Tax, trusts and gifts

Samuel Hoare reports on *Commissioner of Taxation v Carter* [2022] HCA 10

The High Court has held that s 97(1) of the *Income Tax Assessment Act 1936* (Cth) (Act) has the effect that the assessable income of a trust beneficiary is determined by ascertaining the proportion of the distributable income of the trust to which that beneficiary has a present entitlement immediately prior to the end of the relevant income year. A disclaimer after that time is therefore ineffective to alter a beneficiary's tax liability.

Background

The trust deed by which the 'Whitby Trust' was settled had the effect that if the trustee failed, before the end of an income year, to appoint the trust income to or for its beneficiaries or to accumulate the income, that income would be held in trust for listed beneficiaries in equal shares. The vesting date for those trusts was the last day of the relevant income year.

In the 2014 income year, the trustee failed

to appoint or accumulate the income of the trust. The trustee then distributed the income for that income year to the listed beneficiaries, three of whom were the respondents to the appeal, in five equal shares.

Section 97(1), appearing in Div 6 of Pt III of the Act, relevantly provides that:

> where a beneficiary of a trust estate who is not under any legal disability *is presently entitled* to a share of the income of the trust estate… the assessable income of the beneficiary shall include… so much of that share of the net income of the trust estate as is attributable to a period when the beneficiary was a resident. (*Emphasis added.*)

Relying on s 97(1), the commissioner of taxation issued amended notices of assessment for the 2014 income year to each respondent which included as assessable income one-fifth of the income of the trust. The respondents then executed deeds of disclaimer in respect of the distributions by which the respondents purported to disclaim any right, title or interest conferred by the trust deed to any such income.

The respondents objected to the amended notices of assessment on the basis that, relevantly, each had disclaimed the distributions. The Full Court of the Federal

Court accepted that the respondents' disclaimers 'expunged' their entitlements to the distributions for the purposes of s 97(1), despite occurring after the end of the 2014 income year.

The High Court's decision

Gageler, Gordon, Steward and Gleeson JJ (Edelman J concurring at [33]) allowed the commissioner's appeal.

First, as the court had previously held in *Commissioner of Taxation v Bamford* (2010) 240 CLR 481, the key expression in s 97(1), 'is presently entitled', focuses on a beneficiary's legal entitlement to the income (i.e., right as a matter of the law of trusts) not receipt ([1], [20]). This follows from the text of the expression, confirmed by the purpose of Div 6, being to treat trusts as conduits through which a beneficiary receives income.

Secondly, contrary to the Full Court's decision, the key expression directs attention to the entitlement that existed immediately before the end of the income year for which the assessment is being made ([22]). Textually, the expression is in the present tense ([19]). Contextually, the other criteria in s 97(1), being absence of legal disability and tax residency, and other provisions of Div 6 (and Div 5, in respect of partnership income) have a similarly fixed temporal focus ([23]). Purposively, this focus promotes certainty in the assessment of taxation liability and is consistent with the object of Div 6 being to tax a beneficiary by reference to entitlement not receipt ([24], [26]).

Applying this construction of s 97(1), the court held that one-fifth of the income of the trust was held for each of the listed beneficiaries immediately prior to the end of the 2014 income year and therefore formed part of the respondents' assessable income for that income year. The deeds of disclaimer could not retrospectively alter the rights against the respondents gained by the commissioner by operation s 97(1), so construed ([27]).

The respondents' alternate contention

The respondents contended in the alternative that the deeds of disclaimer were evidence that they had never intended to accept the distributions. Assent of the donee being an element necessary for an effective gift, it was said to follow that they had not been presently entitled to the distributions when s 97(1) operated ([28]).

The first premise of the contention was that the presumption that a donee assents to a gift is an evidentiary presumption or inference capable of rebuttal. The court rejected that premise, affirming that the presumption of assent is one of law within the typology explained in *Masson v Parsons* (2019) 266 CLR 554 ([29]- 30], [46]).

The second premise was that assent of the beneficiaries was necessary at all. Gageler, Gordon, Steward and Gleeson JJ considered the case an inappropriate vehicle to examine the issue ([31]).

Edelman J, however, took the opportunity to explain that the second premise conflated requirements for the voluntary transfer of legal title to property with principles governing the creation or alteration of new equitable rights with respect to that title. Assent of a beneficiary is unnecessary for the creation or alteration of equitable rights, like those of the respondent beneficiaries by reference to which s 97(1) operated ([38]-[40]). While a disclaimer of those equitable rights generally has retrospective effect as between trustee and beneficiary, it does not for the purposes of s 97(1) as construed ([48]). BN