TAXATION RULING NO. MT 2019

FRINGE BENEFITS TAX : SHAREHOLDER EMPLOYEES OF FAMILY PRIVATE COMPANIES AND DIRECTORS OF CORPORATE TRUSTEES

F.O.I. EMBARGO: May be released

REF H.O. REF: L85/10-3 DATE OF EFFECT: Immediate

B.O. REF: DATE ORIG. MEMO ISSUED:

F.O.I. INDEX DETAIL

REFERENCE NO:	SUBJECT REFS:	LEGISLAT. REFS:
I1209552	Fringe Benefits Tax	Fringe Benefits Tax Assessment Act: S.136, 137 and 148

OTHER RULING ON TOPIC : MT 2016

PREAMBLE This ruling deals with the application of the fringe benefits tax (FBT) to benefits provided by a family private company to a shareholder of the company who is also a past or current employee of the company or an associate of such an employee. It also deals with benefits provided by a company in the capacity of trustee of a family trust estate to a beneficiary of the trust estate who is also a director of the company.

*[**Note:** This is a consolidated version of this document Refer to the Tax Office Legal Database (http://law ato gov au) to check its currency and to view the details of all changes]*

2. To be subject to FBT, a benefit must be a "fringe benefit" as defined in sub-section 136(1) of the Fringe Benefits Tax Assessment Act 1986. That definition requires, among other things, that the benefit must be provided to an employee (or to an associate of the employee such as a family member) in respect of the employment of the employee.

3. In relation to benefits provided to shareholders in family private companies, the first point to note is that for the benefit to be liable to FBT, it must be provided to the shareholder at a time when that person is an "employee" or an associate of an employee. The term ‘employee’ is defined in the legislation to mean a current employee, a future employee or a former employee with the term ‘current employee’ further defined in the legislation to mean a person who is entitled to receive salary or wages. A shareholder will meet this definition if at the time when the benefit is provided he or she is in receipt of salary or wages from the company or is a director who receives directors' fees. Correspondingly, a shareholder who at some time in the past has received salary, wages or directors' fees from the company will meet the definition of "former employee".

4. Section 137 of the Fringe Benefits Tax Assessment Act 1986 extends the definition of "employee" for the purposes of that Act to include persons who receive non-cash remuneration for services rendered in circumstances where they would have met the subsection 136(1) definition of ‘current employee’ if that

non-cash remuneration had been received by way of a cash payment. This means, for example, that a director of a company who does not receive any cash remuneration but who does receive non-cash benefits by way of remuneration is treated as an employee for FBT purposes. Conversely, if a non-cash benefit is received by a director solely by reason of his or her shareholding rather than by way of remuneration, the receipt of that benefit would not result in the director being treated as an employee for FBT purposes.

5. If a shareholder of a family private company does meet the definition of "employee", for example, because that person is, or has at some time been, a director of the company in receipt of directors' fees, the company will be liable for FBT on benefits provided to that shareholder (or an associate) in respect of his or her employment by the company. The term "employment" is defined as including, broadly, the activity (e.g., the holding of the office of director) that results, will result or has resulted in the person being treated as an employee within the meaning of the FBT legislation. Thus the benefit must be associated with some past, current or expected future employment activity which results in the person being treated as an employee.

6. By virtue of paragraph 148(1)(a) of the Fringe Benefits Tax Assessment Act, a benefit provided to a person by reason of both his or her employment activity and shareholding will be taken to be provided in respect of the person's employment. If, however, it can be established that a benefit is provided to a shareholder/employee solely by reason of that person's position as a shareholder of the company and not to any extent by reason of that person's employment by the company, the benefit will not be subject to FBT.

7. The question whether a benefit is provided for employment-related reasons is one that also arises under the income tax law. The income tax position is that expenses incurred in respect of benefits provided for employment-related reasons are generally deductible to the company even where the recipient is also a shareholder. However, if the benefit is not employment-related but, in effect, represents a distribution of income to shareholders, the expenses incurred in providing the benefit are not deductible. Furthermore, section 108 of the Income Tax Assessment Act 1936 provides that payments by way of advances or loans made by the company on behalf of, or for the individual benefit of, any of its shareholders shall to the extent that they represent distributions of income be deemed to be dividends paid by the company. As such they are assessable in the hands of the shareholders. The payment of any amount that is deemed to be a dividend under a provision of the Income Tax Assessment Act 1936 is specifically excluded from the definition of "fringe benefit" under the FBT legislation.

RULING Shareholder employees of family private companies

8. Where a benefit is provided to a shareholder/employee of a family company in connection with the performance of his or her duties as an employee, it is considered that the benefit is provided in respect of the person's employment. For example, where a car owned by a family company is used by a shareholder/employee in the course of his or her employment by

the company, it is considered that any use, or availability for use, of the car by the employee (or an associate) for private purposes is a benefit provided in respect of his or her employment. Similarly, where a shareholder/employee uses his or her home telephone in the course of employment by the company, the payment of the telephone account by the company is considered to be a benefit provided in respect of the person's employment. (The extent of business use of the phone would be taken into account in arriving at the amount subject to tax.)

9. In relation to benefits that are not expressly linked to the carrying out of the employee's duties, it is necessary to examine all the facts and circumstances of the case to establish whether the benefit is fairly to be regarded as having been granted to the shareholder/employee in his or her capacity as an employee or as a shareholder. Factors such as the nature of the benefit, any cash remuneration paid, the nature and extent of any trading activities of the company, the extent of any services rendered by the shareholder/employee and the extent of his or her shareholding may be relevant in concluding whether a non-cash benefit was provided as remuneration for services or in the capacity of shareholder.

10. Where a family company incurs expenditure in respect of the provision of a benefit to a shareholder/employee and claims an income tax deduction in respect of that expenditure, the company is, in effect, contending that the benefit was provided by way of remuneration. Where the total remuneration (including non-cash remuneration) claimed to have been paid to the shareholder/employee is reasonable having regard to the services rendered, it would generally be accepted that the company is entitled to a deduction for the cost of providing the benefit. In those circumstances, it follows that the benefit is provided in respect of employment and thus subject to FBT.

11. The treatment outlined in the preceding paragraph would apply, for example, where a company carrying on a business of primary production has claimed deductions in respect of the 'homestead' dwelling on the basis that it is occupied by an employee, usually the principal shareholder director. Deductions attributable to the dwelling which have been claimed on this basis include depreciation, interest, rates, insurance, repairs and fuel.

12. The true position may be, however, that a family company permits shareholder/employees to occupy a dwelling owned by the company in their capacity as shareholders. For example, where a family home is owned by a company which has not carried on a business and the dwelling is occupied rent-free by shareholder directors who have performed only nominal duties for the company, the strong inference would be that the benefit was granted because of something other than employment. If, in these circumstances, the company has not claimed deductions relating to the dwelling, it would be accepted that the free occupancy was not provided in respect of employment. Similarly, if the home has been rented to the shareholder directors for a rental equal to the expenses incurred by the company, it would generally be accepted that the accommodation was not provided in respect of their employment. Here the facts would suggest that the arrangement was essentially a family one with the occupant effectively "reimbursing" the company for what are essentially

private expenses.

13. The position is less clear where a family company which carries on a business such as a farm or a motel provides free occupancy of a dwelling (e.g., a farm house or motel unit) to a shareholder/employee who receives a salary for managing the business. The provision of such accommodation is a normal element of the remuneration that would be expected to be provided to an arm's length manager. Nevertheless, it is accepted that in these circumstances it is still open to the company to show that the benefit of free occupancy was granted to shareholder/employees solely by reason of their shareholding or family status.

14. As indicated in paragraph 13 of Taxation Ruling No. MT 2016, there would need to be clear evidence that the arrangement under which title to the homestead or other dwelling lies in the family company has been treated by the parties as a family arrangement rather than as a business one. In that regard, it would be relevant to determine whether income tax deductions had been claimed in respect of any part of the expenditure incurred in relation to the dwelling. Taxation Ruling No. MT 2016 referred to the case where expenditures such as fuel and repairs were met by the occupants. If such expenses were met by the company, it would generally be expected that they would not be claimed by it as deductions. Where the company meets expenditures (e.g., interest and rates) that relate to the entire property on which the dwelling is located, it would be expected that so much of the expenditure as relates to the dwelling would not be claimed as deductions. While the non-claiming of deductions in relation to a dwelling is strongly indicative of a non-remunerative character in the arrangements, that will not be the case if the benefit is of a kind more readily seen as business related, e.g., private use of a business vehicle.

15. In some situations, a family company does not incur any expenditure in respect of the provision of a benefit to a shareholder/employee. For example, a family company may make its accumulated profits available to a shareholder/employee to meet private expenses, i.e., in effect an interest-free loan.

16. In some cases, it will be clear that the granting of a low-interest or interest-free loan was intended to form part of the remuneration of a shareholder/employee. For example, a family company might employ particular family members (e.g., an adult son) under employment conditions similar to those that would apply under an arm's length employment agreement. In these circumstances, a low-interest loan made to a shareholder employee could well be an element of his or her remuneration. If the value of loan benefits provided to shareholder/employees varied in line with their services provided to the company rather than their shareholdings, this would also be an indication that the loan was provided in respect of employment.

17. Other examples of employment-related loans to shareholder/employees could include where a loan is made for the purpose of enabling the employee to purchase a car that is used in the course of his or her employment by the company. Another example could be an advance made by the company to a particular employee with a nominal shareholding on the basis that the loan would be repaid from the person's future salary entitlements.

18. In other cases, it will be equally clear that a loan was granted to a shareholder/employee solely by virtue of his or her shareholding. This would be the case, for example, where a family company which has been used merely as a vehicle for holding family investments such as the family home or shares disposes of those assets and then lends the accumulated funds to shareholder directors who have performed only nominal duties for the company. Directors who perform only nominal duties would not ordinarily be expected to receive large interest-free loans by way of remuneration.

19. As a general rule, where there are no facts or circumstances which positively indicate that a loan to a shareholder/employee is associated with that person's employment and the loan is consistent with his or her status as a shareholder, it would ordinarily be inferred that the loan was made by virtue of the shareholding. This approach recognises that major shareholders of a family company may obtain loans from the company on a view that these are merely as a return of their own money rather than a reward for any services rendered to the company. However, questions as to the application of section 108 and Division 7A of the Income Tax Assessment Act (1936) might arise in these cases and in others where amounts paid as loans, advances or other payments for the benefit of shareholders of a private company may be deemed to be dividends paid to the shareholders.

Directors of corporate trustees

20. Where a company is a trustee of a trust estate, the company may be an employer for FBT purposes in two capacities. First, the company will be an employer in its own right if it employs persons in those activities (which may include holding the position of trustee of one or more trust estates) that it carries out in its own right. The directors of the company would be employed in this capacity. Secondly, the company will be an employer in the capacity of trustee of a trust estate if it employs persons in activities carried on by the trust. For example, it is not unusual for the trustee of a trading trust to employ persons in the business carried on by the trust.

21. Questions have been asked as to whether the FBT would apply where the corporate trustee of a family trust estate provides a non-cash benefit such as the free occupancy of a family home to a beneficiary of the trust estate who is also a director of the corporate trustee, but is not employed in any activities carried on by the trust. This could occur where a resolution is passed by the corporate trustee authorising the granting of the non-cash benefit to the beneficiary pursuant to the terms of the trust deed.

22. In these circumstances, it would ordinarily be clear that the benefit is provided to the beneficiary by reason of his or her position as a beneficiary of the trust estate rather than by reason of his or her position as director of the corporate trustee. Where non-cash benefits are provided in such situations it may be necessary to consider whether an effective distribution of trust income for income tax purposes has been made to or for the benefit of the beneficiary.

23. Some illustrative examples of where the application of

this ruling would result in no FBT being payable are set out in the attachment.

COMMISSIONER OF TAXATION
30 June 1986

APPENDIX

ATTACHMENT A

The following case studies represent instances where, under the principles set out in this ruling, the employer would not be liable to fringe benefits tax on the benefits under examination. It may be assumed that there are no material facts other than those described.

. Company A is a family private company with two shareholders, a husband and wife, who are also directors. The only asset owned by the company is a house used as the private residence of the shareholder/directors. The company has no income from any source. The house has not been rented to the shareholder/directors or any other person. All expenses of the house - rates, repairs, maintenance etc - have been treated as private expenses and paid for directly by the director/shareholders.

. A husband and wife are director/shareholders of a family private company. In consequence of a Family Court settlement, the wife received a low-interest loan from the company in consideration for giving up her equity in, and future claims on, the company. In its decision the Court was not called on to take account of any services rendered to the company by the wife.

. Company B is another family private company used as a vehicle to hold investments. The principal shareholder, Mrs C, is also a director of the company and receives directors fees. The company owns a home unit used as a retirement home for the parents of Mrs C, Mr and Mrs D. Company B has not claimed income tax deductions in respect of any costs associated with the unit. All costs have been paid directly by either Mrs C or Mr and Mrs D.

. A widow was previously a director of the family private company. Subsequent to her husband's death, the company ceased trading and was left with paid up capital of $100,000. An interest-free loan of $100,000 was then made to the widow effectively representing a return of her invested capital.

. Company E is a family private company. A husband and wife are director/shareholders but receive no directors' fees. The company leases the family residence to the husband and wife for $30 per week, which is less than the market rental value but is calculated to meet costs incurred by the company in holding and maintaining the residence.

. Company F, a family private company, has ceased trading, realised its assets and loaned the

resultant funds to shareholders, some of whom are former directors, pending liquidation. The loans are granted to all shareholders on equal terms both as to amount and repayment conditions.

. Company G is the trustee of a family trust. The directors of G are a husband and wife who, together with their children, are also the beneficiaries of the trust and reside in a house owned by the trust. The trust instrument provides for the beneficiaries to have a life tenancey in the house.