

# GST on in specie transfers of assets from discretionary trusts to beneficiaries

This paper examines the GST treatment of in specie transfers of assets from discretionary trusts to beneficiaries and in particular the question of how such transfers can be made in the furtherance of a trust's enterprise for GST purposes (in light of Draft GST Determination GSTD 2008/D2).

## General principles

Under section 9-5 of the GST Act, an entity makes a taxable supply if:

- It makes a supply for consideration
- The supply is made in the course or furtherance of an enterprise that it carries on
- The supply is connected with Australia
- It is registered, or required to be registered.

The existence of a 'supply' itself is an essential element in determining whether the distribution is a taxable supply under section 9-5 of the GST Act.

'Supply' is defined in subsection 9-10(1) of the GST Act to include any form of supply whatsoever. In this case, the distribution by the entity is the supply.

'Consideration' is defined in paragraph 9-15(1)(a) of the GST Act to include any payment, or any act or forbearance, in connection with a supply of anything. In some trust arrangements, beneficiaries have indefeasible rights to the trust property.

In the case of a discretionary trust, a beneficiary does not have a vested interest in either the income or the assets of the trust. The beneficiary merely has their right to demand that the trustee administers the trust according to the trust deed. As such, when the trustee makes a distribution, the beneficiary has no rights to surrender and gives no consideration.

Although the supply is not being made for consideration, a distribution made by a discretionary trust may still be a taxable supply where Division 72 of the GST Act applies. Division 72 removes the requirement for consideration from section 9-5 of the GST Act in certain circumstances where the recipient is an associate.<sup>1</sup>

Section 72-5 of the GST Act provides that a supply to an associate for no consideration will be a taxable supply if the associate is not registered or required to be registered, or the associate acquires the thing supplied otherwise than solely for a creditable purpose. When a discretionary trust makes an in specie distribution to a beneficiary that is registered or required to be registered, and the distribution is used solely for a creditable purpose, the supply will not be a taxable supply under section 9-5 of the GST Act.

As section 72-5 of the GST Act is not applicable, the requirement for consideration under paragraph 9-5(a) of the GST Act is not satisfied.

## Draft GST Determination GSTD 2008/D2

In this draft Determination, the ATO argues that an in specie distribution of an asset that is applied or intended to be applied in an enterprise carried on by a discretionary trust to a beneficiary is made in the course or furtherance of the trust's enterprise and is therefore a taxable supply in accordance with section 9-5 of the GST Act.

An "in specie" distribution is defined as the supply of trust property other than money where the recipient is entitled to the property because the recipient is a beneficiary of the trust, and not because of any contractual relationship with the trustee.

The ATO asserts that the phrase "in the course or furtherance" should be given broad scope so as to encompass supplies made in connection with the enterprise. They argue that the fact the supply of the asset is by way of an in specie distribution will not alter the fact that the asset was in the course or furtherance of the enterprise being carried on by the trust. They rely on the Explanatory Memorandum to the GST Bill in order to support their position:

<sup>1</sup> The term associate which is defined in section 318 of the *Income Tax Assessment Act 1936* includes a beneficiary and the trustee of a trust.

*In the course or furtherance is not defined, but is broad enough to cover any supplies made in connection with your enterprise.*

Other important arguments raised by the ATO in this draft Determination include:

- That a supply is made for the private purposes of the recipient cannot affect whether the supply is made in the course or furtherance of the supplier's enterprise
- The GST Act does not require that the asset must be applied primarily or principally in carrying on the enterprise for the supply of the asset to be in the course or furtherance of the enterprise
- Therefore, a supply by way of in specie distribution of an asset that is applied or was intended to be applied in the enterprise is a supply made in the course or furtherance of that enterprise

The test under section 9-5(b) is whether or not the supply was made in the course or furtherance of an enterprise carried on by the taxpayer. The word "in" has significant importance here and on the face of it does not seem to include a supply that was intended to be made in the course or furtherance of the enterprise. The ATO seeks to substitute an alternative test to that stated in section 9-5.

Furthermore, there are two main questions that should be considered when applying section 9-5(b) to this scenario:

- What is the identified enterprise being carried on by the trust? This is a question of fact, i.e. What are the parameters of the enterprise being carried on by the trust?
- Is the given in specie distribution of a trust asset made in the course or furtherance of the relevant identified enterprise?

There appears to be no basis for the ATO to treat a supply as taxable when the asset has not been used in the enterprise, but is only intended to be used in the enterprise. There is no discussion in the draft Determination regarding the required nexus between the supply of the particular asset and the identified enterprise of the trust.

Furthermore, the application of the draft Determination to an in specie distribution by way of capital distribution to a beneficiary is not consistent with similar arrangements that result from property distributions under the Family Law Act or in other similar circumstances that are discussed in GST Ruling GSTR 2003/6.

This Draft Determination will be issued in final form early this year.

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