Coster Galgut
Chartered Accountants

Tax Update – April 2022

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The Government is in caretaker mode pending the Federal Election…but that doesn't mean nothing is happening.

The High Court decision in Carter & Ors was a win for the ATO in a case exploring whether beneficiaries can disclaim their entitlement to trust distributions.

And, in the London case, a taxpayer has been allowed to claim a deduction for gym membership costs but as usual, life is not that simple and practitioners need to be aware of the details before helping clients to claim their fitness related costs.

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From Government

Uncertainty on trusts

The Assistant Treasurer has issued a media release in relation to the draft guidance released by the ATO on section 100A. The Assistant Treasurer raises the possibility of the Government making legislative amendments in this area. The Government will monitor the consultation process for the ATO's draft guidance and will consider any appropriate changes to the law should any adverse retrospective impacts arise.

The media release also refers to the recent High Court decision in the Carter case (see below for more details) and indicates that the Government will be considering the implications of the decision and whether any inequitable outcomes can be dealt with by legislative change. The case deals with the tax impact of a beneficiary seeking to disclaim a distribution from a trust.

More information

- Certainty and stability for family trusts

From the ATO

Fuel tax credit rate changes

The ATO has released updated fuel tax credit rates that apply for the period from 30 March 2022 to 30 June 2022. The Government has temporarily halved the excise and excise equivalent customs duty rates for petrol, diesel and all other petroleum-based products (except aviation fuels) for 6 months from 30 March 2022 until 28 September 2022. This has caused a reduction in fuel tax credit rates.

During this 6 month period businesses using fuel in heavy vehicles for travelling on public roads won't be able to claim fuel tax credits. This is because the road user charge exceeds the excise duty payable, and this reduces the fuel tax credit rate to nil.

The ATO's fuel tax credit calculator has been updated to apply the current rates.

More information

- Fuel tax credit rates have changed
- From 30 March 2022 to 30 June 2022
- Fuel tax credit calculator

Deductions for COVID-19 tests

The ATO confirms that COVID-19 tests purchased by employees for work purposes from 1 July 2021 can be claimed as a deduction. This is the result of legislation that passed through Parliament shortly after the 2022-23 Federal Budget was handed down.

This also means that employers who provide COVID-19 tests for their employees for work purposes can generally reduce the taxable value of the relevant fringe benefit by applying the otherwise deductible rule.

More information

- COVID-19 tests and fringe benefits tax (FBT)

Debts placed on hold by the ATO

The ATO has provided some brief updated guidance on the treatment of tax debts that are placed on hold (not pursued). These will not be visible on the balance of the taxpayer's accounts, however taxpayers should receive written notification of the decision to place the debt on hold. The ATO guidance also sets out how these debts can be viewed by using online services, for both the taxpayer and for registered tax professionals.

Generally these debts will not be subject to any collection action because it is not considered economical to do so. A debt deemed uneconomical for collection action will however be re-raised at a later date if the taxpayer becomes entitled to credits, which will be applied to reduce the balance, or if their circumstances change.

Where credits arise the ATO will notify the taxpayer when a debt is re-raised to offset the credit.

More information

- Non-pursued debts

Rulings, determinations & guidance

Deferred taxation of ESS and genuine disposal restrictions

TD 2022/4

The ATO has finalised a tax ruling which looks at whether shares provided under an employee share scheme (ESS) are subject to genuine disposal restrictions.

When shares are provided to employees under an ESS and they qualify for deferred taxation it is necessary to determine when the deferred taxing point is triggered. In some cases the deferred taxing point will be triggered when there is no longer a real risk of the shares being forfeited and when the employee is no longer genuinely restricted from immediately disposing of the shares.

In order for disposal restrictions to be 'genuine' they must be sufficiently identifiable (real and objectively demonstrable), certain and legally enforceable (not spurious or hypothetical). There must be serious and enforced consequences when a breach of a scheme's disposal restrictions occurs in order for the shares to be subject to a genuine disposal restriction.

When determining whether shares are subject to genuine disposal restrictions it may be necessary to refer to the offer document relating to the ESS arrangement or other governing documents of the scheme, documented company policies and/or the taxpayer's employment contract.

Deductibility of costs incurred in establishing and maintaining an ESS

TD 2022/8

This determination explains when expenses incurred by an employer in establishing and administering an ESS can be deducted.

The determination confirms that the expenses incurred in establishing or amending the terms of an ESS are not generally deductible to the employer under section 8-1 because they are capital in nature. If the employer company is carrying on a business, these expenses should generally be deductible to the employer company over five years under the blackhole expenditure rules in section 40-880.

On the other hand, the ATO indicates that ongoing expenses associated with the administration of an ESS can be deductible under section 8-1. Ongoing expenses may include brokerage fees, audit fees, bank charges, making new offers to employees under an existing ESS and other ongoing administrative expenses.

Cases

Disclaiming an entitlement to a trust distribution

FC of T v Carter & Ors [2022] HCA 10

This case considered whether it is possible for beneficiaries to disclaim their entitlement to trust distributions after the end of an income year, with the result that they are not assessable on the income. The High Court has held that the relevant time is the end of the income year and that actions undertaken after this time cannot alter the operation of section 97 ITAA 1936.

In this case the trustee of a discretionary trust had failed to make any resolution regarding the distribution of the income of the trust for the 2014 income year. The trust deed contained a default distribution clause which was drafted to ensure that any income not appointed to beneficiaries by the end of a particular income year would be allocated to certain named beneficiaries (i.e., default beneficiaries). The trust deed was presumably drafted in this manner to ensure that no part of the net income of the trust would be assessed in the hands of the trustee at the top marginal rate.

In October 2015, the Commissioner issued amended assessments to the relevant individuals and included one-fifth of the net income of the trust for the 2014 income year in the assessable income of each of the five default beneficiaries, on the basis that they were presently entitled to that proportion of the income of the trust within the meaning of section 97.

On the 3 and 4 November 2015 three of the individuals executed deeds of disclaimer in respect of the default distributions, but these disclaimers were ineffective. These individuals subsequently executed further disclaimers in September 2016. This case considered whether the third attempt to disclaim the distributions was effective for tax purposes.

The AAT initially held that the disclaimers were ineffective because they had been made after the individuals (with knowledge) had failed to disclaim and had accepted the gits. However, this decision was overturned on appeal by the Full Court of the Federal Court. The Full Court held that there was nothing in section 97 to indicate that a beneficiary's liability was to be determined once and for all at the end of the income year by reference to the legal relationships then in existence. The Commissioner appealed the decision to the High Court.

The High Court has overturned the Full Federal Court decision and has confirmed that whether a beneficiary is presently entitled to the income of a trust needs to be determined as at the end of the income year. That is, attempts to disclaim a trust distribution after the end of the income year cannot be effective when applying the tax legislation.

With reference to the decision in the *Bamford* case, the Court noted that *"the taxation liability of the beneficiaries is determined by ascertaining the proportion of the distributable income of the trust estate to which each beneficiary is presently entitled at that point in time - just prior to midnight at the end of the year of income - and then applying that proportion to the 'net income of the trust estate'."*

That is, the question of the "present entitlement" of a beneficiary to income of a trust must be tested and examined at the close of the income year, not some reasonable period of time after the end of the year.

This decision poses a serious practical issue for beneficiaries of a trust who might not realise that they have become presently entitled to trust income. The decision also appears to be inconsistent with material published by the ATO in relation to the disclaimer of trust income entitlements, especially the comments in ATO ID 2010/85 and Trustee resolutions (QC 25912). Hopefully the ATO will issue a decision impact statement on this case shortly to explain how the ATO will be administering this area going forward.

Deductions for gym memberships

London v FC of T [2022] AATA 644

The AAT has allowed a prison dog handler to claim a deduction for gym membership costs but practitioners need to look carefully at the details of the decision before advising clients to claim fitness related costs.

The taxpayer was a dog handler who worked with the South Australian Department of Correctional Services. In the relevant income year he was responsible for training and maintaining two dogs. The taxpayer was required to be available to assist in emergencies that might arise. While these emergencies didn't arise often the taxpayer had to be prepared for the possibility of an emergency arising at any time.

In reaching the decision, the AAT noted that:

- The taxpayer was required to maintain a high degree of anaerobic fitness (including muscle strength sufficient to control a large German shepherd on a lead in a volatile situation);
- The taxpayer was required to maintain a high degree of aerobic fitness (that is, a degree of speed and agility sufficient to enable him to move effectively with, and control and direct, his dog in an emergency); and
- The taxpayer must also be prepared to restrain prisoners himself.

The AAT was satisfied that the gym memberships in the tax year in question were all taken out with a view to the taxpayer maintaining the high level of fitness necessary for his work. While the employer did not specify any particular level of fitness, a superior level of fitness was implicitly demanded by his role.

While it is normally difficult to claim the costs of gym memberships, even for taxpayers in physically demanding jobs, there are exceptions to this. There are some key points to take from this case.

First, the AAT referred to TR 95/113, an older tax ruling relating to deductions that can be claimed by police officers. In the ruling the ATO notes that fitness expenses can be claimed by a police officer if their income producing activities involve strenuous physical activities on a regular basis. The ruling states that *"members of special emergency squads, diving squads, and police officers who work regularly with police dogs and train them, may be able to demonstrate that their income-producing activities demand a high level of physical fitness."*

The AAT indicated that there was no reason why this approach should not extend to correctional-services officers who are members of Emergency Response Groups and train and control dogs.

While the ruling refers to an officer whose income producing activities involve strenuous physical activities on a regular basis, the fact that the taxpayer might rarely be called upon to exert themselves strenuously in an emergency situation should not prevent a deduction from being claimed if they are required to train dogs for such an emergency and be ready to respond to any emergency that may eventuate.

Some commentators have suggested that this decision might open the floodgates and give rise to a large number of claims being made for gym membership costs. However, it is important to note that the AAT distinguishes between regular police or correctional officers and those who are members of an Emergency Response Group. That is, the fact that someone might need to respond to a situation with physical force and speed is not necessarily sufficient to claim a deduction for fitness related expenses.

While the AAT allowed a deduction to be claimed for the gym membership expenses, the Tribunal did not allow the taxpayer to claim a deduction for gym clothing, supplements or travel between the taxpayer's home and the gym. The AAT held that these costs were private in nature and did not have a sufficient connection with the taxpayer's income producing activities.

Legislation

While all legislation before Parliament has now lapsed following the calling of the Federal election, there have been some legislative instruments released in the last month which tidy up details relating to some recent tax measures.

Tax-free status of COVID-19 grants

Income Tax Assessment (Eligible State and Territory COVID-19 Economic Recovery Grant Programs) Declaration 2020

Following the 2022-23 Federal Budget the Treasurer has issued a new legislative instrument which expands the list of COVID-19 related grants and payments from State and Territory governments which can qualify as non-assessable non-exempt (NANE) income.

An updated list of all COVID-19 grants which can qualify as NANE income can be found on the ATO website at the following link.

It is important to note that NANE income treatment can only apply if the taxpayer which receives the grant carries on a business, has aggregated annual turnover of less than $50m and must receive the grant in the 2021 or 2022 income year.

Flood disaster recovery

Social Security (Australian Government Disaster Recovery Payment—South East Queensland floods) Determination 2022 (No. 6)

This legislative instrument sets out the qualification criteria for determining whether an individual has been adversely affected by the Queensland floods in February 2022 and may potentially qualify for the disaster recovery payment.

The instrument provides that a person is taken to be adversely affected by the major disaster if any of the following circumstances apply:

(a) the person is seriously injured as a direct result of the disaster;
(b) the person is an immediate family member of an Australian who is killed as a direct result of the disaster;
(c) the person's principal place of residence has been destroyed or has major damage as a direct result of the disaster;
(d) a major asset or assets of the person has or have been destroyed or suffered major damage as a direct result of the disaster;
(e) the person is a principal carer of a child to whom paragraph (a), (b), (c) or (d) applies.

Defined benefit income streams and commutation

Treasury Laws Amendment (Allowing Commutation of Certain Income Streams) Regulations 2022

A legislative instrument has been enacted which allows the commutation of certain income streams for the purposes of meeting the superannuation transfer balance cap.

Broadly, the instrument allows a debit in the transfer balance cap account (reducing the balance) where a taxpayer receives a lump sum as a result of a capped defined benefit income stream being commuted and the lump sum is transferred directly to the purchase of a superannuation income stream of a type specified by the instrument. This offsets the credit that would arise due to the receipt.

The change allows increased flexibility in this area. Previously, taxpayers may have needed to commute their account-based income streams in order to reduce their transfer balance cap account amount.

Extending the reduction in minimum pension drawdowns

Superannuation Legislation Amendment (Superannuation Drawdown) Regulations 2022
The Government previously temporarily reduced the minimum required rates for withdrawals from pension accounts by 50% for the 2020, 2021, and 2022 income years.

These regulations extend this measure to cover the 2023 income year as well.

For example, a taxpayer aged 67 with an account-based pension would ordinarily be required to make a withdrawal of a minimum of 5% of their account balance in the income year. For 2020 - 2023 this has been reduced by 50% (i.e., to 2.5%).