Senate Standing Committee on Economics

ANSWERS TO QUESTIONS ON NOTICE

Treasury Portfolio

Budget Estimates 2012

30 May 2012

QUESTION: **BET 10**

Topic: **Trusts – evasion of creditors (ATO)**

Hansard Page: **93**

Senator CAMERON asked:

Senator CAMERON: If it is starting to appear then I am sure that there has been some analysis done as to whether this is a culture of tax evasion or avoidance of debts. It would be interesting to hear your view on that, so if you could take that on notice, as well as to the extent of the use of trusts for the purposes that I have outlined in that first question.
Can you tell us the methods by which trusts are used to minimise tax and evade creditors?
Mr Quigley: I am not sure about the evasion of creditors but, as Mr D'Ascenzo said, there is a whole range of activities through trusts and other things to try to avoid paying the correct amount of tax. Some of it is the absence of rules to prevent trafficking in trust losses, for instance. That is one. I mentioned they tried to separate the tax outcome from the business outcome. There is a whole range of strategies that we have seen.
Senator CAMERON: Could you take it on notice, then, and provide me with details of the strategies that are being used, the strategies that you are coming across in terms of tax evasion by using these trusts? I would be interested to see that.
Mr Quigley: Yes, absolutely.

Answer:

Strategies used by some trusts for tax avoidance/evasion post *Bamford* - Division 6 exploitation

While trusts may be a legitimate tax planning tool, we are particularly concerned about the emergence of arrangements that seek to exploit the manner in which trust income is taxed under Division 6 of the *Income Tax Assessment Act 1936*, as confirmed in the *Bamford* decision discussed in the answer to BET 9.

These arrangements seek to engineer a mismatch between trust income and trust taxable income. Generally it is sought to create a much reduced amount of trust income as compared to trust taxable income. This results in the beneficiary entitled to the small amount of trust income having a large tax liability. This beneficiary may have tax losses to offset against its share of the trust taxable income; or be a company with no resources to pay the liability; or be an exempt entity with no obligation to pay tax.

As noted in the answer to BET 9, the Government introduced interim law changes in 2011 that included targeted anti-avoidance rules to address some of these issues.

The Government has also announced that it will consult on options to modernise the taxation of trust income to deal with matters not covered by the interim law changes.

ATO compliance activity

Trust task force – Cross agency compliance action

A seven month joint investigation between the AFP and ATO as part of Project Wickenby has identified the largest tax fraud since that project commenced in 2006.

The case raises the trust taxing difficulties highlighted in the *Bamford* case – in addition to the application of the general anti-avoidance provision in Part IVA of the ITAA 1936 and the promoter penalty laws, the use of tax havens, and possible criminal conduct by the promoters of the arrangements.

Enquiries are ongoing and further arrests and operational activity has not been ruled out.

The ATO and AFP joint media release in relation to the case can be accessed via this link:

http://www.ato.gov.au/content.aspx?ms=corporate&doc=/content/00317822.htm

The media release by the Justice Minister can be accessed via this link:
http://www.ministerhomeaffairs.gov.au/Mediareleases/Pages/2012/Second%20Quarter/24-April-2012---$40-million-in-assets-seized-including-Rolls-Royces-yachts-a-Lamborghini-and-an-Aston-Martin.aspx

Taxpayer Alerts – Trust issues

The Commissioner has alerted taxpayers to other identified arrangements by publishing 'Taxpayer Alerts' on the ATO website. Arrangements identified in alerts issued since 2010 are summarised below:

Taxpayer Alert TA 2012/02

A New Zealand based foreign discretionary trust is used to avoid taxation on Australian sourced income. These arrangements may involve the provision of services, at a mark up, to an Australian resident business, or the diversion of Australian sourced income. The ATO is investigating these arrangements, including through Project Wickenby (see further Taxation Ruling TR 2005/14).

Taxpayer Alert TA 2011/05

An employer establishes an employee benefit arrangement for employees to acquire 'share units' in a purported employee share trust. The acquisition of share units by employees is funded by way of a loan from the trustee and that loan is repaid by the employer paying amounts which have been salary sacrificed by the employees. That is, the employees have agreed to forego part of their total remuneration that they would otherwise have expected to receive as salary or wages.

The arrangement may be an attempt by the employer to provide a benefit to employees without regard to the application of the *Fringe Benefits Tax Assessment Act 1986* (FBTAA) as the taxable value of benefits provided is not included as part of the employer's fringe benefits tax liability.

Taxpayer Alert TA 2011/02

A labour hire firm makes a discretionary trust structure available for the use of individual taxpayers for the purpose of alienating income from personal services and splitting it between the individual taxpayers who perform the services and their associates.

This arrangement attempts to circumvent the personal services income regime of Part 2-42 of the *Income Tax Assessment Act 1997* (ITAA 1997), as well as other income tax and superannuation obligations such as the Pay As You Go Withholding system and the Superannuation Guarantee, but may be ineffective under these provisions or the general anti-avoidance rules.

Taxpayer Alert TA 2011/01

A company limited by guarantee (LBG company) is established to receive trust distributions. The LBG company members and directors usually control the trust and are also beneficiaries of the trust. The distributions from the trust are loaned by the LBG company to its members and directors or their associates for minimal or no interest. The loan amounts are not returned as income by the members and directors or their associates. The stated purpose of the LBG company is to protect its assets, however the only assets held are these loans.

Taxpayer Alert TA 2010/06

A private company invests funds in an unrelated trust. The trust then on lends the funds to a shareholder, or an associate of a shareholder, of the private company. This arrangement may be an attempt by the shareholder or associate to access funds of the company without due regard to the application of Division 7A of Part III of the ITAA 1936.

Taxpayer Alert TA 2010/05

A self-managed superannuation fund (SMSF) invests funds in an unrelated trust. The trust then on lends the funds to an SMSF member or a relative of the member.

This arrangement attempts to circumvent the prohibition on SMSF trustees lending money or providing financial assistance to a member or a relative of the member using the resources of the fund (see also SMSFR 2008/1).