TWO SURPRISING DECISIONS ON COMMISSIONER'S POWER TO AMEND

Often the Commissioner finds himself outside the 2, 4, or 6 year periods in which he can amend an assessment.

The normal amendment period under s170 is 4 years, except where an individual taxpayer's affairs are "simple" in which case the amendment period is 2 years, or where the general anti-avoidance provision (Part IVA) applies, in which case the amendment period is 6 years.

Most tax practitioners have had the experience of the Commissioner asserting that the taxpayer has been involved in "fraud or evasion", in order to justify the issue of amendments outside the period which would otherwise apply.

"Evasion"

The case law on what is "evasion" for those purposes, is long standing[1], and while simple enough to express ("the taxpayer was involved in some blameworthy act" - which would usually be less than would constitute a crime), it can be difficult to apply in the self assessment context, where there is no obligation on the taxpayer, unless asked, to make a "full and true disclosure", which was the position when the case law test was formulated[2].

Prior to 1992, s170(2) required the taxpayer to make a "full and true disclosure of all material facts" necessary for his assessment. Since 1992, the taxpayer lodges his return by providing the figures in the boxes on the return, or answering questions yes/no, needing to make up his own mind on the application of the law to his facts, rather than providing all his material facts to the Commissioner.

In *Fitzroy Services Pty Ltd v FC of T* [2013] FCA 471 the Federal Court relied on the criminal law definition of "evasion" as expressed by Gleeson CJ in *R v Meares* (1997) 37 ATR 321 at 323, to find that the Commissioner was out of time to amend the taxpayer's 2005 assessment, without reference to the case law on the concept of "evasion" as has been found in relation to amendment periods. In *Meares* it was said:

1."Evasion" for the purposes of s170 has be held to occur where there is income omitted due some "blameworthy act" where there is "no credible explanation for the income's omission": *Denver Chemicals Manufacturing Co Ltd v Commissioner of Taxation (NSW)* (1949) 79 CLR 296; *Barripp v Commissioner of Taxation* (1941) 6 ATD 69. However, the omission may not be accompanied by sufficient intent, to be proved to be a crime at the criminal burden of proof. That is, in the expression "fraud or evasion", the meaning of "evasion" is something less than "fraud".

2 There are penalties for not taking "reasonable care" in lodging a return. However, a taxpayer who does not seek a private ruling on a contentious issue will not necessarily have lacked reasonable care: *MLC Limited v FCT* (2002) 51 ATR 283 at [40]-[54], and *North Ryde RSL Country Club Ltd v FC of T* 2002 ATC 4293.

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> "If the parties to a scheme believe that its possibility of success is entirely dependent upon the revenue authorities never finding out the true facts, it is likely to be a scheme of tax evasion [criminal], not tax avoidance [not criminal]."

Accordingly, long standing law is that the "evasion" carried out by the taxpayer in order for the Commissioner to amend an assessment at any time, is a lower threshold than is required to constitute a crime.

Whilst it is expected that the Commissioner would be likely to appeal, if that happens there will be an opportunity for a Full Court for a proper consideration of what is "evasion" in the self assessment context, which has not happened so far for some reason[3].

Beneficiary of a trust

The 2 year amendment period for individual taxpayers with "simple" tax affairs, was introduced in recent years. In order to be regarded as having "simple" tax affairs, the taxpayer must not be carrying on a business; be a member of a partnership, or be a "beneficiary" of a trust[4].

In *Yazbek v FC of T* [2013] FCA 39 the Federal Court confirmed the AAT decision [2012] AATA 477 that the taxpayer was a "beneficiary" of a trust, in circumstances where he had not received a distribution or loan from the trust in the year of income, or apparently at any previous time[5]. The Commissioner simply relied on the fact that he was in law, a "mere discretionary object" of a trust[6], to issue an amended assessment to include apparently unrelated income[7], outside the 2 year period.

As the Court found, it is the case that the word "beneficiary" of a trust is used in various places in the tax law, for different purposes, so the context in which the word is used governs the meaning it takes in that context. However, the Court did not find it necessary to "read down" its meaning in the context of amendment periods to situations where the taxpayer who was a "mere discretionary object" had in fact received at some time, a distribution or even a loan from such a trust, or had some control over the trust's affairs.

In dealing with the submission for the taxpayer that an individual could have a 4 rather than 2 year amendment period, because they were a "mere discretionary object" of someone else's trust without being so aware, the Court noted without comment, that the AAT had said that the taxpayer, on becoming so aware, could disclaim their interest in such a trust. The AAT said such a disclaimer

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[3] There have been no reported cases where it was argued that the meaning of "evasion" has now to be viewed in the context that the law changed in 1992 to introduce self assessment. As a result, recent cases have seen *Denver Chemicals* as the end of the matter: e.g. *Weyers v FC of T* [2006] FCA 818; AAT case [2005] AATA 622; *R&D Holdings Pty Ltd v FC of T* [2006] FCA 981; and *Kajewski v FC of T* (2003) 52 ATR 455.

[4] Unless the business, partnership or trust was a "small business entity".

[5] Neither the Court nor the AAT referred to what might have happened in earlier years, and could have been expected to refer to that, if it was indeed the case.

[6] Albeit it was in this case, a trust related to his family.

[7] Neither the Court nor the AAT specified what the nature of the income was.

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would apply retrospectively, and referred at [72] to *FC of T v Ramsden* [2005] FCAFC 39 at [30]. However, whilst the disclaimer of an entitlement to income, may mean that they were never entitled to that income, but would not retrospectively mean that they weren't a "beneficiary" e.g. in relation to capital, at an earlier time, so as to allow the Commissioner to use the 4 rather than 2 year period.

Given that it is very common for family discretionary trusts to have very wide classes of "mere discretionary objects", the Court's decision in practice makes it quite possible one can never be certain that the 2 year limitation period should apply. What level of enquiry would constitute "reasonable care" to determine whether a taxpayer is a "mere discretionary object" of someone else's trust? The decision has been subject to criticism in "Taxation in Australia"[8].

Care should be taken in drafting objections to ensure the argument is made that the Commissioner's amended assessments may be out of time. Correspondingly, care needs to be taken that an objection is made within the applicable time limits.

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If you find this article of interest, feel free to forward to a colleague.

[8] "Beneficiary" by TaxCounsel Pty Ltd Vol 47(8).