Family tax benefit: child income

SECRETARY TO THE DFaCS and TOUGH
(No. 2002/1212)

Decided: 22 November 2002 by S. Forgie.

The issue

The critical issue in this matter was whether Tough was entitled to family tax benefit (FTB) in the period July 2000 to April 2001. In this period she received a total of $1732 in FTB, which Centrelink sought to recover from her. The SSAT in November 2001 determined that no debt of FTB was owing, and Centrelink subsequently waived $1000 of the debt amount, but sought review of the SSAT decision in relation to the balance of $732.

Background

Tough was in receipt of FTB in the 2000–2001 year, and was being paid her entitlement by instalments. It was not in dispute that Tough met the formal criteria for eligibility for FTB during the period in question, in that she had two sons Steven and Brent in her care who were under the relevant age limit. Both sons earned income during the relevant year. On or about 16 January 2001 Steven's income exceeded the relevant FTB income threshold, and similarly Brent's income exceeded the threshold on or about 18 April 2001. In both instances Tough advised Centrelink on or about these dates of her sons' income situations.

The SSAT view was that Tough was not entitled to any FTB once her children exceeded the income limit. However, as she had promptly notified Centrelink once that limit was reached, and FTB payments were then cancelled, the SSAT determined that she did not incur a debt in respect of FTB payments already received by her. The Centrelink view was that FTB was a benefit paid annually and that once the relevant income threshold was exceeded the whole of the payment amounts must be reviewed.

The legislative requirements

The Tribunal carefully considered the use and meanings of the terms 'entitled' and 'eligible', both of which are used in various connotations in the relevant legislation — *A New Tax System (Family Assistance) (Administration) Act 1999* (the FAA Act), and related legislation. The Tribunal noted the dictionary definitions of 'eligible' to include 'fit or entitled to be chosen for a position, award etc.' and of 'entitle' to include 'confer on a person a rightful claim to something or a right to do it …'

The Tribunal concluded that the decision that a person is ineligible for FTB did not necessarily mean that he or she was not entitled to FTB for the whole of the relevant year. The separate use of the terms 'entitle' and 'eligible' in the legislation meant that each must be separately considered. First, the criteria necessary to determine whether or not a person is an appropriate person to receive FTB (for instance, whether the person concerned had an appropriately aged child) must be considered (ie eligibility), after which the question of whether FTB will actually be paid to that person depends on satisfaction of such requirements as the making of an appropriate claim and provision of any required information (ie entitlement). Once a determination is made that a person is entitled to FTB, that determination remains in force until another determination is made in its stead.

The Tribunal concluded that in respect of FTB there were two categories of decision on which a change in FTB could be based — essentially, either by the making of a new determination, or by review of an earlier determination.

First, s.31 of the FAA Act provides that where a person is receiving FTB by instalments and an event occurs which would cause Centrelink to determine that the person was no longer eligible for FTB, then Centrelink must make a fresh determination that the person is no longer entitled to FTB from the date of the event or occurrence. In Tough's situation, the only such events that occurred after she commenced receiving FTB by instalments, were when her sons' taxable incomes exceeded the relevant income threshold, at which points each ceased to be an FTB child (and so, too, she ceased to be 'eligible' for FTB). The date of effect of the varied determination was the date on which the sons' income exceeded the relevant threshold. It followed from this view, that Tough's entitlement to FTB did not cease until the dates on which her sons' income levels exceeded the threshold, and any debt could only arise in respect of payments received after those dates.

However, the Tribunal noted that a second basis for reviewing eligibility for FTB was provided in s.105 of the FAA Act, which allows for review of an earlier determination when '… the Secretary is satisfied that there is sufficient reason to review the decision'. The Secretary may, consequent upon such a review, decide to affirm, vary or substitute the original decision with a new one, which then takes effect from the date of the original decision. The power to review the whole period of eligibility, and so entitlement for the whole period, was consistent (the Tribunal noted) with other provisions in the FAA Act and related legislation which allowed for a person to apply for FTB in respect of a past period.

Following this line of argument, the Tribunal noted that neither of Tough's children could be an FBT child at a 'particular time' if the child's taxable income exceeded the relevant cut off amount for '… the income year in which the particular time occurred …' (s.22A of *A New Tax System (Family Assistance) Act 1999* (the FA Act)). Having regard to the income earned by Brent and Stephen, which exceeded the required thresholds, the Tribunal concluded that —

> … at no particular time in that year, could [Brent] be an FBT child of Mrs Tough. As [he] could not be an FBT child at any time during the financial year, Mrs Tough was not entitled to FBT for any period during the financial year …

(Reasons, para. 42)

Formal decision

The Tribunal set aside the SSAT decision and determined that the amount of FTB paid to Tough during the period in question was a debt to the Commonwealth.

[P.A.S.]

Testamentary trusts: attributable income and assets

SECRETARY TO THE DFaCS and COCKS
(No. 2002/1179)

Decided: 1 November 2002 by J. Handley.

Background

Cocks was a beneficiary of her father's will. When he died he left all chattels to Cocks, the balance of his estate to be held on trust, with the income from the estate to be paid to Cocks during her lifetime.

The will also provided that if this income was insufficient the trustee would have the discretion to apply the 'corpus' for her 'maintenance, benefit, welfare and comfort' during her lifetime. The

Trustees were to hold property on trust and divide it between the surviving children of Cocks.

The Department attributed the assets of the estate to Cocks and decided that the allowable assets limit had been exceeded and consequently cancelled parenting payment.

The SSAT set aside this decision, concluding that Cocks was not an attributable stakeholder and therefore the assets of her fathers' estate should not be attributed to her under s.1208E (1) of the *Social Security Act 1991*.

The issues

The issues in dispute in this appeal were whether Cocks satisfied the control test, whether she was an attributable stakeholder and, if so, what the appropriate asset and income attribution should be.

The facts

Cocks received income from three sources: parenting payment, casual work and income from the trust.

Cocks lived in the house of her father which was registered in the name of the trust. She paid no rent or rates, but paid for utilities. The trustee was Perpetual Trustees.

Cocks had, over the years, applied for various payments from the trust and the trustee confirmed that payments were permitted for unusual or extraordinary expenses. Some of these applications had been successful, some not, for example, an application made in March 2002 for income to supplement annual expenses was rejected.

The trustee gave evidence that it was bound to ensure that Cocks did not suffer hardship, however the trustee was also obliged to preserve capital of the trust for the ultimate beneficiaries.

Submissions

The submission on behalf of the Department was that the policy underlying the new legislation was to avoid situations where persons established trusts to conceal their assets. In this case it was submitted that where resources were available to maintain a person, those resources should be used rather than taxpayer funds.

It was submitted that because Cocks is the sole beneficiary during her lifetime, and she has access to trust income and assets, then 100% of the assets should be attributed to her.

The Department argued that Cocks satisfied the control test because the aggregate of her beneficial interest in the capital income of the trust was 50% or more.

On this point, it was argued on behalf of Cocks that s.1207V(2)(d) required a beneficial interest in 50% of the entire trust, not 50% of the income.

It was further argued that Cocks was not an attributable stakeholder as set out in s.1207X(2) as the relationship between Cocks and the Perpetual Trustees was far removed from the relationship between a beneficiary and trustee. It was argued that Cocks had no guarantee that payments would be made other than by way of income.

Findings

The Tribunal found firstly that the trust was a designated private trust and a controlled private trust within the meaning of ss.1207P and 1207V.

The Tribunal found that Cocks satisfied the control test as she held an aggregate of 50% or more of the beneficial interest in the corpus of income of the trust (s.1207V(2)(d)).

Consequently, the Tribunal found that Cocks was an attributable stakeholder, unless determined otherwise by the Secretary.

The basis for making a decision that a person is not an attributable stakeholder is set out in the *Attribution Principles*. A finding that the attribution percentage is less than 100% is also decided on the basis of these principles.

Principle 6 states that the decision maker must consider:

> the effect of one or more of the circumstances mentioned in this part in relation to the individual and the company or trust provides a sufficient basis on which to determine that the individual is not an attributable stakeholder of the company or trust.

The Tribunal found that not all the guidelines set out in principles 7–13 need apply. It found that:

Cocks had received all income from the trust and some payments of capital (principle 9);

It was foreseeable that all future income and some payments of capital would be made in the future (principle 10);

Cocks lived in the home which was owned by her father rent-free and therefore derived benefit from the assets of the trust (principle 11);

- Cocks was not an attributable stakeholder in relation to any other company or trust (principle 12); and
- Cocks had made no contributions to the trust (principle 8).

The Tribunal then considered in detail Principle 7:

> **7. Circumstances affecting relationship with company or trust**
>
> (1) The Secretary must consider whether there are relevant circumstances that make it inappropriate for the individual to be an attributable stakeholder of the company or trust.
>
> (2) For subsection (1), **relevant circumstances** include the extent to which the relationship between the individual and the company or trust is affected by any of the following circumstances:
>
> (a) circumstances arising from the legal structure of the company or trust;
>
> (b) circumstances arising from the administrative arrangements of the company or trust;
>
> (c) whether, having regard to the relationship between the individual and the company or trust, the individual can reasonably be expected to exercise effective control in relation to the company or trust.

The Tribunal considered the meaning of 'effective control'. Referring to the Penguin Macquarie dictionary it found the word 'effective' defined as 'serving to effect the purpose; producing the intended or expected result'. The word control is defined at s.1207A as follows:

> Control includes control as a result of, or by means of, trusts, agreements, arrangements, understandings and practices, whether or not having legal or equitable force and whether or not based on legal or equitable rights.

The Tribunal found that Cocks had some effective control by way of her role as the beneficiary. This included her ability to enforce the rights to be paid income, enforce her rights to acquire chattels and assert her right to be paid capital for her welfare and comfort. A failure by the trustee to comply with the first two of these rights would give Cocks rights against the trustee. The Tribunal found that this was 'effective control' because 'the purpose of the trust is "effected" and Cocks can exercise "control" within the above definition'. (para 82).

The Tribunal conceded that there were competing arguments that Cocks could reasonably be expected to effectively control the trust however it referred to principle 6(3) which requires consideration of:

> whether the effect of one or more of the circumstances mentioned in this Part, in relation to the individual and the company or trust, provides a sufficient basis on which to determine that the individual is not an attributable stakeholder of the company or trust.

In an overall assessment of the relevant principles, the Tribunal found that

Cocks satisfied principles 9, 10 and 11 and Cocks had a continuing entitlement to benefit from the trust which should be considered in the context of principle 13.

In essence, the Tribunal found that:

> Cocks cannot in my view exclusively receive all income from the capital assets of the trust but deny attribution of those assets. To decide otherwise would also be contrary to the applicable legislation and its intent and the policy of Government which did receive parliamentary scrutiny (refer Drake) (para. 85).

The Tribunal in effect placed the burden of proving that the principles did not apply on Cocks by stating that it was 'not satisfied that Cocks had been able to demonstrate a sufficient basis on which to determine that she was not an attributable stakeholder'. Similarly the Tribunal could not find any basis for reducing the attribution percentage to an amount less than 100%. It found that 100% attribution was required because Cocks was the sole beneficiary of the trust.

Formal decision

The AAT set aside the decision and substituted its decision that Cocks was an attributable stakeholder of the trust and had an income and assets attribution percentage of 100%.

[R.P.]

Loans to trusts: attributable income

BACKER AND SECRETARY TO THE DFaCS
(No. 2002/1335)

Decided: 24 December 2002 by R.G. Kenny.

Background

Mr and Mrs Backer were receiving age pension when the Department decided to reduce their rate of pension under the new trust legislation. This decision was affirmed by the Social Security Appeals Tribunal.

Mr and Mrs Backer were directors of the trustee company for the Backer Family Trust. They each held a 35% shareholding in the company and were the primary beneficiaries.

The balance sheet showed, amongst other things, beneficiary loan accounts of $130,025.43 in the name of Mr and Mrs Backer. This amount represented money received when they sold a nut farm and paid proceeds into the trust for investment purposes.

The Department decided that the trust was a designated private trust and that Mr Backer was an attributable stakeholder with an attribution percentage of 100%. The loans made by Mr and Mrs Backer to the trust were treated as financial investments and the income of the trust was attributed to Mr Backer. This reduced the rate of pension payable to them.

The issue

The issue in dispute in this appeal was whether the moneys paid by Mr and Mrs Backer into the trust, and recorded in the beneficiary loan accounts, were loans under the Act. If they were, should the Backers be subject to the attributed income legislation and subject to the income deeming rules?

Submissions

Mr and Mrs Backer's argument was that the Department's decision 'doubled up' the amount that the Department took into account as income for the purposes of the income test. They said that the trust had been established as a vehicle to sell the nut farm. Proceeds were paid into the trust and they constituted Mr and Mrs Backer's money, rather than a loan to the trust. They said that the purpose of this was to generate capital so they would not have to rely on income support payments.

Mr and Mrs Backer ultimately conceded that the moneys paid into the loans were treated as loans for taxation purposes and that there was a taxation advantage to the moneys being placed in the trust. However they argued that this did not reflect the real character of the moneys. They said that they made the loans under duress as Centrelink had told them that if they had not taken this action the money would be treated as assets.

The Department argued that the moneys provided to the trust were loans and therefore financial assets under the Act. Consequently legislation allows for the attribution of the trust income.

Findings

The Tribunal found that the proceeds of sale of the farm were paid to the trust and treated as loans for taxation purposes. As the loans had not been repaid they were a financial investment, and consequently a financial asset (see s.9(1)).

Subsections 1077 (3) and (3A) then have the effect of deeming income on this asset. In this case an amount of $5488.47 was deemed income for both Mr and Mrs Backer.

The Tribunal then went on to consider the effect of the new trust legislation which commenced operation on 1 January 2002.

The Tribunal was satisfied that the trust in this case was a designated private trust (s.1207(1)). Mr Backer was found to satisfy the control test (s.1207V(2) as the trustee company was an associate of Mr Backer (s.207C(1)) and sufficiently influenced by him.

Under ss.1207X(2) Mr Backer was an attributable stakeholder of the trust unless the Secretary decided otherwise. The Tribunal concluded that this was the case and that his income attribution percentage in relation to the trust was 100%. Consequently under s.1207Y the income of the trust was attributable to Mr Backer. As the trust's net profit for the relevant financial year was $15,216, this amount was attributed to Mr Backer as part of his ordinary income.

The Tribunal went on to consider excluded income as provided for in ss.1207Y(2) to (4) and the Social Security (Attribution of Income) Principles 2002. These principles apply in circumstances where there has been a distribution to the beneficiary of the trust or transfer of capital of the trust. This was not the case in this appeal.

The Tribunal concluded that the ordinary income of Mr and Mrs Backer included both the deemed income and the attributed income. The Tribunal noted Mr and Mrs Backer's concern that the legislation operated unfairly in this case, but stated that the legislation is clear in its application and referred to ss.1207Y(1)(e) which requires that attributed income be considered in addition to any other ordinary income of the individual.

Formal decision

The AAT affirmed the decision of the SSAT.

[R.P.]