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## **Public advice and guidance compendium – TD 2017/22**

This is a compendium of responses to the issues raised by external parties to draft Taxation Determination TD 2016/D7 *Income tax: where an Australian corporate tax entity is a beneficiary of a trust, can the trust 'hold' a direct control interest (within the meaning of section 350 of the Income Tax Assessment Act 1936) in a foreign company for the purpose of Subdivision 768-A of the Income Tax Assessment Act 1997?*

This compendium of comments has been edited to maintain the anonymity of entities that have commented.

### **Summary of issues raised and responses**

| <b>Issue No.</b> | <b>Issue raised</b>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                    | <b>ATO Response/Action taken</b>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                 |
|------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 1.               | <p>The interpretation adopted in the draft Taxation Determination is problematic and appears unfair.</p> <p>The conclusion in the draft Taxation Determination ends up with a test time by reference to a long period, rather than a point in time as intended by the quite clear words of section 768-5(2)(d) of the ITAA 1997.</p> <p>The conclusion also results in the effective dates for determining whether there is a participation interest being different for holdings through partnerships and trusts.</p> | <p>We have reconsidered and revised our view; in particular, our interpretation of subsection 351(2) of the ITAA 1936.</p> <p>Our revised interpretation now focuses on the beneficiary's entitlement to trust income at the point in time the relevant dividend is paid (that is, the test time), rather than the beneficiary's entitlement at the end of the year. We consider that the revised view, as set out in the final Taxation Determination, is the better view.</p> <p>We also note that this resolves the concern about the effective dates for determining an entity's participation interest through partnerships and trusts being different.</p> |
| 2.               | <p>The test time for determining whether there is a participation interest should be highlighted to avoid misunderstandings.</p>                                                                                                                                                                                                                                                                                                                                                                                       | <p>We have highlighted the relevant test time in each of the Examples.</p>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                       |
| 3.               | <p>The position reached in the draft Taxation Determination is problematic for all trusts but is particularly challenging for fixed trusts with semi-annual distributions (or more frequent distributions in a year) where trust interests are sold ex-distribution before the end of the income year.</p> <p>The ATO should review its application of statutory interpretation principles to consider if another more equitable outcome can be achieved.</p>                                                          | <p>See ATO response to Issue 1.</p>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                              |

| Issue No. | Issue raised                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                          | ATO Response/Action taken                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                           |
|-----------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 4.        | <p>The draft Taxation Determination should cross reference the related guidance in draft Taxation Ruling TR 2016/D2 <i>Income tax: distributions from foreign companies – meaning of ‘at the time the distribution is made’ when applying the participation test</i> and draft Taxation Determination TD 2016/D6 <i>Income tax: where an Australian corporate tax entity is a partner in a partnership, can the partnership ‘hold’ a direct control interest (within the meaning of section 350 of the Income Tax Assessment Act 1936 ) in a foreign company for the purpose of Subdivision 768-A of the Income Tax Assessment Act 1997?</i></p> <p>It would also be desirable to briefly highlight that the effective dates for determining whether there is a participation interest in respect of indirect holdings is different for holdings through partnerships and trusts.</p> | <p>We have added a reference to the related guidance in footnotes 6 and 10.</p> <p>The reader is directed to the relevant guidance where the interposed entity is a partnership rather than a trust.</p> <p>See also ATO response to Issue 1.</p>                                                                                                                                                                                                                                                                                                                                                   |
| 5.        | <p>The focus on the ‘year-end’ position for interposed trusts is inconsistent with the approach to participation test time in respect of interposed partnerships and companies (which focuses on a point in time).</p>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                | <p>See ATO response to Issue 1 – the revised view now focuses on the beneficiary’s entitlement to trust income at the point in time that the relevant dividend is paid (which is similar to the approach in relation to partnerships and companies).</p>                                                                                                                                                                                                                                                                                                                                            |
| 6.        | <p>The approach in the draft Taxation Determination does not align with section 768-5 of the ITAA 1997 which clearly:</p> <ul style="list-style-type: none"> <li>• applies to trusts and applies the participation test at a point in time, and</li> <li>• refers to taxpayers which would have included the dividend income in their assessable income by virtue of Division 6 of the ITAA 1936.</li> </ul> <p>The draft Taxation Determination as currently drafted, which determines a participation interest by reference to an overall share of income or right to corpus of the trust at the</p>                                                                                                                                                                                                                                                                                | <p>The combined effect of subsection 960-190(1) and section 351 of the ITAA 1936 is that a beneficiary’s participation interest in a trust is determined by reference to its entitlement to a share of the overall trust income for the year (or corpus as at the end of the year) rather than its interest in the particular dividend paid by the foreign company. Determining the beneficiary’s participation interest by reference to its overall share of trust income (or corpus at the end of the year) aligns with Division 6 of the ITAA 1936.</p> <p>See also ATO response to Issue 1.</p> |

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| Issue No. | Issue raised                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                     | ATO Response/Action taken                                                                                                                                                                                                                                                                                                                                                                 |
|-----------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
|           | <p>end of the year (per subsection.351(2) of the ITAA 1936) is not ideal in light of the above two aspects of section 768-5. It does not necessarily allow those beneficiaries who are actually taxed on the dividend income to be attributed with the requisite indirect interest to claim the relief under Division 768-A.</p> <p>An approach that would achieve the above two focusses of section 768-5 would be, for fixed trusts, to test the beneficiary's interest in the particular dividend income to which it has been made presently entitled under the trust deed and this would give a more appropriate result.</p> |                                                                                                                                                                                                                                                                                                                                                                                           |
| 7.        | The draft Taxation Determination should have a much clearer initial statement that the test for the beneficiary's participation interest looks to the beneficiary's interest at the end of the income year.                                                                                                                                                                                                                                                                                                                                                                                                                      | See ATO response to Issues 1 and 2.                                                                                                                                                                                                                                                                                                                                                       |
| 8.        | The explanation does not refer to the inconsistency of the outcome when compared with subsection 768-5(2).                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                       | See ATO response to Issue 1.                                                                                                                                                                                                                                                                                                                                                              |
| 9.        | Paragraph 1 of the Taxation Determination should state that the direct participation interest is calculated in accordance with section 960-190(1) Item 2 and section 351(2) of the ITAA 1936.                                                                                                                                                                                                                                                                                                                                                                                                                                    | <p>As noted in ATO response to Issue 2, the test time for determining whether there is a participation interest has been highlighted in each of the Examples.</p> <p>We have also added a reference to the fact that a direct participation interest in a trust is calculated in accordance with item 2 of subsection 960-190(1) and section 351 of the ITAA 1936 in the Explanation.</p> |
| 10.       | Each of the Examples should clarify that the direct control interest is to be tested at the end of the year of income.                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                           | See ATO response to Issues 1 and 2.                                                                                                                                                                                                                                                                                                                                                       |
| 11.       | Paragraph 58 of the draft Taxation Determination should be promoted to the front of the explanation, or alternatively there should be a subheading inserted to highlight it.                                                                                                                                                                                                                                                                                                                                                                                                                                                     | In light of our revised view, paragraph 58 of the draft Taxation Determination has been deleted. Our revised view on the application of section 351 of the ITAA 1936 is explained in paragraphs 60-62 of the final Taxation Determination.                                                                                                                                                |

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| <b>Issue No.</b> | <b>Issue raised</b>                                                                                                                                                                                | <b>ATO Response/Action taken</b>                                                                                                                                                                                                                                                 |
|------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 12.              | The decision to make the Taxation Determination retrospective from the date that Subdivision 768-A commenced (distributions made on or after 17 October 2014) should be appropriate in most cases. | Noted.<br>Further, to the extent that the final Taxation Determination provides a less favourable outcome than the view outlined in TD 2016/D7, taxpayers will be entitled to rely on the view in the draft Determination up until the date of issue of the final Determination. |