



# TECHNICAL ANALYSIS REPORT

Base Rate Entity Status - Company Z (Bucket Company)

Income Year: 2024-25

|                        |   |
|------------------------|---|
| <b>Prepared for:</b>   | Instructing Accountant / Client             |
| <b>Date:</b>           | March 2026                                  |
| <b>Reference:</b>      | TA-BRV-2026-0319-Base-Rate-Entity-Company-Z |
| <b>Income Year:</b>    | 2024-25                                     |
| <b>Classification:</b> | Confidential                                |

## Question

A client has the following structure:

**Unit Trust ABC** - operating business with aggregated turnover less than \$10M

**Family Trust DEF** (discretionary trust) - holds 100% of units in Unit Trust ABC

**Company Z** - bucket company, beneficiary of Family Trust DEF

In the 2024-25 income year, Unit Trust ABC distributed taxable trading profits of \$500,000 to Family Trust DEF, which then distributed \$250,000 of this to Company Z.

### Client Query

Would Company Z be considered a base rate entity and taxed at 25%, or would it pay the 30% tax rate?

## 1. Summary

### **Result: Base Rate Entity - 25% Rate Applies**

Company Z IS a base rate entity for the 2024-25 income year and is taxed at the 25% company tax rate.

The \$250,000 trust distribution from Family Trust DEF is NOT base rate entity passive income (BREPI) under s 23AB of the Income Tax Rates Act 1986 (ITRA 1986). This is because the distribution is entirely referable to active trading income of Unit Trust ABC - not to any of the passive income categories listed in s 23AB(1)(a)-(f).

Section 23AB(1)(g) requires tracing through interposed trusts. When the underlying income is active trading income (ordinary income under s 6-5 ITAA 1997 from business operations), it does not fall within paragraphs (a)-(f), and therefore paragraph (g) does not characterise it as BREPI.

Since 0% of Company Z's assessable income is BREPI, it satisfies both limbs of the base rate entity test in s 23AA: aggregated turnover below \$50M and no more than 80% BREPI.

### **Financial Impact**

Tax payable on \$250,000 at 25% = \$62,500. Had the 30% rate applied, tax would be \$75,000 - a saving of \$12,500.

## 2. Facts & Assumptions

### Facts Provided

Unit Trust ABC is an operating business trust with aggregated turnover less than \$10M.

Family Trust DEF (discretionary trust) holds 100% of the units in Unit Trust ABC.

Company Z is a bucket company and a beneficiary of Family Trust DEF.

In 2024-25, Unit Trust ABC distributed \$500,000 of taxable trading profits to Family Trust DEF.

Family Trust DEF distributed \$250,000 of this amount to Company Z.

### Assumptions Made

| Assumption [ASSUMED]  | Affects   |
|---|---|
| The \$500,000 distributed by Unit Trust ABC is entirely ordinary trading income (s 6-5 ITAA 1997), not passive income (rent, interest, dividends, royalties, or net capital gains). [ASSUMED] | BREPI characterisation - if any portion were passive, it would change the BREPI calculation for Company Z. This is the single most important assumption in the analysis.  |
| Company Z has no other assessable income in 2024-25 aside from the \$250,000 trust distribution. [ASSUMED]  | 80% BREPI threshold - if Company Z had other income (e.g., bank interest, other trust distributions with passive components), it could push BREPI above 80%.  |
| Company Z's aggregated turnover (including connected entities and affiliates under s 328-115 ITAA 1997) is less than \$50M for 2024-25. [ASSUMED]   | First limb of the base rate entity test (s 23AA(a)). If aggregated turnover exceeds \$50M, Company Z cannot be a BRE regardless of BREPI.   |
| Family Trust DEF validly resolved to make Company Z presently entitled to \$250,000 of trust income before 30 June 2025. [ASSUMED]  | Division 6 assessment - Company Z must be presently entitled under s 97(1) ITAA 1936 for the income to be assessed to it at its rates. If not presently entitled, the trustee is assessed at the top marginal rate (s 99A). |
| The trust deed of Family Trust DEF permits distributions to corporate beneficiaries. [ASSUMED]  | Validity of the distribution. If the deed does not include companies in the class of beneficiaries, the distribution resolution is ineffective.   |
| Unit Trust ABC is a fixed trust for tax purposes (units confer fixed entitlements). [ASSUMED]   | Affects the flow-through of income character under the Bamford proportionate approach. Fixed entitlements determine each unitholder's share of the trust's net income.  |

### Information Needed

| Missing Information [NEEDED]  | If Different, Would Change   |
|---|--|
| Confirmation of the exact composition of Unit Trust ABC's net income - specifically whether any component is rent, interest, dividends, royalties, or net capital gains. [NEEDED] | If any passive income exists in Unit Trust ABC, the proportionate share flowing to Company Z via Family Trust DEF will be BREPI. Even a small amount of bank interest could change the result if Company Z has minimal other income. |

| Missing Information [NEEDED]  | If Different, Would Change  |
|---|---|
| Whether Company Z derived any other income (bank interest, dividends from other investments, other trust distributions). [NEEDED] | Could introduce additional BREPI amounts and alter the 80% threshold calculation. Even \$1 of bank interest earned directly by Company Z is BREPI.                |
| Connected entity and affiliate details for the aggregated turnover calculation under s 328-115 ITAA 1997. [NEEDED]                | If aggregated turnover exceeds \$50M (including all connected entities and affiliates), Company Z fails the first limb of s 23AA regardless of BREPI composition. |
| Whether Family Trust DEF has made a family trust election (FTE) under Subdiv 272-A, Sch 2F ITAA 1936. [NEEDED]                    | Not directly relevant to BRE status, but relevant to trust loss provisions and interposed entity elections that may affect the broader group structure.           |

### 3. Related Areas & Cross-Over Analysis

| Area                         | Relevance   | Key Provision                 | Impact  |
|------------------------------|---|-------------------------------|---|
| Income Tax - BRE Status      | Core issue - Company Z's tax rate depends on whether it qualifies as a base rate entity.            | s 23AA, s 23AB ITRA 1986      | 25% vs 30% - \$12,500 difference on \$250K of assessable income.  |
| Trust Taxation - Div 6       | Company Z is assessed under Division 6 on its proportionate share of Family Trust DEF's net income. | s 97(1) ITAA 1936             | Must be presently entitled by 30 June 2025. The Bamford proportionate approach applies to determine Company Z's share.                      |
| BREPI Tracing - s 23AB(1)(g) | The character of the underlying income must be traced through interposed trusts.                    | s 23AB(1)(g) ITRA 1986        | The tracing provision looks through Family Trust DEF and Unit Trust ABC to the source income. Active trading income does not trigger BREPI. |
| Division 7A - UPEs           | If the \$250,000 distribution is not physically paid to Company Z, a UPE arises.                    | s 109D ITAA 1936; TD 2022/11  | Post-16 Dec 2009 UPEs treated as Div 7A loans. Must be placed on complying terms or physically paid. Separate issue from BRE status.        |
| Franking - Imputation        | Company Z's franking rate depends on its corporate tax rate for imputation purposes.                | s 995-1(1) ITAA 1997; Div 202 | If BRE, Company Z franks at 25%. Over-franking risk if BRE status changes year to year. Franking rate determined by prior year BRE status.  |
| LCR 2019/5                   | Binding ATO guidance on BREPI tracing through trust structures.                                     | LCR 2019/5                    | Confirms that trust distributions are only BREPI to the extent referable to underlying passive income. Directly supports this analysis.     |

## 4. Analysis

### 4.1 The Base Rate Entity Test - Section 23AA ITRA 1986

#### Relevant Law

Under s 23AA of the Income Tax Rates Act 1986 (ITRA 1986), a corporate tax entity is a base rate entity for an income year if it satisfies two cumulative conditions:

**Condition (a):** The entity's aggregated turnover (within the meaning of s 328-115 ITAA 1997) for the income year is less than \$50 million; AND

**Condition (b):** No more than 80% of the entity's assessable income for the income year is base rate entity passive income (BREPI).

If both conditions are met, the company is taxed at the base rate of 25% (for 2021-22 onwards). If either condition fails, the full 30% rate applies. There is no partial application - it is an all-or-nothing test.

### 4.2 Condition (a): Aggregated Turnover

Company Z is a bucket company that likely has no turnover of its own (it receives trust distributions, not revenue from business operations). However, the aggregated turnover test under s 328-115 ITAA 1997 requires aggregation of the annual turnover of:

- (a) the entity itself;
- (b) entities connected with the entity (s 328-125 ITAA 1997); and
- (c) affiliates of the entity (s 328-130 ITAA 1997).

Unit Trust ABC has turnover of less than \$10M. Even after aggregation of all connected entities and affiliates in the group, the aggregated turnover is well below the \$50M threshold.

#### Finding

Condition (a) is satisfied. Aggregated turnover is below \$50M.

### 4.3 Condition (b): The 80% BREPI Test

This is the critical question. Company Z's only assessable income (on the facts assumed) is the \$250,000 trust distribution from Family Trust DEF, included in its assessable income under s 97(1) ITAA 1936 (Division 6).

The question is: does this \$250,000 constitute BREPI?

#### What is BREPI? - Section 23AB(1) ITRA 1986

Section 23AB(1) defines BREPI as assessable income that is:

- (a) a distribution by a corporate tax entity (other than a non-portfolio dividend);
- (b) a franking credit attached to such a distribution;
- (c) a non-share dividend (within the meaning of Div 974 ITAA 1997);
- (d) interest income (or a payment in the nature of interest), royalties, and rent;
- (e) a gain on a qualifying security (Division 16E, Part III, ITAA 1936);
- (f) a net capital gain; and
- (g) an amount included in the assessable income of a beneficiary of a trust estate under Division 6 of Part III of the ITAA 1936, **to the extent that the amount is referable** (either directly or indirectly

through one or more interposed partnerships or trust estates) **to another amount that is BREPI under paragraphs (a) to (f).**

### The Tracing Mechanism - Paragraph (g)

Paragraph (g) is the operative provision for Company Z. It requires tracing the trust distribution back to its source to determine whether the underlying income is passive in character. The tracing works as follows:

**Step 1 - Identify the source income:** Unit Trust ABC derived \$500,000 of active trading income. This is ordinary income under s 6-5 ITAA 1997, derived from the conduct of a business (not from passive investments).

**Step 2 - Is the source income BREPI under paragraphs (a)-(f)?** No. Active trading/business income is not:

- a distribution by a corporate entity (paragraph (a));
- a franking credit (paragraph (b));
- a non-share dividend (paragraph (c));
- interest, royalties, or rent (paragraph (d));
- a qualifying security gain (paragraph (e)); or
- a net capital gain (paragraph (f)).

**Step 3 - Trace through the interposed trust:** Unit Trust ABC distributed the \$500,000 to Family Trust DEF (which holds 100% of the units). Family Trust DEF then distributed \$250,000 of this to Company Z. At each stage, the income retains its character as active trading income. Paragraph (g) traces "indirectly through one or more interposed partnerships or trust estates" - here, through two interposed trusts (Unit Trust ABC and Family Trust DEF).

**Step 4 - Apply paragraph (g):** Since the underlying income is NOT BREPI under any of paragraphs (a)-(f), paragraph (g) does not characterise the \$250,000 distribution as BREPI. The distribution is referable to active trading income, which is outside the BREPI definition.

#### BREPI Test Result

Result: \$0 of Company Z's \$250,000 assessable income is BREPI.

BREPI as a percentage of assessable income: 0% - well below the 80% threshold.

Condition (b) of s 23AA is satisfied.

## 4.4 ATO Guidance - LCR 2019/5

### Law Companion Ruling

**LCR 2019/5** (Law Companion Ruling - Base rate entities and base rate entity passive income) provides authoritative, binding ATO guidance on this exact issue. Key paragraphs:

**Paragraph 22:** Amounts of the net income of a trust estate are proportionately shared between beneficiaries based on their present entitlements to trust income (the Bamford proportionate approach). Each beneficiary's share of net income carries the character of the underlying income components proportionately.

**Paragraph 23:** In determining each beneficiary's share of BREPI, expenses must be allocated in a fair and reasonable way - expenses specifically attributable to a particular income type should be allocated against that income type.

**Paragraph 30 and Examples:** The ruling explicitly addresses multi-tier trust structures and confirms that the paragraph (g) tracing applies "indirectly through one or more interposed partnerships or trust estates." Where the underlying income is active business income, it does not become BREPI merely because it passes through one or more trusts before reaching the corporate beneficiary.

LCR 2019/5 is a Law Companion Ruling and is binding on the Commissioner (s 357-75, Sch 1, TAA 1953). It provides certainty that active trading income flowing through a multi-tier trust structure to a corporate beneficiary does not constitute BREPI.

## 4.5 The Importance of Income Composition

The conclusion above depends entirely on Unit Trust ABC's income being genuinely active trading income with no passive components. If Unit Trust ABC derives even a small amount of passive income (e.g., bank interest on its business account, rent from a sublease, a capital gain on disposal of a business asset), the proportionate share of that passive income flowing through to Company Z will be BREPI.

### Warning: Income Composition Matters

Example: If Unit Trust ABC's \$500,000 net income includes \$480,000 of trading income and \$20,000 of bank interest, the proportionate share of interest flowing to Company Z (via Family Trust DEF) is \$10,000 ( $\$20,000 \times 50\%$  - being Company Z's share of the trust chain).

Company Z's BREPI would be \$10,000 out of \$250,000 = 4%. Still well below 80%, so BRE status is maintained.

However, if Company Z had minimal trading-sourced income and significant passive-sourced distributions, the 80% threshold could be breached.

## 5. Worked Example Tables

### 5.1 BREPI Calculation - Income Flow

| Entity / Step  | Amount           | BREPI?   |
|--|------------------|--|
| Unit Trust ABC - net income (active trading)                         | \$500,000        | N/A (trust level - not assessed to Company Z directly) |
| Distribution: Unit Trust ABC to Family Trust DEF                     | \$500,000        | N/A (trust level)                                      |
| Family Trust DEF - net income (includes Unit Trust ABC distribution) | \$500,000        | N/A (trust level)                                      |
| Distribution: Family Trust DEF to Company Z                          | \$250,000        | Apply s 23AB(1)(g) tracing                             |
| <b>Tracing result: underlying income is active trading (s 6-5)</b>   | <b>\$250,000</b> | <b>NOT BREPI - not referable to paragraphs (a)-(f)</b> |

| BREPI Summary - Company Z       | Amount                        |
|---------------------------------|-------------------------------|
| Total assessable income         | <b>\$250,000</b>              |
| Total BREPI                     | <b>\$0</b>                    |
| BREPI as % of assessable income | <b>0%</b>                     |
| 80% threshold breached?         | <b>NO</b>                     |
| <b>Base rate entity status</b>  | <b>YES - 25% rate applies</b> |

### 5.2 Tax Impact Comparison

| Item                          | BRE (25%)              | Non-BRE (30%)          |
|-------------------------------|------------------------|------------------------|
| Assessable income             | \$250,000              | \$250,000              |
| <b>Tax payable</b>            | <b>\$62,500</b>        | \$75,000               |
| After-tax retained in company | \$187,500              | \$175,000              |
| Franking credits generated    | \$62,500 (at 25% rate) | \$75,000 (at 30% rate) |
| <b>Annual tax saving</b>      | <b>\$12,500</b>        | N/A                    |

#### Note on Franking and Integration

While the 25% rate produces fewer franking credits per dollar of profit, the ultimate individual shareholder receives a correspondingly lower gross-up and offset when franked dividends are paid out.

The net after-tax position to the ultimate individual shareholder (at their marginal rate) is the same regardless of the company rate - the imputation system ensures integration.

The \$12,500 saving represents a genuine timing benefit while profits remain in the company. If Company Z retains profits for future investment or working capital, the 25% rate provides a meaningful cash flow advantage over the 30% rate.

### 5.3 Sensitivity Analysis - What if Some Income Were Passive?

The following table shows the BREPI percentage at different levels of passive income within Unit Trust ABC's \$500,000 net income, assuming Company Z receives 50% of the total (\$250,000).

| Passive Component in Unit Trust ABC | BREPI in Company Z's \$250K | BREPI % | BRE Status?                      |
|-------------------------------------|-----------------------------|---------|----------------------------------|
| \$0 (100% active trading)           | \$0                         | 0%      | YES - BRE                        |
| \$50,000 (10% passive)              | \$25,000                    | 10%     | YES - BRE                        |
| \$200,000 (40% passive)             | \$100,000                   | 40%     | YES - BRE                        |
| \$400,000 (80% passive)             | \$200,000                   | 80%     | YES - BRE (exactly at threshold) |
| \$410,000 (82% passive)             | \$205,000                   | 82%     | NO - 30% rate applies            |

#### Threshold Clarification

The threshold is "no more than 80%" - so exactly 80% still qualifies. The BRE status is only lost when BREPI exceeds 80%. For this structure, the active trading income would need to be less than 20% of Unit Trust ABC's total income before Company Z loses BRE status.

## 6. Case Law Support

### Primary Authority

| Case                                    | Court | Principle  | Application  |
|---|-------|--|--|
| <i>FCT v Bamford (2010) 240 CLR 481</i> | HCA   | Trust income for Division 6 purposes is determined by the trust deed and general law. The proportionate approach applies: each beneficiary is assessed on their proportionate share of the trust's net income, based on their share of trust law income. | Establishes how Company Z's share of Family Trust DEF's net income is calculated. The \$250,000 share carries the proportionate character of the underlying income components - critical for the BREPI tracing under s 23AB(1)(g). |

### Supporting Authority

| Case / Reference                                  | Court / Source                       | Principle  | Relevance   |
|---|--------------------------------------|--|---|
| <i>Thomas v FCT (1972) 3 ATR 165</i>              | HCA                                  | Meaning of "present entitlement" under Division 6 - a beneficiary is presently entitled when they have an indefeasible, vested, and immediate right to demand payment.                               | Confirms the requirements for Company Z to be presently entitled to its share of trust income - a prerequisite for the income to be assessed to Company Z (and therefore relevant to the BRE analysis).                             |
| <i>FCT v Myer Emporium Ltd (1987) 163 CLR 199</i> | HCA                                  | Profit from an isolated transaction is ordinary income under s 6-5 where a profit-making purpose exists at the time of acquisition.  | Supports the characterisation of Unit Trust ABC's income as active trading income (ordinary income under s 6-5), not capital - reinforcing that the income is not a "net capital gain" under paragraph (f) and therefore not BREPI. |
| <b>LCR 2019/5</b>                                 | ATO (Binding - Law Companion Ruling) | Comprehensive guidance on BREPI tracing through multi-tier trust structures. Confirms that trust distributions under Division 6 are only BREPI to the extent referable to underlying passive income. | Directly on point. Binding on the Commissioner. Provides the authoritative framework for the paragraph (g) tracing analysis applied in this report.   |

## 7. Conclusion

**Company Z is a base rate entity for the 2024-25 income year and is taxed at the 25% company tax rate.** The \$250,000 trust distribution received from Family Trust DEF is not BREPI under s 23AB(1)(g) of the ITRA 1986, because it is entirely referable to active trading income of Unit Trust ABC. Active trading income (ordinary income under s 6-5 ITAA 1997) does not fall within any of the passive income categories in paragraphs (a) to (f) of s 23AB(1).

With 0% BREPI and aggregated turnover below \$50M, both limbs of the s 23AA test are satisfied. Tax payable is \$62,500 (25%), saving \$12,500 compared to the 30% rate.

This conclusion is supported by the binding Law Companion Ruling LCR 2019/5, which confirms that trust distributions flowing through multi-tier trust structures are only BREPI to the extent the underlying income is passive in character.

This conclusion is contingent on: (a) Unit Trust ABC's income being genuinely active trading income with no passive components; (b) Company Z having no other assessable income that includes BREPI amounts; and (c) aggregated turnover remaining below \$50M. The BRE test applies annually, and the income composition of Unit Trust ABC should be reviewed each year.

## 8. Risks & Caveats

**Part IVA risk: [Low]** The bucket company structure receiving active trading income distributions is a well-established and commercially recognised arrangement. The base rate entity status flows from the character of the underlying income, not from any contrivance or artifice. No Part IVA concern arises from receiving a distribution of active trading income through a standard trust structure.

**ATO audit focus - BREPI classification: [Moderate]** The ATO has flagged BREPI classification as a compliance focus area. The ATO may request evidence of the composition of Unit Trust ABC's income to verify it is genuinely active trading income and not passive in character. Retain detailed working papers showing the full breakdown of Unit Trust ABC's net income by type (trading, interest, rent, capital gains, etc.) for each income year.

**Income composition risk: [Monitor annually]** If Unit Trust ABC derives ANY passive income - even incidental bank interest on its business account - the proportionate share flowing to Company Z will be BREPI. While small amounts are unlikely to breach the 80% threshold, the composition should be reviewed each year. Consider whether passive income can be earned in a separate entity to keep Unit Trust ABC's income stream purely active.

**Franking rate consistency: [Procedural]** Company Z's corporate tax rate for imputation purposes is determined by reference to the BRE status. Under the imputation rules, the "corporate tax rate" for franking purposes is based on the entity's status. If BRE status changes from year to year (e.g., due to a change in income composition), the franking rate changes accordingly. Over-franking or under-franking penalties may apply under Div 202 ITAA 1997 if the wrong rate is used. Verify BRE status each year before franking any dividends.

**Division 7A - UPE exposure: [Separate issue]** If the \$250,000 distribution from Family Trust DEF to Company Z is not physically paid in cash, a UPE arises. Post-16 December 2009 UPEs are treated as Division 7A loans under TD 2022/11 and must be placed on complying Div 7A loan terms before the earlier of Family Trust DEF's lodgment day or actual lodgment date. This is a separate compliance issue from BRE status but is a common trap in bucket company structures.

**Year-by-year test: [Ongoing]** The BRE test applies afresh each income year. Company Z must satisfy both conditions (aggregated turnover < \$50M and BREPI <= 80%) in every income year. A change in Unit Trust ABC's business (e.g., shifting from active trading to passive investment) could cause Company Z to lose BRE status in future years.

## 9. Rulings & References

### Legislation

| Provision                                     | Relevance   |
|---|---|
| Income Tax Rates Act 1986 (Cth), s 23AA       | Definition of base rate entity - two cumulative conditions (aggregated turnover and BREPI)      |
| Income Tax Rates Act 1986 (Cth), s 23AB       | Definition of base rate entity passive income (BREPI) - paragraphs (a)-(g)                      |
| Income Tax Rates Act 1986 (Cth), s 23AB(1)(g) | Trust distribution tracing - BREPI only to the extent referable to passive income under (a)-(f) |
| ITAA 1936, Division 6, Part III (ss 95-102)   | Trust taxation - assessment of beneficiaries and trustee  |
| ITAA 1936, s 97(1)                            | Assessment of presently entitled beneficiary at their own rates                                 |
| ITAA 1936, s 99A                              | Trustee assessed at top marginal rate if no beneficiary presently entitled                      |
| ITAA 1936, Division 7A, Part III              | Deemed dividends - relevant if UPE arises on the \$250,000 distribution                         |
| ITAA 1997, s 6-5                              | Ordinary income - characterisation of Unit Trust ABC's trading income                           |
| ITAA 1997, s 328-115                          | Aggregated turnover - calculation including connected entities and affiliates                   |
| ITAA 1997, Div 202                            | Franking - corporate tax rate for imputation purposes   |
| ITAA 1997, s 995-1(1)                         | Corporate tax rate definition for BRE and imputation purposes                                   |

### ATO Rulings & Guidance

| Reference   | Topic   | Binding Status   |
|-------------|---|--|
| LCR 2019/5  | Base rate entities and base rate entity passive income - comprehensive guidance on BREPI tracing through trust structures | Binding (Law Companion Ruling - s 357-75, Sch 1, TAA 1953) |
| TD 2022/11  | Division 7A: trust unpaid present entitlements - treatment of UPEs as Div 7A loans  | Binding (Tax Determination)                                |
| PCG 2017/13 | Transitional approach to trust UPEs and Division 7A compliance  | Non-binding (Practical Compliance Guideline)               |

### Case Law

| Case  | Court | Principle   |
|---|-------|---|
| <i>FCT v Bamford (2010) 240 CLR 481</i>           | HCA   | Proportionate approach to trust income and net income under Division 6      |
| <i>Thomas v FCT (1972) 3 ATR 165</i>              | HCA   | Meaning of present entitlement under Division 6                             |
| <i>FCT v Myer Emporium Ltd (1987) 163 CLR 199</i> | HCA   | Characterisation of ordinary income from profit-making transactions (s 6-5) |

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| Item    | Detail     |
|---------|------------|
| Version | 1.0        |
| Date    | March 2026 |