LCG 2015/9 - Attribution Managed Investment Trusts: trustee shortfall taxation - section 276-420

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Attribution Managed Investment Trusts: trustee shortfall taxation – section 276-420

Relying on this Guideline

This Guideline describes how the Commissioner will apply the law as amended by the *Tax Laws Amendment (New Tax System for Managed Investment Trusts) Act 2016*.

If you rely on this Guideline in good faith, you will not have to pay any underpaid tax, penalties or interest in respect of matters it covers if it does not correctly state how a relevant provision applies to you.

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What this Guideline is about

1. Under the new regime for attribution MITs (AMITs)[1], the trustee of an AMIT works out the amount of the AMIT's assessable income of different tax characters (net of deductions), exempt income, non-assessable non-exempt income and tax offsets, which it can attribute to its members. These amounts, as worked out by the trustee of the AMIT, are called 'determined trust components'.

2. Broadly, mistakes in the calculation of determined trust components made in one year, can be fixed in the year they are discovered without the need to amend prior year returns.[2] A mistake which understates the amount of a character of assessable income is known as an 'under'.

3. Where a trustee fails to recognise all or part of an under of a character of assessable income in the year it should have been discovered, the trustee may be liable to pay tax under section 276-420 on the shortfall.

4. This Guideline explains the operation of section 276-420.[3]

Date of effect

5. This Guideline is a public ruling, effective for those who rely on it in good faith in respect of assessments for income years starting on or after:

- 1 July 2016, or
- if the trustee has made an irrevocable choice to apply the new tax system for its 2015-16 income year which starts on or after 1 July 2015 – 1 July 2015.

Background: section 276-420

6. Section 276-420 is designed to ensure that disputes between an AMIT trustee and the Commissioner, concerning the correct amount of an 'under' to be recognised in a discovery year, can be resolved at the trustee level through the assessment and objection process.

Explanation

Section 276-420 shortfall taxation

7. Applying section 276-420 broadly requires a comparison to be made between two amounts:

- the 'under' as determined by the trustee in accordance with section 276-345 for a particular discovery year (the 'trustee determined under') – paragraph (1)(a), and
- what the 'under' for that discovery year would have been if it were worked out on the basis of an objective application of the law to what the trustee should have known at the discovery time ('the objectively determined under') – paragraph (1)(b).

[1] An AMIT is a managed investment trust that has elected in to the attribution regime for the taxation of MITs contained in Division 276 of the *Income Tax Assessment Act 1997* (ITAA 1997). All legislative references in this Guideline are to the ITAA 1997 unless otherwise indicated.

[2] Subdivision 276-F.

[3] Section 276-425 applies in a similar way to overs of offsets. To the extent that the two provisions use the same terminology, this Guideline can also be used as an indication of the Commissioner's approach to section 276-425.

8. A trustee of an AMIT is liable to pay tax where the 'trustee determined under' falls short of the 'objectively determined under'. The tax payable equals 45% (47% in a temporary budget repair levy year) of the shortfall.[3A] However, the shortfall is reduced to the extent it is reflected in an under of a later year.[3B] See also the Commissioner's power of remission in paragraph 35 of this Guideline.

9. If there is a shortfall, the 'running balance account' for the determined trust component (in effect, the determined trust component for the base year, plus any prior year 'under' worked out by the trustee and minus any prior year 'over' worked out by the trustee)[4] is increased by the amount of the shortfall.[4A] This ensures that any later adjustments to the running balance account (for example, further unders or overs) appropriately take into account all relevant amounts already recognised – including a shortfall arising under section 276-420.

'Trustee determined under' – paragraph 276-420(1)(a)

10. Broadly, a 'trustee determined under' of a particular income character is recognised when the trustee of an AMIT works out the amount of an under according to section 276-345. This typically occurs where the trustee becomes aware of income that should have been (but was not) taken into account in the calculation of a determined trust component for an earlier 'base year'.

11. The omitted income may result from a change in the trustee's knowledge of the facts and/or the trustee's view of the law. Rather than needing to go back and revise the calculations for the base year and reissue 'AMMA statements'[5], the trustee may choose to account for the variance as an 'under' adjustment to the trust component of that character in the later 'discovery year'.

12. Under subsection 276-345(3), the trustee is to work out the 'trustee determined under' by comparing:

(a) the 'trust component' worked out in the discovery year on the basis of the trustee's knowledge at the discovery time,[6] and

(b) the 'determined trust component' for the base year (if the determined trust component is the first year after the discovery year) or, otherwise, the 'running balance account' amount.[7]

13. The trustee's knowledge at the 'discovery time' includes the trustee's knowledge of the factual circumstances relevant to the calculation of the trust components.

Discovery of under does not necessarily require reallocation of expenses for base year

14. Trust component is defined in section 276-260. A trust component of a particular character for an income year is the amount of that character worked out for the AMIT using the rules in sections 276-265 and 276-270. The trust components of a character relating to the assessable income of the AMIT should be net of deductions. Section 276-270 provides rules for allocating deductions.[7A]

[3A] Subsection 12(13) of *the Income Tax Rates Act 1986* (ITRA) and item 3C of the table to subsection 35(1) of the ITRA.
[3B] Subsections 276-420(4) and (5).
[4] Paragraph 276-345(3)(b).
[4A] Subsection 276-420(3).
[5] AMIT member annual statements.
[6] Paragraph 276-345(3)(a).
[7] Paragraph 276-345(3)(b).
[7A] See also Law Companion Guideline LCG 2015/8 *Attribution Managed Investment Trusts: the rules for working out trust components – allocation of deductions.*

15. When considering the difference between the base year determined trust component and the trust component worked out at the discovery time, provided that the base year deductions were allocated on a reasonable basis (and the under is not attributable to excessive deductions claimed in the base year), there is no need to reallocate the deductions in calculating the discovery year amount. In such cases, the gross income not included in the base year will be the amount of the under.

Discovery of under may affect deductibility of expenses

15A. The nature of an under may affect the deductibility of an expense. For example, if an amount which was treated as exempt income in a base year is treated as assessable income in a discovery year, this may result in an increase in allowable deductions. The additional deductions may be taken into consideration in working out the amount of the under.

'Objectively determined under' – paragraph 276-420(1)(b)

16. The 'objectively determined under' for the discovery year is worked out on the basis of:

- what the trustee *should* have known at the discovery time (that is, what it is reasonable to assume their knowledge should have been in the light of the overall circumstances, including information properly available to the trustee in their capacity as trustee of that trust and information it might reasonably be expected the trustee would have sought), and
- how the law actually applied to those matters the trustee should have known at that time.

16A. For the purpose of working out what the trustee should have known at the relevant discovery time, a position on the law or facts taken by the Commissioner will be taken to be a thing the trustee should have known at the time the Commissioner notifies the trustee of the confirmed position. This is generally when the Commissioner issues a final position paper. This means that if the Commissioner notifies the trustee of the confirmed position before the discovery time for an income year, and (for example) the Commissioner's position is affirmed by Independent Review after the discovery time, the trustee would be taken to have knowledge of the Commissioner's position before the relevant discovery time. If the position in the final position paper is subject to the ATO's Independent Review but that position is not ultimately affirmed by that Review, generally there will be no shortfall.

When will the possibility of shortfall taxation arise in practice?

17. The issue of shortfall taxation may arise where the Commissioner takes the view (on the basis of a view of the law or the facts in respect of a base year) that – in respect of a determined trust component of an income character – there should have been an under (or a greater under) worked out by the trustee in a particular discovery year.

17A. The discovery year in this context is typically the first year in which the trustee could have recognised the under, based on what they should have known at the time, rather than the year in which a compliance review is undertaken. The discovery year may also be a later year.

18. Subject to applicable time limits[7B], if the trustee disagrees with the Commissioner's view, and declines to either make an under adjustment in the current year, or to reissue AMMA statements for the base year, the Commissioner may issue an assessment for the discovery year which includes the tax payable on the shortfall. The trustee may object to this assessment.

[7B] Section 276-350.

19. Subject to applicable time limits[8], the trustee may also eliminate the shortfall after the issue of the assessment by recognising the under in a subsequent income year or by issuing replacement AMMA statements for the base year. To the extent that the amount is dealt with in this way, the shortfall is reduced[9] and the assessment would be amended.

Example 1: making a shortfall assessment

20. *The Lunch Trust is an AMIT. In the 2017-18 income year (the discovery year), its trustee discovers a previously unrecognised amount of $1,000 that relates to the 2016-17 income year (the base year). The trustee considers the discovered amount consists of:*

- *assessable income of $800, and*
- *non-assessable non-exempt income (NANE) of $200.*

21. *Therefore, in the 2017-18 income year, the Lunch Trust recognises:*

- *a $800 under having the character of ordinary income, and*
- *a $200 under having the character of NANE.*

22. *In the 2018-19 income year (the current year), the Commissioner undertakes a compliance review and concludes that the whole of the discovered amount was assessable as ordinary income. As a result, the Commissioner considers $1,000 should have been recognised as an under of ordinary income in the 2017-18 income year, not only $800. This view is communicated to the trustee in a final position paper.*

23. *If the trustee of the Lunch Trust accepts the Commissioner's view, they could adjust for the variance by recognising at the discovery time in the current 2018-19 income year the following amounts as unders and overs in relation to the 2016-17 base income year:*

- *an additional $200 under of an ordinary income, and*
- *a $200 over of NANE.*

24. *Alternatively, the trustee may be able to issue replacement AMMA statements to members for the 2016-17 base income year.*

25. *However, if the trustee neither recognises a further under in the current year (2018-19), nor reissues AMMA statements for the base year, the Commissioner may issue an assessment for the 2017-18[10] or 2018-19[11] income year that includes the tax payable on the $200 shortfall.*

26. *If the trustee disagrees with the assessment, they may object to the assessment in the manner set out in Part IVC to the Taxation Administration Act 1953 or, subject to applicable time limits, reduce the shortfall as outlined in paragraph 19 of this Guideline.*

Time limits relevant to the section 276-420 assessment process

27. Two time limits are relevant to section 276-420 shortfalls: the 'limited discovery period'[12] for recognising unders and the time limit applicable to the replacement of AMMA statements[13].

28. Broadly, under section 276-350, an AMIT does not have an under once the hypothetical amendment period has ended (the limited discovery period). The Commissioner will treat this time limit as also precluding the Commissioner from making an assessment of tax payable under subsection 276-420(2) (a shortfall assessment) once the limited discovery period has ended.

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[8] Section 276-350.
[9] Subsections 276-420(4) and (5).
[10] The Commissioner may issue an assessment before the discovery time for the 2018-19 income year that is, the time just before the trustee works out the determined trust component for the relevant character for 2018-19.
[11] An assessment for 2018-19 can only be issued after the 2018-19 discovery time.
[12] Section 276-350.
[13] Subsection 276-460(3).

28A. This treatment means the trustee and the Commissioner would be precluded from recognising an under or an increase in an under once the time limit has expired. The time limit is determined as if section 170 applied to the assessment the Commissioner is assumed to have made for the purpose of section 276-350. Therefore, there is no time limit if the Commissioner is of the opinion that there has been fraud or evasion. Furthermore, the provisions in subsection 170(7) would be available to extend the limited discovery period.

29. A shortfall assessment under section 276-420 will generally be an amended assessment of the trustee of the AMIT's original assessment of tax payable for the discovery year (including nil). The Commissioner has the power under the amendment rules in section 170 to amend the amended assessment (that is, the shortfall assessment) in a way that reduces the trustee's liability.

30. In some circumstances, a shortfall assessment may be an original assessment.

Example 2: time limits

31. *On 20 September 2017, the trustee of an AMIT creates a document which states the amounts of the AMIT's trust components for 2017*[14]*. The limited discovery period for the 2017 base year is due to expire on 20 September 2021*[15]*.*

31A. *Based on what the trustee should have known at the discovery times*[16] *for the 2018, 2019 and 2020 discovery years, there was no under in any of these years. However, the Commissioner considers that, at the discovery time for 2021 (just before 15 September 2021*[17]*), there was an under in relation to the 2017 base year based on what the trustee should have known at that time. The trustee, however, does not recognise the under in its relevant determined trust component (documented as required by subsection 276-255(2) on 15 September 2021) for the 2021 discovery year. The Commissioner issues a shortfall assessment before 20 September 2021. The trustee lodges a return for the 2021 income year after 20 September 2021. Accordingly, the shortfall assessment is an original assessment.*

32. *If the trustee disagrees with the shortfall assessment, it may object in the manner set out in Part IVC to the Taxation Administration Act 1953.*

33. *If the trustee agrees with the assessment, it will need to pay tax on that shortfall under subsection 276-420(2). Ordinarily the trustee would alternatively have the option of reducing the shortfall by:*

- *revising the determined trust component document for the base year and issuing or reissuing AMMA statements for that year based on the revised amounts, or*
- *including the under in the relevant trust component.*

34. *However, these options are not available to the trustee in this example as:*

- *The option of issuing a replacement AMMA statement for the base year is itself subject to the four year time limit in subsection 276-460(3). In this example, the four years to issue an AMMA statement for the 2017 year expired on 30 June 2021.*

[14] Subsection 276-255(2).

[15] The limited discovery period is a hypothetical amendment period. It is measured by assuming that the Commissioner made an assessment of the trust components on the day the document stating the trust components was created. The hypothetical amendment period will generally be 4 years from the day the document is created: section 276-350.

[16] The discovery time is the time just before the trustee works out the determined trust components for a discovery year: subsection 276-345(2).

[17] Unlike the date on which the limited discovery period ends (that is, 20 September 2021), the discovery time for 2021 is not linked to any earlier date.

- *Section 276-350 prevents an under arising outside the limited discovery period, which in this example ended on 20 September 2021. Any under not already worked out by the trustee at this time can only be worked out when it works out its determined trust components for the 2022 year – which is after the limited discovery period. Accordingly, the trustee will not have an under that reflects the shortfall in respect of which subsections 276-420(4) and (5) would otherwise operate to reduce the shortfall.*

Remission of tax

35. The Commissioner has the power under section 276-430 to remit the whole or part of income tax payable under any of the shortfall or excess taxation provisions in Subdivision 276-G if the Commissioner is satisfied that remission would not result in any detriment to the revenue. For example, to the extent a shortfall under section 276-420 would have been attributed to tax-exempt entities, remission of the tax would not result in any detriment to the revenue.

Commissioner of Taxation
5 May 2016

References

ATOlaw topic(s)	Income tax ~~ Trusts ~~ Other
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	TAA 1953 TAA 1953 Pt IVC Tax Laws Amendment (New Tax System for Managed Investment Trusts) Act 2016