

**FEDERAL COURT OF AUSTRALIA**

**Commissioner of Taxation v Indooroopilly Children Services (Qld) Pty Ltd**

**[2007] FCAFC 16**

**TAXATION** – fringe benefits tax – definition of fringe benefit – whether contribution to employee incentive trust fringe benefit – whether benefits provided in respect of the employment of the employee – whether fringe benefits tax imposed on benefits provided rather than benefits received – whether person participates in or facilitates scheme or plan involving provision of benefit

**PUBLIC LAW** – function of courts exercising federal jurisdiction – obligation of Commissioner of Taxation to administer law as interpreted by judiciary

*Fringe Benefits Tax Assessment Act 1986* (Cth) ss 40, 43, 136(1), 148(1), 154, 159

*Fringe Benefits Tax Act 1986* (Cth)

*Taxation Administration Act 1953* (Cth) s 14ZY

*Income Tax Assessment Act 1936* (Cth) s 26AAB(14)

*Attorney-General (NSW) v Quin* (1990) 170 CLR 1 cited

*Caelli Constructions (Vic) Pty Ltd v Commissioner of Taxation* (2005) 147 FCR 449 cited

*Cameron Brae Pty Ltd v Commissioner of Taxation* (2006) FCA 918; 2006 ATC 4433 cited

*Corporation of the City of Enfield v Development Assistance Commission* (1999) 199 CLR 135 cited

*Essenbourne Pty Ltd v Federal Commissioner of Taxation* 2002 ATC 5201 applied

*J & G Knowles v Commissioner of Taxation* (2000) 96 FCR 402 cited

*Marbury v Madison* 5 US 87 (1803) applied

*P & C Cantarella v Egg Marketing Board* [1973] 2 NSWLR 366 cited

*Smith v Commissioner of Taxation* (1987) 164 CLR 513 cited

*Spotlight Stores Pty Ltd v Federal Commissioner of Taxation* 2004 ATC 4674 cited

*Truth About Motorways Pty Ltd v Macquarie Infrastructure Investment Management Ltd* (1999) 200 CLR 591 cited

*Walstern v Federal Commissioner of Taxation* (2003) 138 FCR 1 applied

**COMMISSIONER OF TAXATION v INDOORROOPILLY CHILDREN SERVICES  
(QLD) PTY LTD**

**QUD 253 OF 2006**

**STONE, ALLSOP AND EDMONDS JJ**

**22 FEBRUARY 2007**

**SYDNEY(HEARD IN BRISBANE)**

GENERAL DISTRIBUTION

**IN THE FEDERAL COURT OF AUSTRALIA  
QUEENSLAND DISTRICT REGISTRY**

**QUD 253 OF 2006**

**ON APPEAL FROM A SINGLE JUDGE OF THE FEDERAL COURT OF AUSTRALIA**

**BETWEEN:                   COMMISSIONER OF TAXATION  
                                  Appellant**

**AND:                        INDOOROPILLY CHILDREN SERVICES (QLD) PTY LTD  
                                  Respondent**

**JUDGES:                   STONE, ALLSOP AND EDMONDS JJ**

**DATE OF ORDER:       22 FEBRUARY 2007**

**WHERE MADE:           SYDNEY(HEARD IN BRISBANE)**

**THE COURT ORDERS THAT:**

1.       The appeal be dismissed.
2.       The appellant pay the respondent's costs of the appeal.

Note: Settlement and entry of orders is dealt with in Order 36 of the Federal Court Rules.

GENERAL DISTRIBUTION

**IN THE FEDERAL COURT OF AUSTRALIA  
QUEENSLAND DISTRICT REGISTRY**

**QUD 253 OF 2006**

**ON APPEAL FROM A SINGLE JUDGE OF THE FEDERAL COURT OF AUSTRALIA**

**BETWEEN:                COMMISSIONER OF TAXATION  
                                 Appellant**

**AND:                     INDOOROPILLY CHILDREN SERVICES (QLD) PTY LTD  
                                 Respondent**

**JUDGES:                STONE, ALLSOP AND EDMONDS JJ**

**DATE:                    22 FEBRUARY 2007**

**PLACE:                  SYDNEY(HEARD IN BRISBANE)**

**REASONS FOR JUDGMENT**

**STONE J**

1                I have had the benefit of reading the reasons for judgment of Edmonds J. I agree with the orders proposed by his Honour and with his reasons for those orders. I also wish to express my agreement with the additional comments of Allsop J.

I certify that the preceding one (1) numbered paragraph is a true copy of the Reasons for Judgment herein of the Honourable Justice Stone.

Associate:

Dated:        22 February 2007

**IN THE FEDERAL COURT OF AUSTRALIA  
QUEENSLAND DISTRICT REGISTRY**

**QUD 253 OF 2006**

**ON APPEAL FROM A SINGLE JUDGE OF THE FEDERAL COURT OF AUSTRALIA**

**BETWEEN:                   COMMISSIONER OF TAXATION  
                                  Appellant**

**AND:                        INDOOROPILLY CHILDREN SERVICES (QLD) PTY LTD  
                                  Respondent**

**JUDGES:                   STONE, ALLSOP AND EDMONDS JJ**

**DATE:                      22 FEBRUARY 2007**

**PLACE:                     SYDNEY (HEARD IN BRISBANE)**

**REASONS FOR JUDGMENT**

**ALLSOP J**

2               I have had the considerable advantage of reading the reasons for judgment of Edmonds J. I agree with his Honour's reasons and the orders that he proposes.

3               I wish, however, to add some comments about the attitude apparently taken by, and some of the submissions of, the appellant. From the material that was put to the Full Court, it was open to conclude that the appellant was administering the relevant revenue statute in a way known to be contrary to how this Court had declared the meaning of that statute. Thus, taxpayers appeared to be in the position of seeing a superior court of record in the exercise of federal jurisdiction declaring the meaning and proper content of a law of the Parliament, but the executive branch of the government, in the form of the Australian Taxation Office, administering the statute in a manner contrary to the meaning and content as declared by the Court; that is, seeing the executive branch of government ignoring the views of the judicial branch of government in the administration of a law of the Parliament by the former. This should not have occurred. If the appellant has the view that the courts have misunderstood the meaning of a statute, steps can be taken to vindicate the perceived correct interpretation

on appeal or by prompt institution of other proceedings; or the executive can seek to move the legislative branch of government to change the statute. What should not occur is a course of conduct whereby it appears that the courts and their central function under Chapter III of the *Constitution* are being ignored by the executive in the carrying out of its function under Chapter II of the *Constitution*, in particular its function under s 61 of the *Constitution* of the execution and maintenance of the laws of the Commonwealth.

- 4 It is the function of the courts exercising federal jurisdiction to declare the meaning of statutes of the Commonwealth Parliament in the resolution or quelling of controversies. To quote Marshall CJ in *Marbury v Madison* 5 US 87 at 111 (1803):

*'It is, emphatically, the province and duty of the judicial department to say what the law is.'*

- 5 This passage has been recognised as central to the administration of justice and to the relationship between the judiciary and executive in this country: *Attorney-General (NSW) v Quin* (1990) 170 CLR 1 at 35-36; *Corporation of the City of Enfield v Development Assistance Commission* (1999) 199 CLR 135 at 152-154 [42]-[44] and *Truth About Motorways Pty Ltd v Macquarie Infrastructure Investment Management Ltd* (1999) 200 CLR 591 at 635 [116].

- 6 Considered decisions of a court declaring the meaning of a statute are not to be ignored by the executive as *inter partes* rulings binding only in the earlier *lis*. As Mahoney J (as his Honour then was) said in *P & C Cantarella v Egg Marketing Board* [1973] 2 NSWLR 366 at 383:

*'The duty of the executive branch of government is to ascertain the law and obey it. If there is any difficulty in ascertaining what the law is, as applicable to the particular case, it is open to the executive to approach the court, or afford the citizen the opportunity of approaching the court, to clarify the matter. Where the matter is before the court it is the duty of the executive to assist the court to arrive at the proper and just result.'*

- 7 There was some inferential suggestion in argument that the appellant was somehow bound by legislation (not specifically identified) to conduct his administration of the relevant statute by reference to his own view of the law and the meaning of statutory provisions, rather than by following what the courts have declared. It only need be said that any such

provision would require close scrutiny, in particular by reference to issues raised by s 15A of the *Acts Interpretation Act 1901* (Cth).

I certify that the preceding six (6) numbered paragraphs are a true copy of the Reasons for Judgment herein of the Honourable Justice Allsop.

Associate:

Dated: 22 February 2007

**IN THE FEDERAL COURT OF AUSTRALIA  
QUEENSLAND DISTRICT REGISTRY**

**QUD 253 OF 2006**

**ON APPEAL FROM A SINGLE JUDGE OF THE FEDERAL COURT OF AUSTRALIA**

**BETWEEN:                    COMMISSIONER OF TAXATION  
                                  Appellant**

**AND:                        INDOOROOPIILY CHILDREN SERVICES (QLD) PTY LTD  
                                  Respondent**

**JUDGES:                   STONE, ALLSOP AND EDMONDS JJ**

**DATE:                      22 FEBRUARY 2007**

**PLACE:                     SYDNEY (HEARD IN BRISBANE)**

**REASONS FOR JUDGMENT**

**EDMONDS J:**

**BACKGROUND**

8                    This is an appeal from a judge of this Court allowing an appeal against an objection decision made by the appellant ('the Commissioner') under s 14ZY of the *Taxation Administration Act 1953* (Cth) ('the Administration Act'). By his objection decision, the Commissioner disallowed the respondent's objection against a private ruling ('the ruling') issued to a number of rulees, including the respondent, by notice dated 30 June 2005 in relation to years of income tax ended 30 June 2005 to 2010 inclusive and years of fringe benefits tax ended 31 March 2006 to 2011 inclusive.

9                    The respondent's objection to the ruling only put in issue the Commissioner's answer to question 1 of the ruling application which was in the following terms:

*'Does the issue of ABC Public shares in accordance with the facts set out in appendix 4 to the trustee of the CSP give rise to a fringe benefit as defined in subsec 136(1) of the FBTAA in relation to ABC Public or any rulee RMC in relation to a year of tax?'*

10 In the ruling, the Commissioner answered this question as follows:

*‘The issue of ABC Public shares in accordance with the facts set out in the application to the trustee of the Carers Share Plan does give rise to a fringe benefit as defined in subsection 136(1) of the Fringe Benefits Tax Assessment Act 1986 in relation to the rulee Regional Management Companies as employers in relation to a year of tax, but not in relation to ABC Public.’*

11 The respondent is a company, one of a number of Regional Management Companies (‘RMC’s’) licensed or franchised to operate childcare centres by ABC Developmental Learning Centres Pty Ltd, a wholly owned subsidiary of ABC Learning Centres Ltd (‘ABC Public’), a listed public company. The factual background to question 1 of the ruling application, and the Commissioner’s answer, was set out in Appendix 4 to the ruling application:

***‘Background***

1. *ABC Learning Centres Ltd (“ABC Public”) is a publicly listed company, whose shares trade on the ASX.*
2. *ABC Developmental Learning Centres Pty Ltd (“ABC”) is a wholly owned subsidiary of ABC Public.*
3. *Prior to the establishment of a franchising structure (detailed below) in 2000, ABC operated childcare centres in Queensland and a smaller number in Victoria. The operations were conducted at premises owned or leased by ABC Public. ABC Public let or sub-let each premises to ABC.*
4. *In various Australian States the relevant statutes regulating the provision of childcare services (Childcare Act (Qld) and Children Services Act (Vic)) require the operator of a childcare centre to be licensed. ABC obtained the appropriate licences, which pertained to ABC and a particular centre.*
5. *ABC employed all the childcare workers for each centre, which was managed by a senior childcare worker (“a Regional Manager”), who was responsible for managing all ABC childcare centres in the same district or region.*
6. *As a result of the rapid expansion of the ABC business the structure of the ABC group business changed completely.*
7. *The operational responsibility of providing childcare services within each region was passed to each Regional Manger, who became directly responsible for his or her own business.*



8. *The new structure involved each Regional Manager being given the opportunity to establish his or her own regional management company ("RMC") to provide directly the childcare services for licensed centres for a particular region. No Regional Manager holds any office or employment in any other RMC or in ABC Public, ABC or any associated companies. No employee of an RMC is an employee in any other RMC. No employee of an RMC provides services to ABC or any other RMC. No employee of ABC Public, ABC or any associated companies is an employee of any RMC.*
9. *New geographical areas for franchise expansion are constantly being identified. ABC has engaged an independent party to establish RMCs in such areas and manage it on a temporary basis. The RMC will employ child carers with a view to one of those child carers becoming qualified as a Regional Manager and being then given the opportunity to take over that RMC from the interim manager by way of purchase. There are no rulee/Beneficiaries who are employees of these "seed" RMCs. Nevertheless, those employees would also be able to qualify as Beneficiaries of the CSP.*
10. *An RMC is fully responsible for the conduct of the day-to-day operations of its regional centres (an RMC might operate more than one childcare centre), including the collecting and banking of fees and the employment of staff. Some expenses common among the RMCs are borne by ABC as agent for each RMC because ABC can obtain volume discounts.*
11. *ABC held the licences to operate each childcare centre in each region. When it changed its operations from that of providing childcare services to that of licensing or "franchising", it licensed to the relevant RMC, under a written Licence Agreement, its right to operate each childcare centre.*
12. *A standard Licence Agreement is enclosed with this ruling request. The parties to the Licence Agreement are ABC, the RMC, and the Regional Manager.*
13. *Under the Licence Agreement, the responsibility for providing childcare services rests with RMC, as does all the day-to-day management of each childcare centre. ABC does not have any rights to conduct a childcare business relating to any centre; its rights relate to the receipt of licence fees from the RMC.*
14. *As the statutory licensee, however, ABC remained responsible for ensuring that the legislation is complied with. That is, a breach of the relevant standards by an RMC would result in a breach of the licence held by ABC. To that end, each Licence Agreement imposes comprehensive obligations on the RMC that mirror the legislative*

*obligations imposed upon ABC. Specifically, the Licence Agreement contains comprehensive termination clauses that are triggered should an RMC breach relevant standards relating to the provision of childcare services. ABC employs people to visit each childcare centre to ensure the Licence Agreements are adhered to. These people do not work in the business of any of the RMCs and are not intended to be beneficiaries of the CSP.*

15. *The branding of the ABC Developmental Learning System is perceived by ABC Public to be important to its success, and the success of the RMCs. In this regard the franchise has similarities with well-known franchises such as McDonalds, where there are standard protocols that are followed, standard teaching philosophies, standard levels or grades of staff throughout the RMCs etc.*

***Reasons for proposed Carers Share Plan (CSP)***

16. *ABC Public perceives there to be medium and long-term benefits associated with establishing the CSP.*
17. *First, the presence of the CSP is expected to engender in the RMCs and their staff a sense of ownership of ABC Public – its success is their success. In particular, the structure of the CSP provides goals for employees of the RMCs to achieve progressively.*
18. *Second, the method chosen does not involve ABC Public or ABC in any significant cost, for the shares to be issued will simply dilute the holdings of the existing shareholders. The synergistic benefits, however, are perceived to outweigh any immediate dilution in value.*
19. *Third, a key aim of the CSP is the retention of staff for longer periods of time. It is perceived that staff turnover in the childcare industry is a major cost, given that the labour is necessarily skilled labour. As franchise fees payable to ABC are linked to the revenues and expenses of each RMC, the reduction in staff turnover costs for the RMCs has a direct positive bearing on the revenues of ABC.*
20. *Fourth, the CSP is designed in a way to attract new staff from competitors to the RMCs. Again, this is expected to give rise to a material cost saving in staff training, in that experienced outside child carers are given an incentive to join with an RMC.*
21. *Fifth, ABC Public considers that the establishment of the CSP allows it to be seen by its shareholders to be keeping ahead of what is now a deepening and more competitive market.*
22. *There is also an immediate advantage that arises to ABC. It is proposed, as set out below, that only employees of RMCs who sign Australian Workplace Agreements qualify as Beneficiaries of the CSP.*

*There are expected to be material administrative savings from having the employees of each RMC operating under the same terms and conditions set out in the AWA.*

23. *There are perceived to be no taxation benefits to ABC Public or its associates, and none are intended. ABC Public will not claim any tax deductions for issuing fully paid ordinary shares. Conversely, there are expected to be no taxation detriments to any party. Rather, the employees of the RMCs who receive shares are expected to include the value of those shares in their assessable income when received.*
24. *The Board of ABC Public considers it appropriate to have the taxation neutrality of the CSP confirmed by the ATO.*

### ***Involvement of RMCs***

25. *The CSP has been conceived by ABC Public without any consultation with any RMC. The establishment of the CSP will not require the agreement of the RMCs. There does not need to be, and there will not be, any understanding between ABC Public, its associates and the trustee on the one hand and the RMCs on the other as to when and in what amount ABC Public shares will be issued to the trustee and provided to Beneficiaries. The RMCs will not provide any compensation or other payments directly or indirectly to ABC Public or its associates in relation to the CSP.*
26. *The controllers of the RMCs, who are employees of the RMCs and will be Beneficiaries, will be explained how the CSP operates and will be informed of the number of shares that ABC Public proposes to issue.*
27. *The RMCs are not necessary to facilitate the operation of the CSP, or be otherwise involved in its operation. As with other advertising of the ABC franchises, ABC Public and ABC will undertake all promotion of the CSP, e.g. by way of media advertising, information leaflets to the RMCs and their employees.*
28. *In relation to the ongoing operation of the CSP, the trustee will not need any participation in its activities by any RMC. The trustee, in order to satisfy its fiduciary obligations to all Beneficiaries, will need to make inquiries of the Beneficiaries as to their status, e.g. length of service, whether employed, whether any disqualifying events have occurred. It can be expected that the trustee will request this information from ABC, who obtains this information through a subcontractor independent from the RMCs in carrying out its obligations under the Licence agreements. No party other than the trustee will have any involvement in the exercise of the trustee's discretion to appoint ABC Public shares to any particular Beneficiary.*

**Outline of the CSP****A. Independent Trustee**

29. *The CSP will be governed by an independent professional trustee (the trustee has not been selected yet by the board of ABC Public). The trustee will ensure that the business of the CSP is conducted as detailed in the Trust deed. The trustee will be entitled to pay to itself (or any manager it appoints) professional fees for carrying on the business of the trust.*
30. *ABC Public will have a power to remove the trustee and replace it with another independent professional trustee.*
31. *The usual clauses required by professional trustees by way of indemnity will be included in the deed.*

**B. Trust Property**

32. *The trust property will be ordinary shares in ABC Public, issued directly by ABC Public as fully paid. The trustee will not give any consideration for the issue of the shares.*
33. *ABC Public will promulgate guidelines as to when and in what amounts it will gift shares into the CSP. These guidelines are discussed immediately below.*
34. *ABC Public will not issue ordinary shares to the trustee in a haphazard fashion. Rather, the method it chooses will be visible, as an incentive, to the employees of the RMCs and will be based on the RMC's status and the status of each employee with the RMC.*
35. *The following table sets out the number of shares ABC Public expects to issue:*

<i>Position</i>	<i>Years of Service in position at an ABC centre</i>	<i>Signatory to AWA</i>	<i>Number of Shares</i>
<i>Assistant</i>	<i>2</i>	<i>Yes</i>	<i>300</i>
<i>Group Leader</i>	<i>2</i>	<i>Yes</i>	<i>450</i>
	<i>4</i>	<i>Yes</i>	<i>700</i>
	<i>6</i>	<i>Yes</i>	<i>900</i>
<i>Director and RMC Level 2</i>	<i>2</i>	<i>Yes</i>	<i>900</i>
	<i>2</i>	<i>Yes</i>	<i>1400</i>
	<i>4</i>	<i>Yes</i>	<i>1400</i>
	<i>4</i>	<i>Yes</i>	<i>1850</i>
	<i>6</i>	<i>Yes</i>	<i>1850</i>
	<i>6</i>	<i>Yes</i>	<i>2300</i>
<i>RMC Level 1</i>	<i>2</i>	<i>Yes</i>	<i>1850</i>
	<i>4</i>	<i>Yes</i>	<i>2300</i>
	<i>6</i>	<i>Yes</i>	<i>2800</i>

36. *So, the initial issue of ordinary shares by ABC Public will be calculated by reference to the number of employees of the RMCs who have signed an AWA, hold the positions set out above, and have served a certain full-time (or full time equivalent) period in that position at an ABC centre. There will be some minor adjustments for those employees who have changed categories over the years. There will also be credit given to employees of other childcare centres, in order to make it more attractive for those employees to join one of the RMCs.*
37. *ABC Public's self-imposed criteria for the issue of shares to the trustee of the CSP, however, is separate from the trustee's selection criteria for the exercise of its powers of appointment detailed below. No person has any right to have ABC Public issue ordinary shares to the trustee.*

**C. Trust Income**

38. *The income of the trust estate will be dividends paid by ABC Public in the ordinary course of its business.*
39. *The trustee will have no powers of investment. Rather, it must hold the ABC Public shares solely to provide to the Beneficiaries over time. It can be expected to receive cash dividends as and when declared by ABC Public. It will not be permitted to take part in any voluntary scrip dividend plan.*

**D. Beneficiaries**

40. *The class of beneficiaries of the CSP will be defined in the following fashion:*

*"Any employee of an RMC that:*

- (a) holds the position of Assistant, Group leader, Director, or Regional Manager; and*
- (b) is a signatory to an Australian Workplace Agreement with an RMC; and*
- (c) is not an Excluded Person."*

41. *"Excluded Person" will be defined to include employees of ABC Public, ABC, the trustee and their associates.*
42. *The CSP will be a discretionary trust. The trustee will have powers to appoint the income and the capital of the trust fund among the*

*Beneficiaries on such terms and in such proportions as it sees fit, subject to the restrictions set out above. No Beneficiary will have any contingent or vested entitlement to any shares (or income) except to the extent that the trustee exercises its discretion in that Beneficiary's favour.*

43. *The trustee can exercise its powers on two occasions each year, 1 March and 1 September.*

***E. Appointment of Income***

44. *The trust deed will contain detailed selection criteria to guide the trustee in the exercise of its power to appoint income at each appointment date based on:*

- *The number of shares gifted by ABC Public;*
- *The absence of any disqualifying events (such as fraud, misconduct);*
- *The Beneficiary's position or positions (i.e. Assistant, Group leader, Director, Regional Manager etc);*
- *Years of service in position at any ABC childcare centre and qualifications;*
- *Years of full-time (or equivalent) employment with an RMC since becoming a Beneficiary.*

45. *The following table sets out the specific years employment in each position required to qualify:*

<i>Position</i>	<i>Qualifications</i>
<i>Assistant</i>	<i>1 yrs qualification</i>
<i>Group Leader</i>	<i>2 yr qualification</i>
	<i>2 yr qualification</i>
	<i>2 yr qualification</i>
<i>Director and RMC Level 2</i>	<i>2 yr qualification</i>
	<i>3 yr qualification</i>
	<i>2 yr qualification</i>
	<i>3 yr qualification</i>
	<i>2 yr qualification</i>
	<i>3 yrs qualification</i>
<i>RMC Level 1</i>	<i>3 yr qualification</i>
	<i>3 yr qualification</i>
	<i>3 yr qualification</i>

46. *Once the trustee has determined that a Beneficiary has satisfied the selection criteria for an appointment of income, a Beneficiary can be appointed income pertaining to a notional number of shares.*
47. *The trustee can be satisfied of the relevant criteria by a certification by ABC. ABC will be entitled to treat a particular employee's permanent part-time employment as a full-time equivalent. ABC will also be entitled to give a 50% credit for an employee's full-time (or full-time equivalent) experience in childcare with another employer as employment with ABC. (This is an incentive designed, as mentioned earlier, to attract staff from rival childcare organisations.)*
48. *If there remains income to be appointed after expenses and after the trustee has considered the various selection criteria, the trustee must exercise its power to appoint the excess income among the Beneficiaries who are employees of the relevant RMC. There will be no power of accumulation. Subject to administrative workability, the trustee would be expected to appoint the excess income rateably among those Beneficiaries according to their respective expectancies.*

**F. Appointment of Capital**

49. *If a Beneficiary has been appointed income pertaining to a notional number of shares then the trustee would be expected subsequently to appoint that number of shares to the Beneficiary if the following further selection criteria are fulfilled:*
  - (a) *a period of 12 months full time (or permanent part-time equivalent) employment with an RMC since the appointment of income;*
  - (b) *The absence of any disqualifying events (such as fraud, misconduct).*
50. *Any such appointment can be expected to be notional or provisional, in that the Beneficiary must serve a further period of 12 months full time (or permanent part-time equivalent) employment with an RMC. After that time, and only once ABC certifies to the trustee that the Beneficiary has fulfilled all selection criteria, which certification cannot be unreasonably withheld, the Beneficiary can request to be considered for an indefeasible appointment of shares. The trustee can be expected to make such an appointment, although it retains the discretion not to do so.*
51. *In order to protect further the interests of employees of the RMCs a Beneficiary who leaves employment with an RMC [and is not otherwise disqualified] will be deemed to have made a request for consideration immediately prior to leaving employment, and the trustee must consider exercising the power in his or her favour.*

**G. Termination of the CSP**

52. *The CSP will continue until the earlier of 80 years or the liquidation of ABC Public.*
53. *It is expected that the employees of the RMCs will in due course be appointed all the shares issued by ABC Public. In this regard there will be employees who disqualify themselves from benefitting at various stages, or who never meet the selection criteria for appointment of shares, such that there will be a “surplus” at various stages. However, there will also be continual qualification of employees by way of promotion, new employment, or a change in status of an RMC. The “surplus” will be available to meet that need, with ABC Public then issuing a lesser amount of new ordinary shares to the trustee.*
54. *Nevertheless, at the time of the termination of the Trust there can be expected to be a final surplus. The trustee must distribute these surpluses among the respective Beneficiaries for each RMC at that time as it sees fit. It will be empowered to seek recommendations from ABC Public (or the liquidator) as to how it should carry out that duty, but will not be bound to follow any recommendations.’*

12 Detailed reasons for the answer to question 1 were set out in a document entitled ‘EXPLANATION: (This does not form part of the Notice of Private Ruling)’. This document was attached to the Notice of Private Ruling Authorisation Number 53514. After setting out the definitions of ‘Fringe benefit’ and ‘Arrangement’ in subs 136(1) of the *Fringe Benefits Tax Assessment Act 1986* (Cth) (‘the FBTA’), the reasons for the answer to question 1 were expressed in the following terms:

**‘Consideration**

*The issue of shares by ABC Public to the trustee of the CSP will constitute the provision of a fringe benefit by the RMC to its employees if:*

*A benefit is provided to an associate of the employee by:*

- (e) a person (the arranger) other than the employer or an associate of the employer under an arrangement covered by paragraph (a) of the definition of “arrangement” between the employer and the arranger, or*
- (ea) a person other than the employer or an associate of the employer, if the employer:*



- (i) *participates in or facilitates the provision of the benefit; or*
- (ii) *participates in, facilitates or promotes a scheme or plan involving the provision of the benefit;*

*and the employer [or associate] knows, or ought reasonably to know, that the employer [or associate] is doing so,*

*and the **benefit is provided in respect of the employment of the employee**, provided it is **not otherwise excluded** by paragraphs (f) to (r) of the definition of 'fringe benefit.'*

### ***Benefit***

*Shares are considered to be property and therefore a 'benefit' for the purposes of the FBTA.*

### ***Provide***

*When ABC issues shares to the trustee they are considered to provide property to the trustee pursuant to section 154 of the FBTA.*

### ***Associate of the employee***

*The trustee of the CSP is considered to be an associate of an employee where the employee is capable of benefiting under the trust.*

*Thus, when ABC issues shares to the trustee of a trust, and an employee is capable of benefiting under that trust, a benefit will be provided to an associate of the employee.*

### ***Arranger***

*ABC and the RMC are not associates. Thus ABC will be a person (the arranger) for the purposes of paragraph (e) if ABC issues shares to the trustee under an arrangement between ABC and the RMC and the arrangement is covered by paragraph (a) of the definition of 'arrangement'.*

*The applicant advises that the RMCs are aware that ABC intends to issue shares to the trustee for the benefit of the RMCs employees, however they note that ABC has not made an arrangement with the RMC to issue shares to the CSP and that the CSP was conceived by ABC Public without any consultation with any RMC and further its establishment does not require the agreement of the RMCs.*

*It is considered that the RMC would understand that it to [sic] would benefit (whether this be financial or otherwise, eg enhanced retention of experienced staff, reduction in staff training costs, the attraction of experienced staff from competitors) from the issue of shares under the arrangement.*

*However, to fall within paragraph (e), it is arguable that more is required than an understanding on the part of the RMC that they will benefit from the*

*issue of shares to the trustee, ie the shares would need to be issued subject to or as a result of an understanding between ABC and the RMC.*

*Thus it is arguable that ABC is not a person for the purposes of paragraph (e).*

***Person for the purposes of paragraph (ea)***

*ABC and the RMC are not associates. Thus ABC will be a person (the provider) for the purposes of paragraph (ea) if:*

*The RMCs participate in or facilitate the issue of shares to the trustee and know or ought to know they are doing so, or*

*The RMCs participate in, facilitate or promote the CSP and know or ought to know they are doing so.*

*The applicant states that the initial issue of shares by ABC to the CSP will be calculated by reference to the number of employees of the RMCs who have signed an AWA, hold (specified) positions, and have served a certain full-time ... period in that position at an ABC centre.*

*In relation to the ongoing operation of the CSP, the applicant states that the trustee will not need any participation in its activities by any RMC. The applicant notes that the trustee, in order to satisfy its fiduciary obligations to all Beneficiaries, will need to make inquiries of the Beneficiaries as to their status, e.g. length of service, whether employed, whether any disqualifying events have occurred.*

*In a letter dated 28 August 2003 that applicant states that:*

*'ABC does not know how the trustee will carry out its duty to make inquiries of its Beneficiaries. ABC expects the trustee will ask it. ... The trustee might ask the RMCs.*

*As a practical matter ABC will have the necessary information in its possession. Specifically, ABC is obliged to perform administrative services for each RMC under the Licence Agreement, being other services as agreed in schedule 6. These services include managing pay-rolls of the RMCs. As such, ABC has access to all employment history necessary for it to determine which employees meet the qualifying criteria.'*

*From the above it is clear that if the RMCs were to provide this information to the trustee they would be participating in or facilitating the issue of shares to the trustee and participating in or facilitating the CSP and would know or ought reasonably to know they were doing so.*

*Where the information is provided to the trustee by ABC, the RMCs are still considered to be participating in or facilitating the issue of shares to the trustee and participating in or facilitating the CSP, because it is only as a result of their agreement with ABC (under the Licence Agreement), that ABC is able to provide this information.*

*Thus for the purposes of paragraph (ea) ABC is considered to be a person (the provider).*

***The benefit is provided in respect of the employment of the employee***

*Whilst the expression 'in respect of' has no fixed meaning, the full Federal Court in J & G Knowles v FC of T (2000) 96 FCR 402; 2000 ATC 4151; (2000) 44 ATR 22 examined its meaning in relation to Fringe Benefits Tax (FBT) and noted that:*

*...what must be established is whether there is a sufficient or material, rather than a causal connection or relationship between the benefit and the employment ...*

*The Court also suggested that it would be useful to ask 'whether the benefit is a product or incident of the employment'.*

*The CSP is considered to operate as an employee incentive scheme providing rewards to RMC employees for services they provide as employees. As such the issue of shares by ABC Public to the trustee of the CSP is considered to be a product or incident of that employment, having the requisite sufficient or material connection to employment.*

*The definition of 'fringe benefit' also refers to a benefit being provided in relation to 'an employee', and for reasons outlined in paragraphs 45 - 49 of TR 1999/5 the ATO considers a fringe benefit can arise notwithstanding that a benefit provided to a trust may not be provided in respect of a specific employee.*

*Whilst Kiefel J's views in the Essensbourne case [2002] FCA 1577 about the proper interpretation of the definition of a fringe benefit in the fringe benefits tax law are contrary to the views expressed in Taxation Ruling TR 1999/5, the Commissioner has determined that as the Essensbourne case is not an appropriate vehicle to test the issue with the Full Federal Court, the views expressed in TR 1999/5 will remain the ATO position.*

*Notwithstanding the above, it is arguable that the facts in this case can be distinguished from those in Essensbourne. In Essensbourne the employer (Essensbourne) contributed \$252,000 to the trustee of an Employee Incentive Trust in respect of the three brothers employed by Essensbourne. The amount of the contribution was said to be ultimately based on the amount that could be contributed to the Essensbourne Superannuation Fund (in respect of the seven members of this fund, this included the other family members) on the*

*basis of the age limits. Under clause 5.1 of the Trust deed the employer was said 'to make contributions for the benefit of "its employees generally".'*

*In this case, the CSP Deed at Clause A of the Recital, states that the Settlor (ABC Public) 'wishes to establish a trust to benefit certain persons', and at paragraphs 35 and 36 of Appendix 4 it is stated that:*

35. *The following table sets out the number of shares ABC Public expects to issue:*

...

36. *So, the initial issue of ordinary shares by ABC Public will be calculated by reference to the number of employees of the RMCs who have signed an AWA, hold positions as set out above, and have served a certain full-time (or full-time equivalent) period in that position at an ABC centre ...*

*Thus it is arguable that the shares to be issued to the trustee of the CSP will be shares provided in respect of the employment of particular employees.*

***The benefit is not otherwise excluded***

*When ABC Public issues shares to the trustee of the CSP a fringe benefit will arise unless the benefit is specifically excluded from the definition of fringe benefit by virtue of paragraphs (f) to (r) of the definition.*

*Paragraph (h) will not apply as the trustee is not the employee or a relative of the employee.*

*Paragraph (ha) will not apply as the person (being either the employee or the trustee) does not **acquire a share** under an employee share scheme within the meaning of Div 13A.*

*ie The employee does not acquire a beneficial interest in the share at the time and the trustee is excluded because of subsection 139C(5) of the ITAA 1936.*

*Paragraph (hb) will not apply as the shares obtained by the trustee are not shares in the employer company or holding company.*

*None of the other paragraphs are considered relevant.*

*Thus the issue of ABC Public shares to the trustee of the CSP will give rise to a fringe benefit.'*

*shares in accordance with the facts set out in Appendix 4 to the trustee of the CSP give rise to assessable income of any rulee Beneficiary in relation to a year of tax? – in the negative, the Commissioner wrote –*

*‘... the issue of ABC Public shares to the trustee of the CSP is not the acquisition of a beneficial interest in any shares by a rulee Beneficiary ...’*

A contrary submission was put in the Commissioner’s written submissions, but abandoned at the outset on the hearing of the appeal.

### **BEFORE THE PRIMARY JUDGE**

14           The primary judge approached the case before her on the basis that it was viewed by the Commissioner as a ‘test case’. Her Honour held that the shares gifted to the trustee were not a ‘fringe benefit’ because the shares were not provided in connection with any particular employee. Her Honour’s decision adopted the construction of ‘fringe benefit’ of Kiefel J in *Essenbourne Pty Ltd v Federal Commissioner of Taxation* 2002 ATC 5201, and applied by Hill J in *Walstern v Federal Commissioner of Taxation* (2003) 138 FCR 1. The correctness of the decision in *Essenbourne* was argued in *Walstern*, where Hill J held that Kiefel J was ‘clearly right’ on the construction of ‘fringe benefit’ (at [87]), and also in *Spotlight Stores Pty Ltd v Federal Commissioner of Taxation* 2004 ATC 4674 (Merkel J) and *Caelli Constructions (Vic) Pty Ltd v Commissioner of Taxation* (2005) 147 FCR 449 (Kenny J). Merkel J simply expressed his view that he was not satisfied that *Essenbourne* and *Walstern* were clearly wrong and accordingly proposed to follow them (at [121]). Kenny J made no finding, instead her Honour applied *Essenbourne*, on the assumption that it correctly stated the law on the point: See [57] – [62].

15           Following her Honour’s judgment below, in *Cameron Brae Pty Ltd v Commissioner of Taxation* (2006) FCA 918; 2006 ATC 4433 another judge of this Court (Ryan J) embraced the views of Kiefel J in *Essenbourne* and Hill J in *Walstern* (at [67] – [74]).

16           The primary judge canvassed the construction adopted in the cases of *Essenbourne* and *Walstern*, and followed in *Spotlight Stores* and *Caelli Constructions*, at some length, and there is no utility in repeating those observations.

**THE COMMISSIONER'S SUBMISSIONS ON APPEAL**

17           On his appeal to this Court, the Commissioner made a number of submissions, some of which coincide with the reasons for his answer to question 1 in the ruling application, which reasons are set out in [12] above, others of which do not. At the forefront of those submissions, the following propositions emerge:

1.       For a benefit to be a 'fringe benefit', it need not be provided to an employee; it is sufficient if it is provided to an 'associate' of the employee.
2.       The term 'associate' is defined in subs 136(1) of the FBTAA by reference to s 26AAB of the *Income Tax Assessment Act 1936* (Cth) ('the ITAA 1936') and, relevantly, in relation to a person, includes a trustee of a trust estate where the person is capable of benefiting under the trust: See s 26AAB(14)(a)(iv) of the ITAA 1936.
3.       The trustee of the CSP is an 'associate' of an employee where the employee is capable of benefiting under the trust constituting the CSP.
4.       When ABC Public issues shares to the trustee of the CSP, property will be provided by ABC Public to the trustee and, in consequence, a benefit will be provided by ABC Public to the trustee.
5.       If an employee is capable of benefiting under the trust constituting the CSP, a benefit will be provided by ABC Public to an associate of the employee.
6.       The subject of the tax imposed by the FBTAA is the value of benefits provided by the employer, not the value of benefits received by the employee. The construction of the definition of 'fringe benefit' contended for by the Commissioner is that it is sufficient to constitute a fringe benefit if the employer provides the benefit for its employees, where employment is the sufficient and material link to the provision, even though a particular employee may not benefit immediately at the time of provision. The *Essenbourne* construction places the focus wrongly on what the employee receives, rather than on what the employer provides.

18           It is necessary to examine some of these propositions more closely.

**Proposition 1**

19           This proposition is undoubtedly correct. However, unless a benefit is provided **to** an employee or to an associate of the employee, it will not be a ‘fringe benefit’ even if it is provided **by** an employer, an associate of the employer or a person within pars (e) or (ea) of the definition. In short, a benefit will not be a ‘fringe benefit’ as defined unless it is provided **to** one of two possible ‘recipients’ and is provided **by** one of four possible ‘providers’. The dual requirement of the definition is quite clear.

20           There can be no doubt that it was legislative policy to subject a benefit to fringe benefits tax, whether the benefit was provided to an employee or to an associate of the employee. Indeed, that it was intended to apply to benefits provided to an associate of the employee was seen as closing one of the ‘gaps in coverage’ of the old regime. In his Second Reading Speech at the time of introducing the Bill which became the FBTAA, the Treasurer of the day said:

*‘There has over the years been a very strong movement towards the remuneration of employees – especially higher income earners – by fringe benefits packages which allowed income tax to be avoided on substantial parts of the overall remuneration.*

*So called tax-free perks came to dominate salary package negotiations and packages were openly advertised in the market place. Increasingly innovative deals were emerging particularly after the demise of the ‘paper’ tax avoidance schemes in the early 1980s.*

*All of this was aggravated by the inability of the existing income tax system to exact tax effectively from recipients of fringe benefits. Several factors contributed to this ...*

*First there were deficiencies in the income tax law itself. A major one was that it called for case by case subjective judgments to be made as to the value of fringe benefits in the hands of individual employees.*

*That kind of requirement is simply incompatible with the efficient assessment and collection of tax on mass scale and invites disputation.*

***There were also technical defects creating gaps in coverage, for example, when benefits were given to family members and associates rather than to employees directly.*** (Emphasis added)

21           It seems clear that what the Government of the day had in mind was to close off situations where benefits were provided to family members and associates in their own right. It is far more difficult to discern any legislative policy to accelerate and bring to charge benefits provided to a trustee of a trust under which an employee is capable of benefiting, the trustee therefore being an associate of the employee, but may not benefit owing to unsatisfied contingencies or the exercise of discretions vested in the trustee. In other words, it is difficult to discern a policy under which a benefit is to be taxed at the time it is provided to the trustee associate irrespective of whether the employee ultimately takes the benefit, rather than taxation of the employee's entitlement being deferred until it emerges under the trust, if it emerges at all. The Commissioner, in his submissions, seeks to overcome this difficulty by contending (and this comes out of proposition 6) that it is sufficient to constitute a fringe benefit if the employer (or one of the other possible providers) provides the benefit for employees of the employer, where employment is a material link to the provision, even though a particular employee may not benefit immediately, that is, at the time of the provision. Actually, the Commissioner goes further because on the facts of the ruling application he makes this contention even though no employee of a rulee benefits immediately, that is, at the time of the provision, and even though ultimately one or more of those employees may not benefit at all.

22           The Commissioner seems to find comfort for his contention in the fact that the only persons capable of benefiting under the CSP are employees of the rulees; he submits that the fact that their identity at the 'provision time' is unknown does not mean that, at that time, the benefit is not provided in respect of their employment. I deal with this argument at [37] and following below.

### **Propositions 2 and 3**

23           These propositions are, in their terms, self-contained and not controversial.

### **Proposition 4**

24           If there were any doubt concerning the first limb of this proposition, then it is removed by the terms of s 154 of the FBTAA, which provides:



*‘For the purposes of this Act, where a person does anything that results in the creation of property in another person, the first-mentioned person shall be deemed to have provided that property to the other person at the time when the property comes into existence.’*

The second limb of the proposition is supported by s 40 of the FBTAA:

*‘Where, at a particular time, a person (in this section referred to as the ‘provider’) provides property to another person (in this section referred to as the ‘recipient’), the provision of the property shall be taken to constitute a benefit provided by the provider to the recipient at that time.’*

### **Proposition 5**

25           This proposition is consequential to propositions 2, 3 and 4 and is uncontroversial.

### **Proposition 6**

26           This is the controversial proposition which emerges from the Commissioner’s submissions.

27           At the outset, a number of responses can be made to it. First, the FBTAA does not impose fringe benefits tax; that is imposed by the *Fringe Benefits Tax Act 1986* (Cth) (‘the FBTAA’). Second, the FBTAA does not distinguish between the value of benefits provided by the employer and the value of benefits received by the employee. The FBTAA adopts a concept of ‘taxable value’ of a fringe benefit and, in the case of an external property fringe benefit, that is codified in the three alternatives set out in s 43. Interestingly, the fall back alternative in par (c) is ‘... the notional value of the **recipient’s property** at the provision time’. Here the recipient is the trustee of the CSP and the trustee’s property at the ‘provision time’ is the shares in ABC Public. The concept of ‘notional value’ is defined in subs 136(1) in relation to the provision of property to mean ‘... the amount that the person could reasonably be expected to have been required to pay to obtain the property ... from the provider under an arm’s length transaction’. However, at the end of the day, the value at which a fringe benefit is taxed has nothing to do with whether or not the benefit provided, in this case the shares in ABC Public provided to the trustee of the CSP, is a ‘fringe benefit’.

28           I have already responded at [21] to the Commissioner’s contended construction of the definition of ‘fringe benefit’, namely, that it is sufficient to constitute a fringe benefit if the

employer provides the benefit for its employees, even though a particular employee may not benefit immediately, that is, at the time of provision. As I there said, the contention actually goes somewhat further and I deal with that at [37] and following below.

29 The final response to proposition 6 goes to the contention that the *Essenbourne* construction places the focus wrongly on what the employee receives, rather than on what the employer provides. I do not think that this is correct. In *Essenbourne*, Kiefel J did not, contrary to this contention, focus (wrongly) on what the employee receives, rather than what the employer provides. What her Honour said (at [53]) was:

*‘The fact that the focus of the Assessment Act is upon the benefit provided by the employer does not, in my view, mean that property which is made available for the later provision of benefits to employees is to be the subject of the tax.’*

## THE DEFINITION OF ‘FRINGE BENEFIT’ AND THE DIFFERENT TEXTUAL ARGUMENTS

30 The term ‘fringe benefit’ is relevantly defined in subs 136(1) of the FBTA in the following terms:

**‘fringe benefit**, in relation to an employee, in relation to the employer of the employee, in relation to a year of tax, means a benefit:

- (a) provided at any time during the year of tax; or
  - (b) provided in respect of the year of tax;
- being a benefit provided to the employee or to an associate of the employee by:
- (c) the employer; or
  - (d) an associate of the employer; or
  - (e) a person (in this paragraph referred to as the **arranger**) other than the employer or an associate of the employer under an arrangement covered by paragraph (a) of the definition of **arrangement** between:
    - (i) the employer or an associate of the employer; and
    - (ii) the arranger or another person; or
  - (ea) a person other than the employer or an associate of the employer, if the employer or an associate of the employer:
    - (i) participates in or facilitates the provision or receipt of the benefit; or
    - (ii) participates in, facilitates or promotes a scheme or plan involving the provision of the benefit;
 and the employer or associate knows, or ought reasonably to know, that the employer or associate is doing so;
- in respect of the employment of the employee, but does not include:

- (f) *a payment of salary or wages or a payment that would be salary or wages if salary or wages included exempt income for the purposes of the Income Tax Assessment Act 1936; or*
- (g) *a benefit that is an exempt benefit in relation to the year of tax; or*
- (h) *a benefit constituted by the acquisition by the employee, or by a relative of the employee, of a share in a company, or of a right to acquire a share in a company, under a scheme for the acquisition of shares by employees, where section 26AAC of the Income Tax Assessment Act 1936 applies in relation to the acquisition; or*
- (ha) *a benefit constituted by the acquisition by a person of a share or right under an employee share scheme (within the meaning of Division 13A of Part III of the Income Tax Assessment Act 1936); or*
- (hb) *a benefit constituted by the acquisition by a trust of money or other property where the sole activities of the trust are obtaining shares, or rights to acquire shares, in a company, or a holding company (within the meaning of the Corporations Act 2001) of the first-mentioned company, and providing those shares or rights:*
  - (i) *to employees, or associates of employees, of the first-mentioned company; or*
  - (ii) *to persons who are engaged in foreign service (within the meaning of section 139GBA of the Income Tax Assessment Act 1936) for the first-mentioned company, or associates of those persons; or*
- (j) *a benefit constituted by:*
  - (i) *the making of a payment of money to a superannuation fund (as defined by subsection 6(1) of the Income Tax Assessment Act 1936) that the person making the payment had reasonable grounds for believing was a complying superannuation fund (as defined by subsection 267(1) of the Income Tax Assessment Act 1936) for the purpose of making provision for superannuation benefits for the employee (whether or not the benefits are payable to a dependant of the employee if the employee dies before or after becoming entitled to receive the benefits); or*
  - (ii) *the making of a payment of money to a non-resident superannuation fund (within the meaning of section 6E of the Income Tax Assessment Act 1936) where:*
    - (A) *the payment is for the purpose of making provision for superannuation benefits for the employee (whether or not the benefits are payable to a dependant of the employee if the employee dies before or after becoming entitled to receive the benefits); and*
    - (B) *the employee is a temporary resident (within the meaning of the Income Tax Assessment Act 1997) when the payment is made; or*
  - (iii) *the making of a payment of money to an RSA (within the meaning of the Retirement Savings Accounts Act 1997) that is held by the employee; or*

...

In *Essenbourne*, Kiefel J said:

*‘51. ...The definition of “fringe benefit” would appear to require the identification of the employee to whom the benefit is provided. This is the principal contention of Essenbourne.*

*...*

*54. In my view, Essenbourne is correct in its contention that the definition of “fringe benefit” requires reference to a particular employee in connexion with the benefit said to have been provided. This is reflected in the references to a benefit being “provided to **the** employee or to an associate of **the** employee” and to the benefit being provided “in respect of the employment of **the** employee” (emphasis added). The latter reference, in particular, can only be to a particular person’s employment. The Commissioner submitted that the reference to “an employee” in the definition should be read as “employees”, in the case of certain benefits, as s 23 Acts Interpretation Act 1901 (Cth) would permit. In my view the Assessment Act requires that the particular employee be identified in connexion with the benefit. It is their employment which, after all, provides the necessary “link” to the benefit: see *J & G Knowles & Associates Pty Ltd v FC of T* 2000 ATC 4151; (2000) 96 FCR 402. The definition does not admit of a reference to a number of employees in connexion with the benefit, the subject of the assessment.*

*55. The Commissioner did not suggest that there were other aspects of the Assessment Act which were inconsistent with the need to identify a particular employee. A reference to some aspects of the Act would seem to me to confirm this approach. This may be seen in the nature of the benefits provided, which may involve, for example, the private use by an employee or a financial dealing by the employer with them. The calculation of the taxable value of the benefit may also, in some cases, involve considerations personal to the particular employee.*

*56. The link between the benefit and the employment of the employee is required to be sufficient or material: *J & G Knowles*, ATC 4157-4158; FCR 409-410. It arises because of the words “in respect of the employment”. A mere causal link with the employment of the employee will not be sufficient. Essenbourne submits that, at least until the issue of Bonus Units, there is not a sufficient connexion with the brothers’ employment. It seems to me that the substantial link at this point is as between the payment and the deduction sought by Essenbourne. It is not necessary for me to further consider the point for, in my view, the payment by Essenbourne to the trustee does not qualify as a fringe benefit as it is defined.’*

32

In *Walstern*, Hill J said at [87], [88]:

*‘[87] As I have already noted, I would, as a matter of comity, follow the decision of Kiefel J in Essenbourne unless the case was either distinguishable or I was of the view that the decision was clearly wrong. On this point the case is not distinguishable. Further, far from being of the view that her Honour was clearly wrong, I am of the view that her Honour was clearly right. The definition of ‘fringe benefit’ in s 136(1) of the FBT Act makes clear the importance of identification of the employee. The benefit itself is one which is said to be “in relation to an employee”. The benefit is required to have been provided to the employee (or associate of the employee) and is required to be in respect of the employment of the employee. The definition of ‘property fringe benefit’, (if that is the kind of benefit relied upon) requires relevantly provision of property to a particular person there referred to as ‘the recipient’. The valuation formula relevantly here requires that there be a benefit provided ‘to a person’ in respect of the employment of an employee. Any contribution made by an individual employee is taken into account in determining the taxable value of the benefit. Although not relevant in the present case, the exclusion of a benefit otherwise deductible to an employee contemplates taking into account the specific circumstances of the employee himself or herself.*

*[88] It is not surprising that the legislation requires a link between the benefit and a particular employee (or associate of a particular employee) because historically the purpose of the Fringe Benefits Tax Act is to provide a specific means of taxing benefits which are a substitute for income to an employee and in respect of which the provisions of the 1936 Act and particular s 26(e) were thought to be defective. Income tax is a tax upon the taxable income of a particular employee. While fringe benefits tax is a tax for which a employer is made liable and is payable at the maximum personal income tax rate, the theory of fringe benefits tax legislation is that it operates as a final withholding tax payable by the employer on amounts that essentially are or would be income of the employee: see Kumagai Gumi Co Ltd v Federal Commissioner of Taxation (1999) 90 FCR 274 and National Australia Bank Ltd v Federal Commissioner of Taxation (1993) 46 FCR 252 at 262 per Ryan J.’*

33

Before this Court, the Commissioner put his textual argument in the following way:

*“‘An employee’ need not be identifiable with any greater particularity than as a past, present or future employee, being the defined meaning of “employee” for the purposes of the [FBTAA]: Subs 136(1). The primary and natural significance of “an employee” does not require any greater particularity than as a past, present or future employee. The words themselves comprehend a single employee or a group or class of employees, past, present or future: See s 23 of the Acts Interpretation Act 1901. It is apparent from the syntax of the definition [of “fringe benefit”] that the reference to “the employee” is a reference to “an employee” in the opening*

*words – “‘fringe benefit’ in relation to an employee ...”. The definition prescribes the meaning of “fringe benefit” “in relation to **an** employee”. It is not defined in relation to “**the** employee”. In other words, the definition requires that a person in respect of whom the benefit is provided answers the description of “an employee”, but the language used does not require identification of any particular employee.’*

34           The respondent submitted that as all references to ‘employee’ (other than the first) in the definition of ‘fringe benefit’ use the definite article, this clearly indicates that to be a ‘fringe benefit’ it must be in respect of the employment of a particular employee (or employees).

### REASONING ON PRIMARY ISSUE

35           Even if these textual arguments over the use of the definite article as opposed to the indefinite article and vice versa were the only signposts as to the degree of particularity with which an employee had to be identified for the purposes of the definition of ‘fringe benefit’, I would incline to the views of Kiefel J in *Essenbourne* and Hill J in *Walstern* that the references to ‘the employee’ throughout the definition are references to a particular employee who has been identified as ‘an employee’ of the employer in terms of the opening words of the definition. Once identified as an employee of the employer by reference to the opening words of the definition, the terms of the definition which follow are to be applied by reference to the particular employee so identified. The same process follows with respect to the term ‘year of tax’ in the definition. Once a year of tax is identified by reference to the opening words of the definition, the subsequent references to ‘the year of tax’ throughout the definition are references to the particular year of tax so identified and the terms of the definition which follow are to be applied accordingly.

36           However, there is at least one other reason which impels one to this view, apart from those referred to by Hill J in *Walstern*. A benefit may only be a ‘fringe benefit’ if it is provided by one of four possible ‘providers’ to one of two possible ‘recipients’ – the employee or an ‘associate’ of the employee. Even then, the benefit will only be a fringe benefit if it is in respect of the employment of an employee. If the benefit is provided direct to an employee, the identity of the particular employee will be known. On the other hand, if the benefit is provided to a person other than the employee, in many, if not all, cases it will not be possible to determine whether that person is an associate of the employee in respect of

whose employment the benefit is said to be provided, without knowing the identity of the relevant employee. For example, where the recipient is a natural person, it will not be possible to conclude whether or not the recipient is an ‘associate’ of the employee, by reason of being a ‘relative’, without knowing the identity of the relevant employee. This strongly suggests, in my view, that the reference to ‘the employee’ in the definition of ‘fringe benefit’ is a reference to a particular employee.

37           This does not mean, as seems to be suggested in [9] – [14] of the Commissioner’s written submissions, that a benefit provided to a number of employees or a benefit provided to a common associate of a number of employees – such as the trustee of a trust under which those employees are capable of taking a share of the benefit – cannot be a ‘fringe benefit’. It will be a fringe benefit provided the identity of each of the employees who will take a share of the benefit is known with sufficient particularity, at the time the benefit is provided, to enable it to be said that the benefit is provided in respect of the employment of each of those employees.

38           However, where, as here, the identity of those employees capable of taking the benefit who will in fact take the benefit, is not known at the ‘provision time’, as wide as the phrase ‘in respect of the employment’ is – see the discussion in *J & G Knowles v Commissioner of Taxation* (2000) 96 FCR 402 at [22] – [29] and the analysis of the reasons for judgment of the various members of the High Court in *Smith v Commissioner of Taxation* (1987) 164 CLR 513 demonstrating that equal minds can come to different conclusions on such an issue – if the reference to ‘the employee’ throughout the definition is to a particular employee, as I think it is, I am unable to conclude that the benefit here provided by ABC Public to the trustee of the CSP is a ‘fringe benefit’; at the ‘provision time’ the benefit is not provided in respect of the employment of any particular employee or all of the employees capable of benefiting taken as a whole, only some of them, and they are not known. The provisions of subs 148(1) of the FBTAA take the matter no further.

39           This conclusion is consistent with my view that one cannot discern any legislative policy on the part of the Government of the day to accelerate and bring to charge (by a tax (fringe benefits tax) on the employer) a benefit which the employee may never get as against a policy of deferring tax on the benefit unless and until it comes home to the employee, when

it will be taxed in their hands as assessable income. And that is precisely the way in which the Commissioner ruled on question 5 of the ruling application, namely: 'The market value of the ABC Public shares is to be included in the assessable income of a Beneficiary at the time the shares are appointed to that Beneficiary'.

## **PARS (E) AND (EA)**

40 On the premise that ABC Public and the respondent (and all other rulees) are not 'associates', a premise which seems to be common ground, on the view taken of the primary issue, it is unnecessary to consider whether pars (e) or (ea), both or neither apply. For what it is worth, if I am wrong on the view I take of the primary issue, on the facts of the ruling application I am of the view that par (e) would not apply because there does not appear to be any arrangement between ABC Public and the respondent (or any other rulee) for the provision of the benefit to the trustee of the CSP; on the other hand, I incline to the view that par (ea) would apply on the basis that the respondent (or any other rulee) participates in or facilitates a scheme or plan involving the provision of the benefit and knows that it is doing so.

## **THE NOTICE OF CONTENTION**

41 The respondent filed a notice of contention giving notice that at the hearing of the appeal it would contend that in addition to the grounds relied on by the Court below, the judgment should be affirmed on the following grounds:

- '1. *The appellant, having acknowledged that the law was at the time as set out in Essenbourne Pty Ltd v. FCT, was bound by the terms of ss 14ZAF and 14ZAL of the Taxation Administration Act 1953 to express his opinion in the private ruling only on how that law applied in relation to the arrangement.*
3. *As a result, even if this Full Court now decides the law differently from that decided in Essenbourne Pty Ltd v FCT and the other cases referred to in para 4 of the Notice of Appeal (and now also Cameron Brae Pty Ltd v C of T [2006] FCA 918), the appellant, in expressly disregarding the authorities then binding him, wrongly denied to the respondent its right to receive the appellant's opinion on how that law applied to the arrangement. As a result, the private ruling should be corrected in accordance with the law that was then binding on the appellant.'*



42 Having regard to my conclusion on the primary issue, it is not necessary that I address the issues raised by these contentions. Nevertheless, they were the subject of comprehensive argument, both orally and in writing, as well as discourse with the bench, and some comment is called for.

43 At [12] above, I referred to the reasons relied on by the Commissioner for his answer to question 1. Those reasons included the following statement:

*‘The definition of ‘fringe benefit’ also refers to a benefit being provided in relation to ‘an employee’, and for reasons outlined in paragraphs 45 - 49 of TR 1999/5 the ATO considers a fringe benefit can arise notwithstanding that a benefit provided to a trust may not be provided in respect of a specific employee.*

*Whilst Kiefel J’s views in the Essenbourne case [2002] FCA 1577 about the proper interpretation of the definition of a fringe benefit in the fringe benefits tax law are contrary to the views expressed in Taxation Ruling TR 1999/5, the Commissioner has determined that as the Essenbourne case is not an appropriate vehicle to test the issue with the Full Federal Court, the views expressed in TR 1999/5 will remain the ATO position.’*

44 In written submissions, the Commissioner put his position in the following way:

- ‘7. *The Commissioner was not compelled to follow Essenbourne and the other single judge decisions when he ruled on the respondent’s ruling application or when he determined the objection against the ruling which was made.*
8. *The fact that there are single judge decisions on the meaning of the definition of “fringe benefit” does not mean that the Commissioner was bound to follow those decisions as against taxpayers who were not privy to those decisions: Business World Computers Pty Ltd v Australia Telecommunications Commission (1988) 82 ALR 499 at 504.*
9. *There is no principle of estoppel that would bind the Commissioner to apply the single judge decisions to which the respondent was not a party, in relation to the application of the FBT Act to the arrangement the subject of the respondent’s ruling request.’*

45 When challenged from the bench that a proposition such that the Commissioner does not have to obey the law as declared by the courts until he gets a decision that he likes was astonishing, the Commissioner submitted:

*‘The [Commissioner] seeks to make clear that the propositions put in paragraphs 8 and 9 were in response to the respondent’s contentions and were not put as a broader proposition that the appellant is entitled to disregard judicial decisions contrary to the rule of law in the exercise of his statutory powers. On the contrary, the [Commissioner’s] position is that by this private ruling he seeks to have the full court reconsider the first instance decisions because he is mindful of his obligations to apply the law as declared by the courts. It is only in very confined circumstances where the Commissioner would not follow a decision of a single judge of the Federal Court. He was not able to appeal from the observations in Essenbourne in view of the finding on the facts on the income tax case. In Walstern the relevant observations were obiter and there was no order against which the Commissioner could appeal. In Caelli the Court determined the FBT appeal in the Commissioner’s favour “on the assumption” of the correctness of Essenbourne and there was no order against which the Commissioner could appeal. The Commissioner has appealed the Essenbourne construction in each of the three cases in which he has been able, being Spotlight Stores (where the Full Court did not determine the issue), Cameron Brae (the appeal is yet to be heard) and this case.’*

46 In response, the respondent submits that if the Commissioner disagreed with the decision of Kiefel J on the fringe benefits tax issue, the appropriate course was for him to have appealed. In specific response to the Commissioner’s submission asserted in [45] above, that the findings of fact on the income tax case precluded an appeal, the respondent says that an examination of *Essenbourne* reveals no such findings – see in particular [33] to [36]. I am inclined to agree, particularly having regard to the terms of subs 148(1) of the FBTAA. The respondent also pointed out that the Commissioner explained his reasons for not appealing on a different basis in his Media Release of 14 March 2003:

- *The Court held that an income tax deduction was not allowable for an amount contributed by a company to an employee incentive trust because the payment was simply a distribution of the company’s profits to the three principals of the company*
- *However, the Court disagreed with the Tax Office’s view that fringe benefits tax should apply, **but given the scheme was rendered ineffective by denying deductions, the Tax Office did not appeal to the Full Federal Court.** [Emphasis added]’*

47 At the time the Commissioner issued the ruling, Hill J in *Walstern* had indicated that, in his view, Kiefel J’s construction was ‘clearly correct’ and Merkel J in *Spotlight Stores* had indicated his satisfaction that both those decisions were not clearly wrong and that he intended to follow them. In those circumstances, faced with the ruling application, in my

opinion, it was incumbent on the Commissioner, having taken the view that findings of fact precluded him from appealing *Essenbourne* – a view with which I have already expressed my disagreement – either to follow the construction embraced in those cases or seek a declaration from the Court as to the proper construction and apply that construction in the ruling.

48            Since writing these reasons, I have had the advantage of reading the reasons of Allsop J in relation to this particular matter, and wish to indicate my agreement with what his Honour has to say.

### CONCLUSION AND COSTS

49            The appeal must be dismissed. The Commissioner has agreed to pay the respondent's costs irrespective of the outcome.

I certify that the preceding forty-two (42) numbered paragraphs are a true copy of the Reasons for Judgment herein of the Honourable Justice Edmonds.

Associate:

Dated:      22 February 2007

Counsel for the Appellants:      Mr G T Pagone QC, Ms J Davies SC and Ms M Brennan

Solicitor for the Appellants:      Australian Government Solicitor

Counsel for the Respondents:      Mr D Russell QC and Mr B Jones

Solicitor for the Respondents:      Freehills

Date of Hearing:                      6 November 2006

Date of Judgment:                  22 February 2007