

Tax News, Views and Clues

Trust Distributions and Capital Gains

The Tax Office has issued a Practice Statement concerning the tax issues arising when there are distributions of trust income and capital gains to separate beneficiaries.

Based on the technical application of the law, a beneficiary entitled to a share of trust 'income' pays tax on that share of the trust's net (taxable) income. As a capital gain is not 'income', beneficiaries entitled to income may be taxed on capital gains distributed to other beneficiaries, although they have no entitlement to the cash.

The Practice Statement outlines two practical approaches that will be accepted by the Tax Office in certain circumstances.

The first enables the beneficiary who receives the benefit of the capital gain to bear the tax.

Alternatively, in certain cases, the trustee can be chosen to recognise the tax liability. A written agreement may be required between the trustee and the beneficiaries.

The Practice Statement focuses on trusts that have separate 'income' and 'capital' beneficiaries. However, its application to ordinary discretionary trusts is also acknowledged.

Family Trust Elections of Non-Fixed Trusts

The Tax Office has issued a series of three interpretative decisions explaining the availability of tax offsets (franking credits) for beneficiaries of non-fixed trusts that derive franked dividends as a distribution of trust income.

Readers may be aware that, broadly, shares must be owned at risk for a period of at least 45 days in order to qualify the shareholder for tax offsets. Owning shares at risk refers to, for example, owning shares without reducing the risk of loss, or opportunity for gain, by entering into transactions such as options or futures.

In relation to shares held within a non-fixed trust, the Tax Office first restates the position that a beneficiary of a non-fixed trust will not be a qualified person in

relation to a dividend on shares held at risk for at least 45 days unless the trustee has made a family trust election. Consequently, the franking credits will be lost.

A beneficiary's interest in a non-fixed trust is determined by their entitlement to dividend income of the trust. A discretionary beneficiary of a trust is considered not to have an 'interest' in the trust income. However, the tax offsets will still be available where the family trust election is made.

The Tax Office then states that the same position applies even where a beneficiary has an interest in the corpus of the trust. Unless the trustee makes a family trust election, a beneficiary will not be entitled to receive tax offsets (franking credits) on any dividend distributions flowing through the trust.

Finally, notwithstanding the making of a family trust election, the relevant shares must be held by the trustee for at least 45 days at risk in order for the tax offsets to be available.

No Required Holding Period for the Small Shareholder Exemption

The Tax Office has confirmed that an individual may still be qualified to receive tax offsets on franked dividends under the Small Shareholder Exemption even if their shares have not been held at risk for 45 days.

To be eligible for the exemption, the individual must satisfy two requirements.

First, the individual's franking credit total for the relevant year must not exceed \$5,000.

Second, the individual must not have made a related payment in respect of their shares (which would have the effect of transferring the benefit of dividends).

Commissioner's Discretion on Logbook Requirements for Car Fringe Benefits

The Commissioner has the authority under the Fringe Benefits Tax legislation to exercise his discretion and not enforce the substantiation requirements in special circumstances.

The Tax Office recently announced that this discretion would be employed in relation to the substantiation requirements for logbook records for car use. Legislation requires various entries to be made in a logbook in respect of each business journey.

If a taxpayer fails to comply with a requirement, the Commissioner

will base his decision on the impact the omission has had on the integrity of the logbook.

Accordingly, where no or minimal impact is present, the Commissioner is likely to overlook the taxpayer's omission.

- **Tip:** Such a logbook must record only business journeys and be kept for a minimum of 12 consecutive weeks.

CGT Rollovers on Asset Transfers to a Company

The Tax Office has released two Interpretative Decisions in regard to the availability of CGT rollover relief on asset transfers from an individual or trust to a company.

Rollover relief disregards any capital gain or capital loss made by an individual or trust as a result of the disposal. In order to obtain rollover relief, the asset transfer must satisfy a series of conditions including:

- the transferor must own all the shares in the company after the disposal of the asset;
- the company must not be a tax-exempt entity; and
- if neither the trust (transferor) or the company (transferee) is a resident, the asset must have the necessary connection with Australia.

In addition, any consideration received by the transferee for the disposal of the asset to the company must be limited to shares in the company and/or the assumption of liabilities in relation to the asset.

In the situation where the transferor receives no consideration for the assets

disposed of, the ATO states that rollover relief may still be granted, as the law does not specifically require that consideration be received for the asset transferred.

ATO Targets Property Schemes

The ATO is looking into alleged GST avoidance schemes involving the use of a joint venture as an interposed entity when supplying new residential premises. The ATO has recently issued a media release warning against the abuse of such arrangements.

The particular scheme targeted by the ATO involves the use of a GST joint venture to create an 'artificial' first sale of new residential premises by a joint venture operator to a joint venture participant.

Supplies by a joint venture operator to a joint venture participant are not generally subject to GST (conditions involving the use of the acquisition by the joint venture participant exist).

On subsequent supply to a customer by the joint venture participant, the supply is claimed to be input taxed as the premises are no longer new, i.e. they have previously been sold as residential premises.

The ATO has indicated that it will be targeting such schemes on the basis that either they do not involve a true joint venture, do not amount to a sale of the premises or the anti-avoidance provisions of the GST Act apply.

- **Caution:** If you are thinking of entering this type of arrangement, be aware that the ATO may deem the subsequent sale to the end user to be subject to GST.

Important: This is not advice. Clients should not act solely on the basis of the material contained in this Bulletin. Items herein are general comments only and do not constitute or convey advice per se. Also changes in legislation may occur quickly. We therefore recommend that our formal advice be sought before acting in any of the areas. The Bulletin is issued as a helpful guide to clients and for their private information. Therefore it should be regarded as confidential and not be made available to any person without our prior approval.