

TD 2002/1 - Income tax: Is a payment by a taxpayer to a fighting fund deductible to the taxpayer under section 25-5 of the Income Tax Assessment Act 1997 ('the Act') where it is set up to fund litigation, negotiate a settlement outcome, or to otherwise manage an income tax dispute arising from an investment or scheme?

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Taxation Determination

Income tax: Is a payment by a taxpayer to a fighting fund deductible to the taxpayer under section 25-5 of the *Income Tax Assessment Act 1997* ('the Act') where it is set up to fund litigation, negotiate a settlement outcome, or to otherwise manage an income tax dispute arising from an investment or scheme?

Preamble

*The number, subject heading, date of effect and paragraphs 1 to 5 of this Taxation Determination are a 'public ruling' for the purposes of Part IVAAA of the **Taxation Administration Act 1953** and are legally binding on the Commissioner. The remainder of the Determination is administratively binding on the Commissioner. Taxation Rulings TR 92/1 and TR 97/16 together explain how a Determination is legally or administratively binding.*

Date of Effect

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 settlement of a dispute agreed to before the date of the Determination (see paragraphs 21 and 22 of Taxation Ruling TR 92/20).

1. Yes, provided that payments by the fund will be for managing the tax affairs of the contributors and are, therefore, 'tax-related expenses' under section 25-5 of the Act.
2. The payment is incurred and is an allowable deduction to the contributor in the year in which the contribution is made to the fighting fund where the following conditions are met and can be demonstrated to the satisfaction of the Commissioner:
 - The fighting fund is set up for the purpose of funding litigation, negotiating a settlement outcome or to otherwise manage an income tax dispute in relation to an investment or scheme;
 - A taxpayer contributing to the fund and seeking a deduction:
 - is a participant in the investment or scheme;
 - has claimed or will claim a deduction in relation to the investment or scheme;
 - has had or will have a deduction disallowed; and
 - is disputing or will dispute the disallowance of the deduction;

- It is reasonable to expect that the outcome of the dispute will apply to the contributor; and
- The fighting fund is a properly administered trust fund such that:
 - contributions received are held in trust to meet the costs of litigation, the costs of negotiating a settlement outcome, or to otherwise manage an income tax dispute of the contributors, and can only be applied towards meeting such costs and expenses;
 - any funds not applied to funding litigation, negotiation, or to otherwise manage an income tax dispute (i.e., any surplus funds after the costs are paid) will be returned to the contributors in proportion to their contributions;
 - any costs recovered are to be paid back to the fighting fund and any surplus will be passed on to the contributors once all the expenses are met;
 - the trust fund will be wound up when the matter in dispute is finalised; and
 - the trustee of the fund properly accounts for all amounts received and paid.

3. Any amounts recouped from the trustee will be assessable income under section 20-30 of the Act in the income year they are received.

4. In some cases it may not be practicable or possible to return surplus funds to contributors upon termination of the fund. In these circumstances, payment of the surplus to a deductible gift recipient under the Act will not result in the denial of the section 25-5 deduction.

Example:

5. *The 'ABC Trust' is set up to fund litigation resulting from a disallowance of deductions in the B Investment Venture. The litigation involves Betty, a participant in the B Investment Venture who has had her deductions in relation to the scheme disallowed. John, who is also a participant in the scheme, contributes \$5000 to the fighting fund during October 2001. John is entitled to claim a deduction for the \$5000 in the income year in which the payment is made.*

The total contribution from all contributors is \$110,000.

At the completion of the litigation there is a surplus amount in the trust which is returned to the contributors. John receives 5000/110,000 of the surplus, which he includes in his assessable income in the income year in which he receives it.

Commissioner of Taxation

16 January 2002

Previous draft:

Previously released in draft form as TD 2001/D12

Subject references:

- Tax-related expenses
- Managing your tax affairs
- Tax affairs

Legislative references:

- ITAA 1997 25-5

- ITAA 1997 20-30

ATO references:

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