



THE TAX INSTITUTE

# PART IVA – HOW'S YOUR POSTULATE?

**David W Marks CTA**  
Inns of Court, Brisbane

# What has happened?

---



- Part IVA got redrawn by parliament
  - The Commissioner lost *Futuris* and *RCI*.
  - But rumblings since 09/10 Budget.
  
- HCA looked at the rule about relying on an express election – *Unit Trend Services*

# The journey

---



- Part IVA introduced - 1981
- First case decided – 18 Sep 92 *(Peabody)*
- Minister Bowen PR – 12 May 09 *(09/10 budget)*
- Minister Shorten DP – 18 Nov 10
- *RCI* – no special leave – 10 Feb 12
- Minister Arbib's PR – 1 Mar 12 *(PR 10/12)*
- Confidential consultation - 2012
- ED – 16 Nov 12 (retroactive date) *(PR 143/13)*
- Bill in HR - 13 Feb 13; Assent – 29 Jun 13

# The destination

---



- Eliminate “do nothing” counterfactual
- Bifurcate the postulates:
  - Annihilate leaving a tax benefit exposed
  - Reconstruct to make a tax benefit
- Refocus on purpose

# Bifurcated postulates

---



- “Would”
  - = Annihilate leaving a tax benefit exposed
  
- “Might reasonably be expected”
  - = Reconstruct to make a tax benefit
  
- Not merely gradations on a scale
  - 2 separate concepts
  - To overcome eg Full Ct in *RCI*

# Role of ‘reasonable alternative’

---



THE TAX INSTITUTE

- On reconstruction –
  - postulate must be a “reasonable alternative to entering into ... the scheme”
  - Dynamics of proof: *Macquarie*
  
- Annihilation
  - No “reasonable alternative” requirement for postulate
  - Residual work for ‘would’?

# ‘Unreasonable alternative’

---



THE TAX INSTITUTE

- On reconstruction - postulate must be a “reasonable alternative to entering into ... the scheme”
- But disregard tax consequences of a postulate in judging whether ‘reasonable alternative’
- Effectively kills the ‘do nothing’ alternative: *Futuris & RCI*

- Annihilation –
  - Postulate based only on the facts left standing
  - Case management issues if run alternative postulates
  - Attractive to Commissioner because no ‘reasonable alternative’ test
  - Does not suit some cases
  - Typically better for a deduction case, not an income case
  
- Reconstruction – better suited to some cases; no change to present case management issues



# Refocusing s.177D

---



THE TAX INSTITUTE

- Shuffling words
- At best no change, at worst slight confusion

# What case results would change



THE TAX INSTITUTE

- Best guess

<b>Case</b>	<b>Result</b>	<b>Altered result?</b>
Noza	Taxpayer	No – no tax benefit, no purpose
BATA	Commissioner	No
Citigroup	Commissioner	No
Axa	Taxpayer	No (?) – alternative postulate unlikely
Macquarie	Taxpayer	No – no purpose
Ashwick	Taxpayer	No – no purpose
RCI	Taxpayer	Yes – do nothing alternative
Futuris	Taxpayer	Yes – do nothing alternative

# Words won't fix

---



THE TAX INSTITUTE

- Forensic choices
  - Not running evidence
  - Not seeking an adjournment when truly needed
  - Not cross-examining

# Scenario – trust distribution

---



THE TAX INSTITUTE

- Ann is on top marginal rates personally
- She is trustee of a discretionary trust
- She can appoint income to herself, her children, relatives, and a named ‘charity’
- Her former husband is the default beneficiary. (He does not know this. It was done out of spite.)
- She validly appoints \$50,000 income to the charity.
- She pays it to the charity
- The Commissioner investigates the charity’s finances

# Analysis of tax benefit – trust distribution

---



THE TAX INSTITUTE

- A [rare?] example of an income scheme which works under annihilation
  - She is trustee of a discretionary trust
  - She can appoint income to herself, her children, relatives, and a named charity
  - Her former husband is the default beneficiary (unbeknownst to him)
  - ~~– She validly appoints \$50,000 income to the charity~~
  - ~~– She pays it to the charity~~
- Leaves either trustee (s.99A) or husband exposed

# Further analysis of tax benefit – trust

---



THE TAX INSTITUTE

- Leaves either trustee (s.99A) or husband (default beneficiary) exposed
- But husband validly disclaims his interest as default beneficiary
- That would leave trustee liable under s.99A, unless Commissioner also annihilates husband's disclaimer

- If the annihilation scheme is simply distribution to a non-genuine charity –
  - purpose enquiry under s.177D starts well for Commissioner
  - Tax benefit is non-inclusion of income for husband
  - Ann’s purpose is nakedly to ensure ‘a tax benefit’ is secured
- If annihilation scheme also includes the disclaimer:
  - leaves former husband exposed despite his refusal of gift
  - Ann is ‘one of the persons’, and her purpose is as above

- Ann & Ben
  - Marriage ended with little acrimony
  - Ann has CGT assets, Ben has nothing but liabilities
  - Ann amenable to transfer Blackacre to Ben to settle affair
  - Blackacre is pregnant with gain
  - Appoint arbitrator under s.13H *FLA*, make joint submissions, arbitrator makes award accordingly
  - Ann transfers Blackacre to Ben
  - Ann suffers no gain: s.126-5



- An income case where annihilation works:
  - Marriage ended with little acrimony
  - Ann has CGT assets, Ben has nothing but liabilities
  - Ann amenable to transfer Blackacre to Ben to settle affair
  - Blackacre is pregnant with gain
  - ~~■ Appoint arbitrator under s.13H FLA, make joint submissions, arbitrator makes award accordingly~~
  - Ann transfers Blackacre to Ben
  - Ann suffers no gain: s.126-5

# Tax benefit – family law

---



THE TAX INSTITUTE

- Deleting the arbitration
- Leaves exposed a transfer of asset pregnant with gain
- Tax benefit is the gain, subject to discount, or other concessions & losses

# Purpose – family law

---



THE TAX INSTITUTE

- If there was no need to arbitrate, the sole purpose of the arbitration appears to be accessing the rollover
- Rollover non-elective, so s.177C(2) does not apply
- This segues into a discussion of *Unit Trend Services*

# No tax benefit where elective?

---



- Not that simple!
- eg s.177C(2)(a):
  - non-inclusion of income attributable to express election
  - scheme not entered into for purpose of allowing election to be made
- Must be express election, not simply a choice otherwise made: *Case W58*
- Must truly be attributable: *Noza*

# Whether attributable to election

---



THE TAX INSTITUTE

- *Unit Trend Services* – HCA
- GST language was “not attributable”
- Held – benefit was “not attributable” to elections
  
- Discounted applicability of earlier HCA CGT case, about width of “attributable”: *Sun Alliance*
- Therefore *Sun Alliance* still good law for s.177C?

# Scheme to set up election

---



THE TAX INSTITUTE

- If *Sun Alliance* still good law for s.177C, still face a second guardian
- Second guardian under s.177C – where purpose of scheme to access the election
- This was effective in *Walter*

# Upshot of *Unit Trend*

---



THE TAX INSTITUTE

- Wording of s.177C differs critically as to 'attributable'
- The 'scheme for an election' element remains effective

# Scenario – election to consolidate

---



- Holdco is a cleanskin, recently incorporated
- OpCo runs 2 businesses, with internally generated goodwill. It is wholly unrelated to Holdco.
- Holdco issues shares to raise capital
- Holdco buys all issued shares in OpCo
- Holdco elects to consolidate
- OpCo sells one business to Holdco
- OpCo sells 2<sup>nd</sup> business to independent 3<sup>rd</sup> party
- OpCo is liquidated



# Issues – election to consolidate

---



THE TAX INSTITUTE

- Scheme for OpCo to escape tax on sale of business to Holdco?
  - simply annihilate the election? Or the share sale as well?
- Tax benefit:
  - To whom under consolidation
  - Whether attributable to election; or scheme for an election
- Purpose:
  - seems a vanilla way of getting business into a cleanskin
  - OpCo's former shareholders pay tax on share sale
  - Relevance of those two points?

- Some Part IVA amendments work powerfully:
  - annihilation postulate is free of “reasonably ... expected”
  - reconstruction postulate
    - elimination of tax cost as consideration
    - policy headaches
    - commercial headaches
- Refocus on purpose – drafting a bit esoteric
- Case law on exception for ‘tax benefit’ for election
  - *Unit Trend Services* does not end this, actually helps
  - scope of exception remains inexact science



© David W Marks 2014

**Disclaimer:** The material and opinions in this paper are those of the author and not those of The Tax Institute. The Tax Institute did not review the contents of this presentation and does not have any view as to its accuracy. The material and opinions in the paper should not be used or treated as professional advice and readers should rely on their own enquiries in making any decisions concerning their own interests.

Liability limited by a scheme approved under professional standards legislation.