

Issue No. 3 8 October 2007

# Tax Update

## Welcome to ...

... the second edition of the Tax Update this month!

So far it has been another big year for legislative and case law developments in taxation, and we set out some of the more interesting recent developments in this Update. As always, if you have any queries or concerns about anything to do with tax or superannuation, please do not hesitate to call our tax team.

## 2007 Measures No 5 Act now in force

On 16 August 2007, Tax Laws Amendment (2007 Measures No 5) Bill 2007 was introduced into the House of Representatives.

The Bill received assent on 25 September 2007 as Tax Laws Amendment (2007 Measures No 5) Act 2007 (Act No 164 of 2007).

The following is an extract from the Explanatory Memorandum. Items of interest include:

- Schedule 2, which amends the ITAA 1997 to change the definition of 'excluded equity interest'. The effect of the change is to exclude from the definition those equity interests that remain on issue for a total period of 180 days or more, whether or not this was the case at a specific valuation day. This amendment commenced on the day the Act received Royal Assent (i.e., 25 September 2007) and will apply to income years starting on or after 1 July 2002 (the date when the definition of 'excluded equity interest' took effect).
- Schedule 4, which amends the ITAA 1997 to extend the capital gains tax (CGT) marriage breakdown roll-over to in specie transfers of personal superannuation interests from a small superannuation fund to another complying superannuation fund under specific conditions.



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## 2007 Measures No 5 Act Continued

This enables separating spouses to achieve a 'clean break' from each other in terms of their superannuation arrangements. This measure applies to CGT events that happen on or after 1 July 2007.

- Schedule 6, which amends the company loss recoupment rules in the ITAA 1997 to remove the \$100 million total income cap on the same business test. These amendments apply to losses incurred in an income year commencing on or after 1 July 2005.
- Schedule 7, which amends the ITAA 1997 to extend the existing statutory licence capital gains tax (CGT) roll-over under Subdivision 124-C to provide for roll-over where one or more new licences are issued in consequence of the ending of one or more licences and to provide for a partial roll-over. A partial roll-over applies where one or more statutory licences end and are replaced by one or more new licences and the licensee also received non-licence capital proceeds such as money. This measure will apply to CGT events that happen in the 2006-07 income year and later years.
- Schedule 8, which amends the ITAA 1997 to provide holders of ownership interests in stapled entities with a capital gains tax (CGT) roll-over when a public unit trust is interposed between those holders and the stapled entities.

This Schedule also amends the ITAA 1936 to ensure that such restructures do not result in the interposed head trust being taxed as if it were a company. In addition, public unit trusts will be able to acquire controlling interests in, or control, foreign entities whose business consists primarily of investing in land outside Australia for the purpose, or primarily for the purpose, of deriving rent. The CGT roll-over amendments apply to CGT events that happen on or after 1 July 2006. The other amendments will apply to the 2006-07 year of income and later years of income.

## Recent cases

### **Tyco Australia Pty Limited v Commissioner of Taxation [2007] FCA 1055**

This case considered whether payments (totalling \$132,284,530 in the three relevant years of income) made by a taxpayer to its Authorised Dealers were on revenue, rather than capital, account and therefore deductible under section 8-1 of the Income Tax Assessment Act 1997.

The taxpayer carried on a business of electronic security monitoring in Australia. The taxpayer acquired from independent contractors called "Authorised Dealers" service agreements that the Authorised Dealers had entered into with customers who had installed electronic security systems. The service agreements had an agreed monitoring term of at least 36 months and provided that the agreements could be assigned to the taxpayer. The taxpayer paid a fee to the Authorised Dealers for each service agreement that it acquired. It sought a deduction for the fees so paid. The Commissioner denied the claim for a deduction on the basis that the purchase of the contracts was the establishment of a profit yielding structure, for the business of providing monitoring services. The taxpayer appealed to the Federal Court.

In upholding the taxpayer's claim for a deduction, the Federal Court said: "The asset or the so-called accretion to structure was, in practical and business terms (and in legal terms), the winning of a customer. That a very attractive (to the Authorised Dealer) Assignment Fee was set reflected the anticipation not of the value of the contract rights themselves that were assigned, but rather the future value of the connection with the customer and the future revenue stream once the customer was won. The advantage sought by each payment was the winning of a customer, so that he, she or it might be retained and exploited (using that word in a

neutral sense) for future revenue for services to be provided."

The Court also said: "When one steps back from each individual assignment and places the AD [Authorised Dealer] Program in its context, it amounts to one business method of seeking out, contracting and profiting from additional customers. It could have been done by many methods, including employees, commission agents or, as here, independent contractors, going out to obtain customers. The instrument used (whether employee, agent or independent contractor) would need to be remunerated. The method of remuneration does not affect the character of the advantage sought: the incremental addition to the customer base of [the taxpayer] and the future obtaining of revenue therefrom.... This was not the purchasing or creation of a business structure. It was, to paraphrase and elaborate upon the words of Dixon J in *Sun Newspapers* 61 CLR at 360, the building of the extent of the profit-yielding subject (being the customer base of [the taxpayer]) as the product of the course of operations, by the incremental winning of customers by the chosen method of organising and remunerating an independent, but controlled, sales force."

The Commissioner's decision to disallow the taxpayer's objections was set aside.

### **Tolich v FCT [2007] FCA 1195**

The Federal Court (Besanko J) has upheld the Commissioner's disallowance, as deductions, of non-cash outlays incurred by the taxpayers in relation to their investment in projects which were referred to collectively as the Travel Vision Projects. The Court held that the Commissioner was right to conclude that Part IVA of the Income Tax Assessment Act 1936 ("ITAA 1936") applied to each of the projects.

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