



Taxation Determination

Fringe benefits tax: where an employer recognises they mistakenly paid to their employee an amount that the employee is not legally entitled to, but is obliged to repay, and afterwards allows the employee time to repay the amount, is there a 'loan benefit' under subsection 16(1) of the *Fringe Benefits Tax Assessment Act 1986*?

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Ruling

1. Yes. In these circumstances there is a 'loan benefit' under subsection 16(1) of the *Fringe Benefits Tax Assessment Act 1986* (FBTAA).¹ By allowing time for the repayment of the mistakenly paid amount the employer is making a 'loan' (as that term is inclusively defined in subsection 136(1)) to the employee.
2. A loan benefit can arise and continue even where the obligation to repay an amount or part of it is not enforceable by legal proceedings. The employee will cease to be under an obligation to repay the whole or any part of the loan once the loan is fully repaid or that obligation is waived by the employer.

¹ All subsequent legislative references in this Determination are to the FBTAA unless indicated otherwise.

3. It is the employer's allowing of time to the employee to repay the mistakenly paid amount (rather than the employer's payment under a mistake) that gives rise to a loan benefit. Accordingly, the loan benefit will not be excluded from being a 'loan fringe benefit' by reason of paragraph (f) of the definition of 'fringe benefit' in subsection 136(1) of the FBTAA, as the loan benefit, being the allowing of time to repay, is not a payment of salary or wages or a payment that would be salary or wages if salary or wages included exempt income for the purposes of the *Income Tax Assessment Act 1936*.
4. However, the loan benefit may in some circumstances be excluded from being a loan fringe benefit because the benefit is an exempt benefit.

Example

5. *Julia works as a public servant in a government department (the employer). Julia is paid her salary on a fortnightly basis by direct credit into her bank account. During the period 5 July 2006 through to 31 January 2007 (2006-07 FBT Year) Julia temporarily performed duties at a higher pay scale level. A review of the higher duty payments to Julia by the employer's human resources section in early March 2007 identified that Julia had, in error, mistakenly been paid a number of amounts totalling \$7,200 during the period that she performed duties at the higher pay scale. Julia was not legally entitled to the mistakenly paid amounts. The circumstances are such that Julia has an obligation to repay the \$7,200 paid by mistake.*
6. *The employer subsequently advises Julia that she is required to repay the mistakenly paid amounts. Julia advises her employer that she is unable to immediately repay the \$7,200. As such, on 1 April 2007 Julia's employer agrees to allow one year for Julia to repay the \$7,200. The agreement is that the period will be interest-free and there will be 12 monthly instalments of \$600 payable on the last day of each month commencing on 30 April 2007. Julia adheres to the repayment schedule over the 12 month period.*
7. *The employer's allowing of time from 1 April 2007 for Julia to repay the \$7,200 gives rise to a loan benefit in the 2007-08 FBT year under subsection 16(1). The benchmark interest rate for the 2007-08 FBT year is 8.05% and as such the 'notional amount of interest' on the loan is calculated as \$312 for the 2007-08 FBT year. The actual interest on the loan is nil for the 2007-08 FBT year that is, the employer has not charged the employee any interest on the loan. The loan benefit cannot be an exempt benefit under section 58P as the 'notional taxable value' of the benefit is not less than \$300.²*

8. **Note:** this Determination only applies to those cases where the recipient of the payment in question is obliged to repay this amount. Whether or not a recipient of a payment claimed to have been made under a mistake of fact or law fits this description can be a difficult legal question to resolve. For example, the recipient, an employee, may be able to establish a defence to a claim for restitution (see for example, the defences discussed in *David Securities Pty Ltd v. Commonwealth Bank of Australia* (1992) 175 CLR 353; 92 ATC 4658; (1992) 24 ATR 125), and so establish a right to retain the money in question. Where it is established that an employee recipient is under no obligation to repay the amount in question, no loan benefit in respect of that amount can arise for fringe benefits tax purposes.

² Assuming that the 'otherwise deductible rule' in section 19 does not apply so as to reduce the notional taxable value to less than \$300.

Date of effect

9. This Determination applies to years of income commencing both before and after its date of issue. However, the Determination does not apply to taxpayers to the extent that it conflicts with the terms of settlement of a dispute agreed to before the date of issue of the Determination (see paragraphs 75 and 76 of Taxation Ruling TR 2006/10).

Commissioner of Taxation30 April 2008

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.*

Explanation

10. It is the employer's allowing of time to the employee to repay the mistakenly paid amount (rather than the employer's payment under a mistake) that gives rise to a loan benefit. The employer's allowing of time for the employee to repay the mistakenly paid amount to which the employee is not legally entitled, but is obliged to repay, gives rise to the making of a 'loan' as that term is inclusively defined in subsection 136(1). 'Loan' is defined to include:

- (a) an advance of money;
- (b) the provision of credit or any other form of financial accommodation;
- (c) the payment of an amount for, on account of, on behalf of or at the request of a person where there is an obligation (whether express or implied) to repay the amount; and
- (d) a transaction (whatever its terms or form) which in substance effects a loan of money.

11. The employer's allowing of time for the employee to repay the mistakenly paid amount may be express or implied. The employer may expressly agree (either orally or in writing) with the employee to allow the employee time to repay the amount. Alternatively, the employer's allowing of time to repay the amount may be implied from the employer's conduct, which may include a lack of action to recover the amount or insist upon its repayment in a lump sum, or an acceptance of its repayment by instalments.

12. However, a short delay between the employer's identification of a mistakenly paid amount and the employer's request for the employee to repay the mistakenly paid amount would not normally be taken to imply the allowing of time to repay in this context.

13. The circumstances that are the subject of this Determination satisfy paragraphs (b) and (d) of the definition of 'loan' in subsection 136(1). The employer's allowing of time for the employee to repay the mistakenly paid amount satisfies paragraph (b) of that definition as the 'provision of credit or any other form of financial accommodation'. 'Financial accommodation' is not a technical legal expression so recourse is had to its ordinary meaning. The *Macquarie Dictionary* defines 'accommodation' relevantly as 'anything which supplies a want ... a loan or a pecuniary favour' and 'financial' relevantly as 'relating to monetary receipts and expenditures; relating to money matters; pecuniary'. Clearly then, the employer's allowing of time for the employee to repay the mistakenly paid amount, which the employee is obliged to repay immediately, is the provision of a form of financial accommodation.

14. Paragraph (d) expands the definition of 'loan' to include a 'transaction (whatever its terms or form) which in substance effects a loan of money'. 'Transaction' is not defined for the purposes of the FBTAA. In *Grimwade v. Federal Commissioner of Taxation* (1949) 78 CLR 199 at 222, Rich J stated that the ordinary meaning of 'transaction' is 'an act, doing, negotiation or dealing.' The employer's allowing of time for the employee to repay the mistakenly paid amount clearly satisfies that ordinary meaning of 'transaction', in that it is an act of, or the doing of something by, the employer, with respect to the employee.

15. Further, where the employer and employee expressly agree to allow the employee time to repay the amount that is clearly a 'negotiation' or 'dealing' between the two. Paragraph (d) of the definition of 'loan' in subsection 136(1) then requires that the transaction be one that 'in substance effects a loan of money'. The essence of a loan of money is the obtaining of the use of an amount of money for a period of time with an obligation to repay the amount.

16. The employer's allowing of time for the employee to repay the mistakenly paid amount 'in substance effects' (that is, brings about or results in) a loan of money in that the employee obtains for a period of time the use of the money mistakenly paid by the employer with an obligation to repay the amount to the employer at the later time than originally obliged to do so. Therefore, the employer's allowing of time for the employee to repay the mistakenly paid amount satisfies paragraph (d) of the definition of 'loan' in subsection 136(1).

17. The making of a 'loan' by the employer to the employee is taken under subsection 16(1) to constitute a benefit provided by the employer (the provider) to the employee (the recipient) and that benefit is taken to be provided in respect of each year of tax during the whole or a part of which the recipient is under an obligation to repay the whole or any part of a loan.

18. The employee is under an obligation to repay the relevant 'loan' that is the subject of this Determination from the time the employer gives the employee time to repay the mistakenly paid amount.

19. Under the definition of 'obligation' in subsection 136(1), in relation to repayment of an amount, the obligation to repay includes an obligation that is not enforceable by legal proceedings. So a loan benefit can arise and continue even where recovery of the amount of the loan or part of it is statute barred, that is, the obligation to repay an amount does not cease. The employee will cease to be under an obligation to repay the amount of the 'loan' that is the subject of this Determination once the amount of the 'loan' is fully repaid or that obligation is waived by the employer.

20. A loan benefit will be a loan fringe benefit where it satisfies the definition of 'fringe benefit' in subsection 136(1). Whether it satisfies that definition depends on, among other things, whether the benefit is provided 'in respect of the employment of the employee'. Subsection 136(1) provides that 'in respect of', in relation to the employment of an employee, includes by reason of, by virtue of, or for or in relation directly or indirectly to, that employment'.

21. The leading case on the phrase 'in respect of the employment of the employee' in subsection 136(1) is the Full Federal Court decision in *J & G Knowles & Associates Pty Ltd v. Commissioner of Taxation* (2000) 96 FCR 402; 2000 ATC 4151; (2000) 44 ATR 22. In that case the Full Federal Court held that:

the phrase requires a 'nexus, some discernible and rational link, between the benefit and employment'. That, however, does not take the matter far enough. For what is required is a sufficient link for the purposes of the particular legislation ... It cannot be said that any causal relationship between the benefit and the employment is a sufficient link so as to result in a taxable transaction. (at FCR 408; ATC 4156-7; ATR 28) ... what must be established is whether there is a *sufficient* or *material*, rather than a, causal connection or relationship between the benefit and the employment (at FCR 410; ATC 4158; ATR 30).

22. Unless there are facts indicating a contrary conclusion (such as some capacity other than as employee in respect of which the benefit was provided by the employer to their employee), the loan benefit taken under subsection 16(1) to be provided by the employer to the employee in the circumstances that are the subject of this Determination is likely to possess a 'sufficient or material' connection with the employee's employment and is therefore considered to be a benefit provided by the employer to the employee 'in respect of the employment of the employee'. However, whether this is the case is a question of fact to be decided on the circumstances of each case.

23. A benefit will not be a fringe benefit where the exclusion contained in paragraph (f) of the definition of 'fringe benefit' in subsection 136(1) is satisfied, that is, where the benefit is 'a payment of salary or wages or a payment that would be salary or wages if salary or wages included exempt income for the purposes of the *Income Tax Assessment Act 1936*'.

24. Since it is the employer's allowing of time for repayment once the mistakenly paid amount has been identified that satisfies paragraph (b) or (d) of the definition of 'loan' and because the benefit provided by the employer to the employee by allowing time to repay is not itself a payment to the employee, that benefit is not a payment of 'salary or wages' within the meaning of that expression in subsection 136(1). Therefore that benefit is not excluded from the definition of 'fringe benefit' by paragraph (f) of the definition of that expression in subsection 136(1).

25. The loan benefit may in some circumstances be excluded from being a loan fringe benefit by reason of paragraph (g) of the definition of 'fringe benefit' in subsection 136(1) because the benefit is an exempt benefit.

26. It may be that the loan benefit is a minor benefit that is exempt in relation to the particular FBT year pursuant to section 58P. It is not possible to make general conclusions about whether section 58P will always apply to the loan benefit because the satisfaction of several of the requirements for the exemption will depend upon the particular circumstances being considered. For example, the amount of the loan and the length of time during which the recipient is under an obligation to repay the whole or any part of the loan will have a great bearing on whether 'the notional taxable value of the minor benefit in relation to the [relevant] year of tax is less than \$300'³ so as to satisfy paragraph 58P(1)(e).⁴

27. The view expressed in this Determination that a loan benefit can arise in circumstances that are the subject of this Determination has clear policy support from the Explanatory Memorandum to Taxation Laws Amendment (Fringe Benefits and Substantiation) Bill 1987 (the EM). In introducing the exemption for 'minor benefits' as contained in section 58P, the EM, when discussing those kinds of benefits that the exemption in section 58P was likely to apply to and make exempt, listed five examples. One of those examples was 'the recovery of overpaid salary by instalment arrangements'.

28. Whether a 'loan fringe benefit' arises will, as discussed at paragraphs 20 to 26 of this Determination, be dependant on whether the loan benefit satisfies the definition of 'fringe benefit' in subsection 136(1), which includes consideration of whether the loan benefit is an exempt minor benefit.

³ Paragraph 58P(1)(e) of the FBTAA was amended by *Tax Laws Amendment (2006 Measures No. 5) Act 2006*. With effect from 1 April 2007, the minor benefits exemption threshold was increased from 'less than \$100' to 'less than \$300'.

⁴ Taxation Ruling TR 2007/12 Fringe benefits tax: minor benefits, sets out the Commissioner's views on the application of the minor benefits exemption in section 58P.

29. Essentially, the taxable value in relation to a FBT year of a loan fringe benefit that arises in the circumstances that are the subject of this Determination is, in accordance with section 18, the amount (if any) by which the notional interest that would have accrued on the 'loan' during that year (calculated on the daily balance of the loan at the statutory interest rate in relation to that FBT year) exceeds the amount of interest (if any)⁵ that actually accrued on the loan in respect of that FBT year.

⁵ In the ordinary case it is unlikely that interest will actually accrue on the loan that arises in the circumstances that are the subject of this Determination. However, there may be an obligation on the employee to pay interest as part of an agreement with the employer to allow the employee time to repay the 'loan'.

References

Previous draft:

TD 2007/D22

Related Rulings/Determinations:

TR 2006/10; TR 2007/12

Subject references:

- exempt benefits
- FBT loan interest
- FBT statutory interest rate
- fringe benefits
- fringe benefits tax
- in respect of employment
- loan benefits
- loan fringe benefits
- minor benefits

Legislative references:

- FBTA 1986
- FBTA 1986 16(1)
- FBTA 1986 18
- FBTA 1986 58P
- FBTA 1986 58P(1)(e)

- FBTA 1986 136(1)
- ITAA 1936
- TAA 1953
- Tax Laws Amendment (2006 Measures No. 5) Act 2006

Case references:

- David Securities Pty Ltd v. Commonwealth Bank of Australia (1992) 175 CLR 353; 92 ATC 4658; (1992) 24 ATR 125
- Grimwade v. Federal Commissioner of Taxation (1949) 78 CLR 199
- J & G Knowles & Associates Pty Ltd v. Commissioner of Taxation (2000) 96 FCR 402; 2000 ATC 4151; (2000) 44 ATR 22

Other references:

- Explanatory Memorandum to Taxation Laws Amendment (Fringe Benefits and Substantiation) Bill 1987
- Macquarie Dictionary, [Multimedia], version 5.0.0, 1/10/01

ATO references

NO:	2007/2924
ISSN:	1038-8982
ATOlaw topic:	Fringe Benefits Tax ~~ Loan fringe benefits