

**LEGAL PROFESSION ADMISSION BOARD**

**SEPTEMBER 2009**

**TAXATION AND REVENUE LAW**

**Time: Three Hours**

This paper consists of **six** questions.

Candidates are required to attempt any **four** questions.

All questions are of equal value.

If a candidate answers more than the specified number of questions, only the first **four** questions attempted will be marked.

All questions may be answered in one examination booklet.

Each page of each answer must be numbered with the appropriate question number.

Candidates must indicate which questions they have answered on the front cover of the first examination booklet.

Candidates must write their answers clearly. Lack of legibility may lead to a delay in the candidate's results being given.

**Permitted Materials:**

**This is an open book exam. Candidates may refer to any books and any printed or handwritten material they have brought into the examination room.**

**As some instances of cheating and of bringing unauthorised material into the examination room have come to the attention of the Admission Board, candidates are warned that such conduct will result in instant expulsion from the examination and may result in exclusion from all further examinations.**

*This examination should not be relied on as a guide to the form or content of future examinations in this subject.*

## Question 1

### Part A

Consider the following scenarios:

- (i) child minding expenses paid by a single father (his wife is deceased) in respect of his child in order that he is able to go to work and earn a living;
- (ii) contributions made by a company to a fund established by the Federal Government in order to compensate former employees of the company, and members of the public, who have contracted serious illnesses as a consequence of being exposed to toxic substances manufactured and sold by the company;
- (iii) money paid to celebrities to ensure that they will appear on quiz shows;
- (iv) gold medals won at the Olympic Games by Australian athletes;
- (v) the costs of printing, mailing, radio and newspaper advertisements incurred by a company (at the instigation of the current management team) of lobbying shareholders not to sell their shares to a rival bidder;
- (vi) travelling expenses incurred by an installer of television antennas in travelling from home to install television antennas for customers.
- (vii) the purchase by a company of a machine for \$100,000 for mining operations on 1 July 2008 which due to continuous use in the mine will only have an effective life of 6 months;
- (viii) the payment of interest by a company on money borrowed from a bank to pay income tax and dividends.

**For each of the above scenarios advise the relevant entity as to the taxation implications.**

**(15 marks)**

### Part B

**What were the facts and issues decided by the High Court in *Tennant v Smith* [1892] AC 150 and *FCT v Cooke and Sherden* (1980) 80 ATC 4140. If the facts in those cases were to arise today what would be the tax implications?**

**(10 marks)**

**(Question 2 follows)**

## Question 2

### Part A

James Regent (“James”) was a backpacker from the United Kingdom who was holidaying in the Blue Mountains. Late one evening he went for a bush walk and became lost in the bush.

He managed to survive 15 days in the bush before he struggled onto a road and was picked up by passers-by. In the interim the police, with assistance from members of the Blue Mountains Volunteer Rescue Services Limited (“BMVRS”), had mounted a search for him that had cost a significant amount of money.

There was a lot of public interest surrounding the search. When James was found he was approached by a publicity agent who wanted to act on his behalf to sell his story to the press. The publicity agent was engaged by James to sell his story.

James’ father initially said that any money paid to his son from the sale of his story would be given to the BMVRS. The BMVRS is a body that organises searches by its members for persons missing in the Blue Mountains.

The agent managed to sell James’ story to Channel 8 for \$150,000. The contract was entered into in Sydney and the interview took place at the studios of Channel 8 in Sydney.

James gave \$100,000 from the sale of his story to the BMVS. He kept \$20,000 for himself and applied the remaining \$30,000 as follows: \$5,000 was applied in reimbursing himself for his expenses in flying to Australia for his holiday, \$5,000 was applied in reimbursing his father for the cost of flying to Australia to assist in the search for James and \$20,000 was paid to his publicity agent.

**Advise James as to the tax implications to him in respect of the above arrangements. Would it make any difference to your answer if James entered into the contract to sell his story in the United Kingdom, and undertook the interview in the United Kingdom?**

**(15 marks)**

### Part B

**Explain by reference to the relevant statutory provisions and case law whether “initial” repairs (i.e. repairs to defects existing at the time an item is purchased by a taxpayer) are deductible.**

**(10 marks)**

**(Question 3 follows)**

### Question 3

#### Part A

At 1 July 2008, Garden Supplies Pty Ltd ("Garden") had opening trading stock of \$150,000. During the year of income it made the following purchases of trading stock:

Month	Amount(\$)
July	100,000
November	500,000
March	400,000
June	500,000
Total	1,500,000

As at 30 June 2009 the amount of \$200,000 was owing to creditors for the supply of the trading stock that had been purchased during the year of income.

On 30 June 2009 Garden undertakes a stock take that reveals the following stock on hand at the end of the income year:

Stock	Quantity	Cost Price	Market selling price	Replacement price
Ladders	5,000	4	3	2
Spades	4,000	2	6	4
Shovels	6,000	9	5	7
Picks	4,000	6	8	3

**Advise Garden as to the following:**

- (a) the deductibility of the purchases of trading stock;**
- (b) the manner of valuing trading stock to minimise taxable income (doing the calculation and referring to relevant provisions of the tax legislation); and**

**(Question 3 Part A continues)**

**(Question 3 Part A continued)**

- (c) the manner of valuing trading stock to maximise taxable income (doing the calculation and referring to relevant provisions of the tax legislation). Give at least one example as to when a taxpayer might seek to maximise its taxable income.**

**(15 marks)**

**Part B**

**Explain the background leading to the inclusion of the definition of “royalties” and section 6C in the tax legislation, and the rationale for section 15-20 requiring the definition of “royalties” to be disregarded in its application.**

**(10 marks)**

**Question 4**

**Part A**

Beta Pty Limited (“Beta”) maintains a franking account so as to enable it to determine its ability to pay franked dividends. For the year ended 30 June 2009 the following events took place:

- (i) Beta receives a dividend of \$7,000 from another company that is fully franked;
- (ii) Beta receives a dividend of \$14,000 from another company that is franked to 50%;
- (iii) Beta pays a tax instalment to the Australian Taxation Office of \$3,000;
- (iv) Beta pays a dividend of \$420 to Jack (the only shareholder in the company) which is franked to 25%;
- (v) Beta is unsuccessful in a dispute with the Taxation Office and is required to pay the balance of tax owing being \$21,000 to the Taxation Office;
- (vi) After the lodgement of the tax return the company receives a notice of assessment requiring it to pay further tax of \$7,000.

**Advise Beta as to the effect (if any) on its franking account in respect of the above events. Also advise Jack of the tax consequences to him of being paid a dividend of \$420 franked to 25%. (You may assume a company tax rate of 30% and an individual tax rate of 50%.)**

**(15 marks)**

**(Question 4 Part B follows)**

## **Part B**

**Detail the facts and issues decided by the High Court in *BP Petroleum v FCT* (1965) 112 CLR 386.**

**(10 marks)**

### **Question 5**

#### **Part A**

On 1 July 2008 Robert Richards settles an amount of \$20 on a trustee in favour of his wife Deidre and his two children. The children were Lucy aged 20 and Andrew aged 14. The trust deed provided that the income was to be applied as to one third to his wife Deidre during her life, and the remaining two thirds to be held at the discretion of the trustees until the children attained the age of 25 years. During this period the trustee had the discretion to make payments to Robert Richards for the children's maintenance, education and advancement.

Any unspent income was to be accumulated for the children in equal shares and should either of them die before attaining the age of 25 years, the accumulated income is to be held on behalf of his or her estate.

During the year of income ended 30 June 2009 the income of the trust estate consisted of interest (\$10,000) and unfranked dividends (\$20,000).

In accordance with the trust deed the trustee paid \$10,000 to Deidre, \$5,000 was applied to assist Lucy in paying her university fees and \$5,000 was applied to paying the school fees of Andrew.

**Advise the trustee, Robert Richards, Deidre, Lucy and Andrew as to the tax implications for the trust in respect of the year of income ended 30 June 2009.**

**(15 marks)**

#### **Part B**

**What are the relevant factors to be taken into account in deciding whether to appeal an objection decision to the Administrative Appeals Tribunal ("the Tribunal") or the Federal Court?**

**If the taxpayer was objecting against an amended assessment pursuant to which the Commissioner had included an amount in his assessable income under section 109 would you recommend the taxpayer appeal the objection decision to the Tribunal or Federal Court, and give reasons for your recommendation to the taxpayer.**

**(10 marks)**

**(Question 6 follows)**

## **Question 6**

### **Part A**

On 31 December 2007 Alpha Pty Limited purchased a machine for use in its factory for \$100,000. The machine had an effective life of 4 years for income tax purposes and the company claims the capital allowance using the diminishing value method. The machine is sold on 30 June 2009.

**Explain the tax consequences (including any capital gains tax consequences) of the sale where the sale price is alternatively:**

- (a) \$20,000;**
- (b) \$50,000; and**
- (c) \$105,000.**

**(15 marks)**

### **Part B**

Geoff is a member of an exclusive tennis club with annual membership fees of \$5,000. The membership fees are not tax deductible. In order to raise funds for the building of new facilities the club has offered a “free” annual membership to persons who lend the club \$50,000 on interest free terms.

If Geoff had kept the \$50,000 in his bank he would have earned \$5,000 interest but, after tax at the rate of (say) 50% he would only have received \$2,500. Accordingly Geoff considers the proposal quite advantageous from his point of view and decides to loan the tennis club \$50,000 interest free for a year.

**Advise Geoff of the tax implications including the potential application of Part IVA (the general anti-avoidance provisions) to the above arrangement.**

**(10 marks)**

**END OF PAPER**