Edited version of your private ruling

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Ruling

Subject: CGT and the deductibility and timing of 'gifts'

Question 1

Will a donation made by the Taxpayer pursuant to the x (the **Commitment**) be treated as a 'gift' for the purposes of deductibility under section 30-15 of ITAA 1997?

Answer

Yes.

Question 2

To the extent a deduction is available under section 30-15 of ITAA 1997 for the donation of shares or payment of a cash equivalent amount pursuant to the Commitment, will the Taxpayer's tax deduction only become available upon transfer of the shares or payment of a cash-equivalent amount?

Answer

Yes.

Question 3

Will execution of the Commitment trigger CGT Event A1 (disposal of an asset) pursuant to section 104-10 of ITAA 1997?

Answer

No.

Question 4

Will execution of the Commitment trigger CGT Event D1 (creation of contractual or other right) pursuant to section 104-35 of ITAA 1997?

Answer

No.

This ruling applies for the following periods:

The income years ending 30 June 2021 through to 30 June 2033.

The scheme commences on:

1 July 2020.

Relevant facts and circumstances

This ruling is based on the facts stated in the description of the scheme that is set out below. If your circumstances are materially different from these facts, this ruling has no effect and you cannot rely on it. The fact sheet has more information about relying on your private ruling.

Background

The Commitment

- Under the Commitment, the Taxpayer commits to the gifting of shares or cash-equivalent to one or more nominated Australian charitable organisations that is approved by the ATO as a 'deductible gift recipient' (the **Default Charitable Recipients**).

- The donation may either be made as shares of cash-equivalent (**Gift**).

- The Gift may be made by the Taxpayer at any time, but must be made to the Default Charitable Recipient(s) at the time the Nominated Entity undergoes a 'Liquidity Event' as defined in the Commitment, such as a x or x.

- The Taxpayer receives no consideration for entering the Commitment, or for making the Gift.

- The entity or entities nominated under the Commitment throughout the validity period of the Commitment, and up until a Liquidity Event, are the Default Charitable Recipient/s, however the Taxpayer, at their sole discretion, can change the nominated Australian charitable organisation(s) under the Commitment at any time. Australian charitable organisations which may become recipients if nominated under the Commitment are referred to as Potential Charitable Recipients.

- The Taxpayer must make the Gift to one or more Australian charitable organisations (which may or may not include the named Default Charitable Recipient at the time of execution of the Commitment) in proportions as the Taxpayer sees fit. If the Taxpayer does not nominate one or more Australian charitable organisations and the proportions, the donation must be made to the Default Charitable Recipient.

- The commitment to Gift under the x is intended to last for a period of x years following execution. In the event a Liquidity Event has not occurred within x years of execution, but there are reasonable prospects of a Liquidity Event occurring in the next x years, the Commitment may be extended for a further x years.

- In the event the Commitment is not triggered after the end of x years, or after the end of x years if the extension mentioned above is applied, the Commitment is terminated and the obligation to donate the Gift under the Commitment ceases.

Rights under the Commitment

- The ATO has been advised by an authorised representative of the Taxpayer that:

  – The commitment to donate under the Commitment is a legally binding and enforceable promise.

  – The Taxpayer does not have the ability to unilaterally revoke or terminate the Commitment at any point before a Liquidity occurs, however the nominated Default Charitable Recipient holds no enforceable right against the Taxpayer to make the gift under the terms of the Commitment until a Liquidity event occurs, at which point they may or may not be the named Default Charitable Recipient.

  – The Default Charitable Recipient(s) named at the time of a Liquidity Event can then take legal action against the Donating Shareholder to enforce the voluntary choice of the Taxpayer if needed at or after the time of a Liquidity Event.

  – The only legally enforceable rights of the nominated Default Charitable Recipient under the Commitment prior to the Taxpayer being obliged to make the donation are the rights to notification of being a Default Charitable Recipient and information as set out in the Commitment.

The Taxpayer

- x

- The key terms of the Commitment are as follows:
  – The Taxpayer
  – *Donor*
  – *Nominated Entity*
  – *Gift*
  – *Default Charitable Recipient*
  – *Timing* – Upon a Liquidity Event (as defined in the Commitment) occurring within x years of execution of the Commitment. If no Liquidity Event has occurred within x years and there is a reasonable prospect that a Liquidity Event may occur within the subsequent x years, the Commitment may be extended a further x years. In the event no Liquidity Event has occurred after x years (as the case may be), the obligation to donate the Gift ceases. Notwithstanding the above, the Gift may be donated by the Taxpayer at their sole discretion at any time throughout the above period.

- x is the Taxpayer making the Gift under the Commitment, where the nominated entity exercises its discretion to make a distribution to the Taxpayer prior to, or at the time, the obligation to donate arises.

- The Default Charitable Recipient is not party to the Commitment, nor will it be making the relevant donation nor seeking a corresponding deduction.

Relevant legislative provisions
Income Tax Assessment Act 1997 Section 30-15.
Income Tax Assessment Act 1997 Section 104-10.
Income Tax Assessment Act 1997 Section 104-35.

Reasons for decision

These reasons for decision accompany the *Notice of private ruling* for the Taxpayer.

While these reasons are not part of the private ruling, we provide them to help you to understand how we reached our decision.

Question 1
Will a donation made by the Taxpayer pursuant to the Commitment (either as a donation of shares or cash-equivalent) be treated as a 'gift' for the purposes of deductibility under section 30-15 of ITAA 1997?

Summary
Yes, the donation will be treated as a gift for the purposes of deductibility under section 30-15 at the time the gift is actually made.

Detailed reasoning
There is a distinction between expressing a commitment to make a donation by entering the Commitment, and the Donation itself. The deduction is not available when the Commitment occurs (i.e. when the Commitment is entered), but rather when the Commitment is implemented, and the Donation is made (e.g. money or property is transferred to the Default Charitable Recipient).

1. General principles

Section 30-15 provides that you can deduct a gift or contribution (or the value thereof) that you make in certain situations set out in that section.

Relevantly, section 30-15 provides that a gift or contribution may include the voluntary transfer of 'money or property' (i.e. something must pass to the recipient, such as ownership of a share in the company (see e.g. paragraph 83, Taxation Ruling (**TR**) 2005/13)), from the Donating Shareholder to the Default Charitable Recipient, and must not be to extinguish some other obligation.

TR 2005/13 outlines the Commissioner's view on what a gift is for the purposes of the gift deduction provisions (Division 30 of the *Income Tax Assessment Act 1997* (**ITAA 1997**)). It outlines principles relevant to the factual determination of whether certain transfers of money or property constitute a gift.

2. To extinguish some other obligation – voluntary?

In particular, to be a gift, the Donation must be a voluntary payment. The making of a "gift" will not be a voluntary payment where '... it has the effect of discharging or reducing a contractual obligation owed by the giver to the [recipient]'. This typically captures a pre-existing obligation to provide the Default Charitable Recipient services, such that a subsequent 'donation' may be to extinguish that obligation and is therefore not a gift – see e.g. paragraph 105 TR 2005/13.

In determining this, it is important to note that the Commitment is not an agreement between two parties, as the action of executing the Commitment is a unilateral decision by the Taxpayer to commit to making the Gift. It is binding on the person entering into the Commitment, although the Default Charitable Recipient has no rights to enforce under the Commitment aside from notification and information, until such time that a Liquidity Event occurs.

The Taxpayer intends to commit to the transfer of shares (which may be distributed to him at the discretion of the Nominated Entity) to a valid recipient under the commitment, or otherwise a donation of a cash equivalent amount.

As was stated by Lord Denning in *Vincent v Premo Enterprises (Voucher Sales) Ltd* [1969] 2 All ER 9:

> *A deed is binding on the maker of it, even though the parts have not been exchanged, as long as it has been signed, sealed and delivered. 'Delivery' in this connection does not mean 'handed over' to the other side. It means delivered in the old legal sense, namely, an act done so as to evince an intention to be bound. Even though the deed remains in the possession of the maker, or of his solicitor, he is bound by it if he has done some act evincing an intention to be bound, as by saying: 'I deliver this my act and deed.*

Importantly, whether a Donation is considered a discharge of an obligation determines whether the payment is 'voluntary' (and in turn, whether it is a 'gift'). Put another way, the Donation will not be considered voluntarily made (and therefore not a gift) if it has the effect of discharging another obligation.

The obligation created under the Commitment in this case is merely the voluntary choice to donate to a Default Charitable Recipient of the Taxpayer's choosing, the timing and means of which are determined by the Commitment. There is no other separate obligation for which that Donation extinguishes. Since the execution of the Commitment was a voluntary choice to donate, it follows that the Donation it makes once the Commitment is implemented, is also voluntary.

There are no prior contractual relations or outstanding obligations between the Taxpayer and Deductible Gift Recipient (or any Potential Charitable Recipients). As such, the making of any donation by the Taxpayer would not constitute the discharge of a contractual obligation

Question 2

To the extent a deduction is available under section 30-15 of ITAA 1997 for the donation of shares or cash-equivalent, pursuant to the Commitment, will the Taxpayer's tax deduction only become available upon transfer of the shares or cash-equivalent amount?

Summary

Yes, the tax deduction only become available upon transfer of the shares or payment of the cash-equivalent amount.

Detailed reasoning

The Donation should be a gift that becomes deductible to the Donor under section 30-15 when it is *made* (subject to special conditions outlined in Division 30 of ITAA 1997).

The deduction is not available at the time when the Commitment is entered, but rather, when the Commitment to donate is acted upon and actually 'made' by the Taxpayer (subject to special conditions outlined in Division 30 of the ITAA 1997).

Relevantly, TR 2005/13 at paragraph 104 provides as Example 27:

> *W voluntarily enters into a deed of gift to transfer five yearly instalments of $2,000 to be paid to a DGR on 30 June each year. Despite having the obligation to make the five $2,000 instalments, they are gifts when paid to the DGR. The decision to enter into the deed of gift was voluntary, and no consideration was received by W in respect of the transfer.*

Whilst this example is not strictly on ‘all fours’ with the proposed Commitment, it suggests that a transfer of cash to a Default Charitable Recipient implemented by a Deed, is deductible when that transfer is *made*.

It emphasises that the choice to enter a deed is voluntary, and therefore the transfer of Gift is also a voluntary choice.

Question 3
Will execution of the Commitment trigger CGT Event A1 (disposal of an asset) pursuant to section 104-10 of ITAA 1997?

Summary
No, execution of the Commitment will not trigger CGT Event A1.

Detailed reasoning
Subsection 104-10(1) of the ITAA 1997 states that a CGT even A1 happens when a taxpayer disposes of a CGT asset. A disposal occurs either when you enter the contract for disposal of an asset, or if there is no contract, when the change of ownership from the Taxpayer to another entity occurs. A capital gain or loss may be made if the capital proceeds from the disposal of a CGT asset are more or less than the cost base of the asset.

In this case the Taxpayer will be executing a Commitment which is not an agreement nor contract. It is a unilateral action representing a Commitment. On executing the Commitment, the Taxpayer is not disposing of any CGT asset, as no change of ownership occurs. This may occur at some time in the future, if a Liquidity Event occurs.

Question 4
Will execution of the Commitment trigger CGT Event D1 (creation of contractual or other right) pursuant to section 104-35 of ITAA 1997?

Summary
No, execution of the Commitment will not trigger CGT Event D1.

Detailed reasoning
CGT event D1 (section 104-35 of the ITAA 1997) happens *‘if you create a contractual right or other legal or equitable right in another entity’*. The event happens when the contract is entered into or the other right created. A legal or equitable right is a CGT asset under paragraph108-5(1)(b) of the ITAA 1997.

You will make a capital gain if the capital proceeds from creating the right are more than the incidental costs you incurred that relate to the event. You will make a capital loss if those capital proceeds are less than those costs.

In the Taxpayer’s case, the only rights created in the nominated Default Charitable Recipient under the Commitment prior to the Taxpayer being obliged to make the donation at the time of a Liquidity Event are the rights to notification of being a Default Charitable Recipient and information as set out in the Commitment.

There is no certainty in respect of the identity of ‘another entity’ with which a right to a donation might subsist. The Taxpayer has sole discretion to nominate additional recipients or change the Default Charitable Recipient to an Australian charitable organisation of his choice. Until such time as a Liquidity Event occurs, the named Default Charitable Recipient or any Potential Charitable Recipient (whomever is named at the time of the Liquidity Event) holds no enforceable right against the Taxpayer to make the Gift under the terms of the Commitment.

Any expectancy of a donation later on is therefore contingent on a Liquidity Event occurring, and the donor not changing the nominated Default Charitable Recipient.

Not all things often referred to as 'rights' will be assets for CGT purposes. To be an asset, a right must be recognised and protected by law.

The explanatory memorandum to the *Taxation Laws Amendment Bill (No.4) 1992* confirms that:

> *Not all things often referred to as “rights” will be assets for CGT purposes. To be an asset, a right must be* ***recognised and protected by law - a court of law or equity will assist in enforcing it****. Personal liberties and freedoms, such as the freedom to work or trade or to play amateur sport, are not legal or equitable rights and accordingly will not be assets for CGT purposes.*

The Commissioner considers that in your circumstances the right to shares or cash-equivalent amount are not legal or equitable rights which a court of law would enforce at the time the Commitment is entered. For this reason the better view is that there are no ‘rights’ which satisfy the definition of a CGT asset (legal or equitable right that is not property), such that the execution of that Commitment would not trigger CGT Event D1 at that time pursuant to section 104-35 of the ITAA 1997.

In the alternative, if CGT event D1 were to apply at the time the Commitment is executed, there are no capital proceeds received in relation to entering the Commitment since it is a voluntary choice to donate, such that practically there would be no CGT consequences.

Where there are no capital proceeds in respect of a CGT event, section 116-30(1) ITAA 1997 applies to modify the amount taken to have been received. Section 116-30(1) states that *‘If you received no capital proceeds from a CGT event, you are taken to have received the market value of the CGT asset that is the subject of the event. (The market value is worked out as at the time of the event.)’*

However, section 116-30(3) of the ITAA 1997 specifically excludes the market value substitution rule applying where CGT event D1 occurs. Therefore, in the event CGT event D1 is taken to have occurred upon execution of the Commitment, the Taxpayer should have no capital gain.