The Tax Summit

Session 3.1: The latest on Section 100A - Part 1

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Contents

1. Currency

1. This paper was originally prepared and published under the title *'Section 100A: Evolving to a higher animal?'* for The Tax Institute's Noosa Tax Convention on 18 November 2022.

2. When this paper was originally prepared and published:

   a. The primary decision (Logan J) in *Guardian AIT Pty Limited ATF Australian Investment Trust v Commissioner of Taxation*[1] (**Guardian AIT**) had been handed down (21 December 2021);

   b. The primary decision (Thawley J) in *BBlood Enterprises Pty Ltd v Commissioner of Taxation*[2] (**BBlood**), 2022 by had been handed down (19 September 2022); and

   c. The Commissioner of Taxation (**Commissioner**) had released his administrative guidance on section 100A in draft in *TR 2022/D1 - Income tax: section 100A reimbursement agreements* (**TR 2022/D1**) and *PCG 2022/D1: Section 100A reimbursement agreements - ATO compliance approach* (**PCG 2022/D1**).

3. Since that time:

   a. the appeal decision (Hespe, Perry and Derrington JJ) in F. C. of T. v Guardian AIT Pty Ltd ATF Australian Investment Trust [2023] FCAFC 3 was handed down on 24 January 2023 (**Guardian (FFC)**);

   b. the appeal decision (Moshinsky, Colvin and Hespe JJ) in *BBlood Enterprises Pty Ltd and B&F Investments Pty Ltd as Trustee for the Illuka Park Trust v F. C. of T*. [2023] FCAFC 3 was handed down on 9 June 2023 (**BBlood (FFC)**);

   c. The Commissioner, following a period of public consultation[3], issued his administrative guidance in final form as *TR 2022/4: Income tax: section 100A reimbursement agreements* (**TR 2022/4**) and *PCG 2022/2 - Section 100A reimbursement agreements - ATO compliance approach* (**PCG 2022/2**);

   d. The Commissioner further announced that TR 2022/4 would be reviewed following the decision in BBlood (FFC)[4]. At the time of writing, no such revisions have been finalised.

[1] [2021] FCA 1619.
[2] [2022] FCA 1112.

[3] Comments on TR 2022/D1 arising from the public consultation process are set out in Ruling Compendium TR 2022/4EC.
[4] See: the Commissioner's *Decision Impact Statement* on Guardian AIT (FFC).

4. The current version of this paper has been revised and updated to account for the new, and important, authorities concerning section 100A since its original publication, and accompanies my presentation at the Tax Institute's Tax Summit in September 2023.

2. An evolutionary study of section 100A

> "Thus, from the war of nature, from famine and death, the most exalted object which we are capable of conceiving, namely, the production of the higher animals, directly follows. There is grandeur in this view of life, with its several powers, having been originally breathed into a few forms or into one; and that, whilst this planet has gone cycling on according to the fixed law of gravity, from so simple a beginning endless forms most beautiful and most wonderful have been, and are being, evolved."

5. It was with these evocative words that Charles Darwin (1809 to 1882) described the revolutionary theory of evolutionary biology that was propounded in 1859 in his seminal text, *On the Origin of Species*[5].

6. To my mind, this passage reveals Darwin to be many things apart from a brilliant theoretician. A lover of the whimsy and melody that can be captured in the English language. A skilled promoter of his work (perhaps necessary given some of the more brutal elements of his evolutionary theses may have jarred the sensitivities of his prospective Victorian readership). But above all, an unstinting optimist.

7. What I hear Darwin to be saying with these words is this: There is beauty in tension and destruction in the natural environment (the 'war of nature'). Tension and destruction in the natural environment beget creation, which occurs on a natural upward trajectory, leading to higher and better forms of being (the 'most exalted object which we are capable of conceiving'), for all species on earth (the 'higher animal').

8. Why talk about Darwin, tension, destruction, and creation, in the introduction of a tax paper? First, I take licence from Logan J, to start this paper by referring to a great theoretician of the scientific realm[6]. Second, I see echoes of what Darwin says about biological evolution in the evolution of tax anti-avoidance provisions, both generally and section 100A of the *Income Tax Assessment Act 1936* (the **1936 Act**) specifically.

[5] Darwin, Charles, and Leonard Kebler: *On the origin of species by means of natural selection, or, The preservation of favoured races in the struggle for life*; London: J. Murray, 1859.

[6] *Guardian AIT Pty Ltd ATF Australian Investment Trust v Commissioner of Taxation* [2021] FCA 1619 at [1]: "*It was the great, twentieth century, Swiss analytical psychologist, Dr Carl G. Jung who conceived of the concept of "synchronicity", a word which has passed into the English language as descriptive of "events which coincide in time and appear meaningfully related but have no discoverable causal connection" (Oxford English Dictionary)*."

2.1 The 1970's Galapagos: the 'war of nature'

9. Much like Darwin in the Galapagos[7], a study of the natural environment in which the evolution of a species has occurred can yield revelatory insights about the manner and nature of the species evolution.

10. Section 100A was enacted in 1979 by the passage of the *Income Tax Assessment Amendment Act* 1979. The period preceding it, and which precipitated its introduction, was characterised by:

    a. rampant tax avoidance behaviour;

    b. a judicial attitude of 'strict legalism' that created the conditions for aggressive tax planning to thrive;

    c. a tax administration system that could not keep up with the pace set by those seeking to avoid tax (and those who facilitated and enabled them); and

    d. a tax system that was structurally dependent on a narrow assessable base, where corporate and individual tax rates were exceptionally high compared to current standards, and where the Commissioner did not have the arsenal of anti-avoidance provisions he has today.

11. As it provides important context for the discussion in this paper, and to section 100A more broadly, I elaborate on these points below.

12. Of course, no reasonable person (or even tax practitioner) would quarrel with the proposition that blatant tax avoidance, when left to run rampant and unchecked, is a public scourge. Tax avoidance apportions financial costs and benefits unfairly across society and undermines public confidence in the rule of law. Moreover, if the wealthy, powerful or well-connected are seen to be getting away with paying little or no tax compared to the ordinary person, a more generalised attitude of tax non-compliance may take hold and spread like a contagion. The confluence of these factors disturbs the natural order of and harmony of a society: a 'war of nature'.

2.1.1 The prevailing tax compliance environment

13. The period preceding the introduction of section 100A, and the tax compliance (or, more aptly, non-compliance) environment that prevailed at that time, has been amply chronicled[8]. The 1970's were an era where 'bottom of the harbour' schemes ran rampant and tax promoters

[7] As a 22 year-old, Charles Darwin embarked on a five-year journey (1830 to 1836) across South America on the *HMS Beagle* as a naturalist. Darwin's theory of evolutionary biology was fomented in large part by his observation and study of the endemic wildlife on the Galapagos Islands; so much so that the Galapagos Islands are now largely synonymous with Charles Darwin.

[8] See the detailed survey of contemporaneous media reporting provided by Michael Butler in his excellent paper: M Butler, (2020), 'The Increasing use and threat of section 100A', 24(2) The Tax Specialist at 45 -61 (**Butler**).

operated with flagrant disregard for the law. Data from the time estimated that 6,688 companies involved in schemes meeting this description, with a total revenue leakage in the billions of dollars[9]. It led to a Royal Commission (the Costigan Royal Commission) and several individuals involved in the planning, promotion or carrying out of these schemes being charged and imprisoned[10].

2.1.2 Judicial attitudes to the interpretation of tax legislation

14. The 'strict literalism' that characterised the High Court under Sir Garfield Barwick[11], who served as the Chief Justice from 1964 to 1981, fomented a facilitative environment for the ingenuity of taxpayers and their advisors to flourish, largely unfettered, and be channelled into all manner of increasing aggressive tax planning.

15. Kirby J, in his decision in *Raftland Pty Ltd as trustee of the Raftland Trust v Commissioner of Taxation*[12] (**Raftland**), described the period as being the '…heyday of tax avoidance schemes that found favour in [the High Court]'. Kirby J contextualises this comment, and the evolution of the law to a more purposive approach to statutory interpretation[13], in the following passages:

> "[109] *Murphy J's dissent in Westraders*: In the heyday of tax avoidance schemes that found favour in this Court, according to a literal interpretation of the impugned documentation, Murphy J, in dissent in Federal Commissioner of Taxation v Westraders Pty Ltd, cited the foregoing United States decisions. He expressed a preference for their approach. He favoured it over the kind of "strict literalism" that he regarded as prone to defeat the obvious purpose of revenue legislation…
>
> [110] Looking back at Westraders, some of the remarks of Murphy J appear to **herald the general change that was later to emerge in this Court in the interpretation of federal legislation - a move from the "literalist" approach of earlier times to the more "purposive" approach now generally followed**. Murphy J's search was for the purpose

[9] Freiberg, A. (1988). '*Ripples from the bottom of the harbour: some social ramifications of taxation fraud*'. Criminal Law Journal, 12(3), 136–192.

[10] Ibid.

[11] See *Westraders v Federal Commissioner of Taxation* (1978) 8 ATR 43 and Butler.

[12] [2008] HCA 21, per Kirby J at 109.

[13] The decisions with Kirby J points to as being indicative of the more 'purposes' approach to statutory interpretation are (as at footnote [74] of the judgement): *CIC Insurance Ltd v Bankstown Football Club Ltd* (1997) 187 CLR 384 at 408; [1997] HCA 2; *Newcastle City Council v GIO General Ltd* [1997] HCA 53; (1997) 191 CLR 85 at 112-113; [1997] HCA 53; *Project Blue Sky Inc v Australian Broadcasting Authority* [1998] HCA 28; (1998) 194 CLR 355 at 381 [69], 384 [78]; [1998] HCA 28.

and object of the applicable statutory provisions. He declared that it was "an error to think that the only acceptable method of interpretation is strict literalism". He went on:

> "In tax cases, the prevailing trend in Australia is now so absolutely literalistic that it has become a disquieting phenomenon. Because of it, scorn for tax decisions is being expressed constantly, not only by legislators who consider that their Acts are being mocked, but even by those who benefit. In my opinion, strictly literal interpretation of a tax Act is an open invitation to artificial and contrived tax avoidance. Progress towards a free society will not be advanced by attributing to Parliament meanings which no one believes it intended so that income tax becomes optional for the rich while remaining compulsory for most income earners." (emphasis added and footnotes omitted)

2.1.3 The Commissioner's administrative capacity and resources

16. The Commissioner's capacity to detect the most egregious taxpayers and tax avoidance behaviour and enforce the law against them was significantly limited in the 1970's in comparison to modern times. Indeed, one can imagine Messrs Edward Cain, the Commissioner of Taxation from 1964 to 1976, and William O'Reilly, the Commissioner of Taxation from 1976 to 1984, looking with envy upon what their successors have enjoyed, in terms of:

    a. funding and personnel levels allocated to the Australian Taxation Office (**ATO**), which have expanded considerably on an ever-increasing upward trajectory;

    b. the cumulative advancement in technology over the past four decades, and the Commissioner's capacity to employ technology to detect and monitor taxpayer behaviour in 'real time', through sophisticated data-matching and similar programs; and

    c. the scope and reach of inter-entity information sharing and collaboration agreements, both among domestic regulators and tax authorities abroad.

2.1.4 Limitations of the tax system in the 1970's

17. The tax system in the 1970's was vastly different to that with which we are familiar with today. The tax system relied on a narrow tax base, that didn't include capital gains. The 'classical' system of dividend taxation meant that company profits were effectively double taxed, at the entity and shareholder level, and made the use of trusts widely prevalent for the comparative tax

benefits viz. companies[14]. And the Commissioner's arsenal of anti-avoidance provisions was largely limited to section 260 of the 1936 Act.

18. The year 1979 marks, with almost uncanny precision, the starting point of what would be two decades of profound foundational reform of the Australian taxation system, largely designed by two individuals: John Howard and Paul Keating, each serving as Treasurer and Prime Minster respectively. The period between 1979 and 1999 would see:

    a. the introduction of the general anti-avoidance provisions of Part IVA of the 1936 Act in 1981 (including the introduction of specific 'dividend stripping' provisions contained in section 177E of the 1936 Act);

    b. perhaps the most significant broadening of the tax base with the introduction of capital gains tax in 1985;

    c. perhaps the most significant reform to the taxation treatment of companies with the introduction of the dividend imputation system in 1987;

    d. a specific anti-avoidance provision aimed at shareholders making 'disguised' distributions of corporate retained earnings, through the introduction of Division 7A of the 1936 Act in 1997;

    e. the staged reduction of the (headline) corporate tax rate from 46% in 1980 to 36% in 1999 (and now between 30% and 25%);

    f. the staged reduction of the (headline) highest individual marginal tax rate from 61.5% in 1980 to 47% in 1999 (and now at 45%, excluding Medicare levy);

    g. the repeal death and estate duties by most states and territories (by 1982).

2.2 The evolutionary response: towards a 'higher animal'

19. This condition of 'tension and destruction' of the era which seeded section 100A, which I have described, called for a Darwinian response from the legislature. To not do so would impugn the legislatures status as the apex species in our sociological environment. And so, in 1979, section 100A emerged: a reactive, evolutionary response from the legislature to the tax non-compliance environment that prevailed at the time. So much is made clear from the explanatory material that

[14] D Dixon and R Van, '*An Examination of the Imputation System in the Context of the Erosion of the Company Tax Base*', 1987, 4 Australian Tax Forum 63.

accompanied the introduction of section 100A[15] and contemporaneous commentary in the time of, and preceding, its introduction[16].

20. Looking at section 100A through a Darwinist prism, if section 100A is, as I have posited, a product of an evolutionary response which directly followed the tension and destruction of the 1970's non-compliance tax environment, we must now ask: is section 100A a 'higher animal'?

2.2.1 An evaluative standard for tax law

21. There are many normative and empirical standards against which a law may be evaluated. Invariably, political or ideological beliefs will influence that evaluation, as might financial self-interest. For the purposes of this paper, being of the view that a tenacious theory is a good one, I look to the evaluative standards against which tax laws may be appraised posited by another great theoretician, the Scottish economic philosopher Adam Smith (c.1723 to 1790).

22. Smith, in his seminal work *An Enquiry into the Nature and Causes of the Wealth of Nations*[17], laid down four 'canons' of taxation against which a good system of taxation, and by extension, a good tax law, should conform[18]. The four canons are: *equity, neutrality, certainty, and efficiency*. In this paper, I will focus on one of the Smithsonian canons: certainty.

2.2.2 Certainty in tax law: an evaluative analysis

23. Adam Smith's canon that a tax law should aspire to certainty in terms and application was cited by the High Court in *Giris Pty Limited v Federal Commissioner of Taxation*[19] (**Giris**).

24. Giris brought sections 99 and 99A of the 1936 Act to the court examination: more particularly, subsection 99A(2), insofar as it affords the Commissioner of Taxation (the **Commissioner**) a discretion to form an opinion about the reasonableness of section 99A applying in certain circumstances.

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[15] The Explanatory Memorandum to the *Income Tax Assessment Amendment Bill (No 5),* 1978 (the **Explanatory Memorandum**).

[16] See the then Treasurer John Howard's Press Release of 11 June 1978 (the **Press Release**), in which the government announced its intention to introduce legislation designed to combat 'trust stripping schemes' and the detailed survey of contemporaneous media reporting provided by Michael Butler in his excellent paper: M Butler, (2020), '*The Increasing use and threat of section 100A*', 24(2) *The Tax Specialist* at 45 -61.

[17] Smith, Adam. *An inquiry into the nature and causes of the wealth of* nations, Glasgow, 1805.

[18] For further reading, see: Douglas Brown, '*The Canons of Construction of Taxation and Revenue Legislation'* (1976) 5 AT Rev 81.

[19] (1969) 119 CLR 365 (**Giris**).

25. The taxpayer in Giris, inter alia, submitted that the discretionary element of subsection 99A(2), '…*involved a delegation by Parliament of its legislative power which was invalid as going too far and amounting to an abandonment by Parliament of its function and duty'*, and consequently was constitutionally ultra vires[20]. Ultimately, the court held that subsection 99A was not 'outside the bounds' of constitutional validity, but that it was (in the view of Windeyer J), '…*very close to the boundary, and that it would be questionable as a precedent for legislation of a similar character*'[21].

26. In Giris, Windeyer J, opens his judgement with the following exposition:

> "[1] In 1964 the Australian Parliament amended the Income Tax Assessment Act and enacted ss. 99 and 99A. This was more than two hundred years since the Wealth of Nations was published. **Yet anyone remembering the record of Adam Smith's four "canons" of taxation must be beset by misgivings and regrets that Parliament forgot it**:
>
> > "The tax which each individual is bound to pay **ought to be certain, and not arbitrary**. The time of payment, the manner of payment, the quantity to be paid **ought all to be clear and plain to the contributor, and to every other person**. Where it is otherwise, **every person subject to the tax is put more or less in the power of the taxgatherer**. . . . "
>
> [2] Yet Parliament has in effect left it to the discretion of the Commissioner in certain circumstances to say whether a taxpayer should be required to pay tax in respect of certain transactions at a higher or at a lower rate. The criterion of differentiation is whether "the Commissioner is of the opinion that it would be unreasonable that s. 99A should apply". And there are no **absolute, precise or objectively determinable** tests of what is here reasonable or unreasonable." (emphasis added)

2.2.3 Smith and Windeyer J's challenge

27. So, does section 100A withstand the scrutiny when put up to the light against:

    e. Smith's canon that tax law should be 'certain…and not arbitrary' such that it is 'clear and plain to the contributor'; and

[20] Giris, per Windeyer J at [3].

[21] Giris, per Windeyer J at [6].

f. the yardstick Windeyer J sets out in Giris, that a tax law should aspire to provide an 'absolute, precise or objectively determinable' basis for its application?[22]

2.2.4 'Certain…and not arbitrary'

28. For the reasons following, I submit that section 100A is not capable of interpretation with any certainty. Rather, the broad scope of section 100A, and basic elements which determine its application, means that section 100A may attach itself without constraint to a range of arrangements, save for those that fall within the amorphous 'ordinary family or commercial dealing' limitation, which we will get to shortly. This includes arrangements which taxpayers and their advisors might otherwise regard as being mainstream and innocuous forms of tax planning and, in any event, not characteristic of tax avoidance or aggressive tax planning behaviour. And in entering such arrangements, taxpayers and their advisors may unknowingly be stepping into the complexity of section 100A.

The legislative text of section 100A: the 'express' limitations on the scope of its application in the legislative text

29. On the express terms of section 100A, its application is only excluded where the conditions set out in the following provisions are satisfied:

a. Subsection 100A(13), referred to in this paper as the "**ordinary family or commercial dealing**" condition, which provides:

> agreement" means any agreement, arrangement or understanding, whether formal or informal, whether express or implied and whether 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**. (emphasis added)

b. Subsection 100A(8), referred to in this paper as the '**tax reduction purpose**' condition, which provides:

> (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**

[22] it should be kept in mind that, unlike section 99A, section 100A does not provide for any discretionary or opinionative element afforded to the Commissioner, but rather is a self-executing provision to be assessed by the taxpayer, and that Windeyer J comments were made in 1969, two decades before the introduction of section 100A.

> **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**.

The legislative scope of section 100A: is there a limitation on the scope of its application based on the statements made about its purpose and intent at the time of its introduction?

30. The question of whether there is a limitation on the scope section 100A's application to those arrangements or schemes that exhibit the features the explanatory material accompanying its introduction in 1979 suggest, though not exhaustively[23], that it was intended to counter, or that were prevalent at the time that it was introduced, is a vexed one.

31. Other commentators and professional colleagues have canvassed, with a detailed and skilful level of analysis, the extrinsic materials which accompanied the introduction of Division 100A[24]. I have no desire to elongate this paper more than necessary, but the full text of the explanatory statement of the then Treasurer, John Howard, on 11 June 1978 (the **1978 Statement**) and the explanatory memorandum that accompanied the Income Tax Assessment Amendment Bill (No 5) 1978 (the **Explanatory Memorandum**) (together, the **Explanatory Materials**), bears repeating, lest something be lost in summarisation.

32. The 1978 Statement provides:

> "A feature of several of the schemes is a very wide power given to the trustee under the terms of the trust instrument as to the distribution or application of trust income. In reliance on this power, the trustee agrees with promoters of tax schemes and other compliant parties to distribute or apply the bulk of the trust income - either directly or through an interposed trust - for the apparent benefit of specially introduced beneficiaries who do not pay any, or any substantial, amount of tax on the amount distributed or applied.
>
> In some cases the nominal beneficiary selected is a tax-exempt body, such as a charitable institution or sporting association. In other cases, it is a company, set up for the purpose by the promoters of the scheme, that by one means or another escapes payment of tax on the income. One technique is to set artificially-created paper 'losses' off against the income received from the trust. Another technique is to strip assets from the recipient company so that tax assessed on the income cannot be collected. Yet again, the income

[23] See: *Federal Commissioner of Taxation v Prestige Motors* (1998) 82 FCR 195, per Hill and Sackville JJ (Beaumont J agreeing) at 220 (**Prestige Motors**).

[24] See: M Butler, (2020), '*The Increasing use and threat of section 100A'*, 24(2) The Tax Specialist at 45 -61; P Sokolowski, (2018), *'Plato's Cave, section 100A and the reality behind the shadows*, October 2018 Breakfast Club, The Tax Institute, 25 October 2018; B Freudenberg, (2022), '*Ordinary Family Dealings in s 100A: Scant law leading to confused lore*', Tasmanian Convention, The Tax Institute, 8-9 September 2022.

may be distributed to non-resident individuals each of whom does not have enough Australian taxable income to be liable to tax, but who will account for the income to the Australian family concerned.

The essential element common to the schemes is that, while the income concerned is effectively freed from tax in the hands of the nominal beneficiary, the terms of the underlying arrangement ensure that the beneficiary does not enjoy anything like the full use or benefit of the income. Instead, the arrangement, requires a broadly equivalent capital sum - but reduced by the promoter's fee and a modest reward for the services of any participating exempt body - to be directed to persons intended all along as the real beneficiaries of the trust.

The arrangements are often very complex and the party responsible for putting the real beneficiaries in funds may be an associate of the nominal beneficiary. The return of the funds may be achieved by a settlement on another trust established for the benefit of the real beneficiaries of the main trust or their families, by the making to them of what is known colloquially as a 'collapsible loan', i.e. a loan that effectively does not have to be repaid, or through the nominal beneficiary having acquired the right to the income by payment to the real beneficiaries of a broadly equivalent sum.

...

The legislation to counter tax avoidance through trust stripping schemes will broadly be on the lines that any distribution or application of income by a trustee, pursuant to a relevant contract, arrangement or understanding, will be treated as not having been made. This means that the trustee will be liable to be assessed and pay tax at the rate of 60 per cent on the amount involved as if it had been accumulated in the trust.

In broad terms, a relevant contract, arrangement, or understanding will be one the terms of which contemplate conferring on a particular beneficiary a 'present entitlement' to income of a trust, and under which the beneficiary or an associated party is to provide funds or benefits in money's worth for another person, company or trust."

33. The Explanatory Memorandum provides:

"The arrangements generally turn on the operation of section 97 which, as described earlier in this memorandum, provides for a beneficiary to be subject to tax where the beneficiary is presently entitled to a share of the income of a trust estate and is not under any legal disability. In those circumstances, the beneficiary's share of the trust net income is included in his assessable income and the trustee is not required to pay tax on the income. Where the trustee has a discretion to pay or apply income for the benefit of one or more specified beneficiaries and the trustee exercises the discretion in favour of a

> beneficiary, section 101 deems the beneficiary to be presently entitled to the amount paid or applied. Such an amount thus also falls to be taxed to the beneficiary under section 97.
>
> A common feature of the tax avoidance arrangements at which the proposed section is directed is for a specially introduced beneficiary to be made presently entitled to income of the trust estate, so that the trustee is relieved of any tax liability on the income. Under the arrangements, the beneficiary also does not pay tax, e.g., because of a peculiar tax status. For example, the beneficiary may be a body or organisation that qualifies for exemption of its income under specific provisions, or it may be another trust that has sufficient deductible losses to absorb its share of income as a beneficiary of the first trust estate.
>
> Invariably, the arrangements require this introduced beneficiary to retain only a minor portion of the trust income and to ensure that some other person - the one actually intended to take the benefit - effectively secures enjoyment of the major portion of the trust income but in tax-free form (e.g., by the settlement of a capital sum in another trust estate for the benefit of that person).
>
> The proposed section 100A will look to the existence of an agreement or arrangement that is entered into otherwise than in the course of ordinary family or commercial dealing and under, or as a result of which, present entitlement to a share of trust income is conferred on a beneficiary in return for the payment of money or the provision of valuable benefits to some other person, company or trust. In those circumstances, the section will require the income of the trust that is dealt with under the 'reimbursement agreement' to be treated as having been accumulated by the trustee as income to which no beneficiary is presently entitled. This will result in the trustee being liable to pay tax on the income under section 99A at the prescribed tax rate, 61.5 per cent for 1978-79.
>
> The new section is to apply to reimbursement arrangements giving present entitlement to an introduced beneficiary where the relevant trust income is paid to or applied for the benefit of the beneficiary after 11 June 1978, the day on which the Government announced its intention to introduce legislation to overcome these arrangements."

34. In decisions involving section 100A, counsel have advanced the argument that the scope of section 100A should be limited or 'read down', as applicable only to arrangements that align to those which are set out in the Explanatory Materials: that is, that section 100A is a specific anti-avoidance provision introduced to counter a specific form of 'trust stripping' arrangement, that involved the introduction or interposition of a specific entity, with a preferential tax profile (for example, one that is tax exempt or that has carried-forward tax losses), resulting in a nil or comparatively low tax outcome[25].

[25] See: Prestige Motors, submissions advance by D Bloom QC on behalf of the taxpayer, as set out at by the court at 218.

35. Courts have generally given attempts to circumscribe section 100A to a specific type of arrangement exhibiting the precise features outlined in the Explanatory Materials a swift and resounding denouncement. Illustratively, when such an argument was advanced by Counsel for the taxpayer in *Commissioner of Taxation v Prestige Motors Pty Limited*[26] (**Prestige Motors**), the courts (Hill and Sackville JJ) addressed it as follows[27]:

> "Mr Bloom relied primarily on the proposition that s 100A is a "specific, anti-avoidance" provision designed to deal with trust stripping to support the submission that the section should be construed more narrowly than its language itself might suggest. He submitted that the extraneous materials demonstrated that what the legislators had in mind was a specific form of trust stripping, involving an existing trust which has income that would be assessable to the beneficiaries or the trustee if steps were not taken. Accordingly, a new beneficiary, such as a tax-exempt body, is introduced into the trust and the trust income is effectively diverted to the introduced beneficiary. That beneficiary effectively "reimburses" the major portion of the income received by it to the existing beneficiary or trustee, but in a tax free or largely tax-free form.
>
> There are several answers to this submission. **First, the mere fact that s 100A can be characterised as a specific anti-avoidance provision does not demonstrate that it should be given a narrower approach than its ordinary meaning and grammatical sense suggest**. It is clear from *Cooper Brookes v FCT* that a specific anti-avoidance provision (there s 80C of the *ITAA*) can be given its literal meaning if to do so gives effect to the intention of the legislature, although the literal interpretation will not be adopted if it results in an operation which is capricious and irrational: at 310-311, per Stephen J; at 321 per Mason and Wilson JJ. Of course, as we have said, this is consistent with s 100A being construed with an eye to the mischief it was designed to remedy: *Federal Commissioner of Taxation v Radilo Enterprises Pty Ltd* (1997) 97 ATC 4151, at 4155, per Lee J.
>
> Secondly, there is nothing to suggest that irrational or absurd consequences flow from applying s 100A to trusts set up in consequence of what are otherwise reimbursement agreements, as distinct from trusts which were in existence prior to the agreements being entered into. It must be remembered that s 100A has its own safeguards, notably the exclusion of agreements not entered into for tax avoidance purposes (s 100A(8)) and of agreements entered into in the course of ordinary family or commercial dealing (s 100A(13)). There may well be tax avoidance arrangements that satisfy s 100A, yet contemplate the creation of a new trust. For example, the arrangements may provide from the beginning a class of beneficiaries wide enough to include a tax exempt body, with the intention that expected income be paid to that body in return for an agreed capital payment.

[26] (1998) 82 FCR 195.

[27] Prestige Motors, at 218 to 219.

> Of course, the fact that a new trust is to be created may bear on the question of purpose and of ordinary commercial or family dealing. **But there is no reason to read down the language of s 100A to exclude a particular category of tax avoidance arrangements that otherwise satisfy the statutory language, merely because the trust was not in existence when the arrangements were formulated**.
>
> Thirdly, the extrinsic materials do not support the proposition that Parliament intended to impose the special rate of tax only in the circumstances identified by Mr Bloom. It is clear that the Treasurer's statement of 11 June 1978 and the Explanatory Memorandum accompanying the subsequent Bill identified trust stripping as the avoidance device that had to be counteracted. **But it is equally clear that the examples given were intended to be illustrative, and not an exhaustive statement of the transactions that were to be subject to the legislation**. This was made explicit in the Treasurer's second reading speech which pointed out that there were several variants of a trust stripping scheme but "for the most part" they relied on a nominal beneficiary being introduced into a trust and being made presently entitled to income: *Cth Parl Deb*, HR, 23 November 1978, 3310.
>
> Examples given in Explanatory Memoranda or second reading speeches of transactions or arrangements intended to be caught by legislation may be very helpful in identifying the mischief to be addressed and in construing otherwise ambiguous legislation so that it does apply to the identified transactions or arrangements. **But considerable care should be exercised before relying on examples given in this way in order to read down the statutory language. The extrinsic materials in the present case are entirely consistent with the legislation having been framed broadly enough to catch not merely the transactions referred to in those materials, but other arrangements having similar characteristics**. For example, all the illustrations of trust stripping arrangements given in the extrinsic materials contemplate the payment of trust income to a body not liable to pay any tax at all (as was the case with RLAV by reason of its accumulated losses). Yet there is no reason to think that s 100A was intended to be restricted to arrangements which provide for the payment of income to entities not liable to **any** tax. The RLAV transaction, as we have said, involved the payment of interest to Cholmondeley, subject to the deduction of withholding tax at the rate of 10 per cent. The fact that tax at this rate was deducted (comparing, as it does, to the special rate of up to 61.5 per cent) hardly takes the transaction outside the mischief Parliament sought to attack." (emphasis added and footnotes omitted)

36. However, while Courts have rejected the proposition, on submission from taxpayers, that the broad application of section 100A should be limited or read down by reference to the Explanatory Materials and the arrangements outlined therein, arguments that the Explanatory Materials should inform the interpretation of section 100A on more specific questions have found favour.

37. In **Guardian AIT**, Logan J looked to the Explanatory Materials in considering the part that the adjective 'ordinary' has to play in the definition of 'ordinary family or commercial dealing'. His Honour states (at 144):

> "Read in context, the adjective "ordinary" in "ordinary family or commercial dealing" has particular work to do. It is used in contradistinction to "extraordinary". It refers to a dealing which contains no element of artificiality. **This is confirmed by reference to the relevant explanatory memorandum, where one finds reference to addressing the mischief of specially introduced beneficiaries having a fiscally advantageous status**. This explanatory memorandum confirms what a reading of s 100A would suggest, which is that the section is directed to addressing, according to its terms, "trust-stripping"." (emphasis added)

The statutory language of section 100A

38. We recall that in Grilis, Windeyer J says that where the legislation imposes a test (or, inferentially, a standard against which a taxpayer's behaviour is to be assessed), then it should be a test or a standard that is 'absolute, precise or objectively determinable'.

39. The language in which section 100A is couched does not make for easy reading. Indeed, it has been judicially described as being, in parts, 'awkward'[28]. More materially, however, the key words and phrases chosen by the legislature are ones which are inherently subjective and open to disparate interpretation, including by incisive judicial minds.

40. We return to the central concept, and only express limitation on the application of, section 100A: an 'ordinary commercial of family dealing'. An arrangement will only be excluded from the operation of section 100A where it answers to this definition. Can an 'ordinary family or commercial dealing' be understood in an 'absolute, precise or objectively determinable' way? I argue that it cannot.

41. Consider the adjective 'ordinary'. What is 'ordinary' is entirely subjective. What to one person may be entirely 'ordinary' may to another person be entirely 'extraordinary'. In everyday usage, one might think that something 'ordinary' is something that happens usual, mainstream, and common. However, in the context of section 100A, the Commissioner takes a different view.

42. In describing the term 'ordinary', as used in section 100A, both courts and the Commissioner (in his administrative statements' have been similarly nebulous. What utility is there in saying, for example, that the term 'ordinary' is used in section 100A '…in contradistinction to

[28] *Guardian AIT Pty Ltd atf Australian Investment Trust v Commissioner of Taxation* [2021] FCA 1619, per Logan J, at [125], referring to section 100A(8) and 'its succession of negatives' and [142], referring to section 100A(7).

extraordinary…'[29]?. I submit it is entirely unhelpful to define one ambiguous and subjective term by reference to another equally ambiguous and subjective term. Indeed, there is a circularity in this manner of definition that borders on being satirical.

43. Similarly, against what standard might one evaluate how family members transact or financially interact, and determine what is 'ordinary' and what is not? And what is a valid family objective as against an invalid family objective? Again, reasonable people will invariably differ in their views on these matters, and as the discussion of the recently decided cases involving section 100A which follows in this paper I hope will show.

44. Similar quandaries arise in considering what might comprise an 'ordinary' commercial dealing or a valid commercial objective. This is relevant in a practical context as an often cited 'commercial' objective in the establishment of a particular structure or arrangement is the desire to achieve 'asset protection' or 'business succession': the discussion which follows in this paper about Guardian and BBlood (both the primary and appeal decisions) explores the judicial consideration of those objectives in further detail.

45. In my submission, the breadth of section 100A and the expansiveness of its language should not be presumed to be an accident or failing by the legislature. Rather, the expansiveness of the language serves a purpose. It ensures that section 100A remains a pliable and adaptable provision, such that it may attach to arrangements that may evolved over time but were not in contemplation at the time of its enactment, or indeed, arrangements or schemes that may be crafted specifically to avoid or subvert it. An apt quotation which is illustrative of this is one also attributable to Charles Darwin, though apocryphally:

"Building a better mousetrap merely results in smarter mice!"

46. But structuring a provision such that is expressed in expansive language, that is incapable of absolute, precise, and objective definition or interpretation, to stop the (sneaky) mice getting smarter, has an unwanted side-effect. It increases the cost and burden of compliance for taxpayers that simply want to structure their affairs and meet their tax obligations with certainty, without the spectre of an examination by the Commissioner looming over them. As is typical of anti-avoidance tax legislation, the measures adopted to stop the 'troublesome 3%'[30] of taxpayers who will do the wrong thing imposes a compliance burden on the 97% of taxpayers who want to do the right thing.

Judicial consideration and interpretation

47. Of course, the task of statutory interpretation falls to the courts. Where, as with section 100A, parliament drafts a provision which, drawing on a fishing metaphor, casts a wide net into the

[29] BBlood Enterprises, per Thawley J, at 144.

[30] I attribute this phrase to my colleague and Partner, Andrew O'Bryan.

ocean, we rely on judges to sort through the 'catch' and decide which fish should be returned to the water to go about things as before and which should face more grave and less palatable consequences.

Judicial consideration of section 100A

48. In its 43 years, section 100A has been the subject of direct judicial consideration in just six cases. Listed chronologically, with a summary of the relevant appeal history, these cases are:

    a. *East Finchley Pty Ltd v Federal Commissioner of Taxation*[31], 1989, heard by a single judge of the Federal Court (Hill J), who held for the Commissioner (**East Finchley**).

       First Instance: heard in the Administrative Appeals Tribunal (**AAT**) which found in favour of the Commissioner.

    b. *Prestige Motors*, 1998, heard by the Full Court of the Federal Court (Beaumont, Hill and Sackville JJ), which held for the Commissioner.

       First instance: heard in the Federal Court before Emmet J, who held in favour of the Taxpayer (Commissioner's appeal allowed).

    c. *Idlecroft Pty Limited v Commissioner of Taxation*[32], 2005, heard by the Full Court of the Federal Court (Ryan, Tamberlin and Kiefel JJ), which held for the Commissioner (**Idlecroft**);

       First Instance: heard in the Federal Court before Spender J, who held in favour of the Commissioner (Taxpayer's appeal disallowed)

    d. *Raftland*, 2008, heard by the High Court (Gleeson CJ, Gummow, Kirby, Heydon and Crennan JJ), which held for the Commissioner (**Raftland**).

       Appeal: heard in the Full Federal Court before Dowsett, Conti and Edmonds JJ, who held for the Commissioner (Taxpayer's appeal disallowed).

       First Instance: heard in the Federal Court before Keifel J, who held for the Commissioner (Taxpayer's appeal disallowed).

    e. Guardian AIT, 2021, heard by a single judge the Federal Court (Logan J), who held for the Taxpayer (**Guardian AIT**).

       Appeal: heard in the Full Federal Court before Perry, Derrington and Hespe JJ, which held (on section 100A) for the Taxpayer.

[31] (1989) 20 ATR 1623.

[32] [2005] FCAFC 141.

f. *BBlood Enterprises Pty Ltd v Commissioner of Taxation*[33], 2022, heard by a single judge of the Federal Court (Thawley J), who held for the Commissioner (**BBlood Enterprises**).

Appeal: heard in the Full Federal Court before Moshinsky, Colvin and Hespe JJ, which held for the Commissioner.

49. The limited body of jurisprudence addressed to section 100A has yielded important judicial interpretational comment on section 100A, from some of the most influential tax jurists of the times in which the relevant cases were heard and decided (Keifel[34], Hill[35] and Edmonds[36] JJ among them).

50. However, in looking for overarching principles of general application for 100A from the reasons of judges, there is a risk of 'over-reading' judicial comment made in obiter, as Hill J cautions in Prestige Motors (at 220):

> "The same caution [*i.e., reading down legislation by reference to extrinsic material*] should be exercised when considering obiter dicta in judgments. Just as the extrinsic materials should not be read more restrictively than the authors intended, so comments made on decided cases should be read in context. For example, *in East Finchley Pty Ltd v Federal Commissioner of Taxation* (1989) 90 ALR 457, at 472-473, Hill J gave illustrations of trust stripping arrangements to which s 100A was clearly intended to apply. However, his Honour plainly did not assay an exhaustive collection of such arrangements and the judgment should not be read as though it did."

51. The search for overarching principles of general application for 100A from the decided cases is also hampered by this incontrovertible fact: courts hear and rule on the facts that are put by the parties to the proceeding before them. The section 100A cases that have gone before the High Court, the Federal Court and the AAT have all involved idiosyncratic fact patterns and arrangements. Moreover, the fact patterns and arrangements that have been presented to the courts in the section 100A cases lend themselves to description as artificial at best and egregious at worst. To illustrate this, I provide a brief survey of the factual background of the decided cases on section 100A (excluding Guardian AIT and BBlood, which are the subject of detailed consideration in this paper), aware of the risk of being overly reductive and reducing the complexity of these matters to brief headlines:

East Finchley

[33] [2022] FCA 1112.

[34] Raftland at first instance (Federal Court) and Idelcroft on appeal (Full Federal Court).

[35] East Finchley at first instance (Federal Court) and Prestige Motors on appeal (Full Federal Court).

[36] Raftland on appeal (Full Federal Court).

The taxpayer company was the trustee of a discretionary family trust which resolved to distribute the trust's income for the 1983 year amongst 126 individuals in India (who were relatives of the directors) in equal shares each of $585, which was then the non-resident tax free threshold. In July 1983, the director went to India and arranged for a pro forma letter to be left with each of the non-resident beneficiaries advising of the distributions and that an amount would be credited to a loan account in the books of the trust in each of their names. He also arranged for pro forma letters to be signed by the beneficiaries authorising the crediting of the loan accounts. In August 1988 the taxpayer borrowed the funds necessary to permit it to distribute to the non-resident beneficiaries the cash amounts in accordance with what was said to have been the distributions. However, those distributions were only made after the Commissioner applied s.100A.

Prestige Motors

The taxpayer was a member of a group of companies and carried on business as a wholesaler and retailer of motor vehicles. In 1979, following a transaction involving Ronald Lyons Australia (Vic) Pty Limited (**RLAV**), the business of the taxpayer began to be carried on through a trust. RLAV was an unrelated, insolvent company with tax losses. The RLAV transaction involved RLAV applying 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. The taxpayer made distributions from trust income to RLAV which were offset by prior year tax losses. Two further, unrelated transactions entered by the taxpayer in 1981 and 1984 involved the issue of 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 pursuant to former s.112A.

Idlecroft

The facts involved five trustees of family discretionary trusts that entered into joint venture agreements with Westside Commerce Centre Pty Ltd (**WCC**) to develop a property. Under the agreements, the taxpayers agreed to fund the development by adding WCC as a beneficiary of their trusts and to appoint trust income to WCC. The taxpayers indicated in their returns that WCC was presently entitled as a beneficiary to the appointed income within the meaning of s.97. WCC had accumulated tax losses, and so it did not pay tax on the income.

Raftland

Raftland Pty Ltd was a member of a group of companies involved in real property development and leasing. Through the implementation of a diabolically complex set of arrangements and transactions (ultimately found to be a ‘sham’ by the High Court), it sought to minimise its income tax by channelling profits through a unit trust with substantial accumulated tax losses.

'Hard cases make bad law'[37]

52. Recalling the oft-repeated legal adage that "*hard cases make bad law"*[38], one is inevitably led to conclude that the idiosyncratic fact patters and arrangements presented to the courts for judicial adjudication in the decided cases, did not provide the best or most appropriate vehicle for judges to elucidate principles of broad application in respect of section 100A, such as to bring greater certainty to the amorphous concepts and language within which section 100A is framed.

53. Moreover, the fact patterns and arrangements that were before the courts in the decided cases, and the aggressive or egregious features of those fact patterns and arrangements, may also explain why the 'ordinary family or commercial dealing' concept, which is a cornerstone of section 100A and the only express limitation to the application of section 100A, was not the subject of direct judicial consideration until the Guardian AIT and BBlood Enterprises decisions.

2.3 Are taxpayers '…put more or less in the power of the taxgatherer'?

54. Let us return now to Adam Smith and assess the current state of section 100A against his injunction, that where a tax law is not certain or is arbitrary:

'…every person subject to the tax is put more or less in the power of the taxgatherer. . .. ".

55. Having considered whether section 100A is beset with interpretative uncertainty, and hopefully convinced the reader that it is so, does this mean that taxpayers and their advisors are largely beholden to the power of the Commissioner as to the application of section 100A, and the vagaries in his views as they may evolve from time-to-time?

2.3.1 ATO Guidance

56. There is no doubt of this: to the extent that the legislature and the courts have left an

[37] I mean no disrespect when referring to the decided cases as standing for 'bad law', nor do I purport to say that the judges hearing those cases were driven by a sense of restorative justice rather than legal reason and precedent in making these decisions. I merely suggest that Windeyer J's comments in Giris, that a tax law that lacks clarity is one which measures up poorly as against the evaluative standards which he propounds in that case, would not apply favourably to section 100A.

[38] See: Heath J of the High Court of New Zealand, *Bad Cases and Bad Law*, [2008] Waikato Law Review 1. His Honour, in an extra-curial paper, explains the concept as follows: Hard cases make bad law' is a well-known legal phrase. It describes a difficult case which might cause the clarity (or purity) of the law to be obscured by exceptions and strained interpretations, designed to achieve justice in a particular case. The underlying idea expressed in the phrase is the need for all courts to apply statutes and binding precedents in a manner that produces consistency in the application of the law.

interpretative 'gap' in section 100A, the Commissioner has filled it.

57. Speaking in other fora, I have described a rediscovery of 'renaissance' in administrative interest in section 100A that commenced in or around 2014 and culminating in the Commissioner's first public 'shot across the bow', a 'Factsheet' published on the ATO website initially in July 2014 and updated in May 2016 and again in July 2022[39] (**ATO Factsheet**).

58. Following the issue of the ATO Factsheet, the Commissioner embarked on a path to issuing more formalised guidance. This commenced with the release of TR 2022/D1 on 29 April 2022. TR 2022/D1 sets out the Commissioner's interpretative technical views on section 100A, illustrated with numerous examples. On the same date, the Commissioner released a draft Practical Compliance Guideline PCG 2022/D1 (**PCG 2022/D1**). Practical Compliance Guidelines represents a relatively new form of ATO 'product', which in the Commissioner's words, are intended to 'provide broad law administration guidance, addressing the practical implications of tax laws and outlining our administrative approach'[40].

59. Following a public consultation period, the Commissioner released his administrative views in final, in TR 2022/4 and PCG 2022/2 (both released on 12 December 2022). The public consultation did result in a number of material revisions to TR 2022/D1 and PCG 2022/2, and **Appendix 2** of this paper sets out a comparative analysis of TR 2022/4 against TR 2022/D1 and PCG 2022/2 against PCG 2022/D1. In this paper, I refer to the ATO Factsheet, TR 2022/4 and PCG 2022/2) collectively as the **ATO Guidance Material**.

60. A few additional points should be made for context.

61. *First*, while the ATO Factsheet was the 'first shot across the bow', as I've described it, the Commissioner's focus on section 100A has been presaged before then, in the comments of senior ATO officials in open forum, and by being ventilated as an issue in a number of taxpayer audits and examination, some of which my colleagues and I were involved in.

62. *Second*, while the Commissioner did fill the interpretative gap in section 100A, he did in large part in response to calls from the profession that the Commissioner 'show his hand' on section 100A and publish administrative and compliance guidance. Of course, when the Commissioner did so, the content of that guidance was not everything that the profession was hoping for: when it is the taxgatherer proffering a view one should not be surprised that it is a view which has a bias toward tax collection!

[39] ATO, '*Trust taxation - reimbursement* agreement', accessible at: https://www.ato.gov.au/General/Trusts/In-detail/Trust-entitlements---draft-guidance/Trust-taxation---reimbursement-agreement/

[40] Sourced at: https://www.ato.gov.au/General/ATO-advice-and-guidance/ATO-guidance-products/Practical-compliance-guidelines/

63. *Third*, with his section 100A guidance, the Commissioner has acknowledged the limitations of his administrative opinion on section 100A, which lends itself to widely diverging views, and one thinks it is for this reason that he has both chosen to pursue litigation against taxpayers with a view to obtaining a judicial determination on particular agreements that he has marked as being of compliance concern, namely Guardian AIT and BBlood, and to hold-off finalising his administrative guidance while these decisions, and the related appeals, were pending. In the practical world, at least based on our experience, it has also meant that several 'live' taxpayer audits and examinations have also been in a state of suspense awaiting further judicial certainty and clarity.

2.3.2 Interpreting the ATO Guidance

64. If nothing else, and at the risk of making a facile observation, the ATO Guidance Materials reinforce the points I sought to make earlier, about the inherent interpretative complexity arising when the parliament chooses to couch an anti-avoidance provision in broad language that is incapable of absolute, precise, or objective definition.

65. Take the question postulated above: against what standard does one measure what comprises a 'valid' familial or commercial objective as against an 'invalid' familial or commercial objective?

66. The Commissioner's view, as expressed in TR 2022/4, on a 'family or commercial objective' is expressed as follows:

> *Family or commercial objectives*
>
> 101. 'Family' in 'ordinary family or commercial dealing' takes its ordinary meaning. It refers to a relationship of natural persons based on birth or affinity, and may often involve co-residence. Family is not limited to any particular type of family relationship that is more common at a point in time than others.
>
> 102. For a dealing to be able to achieve commercial objectives, the parties would be expected to advance their respective interests. Transactions which would be normal or regular if seen in trade or commerce demonstrate that a dealing is founded in commercial objectives. A dealing can achieve commercial objectives, even in the absence of market value or where the parties do not deal at arm's length.

67. Now, let us turn to the examples in TR 2022/4. An arrangement between family members, involving a gifting of funds by a parent to a child, where those funds originate in a distribution from a family trust to a parent, for the purpose of assisting a child to obtain a foothold in the property market, is an acceptable 'familial' objective: see Example 8 (paras 143 and 144). But to not be lulled taxpayers into a false sense of security, the Commissioner caveats his statements,

saying that the situation will not be 'familial' where a tax rate arbitrage between the parents and the child is in play:

Example 8 - gift from parents to a child

143. *Assume the same facts as Example 7 of this Ruling. In one year, Alex (being Lisa's eldest daughter and Jessie's stepchild) purchases a property. Lisa and Jessie pay for the deposit for the purchase of the home as a gift to Alex, from funds attributable to their distribution from the Rosegum Family Trust. While on these facts, the creation of an entitlement and gifting from that entitlement may raise questions about whether the entitlement arose under or in connection with an agreement between the parties****, the making of gifts between family members for ordinary family objectives, such as parents contributing to the purchase of a house, would usually be ordinary family or commercial dealing.***

144. *The following* ***additional or alternative facts*** *may change the conclusion made in paragraph 143 of this Ruling and make it less likely that an agreement has been entered into in the course of ordinary family or commercial dealing. Were that the case, it would be of greater relevance to examine whether one or more persons have a purpose of reducing income tax when entering the agreement (so as to cause the tax reduction purpose requirement to be met) and examine further whether the connection requirement is met:*

• *If the arrangements were to involve parents gifting money received from a trust to their children repeatedly and one or more of the following factors are present*

- *the parents have a lower marginal tax rate*

- *the parents have lesser financial means than the adult child, or*

- *the adult child is also capable of benefitting under that trust in their own right; for example, the parents may be subject to lower tax rates because they are retired and in pension phase or have significant losses to reduce tax payable on trust distributions.*

• *Arrangements where the situation is reversed, so that Alex (who has limited financial resources apart from a distribution made to her and has a lower marginal tax rate) gifts money to her parents Lisa and Jessie who are subject to higher rates of tax, and there is no financial or cultural circumstance that would explain the gift.*

> • *Arrangements where Alex, who has a lower marginal tax rate, agrees to apply her trust entitlements to reimburse her parents for costs incurred by them on her maintenance, education and financial support while Alex was a minor.*

68. So, in essence, a gift of money for the purchase of a home, is a 'familial' objective - so long as it is a gift from the higher-rate taxpayer to the lower-rate taxpayer, and some form of means testing is applied to the family group? Moreover, I question whether the recourse for the Commissioner to address such an arrangement is section 100A at all, when the arrangement, to the extent to which it depends on an assertion that there was a contractually binding obligation between Alex and her parents, entered into when Alex was a minor, that she be subject to a legally enforceable obligation to repay her parents for costs relating to her maintenance and education: among other things, as a minor, Pauline would not have (and could not have) been incurring such liabilities in her personal capacity, but rather they were personal liabilities of her parents, as even a cursory look at the fee slip issued by any private fee-paying school will confirm!

2.3.3 PCG 2022/4 and the administrative 'bargain'

69. As noted above, PCG 2022/2 is representative of a relatively more recent genus of ATO product, aimed at 'practical compliance' rather than a detailed exposition of the Commissioner's technical interpretative position on an area of law where there may be interpretative ambiguity. Seemingly as a complement to the self-assessment system, such products are phrased in 'risk management' style terms, allowing taxpayers to have a sense of the areas on which the Commissioner has the compliance spotlight. In PCG 2022/2, the Commissioner outlines the purpose of the document in these terms:

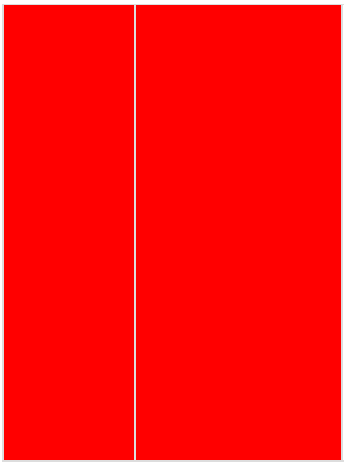
> 2. This Guideline sets out how we differentiate risk and how we manage that risk through our compliance approach for a range of trust arrangements to which section 100A may potentially apply. We aim to give you more certainty by setting out how we will engage with you; in particular, how we:
>
> (a) assess the level of risk regarding trust distribution arrangements based on a risk framework
>
> (b) determine the level of engagement you can expect from us, and
>
> (c) will allocate compliance resources to consider section 100A.
>
> 3. This Guideline uses 3 coloured zones to denote risk ratings. Table 1 at paragraph 13 of this Guideline summarises each of these zones and the corresponding compliance

approach. The Appendix to this Guideline contains examples of how to apply the risk zones.

4. This Guideline is designed to give you confidence that, if your circumstances align with the principles in the white zone or green zone set out in this Guideline, we will not allocate compliance resources to test the tax outcomes of your arrangement, except to confirm that your arrangements meet the requirements of the zone.

70. As paragraph 3 indicates, PCG 2022/2 sets out a cascading level of potential ATO scrutiny that will be applied to arrangements, denoted chromatically, as follows:

Risk level	Risk zone	Description and compliance approach
Low risk	White zone	The white zone applies to arrangements entered into in income years that ended prior to 1 July 2014. Except as described at paragraph 16 of this Guideline, we will not dedicate new compliance resources to consider the application of section 100A to arrangements in the white zone.
Low risk	Green zone	The green zone applies to arrangements that are described in paragraphs 20 to 30 of this Guideline. We will not dedicate compliance resources to consider the application of section 100A to arrangements in the green zone, other than to confirm that the features of the relevant scenario are present in your circumstances.
High risk	Red zone	The red zone applies to arrangements that are described in paragraphs 34 to 48 of this Guideline



Arrangements in this zone will attract our attention and we will conduct further analysis on the facts and circumstances of your arrangement as a matter of priority.

If further analysis confirms the facts and circumstances of your arrangement are high risk, we may proceed to audit where appropriate.

71. Again, as is evident from the above, the arrangements identified as 'white', 'green' or 'red' are illustrated by reference to a number of examples, including examples set out in PCG 2022/2 and those set out TR 2022/4. These examples evince behaviour or arrangements that, in the Commissioner's view at least, are 'low risk', 'medium' risk and 'high risk' of ATO scrutiny. It is notable though that even for those arrangements that are 'low risk', the only offering to taxpayers by the Commissioner is that no 'new' compliance resources will be dedicated to the examination of these arrangements. This phrase offers a significant amount of flex to the Commissioner to consider such arrangements nonetheless, including where the Commissioner has committed compliance resources in the review of a taxpayer on other matters of concern (and a potential section 100A risk is identified in the course of that review) or where the Commissioner has already committed compliance resources to an existing section 100A examination.

72. The Commissioner seemingly affords himself similar flexibility with respect to those arrangements which are in the 'white' zone. Again, the Commissioner's exclusion of arrangements that pre-date 1 July 2014, a date which is pegged to the release of the first 'tranche' of section 100A administrative opinion with the release of the ATO Factsheet in 2014, is subject to at least four layers of conditionality:

> 16. We will not commence **new compliance activities** [*Layer 1*] to consider the application of section 100A for income years ended before 1 July 2014, unless it is outside the green zone [*Layer 2*] and:
>
> (a) we are otherwise considering your income tax affairs for those years [6] [*Layer 3*], or
>
> (b) you have entered into an arrangement that continues before and after that date [*Layer 4*].
>
> 17. See Example 1 of this Guideline for an example of a white-zone arrangement. Example 2 of this Guideline illustrates an arrangement that continues before and after 1

> July 2014. See Example 3 of this Guideline for an arrangement that commenced before 1 July 2014 but is not a white-zone arrangement.
>
> Footnote [6]:
>
> Examples of where we are otherwise considering a taxpayer's tax affairs include where there is suspected fraud or evasion, where a trustee or beneficiary has not met their lodgment obligations or where a trustee's or beneficiary's 4-year period of review has yet to expire.

73. Given the broader proposition advanced in this paper, I am loathe to examine each of the examples provided in PCG 2022/4 in depth, but rather make the broad observations that:

    a. the examples include ones which, in my submission, could be 'attacked' on the basis that they lack legal substance or contractual integrity (e.g., present entitlement that are offset against expenses incurred by the caregiver before the beneficiary turned 18 years of age, at Example 14);

    b. the Commissioner introduces tangential concepts or requirements (e.g., the 'trustee working capital condition' condition at paragraph 26) that are not contemplated by section 100A itself and seek to import into a section 100A compliance instrument requirements that serve a broader compliance purpose (e.g. in imposing a requirement that funds be used only for 'working capital' or 'investment' use and that there not be personal use or enjoyment of the funds) but do not have any legislative foundation.

74. The examples provided are, without doubt, intended by the Commissioner to provide clarity with respect to his views and this is commendable. However, one does question whether specific examples of a provision that has a scope as wide and general as what section 100A does will ever provide clarity about the scope and ambit of section 100A in any general sense. This observation was made, astutely in my view, in the submission made by the Law Council of Australia as part of the public consultation on TR 2022/D1 and PCG 2022/D1[41]:

> "54 The Committee notes that the ATO does not appear to have issued a general public ruling on the application of the GAAR. There may be a number of reasons for not doing so but a key one might be that a clear and useful exposition about whether or not the GAAR applies can only be made on a consideration of the specific facts and circumstances of a particular case such that a public ruling on the topic would not provide any meaningful guidance. Instead, what the ATO has done in relation to the GAAR is issue Practice Statement Law Administration PS LA 2005/24. Although PS LA 2005/24 is said to provide instruction and practical guidance to ATO officers, it has always been a very useful guide

[41] Law Council of Australia (Business Law Section), 6 May 2022, authorship attributed to A Lee and P Sokolowski.

for taxpayers and advisors as well. Further, unlike the Draft s 100A Material, PS LA 2005/24 is not complicated with abstract fact scenarios."

2.3.4 Conclusion

75. Of course, in the same way that there is a danger in 'over-reading' extrinsic material or judicial obiter, as the courts have pointed out, there is equally a danger in over-reading ATO guidance material.

76. Just as the examples provided in the explanatory material that accompanying the introduction of section 100A were held by the courts to not limit the scope of section 100A in any broad sense, so should the examples provided in the ATO Guidance Materials be seen as expanding the scope of section 100A in any broad sense. A view which the Commissioner expresses in a public ruling is an administrative opinion; it does not rise to legislative status. As Brett Freudenberg states (paraphrasing Paul Keating), what the ATO publishes as LORE should not be elevated to LAW[42].

77. Of course, the Commissioner, quite properly, provides the examples in the ATO Guidance Material merely as examples, and the application of the law in any scenario will be dependent on the particular facts of each case and the judicial evaluation of those facts, if a matter is ventilated in court. Nothing illustrates this better than the fact that fact patterns that were largely on all-fours with two of the examples the Commissioner provides in the ATO Guidance Material, one involving a circular flow of distributions between a trust and a corporate beneficiary[43] and one share buy-back[44], were litigated, in Guardian AIT and BBlood respectively. In Guardian AIT, the court found that the facts and evidence did not support the application of section 100A and in BBlood, the court found that the facts and evidence did support the application of section 100A. Both cases are considered in depth in the next part of this paper.

[42] ; B Freudenberg, (2022), '*Ordinary Family Dealings in s 100A: Scant law leading to confused lore*', Tasmanian Convention, The Tax Institute, 8-9 September 2022

[43] Example 12 in TR 2022/4.

[44] Example 11 in TR 2022/4.

3. Guardian AIT and BBlood

3.1 Introduction

78. Continuing the theme with which we began this paper, the goal of the analysis that follows is to consider whether the two most recently heard cases involving section 100A, Guardian AIT and BBlood, have helped us to evolve our understanding of section 100A and its operation in the practical world and to the practical problems of our clients.

79. In both Guardian AIT and BBlood, the Federal Court was called on by the parties to address section 100A to two schemes which, as I discussed above, had found their way into the ATO Guidance Materials as examples of fact patterns where there was a substantial risk of section 100A applying: the fact pattern in Guardian AIT mirrors the 'circular distribution' (described somewhat inelegantly sometimes as the 'washing machine' arrangement) and that in BBlood reflects the share buy-back arrangement, both outlined in TR 2022/4

80. As it turned out, the taxpayer prevailed in Guardian AIT and the Commissioner in BBlood (both at first instance and on appeal - although in Guardian AIT-FFC, the Commissioner was successful on a part of his claim mounted under Part IVA of the 1936 Act. This of itself does not suggest any broad validation of either the view that taxpayers or the Commissioner might take, in relation to the facts under consideration in these particular cases, or more broadly in relation to any of the fact patterns the Commissioner has marked as being high-risk in the ATO Guidance Materials. Rather, in my submission, what these cases show is that the idiosyncrasies of the facts and, most importantly, the evidence of each case is the sole factor that is determinative of the outcome.

3.2 A bit about evidence

81. At the risk of straining the point, the importance and gravity of evidence, both in terms of the documentation and correspondence that is contemporaneous to the relevant events, and the oral testimony given by witnesses in court, cannot be underestimated. This is especially true given that, as with all matters, the taxpayer bears the onus of proof[45].

82. A reading of the judgement in Guardian AIT makes it clear that the taxpayer in that case, Mr Springer, and his advisors who were called to give evidence, acquitted their task as witnesses admirably, being described individually and collectively by Logan J as having provided "honest, candid, consistent evidence, which also sat well with this correspondence."[46] There can be no

[45] Section 14ZZO(b) of the *Taxation Administration Act 1953* (Cth)/

[46] Guardian AIT at [39].

doubt was influential in the decision being made in his favour, and that absent this factor, the decision may well have been a different one. Moreover, the evidence of taxpayer was largely undisturbed in Guardian AIT-FFC[47].

83. As we will see in the coming discussion, both documentary and oral evidence are of crucial importance in a section 100A case. As section 100A will invariably require consideration of a taxpayer's purpose, oral evidence given in court, the veracity of which has tested under cross-examination and judicial observation, may have an elevated influence on the final judicial determination. But given that such evidence will inevitably be self-serving, a healthy dose of judicial scrutiny should be expected. Moreover, the objective facts and documents will be, in a sense, allowed to speak for themselves, and any reasonable inferences that can be drawn from the objective facts, will be drawn.

84. Thawley J makes this clear in the following passage from BBlood:

> "134 The weight to be attributed to a person's evidence about that person's purpose depends on the case**, particularly the cogency of the evidence when assessed against the objective circumstances and, if relevant, the fact and consequences of any cross-examination**. In *Pascoe v Federal Commissioner of Taxation* (1956) 30 ALJR 402 at 403, Fullagar J observed:
>
> > Where a person's purpose or object or other state of mind in relation to a given transaction is in issue, the statements of that person in the witness box provide, in a sense, the "best" evidence, but, for obvious reasons, they must, as Cussen, J observed in Cox v Smail ((1912) VLR 274, at p 283), "be tested most closely, and received with the greatest caution".
>
> 135 His Honour was using the word "best" as meaning "most direct" evidence. His Honour was not saying that subjective evidence is the most reliable evidence. **The most reliable evidence of a person's actual purpose is often furnished by the objective facts. The objective facts include the financial, taxation and other consequences of the transaction entered into.**
>
> 136 Contemporaneous documents are often probative of purpose. **They are often of greater weight than ex post facto "subjective" evidence about purpose**: Hart v Federal Commissioner of Taxation [2018] FCAFC 61; 261 FCR 406 at [86] (Robertson, Wigney and Steward JJ). **This is particularly true where those documents can be seen to have been created in circumstances which indicate that they are likely to: (a) record reliably the relevant events as they occurred; or (b) furnish evidence of the**

[47] Guardian AIT-FFC at [121].

> **real reasons why certain steps were taken**. Contemporaneous documents do not always have this character."[48]

85. It is notable that in PCG 2022/2, the Commissioner has included some instructive guidance about the important of 'record keeping' in the context of inter-family group transactions and arrangements (these comments were not present in PCG 2022/D1), as follows:

> Record keeping
>
> 49. You should prepare and keep good records that explain the transactions that have happened. Having a clear understanding as to why a beneficiary has chosen to deal with their entitlement in the way they have and knowledge of the relevant parties to the transaction or arrangement will help support your position. It will also assist in the timely resolution of any compliance activity we undertake.
>
> 50. While each arrangement depends on its facts, the following documents and records are important and should be kept wherever possible:
>
> (a) the trust deed (including amendments), trustee resolutions and contact details of the trustee and former trustees
>
> (b) notes, contemporaneous documents and records of discussions or meetings explaining the transactions that have happened or calculations that have been made
>
> (c) details of how the beneficiary was notified of their present entitlement to trust income
>
> (d) details of how the present entitlement to trust income was satisfied and, where practical, used by the beneficiary
>
> (e) details of how the trustee utilised the underlying funds; for example, to satisfy the trustee retention of funds or the trustee working capital condition referred to in paragraph 25 of this Guideline
>
> (f) copies of loan agreements and records showing how the loan repayments were satisfied from time to time.
>
> 51. We acknowledge that family arrangements are typically conducted with a greater level of informality than dealings between unrelated parties. Nonetheless, to the extent possible, the trustee or their registered tax agent should maintain contemporaneous records that are ordinarily created which demonstrate the objectives an arrangement was intended to achieve

[48] BBlood per Thawley J.

and how it would achieve them. For example, this could be in the form of a file note of a meeting between the trustee and registered tax agent.

52. The maintenance of contemporaneous records by the trustee is part of good governance arrangements for managing the trust's affairs and dealing with the ATO. Notwithstanding that an arrangement is fully documented, section 100A may still apply, particularly where the arrangement is contrived or artificial, is overly complex or has tax-driven features so that the dealings cannot be explained by ordinary family or commercial purposes.

3.3 Guardian AIT and BBlood: The factual story

3.3.1 Guardian AIT

86. The 'executory' elements or steps of the relevant fact pattern in Guardian AIT were as follows:

Step	Date	Action/step
Year of income ended 30 June 1998		
1	17 May 1998	▪ Guardian AIT Pty Limited (**Guardian)** incorporated[49]
2	25 June 1998	▪ Australian Investment Trust (**AI Trust**) settled under deed of trust.
Year of income ended 30 June 2000		
3	14 November 1999	▪ Guardian appointed as trustee of AI Trust (replacing Mr Springer) (further references to AI Trust are to Guardian in in its capacity as the trustee of the AI Trust)
Year of income ended 30 June 2012 (2012 Year)		
4	June 2012	▪ AIT Corporate Services Pty Limited (**AITCS**) incorporated
5	June 2012	▪ Mr Springer (in his capacity as Principal under the terms of the AI Trust) determined that AITCS would be a 'beneficairy' of the AI Trust - resulting in AITCS becoming a member of the eligible class of beneficiaries (discretionary): clause 3, AI Trust deed.

[49] Incorporated as Springer Pty Limited and resolved to change its name to Guardian AIT on 14 December 1999.

Step	Date	Action/step
6	28 June 2012	▪ Appointment of income by AI Trust to AITCS: $2,640,209 (the **2012 AITCS Distribution**) ▪ 2012 Distribution remains unpaid giving rise to an Unpaid Present Entitlement (**UPE**) (the **2012 UPE**)
Year of income ended 30 June 2013 (2013 Year)		
7	17 April 2013	▪ AITCS calls on 2012 UPE to fund 2012 Year tax liability: $792,062 (the **2012 Tax**) - UPE balance $1,848,147
8	1 May 2013	▪ Fully franked dividend declared by AITCS to AI Trust: $1,848,145 [i.e., 2012 Distribution minus the amount of the 2012 Tax - UPE Balance]
9	23 June 2013	▪ Appointment by AI Trust to Mr Springer: AI Trust resolves that the amount of the net income of the Trust for the 2013 Year ***attributable to franked dividends*** be set aside and held on trust absolutely for Mr Springer ▪ Appointment by AI Trust to AITCS: the income ('a share of the net income of the AI Trust) for the 2013 Year: $2,646,166 (**2013 AITCS Distribution**) ▪ The 2013 AITCS Distribution remains unpaid giving rise to a UPE (the **2013 UPE**)
Year of income ended 30 June 2014 (2014 Year)		
10	14 February 2014	▪ AITCS calls on its UPEs to fund 2013 Year tax liability: $595,845 (the **2013 Tax**)
11	27 February 2014	▪ Fully franked dividend declared by AITCS to AI Trust: $1,780,453 [i.e., 2013 AITCS Distribution minus the amount of the 2013 Tax] ▪ Dividend paid by reducing the balance of the 2013 UPE of AITCS from $1,780,453 to 0.
12	23 June 2014	▪ Appointment by AI Trust to Mr Springer: AI Trust resolves that the amount of the net income of the Trust for the 2014 Year ***attributable to franked dividends*** be set aside and held on trust absolutely for Mr Springer.

Step	Date	Action/step
		▪ Appointment by AI Trust to AITCS: the income ('a share of the net income of the AI Trust') for the 2014 Year: $2,670,117 (**2014 AITCS Distribution**) ▪ The 2014 AITCS Distribution remains unpaid giving rise to a UPE (the **2014 UPE**)
Year of income ended 30 June 2015 (2015 Year)		
13	20 March 2015	▪ AI Trust pays AITCS 2015 Year tax liability: $801,034 (the **2014 Tax**) ▪ AI Trust reduces the 2014 UPE by the 2014 Tax (reduced to $1,869,083)
Year of income ended 30 June 2016 (2016 Year)		
14	18 March 2016	▪ AITCS and AI Trust enter into a Division 7A loan agreement for the balance of the 2014 UPE
15	31 March 2016	▪ AITCS files its income tax return declaring as income a **$1,471,755** trust distribution made to it by AI Trust in the 2015 Year resulting in tax liability of $441,532.50.
16	2 May 2016	▪ AI Trust repays the balance of the loan (now under Division 7A terms) to AITCS by transfer of funds to AITCS bank account.

87. In addition, the following facts were salient:

a. *Assets of AI Trust*: in the relevant income years, the AI Trust held interests in various companies that carried on business and investment activities, involving land holding and forestry operations, and which were part of Mr Springer's family group.

b. Mr Springer had ceased to be tax resident of Australia (and was a tax resident of Vanuatu) in the year of income ended 30 June 2008 and was a non-resident of Australia in each of the 2012, 2013 and 2014 Years. As a result of this, as the distributions from the AI Trust to Mr Springer, which occurred on 23 June 2013 and 23 June 2014, which were referrable to franked dividends, when Mr Springer was a non-resident of Australia, would not be subject to dividend withholding tax[50] or any further tax liability for Mr Springer[51].

[50] Section 128B.

[51] Ibid.

3.3.2 BBlood

88. The 'executory' elements or steps of the relevant fact pattern in BBlood were as follows:

Step	Date	Action/step
	Pre-30 June 2013	▪ The Iluka Park Trust (**IP Trust**) settled with B&F Investments Pty Limited (**IP Trustee**) as trustee. ▪ IP Trust owned 99% of the shares in Iluka Park Pty Limited (**IP Co**) (1% owned by Mrs Blood). ▪ B&F Investment Trust (**B&F Trust**) owned shares in the Blood Group operating entities (motor vehicle trading). ▪ The B&F Trust had made substantial distributions to IP Co (as a General Beneficiary). ▪ IP Co's retained earnings on 30 June 2013 were $7,421,721.92 (sourced largely from distributions of income from the B&F Trust).
Year of income ended 30 June 2014 (2014 Year)		
1	25 March 2014	▪ BBlood Enterprises Pty Limited (**BE Co**) incorporated
2	On or around 31 March 2014	▪ B&F Trust made an interim distribution of its income for the period ended 31 March 2014 as follows: o To **IP Trust**: $123,237.66; o To **IP Co**: $2,999,496.10 (adding to IP Co's retained earnings[52] but not paid and presented as a UPE owed by the B&F Trust to IP Co).
3	31 March 2014	▪ **IP Co** declared a dividend to **IP Trust** of $121,739
4	30 April 2014	▪ **IP Co** declared a dividend to **IP Trust** of $59,400
5	13 June 2014	▪ Deed of Variation executed to amend the **IP Trust**'s deed
6	25 June 2014	▪ **IP Co** carried out a share buy-back of shares held in it by IP Trust: o Offer and notification to shareholders on 10 June 2014; o Circulating resolution approving buy-back on 25 June 2014; o Share buyback agreement dated 25 June 2014; ▪ Share buyback purchase price is **$10,189,869**. Of this: o $99 is debited to share capital of IP Co; and

[52] Particularised at [30].

Step	Date	Action/step
		○ $10,189,770 is debited to retained earnings of IP Co (the **Share Buyback Dividend**). ▪ IP Co allocates franking credits of $4,367,002 to the share buy-back dividend. ▪ IP Co settled the purchase price by crediting IP Trust's at call loan account.
7	30 June 2014	▪ IP Trust distributed to BE Co all the 'income' of the IP Trust for the 2014 Year.

89. The following matters are also noted to give further context to the executory elements of the fact pattern in BBlood:

a. *Trust deed variation*: the IP Trust's Deed was varied on 13 June 2014 to delete the existing definition of "income" and replace it with the following:

> "**income**" of the Trust Fund in respect of an Accounting Period shall mean:
>
> (i) the income of the Trust Fund determined by the Trustee according to ordinary concepts; or
>
> (ii) such other definition determined by the Trustee in writing on or before the end of the relevant Accounting Period,
>
> less those outgoings, expenses, charges, provisions and payments that the Trustee determines in its absolute discretion, is properly referable to the derivation of that income having regard to the provisions of the Deed and the nature of the income,

b. *Trust law income*: Applying the IP Trust's definition of income, as amended, such that the IP Trust's income would be determined in accordance with 'ordinary concepts' would mean that the Share Buy-Back Dividend, while income for tax purposes[53], was not 'income' of the IP Trust for trust purposes as determined under the deed: rather, it was treated as a capital receipt that accrued to the trust's corpus[54]. The IP Trust's income, determined under the terms of its trust deed, was $304,376.97 (**Trust Deed Income**), comprising:

i. the distribution made by the B&F Investments Trust on 31 March 2014 ($123,237.66);

[53] See section 159GZZZP of the 1936 Act.

[54] BBlood at [29].

ii. the dividend paid by IP Co on 31 March 2014 ($121,739); and

iii. the dividend paid by IP Co on 30 April 2014 ($59,400).

c. Effect of distribution: by the general operation of Division 6, by the IP Trust creating a present entitlement to the Trust Deed Income in favour of BE Co, the full distribution determined in accordance with tax principles under section 97 of the 1936 Act, which included that referrable to the Share Buyback Dividend (which BE Co has no legal entitlement to, but which remained with the IP Trustee and went to corpus of the IP Trust), was attributed to BE Co. As there was no amount of the Trust Deed Income to which no beneficiary was presently entitled, no assessment to the IP Trustee arose under section 99A. Moreover, BE Co was not subject to any additional tax on the attributed distribution which included the Share Buyback Dividend, as this was fully franked[55]. In this sense, as the Commissioner characterised it in his submissions, '…the tax result relied on creating a mismatch between (trust) income and (tax) net income', though the Court noted that this arises as an ordinary incident of the operation of Division 6 of the 1936 Act[56].

3.4 The elements of section 100A

90. Our examination now turns to how the Federal Court, in Guardian AIT and BBlood, addressed section 100A, in terms of its three key elements or conditions:

a. ***Agreement, arrangement and understanding (and causation):*** That a beneficiary, not under a legal disability, is presently entitled to a share of the income of a trust which arises 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: subsection 100A(1). The term 'agreement' in this context has an extended meaning, to include any 'agreement, arrangement, or understanding': subsection 100A(13).

b. ***Ordinary family or commercial dealing:*** that an 'agreement, arrangement or understanding' for the purposes of section 100A will not include one which is entered into 'in the course of an ordinary financial or commercial dealing': subsection 100A(13).

c. ***Tax reduction purpose***: that an 'agreement' for the purposes of section 100A does not include an 'agreement' unless it has the purpose of reducing an entity's tax: subsection 100A(8).

[55] BBlood at [31] to [33].

[56] BBlood at [33].

3.5 Agreement, arrangement or understanding (and causation)

3.5.1 Guardian AIT / Guardian AIT (FFC)

Framing the test

91. Logan J starts his judgement in Guardian AIT by referencing the Dr Carl G Jung, the great Swiss analytical psychologist, and the concept of 'synchronicity': "events which coincide in time and appear meaningfully related but have no discoverable causal connection"[57]. To Logan J, an examination of section 100A must begin with a search for something beyond a 'synchronicity': rather there must be a causal connection and relationship between events which must be made out on the evidence.

92. Moreover, not merely must this be so, but there is also a particular 'temporal sequence' the said events must follows: a 'reimbursement agreement' must exist ***before*** a present entitlement arises, and the facts must show this to be the case prospectively and not in hindsight. Logan J finds support for this view in the text of subsection 100A(1):

> 128 A textual approach does support a submission made on behalf of Guardian. That submission was that, for s 100A to have application**, the reimbursement agreement concerned must precede** "the payment of money or the transfer of property to, or the provision of services or other benefits" (flowing from the text of s 100A(7)) and the present entitlement of the beneficiary (flowing from the text of s 100A(1)(b)).

93. In Guardian AIT (FFC), the judgement of Hespe J (with whom Perry and Derrington JJ agreed), emphasis was placed on both the *timing* of the agreement as well as the *content* of the agreement: this is addressed below.

Application of the evidence

94. Logan J, on the facts of the case, found that there was no agreement, which preceded the present entitlement created by the AI Trust in favour of Mr Springer in either the 2012 or 2013 Years. The Commissioner sought to characterise the elemental steps undertaken by Mr Springer, commencing with the incorporation of AITCS, the retention of funds (in the form of a UPE) by the AI Trust of the 'present entitlement' created in favour of AITCS, and the ultimate distributions to Mr Springer, as a single agreement or understanding (the '2012 Understanding'). Logan J found no such agreement existed. He states:

[57] Guardian AIT at [1].

> 132 Like Hill J in East Finchley, at 474, I have no difficulty in accepting that a "reimbursement agreement" need not be legally enforceable and may be attended with great informality. How could it be otherwise in the face of the definition in s 100A(13)? But accepting this breadth of meaning, it must be possible to conclude that something answering the description of "reimbursement agreement" in s 100A(7) pre-existed the present entitlement. **There is just no support for this in the contemporaneous evidence as to events in June 2012 on or prior to the resolution on 28 June 2012 which created the present entitlement of AITCS, not even a foundation for reasonable inference**. A hypothetical contingency open in law but never considered is not sufficient to yield that. **It is only many months later that even the possibility of the declaring of a dividend by AITCS emerges. The requisite temporal sequence is lacking. There is no "relevant connection". (emphasis added)**

95. Logan J details an extensive factual background with respect to Mr Springer, his business activities, his personal motivation to transition to retirement from business and arrange his affairs so as to achieve a degree of asset protection, his family circumstances and evidence which is suggestive of the manner in which he organised and managed his financial and tax affairs, with the assistance of his professional advisors[58]. Of these many facts, what I see as being most influential on Logan J's finding, that there was no 'temporal sequence' in the events, and no coherent, integrated and predetermined plan with respect to the flow of funds between the AI Trust, AITCS and himself, is reflected in this passage, which comments on the generalised approach Mr Springer took in relation to the management of his financial and tax affairs:

> 59 It emerged in his cross-examination that a feature of Mr Springer's operation of the Springer Group (and I infer earlier other companies controlled by him) was that **no formal, forward operating budgets regarding cash flow needs were prepared. Rather, as Mr Springer agreed in his evidence, he engaged in a form of reactive management, meeting expenses as and when required or identified from funds available within the Springer Group (or, earlier, other companies controlled by him) at a given time**. The retainer of Mr Fischer's firm to provide advisory and accounting services to the Springer Group did not extend to a forward budgeting task. At most what occurred, as Mr Fischer confirmed in evidence, was an annual review, prior to the close of an income year, by his firm of the overall position of Mr Springer and of the companies and trusts controlled by him and of transactions which had occurred in the year to date. **This review did not identify future cash flow needs as such, as opposed to identifying from transfers where those needs had occurred and what distributions should be made and to which entity.** (emphasis added)

[58] Guardian AIT, 39 to 119.

96. Moreover, Logan J particularises the correspondence that Mr Springer had with his professional advisors at some length (in documentary form[59]) and both he and his advisors were subject to cross-examination of their oral testimony. From this, Logan J finds that there is no integration, coherence or sequence as between the making of a distribution from the AI Trust to AITCS and AITCS resolving to declare a dividend in favour of the AI Trust: rather, the evidence shows that these decisions were made independently and after the passage of some time ('several months later' as Logan J finds at para. 132). There was no evidence that the correspondence between Mr Springer and his advisors did anything other than portray an accurate and contemporaneous version of the relevant events.

97. In Guardian AIT (FFC), Hespe J (with whom Perry and Derrington JJ agreed) finds that at the critical date of 23 June 2013, being the date on which there was an appointment of the income of the AI Trust to Mr Springer and to AITCS (see executory step 12 at paragraph 86 of this paper), it was not open on the facts to conclude that the payment of a dividend by AITCS to the AI Trust was 'wholly conjectural', and as such, that no 'reimbursement agreement' had been formed[60]. However, Hespe J goes on find as follows:

> 117. However, there is a difference between a matter **not** being wholly conjectural and a matter being the subject of an understanding or arrangement. **For s 100A to be satisfied, there must be an "agreement" in existence at or prior to the date of the resolution by which AITCS [being a beneficiary of the Australian Investments Trust] was made presently entitled**. As Hill J considered in East Finchley 90 ALR at 474, where the reimbursement agreement is said to require the payment by a beneficiary, the parties to the agreement must include that beneficiary or at the least a representative or controller of that beneficiary. **An expectation by a party that an arrangement could be reached with AITCS at some later date for a dividend to be paid by AITCS to the AIT is not sufficient. For s 100A to be satisfied as at 23 June 2013 there had to be an arrangement or understanding between two or more parties that AITCS would pay a dividend to the AIT.** (emphasis and interpolation added)

98. Moreover, in Guardian AIT (FFC), Hespe J opines on what is required for there to be an 'agreement' (as a precondition to a 'reimbursement agreement'), and how an agreement may be made out, particularly in a case where there is a purported attribution of the intention or purpose of an advisor to a taxpayer. Hespe J states:

> 124. The inquiry in relation to the existence of a reimbursement agreement in s 100A is different [to an inquiry of 'purpose' for the purposes of Part IVA]. **It requires the existence of an "agreement" (as defined in s 100A(10)) invoking, as it does, a requirement of consensus and adoption. The scope for attribution in that context is far more limited**

[59] Guardian AIT at 84 to 119.

[60] Guardian AIT (FFC), 112 to 116.

> [than it would be for the purposes of Part IVA]**.** 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 had authorisation to act on or behalf of those entities in order to conclude that there was consensus or adoption by Guardian and Mr Springer. No such finding was made by the primary judge 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 before this Court. 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. **Whilst the evidence supports a finding that Mr Springer generally followed the advice of Mr Fischer, there is no evidence that Mr Fischer was an authorised representative of Mr Springer or the Springer Group.** (emphasis and interpolation added)

3.5.2 BBlood

Framing the test

99. In BBlood, Thawley J places less emphasis than Logan J in Guardian AIT did on 'temporal sequence' in the executory steps comprising the overall fact patter to which section 100A is addressed. In part this may be because the particular facts before Thawley J gave less scope for the argument to be made. But more than that, Thawley J seems to suggest, in the passage following, that the 'particular order of events' may be a relevant factor but not a determinative one, in contrast to Logan J[61]. Rather, the relevant inquiry for Thawley J is a more holistic one: the inquiry for Thawley J is whether there exists '*…a connected series of steps that were intended to operate in conjunction with each other as part of an overall agreement, arrangement or understanding*'[62].

100. Moreover, in looking to establish a 'causal' connection between the 'reimbursement agreement' and the 'present entitlement', for the purposes of section 100A, Thawley J cautions against a unitary approach (such as a 'but for' test, as exposited in Idlecroft[63]) in favour of a multi-factoral consideration:

> 268 The parties agreed that s 100A(1)(b) sets up a "but for" test of causation, referring to Idlecroft Pty Ltd v Federal Commissioner of Taxation [2005] FCAFC 141; 144 FCR 501 at [44] (Ryan, Tamberlin and Kiefel JJ). There is a risk of oversimplification in approaching

[61] BBlood at 268.

[62] BBlood at 80.

[63] Idlecroft at 44.

> the application of s 100A(1)(b) by describing it simply as imposing a "but for" test of causation, and determining the issue posed by s 100A(1)(b) by reference to that test rather than applying s 100A(1)(b) according to its terms. I do not read Idlecroft at [44] as adopting such an approach. **Section 100A(1)(b) contains a number of components, not all of which necessarily imply the same type or quality of connection between the relevant events. The particular order of events might also be relevant**. The first part of the section is satisfied if the present entitlement "arose out of a reimbursement agreement"; the second part is satisfied if the present entitlement **"arose by reason of any act, transaction or circumstance that occurred in connection with, or as a result of, a reimbursement agreement"**. (emphasis added)

Application of the evidence

101. In finding, as he did, that the fact pattern in BBlood comprised *'…a connected series of steps that were intended to operate in conjunction with each other as part of an overall agreement, arrangement or understanding'*, Thawley J placed emphasis on the following evidence:

a. Documentation prepared prior to the implementation of the relevant events, which show that the steps in the plan, as they were in fact carried out, were 'pre-ordained' as part of a singular, coherent strategy, and was the subject of advice provided to the taxpayer entities, and the principals of those entities, by their professional (accounting) advisors:

> 81 This conclusion is also supported by documents created at the time of the relevant events. **A memorandum dated 17 September 2013** [that being some seven or so months prior to the implementation of any of the executory steps], entitled "Share Buy-Back Strategy - Test Case - Geoff Harris Group" sent by Mr Neil Cahir (Fordham) to Mr David Buckley (Fordham) and Leigh Baring (Maddocks) (the 17 September 2013 Memorandum) described a "proposed Share Buy-Back of Ordinary Shares**" comprising substantially the same steps and having substantially the same result as the Illuka Park steps**. (emphasis and interpolation added)

b. The fact that the taxpayer entity's advisors had implemented arrangements like that implemented by the taxpayer entities for other clients (which, I say I find remarkable that this is a matter of relevance), and that a single firm was engaged to prepare all the transaction documentation, and that it was prepared all at the same time and handed to the taxpayer as a single set or 'suite' of documents, to implement the arrangement end to end:

> 82 It was not in dispute that arrangements similar to those implemented by the Brian Blood group were implemented by **at least seven "private" groups during the 2014 year**. The arrangements were implemented by transaction documents prepared by Maddocks. In relation to each of the seven groups, Maddocks sent to Fordham a letter attaching the original signed and dated copies of the following documents: the Deed of Variation in

> respect of the relevant Vendor Trust; the Share Buy-Back Agreement effecting the buy-back of shares held by the Vendor Trustee in the relevant Buyback Co; and the Distribution Minute by which income (but not the buy-back proceeds) was distributed to the relevant Beneficiary Co. The letters requested the documents be kept in a safe place. **The documents were evidently perceived to form part of one overarching transaction or arrangement by those who prepared them, those who advised in respect of them, and those who entered into them.** (emphasis added)

102. In BBlood (FFC), it was accepted that there was no dispute about the question of whether there was an agreement. The Full Court (Moshinsky, Colvin and Hespe JJ) state:

> 40 There was no dispute that there was an agreement. The agreement encompassed the Illuka Park Steps, though the appellant sought to focus on those steps that provided for the payment of the buy-back proceeds as it was by reason of providing for that payment that the agreement satisfied s 100A(7). The buy-back proceeds were not paid to the beneficiary (BE Co) but were paid to and retained for the benefit of IP Trustee.

3.6 Ordinary family or commercial dealing

3.6.1 Guardian AIT

Framing the test

103. For Logan J, the test of whether arrangement meets the definition of being an 'ordinary family or commercial dealing' is a matter to be informed by not only the statutory language of section 100A, but also the Explanatory Materials (as discussed above). Logan J posits that the statutory text should not be read to render the word 'ordinary' in 'ordinary family or commercial dealing' as otiose: it must be read as having work to do, and that can be inferred from the Explanatory Materials.

104. Specifically, by Logan J's formulation, the arrangement in question must exhibit no 'element of artificiality':

> 144 Read in context, the adjective "ordinary" in "ordinary family or commercial dealing" has particular work to do. It is used in contradistinction to "extraordinary". **It refers to a dealing which contains no element of artificiality. This is confirmed by reference to the relevant explanatory memorandum, where one finds reference to addressing the mischief of specially introduced beneficiaries having a fiscally advantageous status.** This explanatory memorandum confirms what a reading of s 100A would suggest, which is

> that the section is directed to addressing, according to its terms, "trust-stripping".(emphasis added)

105. The decision of the Full Court in Guardian AIT (FC) and its finding on the threshold question of whether there was an 'agreement', and thereby a reimbursement agreement, rendered any consideration of whether there was an 'ordinary family or commercial dealing' otiose. Hespe J (with whom Perry and Derrington JJ agreed) states:

> 126 This conclusion [being the conclusion that there was no "agreement" as at 23 June 2013 within s 100A(13)] makes it unnecessary to consider the issues of purpose and the scope of the phrase "ordinary commercial or family dealing". It is noted that the Commissioner's submissions on both of these issues were necessarily predicated on the payment of the dividend forming part of the reimbursement agreement. Counsel for the Commissioner expressly and, in our view, correctly denied that the mere inclusion of a corporate beneficiary as an eligible beneficiary and the fact that a distribution may be made to such a beneficiary would be sufficient to demonstrate a dealing that was not an ordinary commercial or family dealing. The Commissioner's submissions in relation to the non-application of the exception of ordinary commercial or family dealings were premised on the payment of the dividend by AITCS forming part of the agreement.

Application of the evidence

106. Of course, returning to the discussion earlier in this paper regarding ambiguity in the use of 'subjective' words in statutory text generally and section 100A specifically, the question of what is artificial or displays artificiality is one on which reasonably minds may differ. So, let us look now to what features of the fact pattern involving Mr Springer and his entities led Logan J to conclude that it was not a fact pattern that involved any element of artificiality.

107. In finding that the arrangement entered into by Mr Springer and his associated entities was one entered into in the course of an 'ordinary family or commercial dealing', Mr Springer placed emphasis on the following:

a. *The objective to achieve commercial and asset protection for Mr Springer and the entities in his family group as part of his transition to retirement, and a strategy that the court was satisfied would achieve it*: It was crucial to the court that Mr Springer was able to, through documentary evidence and his oral evidence, that he had:

i. an *actual need for 'asset protection'*, given that he had sold an interest in one of the operating businesses carried on by his family group, and was conscious and aware of the need to protect himself from personal liability that may accrue to him, particularly as he had previous experience

in a failed business venture[64]. The court found that the desire for a 'clean skin' corporate entity (AITCS) was explicable by this consideration and driver:

> "150 Of course, in a sense, AITCS was a "specially introduced" corporate beneficiary. **But the purpose of that introduction in June 2012 is wholly explained by Mr Springer's desire to minimise risk in retirement and to have a new separate legal entity to which trust distributions (as an alternative to existing members of the class of eligible beneficiaries) might be made and as a vehicle which might be used for passive investment and wealth accumulation.** The introduced corporate beneficiary, AITCS, enjoyed no special tax status under Australian law. Further but related to that, never having traded, it did not even bring with it whatever tax advantage there may have been in carry forward losses from such trading. The documents contemporaneous to June 2012 reveal a complete absence of contemplation by anyone in Pitcher Partners or Mr Springer personally that AITCS be used as a vehicle for streaming via dividend payments. Axiomatically, in law that was possible but that was never a feature of any prior plan.
>
> **151 Introducing a corporate beneficiary which had never traded, and never would, achieved the desired risk minimisation. It allowed the shielding of distributed income and accumulated wealth from any creditors of individuals who were also members of the class of eligible beneficiaries. It then provided a legal entity separate from those individuals via which wealth might be accumulated and invested. It also retained the advantage, always hitherto present with other but now no longer needed corporate members of the eligible beneficiary class of the AIT, of not having to make a large distribution in a given year to an individual, be that individual Mr Springer or one or the other or each of his sons. There are familial, not just commercial risk minimisation, advantages in such flexibility.** And, on the evidence, Mr Springer had a fractious, not fractured, relationship with his sons and a fractured relationship with a wife. Also a consideration in terms of flexibility was that, as at June 2012, although also a member of the eligible beneficiary class, Mr Springer was a non-resident for Australian taxation purposes. There also existed the contingency, realised in practice as it happened in December 2012 with Eric, that a son might in the future also choose to live abroad."

ii. Evidence that Mr Springer has *a practical, personal understanding of the need for asset protection and how the structure adopted would achieve it*, as shown by the following passage of his evidence:

[64] Guardian AIT at 146.

> "147 Later, towards the close of his evidence, Mr Springer gave, to my direct observation, transparently honest answers to similar effect:
>
> > And did that inform your decision about not using any of the operating companies any further?---Well, I was just worried they would come back and bite me and that was the reason I wanted to get rid of those old companies and have a new one was so that nothing would come out of the past and attack me.
> >
> > The last thing you wanted in retirement?---Exactly."

b. *A pre-existing patter of distributions to corporate beneficiaries (apart from AITCS within the Springer family group):* the evidence presented to the court showed that, prior to the implementation of the arrangement to which the Commissioner addressed section 100A, there had been a 'pattern' of distributions:

i. By the AI Trust to corporate beneficiaries *aside from* AITCS;

ii. By the AI Trust to Mr Springer comprising amount referrable to franked distributions received by the AI Trust; and

iii. to family members aside from Mr Springer (namely, to his adult children); and

and that those distributions occurred, at all times, in a manner which was consistent with the '…prevailing, reactive managerial style…which the evidence showed that Mr Springer adopted, the distributions we in no income year pre-ordained or the result of any '…prior budgeting decisions…' and, as such, the distributions had an 'ad hoc quality both in amount and selected beneficiary…'[65].

Against this background, on the court's findings, the 'switch' to making distributions to AITCS was explicable by the commercial undesirability of making distributions to a corporate beneficiary that was actively trading, or had actively trading, given Mr Springer's transition to retirement and need to secure asset protection, by diverting distributions to a 'clean skin' company (AITCS).

3.6.2 BBlood

Framing the test

108. In his consideration of the 'ordinary family or commercial dealing', Thawley J placed emphasis on the need for a review of the arrangement as a cohesive whole, and not a 'sum of parts'

[65] Guardian AIT at 148.

examination. The statutory question posed by subsection 100A(13), as Thawley J sees is reflected in the following passage from the judgement:

> "93 In amplification of the last point, but expressed in simple terms, it is not sufficient to reason that, because each step in a series of connected transactions is capable of being described individually as "ordinary", therefore the whole agreement is "ordinary"."

109. Thawley J notes that the inquiry demanded by subsections 100(8) and (9), in determining whether an agreement exhibits a tax reduction purpose, may overlap with the inquiry demanded by subsection 100A(13) in assessing whether the arrangement is an 'ordinary family or commercial dealing[66].

110. Like Logan J, Thawley J also reads the 'ordinary family or commercial dealing' condition as requiring an evaluation of the fact pattern against a standard of 'artificiality' or complexity. Thawley J's own words from the decision illustrate this most clearly:

> "95 A dealing might not be an "ordinary family or commercial dealing" if the dealing, or the agreement which arose out of the dealing, is **contrived or artificial or involved more than was required to achieve the relevant objective**. The fact that the objective is achieved through numerous transactions, or that the transactions are complex, is not of itself sufficient to show that the dealing is not "ordinary". **Many ordinary commercial transactions are effected by an interlocking set of documents that might be characterised as complex**. Likewise, agreements entered in the course of a family dealing can be complex.
>
> 96 On the other hand, if the dealing, or the agreement which arose out of the dealing, **is overly complex**, involving more than is needed to achieve the relevant objective, or includes additional steps which are not necessary to achieving the objective, then the dealing might more readily be seen as not being "ordinary"."

111. Thawley J, drawing on the authority of Prestige Motors, also itemises the key consideration that led the court in that case to determine that the relevant fact patter did not comprise an 'ordinary family or commercial dealing'. These were ***an absence*** of:

a. "commercial motivation";

b. "commercial justification", leaving "the only explanation for the entry into the agreement as the elimination or reduction of tax liabilities"; and

[66] BBlood at 94.

c. "commercial necessity or justification for the transaction" or "commercial reason to raise capital from outside the group"[67].

112. In BBlood (FFC), it was conceded by the taxpayer that the the relevant agreement (identified as the Illuka Park Steps) was not an agreement entered into in the course of an ordinary family or commercial dealing[68].

Application of the evidence

113. In finding that the arrangement under review in BBlood was not, as a whole, an agreement entered into in the course of an ordinary family or commercial dealing, Thawley J gave weight to these considerations:

a. *The overall complexity of the arrangement:* Thawley J considered the series of steps involved in the fact pattern in BBlood as complex: a reasonable lay observer would probably agree. But, it is not the complexity of the steps per se that is relevant: as his honour states, may ordinary family or commercial dealings are complex. Rather it is the fact that the complexity of the arrangement was 'not shown to be necessary to achieving a specific outcome sought to be achieved by a dealing aptly described as "an ordinary family or commercial dealing"[69].

b. *An absence of a family succession or commercial purpose:* The Taxpayers, both in their evidence in court, and in the documentary evidence considered by the court, had stated that the proposed arrangement did fact serve a family purpose and a commercial purpose, being:

i. a commercial benefit would be derived by the group, in the form of a simplification of the family group structure, by removing the IP Trust as a shareholder of IP Co: as a consequence of the buy-back of the IP Trust's shares, the only remaining shareholder of IP Co would be Mrs Blood (who was the holder of 1% of the shares in IP Co at all times);

ii. a concomitant family benefit would be derived by the group, and the individual principals of the group, in that with an individual (Mrs Blood) as the only shareholder of IP Co, this would make future succession planning simple, by allowing for those shares to be dealt with under a Will.

The Taxpayer's submissions did not attract the court, with Thawley J finding both rationalisations 'unlikely'[70], largely because the purported simplification and succession-planning efficiency would not be achieved, or achieved to the degree that would justify the steps necessitated to achieve those goals. The court noted that as the share buyback largely denuded IP Co of its (prior to the arrangement, significant) retained earnings, that there was no real benefit in removing the IP

[67] BBlood at 96.

[68] BBlood (FFC) at 23.
[69] BBlood at 100.
[70] BBlood at 200.

Trust as a shareholder of IP Co, insofar as simplifying the group structure[71]. Similarly, the court failed to be convinced that any genuine 'succession planning' benefit would be derived by the transaction being carried out in the way it was, and an advisor to the arrangement recanted his evidence that this was the case under cross-examination[72].

c. *The 'novelty' of steps, particularly those that were facilitative of a tax outcome:* on the evidence, the court found there to be a lack of any historical pattern or behaviours in the distributions that were made or historical precedent for the event that had occurred. For example:

i. the 'creation' of income in IP Trust of some $300,000 had occurred for the first time and was not consistent with the historical behaviour of the parties[73];

ii. the amendment of the trust deed to replace the definition of income applicable under the terms of trust: although this was ultimately accepted to be largely unnecessary, other than to provide a greater degree of 'certainty' of approach[74];

iii. the incorporation of a 'new' corporate beneficiary of the IP Trust, which had been decided on as being necessary or desirable, to be the recipient of a distribution from the IP Trust[75].

Either of these events in isolation might be considered ordinary (perhaps even if they were novel); but according to Thawley J, events are not to be looked at in isolation. Where these events occur or are carried out as part of a '…a connected series of steps that were intended to operate in conjunction with each other as part of an overall agreement, arrangement or understanding', they were in the court's view 'extraordinary', particularly as they were individual steps that facilitated the overall tax outcome that was achieved by the implementation of the scheme (and, in the case of the trust deed variation, were part of the one 'suite' of documents entered into to give effect to the arrangement and was drafted by the same lawyers who drafted all of the transactional documents)[76].

[71] Ibid.
[72] BBlood at 207.
[73] BBlood at 101.
[74] BBlood at 194.
[75] BBlood at 195.
[76] BBlood at 101 and 193.

3.7 Tax reduction purpose

3.7.1 Guardian AIT

Framing the test

114. In framing the tax reduction purpose test in section 100A(8), Logan J (as does Thawley J in BBlood), reference this observation by Hill J in East Finchley:

> "It will be recalled that s 100A(8) requires the purpose of entering into the relevant arrangement to be the reduction of a liability of some person to income tax. It requires the hypothesis to be formulated as to what income tax would become payable if the relevant agreement had not been entered into." [emphasis in original]

115. Drawing on this authority as licence to draw an analogy to Part IVA decision (*AXA Asia Pacific Holdings Ltd v Federal Commissioner of Taxation*[77]), Logan J frames the test as one which requires an objective evaluation, which is however to be informed by a consideration of the prevailing commercial, personal or family circumstances of the relevant taxpayer and the taxpayer's particular actions, all of which may be ascertained subjectively[78]. As such, a consideration of a 'counterfactual' or alternative scenario to that which did in fact occur would be instructive in determining the purpose of the taxpayer in a particular case.

116. In Guardian AIT (FFC), there was no consideration of the tax reduction purpose test in section 100A(8), given the Court's determination that the threshold requirement that there be an agreement was not satisfied.

Application of the evidence

117. In his application of the tax reduction purpose test to the fact pattern before him in Guardian AIT, Logan J reiterates the subjective circumstances concerning Mr Springer and his family group, particularly:

i. that he was in transition to retirement in 2012;

ii. that he had a genuinely held objective in structuring his affairs to achieve a degree of asset protection (which would be facilitated by a 'cleanskin' corporate beneficiary) [79];

[77] (2009) 77 ATR 829.
[78] Guardian AIT at 163.
[79] Guardian AIT at 101.

iii. Mr Springer's financial means overall, which were such that he did not have an immediate need for the funds comprising the distribution (at 165):

> "Yet further, and as Mr Fischer's evidence highlighted, Mr Springer was already a wealthy man. As at 30 June 2012, he had unpaid present entitlements in the AIT of $10.63 million. In addition to that, he had loaned the trust some $3.84 million. There was no suggestion that loan was irrecoverable. He just did not need the trust distribution posited by the Commissioner in order to enjoy his retirement."

iv. Based on evidence of correspondence between Mr Springer and his accounting advisors, that there was no forward-planning with respect to Mr Springer's financial affairs and that determinations with respect to distributions were made 'ad hoc'[80]

118. Against this context, Logan J was compelled to find that it is not open to the Commissioner to Mr Springer's alternative course of action would be one which involved no tax benefit accruing to him or one which would have achieved the same overall outcome, by means of either a 'pay out' of the UPE by the AI Trust to AITCS or AITCS allowing the AI Trust to enjoy the benefit of the funds comprising the distribution to it by means of a Division 7A compliant loan agreement. The Commissioner's postulate, that the trust would have otherwise distributed to Mr Springer as a beneficiary of the AI Trust, rather than the distribution as between the AI Trust and AITCS, while a 'lawful, theoretically available possibility', was not considered by the court to be a tenable 'counterfactual' to that which actually occurred[81].

3.7.2 BBlood

Framing the test

119. It is on this element of section 100A in which the conception of the requirements of the tax reduction purpose test as between Logan and Thawley JJ most differ. Thawley J rebukes the proposition that the interpretation of subsection 100A(8) should incorporate a Part IVA-inspired 'alternative postulate' test[82], his honour noting that Part IVA post-dates section 100A by some years[83], and that no such principle was intended to be incorporated into section 100A by the statement of Hill J in *East Finchley*[84]. His honour notes that section 100A is drafted such that a taxpayer's purpose must only include a tax reduction purpose, as distinct from Part IVA, which

[80] Guardian AIT at 174.
[81] Guardian AIT at 171.
[82] BBlood at 166.
[83] BBlood at 153.
[84] BBlood at 176 and 177.

sets the test at a higher standard (a sole or dominant purpose).[85] Nor is it necessary for any precise amount of tax avoided or reduced to be determined[86].

120. Against what Thawley J considers to be the very wide legislative formulation of subsection 100A(8), he finds it sufficient if[87]:

> *"…it is sufficient if it can be said that the purpose was one of securing that a person not be liable to income tax or be liable to less income tax, even though it might not be possible to identify precisely who the person was or the year of income in which tax would be avoided or necessarily the precise amount."*

121. Thawley J does not frame the 'test' in subsection 100A(8) as being an strictly or completely objective one. Rather, Logan J finds that subsection 100A(8) calls for a consideration and evaluation of:

a. the objective facts, which may include the financial, taxation and other consequences of the transaction entered into[88], and a consideration of what reasonable inferences can be drawn from those facts; **and**

b. direct evidence from a relevant party as to that party's purpose (which may include contemporaneous documents or testimony provided in court and tested under cross-examination)[89].

a. Thawley J's decision, and its examination of the facts and the application of those facts to the requirements of subsection 100A(8), shows that subjective evidence if highly influential, if not equally influential as the objective circumstances.

122. In BBlood (FFC), the Full Federal Court (Moshinsky, Colvin and Hespe JJ) consider the purposive element of sections 100(8) and 100(9). Summarising the principles enunciated by the Full Federal Court:

a. The Full Federal Court held that "[t]he purpose to be identified is not an objective purpose of an agreement but the purpose of *a person who is a party to the agreement*", which is to be ascertained at the time of the entry into the agreement, can include advisors 'formulating the documentation and implementing the arrangement with the knowledge and assent of the controllers of the entities who were parties to the transactions', and need not be the sole or dominant purpose[90];

[85] BBlood at 131.
[86] BBlood at 166.
[87] BBlood at 166.
[88] BBlood at 135.
[89] Ibid.
[90] BBlood (FFC) at 42 and 43.

b. the effect of an agreement and a comparison of the outcome of an agreement against a hypothetical alternative to achieve commercial outcomes is not part of the statutory task required by sections 100(8) and 100(9);[91]

c. an inquiry of the purpose of a party is a historical enquiry as to the purpose of a party and why that party entered into the relevant agreement,[92] and this may require consideration of the party's understanding of the effect achieved and/or the intended effect to be achieved by the arrangement, irrespective of whether that understanding is correct;[93]

d. historical matters to be considered may include departures from earlier practices that do not have a commercial justification[94] and may include facilitative steps that enable an effect to be achieved;[95]

e. of themselves, non-cash transactions (for example the assignment or set-off of debts) to create and satisfy entitlements is not a relevant consideration.[96]

Application of the evidence

123. As Thawley J suggests under his framing of the test required by section 100A(8), if the outcome of an arrangement is a tax benefit for the taxpayer, than the steps that have brought about that outcome, reviewed objectively, are suggestive that the purpose of those steps is to secure the tax benefit obtained. He sets out the 'objective' facts, those which largely 'speak for themselves', in a succinct, clear and linear fashion. He concludes that what those objective facts speak to is a purpose of securing a tax benefit, that being (to paraphrase) the 'parking' of the share buyback proceeds as 'trust capital' in the IP Trust, while at the same time 'passing' the tax liability to IP Co (where, as a franked dividend, it would incur no further tax), where at the same time IP Co would have no legal entitlement to those proceeds. The relevant passage of the judgement is worth extracting:

> "180 The effect of the Illuka Park steps: The effect of the Illuka Park steps, absent the application of s 100A, was as follows:
>
> (1) IP Co transferred its retained profits to the IP Trust.

[91] BBlood (FFC) at 46 and 47.
[92] BBlood (FFC) at 47.
[93] BBlood (FFC) at 50 and 55.
[94] BBlood (FFC) at 56.
[95] BBlood (FFC) at 57 and 58.
[96] BBlood (FFC) at 64.

(2) For trust purposes, the IP Trust received ordinary income (the dividends and a distribution, together totalling $304,376.97) and capital (the proceeds of the share buy-back, namely the Share Buy-Back Dividend of $10,189,671).

(3) For tax purposes, the proceeds of the share buy-back were deemed to be a dividend. BE Co did not receive the benefit of the share buy-pack proceeds but was liable to tax in respect of the whole of the net income of the IP Trust, comprising both the ordinary income ($304,376.97) and the Share Buy-Back Dividend ($10,189,671). Under s 4-10 of the ITAA 1997, the amount of income tax owed is calculated after taking into account tax offsets. IP Co allocated the Franking Credit of $4,367,002 to the Share Buy-Back Dividend. The tax which would have been payable on the Share Buy-Back Dividend if there were no franking credits was wholly offset by the Franking Credit.

(4) The IP Trust retained the amount of the Share Buy-Back Dividend as corpus of the trust. It was not liable to pay tax under s 99A of the ITAA 1936 because it had distributed all of its (trust) income.

182 **An objective assessment of the agreement and its effects weighs heavily in favour of a conclusion that a person had a purpose of securing that a person pay less tax in a year of income."** (emphasis added)

124. In his assessment of the 'subjective' elements that evince purpose, Thawley J places emphasis on:

a. the steps which are idiosyncratic, and which are facilitative of the ultimate tax outcome achieved by the scheme, including:

i. the introduction of income into the IP Trust from the B&E Trust (without which the 'mismatch' between trust and tax net income would not arise), which was inconsistent with the group's historical behaviour and pattern of distributions[97];

ii. the distribution by IP Trust to BE Co, which had been incorporated a week prior[98];

iii. the amendment of the IP Trust's trust deed;

iv. the incorporation of a new corporate beneficiary[99];

v. the implementation of the share buyback[100]; and

vi. the fact that individually, there was no commercial, succession or family rationale for any of these steps.

[97] BBlood at 184 and 185.
[98] BBlood at 187.
[99] BBlood at 195.
[100] BBlood at 200.

b. The fact that the 'strategy' that was implemented was presented to the principals of the taxpayer group 'for reasons which included a purpose of securing that less tax be paid in relation to the distribution of company profits', as reflected in the contemporaneous documents and advice prepared by advisors in connection with the proposed arrangement[101], and originated with the advisors rather than from the group's principals seeking advice on succession planning or group rationalisation[102], as confirmed in testimony from one of those principals, Mr Blood[103] - indicating that these rationalisations were 'retro-fitted' to the arrangements after the fact;

c. the apparent lack of understanding of the minutiae of the transaction by the principals of the group, Mr and Mrs Blood, but an inferred understanding that the transaction, if implemented, would result in a beneficial tax outcome for the group[104];

d. consequently, the advisors had a tax reduction purpose in entering into the agreement, and that purpose was imputed onto Mr and Mrs Blood.

125. In BBlood (FFC), the Federal Court held as follows:

> 61 As explained above, a consideration of alternative ways in which a commercial outcome might be achieved can be relevant in considering the purpose of a party to an arrangement. A consideration of whether there were other ways of achieving the same commercial outcome may assist in understanding why the arrangement in fact entered into was entered into. The primary judge considered that an ordinary commercial transaction to move retained earnings from IP Co to the IP Trust which owned shares in IP Co would be for IP Co to pay a dividend to the IP Trust. There was no error in the primary judge's consideration of the alternatives of the payment of dividends and liquidation in evaluating the purpose of the parties entering into the arrangement at PJ [197]–[204].
>
> 62 The examination of the facts and circumstances relevant to an investigation of the purpose of a party as required by s 100A(8) supports the conclusion that a party (and, in particular, Mr Buckley) **entered into the reimbursement agreement for a purpose of ensuring that the retained earnings of IP Co could be distributed to and retained by the IP Trust without IP Trustee being liable to tax**. It was therefore to be concluded that the reimbursement agreement was entered into for a purpose of securing that IP Trustee who, if the agreement had not been entered into, would have been liable to pay income tax in respect of the 2014 income year, would not be liable to pay income tax in respect of that year of income. The primary judge was correct to hold that the appellant had not discharged its onus of establishing that the carve out provided for in s 100A(8) applied.

[101] BBlood at 215.
[102] BBlood at 216.
[103] BBlood at 236.
[104] BBlood at 236.

4. Appendix A: Executive summary (Guardian AIT and BBlood)

Formulation of the test	Relevant factual considerations and evidence	
	Factors	***Evidence***
Agreement, arrangement or understanding (and causation)		
Guardian AIT		
Temporal sequence: ▪ a 'reimbursement agreement' must exist before a present entitlement [*Guardian AIT at 128*] ▪ the agreement must not be a matter which is 'entirely conjectural' or a mere expectation [*Guardian AIT (FFC) at 117*] ▪ 'Agreement' invokes a requirement of 'consensus and adoption' (in particular, or professional advice) [*Guardian AIT (FFC) at 124*]	▪ Does the timing and sequence of the executive steps or events show that there is a coincidence in those executive steps or events? ▪ Does the taxpayer (assessed prospectively) apply any process and formality to financial and tax affairs: are decisions made in advance or 'ad hoc' and reactive year-by-year?	▪ Timing of the executive steps or events (chronological sequence) [*Guardian AIT at 132*] ▪ Timing (and content) of advice from professional advisors [Guardian AIT at 117] ▪ Contemporaneous correspondence with advisors regarding distribution decisions (around year-end) [*Guardian AIT at 59*] ▪ Year-end planning workpapers (multi-year) [*Guardian AIT at 59]*

BBlood

Singular, unified arrangement: a connected series of steps that were intended to operate in conjunction with each other as part of an overall agreement, arrangement or understanding [*BBlood at 80*]	▪ Is there a pre-ordained strategy/series of executive steps or events intended to operate in an integrated fashion and implemented in a unified way? ▪ Does the timing of events reveal or indicate a unity e.g. has the recipient of the distribution been incorporated shortly before the distribution being made to it? ▪ Is the arrangement implemented by way of an integrated set of documents prepared at the same time and by the same authors, showing that: *they were perceived to form one overarching transaction or arrangement by those who prepared them, those who advised in respect of them, and those who entered into them* [*BBlood at 82*]	▪ Professional advice preceding implementation of the agreement and what is says with respect to the necessary executive steps and events and the tax outcome [*BBlood ay 81*] ▪ Transaction documents (as a 'suite' of documents prepared by a single advisor) [*BBlood at 82*] ▪ The advisor's experience/conduct with other clients [*BBlood at 82*]

Ordinary family or commercial dealing

Guardian AIT

Artificiality:

- Does the arrangement as a whole (but looking at its individual steps or parts) reveal any '*artificiality*', in respect of any executive step or event [Guardian AIT at 144]

- Is the arrangement explicable by a desire to achieve asset protection? If so, will the desired asset protection be achieved by the arrangement in fact and substance?

- Is the arrangement explicable by a desire to achieve a commercial, succession (personal or business) or a family purpose? Is so, will that commercial, succession or family purpose be achieved by the arrangement in fact and substance?

- Does the taxpayer (not their advisor) have a practical understanding of how asset protection will be achieved by implementing the arrangement?

- The taxpayer's professional or business activities and the risks arising from those activities - is it real and appreciable? [*Guardian AIT at 150*]

- The taxpayer's current life circumstances, including retirement intentions, marital status, family relationships [*Guardian AIT at 151*]

- Effectiveness of the structure in achieving asset protection - is there any actual protection from risk (e.g., by introducing a corporate beneficiary or a trust into the structure)? [*Guardian AIT at 151*]

- Taxpayer's evidence of their understanding of the rationale of the arrangement and its effect. [*Guardian AIT at 147*]

- The taxpayer's historical pattern of distributions or tax management behaviour [*Guardian AIT at 148*]

BBlood

Non-tax rationale: Viewing the arrangement and the executive steps and events comprising it as a cohesive whole (not by is individual events or steps):

- is the arrangement contrived, artificial or 'overly complex' such that it involves more than is needed to achieve the objective; and
- does the arrangement exhibit an absence of commercial motivation, justification or necessity [BBlood at 95 to 96]

- Is the arrangement complex, involving multiple steps or events?
- Is the arrangement explicable by a desire to achieve a commercial, succession (personal or business) or a family purpose? If so, will that commercial, succession or family purpose be achieved by the arrangement in fact and substance?
- Are there steps involved which 'facilitate' the overall tax outcome desired to be achieved e.g. The introduction of a new beneficiary or a variation to the terms of the trust deed.

- When assessed against the taxpayer's stated commercial or family purpose for the arrangement, is that commercial or family purpose achieved? [*BBlood at 200*].
- Are any executive steps or events explicable only by reason of the fact that they facilitate the ultimate tax outcome desired to be achieved by the arrangement? [*BBlood at 101, 193 to 195*]

Tax reduction purpose

Guardian AIT

Objective test (informed by subjective evidence):

- when viewed objectively, with reference to a 'counterfactual' grounded in practical reality given the prevailing commercial, personal or family circumstances of the taxpayer (shown objectively), is a purpose of the scheme the reduction of tax? [*Guardian AIT at 163*]

- What is the taxpayer's commercial, personal or family circumstances and objectives or purpose in context of those circumstances (informed by subjective evidence)?
- By what means, other than the arrangement entered into, could the taxpayer's commercial, personal or family objectives have been achieved?

- The taxpayer's professional or business activities and the risks arising from those activities - is it real and appreciable? [*Guardian AIT at 150*]
- The taxpayer's current life circumstances, including retirement intentions, marital status, family relationships [*Guardian AIT at 151*]
- Patterns of historical behaviour as part of the taxpayer's tax management (e.g., patterns of distributions historically) [*Guardian AIT at 148*]
- 'Counterfactual' that would have met the taxpayer's commercial, personal or family objectives or requirements [*Guardian AIT at 171*]

BBlood

Multifactorial test (objective facts and subjective evidence):

- the taxpayer's purpose is to be informed by a consideration of:
  - The objective facts, including the financial taxation and other consequences of the arrangement entered into;
  - Direct evidence from a relevant party (including advisors) as to that party's purpose (either in contemporaneous documents or testimony in court tested under cross-examination) [*BBlood at 135*]
- A consideration of a counterfactual may inform the inquiry but subsection 100A(8) is not a counterfactual evaluation as is the case with Part IVA (confirmed in BBlood (FFC))
- Must be the purpose of a 'party' to the agreement ascertained at the time of entry into the agreement - historical behaviour and patters will be given weight [BBlood FFC at 46 to 64]
- When the executive steps and events in the arrangement are considered objectively, what are the tax and financial outcomes which arise from those executive steps and events?
- Did the taxpayer's advisors present the arrangement as one which was productive of a tax outcome that was beneficial for the taxpayers?
- Are there steps involved which 'facilitate' the overall tax outcome desired to be achieved e.g. The introduction of a new beneficiary or a variation to the terms of the trust deed.
- The tax, financial and commercial consequences of the executive steps and events in the arrangement (considered objectively) [*BBlood at 180 to 182*]
- Advice from professional advisors and whether that was instigated by the advisors or the taxpayers [*BBlood at 215*]
- Evidence (documentary and testimony) from the advisors - what is understood by the taxpayers about the arrangement and what its consequences would be? [*BBlood at 236*]

5. Appendix A: Comparative analysis - Draft v Final ATO Guidance[105]

Substantive Changes made to TR 2022/4 compared with TR 2022/D1

The 'Connection Requirement'

1. The Commissioner has made two substantive alterations to the 'connection requirement'.

    f. First, the Commissioner has altered his position as to what needs to be relevantly connected with the 'reimbursement agreement'. While in TR 2022/D1, the Commissioner contended that the 'reimbursement agreement' must be connected with a 'legally-effective (present) entitlement',[106] this requirement does not appear in the TR 2022/4. Rather, the Commissioner assets the 'reimbursement agreement' must be connected with a 'beneficiaries present entitlement' or 'income paid to or applied for the beneficiary'.[107]

    g. Second, the Commissioner has amended the requirement in relation to the temporal aspect of the 'connection requirement'. In TR 2022/D1, the Commissioner states that the 'reimbursement agreement' must have existed prior to the entitlement arising.[108] However, the Commissioner now asserts that the 'connection requirement' would be satisfied if the agreement 'occurred simultaneously with' the entitlement.[109]

The 'Tax Reduction Purpose Requirement'

    h. The Commissioner had added in TR 2022/4 that, for this requirement to be satisfied, no alternative postulate need be established to identify a specific amount of tax avoided by the transaction.[110]

    i. In TR 2022/4, the Commissioner has stated that 'purpose' refers to an '*actual* purpose of entering the agreement', which may be determined by the parties' evidence and surrounding circumstances behind the transaction entered into.[111] This includes the purpose of an advisor. If the advisor is also a party to the agreement, the purpose of an advisor will be directly relevant. This elaboration seemingly makes this requirement harder to satisfy, as it must be

[105] I acknowledge the assistance provided by Alec Masel with the preparation of this analysis.
[106] TR 2022/D1 at [6]
[107] TR 2022/4 at [8]
[108] TR 2022/D1 at [12]
[109] TR 2022/4 at [16]
[110] Ibid at [22]
[111] Ibid at [21]

proved that the parties actually intended on achieving a tax benefit. However, a purpose may continue to be imputed to a party the agreement who acts on advice from an advisor.[112]

The 'Ordinary Dealing' Exception

j. In TR 2022/4, the Commissioner makes two amendments. First, the Commissioner has added that it 'is not sufficient that each step in a series of connected transactions is capable of being described as ordinary'.[113] Second, the Commissioner has changed the language concerning the presence of tax driven features in arrangements and their effect on an arrangement fitting within the exception. In TR 2022/D1, the Commissioner suggested that the presence of tax driven features is 'relevant' in determining whether the arrangement is within the exception.[114] In TR 202/4, the Commissioner states that 'if the objective of a dealing can properly be explained as the payment of less tax….rather than some other objective…*it is not* an ordinary family or commercial dealing'.[115]

k. The Commissioner has also altered the framing of the test for whether a dealing satisfies this exception. In TR 2022/D1, the Commissioner emphasised that the test was an 'evaluative standard' that required examining the 'objects' the arrangements are apt to achieve.[116] Paragraph [27] of TR 2022/4 expands upon this test, listing a set of factors which suggest the dealing may fall outside the exception. The Commissioner has also added that the historical behaviour of the parties is relevant.[117]

Examples

Context

l. Examples One to Four[118] in TR 2022/4 have been inserted by the Commissioner to illustrate the importance of context to the 'ordinary family or commercial dealing' exception. The examples indicate that certain factual and cultural circumstances, which are not explicitly part of any agreement, have the capacity to render an agreement not a 'reimbursement agreement'. Such factors include medical needs of family members[119] and established cultural practices of providing benefits to family members.[120] However, as Example Four illustrates,[121] the relevant context must explain the provision of the benefit for the exclusion to apply.

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[112] Ibid at [24]
[113] Ibid at [26]
[114] TR 2022/D1 at [30]
[115] TR 2022/4 at [28]
[116] TR 2022/D1 at [21-2]
[117] TR 2022/4 at [27]
[118] See Appendix One TR 2022/4
[119] TR 2022/4 at [96]
[120] Ibid at [110-111]
[121] TR 2022/4 at [113]

m. Amendments made to Example Eight in TR 2022/4 further evidence the Commissioner's view that context is an important factor in determining whether the exception applies.[122] In this example, the Commissioner indicates that 'financial or cultural circumstances' which explain a gift from a family member with a low tax rate to a family member with a higher rate of tax may mean the arrangement fits within the exception. On the previous version of the example,[123] no such caveat is found.

Gifts to Children

n. In Example Eight of TR 2022/4, which relates to gifts made from parents from funds attributable to their trust distributions to their children, the Commissioner has amended their view as to when such gifts may not satisfy the exception.

o. In the equivalent of Example Eight in TR 2022/D1, the Commissioner indicated that gifts made to children, where the parent has a lower marginal tax rate *and* has lesser means that the adult child *and* the child is capable of benefiting under the trust, may not satisfy the exception. This position has been updated such that the presence of any one of these facts suggests the exception does not apply.[124]

p. The Commissioner has also added to Example Eight the situation in which the child, who is on a lower tax rate than their parents, applies their trust entitlements to repay their parents for expenses incurred when the child was a minor. The Commissioner suggests such situations would likely not fall within the exception.[125]

Unpaid Entitlements Held on Trust

q. Example Nine in TR 2022/4 covers the situation of unpaid entitlements continuing to be held on trust for adult family member beneficiaries. The Commissioner has made two substantial amendments to this example.

r. In the updated example, the Commissioner has suggested that where an arrangement simply involves delaying the provision of the benefit to the adult family member beneficiary, the arrangement would likely be considered to fall within the exception.[126] No such statement appeared in TR 2022/D1.

s. In TR 2022/D1, the Commissioner indicated that if the trust's funds were applied 'in a way inconsistent with an intention to satisfy (the beneficiary's) entitlements should the trustee be called upon' to do so, then the exception would not apply.[127] However, this has been

[122] Ibid at [143]
[123] TR 2022/D1 at [114] - Example Three
[124] TR 2022/4 at [144]. Compare with TR 2022/D1 at [115]
[125] Ibid.
[126] Ibid at [146].
[127] TR 2022/D1 at [123]

rephrased in TR 2022/4. The Commissioner here suggests that the exception would not apply if the funds are applied in a way 'inconsistent with an intention that (the beneficiary) would ultimately receive' the benefit.[128]

Non-Commercial Loans Between Family Members

t. Example Ten of TR 2022/4 concerns interest free loans made between family members using funds attributable to trust distributions.

u. One amendment made to this example indicates a more favourable position for the taxpayer concerning the 'tax reduction purpose' requirement. Concerning the situation of a family member with a low tax rate lending money attributable to a trust distribution to a family member on a higher tax rate, the Commissioner has stated in the final ruling that this fact alone does not suggest that the arrangement satisfies the 'tax reduction purpose' requirement.[129] The previous version of the example had no statement to this effect.

v. Another two amendments made to this example shed light on the Commissioner's view of the exception.

w. In the previous example, the Commissioner indicated that 'repeated' non-commercial loans to family members on higher tax rates may not fall within the exception.[130] The Commissioner has updated the phrasing of this example to 'repeated' loans made to members with higher tax rates who are able to support themselves financially may not fall within the exception.[131]

x. In the previous version, the Commissioner indicated that interest free loans between family members fall within the exception 'because of (the) family relationship'.[132] However, the Commissioner has revised this statement in TR 2022/4 to read that such loans would fall within the exception because the 'family relationship and relevant circumstances' which provide context to the loan.[133] This change suggests that interest free loans between family members, without additional context, would not necessarily fall within the exception.

Removals

y. Two examples which appeared in the draft ruling have been removed from the final ruling. The first relates to a 'trust entitlement gifted to (a) trustee'[134] and the second relates to a 'dealing at arm's length and loan on commercial terms'.[135]

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[128] TR 2022/4 at [147].
[129][129] Ibid at [152].
[130] TR 2022/D1 at [127]
[131] TR 2022/4 at [153]
[132] TR 2022/D1 at [126]
[133] TR 2022/4 at [152]
[134] TR 2022/D1 at [116-120].
[135] Ibid at [128-132].

Added examples in TR 2022/4 not appearing in TR 2022/D1 (Tracked Changes)

Example 1 – identifying family objectives

96. *In an income year, family members agree to gift their trust distributions to one family member, Paul, who has significant medical bills. The arrangement is implemented via trust distributions to the family members and a gift by each of them to Paul. That Paul has significant medical bills is not a part of the agreement; however, it is a highly relevant contextual fact which demonstrates the content of the family objectives.*

Example 2 – cultural practice of gifting

110. *Azra is a member of an extended family whose members' cultural values include grandparents gifting money or goods to younger members of the family during the festive season. This cultural practice is relevant in considering whether transactions that involve Azra gifting money to her grandchildren out of funds from a trust distribution she has received have been entered into in the course of ordinary family or commercial dealing.*

Example 3 – cultural practice to support older relatives

111. *Jack lives by the practices that have been common for centuries in the culture that he draws his heritage from. One of those practices is that children will meet the needs for shelter and living of their parents and other older relatives when they are no longer participating in the workforce. This is founded in notions of respect for elders and is practiced irrespective of what means those relatives would have to fund their own needs from available resources. This cultural practice is relevant in considering whether Jack's direction to the trustee of a trust to apply his entitlements to meet mortgage repayments for his aunt, who has retired from her employment working in a factory, is in the course of ordinary family or commercial dealing.*

112. Cultural factors refer to the distinct and observable ideas, customs or practices of people or certain groups within a society. The existence of a cultural factor which is not widely understood in the broader community can be demonstrated by evidence. As the core test is applied to the whole of the agreement, rather than the individual steps, whether the presence of a cultural factor determines if a dealing is entered into in the course of ordinary family or commercial dealing will depend on the facts of the case.

Example 4 – cultural practice of not accepting entitlement

113. *Max and the trustee of a trust he controls agree to distribute certain income of the trust to Asher, a non-resident who for religious reasons will not accept the entitlement. While Asher's beliefs are a cultural factor that explains why the entitlement will not be called for, in these circumstances they do not, without more, explain the objectives for making the resolution to distribute in the first place.*

Example 5 – allocation of capital gains when section 100A applies to a present entitlement

130. Trust income is defined to be equal to section 95 net income. The trustee derives the following income in the income year:

- *interest income of $10,000*
- *non-discount capital gain of $30,000.*

131. Beneficiary A is presently entitled to $5,000 trust income from interest. Beneficiary B is presently entitled to $5,000 trust income from interest and the capital gains. Beneficiary B's present entitlement confers the financial benefit which gives rise to a specific entitlement to the capital gain.

132. Beneficiary B's entitlements are subject to section 100A. Where Beneficiary B's total entitlements are subject to section 100A, the allocation will be as follows:

- *Beneficiary A is entitled to $5,000 trust income from interest*
- *no one is presently or specifically entitled to $5,000 interest and $30,000 capital gain.*

133. The capital gain is taxed in accordance with adjusted Division 6 percentages:

- *Beneficiary A's adjusted Division 6 percentage = [($5,000 ÷ $40,000) × 100] = 12.5%.*
- *Trustee's adjusted Division 6 percentage = [($35,000 ÷ $40,000) × 100] = 87.5%*
- *Beneficiary A is taxed on $5,000, which includes $3,750 (12.5% × $30,000) capital gain*
- *Trustee is taxed on the balance of the capital gain which is $26,250 (87.5% × $30,000).*

Changes made by TR 2022/4 to examples which appeared in TR 2022/D1 (mark-up)

Example ~~1~~6 – trust established under a will

135. A trust established under a will provides that ~~William~~Taylor, the ~~grandson~~grandchild of the deceased, is entitled each year to all of the trust income, although it is not to be paid to ~~him~~them until ~~he is~~they are 25 years of age (and thereafter) or, if ~~he dies~~they die before attaining the age of 25, to ~~his~~their estate.

136. At the time the trust is created, ~~William~~Taylor is 15 years of age. The income is used by the trustee to ~~make~~invest in further income-producing ~~investments~~assets.

137. Section 100A does not apply ~~in relation~~ to the entitlement to income of a minor beneficiary.~~66~~ 124 Additionally, after ~~William~~Taylor turns 18, ~~and absent other facts,~~ section 100A would not apply to the retention of income until ~~William~~Taylor attains 25 years of age and the reinvestment of that income on the terms of the trust on these facts because:

- *even if further evidence were to show that this course of conduct involves an 'agreement' that would satisfy the connection requirement, it would be an ~~arrangement~~agreement entered into in the course of ordinary family or commercial dealing~~.~~*
- *there is nothing in the stated facts to indicate that the tax reduction purpose would be satisfied.*

Example ~~2~~7 – distribution to spouses with mixed finances

~~137.~~138. The Rosegum Family Trust is controlled by spouses~~,~~ Lisa and ~~Matthew~~Jessie Rosegum, who are the primary beneficiaries of the trust. The trust has a widely-drawn objects clause, which includes family members of Lisa and ~~Matthew~~Jessie and their related entities.

~~138.~~139. Each year, the trust makes Lisa and ~~Matthew~~Jessie presently entitled to the income of the trust in equal proportions.

~~139.~~140. Lisa and ~~Matthew~~Jessie have generally shared financial responsibilities and fund their lifestyle from a common pool of assets, save for some expenses which they fund from their own savings individually, such as expenses incurred by Jessie for their hobby garden.

141. While the facts do not indicate whether any person had a purpose of reducing income tax when entering into the agreement, so as to cause the tax reduction purpose requirement to be satisfied, the arrangement is nonetheless unlikely to be a reimbursement agreement.

142. Trust distributions to spouses who generally have shared financial responsibilities and who ultimately enjoy the shared benefits of the distribution would usually be capable of explanation as achieving ordinary ~~familial objects without the need for further explanation. Absent any additional factors taking the arrangement beyond those ordinarily encountered in the organisation of financial affairs between spouses, the arrangement would likely be entered into in the course of ordinary dealing.~~family objectives. On these facts, the organisation of financial affairs between spouses would likely be entered into in the course of ordinary family or commercial dealing.

Example 8 – gift from parents ~~gift~~ to a child

~~114. Assume the same facts as Example 2 of this Ruling. In one year, Lisa and Matthew's eldest child, Kate, purchases a property. Lisa and Matthew pay for the deposit with funds attributable to their distribution from the Rosegum Family Trust. The making of gifts between family members for ordinary familial purposes, such as parents contributing to the purchase of~~

~~a house, without additional facts, would usually be ordinary dealing, as able to be explained as achieving ordinary familial objects without the need for further explanation.~~

143. Assume the same facts as Example 7 of this Ruling. In one year, Alex (being Lisa's eldest daughter and Jessie's stepchild) purchases a property. Lisa and Jessie pay for the deposit for the purchase of the home as a gift to Alex, from funds attributable to their distribution from the Rosegum Family Trust. While on these facts, the creation of an entitlement and gifting from that entitlement may raise questions about whether the entitlement arose under or in connection with an agreement between the parties, the making of gifts between family members for ordinary family objectives, such as parents contributing to the purchase of a house, would usually be ordinary family or commercial dealing.

144. The following additional or alternative facts may change the conclusion made in paragraph 143 of this Ruling and make it less likely that an agreement has been entered into in the course of ordinary family or commercial dealing. Were that the case, it would be of greater relevance to examine whether one or more persons have a purpose of reducing income tax when entering the agreement (so as to cause the tax reduction purpose requirement to be met) and examine further whether the connection requirement is met:

- If the arrangements were to involve parents gifting money received from a trust to their children repeatedly and one or more of the ~~parent has~~following factors are present
  - the parents have a lower marginal tax rate ~~and~~
  - the parents have lesser financial means than the adult child ~~who~~ , or
  - the adult child is also capable of benefitting under that trust in their own right ~~(such as~~ ; for example, the parents may be subject to lower tax rates because they are retired ~~parents repeatedly gifting trust entitlements to higher marginal tax rate children in lieu of the trustee distributing to the adult child directly), or~~and in pension phase or have significant losses to reduce tax payable on trust distributions.
- Arrangements where the situation is reversed, so that ~~Kate, who is less financially advanced, gifted~~ Alex (who has limited financial resources apart from a distribution made to her and has a lower marginal tax rate) gifts money to ~~Lisa and Matthew, particularly where the adult child~~ her parents Lisa and Jessie who are subject to higher rates of tax, and there is no financial or cultural circumstance that would explain the gift.
- Arrangements where Alex, who has a lower marginal tax rate ~~than the parent (see Example 4 of this Ruling).~~ apply her trust entitlements to ~~her parents, or instead of gifting back to the trust, Pauline applies her trust entitlements to repay~~reimburse her parents for costs incurred by them on her maintenance,

education and financial support while ~~Pauline~~Alex was a minor.

Example ~~5~~9 – unpaid entitlements held on ~~separate~~ trust

~~115.~~ From time to time, the trustee of the Davidson Family Trust makes John, who is a family member, presently entitled to a share of trust income. ~~John's~~John's entitlement is determined so his taxable income will not exceed certain marginal tax rate thresholds.

145. *John is a full-time student and does not have income from other sources. ~~In a particular year, funds underlying the present entitlement are set aside to be held by the trustee upon a separate trust for the sole benefit of John, who~~John has indicated to the trustee that he ~~may be unlikely to~~will not call for the payment of the amount of his entitlements until such time as he purchases a home or makes a similar investment. Nonetheless, John is at liberty to ~~call for his trust entitlements~~enforce his rights as beneficiary to recover those amounts at any time.*

146. *~~John's~~ John's tax-free threshold reduces the overall tax on the trust net income. However, in the absence of additional factors, the arrangement that involves John simply delaying the time when he would realise the benefit of his original trust entitlement would likely be entered into in the course of ordinary dealing.*

147. *A different outcome may arise if, for example, ~~instead of setting funds aside for John upon a separate trust,~~ the trustee:*

- *loans the funds on interest-free terms for an undefined period to another person, or*
- *otherwise applies the trust's funds in a way that is inconsistent with an intention ~~to satisfy John's~~that John would ultimately receive the amount of his entitlements~~, should the trustee be called upon by John to do so~~.*

Example ~~6~~10 – non-commercial loan between family members

149. The Jones Family Trust includes in its class of beneficiaries Mr and Mrs Jones and their ~~three~~3 adult children ~~Amy~~, Zara, Ben and ~~Claire~~Sherry. Zara has a higher marginal tax rate than Mr Jones. Each year, the trustee resolves to make each of these beneficiaries presently entitled to 20% of the trust income.

150. In one year, Mr Jones lends ~~Amy~~Zara an amount which is similar to the amount of trust income he is presently entitled to. The advance of the funds is made by Mr Jones directing that the trustee satisfy an amount of his entitlement by paying it to Zara. He does this to help ~~Amy~~Zara move out of her home~~. The~~ because she has recently separated from her de facto partner. The lent funds are used by Zara to cover half of her rental obligations and relocation expenses. Mr

Jones loaned the money on the understanding that Zara would repay him when her financial circumstances allowed. There is no suggestion that interest will be paid.

~~149.~~151. In the following year, Zara is made presently entitled to 20% of the trust income; however, Mr Jones again lends Zara an additional $10,000, sourced from his present entitlement later that year to cover urgent repairs that are unexpectedly required to Zara's car. Again, the loan ~~requires Amy to pay Mr Jones back the principal~~is made on the understanding that Zara will repay the total of the amounts advanced when her financial circumstances permit ~~and~~, without interest.

152. ~~Although the terms of the loan are not commercial~~The loans made by Mr Jones to Zara will cause the connection requirement and benefits to another requirement to be satisfied for his entitlements in the relevant income years.

~~150.~~153. However, in these circumstances, ~~a~~there is no reimbursement agreement. A genuine interest-free loan from parent to child because of their family relationship and relevant circumstances is explicable as an arrangement entered into in the course of ordinary ~~dealing~~family dealing. While there is strictly no need to consider whether an agreement entered into in the course of ordinary family or commercial dealing meets the tax reduction purpose condition, the mere fact that Zara has a higher income tax rate than Mr Jones does not demonstrate that one or more persons entered into the agreement for a purpose of reducing income tax.

~~151. As also noted in Example 2 of this Ruling, a different outcome may arise if, for example:~~

154. ~~Mr Jones loaned money from trust entitlements to Amy repeatedly~~The following arrangements, which differ from the facts described in this Example, may change the above conclusions, as they raise the question whether the arrangements are meant to achieve a tax reduction objective, rather than any family or commercial objective:

- Arrangements where parents on lower marginal tax rates repeatedly loan trust entitlements to children on higher marginal tax rates in lieu of the trustee distributing to the child directly. For example, if Mr Jones lent money from trust entitlements to Zara repeatedly despite Zara being financially able to support her needs and the parent otherwise has a lower marginal tax rate than the adult child ~~(for~~ because he is retired and in pension phase, or has significant accumulated losses that reduce tax paid on the distributions received from the trust.
- Arrangements where adult children on lower marginal tax rates repeatedly loan trust entitlements to parents on higher marginal tax rates in lieu of the trustee distributing to the parent directly. For example, ~~lower marginal tax rate parents repeatedly loan~~if Zara who is not financially able to support her needs nonetheless loans money from her trust entitlements to ~~higher~~Mr Jones, who is a working professional on the top marginal tax rate ~~children in lieu of the trustee distributing to the child directly), or~~.

- ~~*the situation is reversed, so that Amy, who is less financially advanced, loaned money to Mr Jones, particularly where the adult child has a lower marginal tax rate than the parent.*~~

~~Example 8~~ – share buy-back arrangement

155. *The trustee of the Green Family Trust owns ~~all~~99% of the shares in Green Tree Pty Ltd (Green Tree), a private company. The directors of the trustee company and Green Tree are the same individuals~~.~~.*[125]

156. *Green Tree's balance sheet records are as follows:*

- *$~~2~~100 paid-up share capital*
- *$70,~~000~~700 retained earnings, and*
- *assets and liabilities at their current market value.*

157. *Green Tree maintains a sufficient franking credit balance to fully frank a distribution of all of its retained earnings.*

158. *The trustee and Green Tree agree for the company to purchase ~~its~~99% of the shares for market value consideration of $70,~~002~~099 (share buy-back).*

159. *The trustee is paid the $70,~~002~~099 proceeds from the share buy-back, $70,000 of which is taken to be a fully franked dividend paid by Green Tree for income tax purposes.*[~~67~~ 126] *The franking credit is $30,000.*

160. *The trustee also receives $10,000 interest income in the relevant income year.*

161. *The trustee subsequently varies the trust deed to amend the definition of trust income so the 'income of the trust estate' (trust law income) for the relevant income year will be determined according to ordinary concepts. As the buy-back proceeds are a capital receipt, these are excluded from trust income.*

162. *Accordingly, the income of the trust estate is limited to $10,000 (comprised of the interest income), while the section 95 net income of the trust estate is $110,000*[~~68~~127] *comprised of the interest, the deemed dividend equal to the buy-back proceeds and the gross-up for franking credits.*[~~69~~128]

163. *On 30 June, the trustee resolves to appoint 100% of its $10,000 trust law income to Green Frog Pty Ltd (Green Frog), which is controlled by the same individuals. Green Frog lodges a tax return and includes $110,000 in assessable income.*[~~70~~129]

164. *As the dividend component is fully franked, Green Frog has $3,000 income tax payable*[~~71~~130]*, effectively being the income tax payable on the $10,000 interest income.*[~~72~~131]

165. *The $10,000 is paid to Green Frog, satisfying its trust entitlements. In the subsequent ~~year of~~ income year, the $70,~~002~~099 capital proceeds from the share buy-back are paid to Mr and Mrs Green's personal bank account and accounted for as a tax-free distribution of trust capital.*

166. *An agreement, arrangement or understanding can be inferred from the concerted steps taken by the trustee, the ~~two~~2 companies and the controlling individuals. ~~Absent evidence to the contrary~~On these facts, the arrangement (in existence when the present entitlement of Green Frog is created) is designed to achieve a reduction in tax that would otherwise be payable had Green Tree simply paid a dividend to the trust, which would be distributed to Mr and Mrs Green who received the share buy-back funds.*

~~167.~~ *The $10,000 present entitlement of Green Frog is to a share of the income of the trust for subsection 100A(1) purposes. ~~Coupled with this~~Additionally, the payment of $70,~~002~~099 to*

~~168.~~167. *Mr and Mrs Green would satisfy subsection 100A(7). It is not a requirement of subsection 100A(7) that the payment of money, transfer of property, services provided or other benefits are, or are referrable to, income of the trust. Equally, it is not a requirement of subsection 100A(7) that Green Frog not be paid its entitlement.*

~~169.~~168. *The exception for ordinary family or commercial dealing in subsection 100A(13) is not satisfied. Taken as a whole, the arrangement is not entered into in the course of ordinary family or commercial dealing.*

Example ~~9~~12 – circular flow of funds

170. *The trustee of a discretionary trust owns the shares in a private company. The company is also a beneficiary of the trust and it undertakes no substantial business activity. The directors of the trustee company and the beneficiary company are the same (or related) individuals.*

171. *The trustee makes the company beneficiary presently entitled to all, or some part of, trust income at the end of year 1 and distributes it to the company in year 2 before the company lodges its year 1 income tax return.*

172. *The company includes its share of the trust's net income in its assessable income for year 1 and pays tax at the corporate rate.*

173. *The company pays a fully franked dividend to the trustee in year 2, sourced from the trust distribution, and the dividend forms part of the trust income and net income in year 2.*

174. *The trustee makes the company presently entitled to all, or some part of, the trust income at the end of year 2 (possibly including the franked distribution~~).~~).[132] The arrangement is repeated.*

175. *There is a benefit to the trustee (in that capacity). The agreement provides for the payment of income from the trustee to the company on the understanding (inferred from the repetition in each income year and their common control) that the company would pay a dividend to the trustee of a corresponding amount (less the tax paid). For these reasons, the connection and benefits to another requirements are satisfied.*

176. *~~Absent evidence to the contrary~~On these facts, the concerted steps taken by the trustee and company indicate contrivance. The arrangement appears to be designed to achieve a reduction in tax that would otherwise be payable had the trustee simply accumulated the income. The arrangement is unlikely to be considered to have been entered into in the course of ordinary dealing~~. and is likely to meet the tax reduction purpose requirement. The ownership structure and, particularly, the perpetual circulation of funds~~,~~ do not appear to serve ordinary commercial purposes.*

177. *Diagram ~~3~~2 of this Ruling illustrates the circumstances in this example.*

Changes Made From PCG 2022/D1 to PCG 2022/2

White Zone

The White Zone has been retained by the Commissioner. The Commissioner has made only one alteration. Whereas in the draft PCG, the Commissioner stated that arrangements made before 1 July 2014 will not be reviewed unless the trust and beneficiary tax returns that were required to be lodged for those years were not lodged before 1 July 2017, this ground for reviewing White Zone arrangements has been removed.[136] The White Zone has, therefore, slightly expanded.

Green Zone – Scenario One

This scenario has been expanded and now includes situations where the beneficiary makes personal contributions to a superannuation fund or makes a donation to a deductible gift recipient.[137]

Green Zone- Scenario Two

This scenario is new. On the draft PCG, Scenario Two simply referred to examples within TR 2022/D1 which fell within the 'ordinary dealing' exception.[138] This new scenario involves a beneficiary being made presently entitled to income and they receive the income within two years of becoming entitled, the beneficiary uses the income and none of the exclusions in [32] of the final PCG apply.[139] A beneficiary receiving their entitlement includes situations where the entitlement is applied on their behalf, is used by the beneficiary in ordinary ways or, in the case of a trustee or company beneficiary, makes a distribution to beneficiaries or members.[140] However, if the beneficiary uses the entitlement for a dubious investment or other transaction, the beneficiary will not be considered as having used the entitlement.[141]

[136]PCG 2022/2 at [16] CF D[13]
[137] PCG 2022/2 at [20] CF D [17]
[138] PCG 2022/D1 at [19]
[139]PCG 2022/2 at [22]
[140] PCG 2022/2 at [23]
[141] PCG 2022/2 at [23]

Green Zone- Scenario Three A and B

Scenario Three of the draft PCG has been reformatted into two scenarios, with one dealing with individual beneficiaries and one dealing with company or trust beneficiaries.
With respect to this scenario, there has been several substantial alterations made to concepts used. First, there is no 'trustee retention of funds' if the retention ends two years after the beneficiary was made presently entitled.[142] Second, the 'use of funds condition' has been replaced by the 'trustee working capital distinction'.[143] The conditions substantially mirror each other, save for the condition being satisfied if the trustee services a debt in relation to trust assets.[144] Additionally, on the draft PCG, the condition was not satisfied if any 'associate of the trust benefits'.[145] This phrase has effectively been replaced by 'persons other than the beneficiary' other than their spouse or dependents.[146]
Moreover, a definition of a 'loan of commercial terms' has been inserted,[147] which is relevant to Scenario Three B. It requires the loan to have a rate of interest equal to or greater than the benchmark in Division 7A, the loan to not exceed seven years and the loan repayments to be no more favourable to the borrower than provided in the formulate of subsection 109E. A definition of 'same family group' has also been added,[148] which is also only relevant to Scenario Three B.

Three A

Save for the above changes to concepts employed, this scenario is substantially similar to the draft Scenario Three relating to individual beneficiaries.

Three B

For the case of beneficiaries who are a trust or company, there have been several alterations in addition the changes of concepts used. For this scenario to now apply: (b) the beneficiary must not be an exempt entity, (c) the beneficiary must be a member of the same family group of the trustee who made the FTE and (f) the terms on which the entailment is made available for trustee retention of funds is by way of loan on commercial terms.[149] These amendments limit the scope of this scenario.

Blue Zone and Exclusion of Green Zone

The Blue Zone, which acted as a "catch all zone", has been removed. In its place, the Commissioner has outlined arrangements that do not fall into the Green Zone.[150] This paragraph also appeared in the draft PCG, but several substantial amendments have been made. Subparagraph (d) has been amended such that arrangements involving the trustee exercising a power or the deed being amended such that the beneficiary's entitlement is less than their share of net income, *franked dividends of the*

[142] PCG 2022/2 at [25]
[143]PCG 2022/2 at [25(c)]
[144] PCG 2022/2 at [25C ii]
[145] PCG 2022/D1 at [21C]
[146]PCG 2022/D1 at [25]
[147]PCG 2022/2 at [25(e)]
[148]PCG 2022/2 at [25]
[149]PCG 2022/2 at [28]
[150] PCG 2022/2 at [32]

trust and the trust capital gains are now excluded from the green zone.[151] Moreover, subparagraphs (f) to (k) have been added, such that the exclusion from the green zone is expanded. Exclusions (f) to (j) deal with non-natural person beneficiaries (companies and trusts), while (i) to (k) have a more general application. The new exclusions are listed below:

- the beneficiary is a loss company or loss trust[14] that uses its trust entitlement to fund a distribution to its members and that distribution compromises the ability of the beneficiary to repay its existing or future liabilities
- the beneficiary is a private company that uses its trust entitlement to fund a distribution that is made directly or indirectly to a non-resident
- the beneficiary is a private company or trust that uses its trust entitlement to fund a distribution that is made directly or indirectly to the trustee that made the beneficiary presently entitled to income
- the trustee has not notified the beneficiary of their entitlement to trust income by the earlier of the trustee's due date and actual date of lodgment
- where the beneficiary that is presently entitled to trust income in a year is required to lodge a tax return for that year, either the
  - beneficiary has not lodged, or
  - the beneficiary has understated or omitted in that tax return their share of the trust net income, trust capital gains or franked dividends received from the trust
- the beneficiary uses the trust entitlement to pay excessive consideration where the parties are not dealing at arm's length.

Red Zone

In the draft PCG, the Commissioner provided a general description of 'red zone' arrangements.[152] This statement has been removed. The Commissioner now states that if the arrangement fits within the Red Zone (presumably referring to Red Zone Scenarios), then it will attract ATO attention as a matter of priority.[153]

Red Zone Scenario One

The Commissioner has made two amendments to this scenario. First, the situation of funs being made available to the parent or other caregiver of the beneficiary by way of loan or gift after an adult beneficiary has been made presently entitled is now no longer in this zone.[154] Second, the situation

[151]PCG 2022/2 at [32d]
[152]PCG 2022/D1 at [29]
[153] PCG 2022/2 at [33]
[154] PCG 2022/2 at [34]. Compare PCG 2022/D1 at [30]

which applied to non-resident beneficiaries now only applies to non-resident beneficiaries who are a relative of the resident controller of the trust.[155] These two amendments have therefore condensed this Scenario.

Red Zone Scenario Two

There have been three substantial amendments made to this Scenario. This Scenario exists if certain features are all present. Two of the amendments relate to certain features. Concerning (a), the shares of the private company that the trustee controls no longer need to belong to a company that is a beneficiary under the trust.[156] Moreover, the requirement that the 'trustee resolves to make all the company presently entitled to all, or part of, trust income at the end of year 1' has been removed.[157] These two amendments expand this scenario. However, the Commissioner has added that 'an arrangement where a trust receives a dividend that is not sourced from income of that trust, is outside this scenario'.[158]

Red Zone Scenario Three

The Commissioner has made only one significant amendment to this scenario. It now only applies to a trustee of a 'closely held trust', which takes its meaning from section 102UC.[159]

Red Zone Scenario Four

The Commissioner has made an amendment to a necessary condition for this scenario to apply. On the draft PCG, this scenario may have applied if the share of the trust net come included in the beneficiary's assessable income is significantly more than the beneficiaries entitlement to income from the trust.[160] This condition has been changed such that the beneficiary's share of the trust net income included in their assessable income, in addition to their share of franked distributions and capital gains of the trust, must now be significantly more than the beneficiary's entitlement.[161] This alteration therefore expands the operation of this scenario.

Moreover, the Commissioner has changed the wording of another necessary requirement for this scenario. Instead of requiring the difference between the benefits received and the entitlements provided to be the result of 'contrivance',[162] it now must be the result of 'deliberate actions that affect the computation of trust distributable income and that are directed at causing there to be a difference. Examples of actions include amending or varying a trust deed, a trustee determining what is income and capital of the trust, or choosing to undertake a transaction or arrangement in order to create a difference'.[163]

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[155] Ibid
[156] PCG 2022/2 at [36]. Compare PCG 2022/D1 at [32]
[157] Ibid
[158] PCG 2022/2 at [37]
[159]PCG 2022/2 at [41]
[160] PCG 2022/D1 at [39]
[161] PCG 2022/2 at [43]
[162] PCG 2022/D1 at [39]
[163] PCG 2022/2 at [43 a]

Red Zone Scenario Five

This scenario has been altered in four significant respects. First, for this scenario to now apply, the presently entitled beneficiary (who has losses) is outside the 'family group' as defined for Green Zone Scenario Three.[164] Second, a green zone scenario must not apply for this scenario to be apply.[165] These two additional requirements substitute two other requirements which have been removed by the Commissioner. Specifically, the third alteration is that it is no longer a requirement that a reasonable person would conclude the beneficiary was made entitled so losses and deductions could be utilized.[166] Finally, it is no longer a requirement that the 'economic benefit associated with that trust net income' is utilized by someone other than the beneficiary.[167]

Record Keeping

A new section relating to record keeping has been added.[168] It reads:

> 49. You should prepare and keep good records that explain the transactions that have happened. Having a clear understanding as to why a beneficiary has chosen to deal with their entitlement in the way they have and knowledge of the relevant parties to the transaction or arrangement will help support your position. It will also assist in the timely resolution of any compliance activity we undertake.
>
> 50. While each arrangement depends on its facts, the following documents and records are important and should be kept wherever possible:
>
> *(f)* the trust deed (including amendments), trustee resolutions and contact details of the trustee and former trustees
>
> *(g)* notes, contemporaneous documents and records of discussions or meetings explaining the transactions that have happened or calculations that have been made
>
> *(h)* details of how the beneficiary was notified of their present entitlement to trust income
>
> *(i)* details of how the present entitlement to trust income was satisfied and, where practical, used by the beneficiary
>
> *(j)* details of how the trustee utilised the underlying funds; for example, to satisfy the trustee retention of funds or the trustee working capital condition referred to in paragraph 25 of this Guideline
>
> *(k)* copies of loan agreements and records showing how the loan repayments were satisfied from time to time.

[164] PCG 2022/2 at [46(c)]
[165] PCG 2022/2 at [46b]
[166] PCG 2022/D1 at [43] v PCG 2022/2 at [45-6]
[167] Ibid
[168] PCG 2022/2 at [49]

51. We acknowledge that family arrangements are typically conducted with a greater level of informality than dealings between unrelated parties. Nonetheless, to the extent possible, the trustee or their registered tax agent should maintain contemporaneous records that are ordinarily created which demonstrate the objectives an arrangement was intended to achieve and how it would achieve them. For example, this could be in the form of a file note of a meeting between the trustee and registered tax agent.

52. The maintenance of contemporaneous records by the trustee is part of good governance arrangements for managing the trust's affairs and dealing with the ATO. Notwithstanding that an arrangement is fully documented, section 100A may still apply, particularly where the arrangement is contrived or artificial, is overly complex or has tax-driven features so that the dealings cannot be explained by ordinary family or commercial purposes.[20]

Application

The Commissioner has added that:

55. In addition, we will not dedicate compliance resources to consider the application of section 100A to an entitlement arising before 1 July 2022 where you demonstrate to us that:

- your arrangement satisfies the white zone, or
- you have taken reasonable care in applying the administrative position in *Trust taxation – reimbursement agreement* to determine that section 100A does not apply to that arrangement.

Examples

New Examples

The Commissioner has added seven **new** examples to the final PCG. These are listed below.

Example 2 – arrangement continues before and after 1 July 2014

60. Zed Co is a resident company that acts as the trustee of Zed Family Trust

61. Mr Zed, a resident individual, is the controller of Zed Family Trust given that he is both the appointor of Zed Family Trust and he is the sole director of Zed Co.

62. Between the 2012–13 and 2019–20 income years, the trustee of Zed Family Trust has been paid $300,000 franked dividends each year. In each of these income years, the dividend income was appointed by Zed Co as trustee to Ms Lee, a non-resident beneficiary who is the sister-in-law of Mr Zed.

63. Ms Lee's entitlements to the dividend income remains unpaid while Zed Co has permitted Mr Zed to use the corresponding dividend receipts of the trust to both meet his personal expenses and

to repay debt that he owes to other private companies that he controls. The arrangement is not within the green zone.

64. The arrangement is not in the white zone as the arrangement commenced before 1 July 2014 and continued after that date. That is, the arrangement in respect of Ms Lee's present entitlement to trust income for 2012–13 and 2013–14 income years appears to have continued into the 2014–15 and following income years.

Example 3 – taxpayer under audit for fraud or evasion

65. The ATO is undertaking an audit of Cash Discount Trust for the period 1 July 2010 to 30 June 2014.

66. The focus of the audit is the understatement of the assessable income of Cash Discount Trust, with the trustee of Cash Discount Trust having omitted significant cash receipts from its reported assessable income as a result of evasion.

~~61.~~67. During the course of the audit, the ATO ascertains that the beneficiaries used their trust entitlements to make gifts in each year under audit. The recipient of the gifts is the beneficiaries' mother who controls Cash Discount Trust. The arrangement satisfies the criteria of Red zone: scenario 1.

68. The arrangement is not in the white zone as we are otherwise considering the income tax affairs of Cash Discount Trust in connection with evasion that resulted in understating of net income in the trust tax returns.

Example 5 – time lag between a beneficiary becoming presently entitled and that entitlement being satisfied

76. Tortoise Trust holds a number of investment assets and is controlled by Mr Hare Senior.

77. *On 30 June 2023, the trustee of Tortoise Trust makes a determination to appoint 100% of the trust income to Mr Hare Junior.*

78. *On 15 March 2024, the trustee of Tortoise Trust finalises its accounts for* the 2022–23 income year. In doing so, the trustee ascertains that the amount of trust income to which Mr Hare Junior is presently entitled for the 2022–23 income year

is $120,000.

79. *On 18 March 2024, Mr Hare Junior is informed by the trustee of Tortoise Trust as to the amount of his trust entitlement.*

80. *On 31 March 2024, Mr Hare Junior lodges his 2022–23 tax return and includes his trust entitlement of $120,000 from Tortoise Trust in his assessable income. That same day, he calls for a $30,000 part-payment of his trust entitlement, which is then paid by Tortoise Trust so that Mr Hare Junior can pay his tax liability.*

81. *By 30 April 2025 (which is within 2 years of the entitlement being conferred), Mr Hare Junior has received the $90,000 balance of the $120,000 from the trustee of* Tortoise Trust in satisfaction of Mr Hare Junior's trust entitlement for the 2022–23 income year.

82. *Mr Hare Junior uses the funds representing his trust entitlement to invest in a new florist business he has commenced as a sole trader.*

83. *Prior to satisfying Mr Hare Junior's trust entitlement, the $120,000 income receipts had been retained by the trustee of Tortoise Trust as part of the investment portfolio maintained by the trustee.*

84. *We would not dedicate compliance resources to this arrangement as it meets the conditions in Green zone: scenario 2 of this Guideline and the arrangement does not have any features that excludes it from the green zone under paragraph 32 of this Guideline.*

Example 6 – time lag between a loss trustee beneficiary becoming presently entitled and that entitlement being satisfied

85. *Doctor Evergreen controls and is a beneficiary of both Top Trust and Bottom Trust.*

86. *Doctor Evergreen is the specified individual in the FTEs made by each of the trustees of Top Trust and Bottom Trust.*

87. *Top Trust undertakes investment activities.*

88. *Bottom Trust undertakes a business that has prior year tax losses, with the trustee of Bottom Trust indebted to other parties – the debts arose in the course of carrying on the business.*

89. For the 2022–23 income year, the trustee of Top Trust appoints all the income of that trust to Bottom Trust.

90. On 30 September 2023, the trustee of Top Trust finalises its accounts for the 2022–23 income year and ascertains that the unpaid trust entitlement owing to the trustee of Bottom Trust is $250,000 for that year. The trustee of Bottom Trust is informed of the amount of its trust entitlement on the same day.

91. On 31 October 2023, the trustee lodges the trust tax return for Bottom Trust and includes the $250,000 as assessable income. Bottom Trust has nil taxable income as its deductions exceed its assessable income.

92. On 1 December 2023, the trustee of Top Trust receives cash in respect of

~~76.~~93. a 6-month interest-bearing term deposit that has matured. $250,000 is transferred by the trustee of Top Trust into the bank account of Bottom Trust in satisfaction of the entitlement (which is within 2 years of when the beneficiary was made presently entitled).

94. The trustee of Bottom Trust uses the $250,000 in first repaying debts incurred in carrying on the business it undertakes and uses the balance to make a capital distribution to the beneficiaries.

95. We would not dedicate compliance resources to this arrangement as it meets the conditions in Green zone: scenario 2 of this Guideline and the arrangement does not have any features that exclude it from the green zone under paragraph 32 of this Guideline.

Example 9 – distributions involving a trustee undertaking a farming business

110. McDonald Family Trust is a discretionary trust controlled by Old McDonald

111. The trustee of McDonald Family Trust carries on a farming business.

112. The management of the farming business is undertaken by Old McDonald and his daughter Young McDonald.

113. It is intended that Young McDonald will take control of McDonald Family Trust when her father passes away.

114. During the 2022–23 income year, Old McDonald and Young McDonald each draw on funds from the trust bank account to meet their private outgoings.

115. On 30 June 2023, the trustee of McDonald Family Trust makes Old McDonald and Young McDonald each presently entitled to a 50% share of the income of the trust for that year.

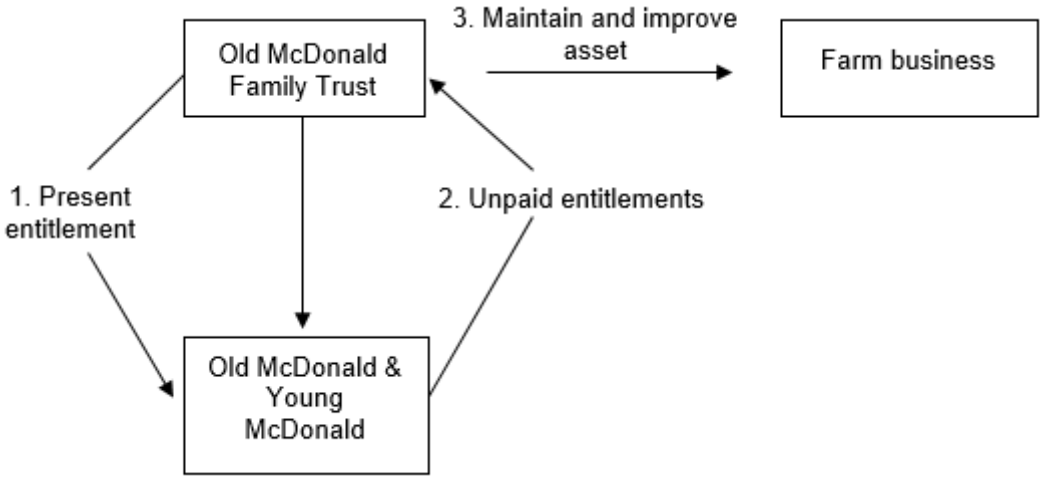
116. The entitlements of both Old McDonald and Young McDonald are first set-off against the amounts each drew throughout the year with the balance remaining unpaid. The funds representing the unpaid entitlements are retained by the trustee and used to maintain and improve the farm.

117. It is intended that Old McDonald and Young McDonald will each call on so much of their

trust entitlements to meet future private outgoings, with funds representing any unpaid entitlements used by the trustee in the farming business and expected to benefit them through future profitability of the enhanced business.

118. Diagram 7 of this Guideline illustrates the facts in this Example.

Diagram 7



Example 10 – testamentary trust

119. A trust established under a will provides that Gemini, the daughter of the deceased, is entitled each year to all of the trust income and to receive the trust corpus once she reaches 30 years of age or (if she dies before attaining the age of 30) to her estate.

120. Gemini is 18 years of age at the time the trust is created.

121. Gemini's entitlement to trust income is not immediately satisfied in full each year. Instead, the trustee pays Gemini a weekly allowance of $500 with the balance of funds representing Gemini's income entitlement retained by the trustee.

122. Gemini uses her allowance to pay her personal living expenses. This includes paying $250 per week to her aunt for food and board.

123. The funds representing so much of Gemini's income entitlement that is retained by the trustee is invested in income-producing assets for Gemini's direct future benefit.

124. The arrangement does not have any features that excludes it from the green zone under paragraph 32 of this Guideline. We would not dedicate compliance resources to this arrangement as it meets the conditions in Green zone: scenario 3A of this Guideline.

125. We would not dedicate compliance resources to this arrangement as it meets the conditions in Green zone: scenario 3A of this Guideline and the arrangement does not have any features described in paragraph 32 of this Guideline.

Example 13 – distributions to a company beneficiary with tax losses

140. Ms Willow is the appointor of Black Trust and her spouse controls Red Pty Ltd.

141. Noir Co is the trustee of Black Trust (all references to Noir Co are in that capacity) and is controlled by Ms Willow.

142. Black Trust carries on a manufacturing business.

143. Red Pty Ltd has prior year tax losses as a result of operating a business venture that continues to operate and has a nil distributable surplus.

144. On 30 June 2023, Noir Co makes a determination to appoint 100% of the trust income to Red Pty Ltd, being $300,000.

145. Red Pty Ltd includes $300,000 in its assessable income, being the net income of Black Trust. After deducting tax losses of $300,000, the taxable income of Red Pty Ltd is nil.

~~140.~~146. The funds representing Red Pty Ltd's trust entitlement were retained by Noir Co for the purpose of funding the working capital for the manufacturing business. Noir Co and Red Pty Ltd subsequently enter into a loan agreement on commercial terms that comply with section 109N.

Substantially Altered Examples

In addition to adding seven new examples, the Commissioner has made amendments to the other examples. Comparison of examples One and Four in the final PCG revealed no substantial changes. As can be seen from the below, the other examples have not substantially changed. Besides changing the order of the examples, dates, names of relevant actors and adding several statements of further guidance, the examples remain substantially similar.

Example ~~2~~7 - use of funds condition and part-~~-~~payment of unpaid present entitlement

~~53. *Greater*~~95. *Homewares Trust is a discretionary trust controlled by Ms Retail. The trustee of Homewares Trust is Homewares Pty Ltd (and all references to Homewares Pty Ltd are in that capacity). The director and shareholder of Homewares Pty Ltd is Ms Retail. The beneficiaries of Homewares Trust include Ms Retail, her spouse Mr Retail and members of their extended family.*

96. *Homewares Trust carries on a retail business selling homewares.*

~~54~~97. *On 30 June 2023, ~~Greater~~Homewares Pty Ltd resolves to appoint 50% of the trust income to Ms ~~Great~~Retail and to appoint the remaining 50% to Mr ~~Better~~Retail.*

~~55~~98. *Mr ~~Better~~Retail and Ms ~~Great~~Retail use some of their trust entitlements for the 2022-23 income year to meet their personal expenses during the 2023-24 income year. The balance of their entitlements remain unpaid and are used to supplement the working capital of the business carried on by ~~Greater~~Homewares Trust.*

~~56~~99. *Diagram 6 of this Guideline illustrates the ~~circumstances~~facts in this ~~example~~Example.*

~~57~~100. *Ms ~~Great~~Retail and Mr ~~Better~~Retail expect to be paid the remainder of their entitlements but they have no firm plans on the timing of payment. They allow the trustee to use those funds in the homewares business ~~to grow their family's wealth~~for working capital purposes.*

~~58~~101. *Funds representing Ms ~~Great~~Retail and Mr ~~Better's~~Retail's trust entitlements have been either paid to them or retained by the trustee for working capital of the business. ~~The arrangement does not have any features described in the red zone. We would not dedicate compliance resources to this arrangement as it meets the conditions in green zone scenario 3 of this Guideline.~~*

102. *We would not dedicate compliance resources to this arrangement as it meets the conditions in Green zone: scenario 3A of this Guideline and the arrangement does not have any features that excludes it from the green zone described in paragraph 32 of this Guideline.*

Example ~~6~~8 - distributions from a family business

~~79. Greater~~103. Newsagent Trust is a discretionary trust controlled by Ms Magazine. The trustee of Newsagent Trust is Newsagent Pty Ltd. Ms Magazine is the director and shareholder of Newsagent Pty Ltd. The beneficiaries of Newsagent Trust include Ms Magazine, her spouse Mr Magazine and members of their extended family.

104. *Newsagent Trust carries on a business as a newsagent.*

~~80~~105. *Danny is aged 18 and is the daughter of Ms ~~Great~~Magazine.*

~~81~~106. *During the 2022-23 income year, ~~Greater~~Newsagent Trust derives income of $150,000 (the trust's net income is also $150,000). On 30 June 2023, the trustee of ~~Greater~~Newsagent Trust makes a determination to appoint $18,000 to Danny and 50% of the remainder to each of Ms ~~Great~~Magazine and Mr ~~Better~~Magazine.*

~~82~~107. *Funds representing Danny's entitlement are paid ~~to~~into her bank account and she subsequently uses them to pay her university fees.*

~~83~~108. *Ms ~~Great~~Magazine and Mr ~~Better~~Magazine do not call for their entitlements to be satisfied~~,~~ and funds representing each of their entitlements are retained by the trustee and used in the working capital of the ~~newsagency~~newsagent business.*

~~84~~109. *We would not dedicate compliance resources to the arrangement in this ~~example~~Example, on the basis that:*

- *(a)it meets the conditions in ~~green~~Green zone: scenario ~~3~~3A of this Guideline in relation to the unpaid entitlements of Ms ~~Great~~Magazine and Mr ~~Better, and~~Magazine*
- *(b)Danny enjoys the benefit of her trust entitlement ~~to trust income.~~, and*
- *(c) none of the features described in paragraph 32 of this Guideline are present.*

Example ~~3~~11 - use of funds condition and unpaid present entitlement

~~59. *Greater*~~126. *Investment Trust is a discretionary trust controlled by Ms Alia. The trustee of Investment Trust is Investment Pty Ltd. The beneficiaries of Investment Trust include Ms Alia, her spouse Mr Aarif, their extended family and Beneficiary Pty Ltd. Ms Alia is the director and shareholder of Investment Pty Ltd and Beneficiary Pty Ltd.*

127. *Investment Trust holds a number of investment assets including shares in listed companies and commercial property from which it derives dividend and rental income respectively.*

~~60. *On 30 June 2023, Greater*~~128. *In the 2022-23 income year, Investment Trust derives income comprised of dividends from listed companies. The income is used to purchase further shares pursuant to dividend reinvestment plans.*

~~61~~129. *On 30 June 2023, ~~Greater~~Investment Pty Ltd resolves to appoint ~~100~~60% of the trust income to ~~Good~~Beneficiary Pty Ltd~~.~~, 20% to Ms Alia and 20% to Mr Iarif. At the time of appointment, there is an understanding between the parties that ~~Good Pty Ltd~~ each of the beneficiaries will use ~~its~~their entitlement to lend money back to ~~the Greater~~Investment Trust. The unpaid entitlements are used by Investment Trust to purchase listed shares.*

~~62~~130. *The arrangement between Investment Trust and Beneficiary Pty Ltd amounts to financial accommodation.*[21] *Ms Alia and Mr Aarif expect to be paid their entitlements, but they have no firm plans on the timing of payment.*

131. *During the 2023-24 income year, ~~Greater~~Investment Pty Ltd enters into an arrangement with ~~Good~~Beneficiary Pty Ltd ~~that complies with the requirements in section 109N~~ to borrow an amount equal to the funds that ~~Good~~Beneficiary Pty Ltd is entitled to receive from the ~~Greater Trust.~~Investment Trust on commercial terms.*[22]

~~63. *Diagram 7 of this Guideline illustrates the circumstances in this example.*~~

~~64~~132. During the 2023-24 income year and subsequent income years, ~~*Greater*~~*Investment* Pty Ltd uses trust receipts to meet its *principal and interest* obligations under the loan agreement.

~~65~~133. Funds representing ~~*Good Pty Ltd's*~~*the beneficiaries'* present ~~*entitlement*~~*entitlements* that have been retained satisfy the use of funds condition and a written loan agreement has been entered into *between Investment Pty Ltd and Beneficiary Pty Ltd* on *commercial* terms ~~*that satisfy section 109N. The arrangement does not have any features described in the red zone.*~~. We would not dedicate compliance resources to this arrangement as it meets the conditions in *Green zone: scenarios 3A and*

3B of this Guideline and does not have any features that exclude it from the green zone ~~*scenario 3*~~*under paragraph 32* of this Guideline.

Example ~~4~~12 - trustee retains funds and services loan agreement

~~66. *Greater*~~134. *Flower Trust is a discretionary trust controlled by Ms Rose. The trustee of Flower Trust is Flower Pty Ltd. The beneficiaries of Flower Trust include Ms Rose, her spouse Mr Rose, their extended family and Plant Pty Ltd. Ms Rose is the director and shareholder of Flower Pty Ltd and Plant Pty Ltd.*

135. *Flower Trust carries on a business as a florist.*

~~67~~136. *During the 2022-23 income year, ~~Greater~~Flower Trust derives income of $100,000 (the trust's net income is also $100,000).*

~~68~~137. *On 30 June 2023, ~~Greater~~Flower Pty Ltd resolves to make ~~Good~~Plant Pty Ltd presently entitled to all of the income of ~~Greater~~Flower Trust.*

~~69. *Greater*~~138. *Flower Trust partially satisfies the entitlement of ~~Good~~Plant Pty Ltd to enable it to pay its tax on the $100,000. The balance of the entitlement remains unpaid and is used by the trustee of ~~Greater~~Flower Trust in funding the working capital of the business. The arrangement amounts to financial accommodation[15][23] and ~~is, therefore, a loan for the purposes of Division 7A. Greater~~Flower Pty Ltd and ~~Good~~Plant Pty Ltd put in place a loan agreement on commercial terms ~~which~~that comply with section 109N.*

~~70~~139. *Diagram 8 of this Guideline illustrates the ~~circumstances~~facts in this ~~example~~Example.*

~~71. *Greater*~~140. *Flower Pty Ltd uses the receipts from the trust's business to make interest and principal payments to ~~Good~~Plant Pty Ltd ~~in fulfilling its obligations in complying~~to comply with ~~Division 7A~~the terms of the loan agreement.*

~~72~~141. *Funds representing ~~Good~~Plant Pty Ltd's present entitlement have been retained by the trustee for working capital of the business and a written loan agreement has been entered into on commercial terms ~~that satisfy section 109N.~~ .*

142. *The arrangement does not have any features described in the red zone. We would not dedicate compliance resources to this arrangement as it meets the conditions in ~~green~~Green zone: scenario ~~3~~3B of this Guideline.*

Example ~~7~~14 - amounts provided to the parent in respect of expenses incurred before the beneficiary turns 18 years of age

~~85. *Brown*~~153. *Patel Trust's beneficiaries include the members of the ~~Brown~~Patel Family. ~~Brown~~Patel Co is the trustee of ~~Brown~~Patel Trust~~,~~ and ~~Bronwyn Brown~~Lila Patel is the sole shareholder and director of the trustee.*

~~86. *Bronwyn*~~154. *Lila is the parent of ~~three~~3 adult children~~; Sandra~~ - Sima (aged 26), ~~Simon~~Kumar (aged 21) and ~~Sam~~Jai (aged 19).*

~~87~~155. *During the 2022-23 income year, ~~Sandra~~Sima is self-employed and has a taxable income of $90,000. ~~Simon~~Kumar and ~~Sam~~Jai study full~~-~~ time and derive no income during the income year. ~~Bronwyn's~~Lila's children live at home with her at all times throughout the income year.*

~~88~~156. *During the 2022-23 income year, ~~Brown~~Patel Trust derives $240,000 in income (the trust's net income is also $240,000). Throughout that year, ~~Brown~~Patel Co makes regular payments totalling $240,000 into ~~Bronwyn's~~Lila's bank account. Those payments are recorded as a 'beneficiary loan' in the accounts of ~~Brown~~Patel Trust. ~~Bronwyn~~Lila uses these amounts throughout the year to meet her personal living expenses and those of the household.*

~~89~~157. *On 30 June 2023, ~~Brown~~Patel Co resolves to make ~~Simon~~Kumar and ~~Sam~~Jai each presently entitled to $120,000 of the ~~Brown~~Patel Trust income.*

~~90. *Brown*~~158. *Patel Co applies their entitlements against the beneficiary loan owed by ~~Bronwyn~~Lila. The entitlements of ~~Simon~~Kumar and ~~Sam~~Jai are each recorded as having been fully paid in the accounts of ~~Brown~~Patel Trust. ~~Bronwyn~~Lila assists in the preparation of ~~Simon~~Kumar and ~~Sam's~~Jai's tax returns and pays the tax liability arising in relation to their entitlements from her personal funds.*

~~91~~159. *The entitlements of ~~Simon~~Kumar and ~~Sam~~Jai are applied in this manner because they each purportedly have an outstanding debt owed to ~~Bronwyn~~Lila in respect of education expenses and their share of the ~~Brown~~Patel household expenses that ~~Bronwyn~~Lila paid before they each turned 18.*

~~92~~160. *Diagram 10 of this Guideline illustrates the ~~circumstances~~facts in this ~~example~~Example.*

~~93~~161. *On the basis that this arrangement meets the conditions in ~~red~~Red zone: scenario 1 of this Guideline, we would apply compliance resources to consider the application of section 100A in these circumstances.*

Example ~~8~~15 - non-resident beneficiary makes a loan or gift to ~~an associate~~another party

~~94. *Orange*~~162. *Oberon Trust is a discretionary trust with beneficiaries including the members of the ~~Orange~~Oberon Family. ~~Orange~~Oberon Co is the trustee of ~~Orange~~Oberon Trust, and ~~Thomas Orange~~Titan Oberon is the sole shareholder and director of the trustee. Both Oberon Co and Titan Oberon are residents of Australia.*

~~95. Orange~~163. Oberon Trust has made ~~a family trust election and Thomas Orange~~an FTE and Titan Oberon is the specified individual in that election.

~~96. Thomas~~164. Titan is aged 44 and his parents are Sylvia (aged 66) and Sylvester (aged 67). His parents reside outside of Australia and are non-residents for tax purposes.

~~97~~165. During the 2022-23 income year, ~~Orange~~Oberon Trust derives $400,000 income that is comprised of fully franked dividends. The dividends are paid directly into ~~Thomas'~~Titan's bank account. ~~Thomas~~Titan uses these amounts to meet his personal expenses and mortgage repayments. The trust income ~~paid into Thomas' bank account~~ is recorded as a 'beneficiary loan' in the accounts of ~~Orange~~Oberon Trust.

~~98~~166. On 30 June 2023, ~~Orange~~Oberon Co exercises its power to appoint income to make Sylvia and Sylvester each entitled to $200,000 of ~~Orange~~Oberon Trust's income. ~~Orange~~Oberon Trust is not required to pay or withhold tax in respect of the distribution to Sylvia and Sylvester.

~~99~~167. At the time income is appointed to Sylvia and Sylvester, they have agreed to use their entitlements to lend $400,000 to ~~Thomas~~Titan on interest-free at-call terms.

~~100~~168. In the accounts of ~~Orange~~Oberon Trust, ~~Orange~~Oberon Co records that Sylvia's and Sylvester's entitlements are fully satisfied in being applied to repay the $400,000 beneficiary loan owed by ~~Thomas~~Titan.

~~101~~169. Diagram 11 of this Guideline illustrates the ~~circumstances~~facts in this ~~example~~Example.

~~102~~170. On the basis that this arrangement meets the conditions in ~~red~~Red zone: scenario 1 of this Guideline, we would apply compliance resources to consider the application of section 100A in these circumstances.

Example ~~9~~16 - the presently entitled beneficiary is issued units by the trustee (or related trust) and the amount owed for the units is set-off against the beneficiary's entitlement

~~103~~171. Johnson Trust is a hybrid trust that carries on a profitable business providing building repair services to the public. Johnson Co is the corporate trustee of Johnson Trust and Lauren Johnson is its sole shareholder and director.

~~104~~172. Hammer Co is a private company with Lauren Johnson as the sole director and shareholder.

~~105~~173. As a hybrid trust, Johnson Trust has ~~two~~2 classes of beneficiaries. One class is comprised of the unit holders and the second class are the discretionary ~~objects~~beneficiaries.

~~106~~174. *The terms of the trust deed for Johnson Trust include the following:*

- *(a)On or before 30 June of a relevant income year, the trustee has the power to appoint income of that year to one or more of the discretionary ~~objects~~beneficiaries.*
- *(b)The unit holders are entitled to so much of the income of the trust for a particular income year that the trustee has not appointed to any discretionary ~~object~~beneficiary with a unitholder's entitlement being proportional to the number of units they hold.*
- *(c)Upon vesting of the trust, or earlier where the trustee chooses, the unit holders are entitled to capital of the trust equal to the paid up value of the units.*
- *(d)The trustee has the discretion to pay the balance of the capital of the trust to one or more discretionary ~~objects~~beneficiaries of the trust.*

~~107~~175. *During the 2022-23 income year, Johnson Trust derives income of $500,000 (the trust's net income is also $500,000) from its business activities. The trust reinvests the net income into its business activities as working capital.*

~~108~~176. *On 30 June 2023, Johnson Trust resolves to distribute 100% of the trust income to Hammer Co which is ~~a beneficiary~~ within the class of discretionary ~~objects~~beneficiaries.*

~~109~~177. *On 1 October 2023, the trustee of Johnson Trust exercises its power to issue new units to Hammer Co for $500,000. The accounts of Hammer Co and Johnson Trust recognise a set-off of Hammer Co's $500,000 ~~unpaid present entitlement~~UPE against the unit subscription amount. The market value of the units is significantly less than $500,000.*

~~110. *As Johnson Trust and Hammer Co treated Hammer Co's unpaid present entitlement as having been satisfied by the issue of new income units, they also do not recognise any associated Division 7A deemed dividends.*~~

~~111~~178. *Diagram 12 of this Guideline illustrates the ~~circumstances~~facts in this ~~example~~Example.*

~~112~~179. *On the basis that this arrangement meets the conditions in ~~red~~Red zone: scenario 3 of this Guideline, we would apply compliance resources to consider the application of section 100A in these circumstances.*

Example ~~10~~17 - the share of net income included in a beneficiary's assessable income is significantly more than the beneficiary's entitlement

~~113. Prior to~~180. Since before 2023, a private group controlled by Ms Day ~~consists~~has consisted of Operating Trust, Passive Pty Ltd and Holding Trust.

~~114~~181. Holding Trust is a discretionary trust and the shareholder of Passive Pty Ltd. The deed of Holding Trust defines trust income as being equal to the net income of the trust calculated under section 95.

~~115~~182. Passive Pty Ltd receives trust distributions from Operating Trust which represent the annual profits from Operating Trust's business. Passive Pty Ltd has retained profits that reflect distributions from Operating Trust over the past ~~five~~5 years.

~~116~~183. Passive Pty Ltd uses its retained profits to make loans to Ms Day.

~~117~~184. During the 2022-23 income year, the private group undertakes the following steps so that most of the retained profits in Passive Pty Ltd can be distributed to Ms Day:

- *(a) The trust deed of Holding Trust is amended so that proceeds from share buy-backs are capital of the trust.*
- *(b)New Bucket Pty Ltd is created with its shares held by Operating Trust.*
- *(c)Passive Pty Ltd buys back 90% of its shares held by Holding Trust for $2.8 million, which is treated as a franked distribution for tax law purposes.[16][24]*
- *(d)The $2.8 million share buy-back proceeds are a capital receipt of Holding Trust.*
- *(e)Holding Trust has trust income for the year of $1,000.*
- *(f)Holding Trust distributes the $1,000 trust income (which does not include the share buy-back dividend) to New Bucket Pty Ltd.*
- *(g)Holding Trust distributes $2.8 million capital to Ms Day.*

~~118~~185. Operating Trust continues to appoint its trust income to Passive Pty Ltd and there are no other changes to the group structure.

~~119~~186. *The tax outcome regarding the share buy-back is that the assessable income of Holding Trust includes $2.8 million dividends and $1.2 million franking credits. This is included in the assessable income of New Bucket Pty Ltd since it is presently entitled to the entire $1,000 trust income of Holding Trust. ~~The company~~New Bucket Pty Ltd obtains no benefit from the share buy-back.*

~~120~~187. *The economic outcome regarding the share buy-back is that Holding Trust has received $2.8 million which is ultimately distributed as capital to Ms Day.*

~~121~~188. *Diagram 13 of this Guideline illustrates the ~~circumstances~~facts in this ~~example~~Example.*

~~122~~189. *On the basis that this arrangement meets the conditions in ~~red~~Red zone: scenario 4 of this Guideline, we would apply compliance resources to consider the application of section 100A in these circumstances.*

Example ~~11~~18 - the presently entitled beneficiary has losses

~~123~~190. *Rouge Trust is controlled by Mr Rouge and has historically distributed to Mr Rouge and members of his family.*

~~124~~191. *During the ~~2021-22~~2022-23 income year, Mr Rouge meets Ms Loss who has ~~little taxable income and~~ significant tax losses from prior years. They agree that Ms Loss will be made entitled to income of Rouge Trust and that only 10% of her entitlements will ~~remain unpaid~~ever be paid.*

~~125~~192. *As Ms Loss is not part of Mr Rouge's family, the trust deed of Rouge Trust is amended to include Ms Loss as a beneficiary of the trust on 1 June ~~2022~~2023.*

~~126~~193. *On 30 June ~~2022~~2023, Rouge Trust has $500,000 trust income (the trust's net income is also $500,000) to which Ms Loss is made presently entitled.*

~~127~~194. *Ms Loss includes the $500,000 net income of Rouge Trust as assessable income in her tax return for the ~~2021-22~~2022-23 income year and reports taxable income of nil after applying deductions for prior year tax losses.*

~~128.~~195. *Only $50,000 of Ms Loss' entitlement to the $500,000 income of Rouge Trust is ~~unpaid and the money~~paid. The remaining $450,000 is used by the trustee to make loans to Mr Rouge in lieu of the trust distributions that have historically been made to him and his family.*

~~129~~196. *Diagram 14 of this Guideline illustrates the ~~circumstances~~facts in this ~~example~~Example.*

~~130~~197. *On the basis that this arrangement meets the conditions in ~~red~~Red zone: scenario 5 of this Guideline, we would apply compliance resources in these circumstances.*