

Ruling Compendium – Taxation Determination TD 2011/7

This is a compendium of responses to the issues raised by external parties to Draft Taxation Determination TD 2010/D2 - Income tax: will the exemption in section 102NA of the *Income Tax Assessment Act 1936* continue to apply to a unit trust that has become the interposed trust of a stapled group pursuant to Subdivision 124-Q of the *Income Tax Assessment Act 1997* if the trustee of the unit trust later gains control (or the ability to control), either directly or indirectly, of operations of an entity that are in respect of a trading business within the meaning of section 102M of the *Income Tax Assessment Act 1936*?

This compendium of comments has been edited to maintain the anonymity of entities that commented on the draft ruling.

Summary of issues raised and responses

Issue No.	Issue raised	Tax Office Response/Action taken
1.	Where a trust controls a company which was one of the stapled entities referred to in Subdivision 124-Q of the <i>Income Tax Assessment Act 1997</i> (ITAA 1997), that company can acquire further companies and the trust will continue to benefit from the specific concession in subparagraph 102NA(2)(b)(ii) of the <i>Income Tax Assessment Act 1936</i> (ITAA 1936).[*] This is because: • there is no mischief which Division 6C of Part III of the ITAA 1936 (Division 6C) needs to protect against in this case; and • this enables the company to 'continue to operate as it had before the restructure', as referred to in extrinsic material, as this includes making further acquisitions.	For the reasons discussed in the Explanation section of the Determination, the Commissioner considers that this is not the better view of the legislation. The extrinsic material to which this comment refers is quoted and discussed in the Determination, including the quoted words, in explaining that in its context the purposes of subsection 102NA(2) of the ITAA 1936 do not connote or require that company-taxed elements under an interposed trust arising from a reorganisation to which Subdivision 124-Q of the ITAA 1997 applies should be able to acquire control (direct or indirect) of any new trading business after the reorganisation. The claim that there is no mischief against which Division 6C should protect, where trading business control is taken by a company-taxed element, is in substance the claim that the benefit of control must be subject to company taxation and therefore Division 6C should not apply. In the wider operation of Division 6C, this argument would imply that the Division should not apply where a public unit trust controls, or is able to control, the conduct of a trading business (or of another entity in its conduct of a trading business) unless the entity actually conducting the trading business is a trust not taxed as a

^{*} All legislative references are to the ITAA 1936 unless otherwise indicated.

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		company. Division 6C is not limited in this way, and in its recent report on Managed Investment Trust taxation options the Board of Taxation rejected the option of limiting Division 6C in this way. Altering the policy and effect of Division 6C in this general way is a policy question.
2.	The intent of the law changes was to improve the international competitiveness of stapled groups and to facilitate their foreign expansion. The view expressed in the Draft TD cannot facilitate direct or indirect foreign (or domestic) expansion, since it limits acquisitions after the reorganisation to eligible investment business only. The important words from the extrinsic material are, at paragraph 8.2 of the Explanatory Memorandum to the Tax Laws Amendment (2007 Measures No. 5) Bill 2007 (the Explanatory Memorandum), 'In addition, public unit trusts will be able to acquire controlling interests in, or control, foreign entities whose business consists primarily of investing in land outside Australia for the purpose, or primarily for the purpose, of deriving rent.' At paragraph 8.5 of the Explanatory Memorandum, 'To enable Australian Listed Property Trusts to acquire overseas vehicles in exchange for their own equity, it is often necessary for the acquirer to issue only its own equity.' At paragraph 8.17 of the Explanatory Memorandum, 'These proposed amendments will facilitate Australian public unit trusts acquiring property and property holding entities offshore.'	The law changes do not have the intent of providing stapled groups with relative advantages in foreign expansion. Their intent was to limit impediments to Australian public unit trusts acquiring property and property-holding entities offshore. This was in part achieved by introducing the relaxed requirements of subsection 102N(2) and so allowing control of foreign rental land entities which do not solely conduct eligible investment business, but which have a business which consists primarily of investing in land primarily for rent; all Australian public unit trusts have the benefit of this provision. The other major part of limiting such impediments was to allow the interposition of a unit trust under a reorganisation of stapled, commonly owned entities without the interposed trust thereby becoming a public unit trust. The interposed trust was intended to be able to acquire foreign rental land entities in exchange for its own equity. Subsection 102NA(2) does not allow the interposed trust to acquire any trading business itself by the issue of its own equity, on any view of the operation of the subsection. Had the intent of the provisions been so wide as to allow foreign expansion into any business at all, the limitation on the interposed trust would not have been required to be maintained.
3.	Plain reading of the words of the legislation supports the alternative view in the draft Determination.	The Determination acknowledges this possible reading of the words of the legislation. However the Explanation section of the Determination explains why this possible reading is not preferred.

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4.	The policy behind the introduction of the roll-over in Subdivision 124-Q of the ITAA 1997 supports the alternative view. The intent is that 'a previously stapled company, owned or controlled by the interposed trust, will be able to continue to operate as it had before the restructure'. This requires that the previously stapled company be able to acquire control, directly or indirectly, of the conduct of new trading businesses, after the restructure to which the roll-over applies. The intent is to improve the international competitiveness of Australian property trusts, such as stapled property groups.	The Explanation section of the Determination discusses extensively the context of the changes of which the roll-over in Subdivision 124-Q of the ITAA 1997, the introduction of subsection 102N(2) of the ITAA 1936, and the introduction of section 102NA of the ITAA 1936 are all part. The roll-over is certainly meant to allow the interposition of a unit trust between stapled entities and their ultimate owners, where some of the stapled entities were taxed like companies and some as trusts. The reorganisation is meant not to tax the interposed trust, which owns all the equity in at least some reorganised entities taxed like companies, like a company itself. The interposed trust is meant to be able to acquire foreign rental land entities in consideration of equity in the interposed trust. The policy behind these changes is fully implemented on the view taken by the Determination. A previously stapled company owned or controlled by the interposed trust is able to continue to operate as it did before the restructure, without the interposed trust being treated as controlling a trading business. If the previously stapled company (or entity taxed like a company) gains control after the restructure of the conduct of a new trading business, it is not operating as it did before the restructure. The interposed trust, which wholly owns the previously stapled company, then gains control (at least indirectly) of the conduct of the new trading business which the company also controls. It is consistent with the policy of the rollover and the other related measures that the interposed trust's new control of the conduct of trading business should not be disregarded. The Second Reading Speech to the Explanatory Memorandum includes the general statement that the CGT roll-over, the interposed head trust for the purpose of overseas acquisitions, and other amendments 'will improve the international competitiveness of Australian property trusts'. This is a statement of an intended overall benefit of specific changes but is not an indication that something other than or beyond those specific changes was intended.

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5.	Principles of statutory interpretation support the alternative view that the Ruling should be 'Yes'. Although the principles are correctly stated in the Explanation section of the draft Determination, they are incorrectly applied, as an interpretation which renders a concession to taxpayers practically redundant should not be favoured where there is an alternative interpretation giving effect to the policy intention of the enactment.	The Commissioner accepts that the principles of statutory interpretation are correctly stated. The interpretation taken by the Commissioner gives full effect and scope to the intent of the enactment, as that intent appears from its terms and its context. The Commissioner's interpretation does allow stapled entities to be reorganised by the interposition of a unit trust without the interposed trust thereby becoming a public unit trust. The interposed trust can acquire foreign rental land entities in exchange for its own equity. The Commissioner does not agree that the policy intent of the enactment extends to allowing the interposed trust, after the reorganisation by which it is interposed, to acquire control or the ability to control any trading business provided it does so in or through a company-taxed entity that was part of the reorganisation.
6.	The consolidation consequences of a reorganisation by which a unit trust is interposed would be anomalous, on the view taken in the draft Determination. If subsequently taking control of a trading business would make the interposed trust a public trading trust, then that interposed trust would be able to elect to consolidate, changing any existing consolidation decisions by company-taxed entities subject to the reorganisation.	The suggested anomaly applies, on any view, if the interposed unit trust itself acquires control of a trading business after the restructure other than through a company-taxed entity that was part of the restructure. Accordingly it would be anomalous if the income tax effect were different provided control of the trading business were through a company-taxed entity that was part of the restructure, rather than by the interposed unit trust itself, through a subsidiary entity that was not part of the restructure, or through some other entity.
7.	We understand the Commissioner accepts acquisition of trading business assets after a reorganisation to which Subdivision 124-Q of the ITAA 1997 applied. Where asset acquisition is permitted, control of a trading business should be permitted.	The Commissioner does not consider that Division 6C permits acquisition of trading assets where this would allow control, directly or indirectly, of a trading business or of an entity in its conduct of trading business. Accordingly the Commissioner does not consider there is any inconsistency between the treatment of trading business acquisition and trading business asset acquisition.

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8.	No subparagraph of paragraph 102NA(2)(b) of the ITAA 1936 is limited to permit only trading businesses controlled before the reorganisation to which Subdivision 124-Q of the ITAA 1997 applied. There is no different effect for companies and trusts taxed like companies which were part of the reorganisation and to which subparagraphs 102NA(2)(b)(i) and 102NA(2)(b)(iii) of the ITAA 1936 apply, and for subsidiaries or entities able to be controlled by those companies and trusts taxed like companies, to which subparagraphs 102NA(2)(b)(ii) and 102NA(2)(b)(iv) of the ITAA 1936 apply.	The Commissioner prefers this view, that all the subparagraphs of paragraph 102NA(2)(b) of the ITAA 1936 have, in context, similar effect. As the Determination states, however, that effect is that none of the subparagraphs disregards an interposed trust under a reorganisation to which Subdivision 124-Q of the ITAA 1997 applied later gaining control of the conduct of a trading business by or through an entity to which a subparagraph of paragraph 102NA(2)(b) of the ITAA 1936 applies.
9.	Reference in subparagraph 102NA(2)(b)(ii) to “a subsidiary of one of those stapled entities” should be interpreted as referring to any company, provided that the company is a subsidiary of any entity that was part of the formerly stapled structure at the time the top-hatting arrangement took place. Subparagraphs 102NA(2)(b)(ii) and 102NA(2)(b)(iv) allow the trustee of an interposed trust to control the affairs and operations of an entity that is controlled by the deliberate use of the current tense word “is” (rather than “was”) and the lack of reference to the time of the scheme was completed in those subparagraphs means that the subparagraphs extend to any entity that is controlled by the entities mentioned in subparagraphs (i) or (iii), regardless of whether the control begins before or after the reorganisation.	The Commissioner does not consider that there is any plausible intent to allowing later acquisition of control (or the ability to control, directly or indirectly) of a trading business to a subsidiary of a company-taxed entity that was part of the reorganisation by which a unit trust was interposed, but not to the company-taxed entity itself. A linguistic interpretation of subparagraphs 102NA(2)(b)(ii) and 102NA(2)(b)(iv) which would distinguish them in this way from subparagraphs 102NA(2)(b)(i) and 102NA(2)(b)(iii) is not considered preferable by the Commissioner.

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9. cont	The reference to the word “was, before the the scheme was implemented” in subparagraphs (i) and (iii) is necessary in order to ensure that the exemption (under subparagraph (ii) and (iv) is only available for subsidiaries and entities that are controlled by the entities mentioned in subparagraphs (i) and (iii) (that is, to ensure that the exemption is not available for entities controlled directly by the interposed trust or by the flow through trust side of a stapled group. Once subparagraphs (i) and (iii) have served this purpose, subparagraphs (ii) and (iv) operate to cover all entities controlled by these particular entities. The omission of time restraints on subsidiary entities under subparagraphs (ii) and (iv) and the use of current tense in these paragraphs provides a clear signal that the legislator intended that the exclusion be available for later acquisitions on the corporate side of a stapled structure. This is particularly so, given that all of Section 102NA is drafted in the current tense (with the only exception being subparagraphs 102NA(2)(b)(i) and 102NA(2)(b)(iii)).	
10.	If a new operating business is acquired after a restructure by which a unit trust was interposed above former stapled entities, and is placed in a new trust acquired by a former stapled trust but is controlled by or through a former stapled company, no exception in paragraph 102NA(2)(b) should apply.	The Commissioner agrees (understanding ‘operating business’ to have the same meaning as ‘trading business’). However for the reasons discussed in the Explanation section of the Determination this intended result follows because, apart from the reorganisation itself to which roll-over under Subdivision 124-Q of the ITAA 1997 applies, taking control of the conduct of any trading business is not permitted by the exceptions in paragraph 102NA(2)(b) of the ITAA 1936.
11.	Lenders who provide funding for a specific asset purchase within a group restructured with a roll-over under Subdivision 124-Q of the ITAA 1997 may require a separate responsible entity to be established for debt security purposes.	Where a specific purchase includes (or includes control of) a trading business, the same issues arise whether the trading business is separated out into a new responsible entity or not. An acquisition of control of a trading business, other than the acquisition of control permitted by the foreign rental land entities provision of subsection 102N(2), is not consistent with the law.

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12.	Capital raisings by the issue of further stapled equity by stapled entities raise capital for each of them, consistently with a reasonable allocation (such as by net value of each stapled entity, or their market values). After a reorganisation to which roll-over under Subdivision 124-Q of the ITAA 1997 applies, further capital raisings are by issue of equity in the interposed trust. Can funds raised in this way be allocated according to funding requirements?	This issue is beyond the scope of the Determination. If an interposed entity raises capital, its use of that capital is subject to the same tax principles as any other raising by an entity which wholly owns other entities. This includes principles relevant to whether and on what terms to invest in or lend to wholly owned entities.
13.	Stapled entities which are not restructured so as to be wholly owned by an interposed trust can take new control of trading businesses without application of Division 6C of Part III of the ITAA 1936. They should be able to do so after a restructure to which roll-over under Subdivision 124-Q of the ITAA 1997 applies.	Before a restructure to which roll-over under Subdivision 124-Q of the ITAA 1997 applies, stapled entities which are not taxed like companies cannot take control of trading businesses. Stapled entities which are taxed like companies can do so, and are not themselves controlled by an entity not taxed like a company. After such a restructure, the interposed trust is likely to control, directly or indirectly, all trading business activities of any formerly stapled entity. The roll-over under Subdivision 124-Q of the ITAA 1997 allows this to be disregarded. There was no equivalent control apart from the restructure.
14.	Section 102NA and subsection 102N(2) are clearly separate amendments which do not depend on each other for operation. Each should be interpreted based on its particular words and its particular purpose, rather than as part of a linked or married purpose.	The context of the introduction of Subdivision 124-Q of the ITAA 1997, of section 102NA of the ITAA 1936, and of subsection 102N(2) of the ITAA 1936 is clearly that they were related parts of a single group of measures. They are so expressed in the Second Reading Speech and the Explanatory Memorandum. The relationship between reorganisation of stapled entities to interpose a unit trust, and practical access overseas to acquiring foreign rental land entities for equity in the interposed trust, is expressly explained in the extrinsic material. It would be contrary to proper principles of statutory construction to disregard the context of the measures which relates them to each other.