a result of, a reimbursement agreement;
>
> the relevant trust income shall, for the purposes of this Act, be deemed not to have been paid to, or applied for the benefit of, the beneficiary.
>
> …
>
> (5) For the purposes of subsection (1), but without limiting the generality of that subsection, where:
>
> (a) a reimbursement agreement was entered into at or after the time when a person became a beneficiary of a trust estate (whether the person became a beneficiary of the trust estate before or after the commencement of this section); and
>
> (b) the amount (in this subsection referred to as the ***increased amount***) of the share of the income of the trust estate to which the beneficiary is presently entitled exceeds the amount (in this subsection referred to as the ***original amount***) of the income of the trust estate to which the beneficiary would have been, or could reasonably be expected to have been, presently entitled if the reimbursement agreement had not been entered into or if an act, transaction or circumstance that occurred in connection with, or as a result of, the reimbursement agreement had not occurred;
>
> the present entitlement of the beneficiary to so much of the increased amount as exceeds the original amount shall be taken to have arisen out of the reimbursement agreement.
>
> …
>
> (7) Subject to subsection (8), a reference in this section, in relation to a beneficiary of a trust estate, to a reimbursement agreement shall be read as a

reference to an agreement, whether entered into before or after the commencement of this section, that provides for the payment of money or the transfer of property to, or the provision of services or other benefits for, a person or persons other than the beneficiary or the beneficiary and another person or other persons.

(8) A reference in subsection (7) to an agreement shall be read as not including a reference to an agreement that was not entered into for the purpose, or for purposes that included the purpose, of securing that a person who, if the agreement had not been entered into, would have been liable to pay income tax in respect of a year of income would not be liable to pay income tax in respect of that year of income or would be liable to pay less income tax in respect of that year of income than that person would have been liable to pay if the agreement had not been entered into.

(9) For the purposes of subsection (8), an agreement shall be taken to have been entered into for a particular purpose, or for purposes that included a particular purpose, if any of the parties to the agreement entered into the agreement for that purpose, or for purposes that included that purpose, as the case may be.

…

(13) In this section:

'agreement' means any agreement, arrangement or understanding, whether formal or informal, whether express or implied and whether or not enforceable, or intended to be enforceable, by legal proceedings, but does not include an agreement, arrangement or understanding entered into in the course of ordinary family or commercial dealing."

Consequences

Consideration of s 100A's potential application is not limited to future tax planning. It is also prudent to review distributions of income that have been made in the past as the Commissioner is not bound by any amendment time limits when giving effect to s 100A.[14]

The consequences of triggering s 100A are such that the beneficiary is deemed never to have been entitled to the trust income,[15] which instead triggers a tax liability for the trustee under s 99A ITAA36.

Additional consequences are also triggered where any deductible amounts incurred as part of the reimbursement agreement are made non-deductible,[16] and any trading stock acquired under the reimbursement agreement will be deemed to have a nil cost.[17]

If enlivened, s 100A can apply to:

- the entire amount to which the beneficiary is presently entitled;[18] or
- an increase to the amount to which the beneficiary was otherwise presently entitled.[19]

So, what are we looking for?

Accepting the section at face value, it appears that a transaction requires the following features to enliven s 100A:

- a beneficiary of a trust (not under a legal disability)
- is presently entitled to a share of the income of the trust[20]
- arising:
  - out of a reimbursement agreement, or
  - by reason of any act, transaction or circumstance that occurred in connection with, or as a result of, a reimbursement agreement
- which reimbursement agreement:
  - provides for someone other than the beneficiary, or the beneficiary together with some other person, to benefit from either the payment of money, the transfer of property or the provision of services,[21]
  - was entered into for the purpose of reducing a person's income tax liability (noting that, if any of the parties to the agreement have the requisite purpose, it will be enough),
  - but does not include an agreement entered into in the course of ordinary family or commercial dealing.

Elements of s 100A

Section 100A is a self-executing provision. If the facts satisfy the terms, it will operate without the need for the Commissioner to make a determination or exercise a discretion.

Further, it is worth noting that, even if the circumstances dictate that s 100A does not apply, the possible effect of the general anti-avoidance provisions in Pt IVA ITAA36 should not be overlooked. Remember, Pt IVA does not contain any carve-out or exclusion for "ordinary family or commercial dealings".

A beneficiary of a trust (not under a legal disability)

This enquiry ought to be straightforward enough – read the deed! Perhaps unsurprisingly though, at least a few taxpayers have sought to defend s 100A assessments on exactly this basis.

In the earliest s 100A case, *East Finchley*, the trustee's June 1983 resolution sought to appoint its income to three resident individuals, with the balance to be distributed to 126 relatives who were residents of India in an amount of $585 each. It also resolved to place such amounts to the credit of the beneficiaries in the books of the trust and hold those amounts on their behalf.

Mr Thomas, one of the controllers of the trustee, subsequently travelled to India in July of that year and delivered letters advising the non-resident beneficiaries of their entitlements. In some cases, he obtained signatures from those beneficiaries who acknowledged the distribution and agreed to lend it back to the trustee.[22] No cash exchanged hands. The Commissioner assessed *East Finchley* on the basis that s 100A was triggered.

In 1988, following commencement of the Commissioner's investigation, the trustee borrowed the funds necessary to make the distributions and subsequently paid them.

The Administrative Appeals Tribunal in the first instance upheld the Commissioner's assessment.

On appeal, the taxpayer put to Hill J that the AAT in the first instance should have:

- found that the appointment of income to the non-residents was invalid, such that the trust's default beneficiaries instead became presently entitled. On that basis, the s 99A assessment to the trustee was excessive because it was the default beneficiaries who ought to have been assessed on that income; and
- defined the parameters of the reimbursement agreement.

The case was ultimately remitted to the AAT[23] on these findings of fact, and Hill J did not have to rule on whether s 100A applied. Further, on return to the AAT, the case was decided on matters that were not relevant to s 100A.

While certain elements of Hill J's reasoning have since been distinguished by other decisions (the most negative of which is contained in the *Idlecroft* decision), the following observations remain instructive:

> "[Section 100A] only applies if there exists present entitlement in persons who are beneficiaries of the trust estate ... Thus the logical first step in any case involving the potential application of sec. 100A will be a finding that the persons, whose present entitlement is to be deemed not to have arisen, be in fact persons who, apart from the application of the section, would be, or be deemed to be, presently entitled to income of the trust estate."[24]

> "... it is clear that if the present entitlement is to arise out of a reimbursement agreement the reimbursement agreement must have occurred first before the present entitlement arose."[25]

> "Section 100A(2) does not deem the beneficiaries of the default clause to be presently entitled, their present entitlement if it exists, must arise by force of the fact that they are entitled to demand payment of the income of the trust estate for trust law purposes."[26]

In the *Raftland* decision, the facts were thus. The Raftland Trust was a discretionary trust controlled by the Heran brothers who together controlled the Raftland Trust and the Heran Developments Trust and operated building businesses primarily through Heran Projects Pty Ltd.

In the early 1990s, things were going well and the business was due to derive taxable profits. One of the brothers investigated (via the solicitor) acquiring a loss trust which could be used to absorb the expected profits.

In line with these instructions:

- Raftland Pty Ltd was incorporated and appointed trustee of the Raftland Trust;
- the E&M Unit Trust (the EM Trust) (a trust with accumulated losses of > $4m) was appointed as a beneficiary of both the Raftland Trust and the Hera Developments Trust; and
- the trustee of the EM Trust resigned and Raftland Pty Ltd was appointed.

A series of financial transactions then took place over several years, the result of which was that the Raftland Trust did not include the amounts it purported to distribute to the EM Trust in its taxable income, and the EM Trust used its losses to offset the distributions and recorded a nil taxable income for the relevant years.

The Commissioner issued amended assessments in respect of the 1995, 1996 and 1997 years, assessing Raftland Pty Ltd on the basis that the distributions made to the EM Trust were ineffective.

Following disallowance of the taxpayer's objection, at first instance, the Federal Court dismissed the appeal, finding that the "distributions" by the taxpayer to the EM Trust and the nomination of the EM Trust as a "tertiary beneficiary" were sham transactions that could and should be disregarded.

Kiefel J also held that, in each of the relevant years, s 100A(1) applied so as to disqualify any beneficiary's present entitlement to a share of income of the Raftland Trust and instead have the income assessed to the trustee pursuant to s 99A.

On appeal to the Full Federal Court, while it agreed that the net income was to be assessed pursuant to s 99A, the court founded its conclusion on different reasons (ie not due to the sham argument).

The Full Court found that the nomination of the EM Trust as a tertiary beneficiary of the Raftland Trust was not a sham, but rather was critical to the intentions of those charged with responsibility for establishing the Raftland Trust. It followed that, in each of the relevant years, the trustee of the EM Trust was presently entitled to the whole of the income of the Raftland Trust, if not by force of resolutions, then by force of the default provisions.

On its analysis of s 100A, the Full Court found that a separate side transaction relevant to the streaming of the income to the EM Trust formed the relevant reimbursement agreement and concluded that the trustee was to be assessed on that basis.

The primary difference between the decision at first instance and on appeal to the Full Federal Court concerned the legal effect of the transactions and, in particular, the matter of present entitlement to certain trust income. In that respect, Kiefel J concluded that the entitlement was not as the taxpayer claimed it to be. The Full Court, on the other hand, accepted the taxpayer's case as to the nature of the relevant legal rights, but held that, notwithstanding those rights, s 100A defeated the taxpayer's attack on the assessments.[27]

Due to the differences in reasoning, on appeal to the High Court, the taxpayers had to succeed on its challenge to both lines of reasoning.[28] Spoiler alert ... they didn't.

In finding for the Commissioner, the High Court stated that:

- Keifel J's approach to construing s 100A was correct, namely, that the provisions of the Raftland Trust deed which purported to create an entitlement in the EM Trust as tertiary beneficiary, and the resolutions which purported to reflect that entitlement, were a façade and were contrary to the intentions of the relevant parties.[29] Under the default provisions of cl 3(b) of the Raftland Trust deed, the primary beneficiaries were entitled to the trust income. Her Honour (correctly) went on to consider and apply s 100A on that basis;
- Kiefel J was correct to conclude that s 100A(1) applied, subject to the question of whether s 100A(3A) denied that result. Her Honour held that s 100A(3A) did not apply to deny the application of s 100A(1) because the primary beneficiaries were not beneficiaries in the capacity of trustees of other trust estates;[30] and
- Kiefel J held that the transactions were clearly not in the ordinary course of commercial dealings. Following *Prestige Motors* and *Idlecroft*, her Honour observed that an "agreement" does not have to be legally enforceable and it is not necessary that the beneficiary be a party to it. It is, however, necessary that a reimbursement agreement provide for the payment of money, the transfer of property or the provision of services or other benefits to a person other than the beneficiary.[31]

Presently entitled

Section 100A affects the question of present entitlement to trust income. If s 100A applies to a beneficiary, the beneficiary is deemed not to be presently entitled to income, thereby rendering the trustee liable under s 99A. Section 100A(3A) provides that, in certain circumstances, s 100A(1) does not apply. In order to give effect to ss 99A and 100A, it is necessary to identify the legal rights and liabilities arising from the facts, the decisive question being one concerning the present entitlement to income of a trust estate, bearing in mind s 95A ITAA36 which extends the concept of entitlement to cover the case of a beneficiary who has a vested and indefeasible interest (s 95A(2)).[32]

A concept underpinning the entirety of Div 6 ITAA36, "present entitlement" is not defined by the legislation so its meaning must be derived from the common law.

Effectively, a beneficiary is presently entitled to a share of the income of the trust estate if, and only if, the beneficiary has:

- an interest in the income that is both vested in interest and vested in possession, and
- a present legal right to demand and receive payment of that income.[33]

Practically, this means that the entitlement must be effectively conferred in accordance with the terms of the relevant trust deed, noting the arguments that the taxpayers sought to advance in *Idlecroft* but which did not ultimately impact the application of s 100A due to the operation of a default income clause which resulted in the necessary present entitlement arising.

At a high level, the facts of *Idlecroft* are as follows.

The trustees of each trust were parties to a joint venture with a property developer (the unit trust), which had tax losses. The trustees varied the terms of their deeds to bring the unit trust within their class of discretionary beneficiaries and subsequently made their contributions to the joint venture by making distributions of income to the unit trust, such distributions resulting in the unit trust being presently entitled as a beneficiary to the appointed income within the meaning of s 97(1) ITAA36.

The Commissioner assessed the taxpayers on the basis that the unit trust was not presently entitled to the relevant income as a result of the application of s 100A.

The taxpayers conceded (at first instance) that the joint venture agreements were reimbursement agreements for the purposes of s 100A, but argued that the unit trust was never presently entitled to the relevant income on the basis that the appointments were invalid and ineffective and so s 100A had no application. Instead, the default beneficiaries became presently entitled to the relevant income and the taxpayers were not properly assessable on the income. They pressed this point on reliance of their interpretation of s 100A(5) — effectively arguing that, if the appointments were invalid, the present entitlement of the default beneficiaries under the deed did not arise out of or in connection with the reimbursement agreement but instead as a matter of trust law.

The Full Federal Court disagreed:[34]

> "In the present appeals, the connecting circumstances *between the entitlements of the default beneficiaries came about because the appointments of income designed to give effect to the reimbursement agreement were invalid*. The appointments came into effect because of the existence of the reimbursement agreement. *The act of appointment and the purpose of the appointments were driven by the attempt to exploit and implement the scheme using the reimbursement agreement. But for the existence of that agreement, the appointments would not have been made.* It is not necessary in order to reach this conclusion to give any strained meaning to the language used. The appointment fits squarely within the ordinary and natural meaning of the language.
>
> … *Section 100A(1) is satisfied if an act or circumstance, in this case the invalid appointment, is connected with the reimbursement agreement.*" (emphasis added)

As a result, simply seeking to rely on invalid or ineffective appointments of income as a way *out* of s 100A is unlikely to work.

Arising out of or by reason of a reimbursement agreement

What is a "reimbursement agreement"?

Interpreting a defined term can be tricky. Where a term is defined by the parliament, there is no general legal proposition that you ought to consider the general meaning of a phrase in seeking to determine its meaning within the statute.

In the legislation, we are told that:

- a "reimbursement agreement" "shall be read as a reference to an agreement, whether entered into before or after the commencement of [s 100A], that provides for the payment of money or the transfer of property to, or the provision of services or other benefits for, a person or persons other than the beneficiary or the beneficiary and another person or other persons" (s 100A(7)), and
- "'agreement' means any agreement, arrangement or understanding, whether formal or informal, whether express or implied and whether or not enforceable, or intended to be enforceable, by legal proceedings" (s 100A(13)),

and such agreement must include a purpose of reducing the tax that would have otherwise been paid by a party to the agreement in that year.

In *Prestige Motors*,[35] the taxpayer was a member of a group of companies and carried on a business as a wholesaler and retailer of motor vehicles.

There were two transactions of concern.

Ronald Lyons Australia (Vic) Pty Ltd (RLAV) was an unrelated, insolvent company with tax losses. The RLAV transaction involved the assignment of RLAV's liabilities to a Singapore incorporated company (Cholmondeley). The sum of $1.3m was loaned to RLAV by a group finance company.

Shortly afterwards, a further $1.8m was loaned by that company to RLAV so that RLAV could apply for 93.3% of the B class units in a newly created trust. The trustee of the trust used the money to buy the taxpayer's business. Soon after, the taxpayer became the trustee and made distributions from trust income to RLAV which were offset by prior year tax losses.

In subsequent years, the taxpayer issued units in the trust to National Mutual Life Association Ltd (NMLA). Fixed distributions over a predetermined period were made to NMLA which were treated by it as exempt due to their tax-exempt status.

The Commissioner treated the amounts distributed to RLAV and NMLA as trust income to which no beneficiary was presently entitled, based on the application of s 100A.

The Commissioner argued that the RLAV transaction and the NMLA transactions were reimbursement agreements.

The taxpayer submitted that:

- because the trust did not come into existence prior to entering the RLAV transaction, the transaction was not a reimbursement agreement;
- no amount was reimbursed by RLAV to the taxpayer for its present entitlement to a distribution of income as RLAV was not a party to the agreements which resulted in the sale of the taxpayer's business to the trust; and
- the sale of this business was an ordinary commercial dealing and the profit received by NMLA was consistent with ordinary commercial dealings.

Prestige Motors had sought to contend that the essential indicium of transactions caught by s 100A is that the beneficiary receives income in a tax-free or capital form. In this case, however, Prestige Motors had not been reimbursed for the income forgone by it; rather, it had been paid the purchase price for the business and continued to receive income from the trust. The court considered that Prestige Motor's submission placed too much emphasis on the word "reimbursement", as distinct from the definition of "reimbursement agreement" in s 100A(7).

The Full Federal Court held that the RLAV transaction and the NMLA transactions contained reimbursement agreements as defined. Specifically:

- "there is no doubt that there was an agreement in the sense in which that word is used in s 100A(13) … the elaborate documentation and series of steps … plainly reflected an understanding or arrangement to which a number of companies and persons were parties";
- the purpose can be inferred that one of the parties to the agreement or understanding had the requisite purpose required by s 100A(8) — given the series of steps taken, it was practically doubtless that the parties knew and assented to the fact that the trustee would no longer derive income in its own name and instead the income would be derived through an entity with accumulated losses and continuing deductions. In respect of NMLA, it should be inferred that at least the chairman who made the offers to the introduced beneficiary intended that tax, which would have otherwise been paid by the prior unitholder, would not be paid by it; and
- the definition of "reimbursement agreement" cannot be controlled by the word "reimbursement" — it is not helpful in these circumstances to resort to the ordinary meaning of a defined word or expression.

As seen later in the *BBlood* decision, Thawley J was unable to agree with the Commissioner that "initiation", "planning" or "implementation" can be said to comprise an "agreement" as opposed, for example, to those things comprising evidence from which it might be inferred that an agreement or understanding came into existence or existed.[36]

When will something arise out of a reimbursement agreement?

Whether a benefit arises out of a reimbursement agreement necessarily involves a timing element.

The present entitlement must arise out of a reimbursement agreement or arise by reason of any act, transaction or circumstance that occurred in connection with, or as a result of, a reimbursement agreement.

This was made clear in the recent decision of *Guardian AIT* where Logan J stated that:[37]

> "... nothing in the joint judgment in *Prestige Motors* calls into question the view reached by Hill J in *East Finchley* that the effect of s 100A(1) was that the 'reimbursement agreement' had to precede the present entitlement. Although the conclusion expressed by Hill J in *East Finchley* was given in the original jurisdiction, and is not therefore binding, I would only depart from it if I considered that conclusion clearly wrong. In this instance, looking at the text of s 100A(1), I respectfully consider his Honour's conclusion to be clearly right."

This interpretation was not pressed by the Commissioner on appeal.[38]

It follows then that the reimbursement agreement (remembering that it includes an agreement, arrangement or understanding, whether formal or informal, whether express or implied, and whether or not enforceable, or intended to be enforceable, by legal proceedings) must exist *prior* to the conferring of the present entitlement.

Guardian AIT Pty Ltd (Guardian) was the trustee of the Australian Investment Trust (the AIT), a discretionary trust. Mr Alexander Springer owned all of the issued shares in Guardian and was the principal of the AIT, as well as a beneficiary of such. In each of the relevant income years, Mr Springer was a resident of Vanuatu.

On 27 June 2012, AIT Corporate Services Pty Ltd (AITCS) was incorporated and appointed as a beneficiary of the AIT. Guardian (as trustee of the AIT) was the sole shareholder of the AITCS.

On 28 June 2012, Guardian appointed the balance of the income of the AIT for the 2012 year to AITCS. However, that distribution was not paid to AITCS, creating an unpaid present entitlement (UPE).

In April 2013, AITCS drew on its UPE to discharge its liability to income tax for the 2012 year. In May 2013, AITCS declared a fully franked dividend to its sole shareholder, the AIT. That dividend was paid by reducing the balance of the UPE of AITCS to the income of the AIT from $1,848,145 to nil.

Similar distributions of the AIT income to AITCS occurred in 2013 and 2014, resulting in more UPEs from which the income tax liabilities of AITCS for those years were discharged. In March 2016, AITCS and the AIT entered into a loan agreement in the amount of the balance of the 2014 UPE. In May 2016, the AIT repaid the loan through the transfer of funds to an AITCS bank account.

The Commissioner assessed Guardian as liable to income tax under s 99A(4A) for each of the three years on the basis that s 100A applied.

The Commissioner's position was that Guardian (as trustee) and Mr Springer had reached an understanding that:

- AITCS would be incorporated for the purposes of being made presently entitled to the income of the AIT;
- Guardian would benefit from the amount to which AITCS was made presently entitled; and
- Mr Springer would ultimately benefit from the amount to which AITCS was made presently entitled.

The Commissioner's contention was that this understanding was a reimbursement agreement for the purposes of s 100A.

In addition to the primary income tax assessments issued to Guardian, income tax assessments were also issued to Mr Springer on the basis that Pt IVA ITAA36 was applicable to each year, ie that the steps taken each year constituted a scheme within the meaning of s 177A(1) ITAA36.

In relation to the Pt IVA assessments, the Commissioner's position was that, if the primary scheme had not been entered into or carried out, Mr Springer would, or might reasonably be expected to, have included in his assessable income the amounts of AITCS's assessable income in the relevant years pursuant to s 98A(1) ITAA36.

At first instance, the taxpayer was successful in all respects. The primary judge (his Honour Justice Logan) found that, when this series of transactions occurred in year one (2012), year two (2013) and year three (2014), the elements of s 100A were not enlivened. Nor was there any "tax benefit" obtained by the arrangement so as to enliven Pt IVA, and if there were, the requisite dominant purpose was not to obtain said tax benefit.

On appeal, the Commissioner only sought to challenge the primary judge's findings in respect of the 2013 year and in respect of Pt IVA.

For the reasons summarised below, the Full Court held that:

- s 100A did not apply to the 2013 year;
- Pt IVA did not apply to the 2012 year; and
- Pt IVA did apply to the 2013 year (the reasons of which are outside the scope of this article).

In forming the conclusion regarding s 100A, the Full Court stated that:

- all parties accepted that s 100A requires a reimbursement agreement to exist at or prior to the time by which a beneficiary is made presently entitled to the net income of the trust;
- while it is not necessary that an understanding be enforceable, or that it be intended to be enforceable, in order to constitute an agreement for the purposes of s 100A, the understanding must nevertheless reflect a common intention or consensus existing between at least two parties;
- where the payment of moneys is proposed to be made to the trustee by a beneficiary, the beneficiary ordinarily needs to be a party to the reimbursement agreement, or at least a representative or controller of that beneficiary;
- for an arrangement or understanding to exist, it must be adopted in the sense that it must be assented to, whether expressly or impliedly;
- an arrangement whereby a person would act in accordance with the wishes of another is capable of being an agreement within s 100A(13); and
- by contrast, an expectation that any arrangement will be entered into after the creation of the present entitlement is not sufficient for the purposes of s 100A.

As a result, for s 100A to be satisfied as at 23 June 2013 (ie the date on or before the present entitlement was conferred on AITCS by the AIT), there had to be an arrangement or understanding between two or more parties that the beneficiary would pay a dividend to the AIT. In accepting the evidence at face value, the Full Court went on to confirm that, even if the advisers had held the requisite understanding, there was no basis to impute that understanding onto the controller.

As such, no reimbursement agreement existed on the facts.

A third party who benefits (either alone or with the beneficiary)

As a starting proposition, if:

- a single beneficiary is entitled to all amounts of trust income and capital and is paid those entitlements, and
- that beneficiary retains that income for its own use or benefit,

s 100A ought not to apply as there is no other person, other than the presently entitled beneficiary, who has benefited from that income or any other amount.

Returning to the facts of *Prestige Motors* as outlined earlier, the next question is whether the reimbursement agreements satisfied the terms of s 100A(7), in that they "provide[d] for" the payment of money or the transfer of property to a person or persons other than the beneficiary.

In the case of the RLAV transaction, in the court's view, it seemed that a number of payments or transfers answered the statutory description. Most obviously, the reimbursement agreement contemplated that the parties to it intended that RLAV (the beneficiary that became presently entitled to income) would pay very large amounts of interest to Cholmondeley.

The flaw in Prestige Motor's approach (in the court's view) was that it examined particular elements of the transaction in isolation from the agreement (in the sense of an arrangement or understanding) which gave rise to the transaction as a whole.

Instead, the inquiry required by s 100A(7) is whether there was an agreement in relation to the beneficiary of a trust estate (RLAV) that provided for the payment of money to a person (Cholmondeley) other than the beneficiary.

A party with purpose

The inquiry into purpose is two-fold.

First, s 100A(8) directs you to determine the actual purpose of entering into the relevant agreement. Specifically, the reimbursement agreement must have been entered into for the relevant "tax avoidance" (read tax reduction) purpose.

Then, s 100A(9) requires reference to an actual purpose of one or more of the parties to the agreement in entering into the agreement.[39] This operates by deeming ("shall be taken") s 100A(8) to be satisfied if the relevant purpose was "a" purpose of a "party to the agreement".

This onus is not discharged simply by being able to point to some other transaction which realistically could have been entered into and which would not have immediately caused a person to be liable to more tax.

The existence of another purpose, or other purposes, does not prevent s 100A from being enlivened. Unlike Pt IVA, s 100A does not require this purpose to be a sole or dominant purpose. Taxpayers who attempt to rely on the judicial construction of provisions in Pt IVA in support of why the requisite purpose did not exist will fail. While Pt IVA is couched in terms of dominant purpose, the threshold for s 100A is far lower and therefore not analogous.

The requisite purpose and who may hold it was illustrated in the recent *BBlood* decision.

The circumstances in the case involved a share buy-back from a discretionary trust, whereby the amount taken to have been paid as a fully franked dividend (ie because of the tax law treatment of the buy-back) was characterised by the trustee as capital of the trust, and did not form part of the income of the trust estate for trust law purposes.

All of the income of the trust estate (determined in accordance with ordinary concepts) in the income year (which did not include the buy-back dividend) was distributed and paid to a single company beneficiary which used that income for their own benefit. The buy-back dividend was retained as corpus of the trust.

As all of the trust law income was distributed to the corporate beneficiary, it was also assessed in respect of that same share of tax law income (ie 100% of the buy-back dividend) which, being a deemed fully franked dividend, did not attract additional top-up tax.

The Commissioner applied s 100A to the distribution of the trust income so that no beneficiary was treated as presently entitled to it for tax law purposes. As there was no share of trust law income to which any beneficiary was presently entitled, there was no corresponding share of tax law income (which did include the buy-back dividend) on which any beneficiary was assessable.

When determining purpose (and indeed whose purpose), his Honour confirmed that:

- contemporaneous documents are often probative and carry greater weight than ex post facto subjective evidence about purpose;[40]
- the reference to the "parties to the agreement" in s 100A(9) must be understood having regard to the operation of the whole section. Section 100A(13) defines "agreement" broadly and so "parties" to the agreement is not to be literally interpreted as the signatory or named parties to a legal document. Instead, it extends to all those parties involved in the broader reimbursement agreement and can therefore extend to advisers;[41] and
- the construction of s 100A(8) should not be constrained by the construction of provisions in Pt IVA. Reference to "alternative postulates", "counterfactuals", "reconstruction" and "annihilation", and drawing analogies between the statutory scheme in s 100A and that in Pt IVA, risks distracting attention from the text and scheme of s 100A.[42]

Practically, even in circumstances where a court may accept that the underlying family group controller may not have fully appreciated the technical nuances of the reimbursement agreement as a whole, if the evidence shows that the advisers had the requisite purpose, once this is explained to, understood and adopted by the individual controller and the entities he controlled, he too will have that purpose.

Not an ordinary family or commercial dealing

As a starting point, the expression "ordinary family or commercial dealing" is not defined in the tax Acts. It is widely accepted that this language is adapted from Lord Denning's reasons in *Newton v FCT*[43] where, in considering the application of s 260 of the former tax Act (a general anti-avoidance provision), he stated:

> "In order to bring the arrangement within the section you must be able to predicate – by looking at the overt acts by which it was implemented – that it was implemented in that particular way so as to avoid tax. If you cannot so predicate, but have to acknowledge that the transactions are capable of explanation by reference to ordinary business or family dealing, without necessarily being labelled as a means to avoid tax, then the arrangement does not come within the section."

The court in *Prestige Motors* held that transactions were not entered into in the course of ordinary commercial dealings because there was no commercial motivation for the sale of the business and it was merely one element of a larger one-off transaction designed to avoid tax. In relation to the NMLA transactions, no commercial reason for raising capital outside the group was demonstrated.

In *Guardian AIT,* Logan J did not attempt to confine his analysis to examples of what would be considered to be "family or commercial", but emphasised the consistency with *Newton's* case and the later case of *Rippon v FCT*[44] that it was not meant to apply to transactions that are "ordinary" in contradistinction to "extraordinary". It refers to a dealing which contains no element of artificiality.[45] On appeal, the Full Court did not need to consider Logan J's application because it ultimately held that s 100A did not apply to any of the relevant years.

In *BBlood*, Thawley J considered that the absence of the following factors may help to determine what is *not* an ordinary family or commercial dealing:[46]

- "commercial motivation";
- "commercial justification", leaving "the only explanation for the entry into the agreement as the elimination or reduction of tax liabilities"; and
- "commercial necessity or justification for the transaction" or "commercial reason to raise capital from outside the group".

It remains to be seen whether these comments are overturned or expanded in the appeal.

The Commissioner's views on "ordinary family or commercial dealing" are found in TR 2022/4:

> "105. The core test involves an inquiry into what the objectives of the dealing are, whether the transactions achieve that objective and whether they are better explained by achieving some other objective. The test is applied on the facts of each case and to the whole of the dealing within which the agreement has been entered into 'in the course of'. In applying the test:
>
> - elements of contrivance or artificiality are factors which point against an agreement being entered into in the course of ordinary family or commercial dealing
> - while complexity can be a necessary feature of transactions to achieve family or commercial objectives, an arrangement that is overly complex or lacking justification to achieve those objectives is a factor that will point against the agreement as having been entered into in the course of ordinary family or commercial dealing, and
> - the presence of other features which show that the arrangement is clearly tax-driven may also indicate that an arrangement is more properly explained by other objectives instead of family or commercial objectives."

The Commissioner appears to accept that the absence of dealings at arm's length or market value will not, by itself, prevent a dealing from being a commercial dealing.[47]

In the *Guardian AIT* appeal, there was no cause to consider Logan J's comments on the exclusion, given that the Full Court agreed that the agreements did not exist due to the lack of connection between timing. It remains to be seen how Thawley J's approach will be considered on appeal.

We shall leave the concluding comments on the exclusion with the court in *Prestige Motors*:

> "It is not to the point, in our opinion, that the interest payments to Cholmondeley, if viewed in isolation, might be thought to be consistent with ordinary commercial dealing. The question posed by s 100A, especially subs (13), is whether the agreement was entered into in the course of ordinary commercial dealing, not whether a particular element in a transaction implemented pursuant to that agreement could be so characterised.
>
> Similarly, it is not a ground for resisting the application of s 100A to characterise the sale of the Business by Prestige to LSP, as trustee of the Trust, as one made in the course of ordinary commercial dealing. The question is not whether that sale, viewed in isolation, could be seen as an ordinary commercial dealing. It is whether the agreement or understanding, which provided for a large number of dealings including the sale of the Business, was entered into in the course of ordinary commercial dealing …
>
> Section 100A(13) does not make it explicit how the issue is to be determined when what is said to be a reimbursement agreement involves parties which have dealt at arm's length with those whose purpose is to avoid liability to pay income tax. In our view, the question is to be addressed, at least principally, from the point of view of those who have that purpose."

The ATO's stated views

While not the focus of this article, it would be remiss of us to not at least mention the ATO's view of the world (given the recency of its publications), and it will be interesting to see whether any further changes are adopted by the Commissioner to the rulings discussed below in light of the commentary that is now available from the Full Federal Court in *Guardian AIT*.

TR 2022/4

TR 2022/4 contains the Commissioner's public analysis of when an "arrangement" (for the purposes of s 100A(13) ITAA36) will be a "reimbursement agreement" (for the purposes of s 100A(1) ITAA36).

The Commissioner proposes that four basic requirements must be satisfied for s 100A to apply:

1. there must be a connection between the present entitlement conferred on a beneficiary and the identified reimbursement agreement ("connection requirement");
2. there must be a benefit to someone other than the beneficiary ("benefit to another requirement");
3. one or more of the parties to the agreement must have a purpose of reducing the tax otherwise payable by a person in that year of income ("tax reduction purpose requirement"); and
4. the agreement must not otherwise be one entered into the course of an ordinary family or commercial dealing ("ordinary dealing exception").

PCG 2022/2

PCG 2022/2 contains the detail, by reference to a risk matrix, of what types of transactions, or features of transactions, are likely to enliven compliance activity by the Commissioner in a client's circumstances.

Protection afforded by public rulings

A public ruling is written binding advice, published by the Commissioner for the information of entities generally, on the way in which, in the Commissioner's opinion, a relevant provision applies or would apply to entities generally, or a class of entities.[48] A public ruling binds the Commissioner if the public ruling applies to the entity and the entity relies on it. An entity relies on a public ruling by acting (or omitting to act) in accordance with the public ruling.

If a taxpayer follows the Commissioner's advice and it later turns out to be incorrect, he will take this into account when determining what, if any, action he should take. In the context of a taxation ruling, this includes protection from income tax shortfall, interest and penalties. For a practical compliance guideline, this means no protection from a tax shortfall but protection from interest and penalties if reliance can be shown to have been in good faith.

So, while practitioners advising in relation to trust distributions should use these tools to evaluate the risk of the Commissioner seeking to apply s 100A in their client's circumstances, they should not be used as a substitute for either the words of the statute, nor the interpretation by the courts.

Risk level	Risk zone	Description and compliance approach
Low risk	White zone	The Commissioner will not commence new compliance activities to consider the application of s 100A for income years ended before 1 July 2014, unless: • the arrangement does not fall within the "green zone"; and • the Commissioner is otherwise considering the income tax affairs for those years; or • the arrangement entered into continues before and after 1 July 2014.
Low risk	Green zone	The green zone applies to arrangements that are described in paras 20 to 30 of PCG 2022/2. In essence, the ATO will not dedicate resources to investigate distributions that are: • paid to jointly held bank accounts, superannuation fund contributions or charities; • paid to the beneficiary within two years of becoming entitled and used by the beneficiary; • made to beneficiaries that fall within the family group (per family trust election definitions) but are otherwise retained by the trustee because it has working capital or investment requirements and the terms of the retention are on "commercial" (ie Div 7A equivalent) loan terms; or • made as part of an arrangement in the course of an ordinary family or commercial dealing. Notwithstanding the above features, there are also several other matters in para 32 of PCG 2022/2 which will knock you out of a green zone scenario.
High risk	Red zone	The red zone applies to arrangements that are described in paras 34 to 48 of PCG 2022/2. If applicable, further analysis and review activity should be expected as a matter of priority. Examples of red zone arrangements include: • the present entitlement is lent or gifted to a third party; • the income distribution is returned by the beneficiary to the trust in the form of assessable income; • in the context of unit trusts: UPEs are created and then units are issued, with the issue price set off against UPEs (ie where the UPEs exceed the market value of the units); • mismatches between trust income and tax income; and • streaming entitlements to loss entities are outside the family group.

The 10 commandments

To summarise, the key takeaways that the authors can distil from the cases are:

1. there must be present entitlement in a beneficiary (not under a legal disability) of the trust;
2. the reimbursement agreement must have been formed both before (or at least at the same time as):
   a. the present entitlement was conferred; and
   b. the payment was made to the third party,

   but the subject trust does not necessarily need to exist before the reimbursement agreement was formed;
3. "reimbursement" in the ordinary sense is not relevant to the enquiry of what makes up a reimbursement agreement;
4. a reimbursement agreement is not required to be legally enforceable in the ordinary sense, it is merely a convenient label. It does, however, require a common understanding or consensus between at least two parties;
5. the purpose enquiry is two-fold:
   a. whether the reimbursement agreement is one which was entered into for *the purpose* of securing that a person pay less tax than the person would have if the agreement had not been entered into; and
   b. whether any party to the reimbursement agreement had *a purpose* (whether or not among other purposes) of securing the imposition of less tax;
6. if, in all relevant respects, a reimbursement agreement exists, there are only two exclusions:
   a. the agreement and no party to it had the relevant tax purpose (albeit this is fairly limited); and
   b. it was entered into in course of an ordinary family or commercial dealing;
7. in respect of the latter, that one aspect of arrangement is capable of explanation as ordinary or commercial is not the point – every step of the reimbursement agreement must be capable of that explanation;
8. understanding purpose is not to be constrained by reference to the construction of Pt IVA;
9. s 100A is just one tool in the Commissioner's anti-avoidance belt! Do not let it distract you from a more global enquiry of a client's circumstances; and
10. complexity does not equate to artificiality, but multiple "ordinary" steps do not guarantee an absence of artificiality.

Elizabeth Allen
Special Counsel
Macpherson Kelley

John Ioannou, CTA
Principal Lawyer
Macpherson Kelley

References

1 M Butler, "The increasing use and threat of section 100A", (2020) 24(2) *The Tax Specialist* 45; P Sokolowski and K Lowdon, "Plato's cave: trusts, section 100A and the reality behind the shadows", paper delivered at The Tax Institute's October 2018 Breakfast Club.

2 Treasury, *A brief history of Australia's tax system*, 2006. Available at https://treasury.gov.au/publication/economic-roundup-winter-2006/a-brief-history-of-australias-tax-system.

3 For example: *Curran v FCT* [1974] HCA 46; *Mullens v FCT* [1976] HCA 47; *Slutzkin v FCT* [1977] HCA 9; and *Cridland v FCT* [1977] HCA 61.

4 A Myers, *Tax avoidance and the High Court since Sir Garfield Barwick*, 2005. Available at https://law.unimelb.edu.au/__data/assets/pdf_file/0005/1585994/2005-Myers1.pdf.

5 A Evans, "Why we use private trusts in Australia: the income tax dimension explained", (2019) 41(2) *Sydney Law Review* 217.

6 Treasurer's press release, 11 June 1978.

7 *East Finchley Pty Ltd v FCT* [1989] FCA 720 (*East Finchley*).

8 *FCT v Prestige Motors Pty Ltd* [1998] FCA 221 (*Prestige Motors*).

9 *Idlecroft Pty Ltd v FCT* [2005] FCAFC 141 (*Idlecroft*).

10 *Raftland Pty Ltd as trustee of the Raftland Trust v FCT* [2008] HCA 21 (*Raftland*).

11 *Guardian AIT Pty Ltd ATF Australian Investment Trust v FCT* [2021] FCA 1619 at [22] (*Guardian AIT*).

12 *BBlood Enterprises Pty Ltd v FCT* [2022] FCA 1112.

13 The most significant modification was in 1981 to address and overcome modifications on the original mischief by using a chain of trusts.

14 S 170(10) ITAA36.

15 S 100A(1) ITAA36.

16 S 100A(6A) ITAA36.

17 S 100A(6B) ITAA36.

18 S 100A(1) ITAA36.

19 S 100A(5) ITAA36, and including a present entitlement arising under ss 101 to 100A(6) ITAA36.

20 Including a present entitlement arising under s 101 (per s 100A(2) ITAA36), and including a beneficiary who is a trustee of sub-trust (s 100A(3) ITAA36) and captures chains of trusts s 100A(3A) and (3B) ITAA36.

21 Including by way of loan (s 100A(10) ITAA36) or by forgiving/failing to demand payment of a debt (s 100A(12) ITAA36).

22 Unfortunately, those letters could not be tended as evidence as they were lost.

23 *Case* X40, 90 ATC 342.

24 *East Finchley* at [44].

25 *East Finchley* at [72].

26 *East Finchley* at [89].

27 *Raftland* at [7].

28 Ibid.

29 *Raftland* at [53].

30 *Raftland* at [63].

31 *Raftland* at [61].

32 *Raftland* at [3].

33 See the High Court decision of *Harmer v FCT* [1991] HCA 51 at [8], quoted by the High Court in *FCT v Bamford* [2010] HCA at [37] and in *FCT v Carter* [2022] HCA 10 at [3].

34 *Idlecroft Pty Ltd v FCT* [2005] FCAFC 141 at [45] and [46].

35 [1998] FCA 221.

36 [2022] FCA 112 at [88].

37 [2021] FCA 1619 at [129].

38 *FCT v Guardian AIT Pty Ltd ATF Australian Investment Trust* [2023] FCAFC 3.

39 [2022] FCA 1112 at [130].

40 [2022] FCA 1112 at [136].

41 [2022] FCA 1112 at [137].

42 [2022] FCA 1112 at [153].

43 [1958] UKPCHCA 1 at [15].

44 [1992] FCA 487. This was a later case on s 260 of the then ITAA36.

45 [2021] FCA 1619 at [144].

46 [2022] FCA 1112 at [97].

47 Para 102 of TR 2022/4.

48 Para 4 of TR 2006/10.

Chartered Tax Adviser

[ch-ah-ted taks ad-vahy-zer] Noun. Designation: CTA

1. a designation representing the highest standard for tax advisers
2. a practitioner with the proven ability to effectively communicate expert tax advice to clients
3. your next career opportunity.

Our Chartered Tax Adviser Program gives you the skills and confidence to rise to the top of your tax career. If you're an experienced tax practitioner with prior learning and relevant experience, you may be eligible to enrol directly in the final subject – CTA3 Advisory.

Learn through practical case studies

Through the use of in-depth case studies, CTA3 Advisory allows you to learn by researching the law, assimilating and synthesising information and exercising professional judgement to develop and communicate client advice.

This practical course directly reflects work you'll do as a leading tax professional.

Study how it suits you

Study in a way that suits your skills, experience and lifestyle. Choose from:

Online: peer discussions through four facilitated online group sessions. Commencing on 24 April.

Online Intensive: the same facilitated online discussion sessions, over a shorter timeframe. Commencing on 17 July.

Assessment-only: already acquired in-depth knowledge and client advisory skills? Progress directly to the CTA3 Advisory assessment.

23-007EDU_03/23

Call today on 1300 829 338 or submit an enquiry online

CTA3 Advisory early bird discounted pricing ends on 24 March. Enrol now to save $100

The Tax Institute

HEPCO Pty Ltd trading as The Tax Institute Higher Education PRV14349.

The life cycle of a tax dispute with the ATO

by Adam Ahmed, Solicitor,
Adam Ahmed & Co

The taxpayer navigates through the well-defined sea that is the tax dispute resolution process towards an inevitable outcome, with the hope it may lead to where they wish to go. The ATO has navigated this course on a number of occasions, and the taxpayer perhaps just once: a fact that dawns on the taxpayer oft too late. For the key to navigating this course lies not in the map – which everyone has – but in knowing the conditions that one faces when they set course. A map does not show the conditions of the wind, the heat, the existence of traps and distractions, or the same one-liners at each step of the process. After navigating this course a number of times, one develops a feeling for its rhythm, and it becomes predictable. This is what this article shares.

Every year, around two million individuals and small businesses are contacted by the ATO about their tax returns, and many find themselves in a dispute over the amount of taxes owed through an audit.[1]

The general process for a dispute in relation to an assessment of a small business follows this structure:

1. a potential problem will be identified by the ATO, often via data checking;
2. the dispute will begin at an audit;
3. if the audit results in an unsatisfactory outcome, the taxpayer will have the option to object and, in some cases, seek an independent review if it is offered;
4. if the independent review is offered and taken, and leads to an unsatisfactory outcome, the next step will be to object; and
5. if the objection is disallowed or the result is otherwise unsatisfactory, the next step is to appeal to the AAT or the Federal Court.

This article discusses the practical elements of each of the above steps, illustrating that the further along the dispute is, the more challenging it is for the taxpayer to achieve an effective resolution. It then concludes by providing recommended principles in communicating with the ATO to increase the chances of a satisfactory result.

Since the process differs across various disputes, it is of note that this article will only cover disputes concerning audit-initiated assessments, and not objections against private rulings or other actions which are not assessments. It will also only look at the ATO's approach towards small and medium-sized businesses, which notably differs from its approach towards large and international businesses.

ATO's identification of a problem

The ATO usually conducts audits if an issue has been flagged or if more information is needed.[2] Data matching is one technique that the ATO uses to find potential issues.[3] The process helps to identify discrepancies between the income and tax information reported by taxpayers and that held by third parties, such as financial institutions, employers and government agencies.[4] For example, data matching might show large deposits into a bank account without a corresponding recognition of income by the owner.

Another example could be that the information provided by a taxpayer may indicate financial performance outside of industry benchmarks. In such cases, the ATO may initiate an audit to understand why this is the case and to ensure compliance with tax laws. This will typically affect businesses that receive all or part of their income in cash.

Cash payments are particularly difficult for both the ATO and the taxpayer. The ATO has no certain way to determine, and the taxpayer has no way to prove, that all of the cash sales went through the register. Ultimately, the onus lies with the taxpayer to prove that the calculation of their taxes is correct.[5]

Another illustration might be that the business has ownership of motor vehicles but has not lodged a fringe benefits tax return, or single-touch payroll data might show that superannuation appears to have been paid incorrectly.

The ATO data-matching opportunities are practically limitless. As technology evolves, the horizons will expand even further. For example, it is the author's view that the ATO will start to access data from cloud-based accounting software providers such as Xero, MYOB and Quickbooks directly, the same way that they currently access bank data.

However, data matching is not the only way an audit may arise. For example, audits may also be conducted following escalation from a retention audit (which verifies whether a GST refund or an R&D tax incentive should be paid), or for other reasons.

The beginning of an audit

After a taxpayer has been flagged, it will usually be classified as a review and the ATO will do some further investigations. This can take the form of seeking data directly from other sources, such as the taxpayer's bank. The ATO will also usually contact the taxpayer to give them an opportunity to amend their tax returns.

If the taxpayer passes up this opportunity, ignores the communication or responds unsatisfactorily, the matter will then be escalated to an audit.

At this stage, the auditor may issue notices for the provision of specific information, depending on the level of cooperation demonstrated by the taxpayer.[6] However, it is important to note that the ATO often possesses a substantial amount of information already, and the notices sometimes serve as a means of evaluating the credibility of the taxpayer by comparing the information provided with that already held by the ATO.

The process of evaluating credibility can also include questioning, attempts to unsettle the taxpayer, or even befriending them. Common techniques include having more ATO officers attend a meeting than was expected, sudden changes from what was organised (such as bringing a USB stick to a meeting and asking for a download of information), and suggesting that they may issue certain notices. All the while, the ATO will be observing the taxpayer's reaction and forming a view on credibility.

Another important element is that the auditor usually has strict timelines to complete the audit, as they try to complete reviews and audits in the shortest possible time.[7] This is ostensibly to the taxpayer's benefit but usually exacerbates the situation in practice as it can lead to a rushed conclusion of the audit, resulting in a suboptimal outcome for the taxpayer.

Independent review

The auditor will eventually reach a conclusion regarding the audit. In some situations, the auditor may present a draft position paper for the taxpayer's review and response. In other cases, the auditor will finalise the audit.

In the latter situation, the taxpayer may have the option of an independent review but there is no guarantee that this will be offered because it is an ATO-developed program as opposed to being within the statutory framework.[8]

The original audit team needs to provide consent for the independent review process to function. This process involves a separate ATO officer reviewing the decision made by the audit team. The independent reviewer will take into account the final positions of both parties and then form a view before amended assessments are issued. They may request additional information or base their review solely on the information already available.

During this time, the assessments are not supposed to be issued, which is why the consent of the audit team is needed because nothing precludes the audit team from issuing an amended assessment at any time.

If an amended assessment has been issued by the audit team, it cannot be reversed because to do so would require the ATO to form the view that the original assessment was correct, therefore requiring the matter to now be dealt with at objection and rendering the independent review process otiose. This can and does happen on occasion.

The independent review process shares some similarities with the in-house facilitation process in that its objective is to resolve disputes with the ATO. The in-house facilitation process, which aims to mediate the position between the taxpayer and the ATO, can be requested at any point during the dispute, but acceptance by the ATO is necessary.[9] The ATO may decline the request, and will often do so, stating that no dispute exists as its position is clear and, therefore, no further facilitation is required.

The degree of cooperation exhibited by an audit team during either of these processes is often influenced by the duration of the dispute and the workload of the department. Generally, as the workload of the department increases, the less likely they will be to accept these processes. It is also affected by the extent to which members of that department interact directly with taxpayers.

In an odd twist, it is usually the departments where communication difficulties and misunderstandings are likely to be at their greatest – such as departments where work is pooled and shared, and that have limited interaction with taxpayers – that will reject the facilitation. These departments also tend to be the busiest.

Finalisation of the audit

In the context of this article, it is assumed that the outcome of the audit is unsatisfactory. Typically, the ATO will issue a standard letter that communicates the following:

1. the taxpayer falls short of the standards expected;
2. the taxpayer's records are unreliable;
3. the ATO has attempted to cooperate with the taxpayer, but the latter has not been cooperative;
4. the ATO will now proceed to determine the tax owed and has done so using the method outlined in the letter, which is deemed to be the best course of action under the circumstances;
5. in some instances, the letter may imply that a concession or favourable treatment has been applied, for example, instead of the additional tax of $1m, the revised assessment is for $900,000, which implies a discount of $100,000 due to the information provided by the taxpayer; and
6. it follows that a penalty will be imposed given the aforementioned circumstances.

The letter issued by the ATO is largely a standardised template that is tailored to the specific facts and circumstances of the audit.

Take point 1, for instance: if the taxpayer claims to have accounting experience, the letter will state that, as an accountant, they should have been aware of the requirements.

On the other hand, if the taxpayer claims to have no accounting experience, the letter will state that it was their responsibility as a director to engage an accountant.

In cases where the taxpayer claims to have engaged an accountant but that the service was unsatisfactory, the ATO will assert that the taxpayer has acknowledged that their accounts were not prepared to an acceptable standard, and therefore suggests that the taxpayer agrees with the ATO's position.

Point 3 is usually accomplished by listing all of the occasions that the ATO tried to call the taxpayer but the taxpayer did not answer the phone.

The audit officer will also typically inform the taxpayer that they have the right to object to the outcome if they disagree with it and, to the eternal frustration of the objection team, suggest that the objection process will function as a continuation of the audit, with the objection officer considering anything else they have to say.

This promise will usually give the taxpayer enough comfort to allow the audit officer to close the file. What is not mentioned is that a debt will be created on the taxpayer's account which will cause problems when the taxpayer seeks to obtain finance from a bank.

The objection process

Once a taxpayer submits an objection, it is assigned to an objection officer. There are specific time limits for lodging objections.[10] However, it is often possible to request an extension of time and the ATO usually grants an extension unless there are valid reasons not to.

The objection officer will typically review the audit file and attempt to gain an understanding of what occurred during the audit. However, it is often challenging for the taxpayer as the negative portrayal of the taxpayer in the audit finalisation letter often creates a poor initial impression. Additionally, the objection officer is being asked to overturn a decision made in relation to a taxpayer who is perceived to be below the standard expected of a taxpayer.

The objection officer usually avoids conducting a complete or partial re-audit, considering that all information should have been provided during the original audit and that their role is to review the audit decision on technical grounds. This viewpoint differs from that of the audit officer, who may suggest that the objection officer will be willing to re-examine any new information provided. It is crucial to keep this in mind as the consequences (and disadvantages) of a refusal by the objection officer to engage in a detailed review fall on the taxpayer.

In the objection process, it is not particularly beneficial to focus on the mistakes made by the audit officer or their perceived shortcomings. Usually, this seems like an attractive course of action when the audit finalisation letter is inflammatory. However, the primary concern at this stage should be determining the correct tax bill and the reasons behind it.[11]

This approach allows for the inference that the auditor overlooked certain items or misinterpreted the law, rather than making it the primary focus. This may also be counterintuitive to the way that grounds of review might ordinarily be written.

There may be instances where the objection process takes an extended period to resolve. In such cases, the taxpayer can issue a notice under s 14ZYA TAA53 to the ATO. However, if the ATO fails to comply with the notice, it will result in the objection being disallowed and the dispute will need to be taken to the AAT or the Federal Court.

Administrative Appeals Tribunal

If the taxpayer is dissatisfied with the objection decision, they have the right to appeal to the AAT or the Federal Court.[12]

This article will focus on the AAT as opposed to the Federal Court. Most small to medium-sized businesses will likely proceed with the AAT due to it being a non-cost jurisdiction that undertakes a merits review. There is also a specific division for small business taxation.

As disputes reach the AAT stage, the attitude is that this issue has already been reviewed twice before – first during the audit and then during the objection process. This is now the third review. The ATO will typically assign an internal solicitor to handle the case, who will likely have multiple cases to handle and may not be inclined to consider additional information or conduct a new audit.

The burden of proof is on the taxpayer to prove their case.[13] It can be challenging for taxpayers to meet this burden of proof. Many taxpayers may attempt to explain why the objection decision was incorrect, but this approach is likely to result in a loss for the taxpayer as it does not provide the AAT with any new information to work with. The approach at this stage should be a clear and positive explanation of the correct tax amount, supported by evidence.[14]

At first instance, the ATO will prepare and file T-documents, which include all relevant documents related to the case, including correspondence and information provided by the taxpayer, as well as information obtained from third parties.

The AAT conducts an initial phone call with the taxpayer to understand the case and, if possible, to set a timetable for each party to provide the necessary documents to the AAT and each other. These documents include the statement of facts, issues and contentions (SFIC) which is a summary of the position and facts relied on, and any evidence relied on.

The AAT is typically busy, so it may ask the taxpayer to file their SFIC and evidence together and to do so within four weeks. This is usually not enough time unless it is a narrow issue. There is an assumption that everything will be ready, given the material was already prepared at objection. As with objection, the process assumes that the previous stage was completed perfectly.

Requesting extra time will require an explanation as to why this assumption is not correct in this instance, and it will usually be opposed by the ATO. The ATO will usually file a response four weeks after the taxpayer files their SFIC and evidence.

The process and documents filed may vary, such as the taxpayer filing a reply or additional evidence, or orders for alternative dispute resolution, such as conciliation.

The ATO will usually argue that there is insufficient evidence to support the taxpayer's case. The ATO does not need to defend the objection decision but only needs to show why the tax calculation proposed by the taxpayer is incorrect.

Some taxpayers do not provide an alternative calculation and focus on why the ATO is incorrect. Although the AAT may agree that the objection decision was not perfect, it will have nothing to replace it with. If there is no alternative calculation provided by the taxpayer, the objection decision is likely to stand. Consistency from the taxpayer is crucial, as any inconsistencies may weaken the taxpayer's case.

The ATO is typically reluctant to attend conciliation unless it believes that there is a possibility of changing its position. However, conciliations usually follow a similar script, where the ATO argues that there is not enough evidence to change its position. Sometimes this is due to a lack of awareness of the evidence provided, making conciliation a useful way for the ATO to become informed.

> "To increase the chances of a favourable outcome, the taxpayer should present their best case from the outset."

The ATO officers present at conciliation usually do not have the authority to settle on the day of conciliation as these decisions need to be made by higher-level officers and approvals need to be obtained first. Therefore, conciliation should be approached as an opportunity to review the material with the ATO, and the conversation can continue after that.

If the matter proceeds to a hearing, the ATO will typically raise different concerns with the evidence or material. The ATO takes an adversarial rather than a constructive approach to calculate the correct tax and believes that it is the AAT's responsibility to form its own view. It will aim to provide the AAT with different problems to consider which would make it difficult to accept the taxpayer's calculation, rather than addressing the points made by the taxpayer.

The great irony is that taxpayers frequently seek to cast doubt on the ATO's decision, but often it is not effective and will result in an ATO victory, whereas the ATO can and does seek to cast doubt on the taxpayer's calculations and this is often effective. This is because, ultimately, the ATO's position is correct by default, unless the taxpayer can prove that an alternative is preferred. Specifically, the taxpayer has to actively provide a tax position and calculation and positively prove that it is correct, while the ATO does not have this burden.

Conclusion and the best way to proceed

In summary, the process generally starts with the ATO identifying a problem, often via data matching. It will then begin an investigation, which often leads to an audit. If the audit results in an unsatisfactory outcome, the taxpayer sometimes has the option to seek an independent review, but will always have the option to object. If the objection is disallowed, the taxpayer will also have the option to appeal to the AAT or the Federal Court.

It is evident in the discussion above that, as the process progresses, it becomes increasingly challenging for the taxpayer to achieve their desired outcome. The objection stage in particular can be difficult, as the objection officer may have a negative portrayal of the taxpayer and their case.

Should the objection result in an unsatisfactory outcome, the situation becomes even more challenging as the AAT assumes that the ATO's position is correct unless the taxpayer can prove otherwise.

To increase the chances of a favourable outcome, the taxpayer should present their best case from the outset. An understanding of the ATO's procedures and behaviours discussed in this article can aid in planning and communication strategies.

The goal should be to effectively address any issues raised by the ATO while avoiding any additional concerns. Building and maintaining a reputation as a credible and compliant taxpayer is key, and this can be achieved by providing accurate and honest responses to any questions asked.

Importantly, if a taxpayer is uncertain of the correct answer, it is better to admit that than to provide an incorrect response. The ATO will verify the information against its records, and providing inaccurate information may damage the taxpayer's credibility and reliability, sometimes irreparably.

Adam Ahmed
Solicitor
Adam Ahmed & Co

References

1 Australian Taxation Office, *Stress less if you have nothing to confess*. Available at www.ato.gov.au/misc/downloads/pdf/qc60201.pdf.

2 Australian Taxation Office, ***Audits***. Available at www.ato.gov.au/Business/Privately-owned-and-wealthy-groups/What-you-should-know/Tailored-engagement/Audits/#Typicalauditprocess.

3 Australian Taxation Office, *Data matching*. Available at www.ato.gov.au/about-ato/commitments-and-reporting/information-and-privacy/data-matching.

4 Australian Taxation Office, *Sources of third-party information*. Available at www.ato.gov.au/About-ATO/Commitments-and-reporting/In-detail/Privacy-and-information-gathering/How-we-use-data-matching/?page=2#Sources_of_third_party_information.

5 Ss 14ZZK(b) and 14ZZO of the *Taxation Administration Act 1953* (Cth) (TAA53).

6 Australian Taxation Office, *Complying with a notice*. Available at www.ato.gov.au/about-ato/commitments-and-reporting/in-detail/privacy-and-information-gathering/our-approach-to-information-gathering/?page=20.

7 Australian Taxation Office, *Taxpayers' Charter – if you're subject to review or audit*. Available at www.ato.gov.au/About-ATO/Commitments-and-reporting/Taxpayers--Charter/Taxpayers--Charter---if-you-re-subject-to-review-or-audit/#Notification.

8 Australian Taxation Office, *When you can request an independent review*. Available at www.ato.gov.au/General/Dispute-or-object-to-an-ATO-decision/In-detail/Avoiding-and-resolving-disputes/Independent-review/Independent-review-for-small-businesses-with-turnover-less-than-$10-million/?page=2.

9 Australian Taxation Office, *In-house facilitation*. Available at www.ato.gov.au/General/Dispute-or-object-to-an-ATO-decision/Options-for-resolving-disputes/In-House-Facilitation/?=redirected_inhousefacilitation#:~:text=house%20facilitation%20form.-,The%20facilitation%20process,by%20phone%20or%20video%20link.

10 Ss 14ZW and 14ZU TAA53.

11 S 14ZU(c) TAA53.

12 S 14ZZ TAA53.

13 Ss 14ZZK(b) and 14ZZO TAA53; *Zappia v FCT* [2017] FCAFC 185 at [2]–[3].

14 *Gashi v FCT* [2013] FCAFC 30 at [76]–[78].

Hybrid mismatch rules: practical considerations

by Ramy Singh, CTA, Tax Risk Management Specialist, Rio Tinto

As Australia's response to the advice of the Organisation for Economic Co-operation and Development to address hybrid mismatches, the hybrid mismatch rules (HMRs) have been enacted in Div 832 of the *Income Tax Assessment Act 1997* (Cth). These rules have increased compliance requirements, some of which are impractical and compromise the effectiveness of the rules, including: the accessibility of key tax information that Australian taxpayers have from structured party arrangements and related parties; the ability of accounting systems to trace transactions through interposed entities (and audit implications); and the knowledge gap that Australian tax professionals have on overseas tax laws (including understanding how the HMRs have been implemented differently across the globe) and the lack of Australian tax expert resourcing.

Introduction

Under action 2 of the base erosion and profit shifting program, Australia has adopted the hybrid mismatch rules (HMRs).[1] These rules intend to combat tax base erosion exploited by multinational organisations from tax treatment mismatches of instruments and structures between tax jurisdictions.[2]

The HMRs have increased administrative and compliance requirements. The purpose of this article is to determine whether HMR-imposed compliance requirements can be appropriately and practically addressed. If the rules are not practical, the effectiveness of the HMRs in neutralising mismatched outcomes will be compromised.

The objective of determining the effectiveness of the HMRs will be achieved by reviewing extrinsic material, legislation and technical papers to get a detailed understanding of the Australian HMR requirements, and identifying the practical compliance issues that the HMRs present. This will be critiqued to determine the effectiveness of the HMRs in neutralising mismatch outcomes.

Policy and legislation

Hybrid mismatches occur where multinationals take advantage of differences in the tax treatment of structures or instruments under the tax laws of two jurisdictions to reduce or defer tax.[3] The most common mismatches are "double deduction" and "deduction/non-inclusion" arrangements:

- double deductions occur where taxpayers receive deductions in two countries for the same payment.[4] This will occur where a payment, or a partial payment: (1) gives rise to a foreign tax deduction in a foreign country; and (2) results in Australian income tax reduction amounts in an income year, or a foreign tax deduction in a foreign country;[5] and
- deductions/non-inclusions occur where deductions are taken in one country but the relevant income is not taxable in the recipient country. This applies where a payment or a partial payment gives rise to an Australian tax deduction in an income year. In this case, the deducted amount is higher than the sum of the assessable amount subject to foreign income tax in a foreign tax period beginning no more than 12 months after the end of the income year, or subject to Australin tax for the income year.[6]

The objective of the HMRs is to neutralise hybrid mismatches by denying deductions or including amounts in assessable income.[7] The neutralising rule applying will depend on whether the neutralising entity is a deducting or a non-including entity.[8] A taxpayer needs to take reasonable care when undertaking this analysis. Reasonable care requires the taxpayer to adopt a top-down or bottom-up approach to the analysis.[9]

The HMRs are set out in Div 832 of the *Income Tax Assessment Act 1997* (Cth) (ITAA97). The types of mismatches targeted by the HMRs are:

- hybrid financial instrument mismatches: where taxpayers enter structured or related party arrangements which exploit differences in the tax treatment of financial instruments resulting in mismatches;[10]
- hybrid payer mismatches: where a deductible payment results in a mismatch where the payment is made by a hybrid entity that is disregarded under the tax jurisdiction of the payee;[11]
- reverse hybrid mismatches: where a deductible payment is not included in the income of the jurisdiction where the payee (or investor of the payee) is established;[12]
- branch hybrid mismatches: where a deductible payment to a branch is not included in ordinary income by the residence or branch jurisdiction;[13]
- deducting hybrid mismatches: where a taxpayer makes a cross-border payment causing a deduction/deduction outcome when calculating net income under the laws of two or more jurisdictions, or where a payment made by a hybrid payer which is transparent to one of its investors is also deductible to that investor;[14]
- imported mismatches: see below.[15]

Under the HMRs, there are no de minimis thresholds and the HMRs can apply to third party arrangements.[16] The HMRs disregard the single entity rule applying under tax consolidation.[17] The HMRs apply to losses just as they apply to payments, and will apply to deductible amounts as they accrue.[18]

If a mismatch is a hybrid payer mismatch or a deducting hybrid mismatch, the hybrid mismatch is neutralised to the extent of dual inclusion income.[19] Income or profits will be dual inclusion income if two or more of the following outcomes arise for the amount:[20]

- it is subject to Australian tax in an income year;
- it is subject to foreign tax in a foreign country in a foreign tax period; and/or
- it is subject to foreign tax in another foreign country in a foreign tax period.

A payment causes a hybrid mismatch under a structured arrangement if:[21]

- the hybrid mismatch is priced into the terms of the scheme under which the payment is made; or
- it can be concluded that the hybrid mismatch is a design feature of the payment scheme.

Entities are in the same Div 832 control group if:[22]

- the entities are members of a group which is consolidated for accounting purposes as a single group;
- one entity holds a total participation interest of 50% or more in the other entity; or
- a third entity holds a total participation interest of 50% or more in each of the other entities.

Specifically for hybrid financial instrument mismatches, related persons are broadly entities which have a minimum 25% associate-inclusive control relationship.[23]

Imported HMRs

The imported HMRs operate to deny a deduction for a variety of payments (rents, royalties, interest, service payments) if they fund an offshore hybrid mismatch arrangement.[24] An imported hybrid mismatch can be:[25]

- made under a structured arrangement (the payer, interposed entities and offshore entities are parties to the arrangement);
- a direct payment (made directly to the offshore deducting entity who is part of the same Div 832 control group); or
- an indirect payment (made through interposed entities to the offshore deducting entity, all of which are part of the same Div 832 control group).

These rules require payment flows to be traced through interposed entities and through payments which make up the imported hybrid mismatch arrangement.[26]

An importing payment is made if:[27]

- either:
  - the payment would otherwise give rise to an Australian tax deduction; or
  - the payment results in a foreign deduction in an overseas jurisdiction which has foreign HMRs in a foreign tax period;
- it is made directly or indirectly to an entity, or through interposed entities; and
- the offshore deducting entity is the entity making the payment giving rise to the mismatch or the mismatch is a deducting hybrid mismatch.

The amount of the imported hybrid mismatch is the lesser of the importing deduction quantum and the amount determined by dividing the importing deduction by the total importing deduction of equal priority multiplied by the remaining offshore hybrid mismatch.[28] The definition of these concepts is outside the scope of this article.

If a payment gives rise to an imported hybrid mismatch and, apart from the HMRs, a deduction would have been available in Australia in an income year, the mismatch is neutralised to the extent that the deduction does not exceed the amount for the imported hybrid mismatch.[29]

Targeted integrity rule

The HMRs include a targeted integrity rule (TIR). The TIR applies to deny deductions for related party interest or derivative payments which are taxed at 10% or less.[30] For these rules to apply:[31]

- there is a derivative financial arrangement or interest payment to a foreign interposed entity;
- a foreign ultimate parent entity exists;
- the ultimate parent entity, the paying entity and the interposed entity are all in the same control group;
- the highest income tax rate applying is 10% or less;
- the outgoing is not subject to Australian income tax; and
- the principal purpose of entering the scheme was enabling a deduction and a low foreign income tax result.

Practical issues in implementation

The HMRs increase taxpayer compliance requirements. Multinationals must confirm that the relevant HMR analysis has been carried out at disclosures 45 to 51 of the international dealings schedule which is lodged with their income tax return.[32] Certain taxpayers may also be required to lodge a reportable tax position schedule with their income tax return. This will require further self-assessment analysis and disclosure to be carried out on the possibility of the HMRs applying.[33]

These obligations create additional compliance burdens for relevant taxpayers to consider from an HMR perspective. Hence, the practicality of the HMRs needs to be considered.

Access to information on tax treatment

The HMRs are triggered depending on the tax treatment of instruments, and the classification of entities, in counterparty jurisdictions.[34] This assumes that the counterparties in other jurisdictions will provide information on the tax treatment of those arrangements. However, this would not necessarily be the case. Broadly, the rules would apply to:[35]

- members within the same control group, which are entities that have common control interests of 50% or more, or are part of the same accounting consolidated group;
- parties which are under structured arrangements (schemes in which the hybrid mismatch is priced into the terms); and
- related persons, which are broadly entities that have a minimum 25% associate-inclusive control interest (although the related persons requirement only applies to hybrid financial instrument mismatches).

Regarding members within the same control group, sensitive tax information on the treatment of instruments, derivatives and structures should be available. This information would be readily available across internal management teams. However, sourcing information from structured parties and related persons may be more difficult. Examples of these situations can include counterparty tax advice on the treatment of structures and arrangements under legal professional privilege (LPP), and market-sensitive transactions.

> "These obligations create additional compliance burdens for relevant taxpayers to consider from an HMR perspective."

Under LPP, an entity can refuse to provide a document if it constitutes independent legal advice under confidentiality.[36] It is common practice for tax advice to be attained under LPP, particularly for issues requiring a technical, detailed tax analysis. Therefore, instances can occur where related parties, or parties under structured arrangements, refuse to provide the tax treatment of arrangements or structures (particularly as the counterparty may not be related to the Australian taxpayer under a structured arrangement, or there may be insufficient control interest to warrant the provision of such information). This would cause compliance issues with the HMRs.

Where the tax treatment of structures or arrangements is pivotal to market-sensitive information, such information may be withheld in counterparty jurisdictions. Where listed companies are involved, there are restrictions on the handling of confidential information which may impact the market. Accordingly, counterparties listed in overseas exchanges are legally restricted on the quantity and disclosure of information which can be provided to external parties, including the tax implications of structures and arrangements.[37]

Capturing information

The HMRs assume that taxpayers have perfect accounting data-capturing systems. This is demonstrated by the following requirements:

- the HMRs apply to payments (including financing, royalties, cost of sales, service fees and depreciation) inside, outside, or partially inside or outside of Australia;[38]
- the tax consolidation rules are disregarded when applying the HMRs;[39]
- there are no de minimis thresholds and the HMRs can apply to third-party arrangements;[40]
- under the imported mismatch rules, an Australian deduction directly or indirectly funds a deduction/non-inclusion or deduction/deduction mismatch elsewhere in the group, including through interposed entities;[41]
- under the imported mismatch rules, an entity will be considered a party to a scheme unless it can be demonstrated, among other requirements, that the financial position of the entity, in each control group, would be the same if it had not given rise to the mismatch.[42]

The capturing of the above accounting data:

- assumes that taxpayers have appropriate systems in tracking all payments and their flows through entities;
- disregards materiality principals (which are typically applied to audited data); and
- assumes that Australian taxpayers have access to the accounting information of parties which do not form part of the accounting consolidated group (including related parties and parties under structured arrangements).

In the author's experience, accounting systems are not sufficiently robust to trace all payments through interposed entities to determine whether Australian-funded deductions have ultimately resulted in hybrid mismatches being imported to another jurisdiction further down the chain. This is due to the volume of transactions undertaken by multinationals, and the difficulty in being able to trace the movement of transactions through groups. Therefore, not all imported hybrid mismatches can be traced and, given the current sophistication of accounting systems, not all imported hybrid mismatches can be identified.

In practice, it may be possible for auditors to impose some degree of requirement to manually capture transaction flows for identifying the impact of imported HMR exposure to tax expenses, current tax liability and deferred tax balances in audited financial statements. This would be in the absence of appropriate accounting systems. However, auditing standards adopt the principle of materiality.[43]

Typically, the materiality threshold of public listed companies is 3% to 10% of profit before tax.[44] In 2021, Australia's top 99 listed companies reported an average earnings amount of $1.038b.[45] Based on this, amounts of less than $31.14m and $103.8m (depending on whether a 3% or 10% materiality is applied) would be immaterial.

Hence, even under the audit procedures of listed multinationals in Australia, significant deductions can be taken without resulting in material misstatements of financial reports. Therefore, the imported HMRs would not be sufficiently effective in denying deductions for imported mismatches under statutory audits. If these multinationals are not audited by the ATO, it is unlikely that immaterial deductions triggering the imported HMRs will be detected or reported.

To the extent that Australian taxpayers are parties to structured arrangements, entities which are outside the control group, or those which are unrelated, will not be required to provide information on the financial position of the entity, or control group, to Australian taxpayers when considering whether the relevant entity is a party to an imported hybrid mismatch scheme. This creates a barrier to HMR compliance. Hence, it is likely that the status quo of any *potential* imported hybrid mismatch will have to be deemed to have caused the imported HMR, in the absence of confirmations from parties of structured arrangements.

Overseas tax jurisdictions

The HMRs require Australian taxpayers, or their advisers, to be versed on foreign tax laws in order to:[46]

- identify the tax treatment of arrangements and structures in overseas jurisdictions in accordance with the policy intent of the HMRs; and
- understand overseas corporate tax rates to identify whether the TIR applies.

The HMRs assume that taxpayers, or their advisers, have perfect resourcing to determine counterparty tax treatments. However, tax laws vary significantly between jurisdictions.[47] Jurisdictions may have different tax laws depending on the maturity of the particular economy.[48] The premise of the HMRs is to address multinationals which are exploiting differing tax treatments between various jurisdictions. Hence, local Australian tax experts would not necessarily be knowledgeable on the specific tax laws of counterparty jurisdictions.

A primary example is the implementation of the HMRs globally. New Zealand's HMR laws have been noted to be mirroring the recommendation of action 2 of the base erosion and profit shifting program, and identify correlations with the Organisation for Economic Co-operation and Development's advice, section by section, to its HMR provisions. Comparatively, the Australian HMRs do not have such explicit replication, and the United Kingdom HMRs have special anti-avoidance laws which have a defence of consistency.[49] Therefore, the implementation of the HMRs differs from country to country. This is because the use of international material to make tax laws varies on the interpretive and constitutional rules of the country designing the laws, the design and detail of the country's specific HMRs, the issues being considered, and the county's relationship with outside parties.[50]

There are specific instances of structural differences in HMR implementation between countries. For example, regarding the hybrid financial instruments rule, Australia and the UK approach hybrid transfers separately from mismatches relating directly to payments under hybrid instruments.[50] Another example is that New Zealand combines the reverse HMR and the branch payee mismatch rule, whereas the UK adds secondary income inclusion under the reverse HMR.[50] These examples indicate a lack of consistency in the implementation of the HMRs across jurisdictions. This indicates that, because an instrument or structure may be subject to the HMRs in Australia, this may not be the case in overseas jurisdictions. Similarly, an instrument which maybe characterised a certain way under the debt/equity rules under Australian tax law may not be treated the same in a counterparty tax jurisdiction.

In the author's experience, if smaller firms are engaged in preparing income tax returns, they do not have the resources to engage member firms in overseas jurisdictions to determine the tax treatment of overseas instruments and organisational structures. Australian tax advisers are rarely trained on the specifics of foreign tax laws.

The author's experience is that the Big 4 accounting firms are usually engaged by multinationals to prepare income tax returns. However, the Big 4 accounting firms are experiencing deficiencies in staff resourcing. As of 2022, 80% of Australian accounting firms have a labour shortage.[50] Of Australia's top 100 accounting firms, 77 have experienced staffing difficulties, including the Big 4 accounting firms.[51] Hence, there is a question of whether the Big 4 accounting firms have sufficient resourcing to review and engage member firms in overseas jurisdictions to determine the tax treatment of arrangements and structures by lodgment date.

Regarding corporate tax rates when determining TIR application, the 2021 global average corporate tax rate was 23.54%, with the lowest average being in Asia at 19.62%.[52] Average tax rates have declined worldwide since 1980 across every region (the average global corporate tax rate was 40.11% in 1980).[53]

The TIR is targeted at interest and derivative payments taxed at less than 10%.[53] If the trend of reducing corporate tax rates continues and economies continue to be globalised and compete for foreign investment and mobile capital, it is likely that more jurisdictions will be captured by this rule. Accordingly, the TIR, as it is currently implemented, will be triggered by interest and derivative deductions in Australia, even where there might not be a tax benefit purpose driving the transaction. Hence, the percentage threshold of the rule, or its broader requirements, may need to be revisited as corporate tax rates continue to reduce across the world.

Conclusion

This article has provided a technical overview of the policy intent of the HMRs. The rules impose an onus on certain taxpayers by requiring an analysis to be done on potential hybrid structures, and disclosures to be prepared in the international dealings schedule and the reportable tax position schedule.

A number of practical challenges from the implementation of the HMRs have been identified, including:

- having access to information on the tax treatment of counterparties;
- the robustness of accounting systems to trace Australian deductions through interposed entities; and
- the difficulties that Australian tax experts face when determining foreign tax treatments to overseas arrangements and structures.

These issues have an impact on compliance with the HMRs, and compromise achieving their desired objectives. The rules should be revisited by addressing their practicality so that hybrid mismatches are more sufficiently neutralised.

Ramy Singh, CTA
Tax Risk Management Specialist
Rio Tinto

References

1 Para 1.3 of the explanatory memorandum (EM) to the Treasury Laws Amendment (Tax Integrity and Other Measures No. 2) Bill 2018.

2 Deloitte, *Understanding the hybrid mismatch rules*, February 2022, p 2. Available at https://www2.deloitte.com/content/dam/Deloitte/au/Documents/tax/deloitte-au-tax-understanding-hybrid-mismatch-rules-100222.pdf.

3 Para 1.9 of the EM.

4 Para 1.10 of the EM.

5 Para 1.73 of the EM.

6 Para 1.65 of the EM.

7 Para 1.18 of the EM.

8 Para 1.33 of the EM.

9 J Barnes, S Urban and J Anderson, *Imported hybrid mismatch rule: limited clarifications provided in final ATO guidance*, 13 January 2022. Available at www.kwm.com/au/en/insights/latest-thinking/imported-hybrid-mismatch-rule-limited-clarifications-provided-in-final-ato-guidance.html.

10 Para 1.127 of the EM.

11 Para 1.182 of the EM.

12 Para 1.228 of the EM.

13 Para 1.256 of the EM.

14 Para 1.284 of the EM.

15 Para 1.116 of the EM.

16 Deloitte, op cit, p 2.

17 Para 1.16 of the explanatory memorandum to the Treasury Laws Amendment (2020 Measures No. 2) Bill 2020.

18 Para 1.48 of the EM.

19 Para 1.118 of the EM.

20 Para 1.119 of the EM.

21 Para 1.136 of the EM.

22 Para 1.134 of the EM.

23 Deloitte, op cit, p 3.

24 Para 1.324 of the EM.

25 Para 1.327 of the EM.

26 Para 1.328 of the EM.

27 Para 1.334 of the EM.

28 Para 1.330 of the EM.

29 Para 1.346 of the EM.

30 Deloitte, op cit, p 1.

31 Deloitte, op cit, p 6.

32 Deloitte, op cit, p 2.

33 EY, *Australian Taxation Office releases final guidance on imported hybrid mismatch rule*, December 2021. Available at www.ey.com/en_gl/tax-alerts/australian-taxation-office-releases-final-guidance-on-imported-hybrid-mismatch-rule.

34 Australian Taxation Office, *Hybrid mismatch rules*, February 2022. Available at www.ato.gov.au/Business/International-tax-for-business/In-detail/Hybrid-mismatch-rules.

35 Deloitte, op cit, p 2.

36 K Watson and L Causer, *Legal professional privilege*, Queensland Government in-house lawyers, August 2021. Available at www.crownlaw.qld.gov.au/resources/publications/legal-professional-privilege-queensland-government-in-house-lawyers.

37 R Halstead and L Humphrey, *Is your announcement "market sensitive?"*, 19 July 2018. Available at www.claytonutz.com/knowledge/2018/july/is-your-announcement-market-sensitive.

38 Deloitte, op cit, p 2.

39 Para 1.16 of the explanatory memorandum to the Treasury Laws Amendment (2020 Measures No. 2) Bill 2020.

40 Deloitte, op cit, p 2.

41 Para 1.328 of the EM.

42 Para 1.141 of the EM.

43 Auditing and Assurance Standards Board, Auditing Standard ASA 320, 2015, p 7.

44 Chartered Accountants Australia and New Zealand, *Audit and assurance*, 2015, p 203.

45 Companies Market Cap, *Top publicly traded Australian companies by earnings*. Available at www.companiesmarketcap.com/australia/most-profitable-companies-in-australia.

46 Deloitte, op cit, p 1.

47 OECD, *Tax policies vary widely from country to country, OECD study shows*, 2005. Available at www.oecd.org/general/taxpoliciesvarywidelyfromcountrytocountryoecdstudyshows.htm.

48 World Population Review, *Highest taxed countries 2022*, 2022. Available at www.worldpopulationreview.com/country-rankings/highest-taxed-countries.

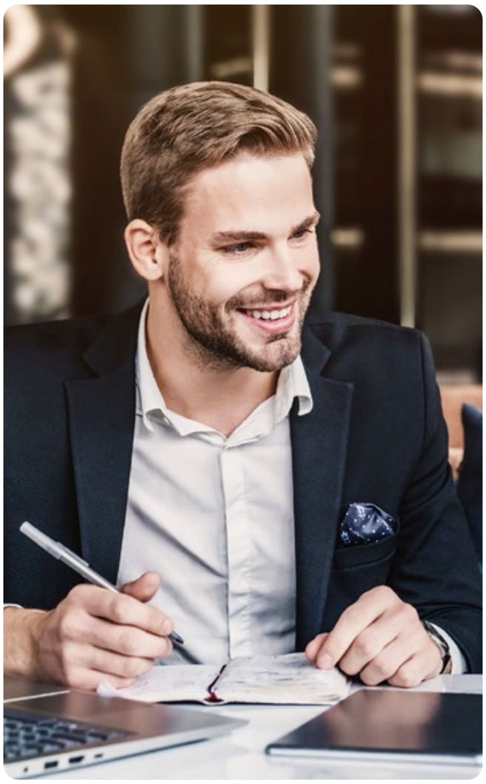
49 M Brabazon, "Are we there yet? International implementation of hybrid mismatch rules", (2019) 73(6/7) *Bulletin for International Taxation* 304.

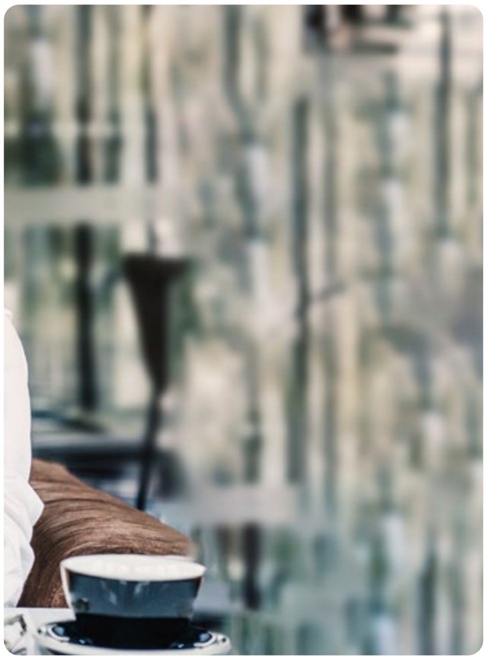
50 Odyssey Accountants, *80% of Australian firms are hampered by labour shortages*, March 2022. Available at www.odyssey-resources.com/2022/03/80-of-australian-firms-are-hampered-by-labour-shortage.

51 E Tedros, *Staffing crisis hits Australia's top accounting firms*, 19 October 2021. Available at www.afr.com/companies/professional-services/staffing-crisis-hits-australia-s-top-accounting-firms-20211014-p59033.

52 Tax Foundation, *Corporate tax rates around the world, 2021*, 2021. Available at www.taxfoundation.org/publications/corporate-tax-rates-around-the-world.

53 Deloitte, op cit, p 1.





A Matter of Trusts

by Simran Joshi, Lawyer, Sladen Legal

Bosanac: presumption of advancement

The High Court has confirmed that, in certain circumstances, the presumption of advancement can apply to contributions to the purchase price of property or the transfer of assets.

Overview

In *Bosanac v FCT*,[1] the High Court considered the ancient equitable principles of the presumption of resulting trust and the presumption of advancement. However, while not overturning the presumptions, the High Court characterised them as "weak" and decided the case on its objective facts without relying on the presumptions.

What are the presumptions?

It is a well-known legal maxim that equity presumes bargains, not gifts. The basic premise in equity assumes that people do not usually intend to make gifts of real property.

A resulting trust arises when a person advances (gifts) purchase monies for a property, but the property is held in the name of another person. The effect of the resulting trust is that the recipient is said to hold the property on trust for the donor unless the presumption can be rebutted.

However, the presumption of advancement is an exception where the presumption of resulting trust does not arise. Based on the nature of the relationship between the transferor and the recipient, the presumption of advancement assumes that the gift was intended. These relationships are limited to advancements from husband to wife (not de facto), male fiancé to his female fiancé, and parent (or person who stands in loco parentis) to child.[2]

Importantly, evidence of intentions of both the parties at the time of purchase can rebut one or both presumptions.[3]

Background

In 2006, Ms Bosanac bought a property to be used as a matrimonial home for her and Mr Bosanac. Ms Bosanac paid the purchase price from existing and new joint loans in their names. Mr and Ms Bosanac separated in 2012 or 2013, and in 2015, Mr Bosanac moved out of the home.

Mr Bosanac owed tax debts to the Federal Commissioner of Taxation. The Commissioner brought proceedings seeking declaration of a resulting trust over the equity in one-half of the property.

The trial judge held that there was a presumption of advancement, instead of resulting trust, and Ms Bosanac was the sole beneficial owner of the property. The Commissioner appealed to the Full Federal Court .

On appeal, the Full Federal Court overturned the decision and concluded that the evidence "tended strongly" against the presumption of advancement and showed an intention to create a (resulting) trust over one-half of the property for Mr Bosanac. Special leave to appeal to the High Court was granted to Ms Bosanac.

Issue for the High Court

The issue before the High Court was whether Ms Bosanac held half of her interest in the property on trust for Mr Bosanac when the purchase of the property was paid from joint funds of Mr and Ms Bosanac.

Decision

The five-judge bench of the High Court unanimously allowed the appeal and set aside the decision of the Full Federal Court. That is, the High Court decided that Ms Bosanac did not hold half of her interest in the property on trust for Mr Bosanac.

However, while unanimously allowing the appeal, the five judges of the High Court, in three separate judgments, did not rely on the presumption of advancement. Instead, they based their decisions on the evidence before them with respect to the intention of Mr and Ms Bosanac at the time of purchase of the property, and the facts and circumstances analysed from the history of the past transactions between the couple.

Laying emphasis on the determination of evidence by the courts relating to the intention of the parties when the property was purchased or transferred, the judges reiterated that the strength of the presumptions will vary from case to case depending on the evidence.[4]

Kiefel CJ and Gleeson J observed that the approach in recent cases is to seek to determine the real intentions of the parties, although noting that the presumption (of advancement) remains present (although weak).[5]

Gordon and Edelman JJ further concluded that the presumption of a resulting trust only arises where the evidence is evenly balanced, and the court is unable to decide.[6] However, as a starting point, it is necessary to evaluate the objective facts as a resulting trust is an inference drawn in the absence of evidence.

The Commissioner also contended that the Full Federal Court was wrong to find, in effect, that, where a husband and wife purchase a matrimonial home, each contributing to the purchase price, and title is taken in the name of one of them only, it is not to be inferred that each of the spouses would have a one-half interest in the property. The Commissioner relied on a statement to that effect in the High Court decision of *Trustees of the Property of John Daniel Cummins v Cummins*.[7]

However, the High Court in *Bosanac* distinguished *Cummins* on the facts and issues saying that the actual intention of Mr and Ms Cummins was joint beneficial ownership and for the rule of survivorship to apply, despite the legal title only being in the name of Ms Cummins. Further, the court in *Cummins* did not concern itself with the issue of presumption of advancement.

Question of intention

The High Court noted that the question of intention is entirely one of fact and concerns the intention manifested by the person(s) who contributed funds towards the purchase of the property. Concluding that Mr Bosanac intended to facilitate Ms Bosanac's purchase of the property, which was to be held in her name, the judges determined the intention of Mr and Ms Bosanac from the following facts:

- the history of Mr and Ms Bosanac holding their substantial real and other property in their own names and, consistent with that, the desire of Ms Bosanac to purchase and hold the property in her name alone;
- the property was not registered in Mr Bosanac's name and there was no transfer of property from Mr Bosanac to Ms Bosanac;
- Mr Bosanac did not advance all of the monies for the purchase of the property;
- there was history of the use of the properties held by each of them in their own names as security for joint loans;
- there was no evidence of the use of joint loans to buy jointly owned property;
- apart from some shared bank accounts, there was no substantial jointly owned property;
- there was "considerable evidence" of separate ownership of property;
- Mr Bosanac was a "sophisticated businessman" who must have appreciated the significance of property being held in Ms Bosanac's name and no inference could be drawn that Mr Bosanac intended to have a beneficial interest in the property; and
- there was no suggestion that Ms Bosanac contracted and purchased the property in her name to assist her husband to avoid creditors.

The High Court thus held that the conduct and objective facts of Mr and Ms Bosanac at the time of acquisition of the property established that their objective intention was inconsistent with a declaration of trust in favour of Mr Bosanac as to 50% of Ms Bosanac's interest in the property, and thus no resulting trust arose.

Where does the presumption of advancement sit in modern society?

The presumption of advancement has drawn criticism for being outdated, sexist and discriminatory.

Notwithstanding the view, as expressed by Kiefel CJ and Gleeson J, that the presumption of advancement is weak, the High Court did not abolish the presumption as contended by the Commissioner on the basis that it was anomalous, anachronistic, discriminatory and had no acceptable rationale.

Kiefel CJ and Gleeson J agreed with Lord Reid's view in *Pettitt v Pettitt*[8] that the considerations that impressed the judges who first applied the presumption of advancement, either in thinking that husbands so commonly made gifts to their wives that they simply assumed it, or that wives' economic independence made it necessary as a matter of public policy to give them this advantage, have under present conditions largely lost their force.

Kiefel CJ and Gleeson J also questioned whether, in a modern society, if the presumption of advancement is to be maintained, it should now apply to transfers of property not just from husband to wife, given the position that many wives now have respective income and property, but also as between spouses more generally given the recognition by statute of de facto relationships in proceedings concerning property and same-sex marriage.[9]

However, Kiefel CJ and Gleeson J concurred with Deane J's view in *Calverley v Green*[10] that, in the absence of knowledge as to the effect of such abolition on existing entitlements, it would be a better course to leave any reform of this branch of the law to the legislature.[11]

Gageler J in his judgment noted that the weight of history was too great for a redesign of that magnitude now to be undertaken judicially.[12] While rejecting the Commissioner's contention that the presumption of advancement should be abandoned, Gageler J further concluded that the presumption of resulting trust and the counter-presumption of advancement are here to stay unless and until they are together reappraised as an exercise in law reform and abolished or changed by legislation.[13]

Conclusion

The question whether the presumption of advancement should remain has practically been made redundant by the decision of the High Court in *Bosanac* where the court effectively ruled that there is no presumption necessary if the objective facts themselves establish the state of affairs. In other words, the presumption does not prevail, it fills a gap only if there is a gap.

The High Court said that reform is for the legislature. As the presumption lies in equity and legislative reform could potentially include federal, state and territory property, family and other laws, legislative reform will not be a simple task. It remains to be seen if the comments by the High Court lead to abolition or amendment.

As stated by the High Court, until the legislature decides to change or abolish the presumption, it is here to stay despite its weakened state. It also seems that, given the High Court's comments on reform, the question of whether the application of the presumption should be extended to include transfers of property between spouses more generally (given the position of women in modern society and the recognition by statute of de facto relationships and same-sex marriages) may also be one for the legislature.

As a result of the High Court decision in *Bosanac*, careful consideration should be put in place at the time of transactions in order to create contemporaneous legal documents setting out the intention of the parties. In addition to recording the intention of ownership, it will also be worthwhile to keep records of contributions towards the purchase price of property.

Simran Joshi
Lawyer
Sladen Legal

References

1 [2022] HCA 34.

2 *Bosanac* [2022] HCA 34 at [8], relying on *Napier v Public Trustee (WA)* (1980) 32 ALR 153 at 158, and *Nelson v Nelson* (1995) 184 CLR 538 at 547–548.

3 *Bosanac* [2022] HCA 34 at [13], relying on *Muschinski v Dodds* (1985) 160 CLR 583 at 612, and *Calverley v Green* (1984) 155 CLR 242 at 251.

4 *Bosanac* [2022] HCA 34 at [21].

5 *Bosanac* [2022] HCA 34 at [16], relying on J McGhee, S Elliott, S Bridge et al, *Snell's equity*, 34th ed, 2020, para 25-007.

6 *Bosanac* [2022] HCA 34 at [102], relying on *S v S* [1972] AC 24 at 41, quoted in JD Heydon, *Cross on evidence*, 13th ed, 2021, pp 386-387. See *Pettitt v Pettitt* [1970] AC 777 at 814.

7 [2006] HCA 6. See *Bosanac* [2022] HCA 34 at [24] and [117].

8 [1970] AC 777 at 792–793.

9 *Bosanac* [2022] HCA 34 at [17].

10 (1984) 155 CLR 242.

11 *Bosanac* [2022] HCA 34 at [30].

12 *Bosanac* [2022] HCA 34 at [58].

13 *Bosanac* [2022] HCA 34 at [60].

Obituary

The Hon. Ian Vitaly Gzell AM QC FTI (Life)

1941–2022

Ian Gzell's time as President of The Tax Institute encompassed the beginnings of the vast changes of the Keating era.

He had followed Graham Hill as our President. Together they represented the Institute at the Taxation Summit in 1985,[1] a summit whose seismic changes are still with us.

And that is fitting.

For Gzell's energy and accomplishments seem to us now almost impossible to credit.

Gzell made things happen.

His service to the professions and the arts began immediately.

In 1962, he was gaining support for a new theatre at The University of Queensland. He was Dramsoc President, and Union Theatre Committee Chair.

And he didn't just write a letter to UQ Senate and wait.

An architect was engaged for sketches. Local theatre companies assured the Union that they would use the new place.

This is the man destined to be our President.

His service to the Bars of Queensland and New South Wales has been noted elsewhere. It is impossible to summarise. But within two years of his 1965 admission as a barrister, Gzell was Secretary of the Bar Association of Queensland.

He continued to serve in responsible and demanding roles, in the law and tax professions, including as President of the Commercial Law Association and Chair of STEP (NSW).

But here I remember his service to this Institute. He served as Queensland Chair, on National Council and as our President, among other active roles.

And few who were present in China on those magic days in April 1989 will forget the Institute's conference in Shanghai and Beijing, with business people and tax professionals. A mission to China, including our Commissioner of Taxation as speaker, was visionary.

Most members now remember Gzell J by his decisions in tax cases, as a Justice of the New South Wales Supreme Court. He served New South Wales well in that role, from 2002 to 2013.

He sat at trial in a groundbreaking payroll tax matter with a surreal name, *Tasty Chicks*.[2]

But he had already noticed a drafting feature of the state tax appeal provisions in NSW that made it possible to seek full justice in the court. The court could effectively compete for business with the tribunal.[3] And the taxpayers came.

The profession was already aware of the possibility of obtaining declaratory relief in the Supreme Court, in federal taxes such as GST, although there were natural limits to this adventure.[4]

But Gzell also sat in some of the most high-profile corporate matters of the day, including matters about NRMA, James Hardie and One.Tel. And he broke ground in a case about the rights of a child, conceived from donated material, in a claim against the estate of the donor father.[5]

As judge, you do not choose the cases that come before you. But you can distinguish yourself in their disposition. Gzell J did.

I remember obtaining Gzell QC's advice in the 1990s. I flew to Sydney to meet him. Suave, welcoming and brief, he already had a draft on his laptop. We discussed some further, abstruse point of law, and I flew back to Brisbane – followed swiftly by his faxed opinion.

On another occasion, he was a speaker at a Law Council conference at the Hyatt Canberra – which happens to be next to the Canberra Croquet Club. Gzell appeared one morning in his whites, and said he had a letter of introduction from his NSW croquet organisation. Off he went to play the Canberrans! It illustrated that, fundamentally, Gzell knew how to get things done. And how to meet new friends.

Gzell continued his interest in the health of the arts. His service in that sphere was significant. And that begins to tell us something of the wider story.

For this was a practitioner of wide interests and great curiosity, and above all (to quote the funeral notice placed in the *Sydney Morning Herald*): "A most sociable and agreeable person."

David W Marks KC, CTA
Level 16 Inns of Court, Brisbane

References

1 Ian Gzell's obituary for Justice Graham Hill, (2005) 40(4) *Taxation in Australia* 179.

2 *Tasty Chicks Pty Ltd v Chief Commissioner of State Revenue* [2009] NSWSC 1007.

3 *Affinity Health Ltd v Chief Commissioner of State Revenue* [2005] NSWSC 663.

4 *Platypus Leasing Inc v FCT (No. 3)* [2005] NSWSC 388; leave to appeal denied [2005] NSWCA 399.

5 "Children of donor win right to inherit", *The Daily Telegraph*, 16 March 2007.

Events Calendar

Upcoming month

MARCH
8–9
Wed–Thu

SA

SA Tax Forum

12 CPD hours

MARCH
16–17
Thu–Fri

VIC

Financial Services Taxation Conference

11 CPD hours

MARCH
22–23
Wed–Thu

WA

WA Tax Forum

12 CPD hours

MARCH
30–31
Thu–Fri

Online

Superannuation Intensive

8 CPD hours

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

Cumulative Index

The following cumulative index is for volume 57, issues (1) to (8). Listed below are the pages for each issue:

Vol 57(1): pages 1 to 56
Vol 57(2): pages 57 to 126
Vol 57(3): pages 127 to 182
Vol 57(4): pages 183 to 242
Vol 57(5): pages 243 to 302
Vol 57(6): pages 303 to 370
Vol 57(7): pages 371 to 434
Vol 57(8): pages 435 to 492

Legislation

Rulings and other materials

Cases

Authors

Contacts

National Council

Chair
Clare Mazzetti

President
Marg Marshall, CTA

Vice President
Todd Want, CTA

Treasurer
Paul Banister, CTA

National Councillors
Leanne Connor, CTA
David Earl, FTI
Eddy Moussa, CTA
Tim Sandow, CTA
Ian Heywood, CTA
Bill Keays, CTA

National Office

CEO: Giles Hurst

Level 37, 100 Miller Street
North Sydney, NSW 2060

T 02 8223 0000
E ceo@taxinstitute.com.au

State Offices

New South Wales and ACT
Chair: Glen Hutchings, FTI

Level 37, 100 Miller Street
North Sydney, NSW 2060

T 02 8223 0031
E nsw@taxinstitute.com.au

Victoria
Chair: Fiona Knight, CTA

c/o Level 37, 100 Miller Street
North Sydney, NSW 2060

T 03 9603 2000
E vic@taxinstitute.com.au

Queensland
Chair: John Ioannou, CTA

Level 11, Emirates Building
167 Eagle Street
Brisbane, QLD 4000

T 07 3225 5200
E qld@taxinstitute.com.au

Western Australia
Chair: Bill Keays, CTA

Level 32, Central Park
152 St Georges Terrace
Perth, WA 6000

T 08 6165 6600
E wa@taxinstitute.com.au

South Australia and Northern Territory
Chair: Nick Wilkins, CTA

The Tax Institute, WOTSO Adelaide
217/219 Flinders Street
Adelaide, SA 5000

T 08 8463 9444
E sa@taxinstitute.com.au

Tasmania
Chair: Ian Heywood, CTA

The Tax Institute, WOTSO Adelaide
217/219 Flinders Street
Adelaide, SA 5000

T 1800 620 222
E tas@taxinstitute.com.au

Taxation *in* Australia ISSN 0494-8343

Publishing House
The Tax Institute
ABN 45 008 392 372

Level 37, 100 Miller Street
North Sydney, NSW 2060

General Manager – Commercial Transformation & Special Projects
James Paterson

Content Delivery Manager, Knowledge & Learning
Carla Reddy

Editorial Advisor
Professor Bob Deutsch, CTA

Managing Editor
Deborah Powell

Graphic Designers
Mei Lam; Nicole Welch; Claus Huttenrauch

Typesetter
Midland Typesetters, Australia

Advertising
Business Relationship Manager
Brian Martin 08 6165 6600

The Tax Institute

taxinstitute.com.au

23-05RES_03/23