Dear Treasury

I want to provide comments on the Closely Held Trust rules as part of the overall review of reforming the taxation of trust income.

I consider myself to be a "stakeholder" as I am a tax agent and accountant with nearly 30 years experience of dealing with the Australian taxation system. I am a chartered accountant, a fellow of The Tax Institute and a director of a company that prepares income tax returns for a significant number of trusts.

My comments should be considered in the context of the Project Objective to improve **and simplify** the taxation of trust income in Australia.

My opinion is that the Closely Held Trust rules should be totally scrapped, as they are complex, poorly understood, badly targetted, time-consuming to apply, and could result in large tax assessments for inadvertent errors. I cannot see that these rules benefit anyone, and that includes Treasury and the Tax Office. The costs outweigh the benefits. For most trusts, the information provided to the Tax Office will be a duplication of what is provided anyway.

At clause 4.8, your consultation paper makes reference to the "trustee beneficiary reporting rules" and closely held trusts. The first two paragraphs of that clause are **grossly misleading**, as they imply that the 1999 ultimate beneficiary reporting rules were relaxed in 2007. In fact, the 1999 ultimate beneficiary rules were a bureaucratic disaster when first introduced, and were effectively withdrawn a few years later. The 2007 rules did **not** relax the ultimate beneficiary rules **-** they constitute a completely new set of onerous reporting and withholding obligations that apply to thousands of trusts for the first time.

Tax Office/Treasury communication

There was very little publicity about the closely held trust rules when they were introduced. Most tax practitioners still find it hard to see the point to the rules. We all thought that Treasury and the Tax Office had learnt from the debacle of the ultimate beneficiary reporting rules. I certainly haven't seen any evidence of widespread tax avoidance that would justify the introduction of these rules. All I see is extra costs being imposed on many trustees who are legitimately going about their usual activities.

An indication of the difficulty of understanding these rules is how hard it is to get any assistance from the Tax Office. There are several fact sheets on the Tax Office website, but these are not easy to understand. Any attempt that I have made to engage in meaningful dialogue with a "real person" from the Tax Office has been fruitless. There may be a few people at the Tax Office who understand the rules, but I have not yet managed to talk to one of them.

Our firm was told by our "relationship officer" from the Tax Office that he would try to arrange for one of their experts to give us training on the closely held trust rules. We accepted this offer with enthusiasm, but that was six months ago and nothing has happened. We have been told that there is no one in Queensland that can talk to us, and it is unlikely that there is anyone in Australia that can talk to us on both the reporting obligations and the withholding obligations at the same time. If that is the position with the Tax Office, what hope does the average trustee have of understanding these rules?

Reporting rules

In certain cases, closely held trusts have to provide further details (a "TB Statement") on distributions to trust beneficiaries.

The definition of a "closely held trust" for the purposes of the reporting rules is different from the definition of a closely held trust for the withholding rules. This creates confusion from the start.

If the reporting rules in relation to a beneficiary are not fully complied with, the trustee pays tax at 46.5% on the beneficiary's share of income. From what I can see, there is **no** discretion allowed to the Tax Office in the application of this tax. The Commissioner has a discretion to allow an extension of time to lodge the "TB Statement", but no discretion to allow the amendment of a statement once lodged. Accordingly, an inadvertent error in completing the statement leads to the imposition of tax at the top marginal rate on the trustee, despite no tax avoidance by trustee or beneficiary. This is just unfair and ridiculous! From what I understand, if the trustee is a company, the directors are personally liable for the tax.

The tax is supposed to be paid within three weeks of the end of the disclosure period, or interest will apply. However, if an inadvertent error or omission is made, the problem will only come to light months or years later, so the trustee will be liable for a hefty interest bill on top of the tax.

Withholding rules

The withholding rules require tax to be withheld from distributions unless TFNs of beneficiaries are provided. If TFNs are provided, the trustee is required to report the details to the Tax Office. This sounds deceptively simple, but the practical application is not.

"Closely held trusts" for purposes of the withholding rules include typical family discretionary trusts that have made a "family trust election". The trustees are often individuals with limited knowledge of the tax law. Distributions are only made to family members and related family entities. The tax returns for the trusts and related parties are often prepared months after the end of the financial year and no tax agent has the resources to finalise trust tax returns shortly after year end. If tax was required to be withheld from distributions , it will already be overdue by the time the returns are prepared. Secondly, if the trustee should have notified TFN details to the Tax Office, the time period for notification will have lapsed. Basically, there is little chance of family trusts complying with the rules on time. However, there is also no loss to the revenue, as the trusts will typically lodge their tax returns on time, notify the TFN details in the returns and pay their tax when assessed. In other words, the withholding rules for most family trusts don't achieve anything other than imposing a potential new liability on trustees.

Withholding tax applies when a distribution is made to a beneficiary. In a typical family trust, there may be many payments to and from beneficiaries, and it is often not clear at the time whether a payment is for a distribution or not. It is not practical to expect withholding tax to be deducted in the right amount at the right time.

Where trustees are provided with TFNs by beneficiaries, the trustees must provide a report to the Commissioner within one month of the end of the quarter (not the end of the tax year). In the case of family trusts, this will not happen, because the trustees will be unaware of their obligations. However, it will not matter, as the TFNs will be included in the trust tax return anyway. It is hard to see that the Commissioner gets any benefit from receiving the earlier TFN report.

As existing trusts are subject to transitional provisions, there is confusion as to when trustees have to report details of beneficiaries. In a family trust, the trustee would usually already be aware of the TFNs of family members and related parties, but may be making a distribution to a particular beneficiary for the first time. It is not clear whether this requires reporting and, if the TFN is to be included in the return, there seems little point to it.

Alternative approach

The cost of complying with the closely held trust rules will far outweigh the benefits. The new rules have imposed onerous new reporting and withholding obligations on many trustees. For the vast majority of these trustees, the rules will not result in any increase in tax collection, as the trustees and beneficiaries were already paying the required tax in full.

The closely held trust rules should be repealed. If the Tax Office considers that some trustees are engaged in tax avoidance, it should pursue those trustees. I totally support the investigation of trustees and beneficiaries if there is a suspicion of avoidance or evasion, but I do not consider that the Tax Office needs the closely held trust rules to do this.

Details of trust beneficiaries have always been included in trustee tax returns. If TFNs are not provided, the returns required full names and addresses of beneficiaries. This should be sufficient information for the Tax Office to follow up suspicious distributions. There is no need to impose these complex rules on all trusts just to attempt to get information on a small percentage of wrongdoers.

I look forward to hearing from you.

Yours faithfully

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