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Dear Messrs Dearness and Ryan

Draft Taxation Ruling TR 2022/D1 - Income tax: section 100A reimbursement agreements
Draft Practical Compliance Guideline PCG 2022/D1 - section 100A reimbursement agreements – ATO compliance approach

1 The Taxation Committee of the Business Law Section of the Law Council of Australia (the **Committee**) welcomes the opportunity to provide the following comments on draft *Taxation Ruling TR 2022/D1 - Income tax: section 100A reimbursement agreements* (**Draft Ruling**) and draft *Practical Compliance Guideline PCG 2022/D1 - section 100A reimbursement agreements – ATO compliance approach* (**Draft PCG**, and together with the Draft Ruling, the **Draft s 100A Material**).

2 This response intends to promote the view that it is in the interests of both the Australian Taxation Office (**ATO**) and the community to achieve the dual goals of:

(a) assisting the Commissioner in his statutory duty to administer the tax legislation according to law and in a manner that promotes confidence in that administration; and

(b) providing taxpayers, and their advisors, with the necessary, balanced and useful guidance to understand the legislation as it is written, and how the Commissioner intends to administer it.

3 The Committee looks forward to continuing to work with the ATO, and other stakeholders, to pursue guidance material that achieves these two goals.

4 The Committee provides its observations on several specific issues which it considers warrant further consideration in relation to the Commissioner's draft views in the Draft s 100A Material, particularly the Draft Ruling. This is not intended to be a comprehensive response to the Draft s 100A Material but one rather focussed on the important specific issues raised below.

5 As an overarching comment, we note that any ruling, and any practical compliance guideline reliant on that ruling, whose contents align with the operation of Australian laws, relevant court decisions and extrinsic material are more likely to be better understood, accepted and of more assistance than ones that do not. In our view, there are instances in the Draft s 100A Material where that alignment is not apparent and

thus invites opportunities for improvement. We would welcome the opportunity to assist with developing that analysis in finalising the ATO's views in the Draft s 100A Material.

6 The Committee also takes this opportunity to make some observations on *Taxpayer Alert TA 2022/1 – Parents benefitting from trust entitlements of their children over 18 years of age* (**TA 2022/1**). These observations are consistent with the matters raised in relation to the Draft s 100A Material.

7 All legislative references are to the *Income Tax Assessment Act 1936* (Cth), unless stated otherwise.

Executive Summary

8 The Committee notes three challenging aspects (without excluding perceptions of other aspects) of the context in which the consultation material has been developed and released, namely: the amending legislation that produced s 100A was introduced 43 years ago, with apparent acceptance (for decades) by the ATO in reviews and audits of arrangements that it now flags as problematic, and that key aspects of s 100A are "*awkwardly drafted*", as Logan J recognised in *Guardian AIT Pty Ltd (as trustee of Australian Investment Trust) & Anor v FCT*.[1]

9 This submission raises a number of key concerns with the Draft s 100A Material, both in terms of its consistency with established principles of statutory construction and authority, and its usefulness as guidance. In terms of specific feedback, the Committee offers the following observations:

(a) The Draft s 100A Material will benefit from a greater exposition of the legislative history and context of s 100A (see paragraphs 21 to 28). The ATO can constructively use the signposts in the extrinsic material to guide its administration. Those signposts should be embraced, not ignored.

(b) A clear meaning of the critical phrase "*ordinary family or commercial dealing*" is not apparent on a plain reading of the text so that, under conventional and accepted principles of statutory construction, the statutory context can and should assist in giving it meaning (see paragraphs 29 to 36). If there is doubt – as there is in relation to the breadth of this key exclusion – taxpayers ought to be given the benefit of it.

(c) The Draft s 100A Material should have prospective application that is clearly expressed (see paragraphs 37 to 41).

(d) The views expressed on the relationship between the income to which a beneficiary is presently entitled and the benefit under s 100A(7) should be reconsidered (see paragraphs 42 to 44).

(e) The views expressed on the interaction between s 100A and the streaming provisions concerning capital gains and franked distributions are controversial and should be reconsidered (see paragraphs 45 to 49). In addition, the Draft s 100A Material would benefit from a more detailed consideration of the interaction between s 100A and other integrity provisions (see paragraphs 50 to 52).

[1] [2021] FCA 1619, [125], [142].

(f) The Committee questions whether a public ruling is the appropriate method by which the ATO expresses its views on s 100A (see paragraphs 53 to 55).

(g) It would be appropriate for the ATO to amend TA 2022/1 to clarify the exclusions in the promoter penalty provisions (see paragraphs 56 to 62).

10 These matters, and others, are addressed in further detail within this submission.

Preliminary observations

11 Section 100A was introduced to respond to an era of poor tax behaviour and administration: the period of the late 1970s when artificial 'paper' tax avoidance schemes were rolled out on an almost industrial scale,[2] were advertised in newspapers,[3] and there existed a "*tax avoider lobby*".[4]

12 Specifically, and in that broader setting of the 'schemes era', s 100A was enacted in March 1979[5] to "*counter tax avoidance through trust stripping schemes*",[6] particularly ones that "*attempt to pass income derived by trusts on to beneficiaries in a tax-free form*".[7] As reflected in the s 100A extrinsic materials,[8] the indicia of schemes s 100A was introduced to counter – as a part of a suite of legislative anti-tax avoidance responses in the late 1970s – were:

(a) "*blatantly contrived and artificial arrangements*",[9] that "*are often very complex*";[10]

(b) "*seeking to bring about the happy situation that neither the trustee nor an intended beneficiary, nor anyone else, pays tax on substantial income derived by the trust estate*";[11]

(c) arrangements devised by or involving the "*promoters of tax schemes*";[12]

(d) the reliance "*on a nominal beneficiary being introduced into a trust and …* [where the "*specially*"[13] *introduced beneficiary also escapes tax by one means or another ...* [for] *example, the nominal beneficiary may be a tax-exempt body*

[2] Boucher, Trevor, *Blatant, Artificial and Contrived*, 2010 Australian Taxation Office, 6. The author describes, in detail, the astonishing breadth and intensity of the 'blatant and contrived' tax avoidance assault on the tax system and the revenue base in the 1970s, with the 'tax avoidance industry' producing schemes, used alone and in combination, including: dividend stripping, e.g., '*Slutzkin*' schemes - wet or dry (at 24, 75-76); '*Curran*' bonus share tax loss schemes (at 27-29); s 36A trading stock schemes (at 36-44); 'deathbed' trust schemes (at 62-64); gift schemes (at 69-74); dividend reimbursement schemes (at 77-79); trafficking in company tax losses (at 91-94); prepaid expenditure schemes (at 99); 'telephone book' trust schemes (at 108-109); and trust stripping schemes (at 110-112).
[3] Boucher, n 2, 41.
[4] Boucher, n 2, 59.
[5] Section 100A was inserted into the *Income Tax Assessment Act 1936* (the **1936 Act**) by the *Income Tax Assessment Amendment Act 1979* (the **1979 Amending Act**), that received assent on 13 March 1979.
[6] Statement of the Treasurer on 11 June 1978 (the **1978 Statement**), set out in *FC of T v Prestige Motors Pty Ltd* (1998) 82 FCR 195, 199-200.
[7] The Explanatory Memorandum (the **1978 Explanatory Memorandum**) to the Income Tax Assessment Amendment Bill (No 5) 1978 (the **1978 Bill**), that was enacted as 1979 Amending Act.
[8] The 1978 Statement, the Treasurer's Second Reading Speech for the 1978 Bill (the **1978 Second Reading Speech**), and the 1978 Explanatory Memorandum.
[9] The 1978 Second Reading Speech.
[10] The 1978 Statement.
[11] The 1978 Second Reading Speech.
[12] The 1978 Second Reading Speech.
[13] The 1978 Explanatory Memorandum, 31.

such as a charitable institution",[14] or "*a company, set up for the purpose by the promoters of the scheme*";[15]

(e) setting "*artificially-created paper 'losses' off against the income received from the trust*" or arranging "*to strip assets from the recipient company so that tax assessed on the income cannot be collected*";[16]

(f) distributing "*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*";[17] and

(g) the payment of "*the promoter's fee and a modest reward for the services of any participating exempt body*".[18]

13 Critically, the extrinsic materials stated that s 100A was to apply to present entitlements to trust income "*under tax avoidance schemes of the kinds mentioned and will not apply in the context of an agreement or arrangement that is entered into in the course of ordinary family or commercial dealing*".[19]

14 Reflecting the seriousness of the arrangements that s 100A was introduced to counter, the Commissioner was (and remains) empowered to amend assessments to give effect to the provision without any time limitation.[20] The unlimited amendment power associated with s 100A indicates that the legislature considered arrangements to which it applied as analogous to circumstances involving fraud or evasion, which also have an unlimited amendment period.[21] This correlation between s 100A cases and fraud or evasion cases is not surprising as the purported creation of present entitlements to income in circumstances where the real benefit of the income is intended to flow to a person other than the nominal beneficiary may be struck down as a sham, as *Raftland Pty Ltd v COT*[22] demonstrates. In contrast, when the general anti-avoidance rules in Part IVA (the **GAAR**) were enacted in June 1981,[23] the making of a determination by the Commissioner under s 177F(1) was subject to a limited amendment period – initially six years[24] and then four years.[25] The fact that Parliament still has not limited the period of amendment for s 100A itself indicates that the section should only be applied in the most egregious cases.

15 Another relevant legislative response that further illustrates the gravity of arrangements that s 100A was intended to counter was the enactment, not long after s 100A, of the *Crimes (Taxation Offences) Act 1980* (Cth) (**CTO Act**). Broadly, the CTO Act makes it an offence to organise the financial affairs of a company or trustee with the intention of securing that the company or trustee will not be able to pay its

[14] The 1978 Second Reading Speech.
[15] The 1978 Statement.
[16] The 1978 Statement.
[17] The 1978 Statement. This was a likely reference to what, at the time, was referred to as 'telephone book' trust schemes: see Boucher, n 2, 108-109, and *East Finchley Pty Ltd v FC of T* (1989) 90 ALR 457.
[18] The 1978 Statement.
[19] The 1978 Second Reading Speech.
[20] 1936 Act, s 170(10) in 1979, and now the table in s 17(10).
[21] 1936 Act, s 170(2)(a) in 1979, and now item 5 in the table in s 170(1).
[22] (2008) 238 CLR 516. See also, *East Finchley* (1989) 90 ALR 457, where Hill J (at 468) raised the question of sham.
[23] Applicable to schemes entered into after 27 May 1981 – see n 29.
[24] 1936 Act, s 177G(1), as originally introduced. The Commissioner had, and continues to have, an unlimited period to amend assessments to make compensatory adjustments in favour of taxpayers.
[25] Section 177G(1) – that provided for a 6 year amendment period for s 177F determinations – was repealed in 2005.

income tax liability.[26] This pre-tax stripping of trust assets to avoid a tax liability was referred to in the s 100A extrinsic material[27] and the CTO Act was considered to be part of the suite of legislative measures that included s 100A.[28]

16 It is useful also to consider the statutory measures that have accumulated around, and encroached into, s 100A's possible field of operation since its introduction in 1979:

(a) **the GAAR** introduced two years later in June 1981 as "*an effective general measure against those tax avoidance arrangements that … are blatant, artificial or contrived*";[29]

(b) **Schedule 2F** introduced 19 years later in April 1998 to "*to prevent the transfer of the tax benefit of* [trust] *losses or deductions*";[30]

(c) **Division 7A** also introduced 19 years later in June 1998 "*to ensure that private companies will no longer be able to make tax-free distributions of profits to shareholders (and their associates)*", including in circumstances where loans are made by trusts with private company beneficiaries whose entitlements to trust income have not been paid;[31]

(d) **Subdivision EA** inserted into Division 7A 25 years later "*to ensure that a trustee cannot shelter trust income at the prevailing company tax rate by creating a present entitlement to a private company without paying it and then distributing the underlying cash to a shareholder of the company*";[32] and

(e) the **streaming rules** for capital gains and franked dividends introduced 32 years later in June 2011 "*to ensure* [such amounts] *can be effectively streamed for tax purposes to beneficiaries by making them 'specifically entitled' to those amounts*".[33]

17 Most, if not all, of the arrangements identified in the Draft s 100A Material could be dealt with adequately and efficiently (positively or negatively) by the GAAR and other integrity measures introduced over the last four decades without resort to s 100A. Indeed, it is difficult to see what role s 100A actually has to play in today's tax system.

18 The ATO cannot, of course, ignore s 100A. However, the Committee considers that it is possible and appropriate to apply s 100A with restraint and consistently within the context summarised above; indeed, in the way in which the ATO has, until recently,

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[26] *Crimes (Taxation Offences) Act 1980* (Cth), ss 5, 6, 7 and 8.
[27] See paragraph 12(e) above.
[28] Boucher, n 2, 208-222.
[29] Explanatory Memorandum to the Income Tax Laws Amendment Bill (No 2) 1981, 2 (enacted as the *Income Tax Laws Amendment Bill (No 2) 1981* that received assent on 24 June 1981, and applied to schemes entered into after 27 May 1981).
[30] Explanatory Memorandum, *Taxation Laws Amendment (Trust Loss and Other Deductions) Bill 1997* (enacted as the *Income Taxation Laws Amendment (Trust Loss and Other Deductions) Act 1998* (Cth) that received assent on 16 April 1998, and generally applied from 9 May 1995).
[31] Explanatory Memorandum, Taxation Laws Amendment Bill (No. 3) 1998 (enacted as the *Taxation Laws Amendment Bill (No. 3) 1998* that received assent on 23 June 1998, and generally applied from 4 December 1997 but s 109UB, dealing with loans by trusts with private company beneficiaries, applied from 27 March 1998).
[32] Explanatory Memorandum, Tax Laws Amendment (2004 Measures No. 1) Bill 2004 (enacted as the *Tax Laws Amendment (2004 Measures No. 1) Act 2004* that received assent on 29 June 2004, and generally applied from 12 December 2002).
[33] Explanatory Memorandum, Tax Laws Amendment (2011 Measures No. 5) Bill 2011 (enacted as the *Tax Laws Amendment (2011 Measures No. 5) Bill 2011* that received assent on 29 June 2011, and generally applied in relation to the 2010-11 income year and later income years).

seen fit to administer s 100A for the last four decades. Unfortunately, that does not appear to be the approach foreshadowed in the Draft s 100A Material.

19 The Committee does not consider that confining the application of s 100A to conventional trust stripping and other similarly egregious arrangements runs against the grain of the few cases that have considered the provision. Over the last 43 years there have only been five s 100A cases heard in the Federal Court.[34] Appeals to the Full Federal Court were made and determined in three of those cases.[35] The most recent primary decision – *Guardian AIT* – is on appeal. Only one of those cases – *Raftland*[36] - was heard by the High Court. The circumstances in the three s 100A cases that have been considered by the Full Federal Court – *COT v Prestige Motors Pty Ltd*[37] and *Idlecroft Pty Ltd v COT*[38] – and the High Court – *Raftland*[39] – were all blatant, artificial and contrived and exemplars of the egregious arrangements highlighted in the s 100A explanatory material. *Raftland* was regarded as a sham. The outcomes in each of those cases – that s 100A applied – were not surprising, and were, with respect, justified. In *Raftland*, resort to s 100A was probably not required. Notably, each of these three cases involved facts and circumstances very different to the types of related party dealings which are the main focus of the Draft s 100A Material.

20 In light of the above, the Committee considers that the principles that should guide the development of ATO guidance on s 100A are as follows:

(a) The guidance must accord with established principles of statutory construction and authority. If there is doubt – as there is in relation to the key exclusion for "*ordinary family or commercial dealing*" – taxpayers ought to be given the benefit of the uncertainty. The ATO can constructively use the signposts in the extrinsic material to guide its administration. Those signposts should be embraced, not ignored.

(b) Further, the outcome imposed by a valid application of s 100A ought to inform the proper approach to its construction. That outcome is imposition of a tax liability on a person who no longer has any entitlement to the income in respect of which that liability is imposed. The section does not set aside the entitlement to the income as a matter of trust law. In these circumstances, a clear case is called for before the section can take effect.

[34] *East Finchley* (1989) 90 ALR 457 (Hill J); *Prestige Motors Pty Ltd as trustee of Prestige Toyota Trust v COT* [1997] FCA 346 (the first instance decision of Emmett J); *Idlecroft Pty Ltd v COT* [2004] FCA 1087 (the first instance decision of Spender J); *Raftland Pty Ltd v COT* [2006] FCA 109 (the first instance decision of Kiefel J); *Guardian AIT Pty Ltd (as trustee of Australian Investment Trust) & Anor v FCT* [2021] FCA 1619.
[35] *COT v Prestige Motors Pty Ltd* (1998) 82 FCR 195 (Beaumont, Hill and Sackville JJ) (special leave to appeal to the High Court was refused on 7 August 1998); *Idlecroft Pty Ltd v COT* (2005) 144 FCR 501 (Ryan, Tamberlin and Kiefel JJ); *Raftland Pty Ltd v COT* [2007] FCAFC 4 (Dowsett, Conti and Edmonds JJ).
[36] (2008) 238 CLR 516.
[37] See n 35. That case concerned three series of complex arrangements involving, broadly, the acquisition of an unrelated loss company and utilisation of the losses by distributions of trust income, and financing arrangements involving a third-party paying capital sums for subscribing for special units in trusts operating businesses, with the trust income being distributed to those special unit holders.
[38] See n 35. That case concerned a scheme, promoted by a firm of accountants, involving the formation of a property development joint venture between the trustees of discretionary trusts (all clients of the accounting firm) and an unrelated unit trust with tax losses, where distributions of trust income were made to the introduced unit trust and absorbed by the losses. The only cash payments were a small percentage of the distributions, that were paid to entities associated with the accounting firm.
[39] Thew case involved the introduction of a loss trust, unrelated to the taxpayer group, as a beneficiary to absorb trading profits of a building business, with a fee being paid to the previous controllers of that trust.

(c) The narrow way in which the ATO has administered s 100A in the past has in fact reflected the proper reach of the section and should be maintained. The suite of other integrity measures referred to above should be used to address the arrangements identified in the Draft s 100A Material with s 100A only playing a role in the most egregious of cases.

(d) The guidance the ATO finally issues will affect many taxpayers. In a report on trusts recently prepared for the ATO,[40] it was observed that by 2022 it was expected that over one million trusts will exist in Australia, and most of those would be discretionary trusts. The activities of trustees of trusts (acting in that capacity) span the spectrum of economic activity, from micro-businesses to the very largest of private groups. Whereas not all trustees of trusts in Australia will create present entitlements to trust income each year, many will and will do so in relation to multiple beneficiaries. It is not difficult to see how critical the Draft s 100A Material will be for millions of taxpayers who have, to date, not engaged with it. In practical ways, it is not just a guidance project because many taxpayers and their advisers will adopt the guidance as the rules to be followed, without regard to (or knowledge of) the fact that the guidance concerns a statutory provision which, despite being in existence for more than four decades, has been used sparingly and has been the subject of very little judicial interpretation. There is much at stake for taxpayers and the fair administration of the tax system.

(e) There can be no objection to an administrator seeking to shape future taxpayer behaviour to conform with a law that has to date not been properly appreciated and understood and that has received little substantial judicial guidance over the last 43 years. It is another thing entirely for an administrator to apply a recently developed perspective to past events and circumstances. Anecdotally, it is clear that the approach in the Draft s 100A Material amounts to a material change in how the ATO has applied s 100A over the last four decades. At the very least, the approach must have prospective application. There is little point in purporting to provide taxpayers with guidance in relation to events and circumstances that occurred in the past, and that cannot now be changed.

Text, context and purpose

21 In *Alcan (NT) Alumina Pty Ltd v Commissioner of Territory Revenue*[41] the High Court said:

> *This Court has stated on many occasions that the task of statutory construction must begin with a consideration of the text itself. Historical considerations and extrinsic materials cannot be relied on to displace the clear meaning of the text. The language which has actually been employed in the text of legislation is the surest guide to legislative intention.* ***The meaning of the text may require consideration of the context, which includes the general purpose and policy of a provision, in particular the mischief it is seeking to remedy****.* (emphasis added)

[40] See https://www.ato.gov.au/About-ATO/Research-and-statistics/In-detail/General-research/Current-issues-with-trusts-and-the-tax-system/

[41] (2009) 239 CLR 27 at [47], per Hayne, Heydon, Crennan, Kiefel JJ. See also [4]–[5], per French CJ.

22 The context referred to by the High Court "*includes legislative history and extrinsic materials* [and understanding] *context has utility if, and in so far as, it assists in fixing the meaning of the statutory tex*t".[42]

23 With particular reference to s 100A, after acknowledging the primacy of the text of the legislation, Hill and Sackville JJ said in *Prestige Motors*:[43]

> *This is not to say that that* [sic] *the legislative text is to be considered in isolation. The words are to be understood in the context of the enactment as a whole, the legislative history of the provision in question (including the mischief to be remedied) and, in appropriate cases, having regard to the consequences that would flow if one construction were preferred over another: … Nonetheless, the starting point must be the text of the law, having regard to its "ordinary meaning and grammatical sense": [citing Cooper Brookes (Wollongong) Pty Ltd v FCT*[44]*]*

24 Their Honours went on to observe, in response to particular submissions made by the taxpayer in relation to implied qualifications in the definition of "*reimbursement agreement*" in s 100A(7):[45]

> *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.*
>
> *…*
>
> *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.*

25 The relevant context to s 100A, including the mischief it was to address, and the range of anti-avoidance provisions and the streaming rules developed since its enactment, are summarised above. Other than to refer generally to s 100A as "*an anti-avoidance provision*",[46] the Draft Ruling does not explain or reflect that context. In the Committee's view, the first substantive guidance on s 100A in 43 years should be shaped by that context in order to achieve balanced guidance on the meaning and future application of the provision.

26 The Committee considers there to be a considerable qualitative difference between the description of the circumstances identified in the explanatory material to s 100A and a number of the circumstances now flagged by the ATO as being potentially of concern. The arrangements prompting the introduction of s 100A 43 years ago were ones involving artificial paper schemes and aggressive tax avoidance that go well beyond many of the arrangements that the ATO has identified as falling within the 'blue' or 'red' zones referred to in the Draft PCG, which involve dealings between members of the same family and entities within the same controlled family group. It

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[42] *COT v Consolidated Media Holdings Ltd* (2012) 250 CLR 503 at [39].
[43] (1998) 82 FCR 195 at 215 (Beaumont J agreeing).
[44] (1981) 147 CLR 297 at 321.
[45] (1998) 82 FCR 195 at 219-220.
[46] Draft Ruling TR 2022/D1 - Income tax: section 100A reimbursement agreements (**Draft Ruling**), [40], [78], [79], [94], [163]. See also: [43] ("*concerned with tax avoidance arrangements*") and [96] ("*a specific provision with an anti-avoidance object*").

would be of assistance to the community if the ATO adverted to the context in more detail and, if the examples referred to in the proposed guidance are now of concern, for the proposed guidance to explain why what was said in 1979 (that led to the introduction of s 100A) can be taken as contemplating what is now being identified as a concern. Content and explanation of this type will help the community understand the proposed administration of the provision.

27 To be clear, we are not suggesting that all the arrangements now identified to be of concern to the ATO should not be queried or challenged. Some of these examples may well give rise to concerns under other provisions – for example, under the GAAR and Schedule 2F. However, we submit that it is inappropriate, and unnecessary, for many of these to be challenged, particularly retrospectively, under s 100A.

28 Not referring to the relevant context may have led to erroneous construction of key concepts – such as "*ordinary family or commercial dealing*" – and it is not helpful for taxpayers or tax officers in considering whether or not the provision should be applied. Furthermore, it is at odds with the Commissioner's approach in s 100A litigation where he has himself "*place*[d] *some reliance upon extrinsic parliamentary materials*".[47]

Ordinary family or commercial dealing

29 In determining whether s 100A applies, the Committee considers that one of the critical threshold questions is whether a particular identified "*agreement, arrangement or understanding*" was one "*entered into in the course of ordinary family or commercial dealing*". Given its central importance, relegating the analysis of the concept as the last of the "*four basic requirements for section 100A to apply*"[48] is inappropriate. It would be preferable to adopt a framework that gives primacy to s 100A(13) in the way Logan J did in *Guardian AIT*.[49]

30 The Committee acknowledges the challenge in substantively addressing the meaning of this phrase given it has no statutory definition, it emerged in an attempt to differentiate what was tax avoidance from what was not, questions remain about what factors are or are not included in the evaluative standard (for example, different cultural approaches to familial dealings) and that there have been a number of subsequent statutory rules, summarised above, that have overlapped or overtaken its possible operation.

31 Contributing to that difficulty is the fact that on the two occasions where s 100A has been substantively considered by an appellate Court (in *Prestige Motors* and *Idlecroft*) no clear guidance has been given about the meaning of the phrase. In *Prestige Motors*, Hill and Sackville JJ (Beaumont J agreeing) said:[50]

> *The wording of the exclusion in s 100A(13) derives from the judgment of Lord Denning, on behalf of the Privy Council, in Newton v Commissioner of Taxation (Cth) (1958) 98 CLR 1 at 8. There his Lordship, in discussing s 260 of the ITAA, contrasted an arrangement implemented in a particular way to avoid tax with ``transactions that are capable of explanation by reference to ordinary business or family dealing''.*
>
> *There is a danger that, when words used in a judgment are translated into the legislation, the change of context may alter the meaning of the words from that*

[47] *Raftland Pty Ltd v COT* [2006] FCA 109 (the first instance decision of Kiefel J), [54].
[48] Draft Ruling, [4].
[49] [2021] FCA 1619, [120].
[50] (1998) 82 FCR 195 at 221-2

which they originally bore. It is clear from both the judgment of the Privy Council and from the language of the High Court in the same case (Commissioner of Taxation (Cth) v Newton (1957) 96 CLR 577) that s 260 was regarded as involving a dichotomy. A transaction was either stamped as one entered into to avoid tax or as one about which it could be predicted that it was entered into in the course of ordinary family or commercial dealing. In the former case the transaction was caught by s 260; in the latter case it was outside the section. We do not need to decide in the present case whether s 100A imports a similar dichotomy. In particular we do not need to decide whether if an agreement is shown to have been "entered into the course of ordinary commercial dealing", the operation of s 100A is spent, regardless of whether the commercial purpose was subsidiary to the purpose of tax avoidance. In our view, none of the transactions was entered into in the course of ordinary commercial dealing.

32 The Committee suggests the ATO consider further engagement with the statement of the Full Federal Court above. If a clear meaning is not apparent on a plain reading of the text, then accepted principles of statutory construction dictate that the context (summarised above) can and should assist in giving the phrase meaning. With that assistance, several of the examples set out in the Draft s 100A Material must be accepted as falling within the "*ordinary family or commercial dealing*" exception.

33 Further, the statement in paragraph 79 that a "*dealing can fail to be ordinary dealing even where it is not artificial*" is not consistent with the context of s 100A, does not appear to be consistent with what was said in *Prestige Motors* and, importantly, is inconsistent with the following observations of Logan J in *Guardian AIT*:[51]

Textually, in relation to s 100A, if there is no "agreement", as defined, s 100A(7) can have no application. This difference as between the definition of "agreement" in s 100A(13) and the definition of "scheme" in s 177A(1) of the ITAA 1936, and this consequence in relation to the absence of application of s 100A(7), may well offer another example of the awkward drafting in s 100A. But it is that text which has been approved by parliament. And, given the exclusion present, it is not to say that purpose is irrelevant to the construction and application of the definition of "agreement" in s 100A(13).

The construction of s 100A adopted in Prestige Motors and Idlecroft binds me. Indeed, that construction carries particular authority, as the discussion by the High Court of s 100A in Raftland Pty Ltd v Federal Commissioner of Taxation (2008) 238 CLR 516 (Raftland), at [60] proceeded on the basis that each of these cases was correctly decided. However, neither in Prestige Motors, Idlecroft nor in Raftland was it necessary to consider the effect, in relation to any possible application of s 100A(7), of a conclusion that an agreement, arrangement or understanding was entered into in the course of ordinary family or commercial dealing.

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".*

[51] [2021] FCA 1619, [142]-[145].

As it happens such an understanding of "ordinary family or commercial dealing" does accord with what the Judicial Committee in Newton and Heerey J in Rippon did not regard as tax avoidance. (emphasis added)

34 Further, it is not easy to reconcile the statement in paragraph 79 of the Draft Ruling – that a "*dealing can fail to be ordinary dealing even where it is not artificial*" – with the statement in paragraph 95 that an arrangement having "*artificial or contrived features*" may "*indicate that a dealing that is being tested is not ordinary dealing*".

35 The Draft Ruling refers to *Guardian AIT* four times: three as supplementary support for non-controversial points (in footnotes 33, 41, and 44), and the final, at footnote 47, appears to both agree and disagree with the last two paragraphs extracted above. Logan J decided, on the evidence and facts in that case, that what the parties did "*was nothing more than an ordinary family or commercial dealing*",[52] and accordingly there was no "*agreement*" as defined in s 100A(13).[53] Considering that the three cases on s 100A determined on appeal (*Prestige Motors*, *Idlecroft*, and *Raftland*) did not need to consider the ordinary family or commercial dealing exception, Logan J's analysis of the exception is vitally important and ought not be relegated to a mere footnote.

36 The fact that *Guardian AIT* is on appeal to the Full Federal Court is a matter that bears reflection. While it is too late now to reverse what has happened, it may have been better to defer release of the Draft s 100A Material until the appeal has run its course. That not being the case, the decision should be respected as judicial guidance and reflected in the Draft Ruling, and if a different result or different principles emerge from the appeal decision, the Draft Ruling can be amended or supplemented.

Retrospectivity

37 For the reasons set out in paragraph 20(e) above, the Draft s 100A Material should have clearly expressed prospective application.

38 By way of general comment, the way in which the Draft PCG sets out how the ATO intends to apply its views on s 100A for past years is complex and confusing.

39 The guidance provided in the Draft PCG indicates that the ATO proposes to not apply compliance resources to certain arrangements arising before 1 July 2014, subject to important conditions being met.[54] Such arrangements are regarded as 'white zone' arrangements in the Draft PCG. However, the Draft PCG also indicates that the ATO intends to apply s 100A retrospectively, and without limitation, to arrangements that would fall outside the 'green zone' specified in the Draft PCG where such an arrangement "*continues before and after* [1 July 2014]".[55]

40 The relevance of the 1 July 2014 date, as noted in the Draft PCG,[56] is that general material was included on the ATO website in July 2014 in relation to the operation of s 100A (**2014 ATO Website Material**). Presumably the ATO's view is that this date should represent something of a 'red line' in relation to the administration of s 100A.

41 The Committee considers that the significance given to the 2014 ATO Website Material is not appropriate, both in principle and in practice, for the reasons outlined below:

[52] [2021] FCA 1619, [152].
[53] [2021] FCA 1619, [154].
[54] Draft PCG, [13].
[55] Draft PCG, [13].
[56] Draft PCG, [47].

(a) The 2014 ATO Website Material lacks the status, formality, detail and analytical rigour associated with a public ruling or guidance statement (draft or otherwise). Irrespective of whether taxpayers or advisers agree or disagree with the views expressed in a draft ruling/determination or PCG, the practical reality is that they are quite clear as to the importance of an issue in the mind of the Commissioner and the approach that the ATO intends to adopt. The same cannot be said for material on the ATO website.

(b) The higher level of formality in rulings/determinations or PCGs means that ATO officers are much more likely to follow the ATO's interpretation of a provision, in contrast to the general information available on the ATO's website. As noted in the background provided above, it is anecdotally clear that in reviews it has conducted (including reviews conducted after 1 July 2014) the ATO has not consistently acted against arrangements, notwithstanding the 2014 ATO Website Material.

(c) The 2014 ATO Website Material deals with a contentious issue with very little recognition of the matters of context referred to above, particularly in relation to the critical "*ordinary family or commercial dealing*" exception.

(d) The 2014 ATO Website Material is light on detail, ambiguous in certain respects, does not engage with difficult points of construction and contains statements that are inconsistent with the Draft s 100A Material. By way of illustration:

    (i) the 2014 ATO Website Material has little to say in relation to dealings between family members, whereas this is a significant focus of the Draft PCG and the sole focus of TA 2022/1;

    (ii) the 2014 ATO Website Material does not deal with the issue of streamed capital gains and franked distributions (see below);

    (iii) the 'use of funds' condition, as expressed in the 2014 ATO Website Material, is considerably less stringent than that prescribed in the Draft PCG[57]; and

    (iv) there is ambiguity in the 2014 ATO Website Material about the extent to which interest-free loans from a trust might be regarded as giving rise to a s 100A risk.

(e) That taxpayers are, according to the Draft PCG, able to rely on the administrative position reflected in the 2014 ATO Website Material in relation to entitlements conferred before 1 July 2022 is considered to be of little or no comfort to taxpayers for two reasons. First, the views expressed in those materials are themselves retrospective in nature, potentially extending back to the date that s 100A was introduced. Secondly, due to the shortcomings of the 2014 ATO Website Materials noted in (a) to (d) above.

[57] At [21] of the Draft PCG, the ATO requires not only that the funds loaned to an associate of the lending trust be placed on terms that would satisfy section 109N, but that the **borrower** of the funds also use the funds in a way that satisfies the new use of funds test. The 2014 ATO Website Material make no reference to any requirements for use of funds by the borrower.

The relationship between the income to which a beneficiary is presently entitled and the benefit – s 100A(7)

42 The Draft Ruling states the following in relation to the definition of "*reimbursement agreement*" in s 100A(7):[58]

> *In particular, there is no requirement that the relevant money, property, services or other benefits provided to a person other than the beneficiary alone, be sourced from, equal to* ***or otherwise be referrable to the share of trust income the beneficiary is presently entitled to receive, was paid or that was applied on their behalf****. (emphasis added)*

43 It may well be the case that no strict tracing is required in relation to the "*relevant trust income*"[59] to which the beneficiary is presently entitled and the benefit required for there to be a "*reimbursement agreement*". But to posit that no referability is necessary takes it too far when there is no authority in support of the proposition highlighted above. The fundamental requirement of the operative provisions is that the present entitlement to income has arisen "*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*". As a matter of statutory construction, reading s 100A(7) together with the operative provisions, ss 100A(1) and (2), there must be some referability or some rational basis, to link the "*relevant trust income*" to the benefit. Where the test is that the entitlement to income arises out of or in connection with the reimbursement agreement, the two cannot be unrelated.

44 The 'no referability' proposition underpins the analysis and conclusion in Example 8 in the Draft Ruling.[60] For a number of reasons, the Committee doubts that s 100A can apply to the circumstances illustrated in that example. The buy-back proceeds in that example are capital receipts, and the trustee is not purporting to re-characterise those receipts. The $10,000 interest income, to which the beneficiary is presently entitled, and which it receives in full and keeps, has no rational connection with the capital distribution of the buy-back proceeds to other beneficiaries. In any case, the transactions in this example are not artificial or contrived and can easily be seen as having been entered into "*in the course of ordinary or commercial dealing*". One beneficiary receives the income to which it is entitled, and another receives capital of the trust.

Streaming of capital gains and franked dividends

45 Whilst s 100A is confined to present entitlements to income,[61] the Draft Ruling states that s 100A may apply to specific entitlements to capital gains and franked distributions.[62] The Committee considers that these statements should be removed.

46 Section 100A is only engaged if there is a beneficiary that "*is* [or is deemed to be] ***presently entitled*** *to a share of the income of the trust estate*"[63] (emphasis added). The effect of s 100A is to deem the beneficiary to not be and never to have been "*presently entitled*" to the relevant trust income. The provision does not deem the beneficiary not to be "*specifically entitled to an amount of a capital gain* [or a franked

[58] Draft Ruling, [15]. See also [67].
[59] 1936 Act, ss 100A(1)(b) and (2)(b).
[60] Draft Ruling, [145].
[61] 1936 Act, ss 100A(1) and (2).
[62] Draft Ruling, [102]–[106].
[63] 1936 Act, ss 100A(1)(a) and (2)(a).

distribution]"[64] nor does it deem the beneficiary not to have "*the financial benefit that is referable to the capital gain* [or a franked distribution]".[65] While the concepts of present entitlement and specific entitlement have common attributes at a simplistic conceptual level, they are different statutory concepts that relate to different subject matter.

47 Further, specific entitlement is confined to particular amounts by Division 6E of Part III and the existence of each is tested at different points in time. Present entitlement, for the purposes of the assessing provisions in Division 6, is determined just prior to midnight at the end of the year of income.[66] Whether or not there is specific entitlement can, at least in relation to capital gains, change by events that happen after the end of the year of income.[67] That timing difference presents difficulties in applying s 100A because, in order for the provision to apply, the reimbursement agreement must precede the present entitlement.[68] If the statements in the Draft Ruling are correct, then the requirements of s 100A would need to be tested at different points in time depending on whether the income in question consists of capital gains and franked dividends or other income. Such an approach is not justified from the text of the provisions, nor the matters referred to in footnote 62 of the Draft Ruling. Different considerations may arise if capital gains and franked dividends are attributed to the beneficiary because of its adjusted Division 6 percentage of the income of the trust for that year of income.[69] But that just reinforces the proposition that s 100A ought not apply to specific entitlements.

48 Whether or not s 100A applies to capital gains and franked dividends to which a beneficiary is specifically entitled is not clear. The issue has not been tested before the Courts and, given that the interaction between Division 6 and Division 6E involves complex issues of statutory construction (as evident from the recent decision in *Peter Greensill Family Co Pty Ltd (Trustee) v COT*),[70] the Committee considers that there is sufficient doubt about the issue to make it inappropriate for inclusion in a public ruling in the manner currently expressed.

49 What is clear, and should be expressly stated, is that s 100A can never apply to distributions of capital gains pursuant to a power of appointment of trust capital (thus creating a specific entitlement to that gain), where those capital gains are not part of the income of the trust as a matter of general law.

The interaction between s 100A and other provisions

50 As noted above, the GAAR, other integrity measures and the streaming rules have been introduced over the last four decades, encroaching into s 100A's possible field of operation.

51 Except in relation to the streaming rules, the Draft s 100A Material does not address the interaction between s 100A and these other provisions. For example:

(a) What is the ATO's approach when it seeks to apply the GAAR and s 100A in relation to the same trust income where the actual taxpayer under each provision is different (as in *Guardian AIT*)? In that scenario, will the ATO seek to assess and collect tax from both taxpayers, thus creating effective double

[64] *Income Tax Assessment Act 1997* (**1997 Act**), ss 115-228, 207-58.
[65] 1997 Act, ss 115-228, 207-58 – definition of "*net financial benefit*".
[66] *Commissioner of Taxation v Carter* [2022] HCA 10, [22]-[23].
[67] 1997 Act, ss 115-228, 115-230.
[68] *East Finchley* at 473-474; *Guardian AIT* at [129].
[69] 1997 Act, ss 115-227(b) and 207-55(4)(b), respectively.
[70] [2021] FCAFC 99.

taxation, or will the assessments be alternatives? If the assessments are alternatives, which is given primacy?

(b) What is the interaction between Division 7A and s 100A? Will the ATO seek to tax different taxpayers on the same underlying trust income under Division 7A, the GAAR and s 100A?

(c) The ATO has also indicated that it will apply s 100A to the creation of present entitlements to income in favour of trusts which have losses, including those controlled by the same family group.[71] There are already extensive provisions in Schedule 2F governing the deductibility of such losses but they apply to loss trusts which receive income. Effectively, this could result in the imposition of tax twice, first in the hands of the trustee under s 100A, and secondly in the hands of the beneficiaries or trustee of the loss trust.

52 The omission in the Draft s 100A Material of any useful consideration of the interaction between s 100A and other provisions might undermine the comments in the Draft Ruling about the "*harmonious interaction of the components of this integrated scheme*".[72]

Is a ruling the most suitable product?

53 The Committee questions whether a public ruling is the appropriate method by which the ATO expresses its views on s 100A.

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

55 The Committee recommends that the ATO consider a similar approach with s 100A, particularly for the reason suggested above in relation to the GAAR but also having regard to the matters of context raised above.

TA 2022/1

56 At a general level, any of the observations made in this submission can be taken as applying to TA 2022/1, where relevant.

57 TA 2022/1 raises the prospect of promoters of arrangements to which TA 2022/1 applies being subject to penalties under the promoter penalty provisions.[73] The Committee understands that the ATO has already received feedback on this point.

[71] See Draft Practical Compliance Guideline PCG 2022/D1 - Section 100A reimbursement agreements – ATO compliance approach (**Draft PCG**), Example 11, [123]-[130].
[72] Draft Ruling, [171], made in the context of the streaming rules.
[73] *Taxation Administration Act 1953* (**TAA**), Schedule 1, Division 290.

58 In raising the prospect of the promoter penalty provisions applying to advisors, TA 2022/1 does not address the implications of having a position that is "*reasonably arguable*". The promoter penalty provisions require that there is a relevant "*tax exploitation scheme*",[74] which is defined to exclude a scheme that is "*reasonably arguable*".[75]

59 For the reasons canvassed above, the Committee considers that a tax agent relying on Logan J's decision in *Guardian AIT* as a "*relevant authority*" under s 284-15(1) of Schedule 1 to the *Taxation Administration Act 1953* (**TAA**) could well have a position that it is "*reasonably arguable*" that s 100A does not apply to the arrangement identified in the Alert and many 'red zone' cases in the Draft PCG. While primarily relevant for shortfall penalty purposes under ss 284-75(2) and 284-90 of the TAA, the "*reasonably arguable*" concept is also relevant for other purposes, including the promoter penalty provisions.

60 There are also other aspects of the promoter penalty provisions that seem not to have been sufficiently considered in the framing of the Alert, most notably the 'mere advice' exception.[76]

61 In addition, the potential referral of tax agents involved with such arrangements to the Tax Practitioners Board does not consider the "*reasonably arguable*" point.

62 The ATO should consider amending TA 2022/1 to clarify that there are exclusions in the promoter penalty provisions in TAA that may apply and to similarly caveat the warning of potential referral of tax agents to the Board to exclude "*reasonably arguable"* positions. Alternatively, the ATO might consider withdrawing the Alert and addressing the issues it covers in the guidance material.

Conclusion and further contact

63 The Committee would be pleased to discuss any aspect of this submission.

64 Please contact the Chair of the Committee, Angela Lee (at angela.lee@vicbar.com.au), or member of the Committee, Paul Sokolowski (at psokolowski@abl.com.au), if you would like to do so.

Yours faithfully

Philip Argy
Chairman
Business Law Section

[74] TAA, s 290-50.
[75] TAA, s 290-65.
[76] TAA, s 290-60.