



In detail

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Payments by private companies – use of assets

How payments by private companies to shareholders and associates are treated as dividends, including use of assets.

Last updated 8 February 2017

From 1 July 2009, a payment includes:

- the provision of an asset for use by a shareholder or their associate (other than a transfer of property)
- when a company asset is available for use by a shareholder or their associate to the exclusion of the company, but not where there is a general entitlement to use the company's assets
- a right to use assets under a licence or lease, but which does not involve a transfer of property. It does not matter when the right to use the asset is granted.

An asset may also be available for use by a shareholder or their associate:

- without a formal agreement
- where there is no actual use.

The time the payment is made is the first time the asset is used with the permission of the private company.

However, where the right to use a company asset continues into another income year, then the provision of the asset for use in the subsequent year is treated as being a separate payment made at the start of that year.

If a company asset is used by more than one entity simultaneously it is necessary to consider whether the use of that asset should be attributed to a particular entity or apportioned.

Example 1 – provision of asset for use by shareholder

On 7 October 2008, Ngo Pty Ltd leases a car for five years and then provides the car to Barry, a shareholder, to use for the duration of that period. Barry pays Ngo Pty Ltd \$5,000 a year for the use of the car. After 1 July 2009, the provision of this car became a payment under Division 7A. The payment occurred on 1 July 2009 when the car was first available for Barry's use in the 2010 income year. It does not matter that the agreement was entered into in the 2009 income year, because the provision of the car continues in the 2010 and later income years.

Because Barry has the right to use the car for the whole of 2010, the value of the payment for 2010 is based on 12 months of use. It does not matter that the car was not driven ('used') by Barry every day during the income year.

Example 2 – use of asset to the exclusion of the company

Brian is a shareholder of a private company that owns a luxury yacht. He does not have a formal agreement with the company in relation to the yacht however he takes the yacht out every

second weekend. Brian keeps the yacht at the company's business premises, but takes the key home. Brian stores several personal items on the yacht.

Brian's fortnightly use of the yacht is a payment under Division 7A. The availability of the yacht for Brian's use is also subject to Division 7A because the yacht is not readily available for use by the company. The company would need to arrange with Brian to get the key and for the removal of Brian's personal items before using the yacht. That is, the asset is available for Brian's use to the exclusion of the company.

Example 3 – provision of asset for use by shareholder and associates

Marina is a shareholder of a private company that owns a city apartment. The apartment is generally available for rent. However, Marina asks the company not to rent the apartment out for a week so that she and her family can use it over a long weekend. Marina's use of the apartment is a payment for the purposes of Division 7A.

Example 4 – provision of assets for use by shareholders

Peter is a shareholder of a private company that owns five cars for company use. Shareholders and their associates have general permission to use the cars on weekends if they are not being used for company business. Peter regularly takes one of the cars home.

Peter's use of the car that he takes home will be subject to Division 7A. This will include driving the car (actual use) and the availability of the car for his use to the exclusion of the company, such as when it is parked at home, or at a restaurant that Peter is visiting.

Although Peter may have general permission to use all five of the cars, he does not use all of them for the purposes of Division 7A.

The four cars that Peter leaves at the company premises are available for the company to loan to another shareholder, employee, customer, or other party. That is, these cars are not available to Peter to the exclusion of the company.

Example 5 – provision of asset for use by shareholders but not associates

Clare and her husband Martin are shareholders of a private company that owns a holiday house. Clare, Martin and their infant son Phoenix have a one-month holiday at the house over summer. They do not pay for the use of the holiday home.

Although Phoenix is an associate of Clare and Martin, the provision of the use of the asset is attributable to Clare and Martin. This is the case particularly because Phoenix has no power to enter into a contract with the company and because of his dependence on Clare and Martin. The company is not providing the holiday house to Phoenix for his use, and his incidental use of the house is secondary to that of Clare and Martin.

The use of the holiday house can therefore be attributed to Clare and Martin in equal shares on the basis that they use the holiday house equally.

Example 6 – provision of asset for use by shareholder with amount paid

Hayden is a shareholder of a private company. Hayden leases a car from the private company for 12 months for a nominal amount of \$10,000. Hayden uses the car to drive his children to school in the morning. Hayden's wife (who is also a shareholder) sometimes drives the car on weekends.

The use of the car is attributable to Hayden's relationship with the company. The use of the car by Hayden's spouse and his

children is secondary to his right to use the asset and is not provided by the company for their use, but Hayden's.

Hayden is assessed on the market value of the use of the car for the full 12 months, less actual consideration paid.

Exceptions to payments

There are some exceptions that determine the provision of an asset for use (other than a transfer of property) will not be a payment. Those exceptions are:

- for the minor use of certain company assets
- certain payments that would otherwise be allowable as a once-only deduction
- the use of certain dwellings owned by a private company.

The exceptions do not apply to all payments made by the private company. They only apply to 'provision of an asset for use' payments, which do not involve a transfer of property.

Minor use of company assets

An amount is not a payment if the provision of the asset would, if provided in respect of employment of an employee, be a minor benefit under the FBT laws. A minor benefit has a notional value of less than \$300. In addition, a number of other matters may be relevant such as the infrequency and the irregularity of the provision of the benefit that may lead to a conclusion that it would be unreasonable to treat the minor benefit as a fringe benefit.

Example 7 – provision of asset for use by shareholder that is a minor benefit

John is a shareholder of a private company that hires out trailers for \$250 day. The company owns a number of trailers, one of which it made available to John for a day during the 2016-17 income year to move furniture and other household items.

John is not an employee of the company. However, because the value of his one-off use of the trailer in the income year is less than \$300 and his use of the trailer would be treated as a minor

benefit under the FBT legislation if he was an employee, the use of the trailer does not constitute a payment under Division 7A.

Otherwise deductible payments

Provision of a company asset for use by a shareholder or their associate would not be a payment if the shareholder or their associate had incurred and paid expenditure for the provision of the asset and a once-only deduction would have been allowable to that shareholder or associate. To determine whether an amount is otherwise deductible it is necessary to test whether the payment for the use of the asset would otherwise be deductible to the user of the asset and not whether the user would be able to deduct the amount had they purchased the asset.

Example 8 – provision of asset where shareholder allowed once only deduction

Shop Pty Ltd owns a shopping centre. Audrey is a shareholder of Shop Pty Ltd and at various times during the 2016-17 income year she is provided with part of the property to run a gift wrapping service. Under her arrangement with Shop Pty Ltd, Audrey is not required to make payments to Shop Pty Ltd for her use of that part of the property.

Had Audrey made payments for the use of that part of the property she would be able to deduct those payments, as they would have been part of the expenses she incurred in running her business. Therefore, while Audrey's use of the property is within the scope of the meaning of a payment for Division 7A purposes, it is disregarded as Audrey would have otherwise been able to deduct any payments made for the use of the property.

The exception would not operate if it was established that Audrey had in fact a lease of real property (that is, a transfer of property to an entity within the meaning of that term in Division 7A). The exception is limited to provision of company asset payments that do not involve the transfer of property.

Certain dwellings owned by a private company

There are three separate exceptions for the provision of certain kinds of dwellings by a private company.

1. Provision of a dwelling for use by a shareholder or their associate where that provision would not meet the otherwise deductible rule. For example, the dwelling is used for private purposes. To qualify for this exception you must satisfy the following conditions:

There must be a connection between the provision of the dwelling and that use, lease, licence or other right to use land, water or building in carrying on a business, even if the business is being carried on by an entity other than the shareholder or their associate living in the dwelling.

Example 9 – provision of asset for use by shareholder that is in connection with carrying on a business

Aaron and Liz Jones are shareholders in a private company called Farm Pty Ltd and beneficiaries of the Jones Family Trust. Farm Pty Ltd owns a property called Greenacre on which the Jones Family Trust runs a farming business.

For the 2016-17 income year Aaron and Liz live in a dwelling on Greenacre. Aaron and Liz do not make payments to Farm Pty Ltd for the use of this dwelling.

As this use is for private purposes, it does not come within the otherwise deductible exception.

However, as their use of the dwelling is in connection with the Jones Family Trust using Greenacre to carry on a business, the provision of the dwelling by Farm Pty Ltd is disregarded.

Liz's brother Tom who is also a shareholder of Farm Pty Ltd does the accounts for the Jones Family Trust from his harbour-side dwelling in Sydney. Farm Pty Ltd also owns this dwelling. Tom's use of the harbour side dwelling is not connected to the use of the land, water or building on Greenacre and therefore is not eligible for this exception.

Example 10 – provision of asset for use by shareholder that is in connection with carrying on a business

Rebecca is a shareholder of a private company called Health Pty Ltd. She is also a doctor who runs a surgery. Rebecca runs her surgery in a house owned by Health Pty Ltd under a licence agreement. The surgery takes up approximately 40% of the area of the house. Health Pty Ltd has also granted Rebecca a right to use the remaining 60% of the house to live in. She does not pay Health Pty Ltd under either arrangement.

Rebecca's licence to use the part of the house to run her surgery is not a payment because she would have been allowed a once-only deduction if she had made a payment for that use.

Rebecca's use of the remainder of the house is also exempt as she is carrying on a business, using a building that she has been granted a licence to use and there is a connection between her carrying on the business and her using the remainder of the house as her dwelling.

Example 11 – provision of asset for use by shareholder that is not in connection with carrying on a business

Ernie is a shareholder of a private company called Electric Co Pty Ltd. Electric Co Pty Ltd owns the dwelling that Ernie lives in. Ernie stores his tools at the dwelling, but does not otherwise use the land or building in carrying on his business. Ernie's use of the dwelling is not exempt because he does not use land, water or buildings in carrying on his business. However, the dwelling may be an exempt main residence.

2. Where the provider of the dwelling is a private company, the provision of a dwelling that was acquired before 1 July 2009 and is the main residence of the shareholder or their associate.

This exception is subject to a continuity of ownership test. The exception is not carried over if the ownership of the private company changes.

Example 12 – provision of main residence by a company for use by shareholder

Jessica is the sole shareholder of a private company called House Pty Ltd. The sole asset owned by House Pty Ltd is a dwelling that the private company acquired in 2005. Jessica currently uses this dwelling as her main residence. As long as there is no substantial change in ownership of House Pty Ltd, the company's provision of the dwelling by House Pty Ltd, for Jessica's use is disregarded.

However, in 2016-17, Jessica sells her ownership interest in House Pty Ltd to Gaurav. The sale of her interest in House Pty Ltd represents a change in the ownership of the company for the purposes of the continuity of ownership test in the tax laws. Therefore if Gaurav seeks to use the dwelling owned by House Pty Ltd as his main residence without paying market value rates, his use of the house will be treated as a payment for the purposes of Division 7A.

Gaurav may then be liable to pay tax (as the company is taken to have paid a dividend to Gaurav) if the payment for the use of the house is not converted to a loan and either repaid before the lodgment day of the private company, or a loan agreement complying with Division 7A requirements is made (and subject to the private company having a distributable surplus).

3. Where company title arrangements is for the provision of a dwelling to a shareholder or their associate where the dwelling is a flat or home unit that is part of a complex of two or more flats or home units. This exception applies where:

This exception does not apply if the interposed entity rules in Division 7A apply.

Example 13 – payment to shareholder of associated entity

Jack owns a share in a private company called Property Company, which owns a duplex.

Jack's shareholding gives him the right to occupy part of the duplex. Jack's use of the duplex will not ordinarily be a payment

under Division 7A. However, if Jack is also a shareholder of a private company with accumulated profits, Profit Company, and that company makes a payment or loan to Property Company as part of an arrangement to make a payment to Jack, then the interposed entity rules will apply and Jack's use of the apartment will be a payment for the purposes of Division 7A.

The value of a payment arising from the provision of an asset for use

If the payment is the provision of the use of an asset not involving the transfer of property, the amount of the dividend is the amount that would have been paid for the provision of the asset by parties dealing at arm's length less any amounts actually paid.

The amount of the payment is nil if the amounts paid equal or exceed the amount that would have been paid by parties dealing at arm's length.

Example 14 – provision of asset for use by shareholder at less than market value

Matt is a shareholder of a private company that owns a holiday home. In the 2016-17 income year, Matt uses the holiday home for one week for which he pays the company 50% less than the market value rent for the property. The market value rent for the property is \$1,000 a week. The company has therefore made a payment to Matt of \$500, which will be assessable to Matt under Division 7A, subject to the company having a distributable surplus.

Next step

- [Contact us](#) – if you need to know more

Debt forgiveness by private companies

How forgiveness by private companies of debts of shareholders and shareholders' associates are treated as dividends.

Last updated 30 May 2024

A private company may be taken to pay a dividend to an entity at the end of the company's income year if it forgives a debt owed by the entity during the year either:

- when the entity is a shareholder or an associate of a shareholder of the company, or
- after the entity ceases to be a shareholder or an associate of a shareholder, and a reasonable person would conclude that the payment was made because the entity was a shareholder or an associate of a shareholder at some time.

The total of all dividends a private company is taken to pay under Division 7A is limited to its distributable surplus for that income year.

A forgiveness of debt by a private company in respect of a debt owed by a shareholder or an associate of a shareholder may be treated as a dividend under Division 7A, even if:

- the shareholder or their associate owed the debt in their capacity as an employee or an associate of an employee, or
- the forgiveness occurs in respect of the employment of an employee.

Fringe benefits tax does not apply because forgiven debts treated as dividends paid to a shareholder or their associates are excluded from the definition of a fringe benefit.

For more information, see:

- [Division 7A - distributable surplus](#)
- [Meaning of 'associate'](#)
- [Division 7A and Fringe Benefits Tax](#)

Debts forgiven by other entities

Division 7A also applies to certain debts forgiven by trustees to a shareholder or an associate of a shareholder of a private company, where the company is presently entitled to an amount from the net income of the trust estate and the whole of that amount has not been paid by a specified date.

For more information, see [Division 7A - trust amounts treated as dividends - debt forgiveness](#)

Forgiving a debt

A debt or part of a debt is forgiven under the following circumstances:

- the shareholder's or their associate's obligation to pay the debt (or part of the debt) is released, waived or otherwise extinguished (other than as a result of fully paying the debt in cash or in property, with a value at least equal to the amount of the debt)
- the private company loses its right to sue for recovery of the debt due to the operation of a statute of limitations. The limitation period is 6 years (except for the Northern Territory where it is 3 years) from the date that the right to sue to recover commences but can be extended if the shareholder or their associate acknowledges the debt, or makes a part payment of the debt.
- the shareholder or their associate enters into an arrangement with the private company, where their obligation to pay the debt will end at a future time without having to pay anything (other than a token amount). The arrangement does not have to be legally enforceable and the debt may still remain in the private company's accounting records
- the shareholder or their associate enters into a 'debt parking' arrangement. This is where:
 - the private company assigns its right to receive payment of the debt to a new creditor, who is either an associate or a party to an arrangement with the shareholder or their associate about the assignment
 - it is reasonable to expect that the new creditor will not require the shareholder or their associate to repay the debt.

- it is reasonable to expect that the private company will not insist or rely on the shareholder or their associate repaying the debt.

Examples of this may include:

- the shareholder or their associate losing the capacity to repay the debt
- the private company never requiring the shareholder or their associate to make a repayment
- the private company not treating the debt as a genuine liability (for example, the debt is not included in financial statements prepared for third parties)
- the shareholder or their associate subscribes for shares in the private company to enable the company to make a payment in discharge of the debt, and the company applies all or any of the subscription money towards the debt. The amount taken to be forgiven is the subscription money applied by the private company. The time of forgiveness is when the money is applied.

Division 7A applies to all debts forgiven on or after 4 December 1997, regardless of when the debt arose.

Example 1: debt parking arrangement

Cosy Pty Ltd is owed \$7,000 by its shareholder Fred. In the 2015 income year, Cosy Pty Ltd assigns its right to receive payment of the debt to Fred's wife, Maxine.

This is a debt parking arrangement because Maxine is an associate of Fred's and it is reasonable to expect that Maxine will not require Fred to repay the debt. Cosy Pty Ltd is taken to pay a dividend of \$7,000 to Fred on 30 June 2015, subject to Cosy Pty Ltd's distributable surplus.

Same debt is forgiven at different times

If the same debt is forgiven at different times, only the first forgiveness is treated as a dividend.

Example 2: same debt forgiven at different times

In example 1, assume that Maxine does not seek to recover the debt. Time passes and Maxine's recovery of the debt becomes barred under a statute of limitations.

The debt is treated as forgiven at the time the debt parking arrangement is entered into in the 2015 income year. The debt is also forgiven when the recovery becomes statute barred. Only the first debt forgiveness is treated as a dividend.

When a forgiven debt is not a dividend

The debt is treated as forgiven at the time the debt parking arrangement is entered into in the 2005-06 income year. The debt is also forgiven when recovery subsequently becomes statute barred. Only the first debt forgiveness is treated as a dividend.

Debt forgiveness is not treated as a dividend where:

- a private company forgives a debt owed to it by another company, unless the other company owed the debt in its capacity as trustee
- the debt is forgiven because the shareholder or their associate became bankrupt or because of Part X of the *Bankruptcy Act 1996*
- the debt that has been forgiven results from a loan from a private company that has been treated as a dividend under Division 7A (or section 108 of the *Income Tax Assessment Act 1936*) in the current year or a previous year
- the Commissioner of Taxation exercises his discretion not to treat the debt forgiveness as a dividend.

To exercise his discretion, the Commissioner must be satisfied that:

- the debt was forgiven by the private company because repayment of the debt would have caused the shareholder or their associate undue hardship
- the shareholder or their associate had the capacity to repay the debt at the time it was incurred
- the shareholder or their associate lost the ability to repay the debt as a result of circumstances beyond their control.

To establish undue hardship, evidence is required of exceptional circumstances that would result from the enforcement of the debtor's obligation to pay so as to make that enforcement excessive, or too great, or not fitting or right, or unjustified. Difficulty or inability to pay other debts as they become due does not constitute undue hardship.

It's possible for the conditions for the exercise of the discretion to be satisfied by a debtor that has incurred the debt as a trustee, although this would not be common. The debtor must establish that they would suffer undue hardship if the debt were not forgiven. Among the factors to consider are the trustee's rights of indemnity and exoneration for trust liabilities and, in the case of a corporate trustee, the limited liability nature of a company.

Failure to make the required minimum yearly repayment on an amalgamated loan in the year of forgiveness

If the debt forgiven was an amalgamated loan, and in the income year the forgiveness occurred the amount paid to the private company was less than the required minimum yearly repayment, the forgiveness of the debt is treated as a dividend. The amount of the dividend is:

- the amount of the amalgamated loan that has not been repaid at the time of the forgiveness

less

- any amount treated as a dividend in an earlier income year for the loan, due to a failure to make the required minimum yearly repayment in that year. Note: this reduction could only occur from the 2007-08 year because the 2006-07 year is the first year in which a shortfall in a minimum yearly repayment may be treated as a dividend.

In either case, the amount treated as a dividend is also limited by the private company's distributable surplus in the relevant income year.

For more information, see [Division 7A - loans by private companies](#).

Interaction with commercial debt forgiveness provisions

The commercial debt forgiveness provisions in Schedule 2C of the *Income Tax Assessment Act 1936* do not apply to a debt forgiveness treated as a dividend under Division 7A to the extent it is included in a shareholder's or their associate's assessable income.

If not all of the debt forgiven is included in a shareholder's or their associate's assessable income because the amount treated as a dividend is reduced by the private company's distributable surplus, the commercial debt forgiveness provisions may apply to the amount of the debt forgiven that was not included in their assessable income.

The amount treated as a dividend

The amount treated as a dividend is the amount of the debt forgiven, subject to the private company's distributable surplus.

Example 3: amount treated as a dividend

On 1 April 1997, Abacus Pty Ltd made a loan of \$50,000 to Phil, a shareholder of Abacus Pty Ltd. In December 2014, Abacus Pty Ltd waived Phil's requirement to pay the full amount owing of \$50,000. Phil was no longer a shareholder at that time.

As the debt was forgiven after 4 December 1997, Abacus Pty Ltd is taken to have paid a dividend to Phil of \$50,000 on 30 June 2015, subject to Abacus Pty Ltd's distributable surplus.

Amounts treated as dividends under Division 7A are generally not frankable, even though they are taken to be paid out of the private company's profits. However, there are some exceptions.

Where a deemed dividend arises because of an honest mistake or inadvertent omission, the Commissioner has the discretion to disregard the deemed dividend, subject to conditions being complied with. He may also allow the private company taken to pay the dividend to choose to frank this dividend.

For more information, see:

- [Division 7A - franking implications](#)
- [Division 7A - the Commissioner's discretion under section 109RB](#)
- [Contact us about Division 7A](#)

Interposed entities

Learn how payments and loans by private companies through interposed entities are treated as dividends.

Last updated 24 January 2020

Payments and loans to shareholders through interposed entities may be treated as dividends under Division 7A.

Payments and loans

Payments and loans made through interposed entities may attract Division 7A. This involves a private company indirectly distributing money to a shareholder or their associate through one or more interposed entities. An interposed entity can be an individual, company, partnership or trust and is inserted between a private company and its shareholder or their associate. Division 7A can apply if the shareholder or associate is the target entity to whom the private company's payment or loan is ultimately directed.

Examples include:

- guaranteeing a loan that an interposed private company with a low distributable surplus makes to the shareholder or their associate
- guaranteeing a loan that an interposed entity makes to the shareholder or their associate where a default occurs on the loan
- a trustee distributing money to a shareholder or their associate through one or more interposed entities where the private company has an unpaid present entitlement (UPE) to trust income.

A private company is taken to pay a dividend to the target entity as if the payment or loan was made directly to the target entity where:

- the private company makes a payment or loan to an interposed entity (called the 'first interposed entity')

- a reasonable person would conclude that the private company made the payment or loan solely or mainly as part of an arrangement involving a payment or loan to the target entity
- the first interposed entity or another interposed entity makes a payment or loan to the target entity
- The total of all dividends a private company is taken to pay under Division 7A is limited to its distributable surplus for the year.

 Flowchart showing two alternative arrangements involving interposed entities and a target entity. In the first arrangement, a box labelled "Private company" is connected by an arrow labelled "Loan/payment" to a box labelled "First interposed entity", which is connected by a second arrow labelled "Loan/payment" to a box labelled "Target entity". A dashed line beneath the diagram connects the private company to the target entity and is labelled "Private company taken to pay a dividend to target entity". The word "OR" separates the first arrangement from a second arrangement. In the second arrangement, a box labelled "Private company" is connected by an arrow labelled "Loan/payment" to a box labelled "First interposed entity". A second arrow labelled "Loan/payment" connects the first interposed entity to a box labelled "Other interposed company", and a third arrow labelled "Loan/payment" connects the other interposed company to a box labelled "Target entity". A dashed line beneath the diagram connects the private company to the target entity and is labelled "Private company taken to pay a dividend to target entity". The diagram illustrates that a private company may be taken to pay a dividend to a target entity through either a single interposed entity or multiple interposed entities.

If the interposed entity makes a loan to the target entity, then the private company is taken to make a loan to the target entity. Similarly, if the interposed entity makes a payment to the target entity, then the private company is taken to make a payment to the target entity.

 Flowchart illustrating an arrangement involving a private company, an interposed entity and a target entity. A box labelled “Private company” is connected by an arrow labelled “Payment” to a box labelled “Interposed entity”. A second arrow labelled “Loan” connects the interposed entity to a box labelled “Target entity”. A dashed line beneath the diagram connects the private company directly to the target entity and is labelled “Private company taken to make a loan (not payment) to target entity”. The diagram illustrates that where a private company makes a payment to an interposed entity and the interposed entity makes a loan to a target entity, the private company is treated as having made a loan directly to the target entity.

Example 1

A private company, A Pty Ltd, enters into an arrangement with an entity, X, under which A Pty Ltd makes a payment to X and X then makes a loan to Y, a shareholder of A Pty Ltd. A Pty Ltd is taken to have made a loan to Y (the target entity) regardless of the fact that it actually made a payment to X (the interposed entity).

Arrangement for the purposes of interposed entity transactions includes agreement, understanding, promise or undertaking and doesn't have to be in writing or legally binding.

Reasonable person

When determining what a 'reasonable person' would conclude in relation to the interposed entity provisions, the following circumstances may be relevant:

- the nature of any relationship between the private company, the interposed entity and the target entity
- the timing of the payments or loans
- the amount of the actual payments or loans
- how the payments or loans are recorded in the accounting records of the private company and the interposed entity
- whether there is a commercial basis for the transaction between the private company and the first interposed entity

- the role and attributes of the interposed entity. For example: why it was formed; what it does; and why it was a participant in the transactions.
- the capacity of the interposed entity to fund the payment or loan outside of any amount received from the private company
- any history or pattern to the transactions
- the primary requirement for, or intended use of, the funds by the target entity
- the target entity's financial position, annual income (including from the private company) and its capacity to make any relevant loan repayments
- the extent to which the target entity draws money from the private company in an assessable form - for example, dividends or salary.

Example 2 – purpose of the transaction

Bill is the sole shareholder of ABC Pty Ltd (ABC). Bill's brother in law, Ben, is a shareholder and director of XYZ Pty Ltd (XYZ).

Bill and his wife Jessica have a son who in the 2014 income year required \$20,000 for legal fees. Bill and Jessica have personal savings of \$30,000 that can be accessed to raise funds for the fees.

ABC, a successful construction business, has made several loans to Bill and Jessica over the years.

XYZ, on the other hand, has suffered years of losses from unsuccessful business ventures and is heavily in debt.

In 2015, the Australian Taxation Office (ATO) is reviewing the taxation affairs of ABC, Bill and Jessica, and discover that:

- on 13 February 2014, ABC made a payment of \$22,000 to XYZ
- on 14 February 2014, XYZ made a loan of \$20,000 to Jessica, on an interest-free at-call basis.

All loans made by ABC directly to Bill and Jessica were put on Division 7A complying terms, and minimum yearly repayments made. Bill has some knowledge of the basic Division 7A rules

gained from advice received while preparing company tax returns.

At the time of the February 2014 transactions, it was evident that XYZ would not have a distributable surplus at 30 June 2014.

Relevant circumstances:

- The loan is not from an arm's length person, rather it is from family
- There was only one day between ABC's payment to XYZ and the loan to Jessica
- The two amounts are quite similar and is the amount of money required to pay the legal fees
- There is no apparent commercial reason for the payment from ABC to XYZ
- Bill and Jessica had capacity to pay the legal fees
- It was evident that XYZ would not have a distributable surplus at 30 June 2014.

Despite Bill and Jessica having access to alternative means of paying the legal fees, this is not sufficient to displace the conclusion that the payment by ABC to XYZ was made mainly or solely as part of an arrangement involving the loan from XYZ to Jessica. A reasonable person would conclude that ABC made the payment to XYZ so that it could lend the \$20,000 to Jessica - accordingly, the interposed entity provisions operate to create a notional loan from ABC to Jessica.

It is noted that although it might also be reasonably concluded that Bill had an intention to avoid the operation of Division 7A, the existence of such an intention is not necessary to trigger the operation of the interposed entity provisions.

Note: While XYZ was taken to have paid a dividend to Jessica as a result of the loan made to Jessica, the amount taken to be paid as a dividend from XYZ is nil due to the lack of a distributable surplus in XYZ.

Example 3 – payment for services

Assume the same facts as in Example 1, except that the amount paid to Jessica by XYZ was not a loan, rather a payment (an

arm's length amount) for administration services provided by Jessica to the company in earlier income years. Due to the financial position of XYZ and the family connections, Jessica agreed not to invoice XYZ and not to receive payment until the company was in a position to pay for the services rendered.

A reasonable person would still conclude that, on balance, ABC made the payment to XYZ so that it could make the \$20,000 payment to Jessica, and ABC would therefore be taken to have made a notional payment to Jessica. However, the fact that the payment relates to the provision of administration services would be taken into account in determining the quantum of the notional payment.

For the purposes of determining the amount of the notional payment, the Commissioner, to the extent that the payment to Jessica will be assessed to her, would determine the amount of the notional payment is nil (see [TD 2011/16](#) - *Income tax: Division 7A - payments and loans through interposed entities - factors the Commissioner will take into account in determining the amount of any deemed payment or notional loan arising under section 109T of the Income Tax Assessment Act 1936*).

Timing of payment or loan

The private company is taken to have made a payment or loan to the target entity at the time the interposed entity made a payment or loan to the target entity. This is regardless of whether the amounts or timing of the payments or loans from the private company to the interposed entity are the same. The situation is different in arrangements involving default of loans with guarantees (see when the private company is taken to have made the payment to the target entity when a default has occurred).

Amount of the payment or loan

Generally, the amount the private company is taken to have paid or lent to the target entity is based on:

- the amount the private company paid or lent to the first interposed entity
- the amount the interposed entity paid or lent the target entity

- **less** any arm's length consideration payable to the target entity from either the private company or any of the interposed entities.
- **less** a proportion of any repayments (of a loan) made by the target entity to the interposed entity (see effect of repayments the target entity makes to the interposed entity).

The calculations are different in arrangements involving guarantees and arrangements involving UPEs .

See also

- Guarantees: loans with guarantees
- Trusts: payments and loans

Example 4 – calculating the amount of the payment

Bill is the sole shareholder of ABC Pty Ltd. Bill's friend Ben is a director of PQR Pty Ltd. Bill and Ben reach an agreement that on 10 February 2016 ABC Pty Ltd will pay \$5,000 to PQR Pty Ltd. PQR Pty Ltd then makes a payment of \$5,500 to Bill's wife Betty, an associate of Bill. Of the \$5,500, \$500 represents a payment to Betty for accounting services for PQR Pty Ltd. The \$500 is an arm's length payment. The payments were made on 30 June 2016.

In this example, PQR Pty Ltd is the interposed entity and Betty is the target entity. ABC Pty Ltd is taken to pay Betty \$5,000. This takes into account the \$5,500 that PQR Pty Ltd paid Betty, reduced by the \$500 for payment of accounting services.

On 30 June 2016, ABC Pty Ltd is taken to pay Betty an unfranked dividend of \$5,000, subject to the distributable surplus of ABC Pty Ltd.

 Flowchart illustrating an arrangement involving a private company, an interposed entity and a shareholder. A box labelled "ABC Pty Ltd" is connected by an arrow labelled "\$5,000 payment" to a box labelled "PQR Pty Ltd". A second arrow labelled "\$5,500 payment (includes \$500 for services rendered)" connects PQR Pty Ltd to a box labelled "Betty (associate of shareholder of ABC Pty Ltd)". A dashed line beneath the diagram connects ABC Pty Ltd directly to Betty and is labelled "ABC Pty Ltd taken to pay a dividend of \$5,000 to Betty". The diagram illustrates that where a private company makes a payment to an interposed entity and the interposed entity passes a related payment to an associate of the private company's shareholder, the private company is taken to have paid a dividend directly to the associate equal to the original payment amount of \$5,000.

Repayments

If the target entity makes a repayment on a loan made to it by an interposed entity, the amount that the private company is taken to have lent the target entity (the 'notional loan') is reduced by the following amount:

Repayment made by target entity to interposed entity	x	Amount of notional loan
		Amount actually lent to target entity

The effect of the repayments the target entity makes to the interposed entity is different in situations involving loans by an interposed private company relying on guarantees.

Example 5 – partial repayment

On 1 November 2015, Virgil Pty Ltd makes a loan of \$10,000 to Tracy Pty Ltd (the interposed entity) under an arrangement in which Tracy Pty Ltd will lend the amount to Penelope (the target entity). Penelope is a shareholder of Virgil Pty Ltd.

On 15 November 2014, Tracy Pty Ltd lends Penelope \$15,000. For the year ended 30 June 2016, Virgil Pty Ltd has a distributable surplus of \$50,000.

Virgil Pty Ltd is taken to have made a notional loan of \$10,000 to Penelope, as this was the arrangement between Virgil Pty Ltd and Tracy Pty Ltd. Before the end of the income year Penelope repays \$3,000 to Tracy Pty Ltd. The amount Virgil Pty Ltd is taken to have loaned Penelope is reduced by a proportion of the repayment Penelope made to Tracy Pty Ltd. The amount of the reduction is:

$$\$3,000 \times (\$10,000 / \$15,000) = \$2,000$$

Virgil Pty Ltd is taken to pay Penelope \$8,000 (that is, \$10,000 - \$2,000). On 15 November 2015 Virgil Pty Ltd is taken to pay a deemed dividend of \$8,000 to Penelope.

 Example 4 diagram

First interposed entity receives a dividend

If the payment or loan from the private company to the first interposed entity is an actual dividend, and certain conditions are satisfied, the private company may still be taken to have made a payment or loan to the target entity. This means, depending on the circumstances, although the amount may have been included in the assessable income of the interposed entity, the payment or loan from the private company to the target entity may be subject to Division 7A.

See also

- [TD 2018/13](#) - *Income tax: Division 7A: can section 109T of the Income Tax Assessment Act 1936 apply to a payment or loan made by a private company to another entity (the 'first interposed entity') where that payment or loan is an ordinary commercial transaction?*

Written loan agreement

If the actual loan from the interposed entity to the target entity is made under a complying Division 7A written loan agreement, the notional loan by the trustee to the target entity is deemed to be under that agreement.

In subsequent income years a dividend will not arise under Division 7A provided the required 'minimum yearly repayment' is made.

Guarantees

Division 7A can apply to arrangements that involve a private company indirectly distributing money to a shareholder or an associate of a shareholder by guaranteeing a loan that an interposed private company or other entity makes to the shareholder or their associate. This can include more complex arrangements that involve a guarantee and loans or payments through a chain of entities.

How a deemed dividend arises

Several provisions within Division 7A deem dividends to occur through the use of guarantees in the same way as if the private company had made a payment directly to the target entity. Essentially, this is where:

1. A private company guarantees a loan made by an interposed entity.
2. A reasonable person would conclude that the private company gave the guarantee solely or mainly as part of an arrangement involving a payment or loan to the target entity.
3. Either:
 - a. As a result of the guarantee, the private company has a liability (other than a contingent liability) to make a payment to the interposed entity, or
 - b. An interposed private company makes a payment or loan to the target entity (there can be more than one interposed entity).

For these purposes, it does not matter:

- whether the interposed private company made the payment or loan to the target entity before, after or at the same time as the first interposed entity received the guarantee from the private company
- whether or not the interposed private company paid or lent the target entity the same amount as the private company guaranteed, or
- whether or not a present liability ever arose under the guarantee.

Amount of the deemed dividend

The Division 7A provisions involving guarantees draw a distinction between a situation where an interposed private company makes a

payment or loan to a target entity, and where other types of entities are used.

Where there is an interposed private company that makes a payment to a target entity, then the amount of the deemed dividend is based on:

- the amount of the loan the private company guaranteed
- the amount the interposed private company paid to the target entity
- **less:** any arm's length consideration payable to the target entity by the private company or any of the interposed entities

For example, the amount the interposed private company paid the target entity might include an amount payable to the target entity for goods or services provided.

- **less** an adjustment for the distributable surplus (of the interposed private company) and other dividends that company is taken to pay that income year.
- The amount of reduction (if any) is equal to the distributable surplus of the interposed private company that made the payment or loan to the target entity **less** any dividends **that** company is taken to pay under Division 7A during that income year (apart from as a result of the payment or loan in question).

Repayments made by the target entity to the interposed private company are not taken into account in working out how much the private company is taken to pay the target entity.

The private company is taken to have made the payment to the target entity at the same time the interposed private company makes the payment or loan to the target entity.

On the other hand, if the arrangement does not involve an interposed private company directly making a payment to a target entity, then the amount of the deemed dividend is based on:

- the amount the private company is liable to pay under the guarantee to the interposed entity as a result of a default on the loan by the target entity
- the amount the interposed entity loaned the target entity
- **less:** any arm's length consideration payable to the target entity by the private company or the interposed entity.

Example 6

Epsilon Pty Ltd guarantees a loan of \$600,000 that its subsidiary Delta Pty Ltd makes to Sam, a majority shareholder of Epsilon Pty Ltd on 12 May 2015. The guarantee is part of an arrangement involving the loan by Delta Pty Ltd to Sam. There is no written agreement outlining the terms of the loan. For the 2014-15 income year, Epsilon Pty Ltd has a distributable surplus of \$1,000,000 and Delta Pty Ltd has a nil distributable surplus.

 Flowchart illustrating a financial arrangement between three parties. On the left, a box labelled "Epsilon Pty Ltd (shareholder of Delta Pty Ltd)" states "Distributable surplus = \$100,000,000". An arrow labelled "Guarantee for \$600,000 loan" points from Epsilon Pty Ltd to a central box labelled "Delta Pty Ltd", which states "Nil distributable surplus". From Delta Pty Ltd, an arrow labelled "\$600,000 loan" points to a box on the right labelled "Sam (shareholder of Epsilon Pty Ltd)". A dashed line beneath the diagram is labelled "Epsilon Pty Ltd taken to pay a dividend of \$600,000 to Sam" and connects Epsilon Pty Ltd to Sam, indicating the deemed dividend outcome resulting from the arrangement.

Epsilon Pty Ltd is taken to pay a dividend to Sam because, as part of an arrangement, it guaranteed a loan that another private company (Delta Pty Ltd) made to Sam. Delta Pty Ltd is not taken to pay a dividend to Sam because its distributable surplus is nil (for further information, see [Division 7A - Loans by private companies](#)).

Epsilon Pty Ltd is taken to pay Sam \$600,000 on 12 May 2014, being the amount Delta Pty Ltd loaned Sam less Delta Pty Ltd's distributable surplus (that is \$600,000 less nil).

On 30 June 2015, Epsilon Pty Ltd is taken to pay a dividend of \$600,000 to Sam.

Example 7

On 10 June 2015, Z Pty Ltd, a wholly owned subsidiary of X Pty Ltd, borrows \$150,000 from Megabank Ltd (a publicly listed financial institution). The loan is guaranteed by X Pty Ltd. The guarantee is part of an arrangement between X Pty Ltd and Z Pty Ltd involving a payment of \$150,000 to Harold, a majority

shareholder of X Pty Ltd. The payment of \$150,000 is made to Harold on 10 June 2015.

For the 2014-15 income year, the distributable surplus of X Pty Ltd is \$250,000 and the distributable surplus of Z Pty Ltd is \$25,000. Z Pty Ltd is not taken to pay any other dividends under Division 7A during that income year. This example is shown below.

Flowchart illustrating a financial arrangement involving a loan and a deemed dividend. On the left, a box labelled "X Pty Ltd" states "distributable surplus = \$250,000". An arrow labelled "Guarantee" points from X Pty Ltd to "Megabank Ltd". An arrow labelled "Loan \$150,000" leads from Megabank Ltd to "Z Pty Ltd", which states "distributable surplus = \$25,000". An arrow labelled "Payment 150,000" points from Z Pty Ltd to "Harold (shareholder of X Pty Ltd)". A dashed line beneath the diagram is labelled "X Pty Ltd taken to pay a dividend of \$125,000 to Harold" and connects X Pty Ltd to Harold, indicating the deemed dividend outcome arising from the arrangement.

X Pty Ltd guarantees a loan made by a publicly listed financial institution (Megabank Ltd) to X Pty Ltd's subsidiary Z Pty Ltd which pays the funds to X Pty Ltd's shareholder Harold. It is reasonable to conclude an arrangement was made to produce this effect. X Pty Ltd is taken to pay a dividend to Harold (the payment amount reduced by Z Pty Ltd's distributable surplus).

All four of the conditions are satisfied for X Pty Ltd to be taken to make a payment to Harold (the target entity). X Pty Ltd is taken to pay Harold \$125,000, being the amount Z Pty Ltd paid Harold less Z Pty Ltd's distributable surplus (that is \$150,000 - \$25,000).

On 30 June 2015 X Pty Ltd is taken to pay a dividend of \$125,000 to Harold.

Z Pty Ltd has made a payment directly to Harold that is treated as a dividend (see [Division 7A - payments by private companies](#)). That dividend arises because Harold is an associate of a shareholder of Z Pty Ltd. The amount treated as a dividend to Harold is \$25,000 (that is the dividend is reduced to Z Pty Ltd's distributable surplus of \$25,000). This assumes that Z Pty Ltd is not taken to pay any other dividends under Division 7A during that income year.

Example 8

On 15 August 2014, Mary takes out a bank loan of \$80,000. The loan is guaranteed by PQR Pty Ltd, of which Mary is a shareholder. The bank is not a private company. The guarantee is part of an arrangement involving a loan to Mary. After repaying \$10,000, Mary defaults on the loan on 30 May 2015 and the bank exercises the guarantee.

 Flowchart illustrating a financial arrangement involving a guarantee, a bank loan and a deemed dividend. On the left, a box labelled "PQR Pty Ltd" is connected by an arrow labelled "Guarantee" to a box labelled "Bank (a public company)". An arrow labelled "\$80,000 loan" points from the bank to a box on the right labelled "Mary (shareholder of PQR Pty Ltd)". A separate arrow labelled "\$10,000 repayment then Mary defaults" points from Mary back to the bank, indicating that \$10,000 of the loan is repaid before default occurs. A dashed line beneath the diagram is labelled "PQR Pty Ltd is taken to pay a dividend of \$70,000 to Mary" and connects PQR Pty Ltd to Mary, showing the deemed dividend amount resulting from the arrangement after the repayment and default.

PQR Pty Ltd is taken to make a payment to Mary equal to the amount it is liable to pay under the guarantee

The amount PQR Pty Ltd is taken to pay Mary is the amount it is liable to pay the bank under the guarantee, which is \$70,000.

On 30 June 2015, PQR Pty Ltd is taken to pay a dividend of \$70,000 to Mary, subject to PQR Pty Ltd's distributable surplus.

Avoiding a deemed dividend

Written loan agreement

A private company will not be taken to make a payment to the target entity if the private company and the target entity enter into a written loan agreement in respect of the debt, and that written loan agreement meets the minimum interest rate and maximum term criteria for a complying loan (see [Division 7A – loans by private companies](#)).

Hardship

A private company is not taken to pay a dividend in relation to arrangements where the private company has a present liability to an interposed entity as a result of the default of a target entity if we are satisfied that:

- the target entity would suffer undue hardship as a result of the deemed dividend
- the target entity had the capacity to repay the loan when it entered into the loan.
- Apply to us in writing, addressing the above points, if you consider you will suffer undue hardship if an amount is treated as a dividend.

Next step

- [Contact us](#) – if you need to know more

QC 51189

Trust entitlements

Work out when Division 7A may apply to trust entitlements of private company beneficiaries.

Last updated 2 July 2026



Bendel case - High Court decision

We're reviewing the content on this page as a result of a recent court decision. Refer to our [Decision Impact Statement](#) for more information.

When Division 7A may apply

Division 7A of Part III of the *Income Tax Assessment Act 1936* (ITAA 1936) operates to ensure that private companies are not able to make tax-free distributions of profits to shareholders or their associates in the form of payments, loans or forgiven debts.

Division 7A may apply to private company beneficiaries' trust entitlements where the:

- trust and private company beneficiary are related entities
- trust entitlements are used for the benefit of the private company's shareholder or their associate (for example, the trust).

If the private company [provides financial accommodation](#) to the entity that has use of the funds, it is treated as having made a loan to that entity.

If Division 7A applies, the loan is treated as an unfranked dividend, in the same way a [loan](#) made directly from the company to the entity would be a deemed dividend.

How you manage trust entitlements to ensure Division 7A doesn't apply will depend on whether the entitlements arose:

- [on or after 1 July 2022](#)
- [before 1 July 2022](#)

If you are unsure about how Division 7A applies to trust entitlements of your private company, you may need to seek professional advice.

Entitlements arising on or after 1 July 2022

We published a revised view on how Division 7A applies to trust entitlements created on or after 1 July 2022.

For trust entitlements created on or after 1 July 2022, see [TD 2022/11](#) *Income tax: Division 7A: when will an unpaid present entitlement or amount held on sub-trust become the provision of 'financial accommodation'?*.

Avoiding Division 7A consequences

To avoid triggering Division 7A, the trustee must act **before** the private company's tax return is lodged, or the date it's due to be lodged (whichever occurs first), to either:

- pay the private company its present entitlement, such as
 - pay in cash
 - distribute assets with a market value equal to the amount of the entitlement

- enter a [Division 7A complying loan agreement](#) with the private company, if the trustee wishes to retain the use of the funds the private company beneficiary is entitled to. If it does, the trustee will need to make [minimum yearly repayments](#) to the private company to avoid being deemed to receive dividends in the future.

Providing financial accommodation

A private company beneficiary, that is presently entitled to income from a trust, is considered to have 'provided financial accommodation' to its shareholder or their associate if either the:

- private company beneficiary has [knowledge of its entitlement](#) but doesn't demand payment from the trust – for Division 7A purposes this is treated as a loan made to the trust
- trustee holds an amount from the main trust fund on a new separate trust (a sub-trust) for the sole benefit of the private company beneficiary, and
 - all or part of the sub-trust fund is used by (or for the benefit of) the private company beneficiary's shareholder or their associate (the amount used is the amount of financial accommodation)
 - the private company beneficiary is aware of this use – for Division 7A purposes this is treated as a loan made to the private company beneficiary's shareholder or their associate.

Knowledge of entitlement

A private company beneficiary would know about its entitlement if either:

- the entitlement has been expressed verbally or in writing to the company
- the company and the trust share the same controlling mind, such as the director of the company is also the director of the corporate trustee of the trust.

A private company beneficiary would generally only know that it can demand a present entitlement be paid to it after the end of the income year in which the entitlement arises.

Example 1 – avoiding a Division 7A deemed dividend

Jack runs a business through a discretionary trust, JJ Family Trust (trust). The trustee of the trust is J&J Pty Ltd (trustee) which is controlled by Jack. The objects of the trust are Jack, his family, and a private company, JAJ Pty Ltd that he controls.

On 30 June 2023, the trustee makes JAJ Pty Ltd presently entitled to 100% of trust income.

Although JAJ Pty Ltd and the trustee are both controlled by Jack, JAJ Pty Ltd only knows the amount it is presently entitled to, being \$50,000, on 1 August 2023. This is when JAJ Pty Ltd knows it can demand payment of its \$50,000 present entitlement.

To avoid a deemed dividend from arising in the 2023–24 income year, the trustee can do one of the following by JAJ Pty Ltd's lodgment date for the 2023–24 income year:

- Pay the \$50,000 entitlement to JAJ Pty Ltd
- Put in place a Division 7A complying loan agreement between JAJ Pty Ltd and the trust. If so, the trustee will make its first minimum yearly repayment by 30 June 2025
- Satisfy the income entitlement by putting \$50,000 on a sub-trust for the sole benefit of JAJ Pty Ltd and ensure none of that fund is used by or for the benefit of JAJ Pty Ltd's shareholder or their associate (including the trust).

Use of sub-trusts

A sub-trust may arise where the trustee holds an amount from the main trust fund on a new separate trust for the sole benefit of the private company beneficiary. Where the entitlement to trust income is met by the setting aside of the income amount on sub-trust for the beneficiary, the trustee's obligation in respect of the entitlement to distributed income ends.

A sub-trustee must ensure that the sub-trust funds are held for the sole benefit of the private company beneficiary and are not used by, or applied for the benefit of, its shareholder or their associate. If this occurs and the private company beneficiary knows (or is taken to know) that this has occurred, Division 7A may apply.

To ensure Division 7A doesn't apply, a Division 7A complying loan agreement should be put in place directly between the private company and the user of the funds.

A sub-trust is treated as a separate trust to the main trust and the sub-trustee must lodge tax returns (and will need a separate tax file number (TFN)) unless an exemption applies.

Exemption from lodging a tax return

A sub-trustee is exempt from lodging a tax return if the sub-trust is a 'transparent trust' as described in Law Administration Practice Statement [PS LA 2000/2](#) *An exemption for the trustees of some trust estates from the requirement to furnish a tax return on behalf of the trust estate*. Income derived by the sub-trustee will be included in the private company beneficiary's assessable income.

Entitlements that arose before 1 July 2022

For trust entitlements (referred to as unpaid present entitlements (UPEs)) that arose before 1 July 2022, the Commissioner of Taxation administers the law in a way that is consistent with the view set out in [TR 2010/3](#) (withdrawn) and [PS LA 2010/4](#) (withdrawn).

A UPE is an amount of trust income which the trustee of a trust appoints, but has not yet paid, to a private company beneficiary.

These UPEs can amount to 'the provision of financial accommodation' by the private company beneficiary, in favour of the trust, and therefore may be loans for Division 7A purposes.

A UPE that results in a loan can occur with all types of trusts, including discretionary trusts and unit trusts, and particularly so where the trust and the private company are part of the same family group.

PSLA 2010/4 (withdrawn) provided options for dealing with UPEs which the Commissioner then accepted would not trigger Division 7A f.

The following materials provide a description of the views in the withdrawn guidance

Avoiding Division 7A consequences

The simplest way for the trustee to avoid Division 7A treating the UPE as a deemed dividend paid by the private company to the trust is by paying out the UPE.

Notwithstanding this, a trustee can still appoint a share of the income of a trust to a private company beneficiary without immediately paying out that entitlement, and without attracting Division 7A.

This can be done through either:

- the creation of a [sub-trust](#) for the sole benefit of the private company beneficiary
- providing the trust with a [Division 7A complying loan](#).

The Commissioner will not treat UPEs [created before 16 December 2009](#) as Division 7A loans.

Sub-trust arrangements

To avoid the UPE being treated as a Division 7A deemed dividend paid by the private company to the trust, the trustee must take certain steps to ensure the private company beneficiary is not financially accommodating the trust by allowing the trustee to retain the funds for use within the trust.

This can be done by placing the funds in a separate sub-trust for the sole benefit of the private company beneficiary by the lodgment day of the trust's tax return.

If the trustee fails to put the funds on a sub-trust for the sole benefit of the private company beneficiary by the date specified, we will consider that the private company beneficiary has provided the trust with a loan, by way of financial accommodation, to the amount of the UPE. Division 7A may then operate to deem the private company to have paid a dividend to the trustee of the trust.

Trustee accessing funds held in a sub-trust

The trustee may invest the funds held in the sub-trust back into the main trust on commercial terms, so that the main trust continues to have access to those funds.

However, we require certain formalities be adhered to by the trustee when investing funds from the sub-trust, such as the parties entering a [legally binding investment agreement](#).

Legally binding investment agreements

Investment agreement documents may be prepared as part of the tax return working papers and don't have to be professionally prepared.

However, you may choose to engage a professional to prepare one for you.

Investment agreement documents:

- must be legally binding
- must [provide sufficient details](#) of the investment from the sub-trust to the main trust, demonstrating that the trustee decided to hold the funds representing the UPE on a sub-trust for the sole benefit of the private company beneficiary in the first place
- may be [ongoing](#) to cover future income years
- aren't the same as a [Division 7A complying loan agreement](#).

Details your investment agreement must contain

A legally binding loan agreement, between the main trust and the sub-trust, must contain:

- the names of the parties
- the loan terms, including the
 - amount of the loan
 - date the loan amount is drawn
 - requirement to repay the principal amount of the loan
 - period of the loan
 - interest rate payable on the loan
 - interest payment to be made annually on the last day of the income year
- that the parties named have agreed to the terms
- when the agreement was made, for example, the date it was signed or executed.

Example 2 – a legally binding agreement

We would consider the following document prepared as part of the tax return working papers for the trust's tax return, when a UPE arises during that year, to be sufficient evidence of a legally

binding agreement. The document has assumed that the 2015 trust lodgment day for DiscFamily Trust is 15 May 2016.

PrivCo's entitlement to \$10,000 of the income of DiscFamily Trust for the 2015 income year has been set aside and held on a sub-trust (known as PrivCo Sub-trust).

The trustee of PrivCo Sub-trust and the trustee of DiscFamily Trust have agreed that PrivCo Sub-trust will lend the sum of \$10,000 to DiscFamily Trust in accordance with Option 1 in PS LA 2010/4. This loan was made and this agreement took effect from 15 May 2016 for a period of 7 years. Interest is payable at the Division 7A benchmark interest rate as defined in subsection 109N(2) of the ITAA 1936.

The parties have agreed that interest payments will be:

- calculated annually on the last day of DiscFamily Trust's income year
- paid by DiscFamily Trust to PrivCo Sub-trust no later than the earlier of
 - the date DiscFamily Trust lodged its tax return for the year in respect of which interest was calculated
 - the due date for lodgment of that return, except for the final interest payment, which is to be paid by DiscFamily Trust to PrivCo Sub-trust no later than 14 May 2023.

The trustee of PrivCo Sub-trust has further agreed to distribute and pay the interest it receives from DiscFamily trust no later than that date.

DiscFamily Trust has agreed and is obliged to repay the \$10,000 to PrivCo Sub-trust no later than 14 May 2023.

Signed: – by the trustee of the PrivCo Sub-trust and DiscFamily Trust

Date: – date

Failure to pay the annual repayments or returns

If the trust fails to pay the annual repayments or returns to the private company by the trust's lodgment day, we will consider that the requirements set by the Commissioner have not been satisfied. This is

because the trustee would have breached the terms of the investment agreement.

The non-payment of the annual repayments or returns may result in a Division 7A dividend being deemed to be paid to the main trust.

Safe harbour investment options

The Commissioner has set out 3 investment options, as follows:

- Option 1 – invest the funds representing the UPE on an interest only 7-year loan
- Option 2 – invest the funds representing the UPE on an interest only 10-year loan
- Option 3 – invest the funds representing the UPE in a specific income producing asset or investment.

These investment options are 'safe harbour' options. This means that if the tax affairs of the main trust are reviewed by us and the sub-trust funds are invested in accordance with Options 1, 2 or 3, we will be satisfied that the conditions the Commissioner has set out have been met.

Funds not used for business purposes

The sub-trust can still invest the funds in the main trust via either Options 1 or 2, even if the funds are not used by the main trust for business purposes.

However, interest paid to the sub-trust by the main trust would not ordinarily be deductible to the main trust if the funds borrowed by the main trust are not used for business or other income producing purposes.

Investing in an existing asset held by the main trust

The trustee of the sub-trust can invest the funds representing the UPE in an existing asset (or in a share of an existing asset) held by the main trust using Option 3.

However, this would generally constitute a disposal of, or part of, the existing asset held by the main trust and an acquisition of the same asset by the sub-trust. Such a transaction may, for example, trigger capital gains tax (CGT) consequences.

Repaying loan principal at the end of the investment

The main trust is expected to repay the principal at the end of the term of the investment, in accordance with the investment agreement. Failure to do so may result in a Division 7A deemed dividend to the trustee of the trust.

Early repayment possible

You can repay some or all the principal any time during the term of the investment agreement. There would be no penalties associated with the early repayment of the principal. Interest should only be calculated on the funds actually owing at the time.

Administrative requirements of the sub-trust

Separate TFN for the sub-trust

As a general rule, a trustee who invests the funds in the sub-trust using either Options 1 or 2 in PS LA 2010/4 and satisfies the exemptions in paragraphs 72 and 84 of PS LA 2010/4 will not need to apply for a separate tax file number (TFN) for the sub-trust.

Separate trust deed for the sub-trust

There is no need to have a separate trust deed for the sub-trust. Many trust deeds already provide for the creation of a sub-trust. We strongly recommend you carefully read your trust deed before creating a sub-trust, to ensure it is within the trustee's powers to do so.

Trust deed silent on UPE to be held on sub-trust

We will consider that the trustee has the power to hold the UPE on sub-trust for the private company beneficiary as long as the trust deed contains words to the effect that the trustee has the power to set aside the income of the trust for the exclusive benefit of one or more of the beneficiaries.

If the UPE has been set aside in a manner consistent with paragraphs 50 to 53 of PS LA 2010/4, we will consider (subject to evidence to the contrary) that the UPE is held on sub-trust.

Separate financial accounts or tax return

As a general rule, a sub-trust is a trust estate and would ordinarily be required to lodge a tax return. However, we do not require a sub-trust to create separate sub-trust financial accounts or lodge a separate sub-trust tax return when the trustee decides to place the UPE on a sub-trust and the sub-trust invests all its funds using either Options 1

or 2, as long as the conditions in paragraphs 72 and 84 of PS LA 2010/4 are satisfied.

This is on the basis that both Options 1 and 2 are interest-only investment options involving one payment of annual return each year and the obligation to repay the UPE at the end of the investment period (of 7 or 10 years). These transactions should be readily visible in the financial accounts of the main trust and of the private company beneficiaries.

Accounting treatment

We are not aware of any specific accounting requirement for how the main trust should account for the sub-trust.

Where there is no requirement to produce separate accounts for the sub-trust, and the sub-trust has invested the funds representing the UPE back into the main trust under Options 1 or 2 set out in PS LA 2010/4, it is expected that the main trust would reflect its obligation to repay the money owing to the sub-trust within the liability section of its statement of financial position or balance sheet.

Division 7A complying loan agreement

Instead of implementing a sub-trust arrangement, the trustee can avoid a dividend being deemed under Division 7A if the private company agrees for its UPE to be set-off against a [Division 7A complying loan](#). This means that they would satisfy the UPE, and lend back the funds representing the UPE.

In these circumstances, the private company would not have any subsisting UPE but rather a loan asset owing from the trust.

Example 3 – pay out the entitlement

Company X receives \$1,000 of distributions from Trust T on 30 June 2016 and the amount remains unpaid. Company X and Trust T both have income years ending on 30 June. The trustee of Trust T fails to put the \$1,000 on a sub-trust for the sole benefit of Company X by the lodgment day for the trust's 2016 return.

The trustee must then, in order to avoid Division 7A treating the UPE as a dividend paid by Company X to Trust T, either:

- pay out the \$1,000 to Company X by the lodgment day for the company's 2017 return
- satisfy the UPE and have Company X lend back the funds representing the UPE under a section 109N complying loan agreement.

UPEs created before 16 December 2009

No requirement to pay out pre-16 December 2009 UPEs first

Where a trustee has several UPEs and they were created both before and after 16 December 2009, there is no requirement to pay out pre-16 December 2009 UPEs to the company first.

Pre-16 December 2009 UPEs not Division 7A loans

The Commissioner will not treat any pre-16 December 2009 UPEs as Division 7A loans, even when the UPEs are not placed on sub-trusts for the sole benefit of the beneficiary.

Therefore, there is no need for you to pay out any pre-16 December 2009 UPEs to prevent them being treated as dividends paid by the private company to the main trust. However, you should quarantine or isolate any pre-16 December 2009 UPEs in the books of the trust so they can be clearly identified.

Subdivision EA of Division 7A can still apply if the trust makes a payment or loan to, or forgives the debt of, a shareholder of the private company (or their associate) for as long as there is a UPE of the company to trust income, including any pre-16 December 2009 UPEs.

UPE by a trust to a trust beneficiary

The principles in TR 2010/3 and PS LA 2010/4 apply to UPEs owing by a trust to any entity, including another trust.

Therefore, if Trust A appoints income to Trust B (a trust within the same family group) but does not pay the funds to Trust B, the UPE can amount to financial accommodation and may be a loan for Division 7A purposes unless the conditions in PS LA 2010/4 are satisfied. This is illustrated in Figure 1.

Figure 1

Conditions required to comply with PS LA 2010/4

Division 7A will not automatically apply even though the UPE is a loan for Division 7A purposes. Essentially, a UPE becomes a loan, within the extended definition in these circumstances if the funds representing the UPE are not reinvested for the sole benefit of the beneficiary by the lodgment day of the trust tax return. See paragraphs 46-48 of PS LA 2010/4.

However, it becomes particularly important where Trust B similarly appoints an amount of income, and does not pay the amount, to a private company beneficiary within the same family group. The paragraphs below highlight two scenarios as examples where Division 7A may potentially apply.

Example 4– potential application of Subdivision EA

Trust A, Trust B and PrivCo C are part of a family group. Trust A and Trust B have the same corporate trustee. Trust A and Trust B are both shareholders of PrivCo C.

In June 2016, Trust A appoints all its net income, but does not pay the amount to Trust B. Similarly, Trust B appoints all its net income, but does not pay the amount to PrivCo C. Before the lodgment day for Trust B's 2016 tax return, the trustee decides to put the UPE owing by Trust B to PrivCo C on a sub-trust for the sole benefit of PrivCo C, using one of the investment options in PS LA 2010/4.

The trustee decides not to put the UPE owing by Trust A to Trust B on a sub-trust before the lodgment day of Trust A's 2016 tax return. The trustee of Trust B is aware of this but does not call for payment of its UPE, or for the funds representing that UPE, to be held for its sole benefit. As a result, the UPE would constitute financial accommodation and therefore a loan by Trust B to Trust A for Division 7A purposes.

The arrangement is illustrated in Figure 2.

Figure 2

Potential application of Subdivision EA

Subdivision EA of Division 7A applies to certain trustee payments, loans and debt forgiveness made in favour of a shareholder (or

associate of a shareholder) of a private company on or after 12 December 2002. Subdivision EA of Division 7A applies to this arrangement to treat PrivCo C as having paid an assessable dividend to Trust A in the 2016–17 income year.

This will occur unless either:

- an exception in Subdivision D of Division 7A applies
- the loan is fully repaid before the 2017 lodgment day of the notional company (that is, the UPE has been paid out to Trust B by that date)
- the notional company has insufficient distributable surplus such that section 109Y will operate.

Example 5: potential application of Subdivisions EA and EB

As with Scenario 1, Trust A, Trust B and PrivCo C are part of a family group. Trust A and Trust B have the same corporate trustee. Trust A, Trust B and Individual D are shareholders of PrivCo C.

In June 2016, Trust A appoints all its net income, but does not pay the amount to Trust B. Similarly, Trust B appoints all its net income, but does not pay the amount to PrivCo C.

On 1 July 2016, the trustee for Trust A decides to provide an interest-free loan to Individual D.

Before the lodgment day for the 2016 trust returns, the trustee decides to put the UPE owing by Trust B to PrivCo C on a sub-trust for the sole benefit of PrivCo C using one of the investment options in PS LA 2010/4. The trustee also puts the UPE owing by Trust A to Trust B on a sub-trust for the sole benefit of Trust B using one of the investment options in PS LA 2010/4.

The arrangement is illustrated in Figure 3.

Figure 3

 Potential application of Subdivisions EA and EB

Subdivision EA of Division 7A applies to certain trustee payments, loans and debt forgiveness made in favour of a shareholder (or associate) of a private company on or after 12 December 2002.

From 1 July 2009, Subdivision EA can apply to (among other things) payments and loans from a trust of which a private company is taken to have an unpaid entitlement to income. Subdivision EB was introduced to ensure that the operation of Subdivision EA cannot be circumvented by interposing an entity either:

- between a trust making a payment or loan and the entity receiving the payment or loan (who is a shareholder of the private company or their associate)
- between a trust and a private company that holds an unpaid present entitlement to an amount from the net income of the trust.

Section 109XI of Subdivision EB may apply in this arrangement to deem PrivCo C to be presently entitled to an amount of the net income of Trust A. Subdivision EA of Division 7A would then apply to treat PrivCo C as having paid an assessable dividend to Individual D in the 2017 income year.

This will occur unless either:

- an exception contained in Subdivision D of Division 7A applies
- the loan is fully repaid before the notional company's 2017 lodgment day (PrivCo C is treated as a notional company in these circumstances)
- the notional company has insufficient distributable surplus such that section 109Y will operate.

For more information about factors the Commissioner will take into account in determining the amount of any deemed entitlement arising under section 109XI of the ITAA 1936, see [Taxation Determination TD 2011/15](#).

Section 100A reimbursement agreement

It is relevant to consider the operation of both section 100A and Division 7A in situations where a private company beneficiary makes its trust entitlement available to the trustee.

Practical Compliance Guideline PCG 2022/2 *Section 100A reimbursement agreements – ATO compliance approach* (Guideline) describes the circumstances in which a private company beneficiary making its trust entitlement available to the trustee on complying Division 7A terms will be considered to present a low risk of section 100A applying. We will not devote compliance resources to these arrangements other than to confirm they are in the green zone of the Guideline.

In situations outside the green zone, if the private company beneficiary's trust entitlement arises out of a [reimbursement agreement](#) and section 100A applies, the effect of section 100A will undo the entitlement and deem it not to exist. The share of trust net income which would have been taxable to the beneficiary will instead be taxed to the trustee. The deeming by section 100A will mean there is no financial accommodation between the beneficiary and the trustee to which Division 7A will apply. This interaction is described in more detail in Taxation Ruling [TR 2022/4](#) *Income tax: section 100A reimbursement agreements*.

[Contact us](#) if you need further assistance.

Commissioner's discretion under section 109RB

You can apply in writing to the Commissioner of Taxation to exercise their discretion under section 109RB to disregard a deemed dividend that has arisen under Division 7A.

For more information about this discretion, see:

- [Division 7A – the Commissioner's discretion under section 109RB](#)
- [TR 2010/8](#) *Income tax: application of subsection 109RB(1) of the Income Tax Assessment Act 1936*
- [PS LA 2011/29](#) *Exercising the discretion under section 109RB of Division 7A.*

Closely held corporate limited partnerships

How to apply division 7A arrangements - closely-held corporate limited partnership to partners or associates.

Last updated 8 February 2017

General corporate limited partnerships are treated as companies for taxation purposes. For example, a reference to a share includes a reference to an interest in a corporate limited partnership. A reference to a shareholder includes a reference to a partner in a corporate limited partnership.

As such, Division 7A applies to loans, payments and debts forgiven by **closely held** corporate limited partnerships to its partners or associates of its partners.

The total of all dividends a corporate limited partnership is taken to pay under Division 7A is limited to the distributable surplus of the corporate limited partnership for that income year.

See also

- [TA 2007/5 – Arrangements designed to avoid the operation of Division 7A through the use of a Corporate Limited Partnership](#)
- [Division 7A - payments by private companies](#)
- [Division 7A - loans by private companies](#)
- [Division 7A - debt forgiveness by private companies](#)

Corporate limited partnerships

A corporate limited partnership is a limited partnership that is an association of persons (other than a company) carrying on business as partners, where the liability of at least one of those persons is limited.

A corporate limited partnership is comparable to a limited liability company in that there are limited partners who are similar to

shareholders in a company - they do not take part in the management of the business, and their liability generally is limited to the extent of their investment.

The following limited partnerships are not corporate limited partnerships:

- a venture capital management partnership
- a venture capital limited partnership
- an early stage venture capital limited partnership
- an Australian venture capital fund of funds.

These limited partnerships are treated as ordinary partnerships (subject to special rules about the use of their losses) under the income tax law.

For a partnership to be a corporate limited partnership, it needs to meet the requirements of the relevant state law.

For more information, see [TD 2008/15](#) *Income tax: can an unincorporated association of persons acting only in Australia who do not carry on a business in common with a view to profit be a corporate limited partnership within the meaning of section 94D of the Income Tax Assessment Act 1936?*

Closely-held corporate limited partnership

A corporate limited partnership is considered to be **closely held** for the purposes of Division 7A if it has fewer than 50 members or an entity has, directly or indirectly, and for the entity's own benefit, an entitlement to a 75% or greater share of the income or capital of the partnership.

Example 1

Kariba LP is a limited partnership that has one general partner and three limited partners. Kariba LP is a corporate limited partnership. As Kariba LP has less than 50 members, it is subject to the application of Division 7A from the 2009-10 income year.

Example 2

Michael has an entitlement to an 80% share of the income of two fixed trusts. The two trusts have between them an entitlement to 100% of the income of a corporate limited partnership. For the purpose of determining whether there is a closely-held corporate limited partnership, Michael has, indirectly and for his own benefit, an entitlement to a 75% or greater share of the income of the partnership.

Division 7A and closely-held corporate limited partnerships

From 1 July 2009, Division 7A applies to **closely held** corporate limited partnerships in the same way that it applies to private companies.

A partner in a corporate limited partnership is taken to be a shareholder. This means that associates of a partner of a closely held corporate limited partnership will be treated as associates of a shareholder for the purposes of Division 7A.

Therefore, a partner or associate of a partner in a closely-held corporate limited partnership which directly or indirectly (for example, through an interposed entity) receives a payment or loan from, or has a debt forgiven by, a closely-held corporate limited partnership, the closely-held corporate limited partnership may be taken under Division 7A to pay the partner or associate of the partner a dividend. Any dividend paid will be limited to the distributable surplus of the closely held corporate limited partnership. The partner or associate of the partner may need to include this amount in their tax return as an unfranked dividend.

Distributable surplus

A private company's distributable surplus for an income year is worked out as follows:

When considering the formula for closely held corporate limited partnerships, 'net assets' means the amount of the partnership's

assets at the end of the partnership's year of income (according to its accounting records) that exceed the sum of the present legal obligations of the partnership and amounts relating to the following provisions:

- provisions for depreciation
- provisions for annual leave and long service leave
- provisions for amortisation of intellectual property and trademarks.

'Paid up share value' is the paid up share capital of a company at the end of its year of income. For a closely held corporate limited partnership this is a reference to the total of the partners' interests in the partnership (because a reference to a share includes a reference to an interest in the partnership).

Next step

- [Contact us](#) – if you need to know more.

QC 23184

Distributable surplus

How to calculate the distributable surplus of a private company and its effect on amounts treated as dividends.

Last updated 8 February 2017

About deemed dividends

The total of all deemed dividends that a private company is taken to pay under Division 7A is limited to its distributable surplus for that income year. The amount of a private company's distributable surplus for its income year is calculated according to the distributable surplus formula.

Next step

- Visit the [legal database](#) to find the latest information about
 - Distributable surplus formula

- Division 7A amounts
- Net assets
- Commissioner's power to substitute
- Non-commercial loans
- Non-commercial loan repayments
- Paid up share value
- Written statement.

See also

- [Division 7A – closely held corporate limited partnerships](#)
- [TD 2009/5](#) *Income tax: Division 7A: in exercising the discretion under subsection 109Y(2) of Division 7A of Part III of the Income Tax Assessment Act 1936 to substitute an appropriate value for a private company's assets, can the Commissioner take into account the value of the company's assets not shown in the company's accounting records?*
- [TD 2012/10](#) *Income tax: when is income tax of a private company a 'present legal obligation' for the purposes of the distributable surplus calculation under subsection 109Y(2) of Division 7A of Part III of the Income Tax Assessment Act 1936?*
- [Division 7A - debt forgiveness by private companies](#)
- [Division 7A - franking implications](#)

Retained earnings and distributable surplus

A private company's retained earnings and its distributable surplus will not necessarily be the same.

For example, when working out a private company's distributable surplus the definition of 'net assets' provides that only present legal obligations and certain provisions are taken into account. In contrast, a company may choose to include **additional** provisions for accounting purposes. If so, the retained earnings figure in a private company's balance sheet may be less than the distributable surplus.

Effect of distributable surplus on dividends

The total amount treated as dividends under Division 7A in an income year is limited to the private company's distributable surplus.

If the total amount that would be treated as dividends (if not for this limitation) is greater than the private company's distributable surplus, the amount of the provisional dividend is reduced to reflect the lower amount of the distributable surplus as follows:

 Provisional dividend multiplied by distributable surplus for the income year divided by total of provisional dividends for the income year

Example 1 – distributable surplus limits shareholder's dividend

On 3 March 2015, DJ's Pty Ltd loaned \$500 to its shareholder Jenn. Assuming the \$500 loan is treated as a dividend, on 30 June 2015 DJ's Pty Ltd is taken to pay a dividend of \$500 to Jenn.

For the income year ended 30 June 2015, DJ's Pty Ltd has a distributable surplus of \$900. The value of loans and payments by DJ's Pty Ltd to shareholders and its associates which would be treated as dividends for that year (including Jenn's loan) is \$1,000. This is the total of provisional dividends.

The amount that is therefore treated as a dividend to Jenn is \$450, worked out as follows:

 \$500 multiplied by \$900 divided by \$1,000 equals \$450

This example shows the calculation of the amount treated as a dividend and illustrates the proportional reduction of provisional dividend where the distributable surplus is less than the total of provisional dividends.

Jenn includes \$450 in her 2015 tax return as an unfranked dividend.

Requirement to issue a written statement

If an amount treated as a dividend is reduced because it is limited to the private company's distributable surplus, the private company must issue a written statement to the shareholder or shareholder's associate.

The written statement must state the private company's distributable surplus and the total of dividends, called the 'provisional dividends', for its income year.

The written statement will allow the shareholder or their associate to work out by how much each dividend is to be reduced.

Next step

- [Contact us](#) – if you need to know more.

QC 17350

Franking implications

Read about private companies are treated as paying dividends to shareholders and shareholders' associates.

Last updated 8 February 2017

In general, amounts treated as dividends under Division 7A are not frankable, and the recipient is not entitled to a tax offset in relation to the dividend.

A franking account is an account that a corporate tax entity (for example, a company) maintains to keep a record of the income tax credits (known as franking credits) that it can pass on to its shareholders.

A franking credit arises in the franking account when a corporate tax entity makes a payment of a pay as you go (PAYG) instalment or income tax, receives a franked distribution (directly or indirectly) or incurs a liability to pay franking deficit tax. A franking debit arises in the franking account in various circumstances, including where a corporate tax entity receives a refund of income tax or makes a franked distribution.

See also

- [Imputation - the franking account](#)
- [Imputation - franking a distribution](#)
- [Imputation - franking account tax return](#)

Some exclusions may apply to Division 7A amounts incurred

Where an amount treated as a dividend under Division 7A arose because of an honest mistake or inadvertent omission, the Commissioner may exercise a discretion to allow the relevant private company to frank the deemed dividend. Where the Commissioner exercises the discretion and the private company franks the deemed dividend, the private company's franking account will be debited as if it had franked an ordinary distribution.

See also

- [Division 7A - exercise of Commissioner's discretion under section 109RB](#)
- [Imputation - the benchmark and anti-streaming rules](#)

Set off of subsequent dividends

If a Division 7A dividend paid by a private company to a shareholder or their associate is wholly or partly set off by a subsequent dividend the company pays to that shareholder or associate, the lesser of the following is not treated as a dividend:

- the unfranked amount of the subsequent dividend
- the amount that is set off.

The balance (if any) of the subsequent dividend is still a dividend, so the shareholder or their associate retain any franking credits allocated to it.

Effect on the private company

However, the whole amount of the subsequent dividend is subject to the normal franking rules, so the company must frank the dividend to the required extent (see [Imputation - the benchmark and anti-streaming rules](#)).

Example 1

In the income year ended 30 June 2015, Rossi Pty Ltd makes a loan of \$1,000 to Alana, a shareholder of Rossi Pty Ltd. This is treated as a Division 7A dividend paid to Alana on 30 June 2015. In the income year ended 30 June 2016, Rossi Pty Ltd distributes an unfranked dividend (the subsequent dividend) of \$1,000 to Alana which is set off against her \$1,000 loan. Alana had not made any repayments of the loan.

The effect of the set off is that no amount of the subsequent dividend of \$1,000 is treated as a dividend. Accordingly, Alana is not required to include the subsequent unfranked dividend in her 2016 tax return.

Example 2

Assume the same facts as in **Example 1** except that the subsequent dividend is a frankable distribution with a franking percentage of 35%.

The effect of the set off is that the unfranked amount of the subsequent dividend (that is, \$650) is not treated as a dividend and is not included in Alana's 2016 tax return. The franked amount of \$350 is included in her assessable income along with the franking credit allocated to the dividend of \$150 (calculated as $\$1,000 \times 30/70 \times 35\%$). Alana is also entitled to a tax offset of \$150.

Next step

- [Contact us](#) – if you need to know more.

Marriage or relationship breakdown – dividends and deemed dividends

See when amounts from a private company are taxed as dividend or deemed dividend, due to marriage/relationship breakdown.

Last updated 7 January 2021

A dividend or a deemed dividend may arise when a payment of money or a transfer of property is made by a private company to a shareholder or their associate because of a marriage or relationship breakdown. This dividend or deemed dividend must be included in the shareholder or their associate's assessable income.

Apart from one exception, these rules have always applied. The one exception is where the Family Court requires the private company to pay money to a spouse who is **not** a shareholder. In that circumstance, the rules only apply where the obligation to pay the money was imposed by the Family Court on or after 30 July 2014.

Throughout this fact sheet, a reference to:

- a marriage includes a de facto relationship
- a spouse includes a former spouse and a party to a de facto relationship
- an order of the Family Court includes a consent order.

See also:

- [TR 2014/5 Income tax: matrimonial property proceedings and payments of money or transfers of property by a private company to a shareholder \(or their associate\)](#)
- [Marriage or relationship breakdown and transferring of assets](#)

Family law obligation

For the purposes of Division 7A, a family law obligation arises when a private company pays money or transfers other property to a person

because of a marriage or relationship breakdown.

The payment or transfer of property may arise because of an order of the Family Court that is made against either:

- the private company
- one of the parties to the marriage.

An ordinary dividend under a family law obligation

An ordinary dividend arises in any circumstance in which a private company pays money or other property because of a family law obligation to a spouse who is a shareholder of the private company.

Example 1:

Mal, Justine and a private company are parties to matrimonial property proceedings before the Family Court. Mal and Justine are both shareholders of the private company. The Family Court makes an order requiring the private company to pay Justine \$250,000.

On 30 April 2015, the private company makes the payment of \$250,000 to Justine.

The payment of \$250,000 is an ordinary dividend to Justine for the 2015 tax year.

Example 2:

Tim, Helene and a private company are parties to matrimonial property proceedings before the Family Court. Tim and Helene are both shareholders of the private company. The Family Court makes an order requiring the private company to transfer a rental property with market value of \$1,000,000 to Tim.

On 30 April 2015, the private company makes the transfer of the rental property to Tim.

The market value of the rental property (\$1,000,000) is an ordinary dividend to Tim for the 2015 income year.

A deemed dividend under a family law obligation

A deemed dividend arises in any circumstance in which a private company pays money or other property because of a family law obligation to a spouse who is not a shareholder of the private company.

Example 3:

Sam, Martha and a private company are parties to matrimonial property proceedings before the Family Court.

Martha is not a shareholder of the private company.

The Family Court makes an order for the private company to pay Martha \$100,000. On 30 June 2015, the private company makes the payment of \$100,000 to Martha.

The payment of \$100,000 is a deemed dividend to Martha for the 2015 income year.

Example 4:

Max, Denise and a private company are parties to matrimonial property proceedings before the Family Court. Denise is the sole shareholder of private company.

The Family Court makes an order for the private company to transfer a rental property with market value of \$500,000 to Max. On 30 June 2015, the private company makes the transfer of the rental property to Max.

The market value of the rental property (\$500,000) is a deemed dividend to Max for the 2015 income year.

If you receive an ordinary dividend

If you are a shareholder of a private company and have received a payment of money from that private company under a family law obligation, you must include in your assessable income the amount of money received

If you are a shareholder of a private company and have received a transfer of property from that private company under a family law obligation, you must include the market value of the property in your assessable income.

If you receive a deemed dividend

If you are the associate of a shareholder of a private company and have received a payment of money or a transfer of property from that private company under a family law obligation, and the private company has a distributable surplus that is equal to or more than your deemed dividend, you include the amount of your deemed dividend in your assessable income.

If you are the associate of a shareholder of a private company and have received a payment of money or a transfer of property from that private company under a family law obligation, and the private company has a distributable surplus less than your deemed dividend, you include the amount of the distributable surplus in your assessable income.

Example 5:

Assume the same facts as example 4 except the private company has a distributable surplus of \$300,000.

As the distributable surplus (\$300,000) is less than the market value of the property (\$500,000), only \$300,000 is included in Max's assessable income for the 2015 income year.

See also:

- [Division 7A - distributable surplus](#)

Franking credits

You can claim a franking credit regardless of whether you receive an ordinary dividend or a deemed dividend received as a result of

marriage or relationship breakdown, provided the private company has franked the dividend.

Example 6:

Assume the same facts as example 5 except the private company franks the deemed dividend such that Max becomes entitled to a franking credit of \$90,000.

Max must include the following in assessable income:

- a franked dividend of \$300,000
- franking credit of \$90,000.

Max is also entitled to claim a tax offset of \$90,000.

See also:

- [Imputation – overview of the imputation system](#)

Adjustments to the cost base

Adjustments need to be made to the cost base (or reduced cost base) of shares held in a private company for capital gains tax purposes, where:

- a capital gains tax event happens in relation to those shares;
- the shares were held at a time when the private company paid a dividend (or was taken to pay a deemed dividend) in respect of a transfer of property; and
- that transfer of property arose because of a family law obligation.

A family law obligation is one which arises from an order of the Family Court (including a consent order).

See also:

- [TR 2014/5 – Income tax: matrimonial property proceedings and payments of money or transfers of property by a private company to a shareholder \(or their associate\)](#)
- [Capital gains tax](#)
- [Marriage or relationship breakdown and transferring assets](#)

When an adjustment to the cost base (or reduced cost base) is to be made

An adjustment is made to the cost base (or reduced cost base) of shares only when the reason for the dividend (or deemed dividend) is a transfer of property by the private company arising from a family law obligation. These cost base (or reduced cost base) adjustment rules have applied in this way since 1 July 1997.

Example 7

Tim, Helene and a Private Company are parties to matrimonial property proceedings before the Family Court. Tim and Helene are both shareholders of the Private Company. The Family Court makes an order requiring the Private Company to transfer a rental property with market value of \$1,000,000 to Tim.

On 30 April 2014, the Private Company makes the transfer of the rental property to Tim.

The market value of the rental property (\$1,000,000) is an ordinary dividend to Tim for the 2014 tax year.

On 30 June 2015, Tim sells his shares to a third party. For capital gains tax purposes, an adjustment is made to the cost base (or reduced cost base) of the shares because the transfer of property was the cause of the ordinary dividend.

Different cost base (or reduced cost base) adjustments

Different cost base (or reduced cost base) adjustments arise depending upon whether or not the recipient of the transfer of property is a shareholder of the private company.

Where the recipient of the transfer of property is a shareholder, the following adjustments are made:

1. the cost base (or reduced cost base) of the shares are reduced by the fall in their market value caused by the transfer of property from the private company to the shareholder; and
2. the cost base (or reduced cost base) of the shares are increased by the amount of the dividend assessed to the shareholder because of

the transfer of property.

Example 8

Assume the same facts as Example 1.

The adjustments made to the cost base (or reduced cost base) of Tim's shares are:

The cost base (or reduced cost base) is reduced by \$500,000 being $\frac{1}{2}$ of the value of the rental property at the time of transfer. NB: $\frac{1}{2}$ of the value is used as Tim held only $\frac{1}{2}$ of the shares in the private company; and

The cost base (or reduced cost base) is increased by \$1,000,000 being the amount of the ordinary dividend assessed to Tim because of the transfer of the rental property.

Where the recipient of the transfer of property is not a shareholder of the private company, the adjustment to cost base (or reduced cost base) of shares is only the fall in their market value caused by the transfer of property from the private company.

Example 9

Assume the same facts as Example 1 except that Tim was **not** a shareholder of the private company and Helene held 100% of the shares in the private company. The adjustment made to the cost base or reduced cost base of Helene's shares is as follows:

The cost base (or reduced cost base) of Helene's shares is reduced by \$1,000,000 being the value of the rental property at the time of transfer. NB: 100% of the value of the rental property is used as Helene held all of the shares in the private company.

The cost base (or reduced cost base) of shares held by other shareholders in the private company is also adjusted; it is reduced by the fall in the market value caused by the transfer of property from the private company.

Example 10

Assume the same facts as Example 1.

The adjustment made to the cost base (or reduced cost base) of Helene's shares is as follows:

The cost base (or reduced cost base) is reduced by \$500,000 being $\frac{1}{2}$ of the value of the rental property at the time of transfer.
NB: $\frac{1}{2}$ the value is used as Helene held only $\frac{1}{2}$ of the shares in the private company.

Next step:

- [Contact us](#) – if you need to know more

QC 42283

The Commissioner's discretion under section 109RB

Learn about the commissioner's discretion to disregard the operation of Div 7A or allow a deemed dividend to be franked.

Last updated 14 October 2024

Taxpayers may apply to seek the Commissioner's discretion to disregard the operation of Division 7A or to allow a deemed dividend to be franked.

Once a Division 7A breach has been identified, the decision making process to determine if the discretion can be exercised may commence.

The decision whether or not to exercise the Commissioner's discretion is a two step process:

STEP 1

Determine whether the relevant breach of Division 7A resulted from an honest mistake or inadvertent omission.

Only if you are satisfied that the answer at step 1 is YES can you proceed to step 2.

STEP 2

Determine whether the Commissioner should exercise his discretion to disregard a deemed dividend, or allow that dividend to be franked.

Generally a decision by the Commissioner to disregard a deemed dividend will be made on the condition that specified corrective action is undertaken within a specified time.

In this fact sheet, a reference to a shareholder or their associate is also a reference to:

- an entity that has been a shareholder, or
- an entity that has been an associate of a shareholder.

How can an exercise of the Commissioner's discretion be requested?

Generally, you must apply to the Commissioner to exercise his discretion to disregard the deemed dividend or to allow the private company to choose to frank the dividend. The application would normally be in writing and include all the information necessary for the Commissioner to make a decision. There is no prescribed or standard application form.

Any request for an exercise of the Commissioner's discretion should include sufficient information to demonstrate to the Commissioner that the failure to comply with one or more of the provisions of Division 7A was the result of an honest mistake or inadvertent omission.

What factors does the Commissioner consider for exercising the discretion?

You will need to demonstrate to the Commissioner that the failure to meet the requirements of Division 7A was the result of an honest mistake or an inadvertent omission.

Once it has been established that there was an honest mistake or inadvertent omission, the Commissioner is able to decide whether or not to exercise the discretion. The Commissioner must have regard to

factors specified in the legislation. The respective weighting of each factor depends on the particular circumstances of each entity requesting the exercise of the discretion.

The factors specified in the legislation are:

- the circumstances that led to the mistake or omission that caused the deemed dividend to arise
- the extent to which action had been taken and how quickly action had been taken to correct the mistake or omission
- whether Division 7A had previously operated in respect of the relevant entities and in what circumstances this had occurred, and
- any other matter that the Commissioner considers relevant.

In your request for the exercise of the discretion, you should address each of the first three factors to the extent that they are relevant to your individual circumstances. You should also include any other matters that you consider relevant, such as the amount of the dividends involved. The Commissioner may also request information that he considers relevant to the exercise of the discretion in your circumstances.

Corrective action

Certain amounts paid, lent or forgiven by a private company to shareholders or their associates may be treated as being a deemed dividend for tax purposes under Division 7A of the *Income Tax Assessment Act 1936* subject to some exclusions. However, to encourage compliance we have discretion to disregard this outcome if the deemed dividend arises as a result of an honest mistake or inadvertent omission.

When deciding whether or not to exercise discretion, one of the factors we consider is the extent to which corrective action has been taken and, if so, how quickly that action was taken. Alternatively, if corrective action has not been fully undertaken prior to the ATO's discretion being sought, we may exercise our discretion subject to the condition that corrective action is taken within a specified time period.

Corrective action is significant as the law requires the Commissioner to consider:

- the extent to which the private company, shareholder or associate or any other entity whose conduct contributed to the failure to comply has taken action to try to correct the mistake or omission, and
- if so, how quickly the action was taken.

There are other factors that the Commissioner must consider. The respective weighting of each factor depends upon the actual circumstances of each case.

What is corrective action?

Appropriate corrective action should put the relevant parties in the position that they would have been in if Division 7A had not been breached.

Corrective action includes:

- converting the payment, loan or debt forgiveness to a loan that complies with section 109N of the *Income Tax Assessment Act 1936* ('section 109N')
- making catch-up or shortfall minimum yearly repayments as if the transaction always complied with section 109N (plus interest compounded to reflect non-payment in earlier years).

See also:

- [PSLA 2011/29](#)

Example

In the 2013 income year, ABC Pty Ltd loaned \$700,000 to an associated trust, the XYZ Trust.

The Commissioner exercised his discretion subject to the following corrective action being taken in the 2016 income year:

- A loan agreement must be entered into commencing in the year in which corrective action is taken and conclude in the year in which it would have concluded had it been entered into at the time the original loan was made. In this case, that would be 2020.

- Under the loan agreement, the interest rate applicable must equal or exceed the benchmark interest rate for the year (these rates are published by the Reserve Bank of Australia).
- XYZ Trust must make catch up repayments of principal and interest in respect of the 2014, 2015, 2016 and 2017 income years.

Calculations

The formula for calculating the minimum yearly repayments that XYZ Trust must make is as follows:

 Minimum yearly repayments

Table 1 below illustrates the minimum yearly repayments that would have been payable had a complying loan agreement been entered into at the time the original loan was made.

Minimum yearly repayments example

Year	Interest Rate	Opening Balance	Interest Amount	MYR	Endir Balar
	%	\$	\$	\$	\$
2014	6.20	700,000	43,400	126,287	617,11
2015	5.95	617,113	36,718	125,300	528,5
2016	5.45	528,531	28,804	123,600	433,7
2017	5.40	433,735	23,422	123,457	333,7
TOTAL INTEREST			132,344		

Table 2 illustrates the amount of catch-up payment that XYZ Trust must make as part of their corrective action (assuming no repayments have been made in any prior year).

Catch-up payment example

Year	Interest Rate	Opening Balance	Interest Amount	MYR	Ending Balance
	%	\$	\$	\$	\$
2014	6.20	700,000	43,400	-	743,400
2015	5.95	743,400	44,232	-	787,632
2016	5.45	787,632	42,926	-	830,558
2017	5.40	830,558	44,850	-	875,408
Catch up Payment Due by 30 June 2017				541,708	333,700
TOTAL INTEREST		175,408			

In both Table 1 and Table 2, the “interest amount” payable in each year is calculated using the benchmark interest rate for each of the relevant years. However, because no repayments have been made in any year, the total “interest amount” payable is compounded in Table 2.

After the catch up payment of \$541,708 is made in the 2017 year (which includes the 2017 minimum yearly repayment), the outstanding balance is what it would have been had a complying loan agreement been put in place at the commencement of the loan. The interest component of the catch up payment would be included in the assessable income of ABC Pty Ltd in the 2017 year.

See also:

- [PS LA 2011/29: Exercise Commissioner's discretion under section 109RB](#)

Consequences of the Commissioner using his discretion

Disregard a deemed dividend

The Commissioner may decide to disregard the deemed dividend that otherwise arises under Division 7A.

The Commissioner may make his decision subject to a condition that:

- the shareholder, associate of the shareholder, or any other entity must make specified payments to the private company or another entity within a specified time – for example, an amount equal to the minimum yearly repayments that would have been made if all the conditions of Division 7A had been complied with, and/or
- a specified requirement of Division 7A be met within a specified time – for example, that the full amount of any payments made to a shareholder be converted into a loan that satisfies all the requirement set out in section 109N for the income year in which the loan was made.

If these conditions are not complied with by the specified timeframe, the deemed dividend is not disregarded.

See also:

- [The Commissioner's discretion under section 109RB](#)

Allow dividend to be franked

The Commissioner may alternatively decide that the private company may choose to frank the deemed dividend. If the private company does frank the deemed dividend, the private company's franking account will be debited.

The Commissioner's discretion to allow dividends to be franked would only apply where the dividend has been deemed to have been paid to a shareholder and not to an associate of a shareholder.

An amount included as if it was a dividend in the assessable income of an entity under Subdivision EA of Division 7A, is not frankable.

How will I be informed of the exercise of the Commissioner's discretion?

If the discretion is exercised, you will receive written advice that the amount that would otherwise be treated as a deemed dividend is disregarded, or the company will be given permission to frank the dividend.

Where the company is given permission to frank the dividend, the dividend will be assessable income to the shareholder or associate of the shareholder, with the availability of a franking credit.

What if the discretion is not granted?

If the discretion is not exercised you will be advised in writing and the deemed dividend must be included as an unfranked dividend in your income tax return.

If you are dissatisfied with the Commissioner's decision you may lodge an objection to your assessment for the income year in which the deemed dividend arises and the decision will be reviewed. If your objection is unsuccessful, you may appeal the objection decision to the Administrative Review Tribunal.

Examples

While they are not prescriptive, the examples below demonstrate if there may be an honest mistake or inadvertent omission:

Example 1

A private company makes a loan to a shareholder in the 2013-14 income year for \$100,000. In making the loan, a written agreement is prepared and the term of the loan is seven years.

However, after the return for the 2014-15 income tax year has been lodged the shareholder discovers that the company had made a mistake and advised the shareholder of the wrong interest rate when calculating the minimum yearly repayment. The shareholder only made minimum repayments of \$19,000 in 2014-15 instead of the required \$20,000. A deemed dividend has arisen as the repayments were lower than required. Once the shareholder realised the payments were lower than required, he corrected that mistake by paying an additional \$1,000 in the 2015-16 income year. This additional payment meant that the shareholder had now paid an amount equal to the amount that would have been paid if the correct interest rate had been used in the previous income years. The shareholder also immediately advised the Commissioner that lower repayments had been made and requested that the Commissioner exercise the discretion.

Step 1: Did the deemed dividend arise as a result of an honest mistake or inadvertent omission?

It is necessary to show that the lower minimum repayments were the result of an honest mistake regarding the correct amount of those minimum yearly repayments. The attempt by the company to comply with the requirement of Division 7A by having a written agreement and making yearly repayments in respect of the loan are relevant in this context.

Step 2: Factors the Commissioner should consider when deciding to exercise his discretion:

- that there was a loan agreement in place between the company and the shareholder that satisfied all of the requirement of section 109N
- the use of the wrong interest rate to calculate the minimum yearly repayment resulted in a relatively small under payment
- once the shareholder discovered the mistake, the taxpayer took action to promptly advise the Commissioner of the mistake
- the shareholder took steps to correct the mistake and to discharge their legal obligation under the loan agreement to make a minimum yearly repayment of \$20,000.

Decision

- It would be reasonable to conclude that the Commissioner's discretion should be exercised.

Conditions

- It is not necessary to impose conditions because appropriate corrective action has already been taken by the taxpayer.

Example 2

In the 2015--16 income year, the Commissioner undertakes an audit on ABC Pty Ltd. In the course of the audit, the Commissioner discovers that a loan was made to a shareholder in the 2012-13 income year. There was no documentation supporting the loan but loan repayments were made, albeit at a rate that was less than the benchmark rate for the relevant income years. The shareholder thought that loan documentation was not necessary provided the interest charged was commercial in nature.

Since there was no written loan agreement in place before the private company's 2013 lodgment day, a dividend was deemed to have been paid to the relevant shareholder.

The shareholder or the private company (or both) may apply to the Commissioner to exercise his discretion to disregard a deemed dividend. Alternatively, the Commissioner may make a decision under this provision without being asked to do so by the company or shareholder.

Step 1: Did the deemed dividend arise as a result of an honest mistake or inadvertent omission?

In order for the Commissioner to exercise his discretion, it must be established that the failure to enter into a loan agreement that satisfies the requirement of section 109N was the result of an honest mistake or inadvertent omission. In this context, evidence of the shareholder attempting to comply with the intent of Division 7A (for example, by making yearly repayments in respect of the loan) would be relevant.

Step 2: Factors the Commissioner should consider when deciding to exercise his discretion:

- the nature of the two mistakes
 - the level of interest actually charged by the company on the loan
 - the actual making of yearly repayments on the loan for each year since the loan was entered into
- whether Division 7A has operated previously in respect of either the private company or the shareholder.

Decision

- It would be reasonable to conclude that the Commissioner's discretion should be exercised.

Conditions

- A complying loan agreement is executed and the shareholder to make additional payments equal to the difference between

the actual repayments made and the repayments that would have been made including any compounding interest.

Example 3

A business consists of a private company (ABC Pty Ltd) and XYZ trust. Both entities are controlled by Sam and Mel. The trust's beneficiaries are Sam and Mel and they are also shareholders of the company. The trust owns land and buildings that are mortgaged to a financial institution. The company has a loan with a different financial institution. The interest on both loans is tax deductible as the loans are used for income generating purposes.

In the 2015-16 income tax year, the company and the trustee of the XYZ trust decide to consolidate their debts. The company extends its pre-existing loan facility and pays out the loan that the trust has with its bank. The discharge by ABC Pty Ltd of the debt owed by the XYZ trust to the financial institution is a payment under section 109C and, given that the trust estate is an associate of the shareholders of ABC Pty Ltd, Division 7A will deem a dividend to be paid by the private company to the trustee of the XYZ trust as a deemed shareholder in ABC Pty Ltd.

The trustee applied to the Commissioner to exercise his discretion to disregard the deemed dividend as soon as it became aware that Division 7A deemed a dividend to have been paid.

Step 1: Did the deemed dividend arise as a result of an honest mistake or inadvertent omission?

In order for the Commissioner to exercise his discretion, it must first be established that the officers and employees of the private company and the trustee made an honest mistake as to the operation of Division 7A to the debt consolidation.

Step 2: Factors the Commissioner should consider when deciding to exercise his discretion

- the circumstances surrounding the mistake or omission, including the amount of the deemed dividend

- the commercial nature of the transaction between the company and the trust
- that once the taxpayers discovered the problem they brought the matter to the Commissioner's attention.

Decision

- It would be reasonable to conclude that the Commissioner's discretion should be exercised.

Conditions

- As a condition of exercising the discretion, the Commissioner could require that the payment of the debt be treated as a loan by ABC Pty Ltd to the trust, that the loan be in writing and satisfy all of the requirements of section 109N, and that minimum yearly repayments be made for relevant income years that would have been required had the written loan agreement be put in place by the required time.

Example 4

Fred and Jen operated a number of separate businesses through different entities including a private company and a trust. They were the trustees of the trust and the only shareholders and directors of the private company. The beneficiaries of the trust are Fred and Jen and members of their immediate family.

During the 2013-14 income year, the trust was incurring substantial losses due to a downturn in business conditions. As no other source of funds was available, the private company made loans to the trust for working capital purposes during the year.

In preparing the 2013-14 income tax returns, their tax adviser considered the application of Division 7A but mistakenly believed that only loans to individual shareholders would be subject to Division 7A. There was no qualifying section 109N written loan agreement put in place before the lodgment day of the private company's 2013-14 tax return and no loan repayments had been made to the private company. However, the loan is recognised in the balance sheets of the private company and the trust and the loan is minuted along with a note that the trust is envisaged to resume profitability by the 2016-17 year, at which time loan repayments will commence.

Fred and Jen changed tax advisers during the 2015-16 income year and the new tax adviser brought to their attention the Division 7A problem in the 2013-14 year. On finding out about the problem, Fred and Jen wished to correct the mistake and promptly advised the Commissioner. Division 7A had not operated previously in relation to the private company or the trustee.

Step 1: Did the deemed dividend arise as a result of an honest mistake or inadvertent omission?

Step 2: Factors the Commissioner should consider when deciding to exercise his discretion

- the fact that the mistake was the result of a misreading of the legal requirements of Division 7A by a professional adviser
- the relatively short period of time that has elapsed between the year in which the dividend was deemed to be paid and the notification to the Commissioner
- the disclosure of the transaction as a loan in the balance sheets of the private company and trust
- the quantum of the sums involved
- that Division 7A had not operated previously in relation to the private company or the trustee.

Decision

- It would be reasonable to conclude that the Commissioner's discretion should be exercised.

Conditions

- As a condition of exercising his discretion, the Commissioner could require that there be a written loan agreement put in place that satisfied all of the requirements of section 109N and for the trustee to make additional payments equal to the repayments that would have been made if the trustee had satisfied the requirements of section 109E.

Example 5

In the 2015-16 income year, the Commissioner undertakes an audit of EFG Pty Ltd. In the course of the audit, the

Commissioner discovers that an interest free at call loan was made to a shareholder in the 2013-14 income year. There was no documentation supporting the loan and no repayments have been made. Nor was the loan disclosed in the company's books of account. In addition, the loan was made out of income that was not disclosed in the tax return of EFG Pty Ltd for the 2013-14 income year.

Step 1: Did the deemed dividend arise as a result of an honest mistake or inadvertent omission?

On the basis of the objective evidence, the taxpayer has failed to establish that the deemed dividend was the result of an honest mistake or inadvertent omission. Rather it appears that the company has deliberately ignored the operation of Division 7A and has simply sought to distribute undisclosed profits to a shareholder

Step 2: Factors the Commissioner should consider when deciding to exercise his discretion.

Not relevant because Step 1 was not satisfied.

Decision

- It would not be reasonable to conclude that the Commissioner's discretion should be exercised.

Conditions

- In such a situation the pre-requisite for the Commissioner to exercise his discretion has not been satisfied.

Example 6

Fred and his wife Wilma the directors and shareholders of Iron Age Pty Ltd, a private company carrying on metal fabrication work.

Fred and Wilma also operate a separate business that installs metal fencing through a partnership structure.

Fred and Wilma are both in their early 70's.

For many years, Wilma's brother Barney, a sole practitioner completed all accounting work for Fred and Wilma. However, Barney suffered a series of strokes, Fred and Wilma became

concerned that, because of Barney's failing health he may have made mistakes in the private company's income tax returns.

Fred and Wilma then engaged Nick, a tax agent, to review the tax affairs of Iron Age Pty Ltd. They instructed Nick to review the last three tax returns to ensure that they were correct as well as preparing their current tax returns.

Fred and Wilma's concerns are confirmed by Nick, who identifies the loan that the company made to Fred and Wilma's partnership. Fred explains that the loan was to provide working capital during the early stages of the partnership, and that Barney had suggested that the partnership borrow the funds from the company because it would assist the partnership to generate income.

Fred tells Nick that the loan has been repaid, but that no interest had been paid by the partnership. Nick advised Fred and Wilma that the loan had breached Division 7A, and a deemed dividend has arisen because the loan was not placed on Division 7A complying loan terms. Nick advises Fred and Wilma to apply for the Commissioner's discretion under section 109RB to disregard the deemed dividend.

Fred and Wilma instruct Nick to amend the relevant prior year returns. They also ask Nick to request that the Commissioner exercise his discretion under section 109RB. At the time of applying for the discretion, Fred and Wilma have also made a 'catch up' payment of principal, and for interest forgone by the company according to the principles of corrective action. The interest was calculated based on the amount that would have accrued had a compliant section 109N loan agreement been in place.

Decision-making process

Step 1: Did the deemed dividend arise as a result of an honest mistake or inadvertent omission?

- Nick's analysis of Barney's working papers demonstrate a progressive decline in Barney's professional capacity.
- The evidence suggests that the breach of Division 7A occurred as a result of an honest mistake or inadvertent omission, precipitated by Barney's health problems, and therefore subsection 109RB(1) has been satisfied.

Step 2: Will the Commissioner exercise his discretion? (Apply the factors in subsection 109RB(3) to make a determination)

- Fred and Wilma have been proactive in seeking review of prior year returns because they were concerned about Barney's ability to carry out his duties.
- Fred and Wilma instructed Nick to make a voluntary disclosure to the ATO as soon as they were made aware of the Division 7A breach.
- Iron Age Pty Ltd had previously made personal loans to Fred, and on that occasion Barney had drawn up section 109N complying loan agreements, in respect of which minimum yearly repayments had been made. There was therefore a demonstrated attempt to comply with Division 7A in the past.
- There have been no previous instances where Division 7A has been breached by any of the relevant parties.

Decision

- It would be reasonable to conclude that the Commissioner's discretion should be exercised.

Conditions

- It is not necessary to impose conditions pursuant to subsection 109RB(4) because appropriate corrective action has already been taken by the taxpayer.

Next step:

- [Contact us](#) – if you need to know more

QC 19545

Division 7A and fringe benefits tax

When Division 7A and Fringe Benefits Tax Assessment Act 1986 both apply to a payment, loan or debt forgiven.

Last updated 8 February 2017

If a shareholder or an associate of a shareholder in a private company is an employee of that same company, the fringe benefits tax (FBT) provisions, instead of Division 7A, may apply to the payments and other benefits received by the shareholder or associate.

Payments

A payment will not be treated as a dividend under Division 7A where it is made by a private company to a shareholder or an associate of a shareholder, if the payment is made to the individual in their capacity as an employee or an associate of an employee.

This means that for payments, including the transfer of property, FBT can apply.

Superannuation contributions made by a private company for a shareholder or an associate of a shareholder in respect of their employment will not be subject to Division 7A and are generally not subject to FBT.

See also

- [Division 7A - payments by private companies](#)

Loans

Unlike payments, Division 7A applies in preference to FBT to loans made by a private company to a shareholder or their associate. This is the case even if:

- the loan is made to the shareholder or their associate in their capacity as an employee or an associate of an employee, or
- the loan is made in respect of the employment of an employee.

However, any loans not subject to Division 7A may be considered 'loan benefits' provided by an employer to employees and therefore FBT may apply. An employer provides a loan benefit if they give an employee a loan and charge no interest or a low rate of interest. A low rate of interest is one that is less than the FBT benchmark rate of interest. This rate is published each year, usually in April.

From 1 April 2007, a loan that is put on Division 7A complying loan terms will not be treated as a 'loan benefit' for FBT purposes, even if the interest charged is less than the FBT benchmark rate of interest.

See also

- [Division 7A - loans by private companies](#)

Debts forgiven

In general, a forgiveness of debt by a private company in respect of a debt owed by a shareholder or an associate of a shareholder is treated as a dividend under Division 7A, even if:

- the shareholder or their associate owed the debt in their capacity as an employee or an associate of an employee, or
- the forgiveness occurs in respect of the employment of an employee.

To the extent Division 7A does not apply, FBT can apply (for example) to 'debt waiver benefits' provided by an employer to employees. An employer provides a debt waiver fringe benefit if they waive or forgive an employee's debt (other than a genuine bad debt).

Double taxation is avoided because forgiven debts treated as dividends paid to a shareholder or their associates are excluded from the definition of a fringe benefit.

See also

- [Division 7A - Debt forgiveness by private companies](#)

Next step

- [Contact us](#) – if you need to know more

QC 17382

Payments by private companies

Learn when payments by private companies to shareholders and shareholders' associates are treated as dividends.

Last updated 8 February 2017

About Division 7A payments

A private company may be taken to pay a dividend to an entity at the end of the company's income year if it pays an amount to the entity during the year:

- when the entity is a shareholder or an associate of a shareholder of the company, or
- a reasonable person would conclude that the payment was made because the entity was a shareholder or an associate of a shareholder at some time.

The total of all dividends a private company is taken to pay under Division 7A is limited to its distributable surplus for that income year.

See also

- [Division 7A - distributable surplus](#)
- [Meaning of 'associate'](#)

However, Division 7A does not apply to shareholder or associate payments in their capacity as employees. In such situations fringe benefits tax (FBT) may apply instead of Division 7A.

For more information, see [Division 7A and fringe benefits tax \(FBT\)](#).

In this fact sheet, a reference to a shareholder or their associate also refers to:

- an entity that has been a shareholder
- an entity that has been an associate of a shareholder.

Division 7A also applies to certain payments made by trustees to a shareholder (or an associate of a shareholder) of a private company.

For more information, see [Division 7A - trusts](#).

Division 7A also applies to certain payments and loans made by private companies to a shareholder or an associate of a shareholder through interposed entities.

For more information, see [Division 7A - payments and loans through interposed entities](#).

Payments for Division 7A purposes

Watch this video to understand what a payment is for Division 7A purposes.

Media: Division 7A: Payments.

<http://tv.ato.gov.au/ato-tv/media?v=bd1bdiubximf5g>  (Duration: 3:38)

Payments by other entities

Closely-held corporate limited partnerships

In general, income tax law treats corporate limited partnerships as companies. For example, a reference to a share includes a reference to an interest in a corporate limited partnership. A reference to a shareholder includes a reference to a partner in a corporate limited partnership. As of 1 July 2009, Division 7A applies to a **closely-held** corporate limited partnership in the same way it applies to a private company.

See also

- [Taxpayer Alert TA 2007/5](#) *Arrangements designed to avoid the operation of Division 7A through the use of a Corporate Limited Partnership*
- [Division 7A - closely held corporate limited partnerships](#)

Trusts

Division 7A applies to certain payments made by trustees to a shareholder or an associate of a shareholder of a private company where the company is presently entitled to an amount from the net income of the trust estate and the whole of that amount has not been paid by a specified date.

However, the rules do not apply in all cases where there is an unpaid present entitlement.

See also

- [Division 7A - trusts](#)
- [Division 7A - unpaid present entitlement](#)

Interposed entities

Division 7A applies to certain payments made by private companies to a shareholder or their associate through interposed entities.

For more information, see [Division 7A - payments and loans through interposed entities](#).

Exclusions

A payment is **not** treated as a dividend:

- if it is made to another company (and they are not acting in the capacity of trustee)
- if the payment would be included in the shareholder's or their associate's assessable income under a provision of the tax law (other than Division 7A)
- if the payment would be excluded from the shareholder's or their associate's income under a provision of the tax law
- if it is made to the shareholder or their associate in their capacity as an employee or an associate of an employee (fringe benefits tax may apply, see also: [Division 7A and Fringe Benefits Tax](#))
- if it discharges a private company's obligation to pay money to the shareholder or their associate and the payment does not exceed the amount required to discharge the obligation if the shareholder or their associate and the company were dealing at arm's-length
- if it is a distribution made in the course of a liquidator winding-up a company
- if it was made on or after 23 June 2009 to a capital gains tax concession stakeholder under subsection 152-325(1) of the *Income Tax Assessment Act 1997* (a retirement exemption payment)
- if it was for provision of asset payments (other than transfer of property), minor use of company assets, certain payments that would otherwise be allowable as once-only deductions and the use of certain residences.

Example 1: payment on behalf of a shareholder

Cody is a shareholder of Barbarian Pty Ltd. Cody is neither an employee nor an associate of an employee of Barbarian Pty Ltd. Barbarian Pty Ltd pays Cody's gym membership fees. Barbarian Pty Ltd is taken to pay a dividend to Cody because the payment of the fees is made on behalf of a shareholder. The amount of the dividend is subject to Barbarian Pty Ltd's distributable surplus.

If Cody was an employee or an associate of an employee, Fringe benefits tax (FBT) would apply instead of Division 7A.

Example 2: payment to shareholder's associate

On 1 February 2016, Tom Pty Ltd pays \$3,000 towards an overseas trip for Mary. Mary is a daughter of Jerry, who is a shareholder of Tom Pty Ltd. Neither Jerry nor Mary is an employee or an associate of an employee of Tom Pty Ltd.

The payment is to a shareholder's associate. On 30 June 2015, Tom Pty Ltd is taken to pay a dividend of \$3,000 to Mary, subject to Tom Pty Ltd's distributable surplus.

Example 3: discharging an obligation

Helen, a shareholder of Riley Pty Ltd, lends the company \$1,000. Riley Pty Ltd repays the loan by making a payment of \$1,000 to Helen. The payment will not be treated as a dividend because the payment discharges an obligation of Riley Pty Ltd to pay money to Helen and the payment is not more than the arm's-length value of that obligation.

Payment types

Transfer or rights to use property

The definition of 'payment' in Division 7A includes the transfer of property. Property includes land, buildings, vehicles, tools, equipment and shares.

A 'right to use' property can be a payment for Division 7A purposes where that right involves a transfer of property.

For example, a right to use property that is made by way of a lease of real property involves a transfer of property to the lessee and is considered a payment for Division 7A purposes.

Before 1 July 2009, the meaning of 'payment' did not include the use of assets under a licence or other right to use (other than the transfer of property). Such use of an asset was not subject to Division 7A.

Use of assets (other than a transfer of property)

From 1 July 2009, a payment includes:

- the provision of an asset for use by a shareholder or their associate (other than a transfer of property)
- when a company asset is available for use by a shareholder or their associate to the exclusion of the company. It does not matter when the right to use the asset is granted.
- a right to use assets under a licence or lease, but which does not involve a transfer of property.

For more information, see [Division 7A - payments by private companies - use of assets](#).

Marriage or relationship breakdown

Transfers of property and other payments related to a marriage or relationship breakdown are caught by Division 7A. Even though they may be non-voluntary, a deemed dividend may arise.

Generally, payments that fall under Division 7A will be unfranked deemed dividends. For the 2007 and later income years, dividends arising from family law obligations may be frankable by the private company taken to pay the dividend.

Circumstances where deemed dividends may be franked include:

- a court order under the *Family Law Act 1975* or a corresponding foreign law

- a maintenance agreement approved by a court under section 87 of the Act, or a corresponding agreement approved by a court under a corresponding foreign law
- a court order under state, territory or foreign law relating to de facto marriage breakdowns.

Example 4: property transfer on marriage or relationship breakdown

Jack and Stephanie divorce. Stephanie owns and controls private company BCD Pty Ltd. The Family Court orders Stephanie to transfer the private company's motor vehicle to Jack as part of the property settlement.

The dividend may be franked irrespective of whether it was made to a shareholder or associate of the shareholder. The recipient is treated as a member of the private company.

For more information, see [Division 7A - marriage or relationship breakdown - dividends and deemed dividends](#).

Amount of the dividend

The amount of the dividend is the amount paid or credited to the shareholder or their associate by the private company, subject to the private company's distributable surplus.

Amounts treated as dividends under Division 7A are generally unfranked, even though they are taken to be paid out of the private company's profits.

If the payment is a transfer of property, the amount of the dividend is the amount that would have been paid for the transfer by parties dealing at arm's length, less any consideration given by the shareholder or their associate for the transfer. The amount of a payment is nil if the consideration given by the shareholder or their associate is equal to, or greater than, the amount that would have been paid for the transfer at arm's length.

'Dealing at arm's length' means that the parties to the transaction are dealing with each other in a manner as independent parties would

normally do, so that the outcome of their dealing is a matter of real bargaining. An important element of an arm's length transaction is that the parties have acted severally and independently in forming their bargain so that there is no question of a conflict of interest.

Where a deemed dividend arises because of an honest mistake or inadvertent omission, the shareholder or their associate may request the exercise of the Commissioner's discretion to disregard the deemed dividend (subject to certain conditions) or allow the private company to frank the dividend.

Example 5: property transfer with amount paid by shareholder

On 3 January 2015, Goldfinger Pty Ltd gives office furniture to Renee, a shareholder who is not an employee or an associate of an employee of the company. The arm's length market value of the furnishings on that date is \$5,000. When the property was transferred, Renee paid Goldfinger Pty Ltd \$100 for the transfer costs.

On 30 June 2015, Goldfinger Pty Ltd is taken to pay a dividend to Renee. The amount of the payment is equal to \$5,000 for the furnishings, less \$100 paid by Renee for the transfer. Goldfinger is taken to pay a dividend of \$4,900 to Renee, subject to Goldfinger Pty Ltd's distributable surplus.

See also

- [Division 7A - franking implications](#)
- [Division 7A - payments by private companies - use of assets](#)
- [Market valuation for tax purposes](#)
- [Division 7A - the Commissioner's discretion under section 109RB](#)

Corrective action

Converting payments to a loan

A payment that is converted to a loan before the private company's lodgment day is treated as a complying loan.

A private company's 'lodgment day' is the earlier of the due date for lodgment or the date of lodgment of the company's tax return for the income year in which the loan is made.

Example 6: convert payment to a complying loan

In the 2015 income year, XYZ Pty Ltd pays the petrol expenses of a vehicle owned by a shareholder Sally. Sally is not an employee of the company and is under no express or implied obligation to repay the amount. Sally and XYZ Pty Ltd have until before the lodgment day of the company's 2015 income tax return to convert the payment into a loan and repay it, or enter into a written agreement that meets the maximum term and minimum interest rate criteria for a loan to be a complying loan,

XYZ Pty Ltd may need to undertake a journal entry in its accounting records to reflect the loan and reverse what may have been recorded as an expense in the financial statements for the 2015 income year. If these have been finalised, an adjustment to retained earnings may be required.

For more information, see [Division 7A - loans by private companies](#).

Next step

[Contact us](#) – if you need to know more.

QC 17340

Loans by private companies

How Division 7A applies to loans made by private companies to shareholders, and associates of shareholders.

Last updated 2 July 2026



Bendel case - High Court decision

We're reviewing the content on this page as a result of a recent court decision. Refer to our [Decision Impact Statement](#) for more information.

Meaning of 'loan' under Division 7A

Division 7A extends the meaning of 'loan' to include:

- an advance of money
- a provision of credit, or any other form of financial accommodation
- a payment for a shareholder or their associate, if they have an obligation to repay the amount whether it's
 - on their account
 - on their behalf
 - at their request
- a transaction (whatever its terms or form) that is the same as a loan of money.

A loan is considered to be made at the time the amount is paid either as an ordinary loan, or if any of these are done in relation to a shareholder or an associate.

Example: loan to a shareholder

Terry Pty Ltd loans \$20,000 to Ann, a shareholder of Terry Pty Ltd. The money is loaned to Ann on the basis that she pays it back when she can. The \$20,000 is a loan from Terry Pty Ltd to Ann because it is an advance of money, and Division 7A may apply.

If a private company makes one or more loans to a shareholder or their associate in an income year, it may be taken to make an [amalgamated loan](#).

If a loan is made by way of a promissory note, it is a provision of credit or a form of financial accommodation, and Division 7A may apply.

Example: promissory note to a shareholder

Lucas Pty Ltd provides \$10,000 to Belinda, a shareholder of Lucas Pty Ltd, by way of a promissory note and under an agreement with Lucas Pty Ltd, Belinda is obliged to repay the amount. The \$10,000 is a loan from Lucas Pty Ltd to Belinda and Division 7A may apply.

If a private company beneficiary, in respect of a [trust entitlement](#) which is unpaid (unpaid present entitlement), provides financial accommodation to the trustee of a trust, it will be taken to make a loan to the trustee of the trust for Division 7A purposes.

Loans by other entities

Loans made by other entities may also have Division 7A apply, such as:

- closely-held corporate limited partnerships
- trusts
- interposed entities.

Closely-held corporate limited partnerships

Generally, [closely-held corporate limited partnerships](#) are treated as companies for income tax purposes.

For example, a reference to a:

- share includes a reference to an interest in a corporate limited partnership
- shareholder includes a reference to a partner in a corporate limited partnership.

Division 7A applies to a closely-held corporate limited partnership in the same way it applies to a private company.

For more information, see [Taxpayer Alert TA 2007/5](#) *Arrangements designed to avoid the operation of Division 7A through the use of a Corporate Limited Partnership*.

Trusts

Division 7A applies to certain payments, loans and debt forgiveness made by trustees to a shareholder or an associate of a shareholder of a private company, where:

- the company is presently entitled to an amount from the net income of the trust estate
- the whole of that amount has not been paid by a specified date.

However, the rules don't apply in all cases where there is an unpaid present entitlement.

Interposed entities

Division 7A applies to certain loans made by private companies to a shareholder or their associate through [interposed entities](#).

Loans that are treated as dividends

A private company may be taken to have paid a dividend at the end of the income year, if it lends an amount during the year, and:

- the borrower is a shareholder, or an associate of a shareholder, of the company
- a reasonable person would conclude that the loan was made because the borrower was a shareholder, or an associate of a shareholder, at some time.

The total of all dividends a private company is taken to have paid under Division 7A is limited to its [distributable surplus](#) for that income year.

A loan will be deemed to be a dividend by Division 7A if it's:

- made to a shareholder or an associate of a shareholder
- not fully repaid before the private company's lodgment day for the year when the loan is made – a private company's lodgment day is the earlier of the due date for lodgment, or the actual date of lodgment of their income tax return for the income year
- not excluded specifically by other sections of Division 7A.

Exclusions

A loan is **not** treated as a dividend if:

- it is made to another company (and that other company is not acting in the capacity of trustee)
- the payment would be included in the shareholder's or their associate's assessable income under a provision of the tax law (other than Division 7A)
- the payment would be excluded from the shareholder's or their associate's assessable income under a provision of the tax law
- it is made in the ordinary course of business and on the usual terms the private company applies to similar loans to entities at arm's length
- the loan has satisfied the minimum interest charge and maximum term requirement and is made or put under a written agreement before the private company's lodgment day
- it is a distribution made in the course of a liquidator winding-up a company
- it is made to purchase shares or rights under an employee share scheme
- it is an amalgamated loan in the year it is made and provided the required minimum yearly repayments are made in the following years
- the loans were made before 4 December 1997 and there has been no variation of terms or amounts since they were made.

Varying the terms of a pre-1997 loan

Loans made before 4 December 1997 are generally not subject to Division 7A.

However, where a loan is varied on or after 4 December 1997 – either by extending the term of the loan or increasing the amount of the loan – the loan will be treated as if it were a new loan entered into on the day it is varied. Therefore Division 7A may apply to this new loan.

Complying loans

A loan is considered to be a 'complying loan' when it meets certain [criteria](#). Additionally, payments made by a private company can be

converted to a complying loan – see [Refinancing loans](#).

When a loan is on a complying agreement, it will be excluded from being a Division 7A dividend.

Media: Division 7A: Complying loans

<https://tv.ato.gov.au/ato-tv/media?v=bd1bdiubxseuzw>  (Duration: 5:49)

Criteria of a complying loan agreement

There are 3 criteria a loan needs to meet to be considered to be a 'complying loan':

- Minimum interest rate.
- Maximum term.
- Written agreements.

Minimum interest rate

The interest rate for each year of the loan must at least equal the [Division 7A – benchmark interest rate](#). The benchmark interest rates are updated annually.

Maximum term

The term of the loan must not exceed the following:

- 25 years for a loan secured by a mortgage over real property, noting
 - the whole of the loan must be secured by a registered mortgage over the property
 - when the loan is first made, the market value of the property (less liabilities secured over the property in priority to the loan) must be at least 110% of the amount of the loan
- 7 years for any other loan.

Written agreements

A written agreement must be in place before the private company's lodgment day for the income year in which the loan amount was paid to the shareholder or their associate.

There is no prescribed form for the written agreement. However, as a minimum, the agreement should:

- identify the parties
- set out the essential terms of the loan, that is the
 - amount and term of the loan
 - the requirement to repay
 - the interest rate payable
- be signed and dated by the parties.

A written agreement can be drafted to cover loans which will be made to a shareholder or their associate for a number of income years in the future.

Example: loan put under written agreement before lodgment day

During the 2023 income year, Frame Pty Ltd made an unsecured loan to Penelope, a shareholder of Frame Pty Ltd. The loan won't be treated as a dividend in the 2023 income year if it is:

- put under a written agreement before the private company's lodgment day
- the term of the loan is no greater than 7 years
- the rate of interest payable in subsequent income years equals or exceeds the benchmark interest rate for those years.

Converting payments to a complying loan

Payments made to a shareholder, or their associate, can be converted to complying loans before the private company's lodgment day to avoid a dividend being deemed.

For payments converted to loans, the private company is taken to have made a loan at the time the payment was made. For more information about payments, see [Division 7A – payments by private companies](#).

Example: payment converted to a loan before lodgment day

In the 2021 income year, XYZ Pty Ltd pays the petrol expenses of a vehicle owned by Sally, its shareholder. Sally is under no express or implied obligation to repay the amount. Unless Sally and XYZ Pty Ltd convert the payment to a complying loan, the Division 7A provisions in respect of payments will apply.

If Sally and XYZ Pty Ltd agree to convert the payment into a loan before the private company's lodgment day, the Division 7A provisions relating to loans will apply.

Refinancing loans

Certain loans can be refinanced without resulting in a deemed dividend.

Loan converted to a loan secured by a mortgage

An unsecured loan that is converted to a loan secured by a registered mortgage over real property can have the loan term extended. The maximum term of the loan becomes 25 years less the period of the term already expired when the loan was unsecured.

Secured loan converted to an unsecured loan

A secured loan can also be converted to an unsecured loan but there will be a corresponding reduction in the loan term.

Loans in place for 18 years or less

The maximum of the unsecured loan is 7 years if the remaining term on the secured loan at the time of conversion was 18 years or less.

Loans in place for more than 18 years

If the secured loan has already been in place for more than 18 years, the maximum term of the unsecured loan will be reduced so that the total term of the loan (in both its secured and unsecured form) will be no more than 25 years. That is, deduct from 7 years the difference between:

- the length of the period starting when the loan was made and ending when the loan was converted
- 18 years.

Loan subordinated to another loan from another entity

A private company loan can also be refinanced when the loan becomes subordinated to another loan from another entity. The subordination must arise as a result of circumstances beyond the control of the entity to which the original loan was made. The private company and the other entity must have dealt with each other at arm's length in relation to the subordination.

In these circumstances, the repayment of the old loan as part of the refinancing is not disregarded for Division 7A purposes.

Example: refinancing a loan

Hilda Pty Ltd has made a loan secured by a mortgage over real property to an associate of a shareholder, Sachin. The term of the loan was 25 years.

However, after 20 years, the terms of the loan are changed so it is no longer secured by a mortgage over real property. If the expired term of the old secured loan was less than 18 years, the maximum term of the unsecured loan would be 7 years. But in this instance, the original secured loan had already been in place for more than 18 years.

As a result, in the written agreement governing the new loan, the maximum term of the loan will be 5 years (that is, 7 years less the number of years by which the existing loan has exceeded 18).

Amalgamated loans

An amalgamated loan is when a private company makes one or more loans to a particular shareholder or associate during an income year, and each loan:

- isn't repaid before the company's lodgment day

- would be treated as a dividend, except it's under a complying loan agreement
- has the same maximum term.

Each of the individual loans are known as 'constituent loans'. The amount of the amalgamated loan is the sum of the constituent loans that have not been repaid before the lodgment day for the year of income in which the amalgamated loan is made.

Converting to a loan secured by a mortgage

An unsecured loan can be converted to a loan secured by a mortgage over real property with a longer maximum term. When the term of an existing loan is extended because of a mortgage, a new amalgamated loan is taken to be made in the income year before the income year in which the extension is made. The previous amalgamated loan is disregarded if the loan comprised of one constituent loan. If the previous amalgamated loan comprised of more than one constituent loan, the amount of the previous amalgamated loan is reduced by the amount treated as a new amalgamated loan.

More than one amalgamated loan

A private company may have a number of amalgamated loans to a shareholder or their associate at any one time. This will occur where relevant constituent loans have been made over a number of income years. Private companies with more than one amalgamated loan will need to maintain records for each loan.

Minimum yearly repayment

[The Division 7A calculator and decision tool](#) can be used to calculate the minimum yearly loan repayment of principal and interest required to repay the amalgamated loan over its maximum term.

However, to calculate the repayment manually, the following steps can be used:

- Step 1: multiply the amount of the loan not repaid by the end of the previous income year by the current year's benchmark interest rate.
- Step 2: divide one by one plus current year's benchmark interest rate.

- Step 3: index the step 2 amount to the power of the remaining term of the loan in years.
- Step 4: one minus the step 3 amount.
- Step 5: divide the step 1 amount by the step 4 amount.

The amount of the loan referred to in step 1 is the amount of the amalgamated loan.

These steps can also be expressed as:

$$\text{MYR} = \text{PI} \div (1 - (1 \div (1 + I))^{\text{to the power of T}})$$

Where:

- MYR = minimum yearly repayment
- P = amount of loan not repaid by the end of the previous income year
- I = current year's benchmark interest rate
- T = remaining loan term (in years).

The minimum yearly repayment needs to be worked out for each income year after the year in which the loan is made.

If the private company has more than one amalgamated loan, each amalgamated loan is considered separately. The loans can't be grouped for the purposes of calculating a minimum yearly repayment. There will be a minimum yearly repayment in respect of each amalgamated loan.

Concepts for the minimum yearly repayment formula

A number of specific concepts apply to the minimum yearly repayment formula. They are the:

- amount of loan not repaid by the end of the previous income year
- current year's benchmark interest rate
- remaining term of the loan.

Amount of the loan not repaid by the end of the previous income year

Generally, you calculate the amount of a loan outstanding (or not repaid) at the end of the previous income year using the following formula:

- opening balance of the amalgamated loan, as of the beginning of the previous income year, minus
- amount of principal repaid during that income year.

However, the calculation differs depending on whether the income year after the amalgamated loan is made is the:

- first income year
- subsequent income years.

First income year

For the first income year after the amalgamated loan is made:

- no interest is payable in respect of the year the loan is made
- the amount of the loan not repaid by the end of the previous income year is calculated by subtracting
 - the total principal repayments made before the private company's lodgment day, from the original amount of the loan.

If no repayments are made before the lodgment day, the balance of the amalgamated loan that hasn't been repaid before the end of the previous income year is the sum of the constituent loan balances at the end of that year.

Example: amount of amalgamated loan not repaid by the end of the income year when the loan is made

During the 2014 income year a private company made loans of \$50,000 and \$25,000 to a shareholder.

The loans were made under complying written loan agreements. Both loans were unsecured loans with a term of 7 years with interest rates set at the benchmark interest rates.

On 31 August 2014 the shareholder made a repayment of \$20,000 on the \$50,000 loan.

The private company's lodgment day for its 2014 income tax return was 15 May 2015 and the return was lodged on that date.

The amount of the amalgamated loan not repaid by the end of the 2014 income year is \$55,000.

Subsequent income years

The amount of the amalgamated loan not repaid by the end of the income year is calculated on the basis that interest is payable on the balance of the amalgamated loan, at a rate equal to the benchmark interest rate for the income year.

For the following income years, to calculate the amount of the loan not repaid by the end of the previous income year, it's important to know how much of the repayment made in the income year is attributable to interest and how much is applied to reduce the principal.

The [Division 7A calculator and decision tool](#) provides a breakdown of the interest and principal components of the payment. To calculate this manually, apply the relevant benchmark interest rate to the amounts outstanding. If the interest rate in the written agreement is different from the benchmark interest rate, the benchmark interest rate is used to calculate the minimum yearly repayment for Division 7A purposes.

The amount of the loan repaid during an income year is obtained by deducting the interest from the actual repayments made during the year. The opening balance of the loan for the next year is the opening balance at the beginning of the previous year less the principal repaid during that year.

Where a repayment is made before the private company's lodgment day for the year in which the amalgamated loan is made, the principal amount at 1 July of the first income year after the loan is made, is not the sum total of the constituent loans at 1 July. Rather, it is the sum of the constituent loans immediately before the lodgment day. For this purpose, payments made before lodgment day are taken to have been made in the year the amalgamated loan is made.

Example: amount of amalgamated not repaid by the end of the income year after the loan is made

This example uses the same facts as the previous example, except on 30 May 2015 the shareholder paid the private company a further \$8,000, being a \$4,000 payment for each

loan. No other repayments were made during the 2015 income year.

Interest is calculated annually in arrears by reference to the daily balance throughout the year as follows.

Firstly, work out the daily balance throughout the year:

The principal as at 1 July 2014 is \$75,000, which is the loan balance.

The repayment of \$20,000 on 31 August 2014 reduces the loan balance to \$55,000.

The repayment of \$8,000 on 30 May 2015 reduces the loan balance to \$47,000.

To calculate the interest:

$$= (\text{interest payable on } \$75,000 \text{ from } 01/07/2014 \text{ to } 30/08/2014) + (\text{interest payable on } \$55,000 \text{ from } 31/08/2014 \text{ to } 29/05/2015) + (\text{interest payable on } \$47,000 \text{ from } 30/05/2015 \text{ to } 30/06/2015)$$
$$= (5.95\% \text{ of } \$75,000 \times (61 \div 365)) + (5.95\% \text{ of } \$55,000 \times (272 \div 365)) + (5.95\% \text{ of } \$47,000 \times (32 \div 365))$$
$$= \$745.79 + \$2,438.68 + \$245.17$$
$$= \$3,430 \text{ (rounded to the nearest dollar).}$$

The 'amount of the loan not repaid by the end of the previous income year' is \$50,430 (\$75,000 principal + \$3,430 interest – \$28,000 repayments = \$50,430).

If the actual interest rate used in the written agreement exceeds the benchmark rate, the 'amount of the loan remaining at the end of the previous income year' will be a notional amount.

Working out the remaining term

The remaining term is the difference between:

- the number of years in the longest constituent loan
- the number of years between the end of the private company's income year in which the loan was made, and the end of the private

company's income year before the income year for which the minimum yearly repayment is being worked out.

If the answer is not a whole number, it is rounded up to the next whole number.

Example: calculate the first minimum yearly repayment (2015)

This example uses the same facts as the previous examples.

To work out the first minimum yearly repayment, the amount of the amalgamated loan not repaid by the end of the 2014 income year is \$55,000 (loans made less principal repayments made before the lodgment day for the 2014 income year) and the benchmark interest rate for the income year ended 30 June 2015 is 5.95%.

The remaining term is worked out as the difference between:

- the number of years in the longest constituent loan included in the amalgamated loan (7 years)
- the number of years between the end of the private company's income year in which the loan was made (2014), and the end of the private company's income year before the 2015 income year for which the minimum yearly repayment is being worked out (that is 2014), that is 0 years.

The remaining term is 7 years (that is, $7 - 0 = 7$).

The minimum yearly repayment for the income year ended 30 June 2015 is worked out as follows:

Step 1: multiply the amount of the loan not repaid by the end of the previous income year by the current year's benchmark interest rate, which is

$$55,000 \times 0.0595 = 3272.5$$

Step 2: divide one by one plus current year's benchmark interest rate, which is

$$1 \div (1 + 0.0595) = 0.943841435$$

Step 3: index the step 2 amount to the power of the remaining term of the loan in years, which is

0.943841435 to the power of 7 = 0.667257208

Step 4: one minus the step 3 amount, which is

$$1 - 0.667257208 = 0.332743$$

Step 5: divide the step 1 amount by the step 4 amount, which is

$$3272.5 \div 0.332742732 = 9835 \text{ (when rounded to the closest dollar)}$$

In determining if there is a minimum yearly repayment shortfall, all repayments made during the 2015 income year (including those made before the private company's lodgment day for the 2015 income year) are taken into account.

The total of the repayments made in the 2015 income year is \$28,000 (the \$20,000 payment made on 31 August 2014 and the \$8,000 payment made on 30 May 2015). As \$28,000 exceeds \$9,835, there is no shortfall and therefore no deemed dividend arises for the 2015 income year.

Example: calculate the minimum yearly repayment for the subsequent income year (2016)

The amount of the loan remaining at the end of the previous income year (that is, the year ended 30 June 2015) is \$50,430 (see conclusion to example 7).

The benchmark interest rate for the 2016 income year is 5.45%.

The remaining term is worked out as the difference between:

- the number of years in the longest constituent loan included in the amalgamated loan (7 years)
- the number of years between the end of the private company's income year in which the loan was made (2014) and the end of the private company's income year before the 2016 income year for which the minimum yearly repayment is being worked out (that is 2015), that is one year.

The remaining term is 6 years (that is, $7 - 1 = 6$).

The minimum yearly repayment for the 2016 income year will be worked out as follows:

Step 1: multiply the amount of the loan not repaid by the end of the previous income year by the current year's benchmark interest rate, which is

$$50,430 \times 0.0545 = 2748.435$$

Step 2: divide one by one plus current year's benchmark interest rate, which is

$$1 \div (1+0.0545) = 0.948316738$$

Step 3: index the step 2 amount to the power of the remaining term of the loan in years, which is

$$948316738 \text{ to the power of } 6 = 0.72731157$$

Step 4: one minus the step 3 amount, which is

$$1 - 0.72731157 = 0.27268843$$

Step 5: divide the step 1 amount by the step 4 amount, which is

$$2748.435 \div 0.27268843 = \$10,079 \text{ (when rounded to the closest dollar)}$$

The shareholder would need to make repayments on the loan totalling at least \$10,079 to not trigger any Division 7A dividend.

Loan repayments not taken into account

Some payments that a shareholder, or their associate, makes to a private company in respect of a loan before the required time will not be taken into account when working out:

- the minimum yearly repayment
- how much of the loan has been repaid.

Examples of these payments include:

- a journal entry that appears to record a payment being made on a date when no payment was actually made (for example, a back dated journal entry) will not be accepted as having been made at that time

- a direction to pay where an entity makes a payment to the private company on behalf of the borrowing entity, but the entity making the payment does not have the capacity to do so, or there is no evidence that the entity made the payment on behalf of the borrowing entity (other than a journal entry)
- agreements to set-off amounts payable between parties where there are no mutually existing liabilities between those parties
- payments where a reasonable person would conclude that the shareholder or their associate, either
 - when making the payment, intended to obtain a loan (directly or indirectly) from the private company of an amount similar to, or larger than, the payment
 - before making the payment, obtained a loan from the private company (directly or indirectly) of a total amount similar to, or larger than, the repayment in order to make the payment
- a loan obtained indirectly through an [interposed entity](#) arrangement in order to make the payment.

For more information on the amount of a loan obtained indirectly, see Taxation Determination [TD 2011/16](#) *Income tax: Division 7A – payments and loans through interposed entities – factors the Commissioner will take into account in determining the amount of any deemed payment or notional loan arising under section 109T of the Income Tax Assessment Act 1936*.

Example: no evidence that a direction to pay occurred before the minimum yearly repayment was due

Pine Co, Oak Trust and Jarrah Trust are all controlled by the same family group.

On 1 February 2024, Pine Co advances a loan of \$1,000,000 to Oak Trust. The loan remains outstanding at Pine Co's lodgment day for the 2024 income year, being 15 May 2025. Prior to lodgment day, Pine Co and Oak Trust had entered into a complying Division 7A loan agreement. As a result, Oak Trust is required to make a minimum yearly repayment of \$150,000 to Pine Co by 30 June 2025.

In August 2025, while balancing and finalising the accounts of the group for the 2025 income year, the controllers discover that Oak Trust had not made a minimum yearly repayment to Pine Co by 30 June 2025. They also note that Jarrah Trust had cash at bank of \$700,000 and an existing loan to Pine Co of \$200,000 as at 30 June 2025. As a result of this discovery, the controllers decide that Oak Trust will borrow \$150,000 from Jarrah Trust and use this amount to make the minimum yearly repayment to Pine Co. No cash transactions occur. However, journal entries which are back dated to 30 June 2025 in the accounts of the relevant entities show that:

- there is a new loan from Jarrah Trust to Oak Trust of \$150,000,
- Pine Co's loan to Oak Trust reduced by \$150,000, and
- Jarrah Trust's loan to Pine Co reduced by \$150,000.

The controllers of Oak Trust contend that, despite the absence of any cash transactions, there was a direction given by Oak Trust to Jarrah Trust to make a payment on its behalf to Pine Co, and this was done by adjusting the loan balances between the entities.

Notwithstanding the contentions made by the controllers and the journal entries, Oak Trust has not made a minimum yearly repayment to Pine Co by 30 June 2025

This is because a journal entry, in itself, is not a transaction, but merely records a transaction that has already occurred. A backdated journal entry will not be accepted as evidence that a transaction occurred on that date. Therefore, in this case, there is no evidence that Jarrah Trust made a payment on behalf of Oak Trust to Pine Co by the due date of 30 June 2025.

Example: new loan obtained before repayment

Alicia obtains a loan of \$10,000 from Cleary Pty Ltd. Alicia is a shareholder of Cleary Pty Ltd. Alicia has until the lodgment day to repay the loan. Two weeks before the lodgment day Alicia

obtains a further \$10,000 from Cleary Pty Ltd. She then repays the original \$10,000 loan a week before the lodgment day.

The repayment of the original \$10,000 loan won't be taken into account because Alicia has borrowed a similar amount from Cleary Pty Ltd and, in this case, a reasonable person would conclude that the loan was obtained to make the repayment of the original \$10,000.

The original \$10,000 loan is treated as a deemed dividend subject to the distributable surplus of the private company.

Example: new loan obtained following repayment

Alpha Trust requires a minimum level of working capital to operate its business. Beta Co is a private company that has significant retained earnings. Alpha Trust and Beta Co are controlled by the same family group.

On 30 March 2020, Beta Co lends \$200,000 to Alpha Trust to use as working capital. The parties enter into a complying loan agreement before Beta Co's lodgment day (being 15 May 2021). On 30 May 2021, Alpha Trust repays \$33,965 to Beta Co, the minimum yearly repayment required. On 2 June 2021, Beta Co lends \$100,000 to Alpha Trust.

Having regard to all the circumstances, a reasonable person would conclude that the trustee of Alpha Trust intended to borrow \$100,000 (which is a larger amount than the repayment) from Beta Co when the repayment was made. Alpha Trust's repayment of \$33,965 may not be taken into account for the purposes of working out how much of the \$200,000 loan has been repaid.

Example: indefinite reborrowing arrangement

Sam is the sole director and shareholder of Plant Pty Ltd. He is told by a mate about a way he can save money on his mortgage

by borrowing the profits made by his company, without having to pay any additional tax on the amount of profit he borrows. He is also told he won't need to enter into a complying loan agreement, and so he won't have to pay interest to his company, if he temporarily repays the amounts he borrows by the end of the income year. Under this arrangement Sam understands that:

- in the first income year of the arrangement
 - he would borrow profits from Plant Pty Ltd that it doesn't need and put them in his mortgage offset account, saving non-deductible interest on his personal mortgage
 - on 30 June he would repay the total amount he borrowed to plant Pty Ltd.
- in following income years
 - on 1 July, Sam would reborrow the amount he repaid Plant Pty Ltd the day before and put it back in his personal mortgage offset account
 - he would then borrow additional amounts of profit made by Plant Pty Ltd throughout the income year that it doesn't need to run its business and deposit them into his personal mortgage offset account
 - Sam will repay the total amount he has borrowed during the income year on 30 June
- he will repeat this arrangement indefinitely year after year, until it is no longer possible, or he doesn't need to.

Before starting the arrangement, he decides to get advice from his tax agent first.

Sam's tax agent correctly warns him that this reborrowing arrangement would result in him being deemed to be paid an unfranked dividend by the company in each income year he undertakes it equal to the amount borrowed (subject to the amount of the company's distributable surplus for that income year).

This is because the repayments he makes on the loan are disregarded by **section 109R**, because a reasonable person would conclude that, when he made the repayment, he intended to reborrow a similar or larger amount from the company.

Sam's tax agent advises him that he will need to include the amount of any deemed dividend he is taken to be paid as a result of the arrangement in his assessable income.

Sam follows his agent's advice and decides not to enter the arrangement and warns his mate about the tax consequences of the arrangement.

Example: interposed entity arrangement

Apple Trust requires a minimum level of working capital to operate its business. Banana Co is a private company that has significant retained earnings. Orange Co is a private company that has no retained earnings. Apple Trust, Banana Co and Orange Co are controlled by the same family group.

On 30 March 2020, Banana Co lends \$200,000 to Apple Trust. The parties enter into a complying loan agreement before Banana Co's lodgment day (being 15 May 2021). On 30 May 2021, Banana Co lends \$100,000 to Orange Co. On 31 May 2021, Orange Co lends \$100,000 to Apple Trust. On 2 June 2021, Apple Trust repays \$40,000 to Banana Co.

The loan between Orange Co and Apple Trust is not a Division 7A complying loan and Orange Co has no distributable surplus.

Having regard to all the circumstances including the timing of payments and the relationship between entities, a reasonable person may conclude that Banana Co lent \$100,000 to Orange Co solely or mainly as part of an arrangement involving a loan to Apple Trust. Banana Co is taken to have made a notional loan of \$100,000 to Apple Trust.

Having regard to all the circumstances, a reasonable person may conclude that before the payment of \$40,000 was made, the trustee of Apple Trust borrowed \$100,000 (which is a larger amount to the payment) from Banana Co in order to make the payment. Apple Trust's repayment of \$40,000 may not be taken into account for the purposes of working out how much the \$200,000 loan has been repaid.

Payments always taken into account

Some payments will **always** be taken into account, even if there's an intention to obtain another loan when the payment is made. These payments are made by offsetting the following amounts against the balance of the loan:

- a dividend payable to the shareholder or their associate by the private company
- work and income support related withholding payments and benefits payable by the private company to the shareholder or their associate (for example, salary or wages)
- payments covered by a voluntary agreement to withhold
- if the shareholder or their associate transferred property to the private company, an amount equal to the difference between the arm's length value of property and the amount that the company has already paid the shareholder or their associate for the transfer.

A payment by legal offset is only effective in making a repayment on the loan if:

- mutual liabilities exist at the time of the offset
- there is an agreement between the private company and the shareholder or their associate to offset the liabilities (which may be express or implied).

A book entry only records a transaction, it doesn't create one. The offset agreement is the legal basis for discharging the liabilities between the parties.

In addition, a payment by another entity to the private company on behalf of the shareholder or their associate will be taken into account (regardless of any intention to obtain another loan) if the amount of the payment is:

- payable by the other entity to the shareholder or their associate, and
- included in the shareholder's or their associate's assessable income in the income year in which the payment is made, or in an earlier income year.

An entity can include an individual, company, trust or partnership.

Example: minimum yearly repayment made by offsetting a dividend

In the 2022 income year Sandy obtains a complying loan from Sunshine Pty Ltd, which she is a shareholder of. In the 2023 income year Sandy is required to make minimum yearly repayments of \$5,500 on the loan.

On 20 June 2023 Sunshine Pty Ltd declares a dividend of \$5,500 payable to Sandy.

On 28 June 2023 Sandy and Sunshine Pty Ltd enter into an agreement to offset their mutual legal liabilities – Sunshine Pty Ltd's liability to pay Sandy a \$5,500 dividend, against Sandy's obligation to pay Sunshine Pty Ltd \$5,500.

Sandy has satisfied the minimum yearly repayment for the 2023 income year, because the agreement to offset the dividend liability against the loan was entered into and executed before the end of the income year.

Failure to make a minimum yearly repayment

A shortfall in a minimum yearly repayment on an amalgamated loan may be deemed to be a dividend (subject to the private company's distributable surplus) if:

- a private company made an amalgamated loan to a shareholder or their associate in an earlier year of income
- the amalgamated loan is not repaid at the end of the current year
- the amount paid to the private company during the current year in respect of the loan is less than the minimum yearly repayment for the current year
- the Commissioner does not exercise their discretion not to treat the amount as a dividend.

If a shareholder or their associate makes a repayment for a constituent loan in an income year after the year in which the constituent loan was made, the repayment is taken to be a repayment in respect of the amalgamated loan.

Commissioner's discretion

If a repayment is less than the minimum yearly repayment on an amalgamated loan, discretion may apply. The shareholder or associate must satisfy us that the minimum yearly repayment was not met because of circumstances beyond their control (and they would suffer undue hardship if the loan were treated as a dividend). If we are satisfied this is the case, then the private company will not be taken to pay a dividend.

Criteria that are considered:

- the shareholder's or their associate's ability to repay the loan at the end of the income year in which the amalgamated loan was made
- any circumstances that reduced the shareholder's or their associate's ability to repay the loan
- whether the shareholder or their associate took all reasonable steps to make the minimum yearly repayment for the current income year
- whether the shareholder or their associate made payments equal to the amount of the deficiency as soon as possible after the current income year.

We may also disregard a deemed dividend and extend the period for repayments where the shareholder or their associate was unable to make the minimum yearly repayments because of circumstances beyond their control. We will specify a later date the minimum yearly repayments must be made and, provided the amount of the shortfall is paid within the specified time, the shortfall will not be taken to be a dividend.

In addition to the above discretion, where a deemed dividend arises under Division 7A because of an honest mistake or inadvertent omission, we have discretion to either:

- disregard the deemed dividend (subject to conditions being complied with)
- allow the dividend to be franked.

For more information, see:

- [Division 7A – the Commissioner's discretion under section 109RB](#)
- [Request to extend time to make 2019–20 minimum yearly repayments for COVID-19 affected borrowers under section 109RD](#)

- [Request to extend time to make 2020–21 minimum yearly repayments for COVID-19 affected borrowers under section 109RD](#)

Amount of the dividend

Where there is no loan agreement in place, the amount treated as a dividend is the amount of the loan that has not been repaid before the company's lodgment day.

For loans made under a written complying loan agreement entered into before the private company's lodgment day, a deemed dividend may arise in subsequent years if the required minimum yearly repayment is not made.

The amount deemed as a dividend is the amount by which the payments made to the company in the current year for the loan falls short of the required minimum yearly repayment for that year.

If the loan is made in the previous year of income in the course of winding-up a company, the amount treated as a dividend is the amount of the loan that has not been repaid at the end of the current income year.

Example: non-complying loan to shareholder with repayment

On 1 January 2021, ABC Pty Ltd made a cash advance of \$10,000 to Peter, a shareholder of ABC Pty Ltd. ABC Pty Ltd lodged its income tax return for the 2021 income year on 28 February 2022. By that date, Peter had repaid an amount of \$2,000 and the loan had not been put on a qualifying commercial footing.

The amount treated as a dividend on 30 June 2021 is the amount of the loan not repaid before the lodgment day (for example, \$8,000) subject to ABC Pty Ltd's distributable surplus.

Franking the dividend

Amounts treated as dividends under Division 7A are generally not frankable, even though they are taken to be paid out of the private

company's profits – see [Division 7A – franking implications](#). However, there are exceptions.

When an amount is taken to be a dividend under Division 7A because of an honest mistake or inadvertent omission, we have [discretion](#) to:

- disregard the deemed dividend (subject to conditions being complied with)
- allow the private company to choose to frank the dividend.

Shareholder's or beneficiary's loan account

Each entry in a shareholder's or beneficiary's loan account needs to be analysed to determine what type of transaction it represents (that is, whether it is a payment, a loan or a debt forgiveness to which Division 7A applies). Additionally, entries representing loan repayments must be analysed to determine if they can be taken into account when working out the amount of a loan repaid or the minimum yearly repayment.

The balance of a shareholder's or beneficiary's loan account in the company or trustee accounts respectively may be in debit or credit at the end of the income year. Although a debit balance at the end of a year of income may indicate that there are loans that have not been repaid and a credit balance may indicate that no loans remain unpaid, neither result leads to the automatic conclusion that Division 7A does or doesn't apply.

If a private company has more than one shareholder's or beneficiary's loan account, the private company in calculating the Division 7A exposure cannot use a credit balance in one account to offset the debit balance in another account. Calculations of Division 7A loans are done in respect of transactions in the loan accounts of each individual shareholder.

The 'lender' is the private company or trustee who made the loan that is subject to Division 7A.

Division 7A Myths debunked

Check out these myths so you can avoid making Division 7A mistakes.

Last updated 20 June 2025

Business structure

How you operate your business

Myth: the tax consequences are the same if I operate my business as a sole trader, partnership, trust or private company.

Fact: each type of business structure comes with its own set of rules and [key tax obligations](#).

If you run your business through a private company, Division 7A may apply to payments and other benefits provided by your company to its shareholders and their associates. For more information, see [Entities and taxpayers affected](#).

Using company money

Myth: if I own a company, I can use the company money any way I like.

Fact: a company is a separate legal entity. It's separate to you, even if you're a shareholder or a director or both. This means the company's money is not your money, and there will be consequences every time you take money or access other benefits from your private company.

You can access private company money in the form of salary and wages, director's fees or dividends. All of these amounts will be included in the recipient's assessable income. Private companies may also provide [fringe benefits](#) to its employees, including directors, for which it may have a fringe benefits tax liability.

Division 7A may apply to [private use of assets](#) or money from your private company in a way not described, for example as:

- [payments by private companies](#) (including [use of assets](#))
- [loans by private companies](#)
- [debt forgiveness by private companies](#).

Who Division 7A applies to

Myth: Division 7A only applies to the shareholders of my private company.

Fact: Division 7A applies to both [shareholders and associates of shareholders](#). The definition of an associate is broad and depends on what type of entity the shareholder is. For example, for individual shareholders, an associate can include their relatives, spouse, children, a company they control (or their associate controls) or a trustee of a trust that they (or their associate) can benefit from.

Record keeping

What you need to record

Myth: I don't need to keep records when my private company makes payments, loans, or provides other benefits to other entities.

Fact: you are legally required to keep records of all transactions relating to your tax affairs when you're running a business. You should adopt good [record-keeping](#) practices to ensure you identify and account for all payments, loans and other benefits correctly. Failing to do so can result in unintended consequences, including breaching Division 7A.

For more information, see [Overview of record-keeping rules for business](#) and the Australian Securities & Investments Commission (ASIC) website for guidance on [company officeholder duties](#) .

Using journal entries to record offsets

Myth: I can record a dividend in a journal entry, after an income year has ended, and use that to effectively offset my minimum yearly repayment obligation for that income year.

Fact: a journal entry, without other supporting evidence and contemporaneous action, won't be effective to offset a minimum yearly repayment obligation on a complying loan.

The dividend and minimum yearly repayment obligations must exist at the time of the offset and the borrower and the company must have agreed to the offsets. The agreement and offsets must be made by the end of the income year, usually 30 June.

For more information, see [Payments always taken into account](#).

Payments to other entities

Using private company money

Myth: there are no tax consequences if I use my private company's money to fund another business or income earning activity.

Fact: Division 7A may apply to any loan a private company makes (directly or indirectly) to its shareholders or their associates. Division 7A may apply regardless of what the loan recipient uses the amounts for, including for any taxable purpose.

Division 7A may apply where a shareholder or their associate use a private company's assets for private purposes. For more information see [Private use of assets](#).

Payments or loans through other entities

Myth: I can avoid Division 7A by making payments or loans to shareholders and their associates through other entities.

Fact: Division 7A may apply to payments or loans made from a private company through other entities, where the private company's shareholder or their associate is the target entity to whom the payment or loan is ultimately directed. The other entities involved in this type of arrangement are called [interposed entities](#). For Division 7A purposes, an interposed entity can be an individual, company, partnership or trust.

Payments or loans to trusts

Myth: Division 7A won't apply to payments or loans my private company makes to trusts.

Fact: Division 7A may apply to payments or loans made from private companies to [trusts](#). Division 7A may also apply to [trust entitlements](#) of private company beneficiaries.

Division 7A benchmark interest rate

Myth: the interest rate I use to calculate my minimum yearly repayment on my complying Division 7A loan is the same every year.

Fact: you need to calculate your minimum yearly repayment for each income year using the benchmark interest rate for that particular income year. The benchmark interest rate generally changes each year.

You can use the ATO's [Division 7A calculator and decision tool](#) to help you calculate your minimum yearly loan repayment.

Attempts to circumvent Division 7A

Making repayments

Myth: I can avoid Division 7A by:

- temporarily repaying my loan before the private company's lodgment day
- using the company's money to make my repayments.

Fact: a repayment you make on a [loan by a private company](#) may not be taken into account if you reborrow similar or larger amounts from the same company after making the repayment, or you use money borrowed from the same company to make the repayment.

For information about loan repayments not taken into account, see [Amalgamated loans](#).

Using private company money to save interest on personal loans

Myth: There are no tax consequences if I:

- borrow money from my private company and put it into my personal mortgage offset account at the beginning of, (and/or during), an income year
- repay the money I have borrowed to my company before the end of the income year, then
- reborrow the amount I've repaid (or a similar amount) at the start of the next income year to put back into my personal mortgage offset account, and
- repeat this arrangement over multiple income years.

Fact: This arrangement has consequences under Division 7A.

A reasonable person would conclude that, when you made repayments under this arrangement, you intended to reborrow a similar or larger amounts from the company. The repayments are disregarded meaning you are deemed:

- not to have repaid the money you borrowed from the company each income year under the arrangement by its lodgment day, and
- to have been paid an unfranked dividend by the company, in each income year you undertake this arrangement.

Calculating net assets

Myth: the net assets amount in the distributable surplus calculation will be a negative amount if the company's liabilities exceed its assets.

Fact: net assets, in the [distributable surplus](#) calculation, mean the amount (if any) by which the company's assets exceed its present legal obligations and certain provisions. The net assets will be zero if the company's net assets don't exceed these amounts.

Commissioner's discretion

Triggering a Division 7A deemed dividend

Myth: if I trigger a Division 7A deemed dividend, the Commissioner will exercise a discretion in my favour to disregard it.

Fact: you can't assume the [Commissioner will exercise a discretion](#) in your favour if you trigger a Division 7A deemed dividend.

There are various discretions available to the Commissioner for Division 7A purposes. For the Commissioner to exercise a discretion in your favour, you must meet certain conditions, and your circumstances must support the exercise of the discretion.

Relying on a tax professional's advice

Myth: the Commissioner will exercise the section 109RB discretion in my favour because I relied on advice from a tax professional.

Fact: whether the [Commissioner will exercise the discretion](#) under section 109RB where you have relied on advice from your tax professional will depend on your individual circumstances.

The actions of the tax professional must have contributed to the breach, and your reliance on their advice must have been reasonable. Relevant factors would include the disclosures you made to your adviser, the nature of their advice and whether the adviser made an honest mistake or inadvertent omission.

It will be difficult to demonstrate that you have reasonably relied upon professional advice for Division 7A purposes where no Division 7A advice is obtained or where your adviser has not turned their mind to the application of Division 7A to your circumstances.

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If you follow our information and it turns out to be incorrect, or it is misleading and you make a mistake as a result, we will take that into account when determining what action, if any, we should take.

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