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Parliament presents bill to amend general anti-avoidance rule

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On 13 February 2013, the Australian government introduced a bill into parliament which, amongst other things, would amend the general anti-avoidance rule in Part IVA of the *Income Tax Assessment Act 1936*.

These amendments, which the government expects to prevent losses to the revenue of over AUD 1 billion per year, originally were announced following a number of recent court decisions that revealed what the government perceived to be weaknesses with Part IVA, and that reduced its effectiveness in countering tax avoidance arrangements.

The proposed amendments should further strengthen Part IVA. These amendments also are expected to create additional uncertainty as to how aspects of Part IVA apply, and differences in interpretation between the Australian Taxation Office (ATO) and taxpayers likely will lead to further litigation.

As background, Part IVA applies where the following requirements are met:

1) There is a scheme;
2) A taxpayer obtains a "tax benefit" in connection with that scheme; and
3) One or more of the persons who participated in the scheme (or part of the scheme) did so for the sole or dominant purpose, objectively ascertained, of enabling the taxpayer to obtain the tax benefit in connection with the scheme.

Where the three requirements for Part IVA to apply are met, the Commissioner of Taxation can cancel the tax benefit.

To determine whether a tax benefit has been obtained, it is necessary to compare the tax consequences of the scheme in question with an "alternative postulate," being the tax consequences that either:

- Would have arisen; or
- Might reasonably be expected to have arisen (the reconstruction approach)

had the scheme not been entered into or carried out.

Applying the "reconstruction approach"

When applying the reconstruction approach, the proposed amendments make it clear that, in determining whether a postulate is a reasonable alternative, it is necessary to:

- Have regard to the substance of the scheme;
- Have regard to any result or consequence for the taxpayer that is, or would be achieved by, the scheme (other than tax results); and
- Disregard any tax results that would be achieved by the postulate for any person (whether or not a party to the scheme).

In respect of the first bullet, substance is directed at the commercial and economic substance of the scheme, rather than the legal form or shape. The substance of the alternative postulate should correspond to the substance of the scheme.

The second bullet requires consideration of any financial or other consequences for the taxpayer that would be achieved as a result of entering into the scheme. The explanatory memorandum accompanying the bill states that it would be expected that a postulate that is a reasonable alternative to the scheme would achieve for the taxpayer nontax results and consequences that are comparable to those achieved by the scheme. The requirement to have regard to the above two matters will narrow the range of alternative postulates that can be developed.

Finally, in determining whether a postulate is a reasonable alternative, regard should not be had to any tax costs that are generated for the taxpayer or any other person. That is, a taxpayer cannot argue that an alternative postulate is unreasonable on the grounds that it would have attracted a higher tax cost in comparison to the scheme.

Application

The amendments, once passed, would apply to schemes entered into, or commenced to be carried out, from 16 November 2012, the date when the draft legislation was released.

Next steps

Taxpayers should review transactions entered into, or commenced to be carried out, as from 16 November 2012. The proposed amendments to Part IVA will mean that, in determining whether or not there is a tax benefit, taxpayers should focus on:

- The nontax results and consequences of the transaction. This will be relevant to determining whether there is a tax benefit; and
- Whether the transaction could have been undertaken in another way, which corresponds in substance to the scheme, and whereby comparable nontax results and consequences could have been achieved for the taxpayer (disregarding any tax outcomes).

Given the importance of evidence in tax disputes and the increasing focus of the ATO on more detailed forensic analysis of possible counterfactuals, it will be important for taxpayers to document their positions.