

2010

**EXPOSURE DRAFT**

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**EXTENDING THE TAX FILE NUMBER WITHHOLDING ARRANGEMENTS TO  
CLOSELY HELD TRUSTS, INCLUDING FAMILY TRUSTS**

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**EXPLANATORY MATERIAL**

(Circulated by the authority of the  
Treasurer, the Hon Wayne Swan MP)



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# **Chapter #**

## ***Extending the tax file number withholding arrangements to closely held trusts, including family trusts***

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### **Outline of chapter**

1.1 Schedule 1 of the exposure draft amends the taxation law to extend the existing rules for tax file number (TFN) withholding to closely held trusts, including family trusts. The effect of these changes will be to allow the Australian Taxation Office (Tax Office) to better align the information obtained from trustees with the amounts reported by the trust's beneficiaries. Additionally, this measure will allow the Commissioner of Taxation (Commissioner) to check whether the assessable income of beneficiaries of these trusts correctly includes their share of the net income of the trust.

1.2 All references to legislative provisions in this chapter are references to the *Taxation Administration Act 1953* (TAA 1953) unless otherwise stated.

### **Context of amendments**

1.3 In the late 1990's it became apparent that complex chains of trusts were being used to avoid or indefinitely defer tax. In order to address this issue, legislation was passed to require a trustee of a closely held trust to advise the Commissioner of certain details about a trust's ultimate beneficiaries and tax-preferred distributions to beneficiaries. Failure to do this, or there being no ultimate beneficiary, rendered the trustee liable to pay an 'ultimate beneficiary non disclosure tax' at the top marginal tax rate plus Medicare levy.

1.4 The purpose of that measure was to allow the Commissioner to check that the assessable income of ultimate beneficiaries correctly included their share of trust income and that the net assets of ultimate beneficiaries reflected their receipt of tax-preferred amounts.

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1.5 This measure proved to be very difficult to comply with for some trustees of closely held trusts. Consequently, from the 2008-09 income year, new rules applied requiring that the trustee of a closely held trust report information to the Commissioner in respect of each beneficiary that is itself a trustee entitled to a share of the trust's net income or to receive tax-preferred amounts.

1.6 However, these new reporting requirements don't apply in respect of individuals or companies, or to family trusts that have made a family trust election under the trust loss provisions in Schedule 2F to the *Income Tax Assessment Act 1936* (ITAA 1936).

1.7 Consequently, as part of the 2009-10 Budget, the Government announced that, with effect from 1 July 2010, it would extend the current TFN withholding arrangements to closely held trusts, including family trusts. This would then ensure that the assessable distributions received by beneficiaries of those trusts aligned with the amounts included by those beneficiaries in their income tax returns.

### Summary of new law

1.8 Schedule 1 of the exposure draft extends the TFN withholding regime under Subdivision 12-E of Schedule 1 to the TAA 1953 to closely held trusts (including family and related trusts) who make assessable distributions to beneficiaries to which these amendments apply. Assessable distributions to those relevant beneficiaries who fail to quote their TFN to the trustee of the trust prior to the trustee making the distribution, will be subject to TFN withholding.

1.9 There are four stages to the operation of these amendments where a relevant beneficiary has failed to provide their TFN to the trustee.

- The first stage imposes a withholding obligation on the trustee when an assessable distribution event occurs.
  - The trustee is required to withhold from the assessable distribution prior to making the payment or when the beneficiary is presently entitled to the amount.
- The second stage involves reporting and remitting those amounts withheld to the Commissioner.

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- The trustee is required to register for pay as you go (PAYG) withholding with the Tax Office as well as report and remit amounts withheld on an annual basis.
- This includes reporting amounts distributed on an annual basis even where no amounts have been withheld in accordance with these amendments.
- The third stage involves the crediting of the amounts withheld by the trustee, to the eligible beneficiary on assessment of their income tax liability.
- The final stage involves penalties imposed on the trustee for failing to withhold and/or failing to remit the amount withheld to the Commissioner.
  - These penalties exist in the current TFN withholding framework and apply in the same manner under these amendments.

1.10 Where a beneficiary has provided their TFN to the trustee prior to the trustee making an assessable distribution, they are not subject to the TFN withholding framework.

1.11 The trustee is required to report the TFNs quoted by the beneficiaries to the Commissioner in the approved form. The trustee is only required to report the quoted TFN once (upon validation of it being the correct TFN) and will report the TFNs collected in a quarterly report. Where the trustee has no new TFNs to report, they are not required to lodge the report.

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### Comparison of key features of new law and current law

<i>New law</i>	<i>Current law</i>
From the 2010-11 income year, trustees of closely held trusts (and family and related trusts) must withhold amounts from assessable distributions where beneficiaries covered by this measure fail to quote their TFN to the trustee prior to the trustee making assessable distributions.	No equivalent.
Trustees of trusts subject to these amendments are required to report and remit amounts withheld under TFN withholding on an annual basis. Trustees are also required to report all amounts distributed (or due because present entitlement has arisen) to beneficiaries on the same report even where there have been no amounts withheld.	No equivalent.
Eligible beneficiaries who have had amounts withheld under these amendments are able to claim a credit for amounts withheld in their annual tax return.	No equivalent.
Trustees of trusts subject to these amendments are required to withhold and remit amounts withheld to the Commissioner or face administrative penalties for failing to withhold and or remit an amount withheld.	No equivalent.
Trustees of trusts subject to these amendments are required to report to the Commissioner any TFNs quoted by their beneficiaries on a quarterly basis.	No equivalent.

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### Detailed explanation of new law

#### Scope of these amendments

1.12 The current arrangements for TFN withholding apply to various relationships including employer/employee, investment body/investor and superannuation provider/superannuant. In the context of trusts, TFN withholding in respect of investments applies to widely held unit trusts and applies to all classes of beneficiaries.

1.13 Schedule 1 of the exposure draft extends the TFN withholding arrangements to closely held trusts, including family trusts. The scope of these amendments is broadly intended to cover all beneficiaries of those trusts. However, there are distributions to certain trusts and beneficiaries that are excluded from this measure.

#### *Trustees and trusts subject to this measure*

1.14 These amendments apply to distributions by trustees of closely held trusts, including family trusts. Closely held trusts are defined in subsection 102UC(1) of the ITAA 1936 and includes a trust that:

- has up to 20 beneficiaries who have fixed entitlements to a 75 per cent or greater share of the income, or a 75 per cent or greater share of the capital, of the trust; or
- is a discretionary trust.

*[Schedule #, item 6, subsection 12-175(1)(b)]*

1.15 The current definition of closely held trusts does not include 'excluded trusts'. Excluded trusts include complying superannuation funds, complying approved deposit funds, pooled development funds, deceased estates or fixed trusts where exempt entities have fixed entitlements.

1.16 The definition of closely held trusts also explicitly excludes family trusts (including trusts covered by a family trust election, which includes those with an interposed entity election or wholly owned by the family trust or family group).

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1.17 However, under these amendments, trustees of family trusts including those covered by a family trust election are specifically included within the scope of these amendments. *[Schedule #, item 6, subparagraph 12-175(1)(b)(ii)].*

1.18 For the purposes of this explanatory material, all references to family trusts are intended to mean family trusts and the trusts covered by a family trust election. These trusts include those with an interposed entity election or wholly owned by the family trust or family group and meet the definition within paragraphs (d) and (e) of the definition of excluded trust in section 102UC of the ITAA 1936.

### *Trustees and trusts excluded from this measure*

1.19 These amendments do not apply to trustees of trusts that are not a closely held trust or a family trust. In addition, closely held trusts or family trusts that are not Australian residents are also excluded from this measure. *[Schedule #, item 6, subparagraph 12-175(1)(b)(i)]*

1.20 Investment bodies and unit trusts that fall within the operation of sections 12-140 and 12-145 of Subdivision 12-E of Schedule 1 to the TAA 1953 are not subject to these amendments. This is because they are already subject to rules that apply for TFN withholding in respect of investments. *[Schedule #, item 6, Note 1 under subsection 12-175(2)]*

1.21 In the situation where a trust could be subject to both the TFN withholding rules in respect of investments and under these amendments, the rules in respect of investments will take precedence. *[Schedule #, item 5, subsection 12-5(2) (table item 5, column headed "in priority to:")]*

### **Example 1.1**

The Newman trust is a closely held unit trust and has ten beneficiaries (five of which are individuals and five are companies). Beneficiaries A, C, H and I have failed to provide their TFN prior to becoming presently entitled to a share of income of the Newman trust.

Consequently, the Newman trust is required to withhold an amount from the share (as if it was a payment) in respect of the investment. As the Newman trust is subject to TFN withholding under sections 12-140 and 12-145 of Subdivision 12-E of Schedule 1 to the TAA 1953, they are not required to withhold under these amendments.

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### *Beneficiaries that are subject to this measure*

1.22 Generally, these amendments apply to assessable distributions to all beneficiaries of closely held and family trusts, irrespective of whether they are individuals, companies or trusts. The amendments however, do not apply to excluded beneficiaries (see paragraphs 1.23 – 1.26).  
*[Schedule #, item 6, subsection 12-175(1)(c)]*

1.23 Additionally, special rules apply to beneficiaries (including trustee beneficiaries and their parent trusts) who are impacted by either the family trust distribution tax or the trustee beneficiary reporting rules. These rules are discussed in further detail below from paragraph 1.25.

### *Beneficiaries that are excluded from this measure*

1.24 Distributions to certain beneficiaries are not within the scope of this measure. These are distributions to beneficiaries who are:

- non-residents (as under Division 6 of the ITAA 1936, the trustee pays tax on their behalf);

*[Schedule #, item 6, subparagraph 12-175(1)(c)(i)]*

- exempt from income tax (as they are already exempt under Division 5 of Part VA of the ITAA 1936); or

*[Schedule #, item 6, subparagraph 12-175(1)(c)(ii)]*

- under a legal disability (e.g. minors and bankrupts) pursuant to section 98 of ITAA 1936 (as the trustee is already liable and required to lodge an income tax return on their behalf).

*[Schedule #, item 6, subparagraph 12-175(1)(c)(iii)]*

### *Treatment of entities subject to family trust distribution tax*

1.25 Special rules apply under these amendments to beneficiaries where their parent trust is subject to the family trust distribution tax.

1.26 Where the parent trust is a family trust and the beneficiary (or trustee beneficiary) is within that parent trust's 'family group', the beneficiary is subject to these amendments in the same way as all other beneficiaries. *[Schedule #, item 6, paragraph 12-175(2)(c)]*

1.27 However, where that parent trust distributes to a beneficiary outside of the 'family group', the parent trust will be subject to the 'family

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trust distribution tax', which is a final tax liability (equivalent to 46.5 per cent). Consequently, the trustee will not be required to withhold in respect of an amount upon which family trust distribution tax is payable. *[Schedule #, item 6, paragraph 12-175(2)(c)]*

1.28 This rule extends to all beneficiaries (including trustee beneficiaries) who receive distributions from the parent trust but are outside of the family group of the parent trust. *[Schedule #, item 6, paragraph 12-175(2)(c)]*

### Example 1.2

Stephen, as the trustee of the Gordon family trust, has made a family trust election. The beneficiaries of the trust include Les, Scott, Tom and the Schneider trust. All of the beneficiaries are members of the family group except Les. Les, Scott and the Schneider trust have failed to quote their TFN to the trustee before the trustee makes an assessable distribution.

When the trustee makes an assessable distribution to Les, the distribution is subject to the 'family trust distribution tax'. As that tax takes precedence over the TFN withholding, the trustee of the Gordon family trust is not required to withhold in relation to Les's distribution.

However, as Scott and the Schneider trust are within the Gordon family trust's elected family group, the trustee will be required to withhold from an assessable distribution to Scott and the Schneider trust.

As Tom has quoted his TFN to the trustee, no withholding will be required from his assessable distributions.

### *Treatment of entities subject to the trustee beneficiary reporting rules*

1.29 There are also special rules that apply to trusts that are subject to the trustee beneficiary reporting rules. Where a parent trust is subject to the trustee beneficiary reporting rules under Subdivision 6D of Part III of the ITAA 1936 (e.g. not a family or related trust), the parent trust will not be required to withhold from distributions made to those trustee beneficiaries. *[Schedule #, item 6, paragraph 12-175(2)(b)]*

1.30 The parent trust will remain subject to the trustee beneficiary reporting rules, and as part of these rules will be required to make a correct TB (trustee beneficiary) statement. The exclusion from this measure exists as the parent trust will already be subject to similar reporting requirements under the trustee beneficiary reporting rules. *[Schedule #, item 6, paragraph 12-175(2)(b)]*

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### Example 1.3

The Spiller trust is a closely held trust. Its beneficiaries include Lolly Pty Ltd, the Simon trust and the McCarthy trust (which are also both closely held trusts). All three beneficiaries have not provided their TFNs to the trustee of the Spiller trust. Upon the determination of present entitlement, the Spiller trust determines that each beneficiary's share of the net income of the trust is \$100.

As Lolly Pty Ltd is a company and a beneficiary of the Spiller trust, it is subject to this measure. Consequently, the Spiller trust is required to withhold from Lolly Pty Ltd's entitlement to the share of net income of the trust.

However, as Spiller trust is a closely held trust, and is already subject to the trustee beneficiary reporting rules in regards to both the Simon trust and the McCarthy trust, the Spiller trust is not required to withhold amounts from their entitlement to the share of the net income of the trust.

Despite this, the Spiller trust will still be required to lodge a correct TB statement and fulfil its obligation in respect of those beneficiaries in accordance with the trustee beneficiary reporting rules.

### Withholding obligation

1.31 For trustees and beneficiaries within scope of this measure, a TFN withholding obligation will arise where the trustee makes an assessable distribution to a beneficiary that has not quoted their TFN to the trustee.

1.32 An assessable distribution in this context means amounts representing the share of income of the trust assessable to the beneficiary. This is regardless of when the amount is paid to the beneficiary.

1.33 This means that the TFN withholding obligation only applies at the 'entitlement time' when a beneficiary becomes presently entitled to the share of income of the trust that is assessable income of the beneficiary pursuant to section 97 of the ITAA 1936.

*[Schedule #, item 6, subsections 12-175(1) and 12-175(2)]*

1.34 The withholding obligation is distinctly separate from the reporting obligations (including the requirement to report amounts withheld and to pay the amounts withheld to the Commissioner). These amendments provide for annual reporting and remittance (discussed further at paragraphs 1.46 and 1.53), whereas the withholding obligation

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under this measure may arise at any point during the income year.  
*[Schedule #, item 6, subsection 12-175(2)]*

1.35 Most commonly, the entitlement time will occur at the end of the income year when the majority of trustees make the determination of present entitlement as part of their trustee resolution. In this situation, a withholding obligation will arise at the end of the income year when the beneficiary becomes presently entitled to the share of the income of the trust. *[Schedule #, item 6, subsection 12-175(2)]*

### Example 1.4

The ABC trust has three beneficiaries (Jo, Rhonda and Sydney Pty Ltd). The ABC trust has not made any payments to the beneficiaries during the income year.

At the end of the income year, the trustee of the ABC trust is in the process of determining the beneficiaries' present entitlement to the income of the trust. Jo and Rhonda have already quoted their TFNs to the trustee of the ABC trust, but Sydney Pty Ltd has failed to quote its TFN.

Consequently, the ABC trust has a withholding obligation for the assessable distribution to Sydney Pty Ltd on the amount that would be required to be included in the beneficiary's assessable income under section 97 of the ITAA 1936.

1.36 However, in the situation where a payment is made to a beneficiary from the trust during the income year or the beneficiary has a vested and indefeasible interest in the income of the trust estate, the beneficiary is deemed under sections 95A and 101 of the ITAA 1936 to be presently entitled to that income.

1.37 Consequently, a withholding obligation may also arise during the income year where that payment is made or where a vested and indefeasible interest arises. This is because the withholding obligation is triggered by the beneficiary being deemed to be presently entitled to a share of the income of the trust. *[Schedule #, item 6, subsection 12-175(4)]*

### Example 1.5

The Kretschmann trust makes regular payments throughout the year to its two beneficiaries (Pierce and Regina). Pierce has provided his TFN to the trustee of the Kretschmann trust prior to the making of these payments but Regina has not.

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As the beneficiaries are deemed to be presently entitled to the income of the trust when the payments are made to them, a withholding obligation is triggered for the Kretschmann trust in respect of the payments made to Regina.

1.38 In summary, the mechanisms for withholding under these amendments arise where:

- The beneficiary has not provided their TFN to the trustee prior to the entitlement time; and
- the beneficiary becomes presently entitled or is deemed to be presently entitled to a share of income of the trust estate.

### ***Amount to withhold***

1.39 Under this measure, the withholding obligation is quantified as follows:

Amount to be withheld = S x R

Where

S = the beneficiary's share of the net income of the trust; and

R = is the rate worked out under the Regulations.

1.40 The withholding rate that applies currently for the purposes of TFN withholding is the top rate, which is defined as the sum of the highest rate specified in Part I of Schedule 7 to the *Income Tax Rates Act 1986* and the rate of levy specified in subsection 6(1) of the *Medicare Levy Act 1986*. This rate is currently 46.5 per cent.

### **Example 1.6**

The Evans trust is a closely held trust and has three beneficiaries. These beneficiaries are Courtney, Michael and Bennett Pty Ltd. The trustee of the Evans trust has reached the point where they are ready to make a determination of present entitlement. However, both Michael and Bennett Pty Ltd have failed to quote their TFNs to the trustee.

Consequently, upon making the determination of present entitlement to a share of the income of the Evans trust estate, a withholding obligation arises. The Evans trust is required to withhold 46.5 percent of the share of the net income of both Michael and Bennett Pty Ltd.

As Courtney has provided her TFN prior to the entitlement time, no withholding obligation has arisen.

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1.41 In the situation where the withholding obligation is triggered by a payment or where a vested and indefeasible interest has arisen during the income year, the quantum of the withholding will be determined on the amount of the payment or the amount to which the vested and indefeasible interest relates.

1.42 This withholding quantum will apply to the full amount of the payment made or the equivalent amount of the vested and indefeasible interest during the year, regardless of whether the payment or interest forms part of the share of the net income at the determination of present entitlement at the end of the income year.

1.43 Like the withholding rate, the withholding quantum in respect of payments or vested and indefeasible interests that arise during the income year will be worked out under the Regulations.

### **Example 1.7**

As in Example 1.5 the Kretschmann trust has a withholding obligation in regards to payments made during the year to the beneficiary Regina.

On 23 September 2011, the Kretschmann trust determines to pay \$1,000 of trust income to Regina. However, as a withholding obligation exists, the Kretschmann trust withholds \$465 from the payment.

1.44 For the purposes of consistency with the TFN withholding framework, the PAYG withholding regime (Part 2-5 of Schedule 1 to the TAA 1953) will continue to apply as if the trustee had paid the share of income to the beneficiary at the entitlement time even though the beneficiary is merely entitled to that share of the net income.

*[Schedule #, item 6, subsection 12-175(3)]*

1.45 Consequently, the trustee will be required to withhold an amount from the deemed payment and must do so at the entitlement time.

*[Schedule #, item 11, subsection 16-5(2)]*

### **Payment of amounts withheld**

1.46 Where a withholding obligation arises, the trustee is required to remit the amount withheld to the Commissioner. Under existing law, entities that withhold from payments must remit those amounts to the Commissioner in accordance with the framework under Subdivision 16-B of Schedule 1 to the TAA 1953. This framework stipulates different remittance cycles for different sized withholders.

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1.47 These remittance cycles apply weekly, monthly or quarterly for large, medium or small withholders respectively. For each withholder, the date of remittance is tied to the date of the withholding event.

1.48 Under these amendments, trusts that are required to withhold from a beneficiary's assessable distribution will not be required to remit under the weekly/monthly/quarterly cycle. Rather, they are required to remit withheld amounts to the Commissioner in an approved form through the Business Activity Statement (BAS) system on an annual cycle.

*[Schedule #, item 13, subsection 16-75(5)]*

1.49 This will require the trustee to register for PAYG withholding with the Tax Office and to pay the amount to the Commissioner by the 28<sup>th</sup> day of the next month following the day the trustee is required to lodge their annual report (discussed at paragraph 1.53).

*[Schedule #, item 13, paragraph 16-75(5)(a)]*

1.50 The requirement to pay the amount withheld within 28 days of the month following required lodgment of the annual report, is intended to administratively align with the monthly BAS cycle and to accommodate for those entities who are deferred BAS payers. However, the payment due date can be longer if the Commissioner allows.

*[Schedule #, item 13, paragraph 16-75(5)(b)]*

1.51 This remittance requirement takes into account the special nature of the withholding event and applies an annual remittance obligation.

### **Example 1.8**

As in Example 1.6, a withholding obligation has arisen for the Evans trust in regards to assessable distributions made to both Michael and Bennett Pty Ltd.

The trustee of the Evans trust makes the determination in respect of the previous income year that both Michael and Bennett Pty Ltd are presently entitled to \$1000 each, which represents their share of the net income of the trust. The Evans trust then withholds the equivalent rate (46.5 per cent) from each entitlement (totalling \$465 each).

The Evans trust annual report is due on 31 August 2011, however the trustee lodges the annual report earlier on 28 July 2011. Despite the early lodgment, the Evans trust still pays the \$930 through the relevant BAS by 30 September 2011.

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### Reporting requirements

1.52 Under these amendments, the trustee is required to comply with two main reporting obligations to the Commissioner and to their beneficiaries.

#### ***Reporting to the Commissioner of amounts withheld and amounts distributed***

1.53 The first reporting obligation requires the trustee to lodge with the Commissioner an end of income year report detailing the amounts withheld and the amounts that would have been withheld had the beneficiary not quoted their TFN to the trustee.

1.54 Under the current law, entities that withhold from payments are required to notify the Commissioner of those amounts withheld on or before the day the payment is due. This is normally achieved through the BAS system as part of the remittance obligation.

1.55 In addition to this requirement, the TFN withholding framework (and in certain circumstances the PAYG withholding framework) require the withholder to provide the Commissioner with an annual report detailing amounts withheld. In the specific case of TFN withholding in respect of investments, withholders subject to those obligations are required to lodge an annual investment report which details extensive information about the investment and the amounts withheld.

1.56 Under these amendments, the trustee is only required to lodge an annual report with the Commissioner. This report is to be made in a form approved by the Commissioner and will be due not later than two months after the end of the income year or longer if the Commissioner allows. *[Schedule #, item 14, subsections 16-153(1A) and 16-153(1B)]*

1.57 The trustee is required to report the amounts distributed or payable to all beneficiaries within the scope of these amendments regardless of whether a withholding obligation is triggered under these amendments. *[Schedule #, item 14, paragraphs 16-153(1A)(a) and 16-153(1A)(b)]*

#### ***Reporting amounts withheld and distributed to beneficiaries***

1.58 The second reporting obligation for the trustee is to notify beneficiaries of amounts withheld by issuing payment summaries. Currently, under the PAYG withholding framework, withholders are generally required to issue payment summaries within 14 days of the end of the financial year notifying the payee/employee/investor of amounts

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withheld. A failure to comply with these requirements constitutes an offence of strict liability which is punishable by a fine not exceeding 20 penalty units.

1.59 Under these amendments, trustees are required to issue an annual payment summary to each beneficiary who has had amounts withheld. *[Schedule #, items 16 and 18, section 16-156 and subsection 16-170(IAAA)]*

1.60 This payment summary matches the annual report insofar as it requires the trustee to detail amounts withheld and also report the amounts distributed or payable to that beneficiary. This will then provide the beneficiary with a notification of how much they have been distributed, so they are aware of how much to include in their income tax return. *[Schedule #, item 16, paragraphs 16-156(1)(a) and 16-156(1)(b)]*

1.61 The payment summary is to be provided in the approved form and has a due date of 14 days after the due date for the lodgment of the annual report (discussed above) or a longer period allowed by the Commissioner. *[Schedule #, items 16 and 18, subsection 16-156(2) and subsection 16-170(IAAA)]*

1.62 Under these amendments, the existing penalty for a failure to provide a payment summary, will continue to operate as a strict liability offence. *[Schedule #, items 21 and 22, subsection 16-175(1)]*. A strict liability offence in this context means that there is no requirement to prove fault, however the defence of mistake is available.

### **Claiming a withholding credit**

1.63 Under the existing TFN withholding framework a payee/investor is entitled to a credit equal to the amount that was withheld from their payment/distribution by the withholder. This entitlement arises where the payee/investor lodges a return and receives an assessment for the relevant income year. Currently, where the claimant of the credit is a trust, then the current TFN framework provides for the credit to flow through to the beneficiary of the trust.

1.64 Under these amendments, when the beneficiary lodges their end of year income tax return, they can also claim a credit equal to the amounts that have been withheld by the trustee to the Commissioner in accordance with the existing crediting framework.

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### Penalties

1.65 Under the existing PAYG withholding regime, there are specific penalty provisions that relate to TFN withholding. These include the failure to withhold penalty under sections 16-25 and 16-30 of Schedule 1 to the TAA 1953 as well as the penalty for failure to pay within time under section 16-80 of Schedule 1 to the TAA 1953. These penalties apply to entities that are required to both withhold from certain payments and pay the amounts withheld to the Commissioner but fail to do so.

1.66 In addition to these PAYG withholding specific penalties, administrative penalties exist under Part III of the TAA 1953 for failure to comply with taxation requirements, making intentional errors in reports and the making of false and misleading statements.

1.67 Under these amendments, the existing penalty regime will apply to the withholding obligations and reporting requirements as required. There are no new penalties specific to the operation of these amendments.

### Specific administrative provisions

1.68 This Schedule also amends the ITAA 1936 to insert Division 4B into Part VA. This new Division 4B contains various administrative provisions to facilitate the extension of the TFN withholding regime to closely held trusts, including family trusts.

#### *Quotation of the TFN*

1.69 Under the current TFN withholding regime, provisions exist to facilitate the quotation of the TFN to the payer, in addition to providing administrative mechanisms for the incorrect quotation of a TFN.

1.70 These amendments will replicate these administrative requirements and facilitate the administrative mechanism for the incorrect quotation of the TFN (discussed below). *[Schedule #, item 1, sections 202DN, 202DO and 202DP ITAA 1936]*

1.71 These amendments are designed to ensure that the beneficiary quotes the correct TFN to the trustee. The effect will be that where the Commissioner has enough detail to correct an incorrectly quoted TFN, the Commissioner may do so and provide notice to the trustee.

1.72 These amendments will do so by providing the Commissioner with the power to correct the TFN quoted by the trustee by giving the

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trustee a notice in writing indicating where the TFN quoted is incorrect or otherwise wrong and that the Commissioner is able to ascertain the correct TFN. *[Schedule #, item 1, subsections 202DR(1) and (2) ITAA 1936]*

1.73 However, where the Commissioner cannot correct an incorrectly quoted TFN or the number is cancelled, the Commissioner must notify the trustee and the beneficiary and provide recourse for the correct quotation. Until the quotation is corrected, the beneficiary is deemed to not have quoted

1.74 These amendments operate so that in the situation where the Commissioner considers the TFN quoted to be incorrect or it has been cancelled and is not satisfied that the beneficiary has a TFN, the Commissioner is required to give the trustee and the beneficiary a written notice and a written statement of reasons indicating this decision. On and from the day the notice takes effect, the beneficiary is taken not to have quoted their TFN to the trustee. *[Schedule #, item 1, subsections 202DR(3)-(6) ITAA 1936]*

### ***Reporting of TFNs quoted***

1.75 Once a TFN has been quoted to the trustee, the trustee is required to report the beneficiary's TFN to the Commissioner.

1.76 Under the current TFN withholding framework, TFNs quoted to the withholder are reported to the Commissioner through different mechanisms. In the employer/employee scenario, TFNs are reported using TFN declarations, whereas in the investment body/investor scenario, TFNs are reported through quarterly reports.

1.77 Under these amendments, as the withholding obligation can occur upon the determination of present entitlement (which is an annual event) or when the beneficiary is deemed presently entitled when the trustee makes a decision to pay an amount (which can occur at any time during the income year), the reporting of the TFNs quoted is quarterly. The reporting of these TFNs will be made in a form approved by the Commissioner and will be due within one month after the end of the quarter in which it relates or longer as the Commissioner allows. *[Schedule #, item 1, subsections 202DP(1) and (2) ITAA 1936]*

1.78 These amendments also provide a mechanism for the Commissioner to notify the trustee of a different reporting period for the purposes of TFN quotation. This provides the Commissioner with the administrative flexibility to set a period longer than three months for the

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trustee to report the quoted TFNs in the appropriate circumstances.  
*[Schedule #, item 1, subsection 202DP(3) ITAA 1936]*

1.79 Failure to report the quoted TFN to the Commissioner constitutes an offence under section 8C of the TAA 1953 wherein the trustee has failed to comply with a requirement under the taxation law. An offence under section 8C TAA 1953 is an offence of absolute liability.  
*[Schedule #, item 1, Note under section 202DP ITAA 1936]*

1.80 An offence of absolute liability in this context means that where a trustee fails to report a quoted TFN, they will have committed an offence and the defence of mistake is unavailable. There is no requirement to prove fault, and the trustee is punishable on conviction of a fine not exceeding 20 penalty units for their first offence. Subsequent offences will render the trustee punishable on conviction of a greater penalty.

### *Changes to the definition of ‘quoted’*

1.81 These amendments also change the definition of ‘quoted’ under section 995-1 of the *Income Tax Assessment Act 1997* (ITAA 1997) to facilitate the requirement to quote a TFN under this measure.  
*[Schedule #, item 3, section 995-1 (definition of quoted) ITAA 1997]*

### *Refunding of amounts withheld in error*

1.82 Under the current TFN withholding framework, those amounts that are withheld by a payer and/or paid to the Commissioner in error can be refunded to the payee, where the payer becomes aware of the error or the payee applies for the refund.

1.83 The application process for the payee requires the payee to provide certain information to the payer in order to have the payer refund the amount to the payee. Similarly, the payer is then required to provide certain information to the Commissioner, in order to recover the amounts refunded to the payee, where the amounts had originally been remitted to the Commissioner.

1.84 Under these amendments, where a beneficiary has amounts withheld and/or paid to the Commissioner in error, they will be able to seek a refund using the current refund framework. *[Schedule #, item 24, subparagraph 18-65(3)(d)(iv)]*

## EXPOSURE DRAFT

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### Application and transitional provisions

1.85 These amendments will apply from 1 July 2010 to a share of the income of a trust for the 2010-11 income year and onwards.  
*[Schedule #, items 25 and 26]*

### Consequential amendments

1.86 There are also various other amendments, which clear up assorted headings, notes, and other things that need to be removed or changed due to the creation of the new provisions for the extension of the TFN withholding rules to closely held trusts, including family trusts.  
*[Schedule #, items 2, 4, 7, 8, 9, 10, 12, 15, 17, 19, 20 and 23]*



