



Class Ruling

Income tax: Department of Health and Human Services (Tasmania) Self-Directed Funding by direct payments

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① This publication provides you with the following level of protection:

This publication (excluding appendixes) is a public ruling for the purposes of the *Taxation Administration Act 1953*.

A public ruling is an expression of the Commissioner's opinion about the way in which a relevant provision applies, or would apply, to entities generally or to a class of entities in relation to a particular scheme or a class of schemes.

If you rely on this ruling, the Commissioner must apply the law to you in the way set out in the ruling (unless the Commissioner is satisfied that the ruling is incorrect and disadvantages you, in which case the law may be applied to you in a way that is more favourable for you – provided the Commissioner is not prevented from doing so by a time limit imposed by the law). You will be protected from having to pay any underpaid tax, penalty or interest in respect of the matters covered by this ruling if it turns out that it does not correctly state how the relevant provision applies to you.

What this Ruling is about

1. This Ruling sets out the Commissioner's opinion on the way in which the relevant provision(s) identified below apply to the defined class of entities, who take part in the scheme to which this Ruling relates.

Relevant provision(s)

2. The relevant provisions dealt with in this Ruling are:

- section 159P of the *Income Tax Assessment Act 1936* (ITAA 1936);
- section 6-5 of the *Income Tax Assessment Act 1997* (ITAA 1997);
- section 8-1 of the ITAA 1997;
- section 15-2 of the ITAA 1997;
- Subdivision 20-A of the ITAA 1997.

All legislative references in this Ruling are to the ITAA 1997 unless indicated otherwise.

Class of entities

3. The class of entities to which this Ruling applies is
- persons with a disability receiving disability services funded by the Department of Health and Human Services (Tasmania) (the Department); and
 - nominated persons as defined in the Self-Directed Funding Direct Payments Guidelines

who have an Individual Support Package and enter into a Direct Payment Deed with the Department to receive funds for the purpose of purchasing disability services. In this Ruling these persons are referred to as recipients.

Qualifications

4. The Commissioner makes this Ruling based on the precise scheme identified in this Ruling.
5. The class of entities defined in this Ruling may rely on its contents provided the scheme actually carried out is carried out in accordance with the scheme described in paragraphs 9 to 21 of this Ruling.
6. If the scheme actually carried out is materially different from the scheme that is described in this Ruling, then:
- this Ruling has no binding effect on the Commissioner because the scheme entered into is not the scheme on which the Commissioner has ruled; and
 - this Ruling may be withdrawn or modified.
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Date of effect

8. This Ruling applies from 1 July 2012. However, this Ruling will not apply to taxpayers to the extent that it conflicts with the terms of a settlement of a dispute agreed to before the date of issue of this Ruling (see paragraphs 75 and 76 of Taxation Ruling TR 2006/10).

Scheme

9. The following description of the scheme is based on information provided by the applicant. The following documents, or relevant parts of them, form part of and are to be read with the description:

- Class Ruling application dated 3 August 2012;
- proforma Personal Support and Funding Plan for Individual Support Packages (July 2012) (the Plan);
- the *Disability Services Act 2011* (Tas) (the Disability Act);
- proforma Direct Payment Deed (the Agreement);
- Self-Directed Funding Individual Support Packages Handbook (the Handbook); and
- Self-Directed Funding Direct Payments Guidelines (June 2012).

10. The Disability Act provides the legislative basis for the funding of Individual Support Packages for persons with a disability. The Disability Act also encourages respect for the right of the person with a disability to independence and the freedom to make individual choices.

11. The aim of the Individual Support Packages is to allow eligible persons to decide the support that they may need to help achieve their goals and live the way they want to. One of the ways funding is managed under the Individual Support Packages is by direct payment to the person with a disability, who is then responsible for paying for the disability services and support.

12. To apply for an Individual Support Package funded by direct payments, the person with a disability must first work with the Department to develop a Plan, outlining the goals to be achieved and the support needed.

13. The Plan will detail:

- the funding administration arrangement which the person with the disability will use to manage the funds;
- the specific services or goods the person with disability will be purchasing;
- the cost of the services and goods; and
- any other information that is critical to the person's support arrangements.

14. A person with a disability who has:

- been allocated an Individual Support Package
- chosen the direct payment option, and
- signed the Agreement,

will receive funds directly from the Department to purchase goods or services that meet the goals specified in the Plan.

15. The recipient will be responsible for managing all aspects of their Individual Support Package – including:

- negotiating and arranging with service providers the details around provision of supporting services and other goods;
- checking the quality of support;
- ensuring that invoices reflect the cost and quantity of services provided;
- paying invoices and maintaining receipts;
- providing information, records and reports to the Department as required; and
- having appropriate insurance in place to cover accidents and meet occupational health and safety requirements for support staff.

16. The Agreement specifies the commencement and completion date, and a payment schedule. It also details the specialist disability services or other goods and services for which funds are approved and the expected outcomes for the recipient.

17. The funds are paid electronically into a bank account (the direct payments account) maintained by the recipient and used only to receive and expend the funds. In accordance with the Agreement, the direct payments account must not have a credit card or overdraft facility, nor be linked to any other bank account.

18. Any interest earned on funds deposited in the direct payments account must be applied by the recipient as if those amounts of interest were monies received from the Department under the Agreement. The recipient is responsible for paying any bank fees that may apply to the direct payments account.

19. The recipient is required, upon request, to provide an acquittal of how the funds have been spent and to keep records of all transactions and accounts. The Department may review expenditure to ensure it has been consistent with the goals of the Plan and may request repayment within 28 days or revise the payment schedule to recoup funds improperly used.

20. Should there be surplus funds at the end of a financial year these may be retained by the recipient and carried over to the following financial year, if provided for in the Plan.

21. If there are unspent funds at the completion date of the Agreement and a new Agreement has not, and/or will not, be signed, the Department may request that these unspent funds be repaid within 28 days.

Ruling

22. The funds received from the Department do not form part of the recipient's assessable income under section 6-5.

23. The funds received from the Department are:

- not given or granted to the recipient in relation to employment or services rendered under section 15-2; and
- not assessable recoupments of the recipient under Subdivision 20-A.

24. The interest earned on funds deposited into the direct payments account, specifically maintained for the purposes of receiving the funds, does not form part of the recipient's assessable income.

25. Any losses or outgoings incurred in managing or obtaining the recipient's disability services under the Agreement are not deductible under section 8-1 or any other provision of the ITAA 1997.

26. None of the amounts paid by the recipient for disability services and in respect of which funds have been received are rebatable amounts for the purposes of the medical expenses tax offset under section 159P of the ITAA 1936.

Commissioner of Taxation

24 October 2012

Appendix 1 – Explanation

❶ *This Appendix is provided as information to help you understand how the Commissioner's view has been reached. It does not form part of the binding public ruling.*

27. A payment or other benefit received by a taxpayer is assessable income if it is:

- income in the ordinary sense of the word (ordinary income); or
- an amount or benefit that through the operation of the provisions of the tax law is included in assessable income (statutory income).

Ordinary income

28. Under subsection 6-5(1) an amount is assessable income if it is income according to ordinary concepts.

29. In determining whether an amount is ordinary income, the courts have established the following principles:

- what receipts ought to be treated as income must be determined in accordance with the ordinary concepts and usages of mankind, except in so far as a statute dictates otherwise;
- whether the payment received is income depends upon a close examination of all relevant circumstances; and
- whether the payment received is income is an objective test.

30. Relevant factors in determining whether an amount is ordinary income include:

- whether the payment is the product of any employment, services rendered, or any business;
- the quality or character of the payment in the hands of the recipient;
- the form of the receipt, that is, whether it is received as a lump sum or periodically; and
- the motive of the person making the payment. Motive, however, is rarely decisive as in many cases a mixture of motives may exist.

31. When considering the first and last factors of paragraph 30 of this Ruling it is appropriate to look at the nature of the relationship between the recipient and the Department.

The nature of the relationship between the Department and the recipient

32. The Department is responsible for the administration of the Individual Support Packages which enable the recipients to use the funds to choose, arrange and directly purchase disability services that they require to meet their needs (in accordance with their Plan).

33. The recipients are required to utilise the funds to directly purchase goods and services previously provided to a person with a disability by the Department.

34. Certain features of the arrangement point to the existence of a fiduciary relationship between the recipient and the Department. In *Hospital Products Ltd v. United States Surgical Corporation* (1984) 156 CLR 41 Mason J made the following observations about fiduciary relationships (at 97):

The critical feature of these relationships is that the fiduciary undertakes or agrees to act for or on behalf of or in the interests of another person in the exercise of a power or discretion which will affect the interests of that other person in a legal or practical sense. The relationship between the parties is therefore one which gives the fiduciary a special opportunity to exercise the power or discretion to the detriment of that other person who is accordingly vulnerable to abuse by the fiduciary of his position.

35. By entering into the Agreement, the recipient agrees to apply the funds to obtain approved goods and services, which would otherwise be provided by the Department. Therefore, the recipient can be said to be acting on behalf of the Department in discharging its duty to provide these services.

36. The arrangement clearly guards against abuse by the recipient. The terms of the Agreement confine the use of the funds to approved purposes, that is, uses permitted by the Plan, which protects the Department and ensures that public funds are used only in a way that discharges the Secretary of the Department's statutory duty. The fact that this protection is expressed in a contract is not inconsistent with the existence of a fiduciary relationship.¹

37. A second critical feature is that the fiduciary may not profit from the position in which he or she is placed: see *Boardman v. Phipps* [1967] 2 AC 46 and cases referred to there by Lord Guest at 115-116; also *Pavan v. Ratnam* (1996) 23 ACSR 214 per Mahoney ACJ at 217. The fiduciary must treat his or her own interests as subservient to the interests of the principal, in this case, the Department. The fiduciary must account for any profit made without the knowledge and consent of the principal. These elements are clearly present.

¹ *Quistclose Investments Ltd v. Rolls Razor Ltd* [1970] AC 567.

38. The recipient can only use the funds for approved purposes. In addition, any interest accruing becomes part of the funds and can also only be used for approved purposes.

39. Further, to say that the recipient holds the funds for their own benefit fails to give proper significance to the totality of the arrangement. The recipient holds the funds for the approved purposes and applies them on behalf of the Department.

40. Therefore, the fact that the funds may be used to obtain the goods and services for the recipient personally does not mean that the recipient profits from the arrangement in the sense referred to in the authorities. The recipient would receive the same level of services if they did not choose the direct payment option.

41. In addition, an express obligation to keep funds separate from the recipient's own money points to the existence of a trust – that is, a fiduciary obligation: *Cohen v. Cohen* (1929) 42 CLR 91, referred to by the majority of the High Court in *Associated Alloys Pty Limited v. ACN 001 452 106 Pty Limited (in liquidation) (formerly Metropolitan Engineering and Fabrications Pty Limited)* [2000] HCA 25 at [34].

42. This obligation is clearly present. The Agreement states that the recipient must maintain a bank account which must only be used for the funds. The bank account must not have a credit card attached to it, have an overdraft facility nor be linked to any other bank account.

43. These characteristics of the arrangement strongly point to the recipient being in a fiduciary relationship with the Department.

The scope of the fiduciary relationship

44. The overall arrangement involves the provision of funds to the recipient to obtain approved goods and services. Apart from holding and applying the funds for the approved purposes, the recipient has no other obligations to the Department under the arrangement. It is clear, then, that the scope of the recipient's fiduciary obligations to the Department relates to the recipient's holding and application of the funds.

45. The discretionary powers the recipient has as to the use of the funds are authorised under the Agreement and the Plan and fall within the purposes for which funds may be provided under the Disability Act. These powers do not conflict with the fiduciary obligations that the recipient owes to the Department. On the contrary, they are designed to further the objects and principles of the Disability Act.

46. The fiduciary duties owed by the recipient to the Department indicate that the funds are not beneficially held and used by the recipient for private purposes but are held and used on behalf of the Department.

47. The recipient under the Agreement is neither an employee of the Department nor in receipt of the payments in relation to the carrying on of a business.

48. However, whether the funds have been received for services rendered must be examined, as payments to a taxpayer for services rendered are assessable income, even though the taxpayer does not provide those services as an employee or in carrying on a business.

49. Under the terms of the Agreement, while the recipient obtains and manages the goods and services, they do not receive any amount as a reward for taking on this role. The Agreement permits the funds to be used only for purchasing disability services and meeting the direct costs of managing these services. The recipient must account for the use of the funds and must repay any money not used for approved purposes. If there are unspent funds at the completion date and a new Agreement has not, or will not, be signed the Department may request that these unspent funds be repaid. These funds must be repaid within 28 days of the request.

50. In these circumstances, the funds are not a payment for services rendered.

51. It is clear that the recipient cannot deal with the money as their own. Their obligations in dealing with the funds have the nature of fiduciary obligations.

52. A primary motive of the Department in providing direct financial assistance is to give the recipient non-material benefits such as the freedom to make their own choices, recognition of their needs and best interests and the ability to participate meaningfully in society. This motive is apparent in the objects and principles of the Disability Act and the principles for self-directed funding set out in Chapter 5 of the Handbook.

53. For the reasons given above, it is not considered that the funds received under the Agreement are ordinary income in the hands of a recipient for the purposes of section 6-5.

Statutory income

54. Section 6-10 includes in assessable income amounts that are not ordinary income. These amounts are called statutory income. A list of the statutory income provisions can be found in section 10-5. That list includes a reference to section 15-2 and Subdivision 20-A.

Employment or services rendered

55. Section 15-2, provides that assessable income shall include:

... the value to you of all allowances, gratuities, compensation, benefits, bonuses and premiums provided to you in respect of, or for or in relation directly or indirectly to, any employment of or services rendered by you ...

56. As discussed in paragraphs 48 to 50 of this Ruling, the recipients do not receive the funds for any employment or services rendered. Therefore the payments to the recipients are not statutory income under section 15-2.

Assessable recoupment

57. Subdivision 20-A operates to include in assessable income amounts received as recoupments of specified losses or outgoings allowed or allowable as deductions. The relevant provision is subsection 20-20(3) which provides that an amount is an assessable recoupment of a loss or outgoing if a taxpayer:

- receives the amount (except by way of insurance or indemnity); and
- can deduct an amount for the loss or outgoing in the current year or has deducted or can deduct an amount for it in an earlier year under a provision listed in the tables at section 20-30.

58. As the payment of funds is not made by way of insurance or indemnity and no deduction is allowable or would be allowable to the recipient in respect of the expenditure incurred for the disability services (see paragraph 62 of this Ruling), the funds received by the recipient from the Department are not assessable recoupments and therefore no amounts are included in their assessable income under Subdivision 20-A.

Interest earned

59. Interest earned on money held in a bank account is ordinarily income from property and assessable to the owner of the bank account.

60. However, any interest accrued in the recipient's direct payments account into which the funds are deposited forms part of the funding and is therefore subject to the same fiduciary obligations owed by the recipient to the Department.

61. Interest accruing to the direct payments account is therefore not ordinary or statutory income of the recipient.

General deductions

62. As the funds received by the recipients are not assessable as either ordinary or statutory income, the losses and outgoings that are incurred in connection with those funds are not allowable as deductions under section 8-1 or any other provision of the ITAA 1997. Consequently, expenses incurred by the recipient in acquiring the goods and services in accordance with the Agreement are not deductible.

Medical expenses tax offset

63. Section 159P of the ITAA 1936 provides that an amount paid by a taxpayer as medical expenses less any amount paid, or entitled to be paid, to the taxpayer or any other person in respect of those medical expenses, is a rebatable amount for the purposes of the medical expenses tax offset.

64. Medical expenses include payments:

- to a legally qualified medical practitioner, nurse or chemist, or a public or private hospital, in respect of an illness or operation;
- for therapeutic treatment administered by direction of a legally qualified medical practitioner; and
- made as remuneration of a person for services rendered by them as an attendant of a person who is blind or permanently confined to a bed or invalid chair.

65. The payments made by the recipient may qualify as medical expenses. However those expenses must be reduced by any payment received or receivable in respect of the expenses to determine the rebatable amount. As the recipient will receive funds from the Department under the Individual Support Package in respect of these expenses there will be no amount which can be treated as a rebatable amount for the purposes of the medical expenses tax offset.

Appendix 2 – Detailed contents list

66. The following is a detailed contents list for this Ruling:

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References

Previous draft:

Not previously issued as a draft

Related Rulings/Determinations:

TR 2006/10

Subject references:

- allowances vs. reimbursements
- assessable income
- assessable recoupments
- deductions & expenses
- disabled care expenses
- income
- medical expenses
- medical expenses rebates
- rebates and offsets

Legislative references:

- ITAA 1936 159P
- ITAA 1997
- ITAA 1997 6-5
- ITAA 1997 6-5(1)
- ITAA 1997 6-10
- ITAA 1997 8-1
- ITAA 1997 10-5
- ITAA 1997 15-2
- ITAA 1997 Subdiv 20-A
- ITAA 1997 20-20(3)

- ITAA 1997 20-30

- TAA 1953
- *Copyright Act 1968*
- *Disability Services Act 2011 (Tas)*

Case references:

- Associated Alloys Pty Limited v. ACN 001 452 106 Pty Limited (in liquidation) (formerly Metropolitan Engineering and Fabrications Pty Limited) [2000] HCA 25; (2000) 46 ATR 91; (2000) 202 CLR 588
- Boardman v. Phipps [1967] 2 AC 46
- Cohen v. Cohen [1929] HCA 15; (1929) 42 CLR 91
- Hospital Products Ltd v. United States Surgical Corporation (1984) 156 CLR 41; 55 ALR 417
- Pavan v. Ratnam (1996) 23 ACSR 214
- Quistclose Investments Ltd v. Rolls Razor Ltd [1970] AC 567; [1968] 3 All ER 651

ATO references

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