TR 2010/8 - Income tax: application of subsection 109RB(1) of the Income Tax Assessment Act 1936

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Taxation Ruling

Income tax: application of subsection 109RB(1) of the *Income Tax Assessment Act 1936*

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This publication (excluding appendixes) is a public ruling for the purposes of the *Taxation Administration Act 1953*.

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If you rely on this ruling, the Commissioner must apply the law to you in the way set out in the ruling (unless the Commissioner is satisfied that the ruling is incorrect and disadvantages you, in which case the law may be applied to you in a way that is more favourable for you – provided the Commissioner is not prevented from doing so by a time limit imposed by the law). You will be protected from having to pay any underpaid tax, penalty or interest in respect of the matters covered by this ruling if it turns out that it does not correctly state how the relevant provision applies to you.

What this Ruling is about

1. This Ruling outlines the requirements to be satisfied before the Commissioner is empowered to make a decision to disregard the operation of Division 7A of Part III (Division 7A) of the *Income Tax Assessment Act 1936* (ITAA 1936)[1] or allow the dividend taken to have been paid under Division 7A to be franked.

2. This Ruling discusses the requirements in subsection 109RB(1), including the meaning of 'honest mistake' and 'inadvertent omission' in paragraph 109RB(1)(b).

3. This Ruling does not deal with the evidence required for a taxpayer to satisfy the Commissioner whether an honest mistake or inadvertent omission has occurred. This will be covered in a Law Administration Practice Statement.

[1] All legislative references in this Ruling are to the ITAA 1936 unless otherwise stated.

Ruling

The reason for the result of the operation of Division 7A

4. For subsection 109RB(1) to be satisfied the result of the operation of Division 7A must arise because of an honest mistake or inadvertent omission of the recipient of the dividend, the private company or any other entity that contributed to the result.

5. The terms honest mistake and inadvertent omission must be interpreted in their context and must be relevant to the operation of Division 7A. The honest mistake or inadvertent omission must relate to the operation of Division 7A and facts relevant to Division 7A. An honest mistake or inadvertent omission in relation to matters that do not relate to Division 7A are irrelevant to the determination of whether an honest mistake or inadvertent omission has occurred within the meaning of subsection 109RB(1).

6. A mistake or omission about a particular matter that is subsequent to or otherwise irrelevant to the particular result of the operation of Division 7A is not relevant.

7. In each case, it is a question of fact whether an honest mistake or inadvertent omission has occurred. All the facts and circumstances must be considered to determine whether an honest mistake or inadvertent omission occurred.

8. The taxpayer must demonstrate on the balance of probabilities that an honest mistake or inadvertent omission has occurred. The facts and circumstances must be sufficiently detailed to demonstrate the existence of the honest mistake or inadvertent omission that is relevant to Division 7A.

Terms honest mistake and inadvertent omission take their ordinary meaning

9. As these terms are not defined, the terms honest mistake and inadvertent omission take their ordinary meaning.

10. In determining whether a person has made an honest mistake or an inadvertent omission, that person's actual state of mind or belief is in issue. However, the available evidence may provide an indication of the person's actual state of mind.

Wide range of potential honest mistakes and inadvertent omissions

11. A mistake in the context of subsection 109RB(1) is an incorrect view or opinion or misunderstanding about how Division 7A operates; about facts that are relevant to its operation; or about other matters that affect its operation. Such a mistake must be honestly made.

12. An omission in the context of subsection 109RB(1) is a failure to take action that is relevant to, or affects, the operation of Division 7A. Such an omission must be inadvertent.

Ignorance

13. A mistake or omission can be the result of ignorance. However, it would need to be established that the relevant entity's ignorance led to the honest mistake or inadvertent omission relevant to subsection 109RB(1) and that the result of the operation of Division 7A arose because of it.

14. Deliberate behaviour to remain ignorant of the operation or requirements of Division 7A up to the time when Division 7A is triggered, where the taxpayer is aware or was made aware of the relevant provisions before that time, does not satisfy the meaning of honest mistake or inadvertent omission.

Circumventing Division 7A, deliberate indifference and wilful blindness

15. Actions or omissions made to circumvent Division 7A cannot satisfy the requirements of honest mistake or inadvertent omission.

16. A deliberate indifference or wilful blindness would not satisfy the requirement of honesty and would not constitute an honest mistake.

Mistakes and omissions made by other entities

17. Where the honest mistake or inadvertent omission is by an entity other than the recipient entity or the private company, it is also necessary that the taxpayer demonstrate that the entity's conduct contributed to the result of the operation of Division 7A.

Common mistakes and omissions

18. The fact that a mistake or omission has commonly occurred does not necessarily establish that an honest mistake or inadvertent omission occurred in the taxpayer's circumstances. However, in the absence of direct evidence, the fact that an error is common may support the conclusion it was an honest mistake or inadvertent omission.

Recurring mistakes or omissions

19. A mistake or omission that is recurring will qualify as an honest mistake or inadvertent omission if it recurs for the same reason and the original mistake or omission qualified as an honest mistake or inadvertent omission. This will also be the case in circumstances where an original mistake of law by a tax agent that qualified as an honest mistake or inadvertent omission is applied to other clients.

Examples

Example 1 – Tax agent accepts summary information received each year without making enquiries about Division 7A transactions

20. *Each year a private company makes a number of loans to a shareholder which fund the shareholder's gambling activities. There is no written loan agreement in place. No interest is paid and repayments are only made some time later when the shareholder has a capacity to make the payment, usually after large gambling wins.*

21. *Each year the private company is taken to have paid a dividend under section 109D in relation to the loans not repaid before the private company's lodgment day.*

22. *The shareholder is a director of the private company. He relies on his tax agent to ensure that he and the company meet all their taxation obligations and no limitations have been imposed on the scope of the work undertaken by the agent.*

23. *The tax agent is aware of the provisions of Division 7A including the application of section 109D. Further inquiry by the Australian Taxation Office (ATO) showed that a Division 7A circular has been sent to the private company and the shareholder recently. The agent prepares the tax returns of the company and the shareholder. The shareholder's only assessable income is a salary received from the private company.*

24. *The tax agent is not involved in maintaining the private company's accounting records and at year end receives summary information from which to prepare the private company's tax return. That summary information does not include details of transactions between the private company and the shareholder.*

25. *Each year the tax agent simply accepts the information received and makes no enquiries as to transactions between the private company and the shareholder. The information provided to the tax agent does not provide the agent with sufficient information to allow him to form a view as to the application of Division 7A to the client's circumstances.*

26. *Although the conduct of the tax agent may have contributed to the result, in the absence of other contributing factors, there is nothing in the facts which demonstrates that the tax agent has made an honest mistake or inadvertent omission in the context of subsection 109RB(1).*

27. *Mistakes or omissions in relation to the maintenance of the private company's accounting records or preparation of the summary information are capable of constituting an honest mistake or inadvertent omission. But it must be established that the relevant mistake or omission caused or contributed to (depending on the relevant entity) the result produced by Division 7A in order to satisfy subsection 109RB(1).*

Example 2 – Arithmetic error

28. *A private company is taken to have paid a dividend to a shareholder because of a minimum yearly repayment shortfall.*

29. *The shortfall arose because the tax agent had made an error in calculating the minimum yearly repayment for one of the amalgamated loans. No similar errors were made in respect of other amalgamated loans, either in the current year or earlier income years. The error related to the remaining term used in the minimum yearly loan repayment formula. The term used was one year longer than it should have been.*

30. *The shareholder had made repayments based on the minimum yearly loan repayment advised by the agent. Both the taxpayer and tax agent were aware of the Division 7A obligations and had attempted to comply. There is no evidence to suggest that the error was anything other than an accidental oversight.*

31. *In these circumstances, the arithmetic error is an honest mistake.*

Example 3 – Mistake in the carrying out of the activities

32. *Jack and Jill are the shareholders and directors of a private company.*

33. *During the year the company refurbished the company premises including the office.*

34. *It is Jack and Jill's practice to maintain separate business and private bank accounts and to pay business and private expenses from the appropriate account by cheque or direct debit. Jack and Jill are both signatories on each account and can sign solely. Jill does not take an active role in the company's business but is aware of the need to keep business and personal affairs separate.*

35. *One day Jill goes shopping for new household furniture at a furniture store. As she is leaving the house she unwittingly takes the business cheque book with her instead of the personal cheque book. She pays $10,000 for the private furniture using the business cheque book (again without realising her mistake) and writes 'New Furniture – Furniture Store' on the cheque butt but does not otherwise indicate whether the cheque was for business or private purposes.*

36. *The amount paid for the private furniture was similar to amounts paid for office furniture.*

37. *Her error goes unnoticed by Jack or by Jill.*

38. *The company's income tax return was lodged and the company was taken to have paid a dividend under section 109C. During the preparation of the income tax return the company's general ledger entries were reviewed and the error was not discovered. The entry neither appeared unusual or inconsistent with other company transactions in terms of the nature of the transaction and the amount of the transaction.*

39. *Soon after the lodgment of the company's income tax return, as a result of a dispute with the supplier of the office furniture, Jack had cause to review the company's records and discovered the error. He took corrective action and repaid the money to the company from his personal bank account.*

40. *Jill's error is capable of constituting an honest mistake.*

41. *The corrective action taken by Jack is relevant for the purposes of paragraph 109RB(3)(b) when the exercise of the discretion is considered. It is irrelevant for the purposes of subsection 109RB(1).*

Date of effect

42. This Ruling applies to years of income commencing both before and after its date of issue. However, this Ruling will not apply to taxpayers to the extent that it conflicts with the terms of a settlement of a dispute agreed to before the date of issue of this Ruling (see paragraphs 75 and 76 of Taxation Ruling TR 2006/10).

Commissioner of Taxation
15 December 2010

Appendix 1 – Explanation

This Appendix is provided as information to help you understand how the Commissioner's view has been reached. It does not form part of the binding public ruling.

Background and context

43. Division 7A operates with the result that all:

(a) payments and loans made by a private company to its shareholders or their associates; and

(b) debts owed by its shareholders or their associates that are forgiven by the private company

are taken to be unfranked dividends paid by the private company for the purposes of the Act unless specifically excluded. Division 7A also operates with the result that under certain interposed entity arrangements, an amount is to be included in the recipient's assessable income as if it were a dividend.

44. Under subsection 109RB(2) , the Commissioner may make a decision that:

- the result of the operation of Division 7A be disregarded, or
- the dividend taken to have been paid under Division 7A may be franked.

45. In making such a decision, the Commissioner must have regard to the factors set out in subsection 109RB(3). A decision by the Commissioner can be made subject to conditions imposed in accordance with subsection 109RB(4).

46. The Commissioner's power to make a decision under subsection 109RB(2) is only enlivened if the circumstances described in subsection 109RB(1) are satisfied. These requirements are explained below.

The result of the operation of Division 7A

47. Division 7A must *operate with the result* that a private company is either:

- taken to pay a particular dividend to a particular entity under the Division (subparagraph 109RB(1)(a)(i)), or
- under Subdivision EA of Division 7A, a particular amount is included, as if it were a dividend, in the assessable income of a particular entity in relation to a private company (subparagraph 109RB(1)(a)(ii)).

The reason for that result

48. The particular result of the operation of Division 7A must have arisen *because of* an honest mistake or inadvertent omission (paragraph 109RB(1)(b)) by the recipient of the dividend, the private company or another entity that contributed to the result.

49. There are a wide range of matters to which honest mistakes or inadvertent omissions may be relevant. These can cover any of the facts and circumstances that are relevant to the Division operating with the particular result. These could range from honest mistakes and inadvertent omissions arising from the carrying out of an activity to those arising from the misinterpretation or ignorance of a particular provision of Division 7A.

50. Division 7A operates on the basis of all the facts and circumstances that are relevant to its operation in a given situation. The mistake or omission must be about a matter which can be said to have caused the particular result of the operation of Division 7A. This is essentially a question of fact.

51. It must be demonstrated objectively that the thing that was mistaken or omitted caused the result of the operation of Division 7A. In practice this means that an inquiry into the nature of the mistake or omission and why the mistake or omission was made will be necessary. A result that arises regardless of the existence of a particular mistake or omission is not a result that arises because of that mistake or omission.

52. The particular result of the operation of Division 7A can not have arisen because of a mistake or omission about a matter that is subsequent to or otherwise not relevant to that particular result. Corrective actions taken after Division 7A has been triggered may in conjunction with other evidence establish that a mistake or omission was made but it does not in itself establish definitively that it is a mistake or omission or that the relevant mistake or omission caused the particular result of the operation of Division 7A. Under paragraph 109RB(3)(b), the Commissioner must have regard to corrective actions in considering whether to exercise the discretion in subsection 109RB(2).

The requirement of 'honest mistake' or 'inadvertent omission'

53. The circumstances must show either an *honest mistake* or an *inadvertent omission*.

54. The circumstance relied on must meet the description of either being an *honest mistake* or an *inadvertent omission*. Other types of circumstances do not qualify. A mistake must be *honest* and an omission must be *inadvertent* to be covered by subsection 109RB(1).

55. The Explanatory Memorandum to the Tax Laws Amendment (2007 Measures No. 3) Bill 2007 (the Explanatory Memorandum) at paragraph 1.33 states:

> 1.33 Whether or not there is an honest mistake or inadvertent omission is an objective question to be determined by reference to all the circumstances surrounding the failure to satisfy the requirements of Division 7A. In practice, the taxpayer will need to demonstrate to the Commissioner that the failure was the result of an honest mistake or inadvertent omission.

56. Paragraph 1.36 of the Explanatory Memorandum adds:

> 1.36 … There is a very wide range of possible mistakes or omissions that would result in Division 7A deeming there to be a dividend paid to a taxpayer. For example, there may be a complete failure to make any minimum yearly repayment over a long period of time, or there may be a simple miscalculation of the minimum yearly repayment in one year. Likewise, there is a wide spectrum of circumstances in which there might be a failure to satisfy the requirement for a written loan agreement under section 109N. For example, there may be no agreement of any kind, or there may be a written agreement that satisfies all the requirements of the provision other than for an interest rate slightly lower than that required by the law.

57. These situations may typically involve a mistake or omission but they can also arise in circumstances other than mistake or omission. Reliance on a mistake or omission that is either common or reasonable is not of itself sufficient but it may be relevant evidence. The fact that certain situations have been identified as frequently involving an honest mistake or inadvertent omission can, in the absence of more direct evidence, be relevant in forming a view on a particular case. However, it is not conclusive of the matter. For example, in a particular case, there may be evidence to the contrary or the particular situation may differ in some relevant respects from those that typically involve a mistake or omission.

58. The circumstances must be sufficiently particularised to establish a finding of honest mistake or inadvertent omission on the material provided. It is for the taxpayer to demonstrate to the Commissioner that the failure to satisfy the requirements of Division 7A was the result of an honest mistake or inadvertent omission.[2] Evidence of an attempt to comply with the intent or requirements of Division 7A can be relevant, as can evidence of why the requirements were not met.[3] As explained earlier, corrective action taken after Division 7A has been triggered does not in itself establish the existence of a mistake or omission, although it is relevant to the exercise of the discretion to disregard the result of operation of Division 7A.

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[2] See paragraph 1.33 of the Explanatory Memorandum.
[3] See Examples 1.8 and 1.9 following paragraph 1.43 of the Explanatory Memorandum.

Ignorance

59. A mistake or omission can be the result of ignorance. However, it would need to be established that the relevant entity's ignorance led to the honest mistake or inadvertent omission relevant to subsection 109RB(1) and that the result of the operation of Division 7A arose because of it. Whether or not this is the case will depend on the particular situation. For example, ignorance of the existence of Division 7A does not of itself establish that the loan itself was a mistake, the fact that it was not repaid was an honest mistake or inadvertent omission or that the absence of a complying written loan agreement was an inadvertent omission. It is necessary to make further enquiries about the circumstances surrounding the ignorance to determine whether an honest mistake or inadvertent omission in fact occurred and that it caused Division 7A to operate with the particular relevant result.

60. In corporate law cases such as *Nichol* v. *Fearby* [1923] 1 KB 480 and *Sanwa Australia Finance Ltd v. Ground-Breakers Pty Ltd (in liq)* [1991] 2 Qd R 456; (1990) 8 ACLC 852, the courts have held that ignorance of the law may amount to inadvertence; however, these cases do not go so far as to suggest that ignorance of the law always constitutes inadvertence.

61. The honest mistake or inadvertent omission must be genuine. The belief relating to the purported mistake must be actually held by the entity. An entity that deliberately ignores the operation of Division 7A does not make an honest mistake or inadvertent omission.[4]

Ordinary meaning applies

62. The terms 'honest mistake' and 'inadvertent omission' are not specifically defined for the purposes of section 109RB or for tax law purposes more generally. Accordingly, each term take on its ordinary meaning as appropriate to the context in which it is used.

Honest mistake

63. *The Macquarie Dictionary*, 2005, 4th Edition, The Macquarie Library Pty Ltd, NSW (Macquarie Dictionary), defines **honest** as:

> 1. honourable in principles, intentions, and actions; upright: *an honest person.*
>
> 2. showing uprightness and fairness: *honest methods.*
>
> 3. acquired fairly: *honest money.*
>
> 4. open; sincere: *an honest face.*
>
> 5. genuine or unadulterated: *honest commodities.*
>
> 6. truthful; creditable; candid.

[4] See Example 1.12 of the Explanatory Memorandum.

64. *The Australian Oxford Dictionary*, 2004, 2nd Edition, Oxford University Press, Melbourne (Australian Oxford Dictionary), defines **honest** as:

> 1. fair and just in character or behaviour, not cheating or stealing;
>
> 2. free of deceit and untruthfulness, sincere.

65. *The New Shorter Oxford English Dictionary*, 1993, Clarendon Press, Oxford (New Shorter Oxford English Dictionary), defines **honest** as:

> 3a. Of an action, one's feelings etc: showing sincerity of character or intention; fair, straightforward; free from fraud;
>
> 4. Of a person: marked by uprightness or probity; fair and righteous in speech and act; fundamentally sincere or untruthful; not lying, cheating, or stealing.

66. The entity's honesty must be in relation to the operation of Division 7A and facts that are relevant to Division 7A. Lack of honesty in relation to a matter that does not relate to Division 7A is not relevant for the purposes of subsection 109RB(1).

67. It has been suggested that anything that is not dishonest must be honest. Whether or not that is true in some other context, the question does not arise in the present context. The statutory test under section 109RB is whether the mistake relevant to the result under Division 7A is an honest one. Whether the mistake is not dishonest is not the test. The fact that the taxpayer has simply been unable to discharge the onus of proof required to satisfy the elements of subsection 109RB(1) due to insufficient evidence does not mean they have been dishonest.

68. The Macquarie Dictionary defines **mistake** as:

> 1. an error in action, opinion or judgment. 2. a misconception or misapprehension.

69. The *Butterworths Australian Legal Dictionary*, 1997, Butterworths, Sydney (Butterworths Australian Legal Dictionary), defines **mistake** as:

> Either a belief in the existence of a thing which does not exist, or ignorance of a relevant thing, or both.

70. The Australian Oxford Dictionary defines **mistake** as:

> 1. an incorrect idea or opinion; a thing incorrectly done or thought;
>
> 2. an error of judgment.

71. The New Shorter Oxford English Dictionary defines **mistake** as:

> 1. A misconception about the meaning of something; a thing incorrectly done or thought; an error of judgment.

72. The distinction made in criminal matters between mistakes of fact and mistakes of law are not relevant for the purposes of subsection 109RB(1). This distinction is not made by the words of provision, and the purpose of that distinction in criminal matters is not relevant for the purposes of section 109RB. The Explanatory Memorandum makes no such distinction and the examples (see examples see 1.9, 1.11 and 1.12) provided in the Explanatory Memorandum do not draw any such distinction.

73. The relevant facts and circumstances must meet the description of *honest mistake*. It is not a requirement that the mistake also meet the description of being reasonable. Subsection 109RB(1) does not explicitly require this, nor is this a necessary implication in the statutory context. The idea of 'honest and reasonable mistake' that can be a defence in criminal matters is inappropriate in the context of subsection 109RB(1). However, the reasonableness of the mistake may be pertinent to the question of whether the belief in the existence of a thing was actually held by the entity: see *R v. Morgan* [1976] AC 182; [1975] 2 All ER 347; *R v. Saragozza* [1984] VR 187.

74. In determining whether a person has made an honest mistake, that person's actual state of mind or belief is in issue. However, this actual state of mind or belief is established on objective evidence. The Privy Council decision of *Royal Brunei Airlines Sdn Bhd v. Tan Kok Ming* [1995] 2 AC 378; [1995] 3 All ER 97 gives guidance on how to approach this objective question. Lord Nicholls said at page 389:

> …acting dishonestly, or with a lack of probity, which is synonymous, means simply not acting as an honest person would in the circumstances. This is an objective standard. At first sight this may seem surprising. Honesty has a connation of subjectivity, as distinct from the objectivity of negligence. Honesty, indeed, does have a strong objective element in that it is a description of a type of conduct assessed in the light of what a person actually knew at the time, as distinct from what a reasonable person would have known or appreciated. Further, honesty and its counterpart dishonesty are mostly concerned with advertent conduct, not inadvertent conduct. Carelessness is not dishonesty. Thus for the most part dishonesty is to be equated with conscious impropriety.

75. The notion that the term honest mistake has a strong objective element in it is set out in the Explanatory Memorandum at paragraph 1.33:

> 1.33 Whether or not there is an honest mistake or inadvertent omission is an objective question to be determined by reference to all the circumstances surrounding the failure to satisfy the requirements of Division 7A. In practice, the taxpayer will need to demonstrate to the Commissioner that the failure was the result of an honest mistake or inadvertent omission.

76. A deliberate indifference or wilful blindness would not satisfy the requirement of honest and would not constitute an honest mistake.

Inadvertent omission

77. The terms **omission** and **omit** are defined by the Macquarie Dictionary as:

> **Omission,** noun 1. the act of omitting. 2. the state of being omitted. 3. something omitted.
>
> **Omit**, verb (t) (omitted, omitting) 1. to leave out: to omit passages of a text. 2. to forbear or fail to do, make, use, send, etc.: to omit a greeting.

78. *Black's Law Dictionary*, 2004, 8th Edition, Thomson West, USA, describes omission as follows:

> **omission**, n 1. A failure to do something; esp., a neglect of duty <the complaint alleged that the driver had committed various negligent acts and omissions>.2. The act of leaving something out <the contractor's omission of the sales price rendered the contract void>. 3. The state of having been left out or not done <his omission from the roster caused no harm>. 4. Something that is left out, left undone, or otherwise neglected <the many omissions from the list were unintentional>.

79. *Stroud's Judicial Dictionary of Words and Phrases*, 2006, 7th Edition, Sweet & Maxwell, London, describes omission as:

> **omission**. An 'omission' to perform a duty involves the idea that the person to act is aware that performance is required or needful.

80. *The Oxford Companion to Law*, 1980, Clarendon Press, Oxford, states that **omission** is:

> A failure to an act, or the not-doing of it. An omission may be deliberate, or be inadvertent, as by forgetfulness. In general, an omission is legally significant only if there was a legal duty to act and not to omit, so that the omission is a breach of legal duty to have acted.

81. The Australian Oxford Dictionary defines **omission** as:

> 1. the act or an instance of omitting or being omitted;
>
> 2. something that has been omitted or overlooked.

82. The New Shorter Oxford English Dictionary defines **omission** as:

> 1. The action or an act of neglecting or failing to perform something, esp. a duty.
>
> 2. The action of omitting or failing to include something or someone, the fact of being omitted.

83. Butterworths Australian Legal Dictionary relevantly defines **inadvertence** as:

> 1. failure to observe or pay attention; … 2. In a restricted sense, ignorance of the law'

84. The Australian Oxford Dictionary defines **inadvertent** as:

> 1. (of an action) unintentional;
>
> 2a. not properly attentive b. negligent.

85. The New Shorter Oxford English Dictionary defines **inadvertent** as:

> 1. Of a person: not properly attentive or observant;
>
> 2. Of an action: unintentional.

86. Inadvertence implies a degree of pre-existing knowledge. Inadvertence is often described as being a failure to observe, or failure to pay attention. Whether an omission will be regarded as inadvertent is a question of fact and degree in each case. The observation of Ridley J. at page 287 in *West Bromwich case; Hazel v. Viscount Lewisham* [1911] 6 O'Malley and Hardcastle's Election Cases 256 is on point:

> …inadvertence, a word which is capable of several interpretations and which has been interpreted in various ways, not always, I think, consistent with one another. It may mean mere thoughtlessness, it may mean what is equivalent to a mere mistake, but in this case it was also ignorance of the law … persons might be fairly described as acting inadvertently because they did not know the law … inadvertence does not cover a case where in the immediate duty which he is performing, he ought to have a full knowledge of the law.

87. As explained at paragraph 60 of this draft Ruling, the authorities do not establish that ignorance of the law will always amount to inadvertence. Moreover, the law requires an inadvertent omission rather than inadvertence as such.

The relevant entities

88. The honest mistake or inadvertent omission must be by the recipient entity, the private company, or any other entity whose conduct contributed to the result: subparagraphs 109RB(1)(b)(i) to (iii).

89. The *recipient entity* is the entity taken to have been paid the dividend by the private company under Division 7A, or the entity that includes an amount as if it were a dividend in its assessable income in relation to the private company under Subdivision EA of Division 7A.

90. The *private company* is the company taken to have paid the dividend under Division 7A or the company in relation to which an amount is included in its assessable income of the recipient entity as if it were a dividend under Subdivision EA of Division 7A.

91. An honest mistake or inadvertent omission by an *entity other than the recipient or the private company* is only relevant if the *conduct* of that entity contributed to the particular result. This requirement is separate and is in addition to the requirement that the result arose *because of* that honest mistake or inadvertent omission. Only where an honest mistake or inadvertent omission has been found not to have been made by the recipient entity or private company that led to the result produced by Division 7A is further regard needed to the circumstances involving another entity.

92. Examples of relevant entities for this purpose can be an interposed entity, a shareholder or associate of a shareholder who is not the recipient, an officer or employee of any relevant entity, a tax agent, an accountant or a legal adviser.

93. Conduct refers to behaviours and actions. In the context of section 109RB, it also includes inactions and failures to act. The conduct must form part of the overall circumstances that gave rise to the relevant result. It is not about the entity's knowledge, state of mind, opinion, attitude or belief. An entity's knowledge, state of mind, opinion, attitude or belief can only be relevant if it leads to the entity's conduct and that conduct contributed to the particular result produced by Division 7A. The entity must still demonstrate that the relevant honest mistake or inadvertent omission was the cause of the particular result produced by Division 7A.

94. Whether an entity's conduct contributed to a particular result depends on the nature of the honest mistake or inadvertent omission and other facts and circumstances of the particular situation.

95. In circumstances where a tax agent has been engaged by the taxpayer, an inquiry into whether the tax agent has made an honest mistake or inadvertent omission is only relevant if the agent's conduct contributed to the result produced by the operation of Division 7A. If the tax agent has made an honest mistake but the conduct did not contribute to the result produced by the operation of Division 7A, subsection 109RB(1) is not satisfied unless another entity (be it the recipient or private company) can be said to have made an honest mistake or inadvertent omission in relation to a fact or circumstance that caused the result produced by the operation of Division 7A.

96. If the tax agent's conduct caused the result produced by the operation of Division 7A but that conduct does not amount to an honest mistake or inadvertent omission, it may be difficult to satisfy the requirements of subsection 109RB(1) because it would be difficult in practice for the taxpayer to demonstrate that another entity's (be it the recipient or the private company) honest mistake or inadvertent omission is the cause of the result produced.

Recurring mistakes or omissions

97. The fact that a mistake or omission recurs does not automatically qualify or disqualify a taxpayer from satisfying the requirements of subsection 109RB(1). Each mistake or omission must be examined separately to determine whether it is in fact an honest mistake or inadvertent omission.

98. A mistake or omission may recur for different reasons and it is necessary to enquire into those reasons to determine whether each occurrence is or continues to be an honest mistake or inadvertent omission. Once a person becomes aware of a past mistake or omission, the circumstances will not support a finding of any new honest mistake or inadvertent omission on those particular circumstances.

99. A mistake or omission may recur for the same reason, that is, it stems from an original mistake or omission which carries over to subsequent years. If the original mistake or omission is an honest mistake or inadvertent omission, the subsequent mistakes or omissions may also qualify.

Appendix 2 – Detailed contents list

100. The following is a detailed contents list for this Ruling:

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TR 2006/10

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- deemed dividends
- dividend income

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