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PRIVATE AND CONFIDENTIAL

Director
The Treasury
Langton Cres
PARKES ACT 2600

By Email: *taxadministrationconsultation@treasury.gov.au*

Dear Director

MODERNISING TAX ADMINISTRATION SYSTEMS

1. Thank you for the opportunity to provide comments to Treasury in relation to the exposure draft legislation titled Treasury Laws Amendment Bill 2025 ("**ED**") and the draft explanatory memorandum ("**EM**") relating to the reporting of tax file numbers ("**TFNs**") of beneficiaries of closely held trusts. We acknowledge that this submission has been provided after the required date, however we have provided our comments nonetheless where they can be assistance in finalising this legislative package.

2. Pitcher Partners specialises in advising taxpayers in what is commonly referred to as the middle market. A significant proportion of taxpayers in the middle market operate through trusts, many of which are directly affected by the TFN reporting requirements in Division 6D of Part III of the *Income Tax Assessment Act 1936* (Cth) ("**ITAA36**").

3. We note that the proposed changes to the TFN reporting rules would require trustees to report beneficiaries' TFNs through the income tax return, rather than via the existing quarterly TFN reporting framework. We agree with this proposed change and welcome opportunities such as this that are aimed at reducing the number of separate lodgements that a trustee must complete.

4. The proposals are a part of the implementation of the next phase of changes to the income tax reporting systems for trusts as announced in the 2024-25 MYEFO. We understand that a significant aim of these changes is to reduce compliance costs for trustees, beneficiaries and their agents.

5. In line with that objective, we believe that there are numerous additional changes that could be made to the income tax provisions that are closely related to the TFN reporting provisions. These changes would both assist in ensuring trust reporting is accurate as well as reducing the compliance costs of completing income tax returns.

TFN withholding for closely held trusts

6. Sections 12-175 and 12-180 of Schedule 1 to the *Taxation Administration Act 1953* (Cth) requires that the TFN of a beneficiary be provided to the trustee prior to the payment of a distribution or the creation of a present entitlement. This imposes an additional compliance issue for tax agents in determining the time at which the beneficiary has actually reported the TFN. With the removal of quarterly reporting, the ability to evidence that this requirement has been satisfied will become more difficult.

7. We recommend that a technical change be made to those provisions that deem the provision to be satisfied where the trustee reports the TFN in the beneficiary schedule of the income tax return where the income tax return is lodged by the due date for lodgement. This provision would only be operative if those conditions are otherwise satisfied. Where they are not, the ordinary withholding provisions would operate.

8. Based on how the change is proposed (i.e. it should only operate where the TFNs are reported in an income tax return lodged on time), there should be no risk to the revenue with this change. We believe that this should complement the proposed changes in the ED, will indicate to the ATO which distributions required TFN withholding, and will reduce compliance costs of agents in determining (unnecessarily) the date of reporting the TFN to the trustee.

Redundant reporting requirements under Division 6D

9. Division 6D currently imposes reporting obligations that duplicate information already disclosed in the income tax return. For example, closely held reporting rules require trustees to report the untaxed part and tax preferred part in the "correct TB statement", despite this information already being largely captured in the statement of distribution.

10. The "untaxed part" refers to the beneficiary's share of the trust's net income that is not already taxed under subsection 98(4) of the ITAA 1936, nor subject to withholding under Subdivision 12-H of Schedule 1 to the *Taxation Administration Act 1953* (Cth). However, within the statement of distribution the trustee is already required to disclose the beneficiary's share of the trust's net income, the amount taxed under subsection 98(4), and any amount subject to withholding. The additional requirement to separately report the residual figure, which is no more than a straightforward mathematical calculation, is therefore unnecessary. Despite this, failure to disclose that amount at the correct label in the income tax return exposes the trustee to administrative penalties.

11. Similarly, the disclosures of 'tax preferred' amounts seem unnecessary given the trustee reports the share of income of the trust estate already. There should be no need for the trustee to report capital distributions to another trustee.

12. Given the detail now included in the annual return, and the proposal to include the beneficiaries TFN within the income tax return, these additional disclosures no longer appear necessary.

13. The original rationale for Division 6D was to provide the ATO with transparency over trust distributions at a time when this data was not otherwise captured. Modern systems – particularly advances made under the Modernisation of Trust Administration Systems ("**MTAS**") project which involved, relevantly, the digitisation of trust income and reporting within the Australian Taxation Office - have removed that gap. As such, the rules now impose compliance costs on small business taxpayers without serving a meaningful

integrity purpose. A similar burden was recognised through the removal of family trusts from the scope of Division 6D.

14. Finally, we note that the Commissioner has the power under subsection 102UK(1A) to, by legislative instrument, determine that a specific class of trustee beneficiary not be required to make a correct TB statement.

15. The Explanatory Memorandum to the *Taxation (Trustee Beneficiary Non-Disclosure Tax) Bill (No. 2) 2007*, in particular, observes that it may be appropriate to exercise if the Commissioner was satisfied, he had all the relevant information already:

> *The Commissioner may make a determination under subsection 102UK(1A) that a specified class of trustees is not required to make a correct trustee beneficiary statement. The determination may be expressed to be subject to conditions and may cover more than one year of income. The determination power will allow the requirement for an annual statement to waived if, for example, the Commissioner is satisfied with other information provided by trustees or held by the Commissioner about the trustee of the closely held trust or its trustee beneficiaries, that would allow net income or tax-preferred amounts to be traced to relevant taxpayers. Another example may be where a trustee of a closely held trust has given the Commissioner a correct trustee beneficiary statement in a year of income, and in future years, the only change may be to the amounts paid to the trustee beneficiaries.*[1]

16. At the very least, we consider that the Commissioner should exercise his power to determine that trustee beneficiaries that already disclose the relevant information in the statement of distribution for the trustee beneficiary, where the TFN of that trustee beneficiary is also reported in the statement of distribution, should not be required to make a correct TB statement. We note that making a legislative change to this effect would help simplify unnecessary disclosures in the income tax return.

Redundant provisions such as circular trust distribution rules

17. We also draw attention to provisions addressing circular trust distributions, which were introduced at a time when the ATO had limited visibility over the flow of trust distributions between entities. With the MTAS project and significantly improved system data matching, these rules appear to have outlived their original purpose. Their continued application adds complexity for closely held groups without providing meaningful integrity protection.

18. Additionally, the outcome in *Advanced Holdings Pty Limited as trustee for The Demian Trust v FCT* [2020] FCA 1479 suggests that the tax payable under section 102UM may not have any practical effect. The case involved a circular distribution that occurred between family trusts in the 2013 income year, before the amendments expanded the rules to cover such trusts.

19. Paragraphs 156 to 168 outline that the Commissioner successfully argued that the distributions were taxable to the trustee at the top marginal rate under section 99A due to very circumstances caused by the circularity resulting in additional net income derived that cannot be made subject of a present entitlement.

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[1] Paragraph 4.20

Recommendation relating to Family Trust Elections

Supporting trust distribution compliance

20. The proposed changes can also be modified to help assist compliance with the family trust election ("**FTE**") provisions. Currently taxpayers may not, appropriately, consider the FTE provisions when making a distribution from a trust.

21. Some simple changes that could be made include: (a) requiring the test individual to be named in the income tax return FTE disclosure; (b) requiring the test individuals' TFN to be included in the income tax return entity in the trust distribution schedule, or (c) state whether the recipient entity is part of the family group of the individual specified in the distributing trust's FTE and, if so, how (e.g. as a wholly-owned entity, member of the family, charity, IEE elected entity, etc). This could ensure that distributions from one trust to another entity outside of the family group are automatically detected by tax compliance software.

22. The proposed changes would assist in data matching for both tax agents and the ATO and would assist in identifying any family trust distribution tax ("**FTDT**") obligations as early as possible. This could help overcome the issue of FTDT being applied retrospectively upon detection many years after the event.

23. The above would require changes, which may be systems changes rather than legislative changes. However, one change that would support the above would be to mandate the requirement to lodge FTEs with the ATO.

Lodging FTEs with the ATO

24. Historically, FTEs were required to be lodged with the ATO. That requirement was removed on the basis that elections could instead be recorded and retained privately by taxpayers and advisers. However, this change has given rise to several practical issues:

    24.1. Difficulty validating that an election was made, particularly where advisers have changed or historical files have been misplaced.

    24.2. Inability for the ATO to substantiate the existence of an election when reviewing taxpayers' positions, which creates uncertainty for both taxpayers and administrators.

    24.3. Lack of continuity between tax practitioners, as new advisers frequently inherit clients without access to complete historical trust documentation.

    24.4. Lack of an ability for agents to identify whether current year distributions give rise to FTDT obligations.

25. Reinstating a lodgement requirement for FTEs would deliver substantial benefits. It would enable the ATO to maintain a central register of elections, display the relevant information in the Tax Portal, and provide continuity of records where advisers, systems, or organisational structures change. This would also support the goals of simplified trust reporting and the modernising trust register project.

Practical pathway to reporting FTEs

26. The above proposed changes require a proper system to support the determination as to whether FTEs have been validly made. The validity of an election and evidencing an election has been made is currently a significant issue.

27. There may be a further opportunity to consider a practical pathway for perfecting historical records in circumstances where an election was validly made but the documentation cannot be located or is not yet reflected in the Tax Portal.

28. For example, by reinstating the requirement to lodge the FTE with the Commissioner, there could be an opportunity to: (a) legislatively accept that FTEs recorded in the ATO portal are deemed to be valid unless disputed within a reasonable time; and (b) provide taxpayers an opportunity to perfect their records on the portal where historical records have not been lodged. These requirements should result in no additional compliance costs to taxpayers. That is:

    28.1. If the income tax return included the test individual and their TFN, this could act as the approved form. Accordingly, lodgement of the income tax return should satisfy the approved form requirement. This could include elections for the most recent specified year and earlier years.

    28.2. Perfection of the records could be done in the following income tax return (following the amendment of the provisions), with a box ticked noting that the records are being perfected. Again, this would remove the requirement to lodge a separate form with the ATO.

    28.3. Where no change is made to the portal information, this could act as 'acceptance' by the trustee that the election is deemed to have been validly made, subject to the satisfaction of other requirements such as the family control test or the requirement about prior distributions being made within the family group for retrospective elections.

29. These minor modifications would provide certainty as to whether FTEs have been made and would help to support tax agents and taxpayers in assessing FTDT at the time of distribution. It would significantly enhance the ATO data matching and reporting function of the income tax return and thus would help support the proposed changes to be implemented by the ED.

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30. We believe that the ED presents a valuable opportunity to reassess legacy provisions that impose compliance costs without delivering commensurate integrity benefits. Streamlining Division 6D, reinstating the lodgement and reporting of FTEs, and reviewing redundant trust distribution rules would materially improve the administration of trust taxation for small and medium businesses and also assist the ATO in identifying distribution compliance in real time.

31. We appreciate the opportunity to contribute to the consultation process and would be pleased to discuss these issues further.

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If you would like to discuss any aspect of this submission, please contact either Leo Gouzenfiter on (03) 8612 9674 or me on (03) 8610 5170.

Yours sincerely

A M KOKKINOS
Executive Director