


TD 96/2 - Income tax: can section 36A of the Income Tax Assessment Act 1936 apply if a sole trader who owns trading assets declares himself or herself to be a trustee of a discretionary trust over the assets?

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 This ruling contains references to repealed provisions, some of which may have been rewritten. The ruling still has effect. Paragraph 32 in [TR 2006/10](#) provides further guidance on the status and binding effect of public rulings where the law has been repealed or repealed and rewritten. The legislative references at the end of the ruling indicate the repealed provisions and, where applicable, the rewritten provisions.

 This document has changed over time. This is a consolidated version of the ruling which was published on *29 November 2006*

This Determination, to the extent that it is capable of being a 'public ruling' in terms of Part IVAAA of the *Taxation Administration Act 1953*, is a public ruling for the purposes of that Part. Taxation Ruling TR 92/1 explains when a Determination is a public ruling and how it is binding on the Commissioner. Unless otherwise stated, this Determination applies to years commencing both before and after its date of issue. However, this Determination does 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 the Determination (see paragraphs 21 and 22 of Taxation Ruling TR 92/20).

Taxation Determination

Income tax: can section 36A of the *Income Tax Assessment Act 1936* apply if a sole trader who owns trading assets declares himself or herself to be a trustee of a discretionary trust over the assets?

1. No.

2. Section 36A is founded on the existence of undivided fractional interests in trading assets and a change in those interests. The section does not apply to all changes in interests in trading assets. *FC of T v. Westraders Pty Ltd* 80 ATC 4357 per Mason J at 4367 and 4368; (1980) 11 ATR 24 at 36 and 37 and *Glenfield Estates Pty Ltd v. FC of T* 88 ATC 4548 per Lockhart J, with whom Wilcox and French JJ agreed, at 4561; (1988) 19 ATR 1426 at 1441 broadly support the view that section 36A comprehensively applies to changes in undivided fractional interests in trading assets.

3. If a sole trader declares himself or herself to be a trustee of trading assets in favour of a class of beneficiaries under a discretionary trust, there is no change in any undivided fractional interests in the trading assets. On one view, the sole trader who legally (and beneficially) owned the trading assets, before the declaration, has a legal interest in the assets after the change - he or she retains legal title to the assets (albeit as a trustee) but has divested himself or herself of a beneficial interest in the assets. On an alternative view, the sole trader in declaring himself or herself to be trustee creates (out of, but distinct from, his or her legal and beneficial ownership of the trading assets as sole trader) an equitable interest which did not previously exist. Subsection 36A(1) does not apply because, on either view, there is no change in any undivided fractional interests in the trading assets and the sole trader has no undivided fractional interest in the trading assets after the declaration of trust.

4. Section 36 also does not apply to the declaration of trust because the sole trader did not transfer the entirety of his or her ownership of the assets. Section 36 is concerned with the disposal of the whole or part of the assets of a business. When section 36 speaks of disposing of the assets of a business, *Rose v. FC of T* (1951) 84 CLR 118; 9 ATD 334 makes it clear that section 36 is speaking of a transfer of the proprietor's entirety of ownership of the assets. Because the sole trader's entire ownership in the assets is not disposed of on the declaration of trust by the sole trader (the sole trader retaining a legal interest in the assets), the same kind of difficulty that arose in the *Rose* case is present and section 36 cannot apply.

Overall effect

5. On the basis that sections 36 and 36A do not apply, the provisions of subsections 25(1), 28(2) and (3) and 51(1) apply, as relevant, to the trading assets in the hands of the sole trader and, after the declaration of trust, in the hands of the trustee of the trust estate.

Definitions

6. The expression 'trading assets' is used in this Taxation Determination to mean assets of a business (being trading stock, standing or growing crops, crop stools or trees which have been planted and tended for the purpose of sale).

The expression 'undivided fractional interest' is used in this Taxation Determination in the same sense that it is used in the *Rose* case. A transfer of an undivided fractional interest in assets is the vesting in another or others of an undivided share or shares in the assets.

Example

Maybell Fresian owns a grazing business in Gippsland, Victoria. Maybell purchased livestock in the 1993-94 income year for \$30,000 and valued them at cost on 30 June 1994. Early in the 1994-95 year she declares that she holds her business and all of its assets as trustee of her family discretionary trust. No consideration is paid for the livestock on the declaration of trust. The trust sells the livestock later in 1994-95 for \$35,000.

Neither section 36A nor section 36 applies to the declaration of trust.

Maybell is entitled to a deduction in 1994-95 of \$30,000 under subsection 28(3).

The trustee, in calculating the 'net income' of the trust estate in terms of the definition in subsection 95(1) for 1994-95, must include the sale proceeds of \$35,000 in assessable income in accordance with subsection 25(1).

Commissioner of Taxation

17 January 1996

FOI INDEX DETAIL: Reference No. I 1014797

Previously issued as Draft TD 94/D68; TD 95/D11

Related Determinations: TD 96/1; TD 96/3; TD 96/4

Related Rulings:

Subject Ref: declaration of trust; discretionary trusts; trading assets disposal; trading assets ownership; trading stock; trustees; undivided fractional interest

Legislative Ref: ITAA 25(1); ITAA 28(2); ITAA 28(3); ITAA 36; ITAA 36A; ITAA 36A(1); ITAA 51(1); ITAA 95(1)

Case Ref: Glenfield Estates Pty Ltd v. FC of T 88 ATC 4548; (1988) 19 ATR 1426; Rose v. FC of T (1951) 84 CLR 118; 9 ATD 334; FC of T v. Westraders Pty Ltd 80 ATC 4357; (1980) 11 ATR 24

ATO Ref: NAT 95/6458-6; TDUMG 94/1

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