BNR PARTNERS
ESTATE & TRUST TAXATION SPECIALISTS

PO Box 1337
Waverley Gardens VIC 3170
estates@bnrpartners.com.au
32/830 Princes Highway
Springvale VIC 3171

Melbourne 03 9781 6800
Adelaide 08 7221 9750
Brisbane 07 2101 5390
Perth 08 6323 5480
Sydney 02 9131 4270

Karen Rooke
Tax Counsel Network
Australian Taxation Office

26 August, 2024

By email: karen.rooke@ato.gov.au
cc: Amy James-Velagic@ato.gov.au

Dear Karen,

Consultation on draft Taxation Determination TD 2024/D2

Thank you for the opportunity to provide feedback on draft Taxation Determination TD 2024/D2 (about the application of section 99B of the ITAA 1936).

BNR Partners is an accounting practice that specialises in the taxation of deceased estates. We see the application of section 99B as one of increasing relevance to us and those solicitors we advise. In that regard, guidance on the application of the section is welcomed.

We note too that in the changing tax practitioner environment, there will be a growing demand for ATO advice and guidance in areas such as this. People will often need to know how the ATO considers that the law applies in order to decide whether to refer themselves or others to the TPB.

We and others have previously lobbied the government, Treasury and the ATO to change the law so that deceased estates would be treated as having the same tax residence for Australian tax purposes as the deceased individual (as is the case in the United Kingdom). This would produce results that are more consistent with the intended policy behind the CGT treatment of gains and losses resulting from the death of an individual. This is especially true where an Australian resident deceased appoints a foreign resident LPR (or where there might be a change of trustee of a deceased estate from resident to non-resident). In particular, such a law change would avoid the application of section 99B in these cases. We ask that you raise this recommendation with Treasury and government.

Ruling

The draft PCG (paragraph 7) makes it clear that the ATO will apply section 99B to certain resident trusts. We recommend that this be made clear in the TD too especially as the TD constitutes ‘advice’ rather than ‘guidance’.

Examples 1, 2 and 3 deal with cases where the trustee has sold trust assets and distributed the proceeds of sale. It would be useful if you could explain in the ruling section how section 99B might apply if the trust asset itself is transferred to a beneficiary.

People might infer from the current examples that the ATO view is that section 99B does not apply to in specie distributions. It's not until paragraph 51 that there is a reference to an asset being distributed. This should be spelt out clearly in the Ruling section.

Could you please explain (including by way of a deceased example) what meaning the ATO gives the term 'derived' in paragraphs 99B(2)(a) and (b) in the context of an unrealised capital gain? In the context of the distribution of an asset, are you suggesting that 'derived' is broad enough to encompass a notional capital gain based on deemed capital proceeds.

We have struggled a little with the separate points being made in paragraphs 4 and 5. We have discussed our understanding of what is being said under Example 1.

Example 1

We understand this to be saying that the hypothetical taxpayer can disregard an amount attributable to a capital gain from a pre-CGT asset as that exemption applies to any type of taxpayer that is a resident. Conversely payments that may be attributable to the CGT discount component of a capital gain are assessable under section 99B to a resident beneficiary because you can't assume that the hypothetical taxpayer is an entity entitled to apply the discount.

In our area of practice, we think that the effect of the hypothetical taxpayer test is that it cannot be assumed that they are a trustee of a deceased estate. This is important in the context of applying the main residence exemption in section 118-195 of the ITAA 1997.

For example, a foreign LPR acquires a resident deceased's dwelling in Australia and sells it outside of the two-year period provided for in the legislation. The sale proceeds are distributed to a resident beneficiary. As nothing about the status of the hypothetical taxpayer (apart from its residence) is to be assumed, it cannot be assumed that they are the trustee of a deceased estate. This means that the distribution of an amount attributable to a gain for the period after the taxpayer's death will be subject to section 99B on distribution. [Presumably, any market value step-up under item 3 of the table in subsection 128-15(3) of the ITAA 1997 goes to your other point about the circumstances that gave rise to the capital gain. That is, the entire capital gain from the dwelling is not subject to tax under section 99B.]

Whether or not we have understood correctly, this would be a useful example to add to the TD to show how the principles apply and the provisions interact.

If our understanding is correct, this is an important issue. Without a law change along the lines of that discussed above, legal practitioners will be exposed to the risk of litigation for failing to draw the issue to the attention of clients when drafting a Will.

Example 2

We suggest that in this example, you change the facts so that the deceased was a resident who appointed their non-resident child as executor of their estate. In our experience, this is a more common scenario than the one you have raised, or at least one where people fail to appreciate that section 99B potentially has application. It would also be useful to add that the central management and control of the trust was not in Australia at any time.

We assume that the deceased died relatively recently in which case the reference to the 1991 acquisition date for the shares is misleading in the context of the current facts. Item 3A in the

table in subsection 128-15(4) of the ITAA 1997 operates with respect to CGT events (deaths) that happened after the day on which T*axation Laws Amendment (2006 Measures No4) Act* received Royal Assent. So, if a non-resident died after that time, their LPR would obtain a market value acquisition cost. [If you take up our suggestion to make the deceased a resident, then the 1991 acquisition date is relevant.]

Paragraph 11

Suggest saying devolved to their legal personal representative (as per legislation). It is not clear to us how the provisions might apply in civil jurisdictions where there is no representative who administers the estate. Though it is a legal question, we understand that in some counties the assets pass directly to beneficiaries.

Suggest deleting the word 'executor'. This is already covered by the reference to legal personal representative.

Paragraph 12

Again, we suggest that you say that the shares were acquired by the LPR (rather than the deceased estate) and replace 'trustee' with 'LPR' to avoid any confusion as to whether trustee was meant to mean something different from LPR (that is, the LPR acting in their capacity as trustee).

Further example

We suggest adding another example to highlight the interaction of the corpus exception and the exception in paragraph 99B(2)(c) for prior taxed amounts. The facts that we often have to deal with and which we would like clarified are as follows.

Resident deceased, non-resident LPR. Sells a property in Australia. Tax is paid on the discounted capital gain in the current year under section 97 or 99. The LPR then distributes the discount component to the beneficiary. Does an exemption apply? Does it make any difference if the beneficiaries were assessed because they were made specifically entitled to the whole of the financial benefit attributable to the gain before discount?

At a more granular level (and this may go to the source of the distribution), assume that there is only one estate asset. It is sold for $150,000. The gain before discount is $100,000 and the LPR paid tax of $25,000 on the post-discount gain.

There is $110,000 left to distribute after payment of tax and other expenses that could not be included in cost base. Can the LPR take the approach that the amount being distributed represents the cost base of the asset ($50,000- not subject to 99B), the taxed capital gain ($50,000 – not subject to 99B) and the discount component ($10,000- which may be taxable under 99B depending on your view).

Source of the distribution

As the PCG acknowledges, this is going to be very problematic for beneficiaries particularly where there have been many injections and outgoings of trust capital from different sources over the life of a trust and all funds have been intermingled (particularly as many non-resident trustees would not have been aware of the possibility of Australian tax issues).

The ATO should indicate some approaches that it might accept to assist trustees and beneficiaries deal with this problem.

For example, does the ATO accept that section 99B would not apply in the following circumstances. A foreign trust has a contributed capital account of $1m, it received a dividend of $200,000 which was credited to a different account. The trustee made a capital distribution of $200,000 to a resident beneficiary by debiting the contributed capital account.

Or does the ATO regard all of the $200,000 as assessable under s99B on the basis that distributions firstly represent assessable amounts before any others? Alternatively, would the ATO regard $33,333 as assessable on the basis that it is attributable as to one-sixth of assessable sources and as to five-sixths non-assessable sources (a pro-rata approach)?

As ever, BNR Partners would welcome the opportunity to discuss issues raised in this submission. Nuances are often lost when reliance is placed solely on written comments and the approach you decide to take in respect of a particular issue may generate further issues that do not benefit from consultation. A free-flowing exchange of ideas will generally result in a better product.

Yours sincerely

Ian Raspin TEP, FCPA, FCA, CTA
Managing Director