

Ruling Compendium – TR 2010/3

This is a compendium of responses to the issues raised by external parties to TR 2009/D8 – Income tax: Division 7A loans: trust entitlements.

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	ATO Response/Action taken
A: POLICY ISSUES		
1.	Policy intent of Division 7A	
	1. Division 7A of Part III of the <i>Income Tax Assessment Act 1936</i> (ITAA 1936)¹ (Division 7A) is directed to a situation where a shareholder or associate of a shareholder is able to use funds for their private use whilst avoiding those amounts being treated as assessable income. Where the trust retains the funds for use in its business or investment operations, shareholders cannot access the funds for their own personal use and no deemed dividend should therefore arise. 2. Subdivision EA of Division 7A (Subdivision EA) (and its predecessor, the former section 109UB) were introduced for the specific purpose of addressing any mischief with respect to unpaid present entitlements (UPEs) (owing to private company beneficiaries. Division 7A was therefore only ever intended to apply to UPEs where a trustee makes a loan or payment to a shareholder or associate of a shareholder of a private company beneficiary that has a UPE in the trust. It was not intended to apply to UPEs more generally.	1. This statement misrepresents the intended scope of Division 7A. The Division applies to certain loans made to shareholders and their associates irrespective of the use that shareholder or associate of the shareholder makes of the funds so advanced. Broadly speaking where a shareholder or its associate is given use of funds representing profits of a private company by way of a loan or payment – it is the fact that the shareholder (or their associate) and <u>not</u> the private company has use of these funds (that is, the fact that the funds have been paid or lent to the shareholder or its associate) that triggers the application of Division 7A, and the subsequent use the shareholder or their associate makes of those funds is not relevant. 2. When former section 109UB was introduced the prevailing view was that UPEs were held on separate trust for the sole benefit of the private company beneficiary. On the basis that the UPEs were so dealt with there was some debate as to whether the UPE would be a subsection 109D(3) loan. Assuming the UPE was not a loan on the basis that it was separately held for the sole benefit of the private company beneficiary, former section 109UB (and later Subdivision EA) addressed the situation where the trustee on-lent funds to shareholders or their associates. The question of whether Division 7A could apply to UPEs more generally when they were <i>not</i> held on sub-trust for the sole benefit of the private company beneficiary was therefore not addressed by former section 109UB or

¹ In this compendium, all legislative references are to the ITAA 1936 unless otherwise stated.

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	3. The broad and clear scheme of the Subdivision EA provisions is to treat the relevant trust effectively as a private company for the purposes of determining whether a deemed dividend arises. 4. If it had been intended that a UPE could be treated as a 'loan' under section 109D, this would have been listed as a specific paragraph in section 109D. The fact that UPEs are specifically mentioned in Subdivision EA and not in section 109D supports the view that the latter was not intended to be tortuously extended to UPEs. 5. If Treasury had intended Subdivision EA to be an integrity provision designed to supplement the main provisions of Division 7A rather than an exclusive code to deal with private companies with UPEs, it is likely that Treasury would have included a specific anti-overlap provision as was the case for section 109T. 6. The approach taken in TR 2009/D8 (the draft Ruling) leaves very little scope for the operation of Subdivision EA as UPEs to private company beneficiaries will almost always attract the operation of section 109D. This cannot have been the intention	Subdivision EA. 3. Division 7A treats trusts and companies differently. The scheme of the Division looks to profits of the private company being able to be used by shareholders or their associates. A trust can be such a shareholder or associate. Division 7A loans to such a trust may be caught under section 109D whereas a similar loan to a private company would be excluded from the application of section 109D (by section 109K). 4. As mentioned in response to issue 1.2 of this section of the compendium, when Division 7A (and section 109D) was introduced, the prevailing view was that a UPE was held on trust for the (implicitly sole) benefit of the private company beneficiary. This arrangement was not thought (nor presumably intended) to itself be a loan within the meaning given in subsection 109D(3). TR 2010/3 (the final Ruling) does not change the position, as it is the Commissioner's view as set out therein that UPEs held on sub-trust for the sole benefit of the private company will not amount to a loan within the meaning of subsection 109D(3). It is therefore accepted that <i>not all</i> UPEs will be loans, nor are intended to be loans. However, in situation outside of this, where the funds representing the UPE are <i>not</i> used to solely benefit the private company beneficiary, the UPE may properly fall within the extended meaning of a loan as set out in subsection 109D(3). 5. The ATO notes that in situations where the predecessor to Subdivision EA was thought to apply (as explained in responses 1.2 and 1.4 of this compendium), an anti-overlap provision would be unnecessary. In these circumstances, no loan will arise under section 109D. Whether a specific anti-overlap provision is required in Subdivision EA to deal with the situations where a subsisting UPE amounts to the provision of financial accommodation or an in-substance loan is a matter for Treasury. Nonetheless, the final Ruling observes that the Commissioner will treat a UPE as remaining unpaid for Subdivision EA purposes if pursuant to the final Ruling that UPE is treated as a loan under section 109D and is subject to that Ruling. It is proposed that this will be further detailed in a Law Administration Practice Statement, of which the draft has been released for public comment. 6. Not all UPEs will be treated as loans under the interpretation in the final Ruling. In particular, where the UPE is held on sub-trust for the sole benefit of the private company beneficiary (as was the view at the time that Division 7A was introduced), Subdivision EA may still apply if funds are then loaned or paid to a

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	of the legislature when Subdivision EA or its predecessor, the former section 109UB, was introduced. 7. The Board of Taxation report to the Government in November 2002 suggesting that consultation take place regarding the replacement of former section 109UB with a section that would set out the consequences 'where a trustee makes a company presently entitled to the income of a trust, but does not pay the funds to the company within a reasonable period' and the suggestion those consequences could possibly be 'either that the trustee would be assessed on the amount of income if there had been no distribution, or that the company would have to pay a top-up tax', is clear recognition that the tax policy underlying Division 7A is that UPEs are not loans under the definition in section 109D. 8. Proposed draft amendments to Division 7A that would add an explanation of Subdivision EA to the simplified outline of Division 7A in section 109B and the introduction of the proposed Subdivision EB of Division 7A demonstrate that Treasury still sees a clear role for Subdivision EA and that a long outstanding UPE is not a loan for the purposes of Division 7A. This is inconsistent with the draft Ruling that would leave only very limited situations in which Subdivision EA would apply. 9. The ATO acknowledges in TD 2004/63 that the clear legislative purpose behind the introduction of what is now Subdivision EA is to modify the event/point on which Division 7A applies. That is, 'instead of the ... [UPE] itself triggering the application of Division 7A, there can be no deemed dividend unless and until the trustee makes a loan to the shareholder of the private company or an associate of such a shareholder' (to quote from paragraph 9 of TD 2004/63).	shareholder or associate of a shareholder of the private company other than on Division 7A compliant terms. 7. The assumption, based on the prevailing view when Division 7A was legislated that UPEs were not loans (at that time when the prevailing view was that they were held on separate trust for the benefit of the private company beneficiary), has seemed to be maintained by the Board of Taxation without any separate analysis of its correctness. That the Board of Taxation's starting point was seemingly an assumption that a UPE was not a loan is not necessarily indicative of Parliament's intent as to whether or not a UPE <i>should</i> be able to amount to such a loan. 8. It is agreed that Subdivision EA still has a role to play. The draft amendments are silent regarding Treasury's view as to whether a UPE can be a loan within the meaning of subsection 109D(3) and in the Commissioner's view does not infer a particular view one way or the other. 9. TD 2004/63 (now withdrawn) did not explain the purpose of Subdivision EA (or its predecessor former section 109UB). Rather, it considered whether repayments of certain loans made by a trustee could reduce a deemed dividend arising under the former section 109UB. Nonetheless, in both the draft and the final Rulings the Commissioner has acknowledged that the ATO had formerly expressed the view that a UPE was not a loan within the meaning of subsection 109D(3). Whilst the statement made in TD 2004/63 was specifically made in respect of loans deemed to be dividends under former section 109UB and did not consider the application of section 109D (in particular, it only applied to loans made by trustees and not by private companies – see paragraph 11), TD 2004/63 was reflective of such a view which the Commissioner has now prospectively moved away from since the publication of the draft Ruling (see

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		paragraphs 27-30 of the final Ruling). As TD 2004/63 referred to a repealed provision and no longer has any practical application, it was withdrawn on 14 April 2010.
2.	Commercial impact	
	1. The draft Ruling will have a significant adverse impact on the administration of many of the thousands of trusts that exist in the middle market as it ignores the fact that UPEs often arise for purely commercial purposes. For example, a trust operating a business may have the profits that are the subject of the UPE tied up in working capital and may not be able to 'physically pay' a trust distribution without either borrowing funds or selling assets. 2. The introduction of a requirement to put UPEs treated as 'loans' under Division 7A on Division 7A compliant terms and therefore physically pay the funds to companies within a certain time frame will put extreme hardship on many small and medium sized businesses that require the liquidity in their business to fund working capital, investment in capital assets and business growth.	1. Broadly speaking, in situations where a UPE is being held for the sole benefit of the private company beneficiary, it will not be taken to be a loan for Division 7A purposes. In these situations, the final Ruling will have no adverse consequences. Even in situations where funds representing the UPE are intermingled with other funds of the trust and used for trust purposes, if the loan that is taken to arise pursuant to the Commissioner's views as set out in Section three of the final Ruling is put on a compliant loan agreement by the lodgement day for the income year in which the loan arises, there will be no adverse consequences under Division 7A. Minimum yearly repayments will have to be made over seven years, but there is no requirement to pay out the UPE at once. Other options are discussed in response to issue 2.2 of this compendium. 2. If the trustee requires use of its income indefinitely, it is difficult to determine why commercially it would seek to make a private company presently entitled to such income where it has the ability to instead retain income for trust purposes. Nonetheless, if it wishes to make the private company presently entitled to its income, but does not want to have the private company make a Division 7A loan back to the trust even under a complying loan agreement, an appropriate sub-trust may be used. If the amount to which the private company is made presently entitled is set aside on a sub-trust and that sub-trust invests these funds back into the main trust on terms requiring that all the benefits from use of these funds flows back to the sub trust, no adverse consequences will arise under Division 7A provided any return on the sub-trust's investment is paid out to the private company. It is proposed that administratively the Commissioner will accept that if funds representing the UPE are invested back into the main trust on terms requiring the payment of a reasonable percentage of the income of the trust (relative to the amount of the UPE invested compared with total trust funds) this will amount to terms requiring all the benefits from use of the funds representing the UPE to flow back to the private company. This administrative treatment will be detailed in a Law Administration Practice Statement, of which the draft has been released for

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	3. The only alternative that a trust operating a business may have in order to avoid a deemed dividend is to borrow the funds from a bank or other third party in order to actually pay the distribution. Such borrowings may be problematic for some businesses. 4. In the case of companies, the retained profits are calculated after corporate tax, which is currently 30%. This takes into account the fact that some of the profits are not distributed and are used to maintain the business. In the case of a trust, the tax on undistributed profits is at the top marginal rate. The taxation rules should therefore take into account that businesses run through a trust structure should be able to use profits to maintain and grow their business without being subject to adverse taxation consequences. 5. Trust beneficiaries are liable to tax in respect of the income year in which their present entitlement is declared, regardless of whether it is paid. Thus, private company beneficiaries are already subject to 30% tax on their unpaid present entitlements. By deeming unpaid present entitlements to be Division 7A loans and therefore, deemed dividends, the same amount of trust income will be taxed a second time. Consequently, an overall tax rate of up to 76.5% (30% + 46.5%) could apply depending on whether the trustee, and individual beneficiary or company bears the liability for double tax. 6. The ruling will potentially have an adverse impact on structures that have been set up on the basis of the previously accepted practice of not treating UPEs as Division 7A loans. Necessary changes to structures flowing from the approach in the draft Ruling may give rise to adverse capital gains tax or stamp duty consequences.	public comment. See also the discussion at issue 4 of section D of this compendium: 'Section three issues (loans within the extended meaning)' 3. There are other options as explained in the responses to issues 2.1 and issue 2.2 of this section of the compendium. 4. In situations where a trustee chooses to retain profits in the trust by making no beneficiary presently entitled to that income and the trustee pays tax at the top marginal rate, the ruling will have no impact. In these situations the private company will have no unpaid present entitlement to the income of the trust that may be taken to be a loan under the final Ruling. 5. The usual operation of Division 7A is to treat certain loans, payments and forgiveness of debts as a deemed dividend taxed to the recipient. The company profits represented by such payments loans and forgiveness will have already been taxed at 30%. The position taken in the final Ruling does not result in deemed dividends being treated any differently to this. 6. The final Ruling does not necessitate a change in structure. Future UPEs can be paid out; treated as loans (such as by being paid out and re-lent via set-off) that are put on section 109N compliant terms; physically held on sub-trust for the sole benefit of the private company or used by the main trust on terms requiring all the benefits from such use to flow to a sub-trust and be paid out to the solely entitled private company beneficiary; all without attracting deemed dividend treatment.

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3.	The ruling should be withdrawn pending legislative change or litigation	
	1. The draft Ruling should be withdrawn and instead Treasury should draft amendments to Division 7A which are open to the usual public consultation process in order to address the matters raised in the draft Ruling. 2. The meaning of 'loan' in Division 7A has not yet had the benefit of interpretation by a court. In this situation, it would be appropriate for the Commissioner to run a test case at a high level before reaching a final conclusion as he does in the draft Ruling.	1. The Commissioner is responsible for administering the ITAA 1936 as enacted, and the final Ruling provides guidance as to the Commissioner's views in respect of the application of section 109D to certain arrangements involving UPEs. Whether or not amendments should be considered to section 109D or other provisions of Division 7A is a matter for Treasury. 2. Part of the ATO's role is to help people understand their rights and responsibilities in relation to the laws administered by the Commissioner. The ATO does this by offering advice and guidance that outline the Commissioner's view of how these laws apply. Sometimes people disagree with the Commissioner's understanding of the law. The final Ruling sets out the Commissioner's views on what is meant by a loan for Division 7A purposes given the expanded definition in subsection 109D(3). In reaching these views the Commissioner has drawn on general principals of statutory interpretation. The ATO is providing this final Ruling to reduce the uncertainty and contention that otherwise exists in respect of these provisions. If uncertainty remains following the publication of the final Ruling and dissemination and administration of the views it contains, further consideration could be given as to whether test case litigation was appropriate.
B: APPLICATION ISSUES		
1.	Date of effect	
	1. The draft Ruling is not sufficiently clear on the date from which the approach in the draft Ruling will apply.	1. Section Two of the draft Ruling deals with situations where the company has made an ordinary loan and this section has both prospective and retrospective application. Section Three deals with situations where a subsisting UPE is taken to be a loan made by the private company to the trustee of the trust under the extended definition of a loan in subsection 109D(3), and (to the extent to which this is unfavourable to the taxpayer) only applies prospectively to UPEs arising on or after 16 December 2009. It will not apply unfavourably to UPEs arising prior to this date at any time into the future (even if, for example, that UPE is partially paid down some time in the future). This is clearly set out in paragraphs 27-30 of the final Ruling. For the avoidance of doubt, the date of effect will be reiterated in a Law Administration Practice Statement, of which the draft

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	2. Since the introduction of Division 7A, it has operated with no suggestion that a UPE would be deemed to be a loan as contemplated in the draft Ruling. The ruling should therefore only apply to UPEs arising after its introduction. In this regard it is noted that paragraphs 55 to 57 of the draft Ruling relate only to Section three and provide no protection from retrospective application with regard to Section two. 3. With regard to the prospective application provided for in paragraphs 55 to 57 of the draft Ruling concerning Section Three, it is not clear whether a UPE arising before 16 December 2009 will never be deemed to be a loan or whether it may be deemed to be a loan but only from after 16 December 2009. For example, it is not clear whether: • a taxpayer is required to inform the Commissioner about UPEs arising before 16 December 2009 to obtain the protection provided under paragraphs 55 to 57 of the draft Ruling • a taxpayer is required to take any corrective action in relation to a subsisting UPE that arose before 16 December 2009 to obtain the protection provided under paragraphs 55 to 57 of the draft Ruling • the payment, after 16 December 2009, of any part of the UPE subsisting before 16 December 2009 to the beneficiary will result in the balance of the UPE being 'refreshed' and therefore lose protection from the application of Division 7A. 4. A period of 'amnesty' should be applied to the principles in the ruling as they are heavily technical and may have been	has been released for public comment. 2. Section two loans are limited to ordinary loans. They are ordinary loans made by the private company to the trustee of a trust, and are not UPEs deemed to be loans within the extended meaning of a loan used in Division 7A. UPEs can only themselves be treated as a loan for Division 7A purposes under Section three of the final Ruling. As stated in paragraph 30 of the final Ruling, it 'has never been doubted that ordinary loans made by private companies to their shareholders (or associates of their shareholders) may attract the operation of Division 7A. As such, the final Ruling applies both before and after its date of issue where an ordinary loan is made as described in Section two'. Such ordinary loans (including those explained in Section two of the final Ruling) made to shareholders or associates of shareholders (such as a trustee considered under the final Ruling) will be subject to Division 7A even if they arise with respect to a UPE created before 16 December 2009. 3. To the extent to which it is unfavourable, Section three will never apply in respect of a UPE that arose before 16 December 2009, irrespective of (for example) whether any notice is given to the Commissioner or not, whether there has been any purported corrective action taken or not, or whether the UPE is partially paid down after 16 December 2009. That Section three of the final Ruling will not unfavourably apply to UPEs that arose before 16 December 2009 is clearly stated in paragraph 28 of the final Ruling. For the avoidance of doubt, this will also be specifically stated in a Law Administration Practice Statement, of which the draft has been released for public comment. 4. Section two will only apply where a private company has made an actual loan to the trustee. This is a situation to which 109D has always applied. However

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	inadvertently misunderstood by taxpayers and advisors.	if the taxpayer has (in particular prior to publication of the draft Ruling) made an honest mistake or inadvertent omission in respect of such loans, the taxpayer should consider applying for the exercise of the Commissioner's discretion in section 109RB. Section three will only apply to UPEs arising on or after 16 December 2009. From this date the ATO view that a UPE could be a loan within the meaning of subsection 109D(3) was set out in TR2009/D8. Under the Commissioner's proposed administrative practices regarding the timing of Division 7A loans made as described in Section three of the Ruling, taxpayers will have until the date of lodgement for the income year <i>following</i> the year in which that UPE arose to pay out that UPE or put it on Division 7A compliant terms to avoid it being treated as a deemed dividend. See also the response to issue 1 in section G of this compendium: 'Other technical issues with this Ruling'.
C: SECTION TWO ISSUES (Ordinary Loan)		
1.	Set-off	
	1. Whilst 'set-off' as described in the draft Ruling is available, the doctrine of equitable set-off rather than legal set-off should be used to support the position in the ruling. 2. There is no explanation/guidance in the draft Ruling on the phrase 'agreed set-off' and it is therefore not possible to discern when an 'agreed set-off' will occur.	1. <i>Re East Finchley Pty Limited v. Commissioner of Taxation</i> [1981] FCA 481; 89 ATC 5280 is good authority for ability to apply the common law principles of set-off as set out in <i>Spargo's case</i> to effect a set off of an obligation in equity by force of the trust deed (to pay a beneficiary's entitlement) against a legal obligation by virtue of a loan agreement. Broadly speaking, equitable set-off on the other hand is concerned with the ability to set off related legal actions. Nonetheless, in the event of any doubt the general term set-off as used in the final Ruling (and explained at paragraphs 53-54) is broad enough to cover the arrangements under consideration therein. 2. The concept of set-off is an ordinary legal principle. It broadly involves the agreement to accept offsetting obligations as paid. It will be a question of fact as to whether such an agreement has been reached but it may for example be evidenced by journal entries made by the respective parties.
2.	Accounting treatment	
	The draft Ruling appears to place significant emphasis on the accounting treatment of a UPE, resulting in a form over substance approach which departs from general ATO practice. This may lead to a situation where an amount that is erroneously recorded as a	The Commissioner will take a substance over form approach. Although accounting treatment may be evidence of a real transaction, it will not of itself be treated as the transaction if the substance is different. This has been clarified in paragraphs 70 to 73 of the final Ruling.

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	loan in the accounts of either the trust or the private company beneficiary will be treated as a loan even though it was done erroneously. Therefore, more than a mere journal entry should be required before a UPE is converted to a loan under Section two. Furthermore, the draft Ruling provides that accounting treatment may indicate acquiescence with knowledge subject to evidence to the contrary, but provides no guidance on what would be considered evidence to the contrary. Furthermore, the ruling should recognise that where UPEs have been mislabelled as loans in the accounts of the trust and/or company that they are not loans unless something further is done to convert them into loans.	An example of other evidence the Commissioner will consider in determining whether or not a UPE has been converted into a loan has been provided in paragraph 76 of the final Ruling.
3.	Payment must be made so that it can be repaid	
	The view in the draft Ruling that a loan can be made by the unilateral actions of one party may not be in accordance with the intention of Division 7A that the provisions will not apply if the loan is 'repaid' by the lodgement date of the company's income tax return for that year (paragraph 109D(1)(b)). The Australian Oxford dictionary definition of 'repay' includes 'pay back (money), return, ...'. This suggests that there must be the action of payment before you can repay an amount. The payment of an amount in satisfaction of an obligation created by virtue of a unilateral act may therefore not be a 'repayment'. It would therefore seem that the creation of a loan obligation without payment, as argued in the draft Ruling, may not allow that amount to be repaid as contemplated by Division 7A.	'Repaid' in paragraph 109D(1)(b) is to be read in the context of the relevant 'loan' under subsection 109D(3). If the relevant loan goes beyond a regular payment and repayment (for example, a provision of credit), the term 'repaid' in the relevant context could just mean payment of an amount owing after having been accommodated. In other situations, the crediting of a loan account by the trustee reflects the treatment of a trust entitlement as having been paid to the beneficiary and then lent back to the trustee of the trust (or applied for the benefit of the beneficiary by way of being lent to the trustee) by way of set off. Once so created, repayment of such a loan by the trustee would amount to a relevant repayment of the amount lent.
4.	Implied agreement through acquiescence with knowledge	
	Acquiescence	
	1. Deemed or inferred 'authorisation through acquiescence' is insufficient to give rise to a loan which attracts the operation of Division 7A. Clear and significant positive action and agreement should be required from both the trustee and the private company beneficiary to acknowledge that a UPE has been specifically	1. The Commissioner agrees that there needs to be the intention to create (or authorise) a loan before a loan will arise by agreement. However, there is no need for this intention to be evidenced by a positive act. It can be inferred from acquiescence with knowledge.

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	converted to a loan before the transaction can attract Division 7A. Division 7A should only apply in circumstances where it is clear that the parties intended to create a loan agreement. 2. Division 7A as an integrity measure imposing double taxation should not be imposed where a private company beneficiary does nothing other than fail to call for the immediate payment of its entitlement, particularly given that payment may be deferred to allow for the working capital needs of the trust business. The ruling should be amended so that only UPEs which have been converted to loans by positive action of the private company are potentially subject to Division 7A. 3. Acquiescence does not constitute acceptance of a contract without showing that a contractual relationship has arisen by the conduct of the parties. See <i>Empirnall Holdings Pty Ltd v. Machon Paull Partners Pty Ltd</i> (1988) 14 NSWLR 523.	2. In not calling for payment of its entitlement in circumstances where the private company beneficiary <i>knows</i> the funds to which it is entitled are not being used for its sole benefit, the private company is allowing the trustee to use funds representing its profits. This is economically no different than had the private company received payment of its entitlement and lent the funds back to the trustee. There is no reason in policy why if the private company does so knowingly it should not be taken to have provided financial accommodation or an in-substance loan to the trustee. 3. Where the private company has knowledge that the trust has treated its UPE as having been satisfied and the funds then lent back to the trust, and then acquiesces to this treatment, the Commissioner is of the view that a contractual relationship between the private company and the trustee does arise. Nonetheless, administratively it is proposed the ATO will not generally seek to treat a private company as having made a loan by agreement including acquiescence with knowledge unless there is some evidence of this on the part of the private company, such as recording the amount owing to it from the trustee in its accounts as a loan asset. This administrative treatment will be detailed in a Law Administration Practice Statement, of which the draft has been released for public comment.
	Knowledge	
	4. The draft Ruling provides that full knowledge would be assumed where the trust and beneficiary form part of the same family group. This is incorrect. Australian law respects the separate legal existence of entities and without specific anti-avoidance provisions or common law principles including sham, it is not open to attribute two or more entities with the same controlling mind in the absence of positive action. 5. The Commissioner relies on <i>Corporate Initiatives</i> [2005]	4. The Commissioner agrees that both the trustee and the private company are separate legal entities. However, unless the trustee is a natural person both the trustee and the private company, as artificial entities will be taken to know what their directing mind and will know. Where that directing mind and will is comprised of the same individual or individuals, the Commissioner will take the view factually that the private company will be taken to know what the trustee knows unless there is something to suggest otherwise. 5. In the final Ruling, the Commissioner relies on <i>Endresz v. Whitehouse</i>

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	FCAFC 62; 142 FCR 279; 59 ATR 351; 2005 ATC 4392 (<i>Corporate Initiatives</i>) and <i>Endresz v Whitehouse</i> 1997 24 ASCR 208 (<i>Endresz v. Whitehouse</i>) in support of his position that the private company will have knowledge of the trustee's actions where the trust and the private company are part of the same family group unless there is sufficient evidence to the contrary. <i>Corporate Initiatives</i> illustrates that where two entities have the same controller and financial advisors, the actions of those controllers and financial advisors can give rise to a scheme involving the entities they control. This simply supports the proposition that inaction, where entities are part of the same group or have the same controlling mind, can be an 'element' of a scheme. This is less than what is required to make a loan. <i>Endresz v. Whitehouse</i> considers the issue of assumed knowledge in the context of a director's obligation to report certain information based on his knowledge of the actions of one or both companies of which he is a director. This is markedly differently to finding that a private company has knowledge of the actions of a trustee of a related trust for the purposes of determining whether it has made a loan. A more relevant case would be that of <i>Re David Payne & Company Ltd</i> (1904) 2 Ch 608 (<i>Re David Payne & Company Ltd</i>), where the English Court of Appeal held that a company should not be taken to have known what a second company was planning to do with certain funds that it lent to it just because a director of that company also had an interest in the second company. This case supports the argument that, for instance, where a trustee records a UPE to a private company as a liability for accounting purposes but does not enter into a formal loan agreement with the company, the company cannot be assumed to have agreed to the conversion of the UPE to a loan through the assumption of knowledge of a person who is both a director of a trustee company and a director of the private company. Furthermore, the proposition that a director or trustee cannot act	and <i>El Ajou v. Dollar Land Holdings plc and another</i> [1993] 3 All ER 717 (<i>El Ajou v. Dollar Land Holdings</i>) in support of this proposition. In <i>Endresz v. Whitehouse</i>, as well as referring to the passage quoted from <i>Ford's Principles of Corporations Law</i>, Ormiston JA observed that in. In <i>Beach Petroleum NL v. Johnson</i> (1993) 115 A.L.R. 411 Von Doussa, J at stated at paragraph 22.21: In ordinary circumstances, if a director knows information which is important to the affairs of the company, he is under a duty both to communicate that information to the company and to receive it. Whilst in <i>Endresz v. Whitehouse</i> there was some doubt as to how far that statement would extend where the information known by the director would be detrimental to another company in respect of which that individual was also a director, the circumstances considered in the final Ruling do not raise such an issue. The treatment by the trust of the UPE is information that is important to the company who has a right that the UPE be invested prudently, and is information the private company has a right to know and that is not detrimental to the trustee to disclose anyway. <i>Re David Payne & Company Ltd</i> involved a director who was agent of the two relevant companies and did not consider issues of directing mind and will or the controlling mind of those company. It is not relevant for the purposes of the issues considered in the final Ruling. In dealing with directing mind and will, <i>El Ajou v. Dollar Land Holdings</i> explains that the mind, intention and knowledge of the directing mind and will of a company, is taken to be the mind, intention and knowledge of the company. Not all directors will be the directing mind and will of a company for all purposes. An individual director or trustee may act with two different minds in different circumstances, without necessarily raising issues of a breach of fiduciary duties.

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	with two different minds leaves open the possibility that by taking an action in one capacity and no action in the other that an automatic conflict of interest arises and a potential breach of fiduciary duty has occurred. 6. It should be made clear that authorisation can only arise through conscious acquiescence with full knowledge. Also, as there is no definition/guidance as to what conscious acquiescence actually entails, taxpayers/tax agents will not be able to determine whether authorisation has or has not occurred. 7. The draft Ruling says that knowledge of the actions of a trustee may be imputed onto a private company beneficiary where both are part of the same 'family group' but is not clear on when exactly this will be the case.	6. The final Ruling observes that acquiescence can only amount to agreement where there is knowledge of that which is being acquiesced to. Conscious acquiescence will be acquiescence with this knowledge. 7. Family group is now defined in paragraph 3 of the final Ruling.
5.	Applying a UPE pursuant to trust deed	
	1. The draft Ruling makes the point that where the trust deed empowers the trustee to <i>apply</i> unpaid entitlements on behalf of beneficiaries, a trustee can create a loan to itself by simply <i>applying</i> the unpaid entitlement. This appears to potentially apply even where there is no specific evidence of any intention to do so. 2. The draft Ruling does not properly outline Case V4 88 ATC 123 (Case V4) and the conclusions contained in 27 to 29 of that case and in what circumstances exactly the ATO would consider this to be an exception (or not be an exception) to the principles outlined in section 2.	1. A power of the trustee to apply the funds on behalf of the beneficiary will not be sufficient to create a loan. The trustee must both have this power and exercise it in order to create a loan so that Section two applies. This has been clarified in the final Ruling. 2. Case V4 is an example of where on the facts of that case the trustee had set aside funds on sub-trust and in its capacity as trustee of that sub-trust had lent funds back to itself in its capacity as trustee of the main trust. Having distributed the relevant amounts to the beneficiaries by setting those amounts aside on sub-trusts to which the beneficiaries were presently entitled, the trustee then had no authority to treat these amounts as loans from the beneficiaries. This is different from the situation where instead of setting aside amounts for the benefit of the beneficiary, the trustee applies trust funds for the benefit of the beneficiary in the form of crediting a loan account in the name of the private company beneficiary. In paragraphs 27-30 of Case V4 Senior Member KL Beddoe states (at ATC 130-131): 27. It is clear enough that the amounts standing to the credit of the beneficiaries' loan accounts were not loaned by the beneficiaries per se. The loans were made by the trustee on behalf of the beneficiaries to itself in its

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		capacity as trustee of the Family Trust. The trustee was acting as trustee for the beneficiary on a separate trust and it was acting as trustee of the Family Trust when it made the loans to itself. 28. The amounts retained by the trustee in its hands and held on trust for the beneficiaries were not part of the Family Trust having been distributed to the beneficiaries. The trustee's deliberate decision to lend those amounts to itself as trustee of the Family Trust does not alter the position. Neither is the position altered by the lack of any provision in the Trust Deed of the Family Trust requiring the trustee to hold sums distributed to beneficiaries on trust for those beneficiaries absolutely. 29. As I have already indicated I am satisfied that although there are not express trusts created for the beneficiaries the obligations on the trustee to hold the amounts distributed by the Family Trust for the beneficiaries are clearly established so that the trustee is liable in equity to account for those amounts held for the benefit of the beneficiaries absolutely. 30. I am also satisfied that the debtor/creditor relationship was established in respect of the loans but it was established between the trustee for the Family Trust and the trustee as constructive trustee for the beneficiaries. The beneficiaries were not the lenders – they did not enter into any contractual relationship with the trustee. The interest was therefore derived by the trustee in its capacity as trustee for each of the beneficiaries and because the trustee held the estates for the beneficiaries absolutely the beneficiaries were presently entitled to the income derived. It is also relevant to note that in <i>Case V4</i> the beneficiaries were minors. Given <i>Case V4</i> involves a unique factual scenario, it is not referred to in the final Ruling.
D: SECTION THREE ISSUES (Loans within the extended meaning)		
1.	Financial accommodation	
	1. The definition of a loan appearing in paragraph 109D(3)(b) was also used in the former section 46D of the ITAA 1936 which was considered in <i>FCT v. Radilo Enterprises Pty Ltd</i> (1997) 72 FCR 312 where Sackville and Lehayne JJ stated: The provision of credit implies a consensual transaction, such	1. If the phrase 'other forms of financial accommodation' is limited to credit type financial accommodation, the extension of paragraph 109D(3)(b) beyond 'a provision of credit' to 'any other form of financial accommodation' would add nothing to the provision. <i>Radilo Enterprises</i> suggests that a financial accommodation must be a

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	as the delivery of goods on terms permitting deferred payment or the granting of overdraft facilities by a bank... Similarly, in its statutory context, the expression... refers to a consensual arrangement between the person providing the accommodation and the recipient. While <i>Radilo Enterprises</i> refers to a 'consensual transaction', the examples make it clear that the relationship referred to is a credit contractual relationship. This construction assumes that the phrase 'provision of credit' limits the phrase 'any other form of financial accommodation' to credit type financial accommodation under the <i>ejusdem generis</i> rule of statutory interpretation. Therefore, the phrase should not be expanded to include, for example, the use of money by a trustee.	consensual arrangement between two parties, one receiving the accommodation and one providing it. In the context of statutory interpretation, <i>ejusdem generis</i> is a presumption that general matters are constrained by reference to specific matters which identify a group of like matters (a genus). It is therefore necessary to establish a genus before the rule can be applied: See <i>R v. Neil, Regos & Morgan</i> (1947) 74 CLR 613; <i>Cody v. JH Nelson Pty Ltd</i> (1947) 74 CLR 629. Spigelman CJ in <i>Deputy Commissioner of Taxation v. Clark</i> (2003) 57 NSWLR 113 at 143 noted that 'unless at least two different species are identified it is not possible to determine a relevant genus which may be used to read down the general words which follow'. For example, in <i>Allen v. Emmerson</i> [1944] KB 362, places of public entertainment, within the meaning of the expression 'theatre or other places of public entertainment' were not limited to places of the same genus of theatres. Similarly, in <i>Field v. Gent</i> (1996) 67 SASR 122 the phrase 'stone or other missile' placed no limitation on the scope of the term 'missile', and in Australia in both <i>Lake Macquarie Shire Council v. Ades</i> [1977] 1 NSWLR 126 and <i>Plummer v. Needham</i> (1954) 56 WALR 1 a 'place' as used in the phrase 'building or other place' was held not to have to be something akin to a building. Likewise here, the financial accommodation provided need not be akin to the provision of credit. Nonetheless, whilst this presumption does not operate to limit the scope of a provision of financial accommodation as it appears in subsection 109D(3), it is noted that the provision of credit as described in the Ruling is broadly allowing time to pay a legal debt. Allowing a trustee to use funds for trust purposes as described in the Ruling by not calling for payment of a UPE (that is, by allowing time to pay through the deferral of the creation of a legal debt) is akin to an arrangement involving the allowing of time to pay in any event. The remaining provisions in subsection 109D(3) also infer a temporal element in connection with a principal sum, and are not all limited to legal debt (for example, transactions in substance effecting a loan of money in paragraph 109D(3)(d)). As such, even if a broader genus can be found in the whole of subsection 109D(3), an interpretation of a provision of 'financial accommodation' that extends to allowing a trustee to use funds represented by a UPE for trust purposes by not calling for that UPE (and thus allowing the trustee time to pay as a result of the

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	2. The draft Ruling says that a private company beneficiary may provide 'financial accommodation' to a trust if it has supplied or granted some form of pecuniary aid or favour to the trust by 'consensual agreement'. It goes on to say that this 'consensual agreement' may arise where the private company authorises, including by acquiescence with knowledge, the continuing use by the trust of funds representing the UPE, or by not calling for the payment of that UPE, or by not calling for the investment of those funds for its absolute benefit with funds instead available to the main trust for general trust purposes. In order for there to be a 'consensual agreement', there should be a positive act on the part of the company. In the absence of a positive act, there is no such agreement. 3. <i>Eldersmede Pty Ltd & Ors v. Commissioner of Taxation</i> 2004 ATC 2129 (<i>Eldersmede</i>) found that by not calling for payment of a UPE or investment of the funds representing that UPE for its benefit, a beneficiary provided a benefit to the trustee under a scheme for the purposes of the trust loss provisions. However, it does not necessarily follow from <i>Eldersmede</i> that in not calling for payment of a UPE or its relevant investment such a beneficiary will also be providing financial accommodation for the purpose of Division 7A. The purpose and scope of the two statutory schemes are different.	deferral of the creation of a legal debt), under an agreement by the parties (including an agreement taken to be reached through acquiescence with knowledge), would be within this genus. 2. There is no need for a consensual agreement to be evidenced by a positive act. Under basic principles of contract law, a consensual agreement can be inferred from acquiescence with knowledge. See also discussion at the response to issues 4.1, 4.2 and 4.3 of section C of this compendium: 'Section two issues (Ordinary Loans)'. 3. Both the intended scope and the wording used in the provisions considered in <i>Eldersmede</i> differ from the relevant provisions being considered in Division 7A. Nonetheless, the Tribunal in <i>Eldersmede</i> conducted a factual analysis and found that in not calling for payment of a UPE or its investment, the beneficiary had provided a relevant benefit to the trustee under a scheme. The identification of such a scheme is not relevant for Division 7A purposes and nor will there be the provision of financial accommodation by merely providing any benefit at large. The final Ruling makes it clear that for there to be a provision of financial accommodation the private company must provide pecuniary aid or favour to the trustee under a consensual agreement, where a principal sum is ultimately payable. Nonetheless, using the same factual analysis as in <i>Eldersmede</i> it is evident that where a corporate beneficiary has allowed a trustee to use the funds to which it is entitled by not calling for payment of its UPE or its relevant investment, the beneficiary will have provided a benefit to the trustee in the ordinary sense of that word, and given the nature of that benefit so provided, it will amount to the provision of pecuniary aid or favour to the trustee (being the

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	4. The ATO should have looked to other legislation that uses the term 'financial accommodation' to discern its meaning, rather than simply combining separate definitions of the two words. For example, the <i>Borrowing and Investment Powers Act 1987 (Vic)</i> contains a narrower interpretation of the term 'financial accommodation' to that in the draft Ruling. 5. Whilst the definition of a loan in section 10 of the <i>Superannuation Industry (Supervision) Act 1993 (SISA 1993)</i> includes a similar inclusion for the provision of financial accommodation, it is more extensive than this part of the definition of a loan in subsection 109D(3) in including loans that are not (or are not intended to be) enforceable by legal proceedings. Accordingly the Commissioner should not draw upon a similar analysis for interpreting a relevant financial accommodation for subsection 109D(3) purposes as what he did for that in the SISA 1993 in SMSFR 2009/3.	provision of a financial amount without appropriate remuneration). 4. The Commissioner has also examined the judicial consideration of that phrase in <i>Radilo Enterprises Pty Ltd</i> (1997) 72 FCR 312. It is not helpful to consider what other legislation has prescribed that phrase to mean. Left undefined as in subsection 109D(3), the phrase necessarily takes on its ordinary meaning as governed by its context. In the context of legislation dealing with 'borrowing and investment' powers (such as in the <i>Borrowing and Investment Powers Act 1987 (Vic)</i>) it may very well be appropriate that Parliament restricted what was meant by the phrase 'financial accommodation' to only those financial benefits arising from the arrangements broadly comprising the subject matter of that legislation. 5. The Commissioner acknowledges the differences in these two definitions. Whilst similar considerations were given to determining the ordinary meaning of the provision of financial accommodation wherever so used, the precise meaning to be given to that term in either instance must ultimately depend on the context it is used and the purpose for which it appears. The meaning given to the term as described in both the draft Ruling and the final Ruling do not depend in any way on the enforceability or otherwise of the accommodation provided.
2.	Use for 'trust purposes'	
	The draft Ruling makes frequent reference to the issue of whether the UPE is used 'for trust purposes' with the main trust deriving 'no benefit' from the use of the funds settled on the sub-trust. A trust (or more correctly a trustee) does not 'benefit' from any use of trust assets or trust funds because all benefits from the trust estate are accountable to the beneficiaries. There is therefore a nonsense in speaking of funds being used 'for trust purposes' in contradistinction to the funds being invested for the 'private company's absolute benefit'.	Paragraph 3 of the final Ruling defines trust purposes as 'purposes of benefiting one or more beneficiaries or discretionary objects of a trust estate; but does not include use of funds representing a private company beneficiary's UPE for the purpose of solely benefiting that private company'. What trust purposes will include is elaborated on in paragraph 103 of the final Ruling, broadly explaining that funds that have remained intermingled in the trust (other than by reason of having been invested back by a sub-trust on terms requiring all the benefits to be paid over to the sub-trust for the sole benefit of the private company beneficiary) may be used for trust purposes.
3.	Sub-trusts	
	1. A sub-trust may not always arise upon payment of a UPE	1. The scenario where there is no sub-trust has been addressed in the final

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	depending on the terms of the trust deed.	Ruling. For example, paragraph 35 now only indicates that amounts <u>may</u> be settled on sub-trust. Paragraph 38 also notes the possibility of there not being a sub-trust.
	2. The Commissioner should confirm in the final Ruling or a practice statement that appropriate documentation and accounting entries will be sufficient in order to demonstrate that the trustee of the main trust has set aside the appointed income for the sole benefit of the corporate beneficiary. The Commissioner should confirm that it is not necessary for the trustee to physically transfer funds to a separate bank account or identify specific trust property.	2. It is proposed that administratively the Commissioner will accept that a sub-trust may arise in some instances without the physical transfer of funds. Guidance as to when this will be accepted will be provided in a Law Administrative Practice Statement, of which the draft has been released for public comment.
	3. The draft Ruling, and in particular Example 5, proceeds on the basis that an amount settled on separate or sub-trust is on the same terms and conditions as those that apply to the main-trust. However, this is not always the case. The sub-trust may be able to distribute income derived in later years to beneficiaries other than the private company beneficiary where the terms of the trust deed allow. It will be the actual terms of the trust deed under which the sub-trust is created that will be relevant. The majority of trust deeds, which allow a trustee to set aside income in a particular year, do not provide how those funds should be subsequently employed in the sub-trust or specifically set out who should benefit from any income derived from the corpus of the sub-trust in future years. Whilst it is acknowledged that the corpus of the sub-trust, being the original UPE, is generally held for the sole benefit of the original beneficiary, it would be reasonable for the trustee to administer the sub-trust under the same terms as the main trust deed such that any beneficiary considered under the main trust deed can be made presently entitled to any future income derived from the corpus of the sub-trust. Example 5 of the draft Ruling seems to support this position. The draft Ruling gives rise to questions including how trust deeds should be amended in order to avoid the application of	3. There are no standard terms consistent across all trust deeds and the scope of trust deeds is vast and varied. It is the Commissioner's view that it is preferable to focus on the meaning of the specific provisions of subsection 109D(3), and how these may apply to UPEs whether or not they are held on a sub-trust (and if so on what terms). The ATO agrees that it will be the actual terms of the trust that are relevant to determining the facts of a particular arrangement and how the final Ruling applies to those facts. The Ruling explains in general terms when the provision of financial accommodation or an in-substance loan will arise. If a sub-trust allows the trustee to distribute otherwise than to the private company beneficiary, it will not be a trust held for the sole benefit of that private company and accordingly its funds will be being put to use for trust purposes. If the private company knows this and allows this to happen it will be providing financial accommodation to the trustee of that trust. Addressing the specific questions that are raised will be different for different trusts.

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	Division 7A, what accounting records would need to be kept for the sub-trust and how much additional compliance costs might amount to. In addition, questions arise as to whether any necessary amendment to the trust deed (for example providing that any amounts settled on sub-trust are held for the sole benefit of the original beneficiary) may amount to a resettlement giving rise to further compliance costs.	
4.	Investment for the private company beneficiary's 'sole benefit'	
	It is not clear from the draft Ruling when funds will be invested for the 'absolute benefit' or 'sole benefit' of the private company beneficiary. The Commissioner should provide taxpayers and tax agents with specific guidance and practical examples on the documentation that would be required to demonstrate that the trustee has set aside trust funds for the sole benefit of the corporate beneficiary. The Commissioner should also consider further consultation with interested parties to determine a practical way forward (that is, to develop examples whereby the Commissioner will accept that funds representing the UPE are being held or used for the private company's sole benefit).	When the investment is only capable of benefiting the private company beneficiary it will have been invested for its sole benefit rather than for trust purposes as now defined in the final Ruling. In situations where a sub-trust arises and that sub-trust has invested funds representing the UPE back into the main trust, it is proposed that administratively the Commissioner will accept that this is an investment for the private company's sole benefit if that investment or loan is on terms requiring the payment of: • The actual benefits from that investment (for example, where the investment is in respect of a specific asset), or • a reasonable percentage of the income of the trust relative to the amount invested as compared with total trust funds (in addition to a return of the principal lent or invested). This administrative treatment (in addition to any other options for accepting that funds representing the UPE are being used for the sole benefit of the private company beneficiary) will be further detailed in a Law Administration Practice Statement, of which the draft has been released for public comment. The Law Administration Practice Statement has been issued as a draft to ensure that appropriate public consultation will occur and all interested parties have the opportunity to comment. This includes giving them the opportunity to comment in respect of the parameters regarding when the Commissioner will consider that funds representing a private company beneficiary's UPE are being used for the sole benefit of that private company.
5.	CGT events	
	1. If the Commissioner is suggesting that all assets acquired	1. This investment need not give rise to any CGT event that would result in a

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	by the trust from the proceeds of monies retained need to be invested for the absolute benefit of the company, we expect this creates a CGT event. If the trust were to use the monies for the purposes of acquiring an asset in the company's name then arguable CGT event E5 will have happened in that a beneficiary has become absolutely entitled to a trust asset. The Commissioner should clearly state whether he considers a CGT event arising if this is a correct interpretation of the situation described in Example 6. 2. Will CGT event E4 apply if the sub-trust makes a payment to the corporate beneficiary that is not included in the corporate beneficiary's assessable income.	gain or loss – it may be a simple investment of money into the main trust on terms requiring all the benefits from use of those funds to flow back to the sub-trust. As discussed in the response to issue 4 of this section of the compendium, guidance as to how this will be practically administered will be provided in a Law Administration Practice Statement, of which the draft has been released for public comment. 2. A consideration of CGT event E4 is outside the scope of the Ruling. Nonetheless, it is not readily apparent that income of the sub-trust would not be included in the corporate beneficiary's assessable income or that a return of the original corpus of the sub-trust would exceed the beneficiary's cost base of their interest in that sub-trust so as to cause a gain under CGT event E4.
6.	Treatment of UPEs arising in subsequent years	
	Would a UPE arising in a subsequent year create a further settlement of new funds on the same sub-trust or the creation of a new sub-trust?	In future years, absent anything specific in the trust deed, there is no reason in equity why a new sub trust would arise when there is already a sub-trust that has set aside amounts apart from the general trust fund that are for the sole benefit of the private company beneficiary. This has been clarified in the final Ruling.
7.	In-substance loans	
	1. Paragraph 109D(3)(d) requires there to be a transaction which in substance affects a loan of money. Whilst the making of the private company beneficiary entitled to an amount of trust income might be a transaction within the common usage of the term, it is the making of the beneficiary presently entitled that is the transaction and not the subsequent non-payment of that amount. Inaction cannot form the basis of a transaction nor does the transaction creating a UPE affect a loan of money. 2. Furthermore, at paragraph 146 of the draft Ruling, the decision in <i>Grimwade v Federal Commissioner of Taxation</i> (1949) 78 CLR 199 (<i>Grimwade</i>) is cited by the Commissioner as authority that to be a transaction there must be a transaction with some other person. However, the decision does not actually support the	1. In paragraph 118 the final Ruling provides that if the private company beneficiary is made aware of its entitlement, and chooses not to call for the amount to which it is entitled or have it used for its sole benefit, the overall transaction will include: - the private company's decision to allow the UPE to remain outstanding for the benefit of the trust; and the - trustee's use of those funds for trust purposes. 2. In <i>Grimwade v Federal Commissioner of Taxation</i> (1949) 78 CLR 199, their Honours found that refraining to vote is insufficient of itself to amount to a transaction because it was not 'with another person'. However, in the case of a UPE that is not called for by the private company beneficiary and then utilised by the trustee for trust purposes, there has been a bilateral dealing such that a

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	Commissioner's reasoning. In <i>Grimwade</i> at CLR 220, their Honours in fact say that the mere act of refraining to vote against a particular resolution is insufficient to amount to a 'transaction'. A trustee deciding to distribute trust income to a private company beneficiary is no different to a shareholder deciding to vote in a particular way. Both decisions are discretionary and cannot be seen as a transaction 'with some other person'. 3. The draft Ruling (at paragraphs 98, 139, 147 and 152) cites the case of <i>Corporate Initiatives v Commissioner of Taxation</i> (2005) 142 FCR 279 for authority that a UPE could amount to a loan. <i>Corporate Initiatives</i> considered whether a UPE was a loan in the context of the trust loss provisions in Schedule 2F. Unlike paragraph 109D(3)(d), Schedule 2F does not require there to be a 'transaction' and is therefore not useful in construing when a loan will have arisen under subsection 109D(3)(d). 4. Paragraph 148 of the draft Ruling says that where a beneficiary has allowed a UPE to remain outstanding for use by the trust, it is equivalent to a UPE being paid to the beneficiary and lent back to the trust for use for broader trust purposes. This ignores the trust law relationship that has been created (typically one of sub-trust) and the manner in which trusts are operated in practice. It assumes that a UPE has been used as a means of providing financial accommodation without any evidence of the parties' intention to do so. 5. The draft Ruling acknowledges that a UPE is not a loan, so it should not be taken to be in substance a loan.	transaction has taken place. 3. <i>Corporate Initiatives</i> was cited in the context of what might amount to an 'in-substance loan'. <i>Corporate Initiatives</i> indicates that there will be a loan in-substance where a trustee uses a UPE for the benefit of all beneficiaries of the trust or at least for purposes other than for the sole benefit of the beneficiary to whom the UPE is owed. 4. Paragraph 148 of the draft Ruling considers the private company beneficiary allowing the UPE to remain outstanding for use for trust purposes rather than for the benefit of that private company. This does not ignore the trust law relationship. Where the trustee has set aside the UPE for the sole benefit of the private company or otherwise allows it to be used for the private company's sole benefit, the private company will not have 'allowed' the trustee to use the UPE for trust purposes. On the other hand where the UPE is used for trust purposes and the private company beneficiary knows this but does nothing to prevent it (such as by calling for payment of the UPE) – it will have implicitly approved or allowed this use, in substance providing a loan of the amount of the UPE to the trustee. The Commissioner's view of the substance of this arrangement has been expanded in paragraph 123 of the final Ruling. 5. The final Ruling explains that where a private company beneficiary has allowed its UPE to remain outstanding and not used for its sole benefit, it has in substance provided an ordinary loan to the trustee.
E: ISSUES WITH EXAMPLES		

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1.	Examples	
	The following comments were made with regard to the examples in the draft Ruling.	
	Example 1	
	The example confusingly appears to establish two separate loans, the first by the crediting of a loan account in paragraph 1 and the second in paragraph 2 by entering into the agreement. This confusion should be eliminated by redrafting.	There is only one loan. This is clarified in the final Ruling.
	Example 2	
	Paragraph 32 of the draft Ruling states that '... Trustee Ltd it [sic] has made a loan to itself as Trustee of the AB Family Trust.' An entity cannot lend money to itself and this paragraph therefore does not make sense.	In this example, the trustee acts on behalf of the private company beneficiary in lending money to itself. Effectively, the trustee is borrowing money from the private company, and the trustee is itself providing those loan funds on behalf of the private company beneficiary by way of an application of trust funds for the benefit of that private company beneficiary.
	Example 3	
	It seems that a private company beneficiary will need to understand what has occurred before it can be taken to have acquiesced to a loan having arisen. The point at which the directors sign off on the private company beneficiary's accounts (and liabilities) is arguably an indication of their acquiescence to the treatment in the accounts. The timing of that sign off will not always coincide with the preparation of the income tax return.	This may very well be correct as a matter of fact in particular circumstances. When the Commissioner will administratively accept the private company as having the requisite knowledge will be discussed in a Law Administration Practice Statement, of which the draft has been released for public comment.
	Example 4	
	The example does not consider on-lending where the journals show the payment of part of all of the UPE to the private company beneficiary and that the private company beneficiary made the loan to the shareholder.	In the draft Ruling this example considered a situation where the private company was taken to have been paid its trust entitlements and have loaned that amount back to the trustee. In such a situation, if the private company had <i>also</i> loaned money to a shareholder, that loan would be subject to a straightforward application of Division 7A. Example 4 has been updated in the final Ruling to provide that where there is evidence that the company has not authorised the treatment by the trustee of the UPE as having been satisfied and lent back, no ordinary loan will be taken to arise by agreement (including by acquiescing with knowledge).
	Example 5 (Example 7 in final Ruling)	

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	The situation described in example 5 of the draft Ruling is not reflective of how trusts operate in practice. Generally, trust deeds state that UPEs are held on trust for the beneficiary. They are rarely specifically set aside in a physical sense and lent back or reinvested in the main trust. Accordingly, Example 5 does not assist in practice as sub-trusts differ according to the specific trust deed which gave rise to it. It is not feasible to apply such a specific example to most sub-trusts and the example should therefore be removed and replaced with a statement that the application of Division 7A to sub-trusts would have to be considered on a case-by-case basis.	In discussions with interested parties this was raised as a scenario for the Commissioner to consider so it is appropriate to be included in the examples addressed. The situation where a sub-trust is not created when a UPE arises has also been addressed in the new Example 5.
	<i>Example 6 (Example 8 in final Ruling)</i>	
	A number of matters remain uncertain regarding the effect of Example 6, specifically: - When will the ATO regard an investment in a main-trust as being on terms entitling the sub-trust to all of the benefits that flow from the use of those funds by the main-trust? What kind of tracing will be required? - Could the ATO confirm that entitlements held on sub-trust can be represented by appropriate accounting entries and do not have to be physically paid into a separate bank account? - Given that in practice the assets in a sub-trust are rarely (if ever) accounted for totally separately to the main trust, what sort of accounting records/evidence will need to be maintained to show that there actually is a sub-trust?	- As explained in response to issue 4 of section D of this compendium: 'Section three issues (loans within the extended meaning)', it is proposed that administratively the Commissioner will accept that a loan or investment by the sub-trust back into the main trust is an investment for the private company's sole benefit if that investment or loan is on terms requiring the payment of: - the actual benefits from that investment (for example, where the investment is in respect of a specific asset), or - a reasonable percentage of the income of the trust relative to the amount invested as compared with total trust funds, (in addition to a return of the principal lent or invested). This administrative treatment will be further detailed in a Law Administration Practice Statement, of which the draft has been released for public comment. - To the extent that these accounting entries are acceptable under trust law, a sub-trust will arise without a physical cash payment. - It is proposed that administratively the Commissioner will, subject to evidence to the contrary, accept that there is actually a sub-trust where: - the amount representing the UPE is set aside separately in the accounts of the main trust as being held on trust for the private company

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	4. As it is often very difficult to establish what (physical) assets/funds are held in a sub-trust as opposed to the main-trust, what type of evidence will the ATO accept to establish the income and expenses of the sub-trust? 5. Is the sub-trust required to distribute all of the principal and interest it receives from the main trust to the private company beneficiary each year? Can those distributions remain unpaid? 6. Instead of the sub-trust investing in the main trust, can the sub-trust <u>co-invest</u> in an asset with the main trust? In that case, the main trust would not owe a return to the sub-trust, but the sub-trust would gain a share of the benefit proportionate with its investment. 7. It is difficult to reconcile the statement at paragraph 11 of the draft Ruling (that a 'loan will not arise in the manner described in paragraph 9... where it is outside the power of the trustee to treat the funds otherwise than as a UPE') with Example 6, which	beneficiary; • separate accounts are prepared for the sub-trust; or • a separate bank account is opened in the name of the trustee as trustee for the private company beneficiary in respect of the funds within the sub-trust. This administrative treatment will be set out in a Law Administration Practice Statement of which the draft has been released for public comment. 4. A Law Administration Practice Statement (of which the draft has been released for public comment) will set out how to determine how much of the income of the main trust is attributable to the sub-trust where the sub-trust has invested its funds back into the main trust. See the response to issue 1 of this section of the compendium for further details. 5. So much of the UPE that is set aside on sub-trust for the sole benefit of the private company beneficiary will form the corpus of the sub-trust. There is no requirement that this be distributed to the private company each year from a sub-trust that physically holds those funds for the benefit of the private company or invests them back into the main trust for a full flow through return of the benefits from this investment. However, when the sub-trust derives income (for example, from an investment into the main trust) the sub-trust should pay this out to the private company or risk the application of Subdivision EA in respect of any relevant payments or loans it has made to, or amounts forgiven of, the shareholders or associates of shareholders of the private company (for example, a Division 7A loan it has made to the main trust). 6. Yes – where those assets are arm's length income producing assets or capital assets used (or proportionately used) for the private company's benefit, this would not result in the private company being taken to have provided financial accommodation to the main trust. Such examples will be addressed in a Law Administration Practice Statement, of which the draft has been released for public comment. 7. As explained in the response to issue 5 of the section titled Section two issues (ordinary loan) of this compendium, for a loan to arise as a result of a trustee exercising a power to apply funds for the benefit of a beneficiary, not only does the deed have to give the trustee this power, but the trustee has to have

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	seems to suggest that a loan might not be taken to arise if the trustee does have the power to treat a distribution otherwise than as a UPE.	exercised it. In Example 6 of the draft Ruling there is nothing to suggest that the trustee has exercised a power to apply funds on behalf of the private company in the form of creating a loan for the benefit of that private company. Instead, the trustee has created an entitlement to trust income in the private company, and set aside the amount of that entitlement on sub-trust for the sole benefit of that private company.
2.	Does the sub-trust need to lodge a separate tax return to the main-trust?	
	If taxpayers decide to set up their affairs in accordance with Example 6 of the draft Ruling, so that any investment by a sub-trust in a main-trust is on terms entitling the sub-trust to all of the benefits that flow from the use of the funds by the main-trust, will the sub-trust need to obtain its own Tax File Number and lodge separate tax returns?	As a general rule, the Commissioner requires trustees of trust estates to lodge a return in accordance with section 161. ² However, pursuant to Law Administration Practice Statement PS LA 200/2, a specific exemption is available to transparent trusts. It is proposed that where a sub-trust is created for the sole purpose of setting aside the funds representing the UPE for the absolute benefit of the private company beneficiary, the Commissioner will accept that the sub-trust is a relevant transparent trust. It is proposed that this administrative position will be set out in a Law Administrative Practice Statement, of which the draft has been released for public comment.
F: ISSUES WITH INTERACTION WITH SUBDIVISION EA		
1.	Interpretation may give rise to double tax	
	As there is no specific anti-overlap rule between the general rules in Division 7A and the specific UPE provisions in Subdivision EA, both could potentially apply. Where both Subdivision EA and section 109D are capable of applying, Subdivision EA should be applied rather than section 109D as it is more relevant practically as it follows through to where the cash ends up, which is consistent with the scheme of the balance of Division 7A of only taxing the taxpayer who gets the benefit of the actual cash or economic benefit.	Subdivision EA does not always apply to 'follow the cash' paid out of a trust to a shareholder or an associate of a shareholder in the form of a relevant payment, loan or forgiveness. It is limited to cash paid/lent/forgiven by the trustee that are reflected by UPEs of a relevant private company. If that private company had simply lent money to the trust rather than allowed its UPEs to remain outstanding, Subdivision EA would have no role to play even if the trust subsequently paid the cash out to shareholders or their other associates. That is, if all there is are loans, Subdivision EA will have no role to play. Consistently with this structural approach of Division 7A, the final Ruling observes (at paragraph 182) that the Commissioner will not treat a UPE that is subject to the Ruling and is considered to constitute a Division 7A loan as a present entitlement that remains unpaid for Subdivision EA purposes. This will be further clarified in a Law Administration Practice Statement,

² See for example Legislative Instrument TPAL 2009/1 – *Lodgment of returns for the year of income ended 30 June 2009*.

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		of which the draft has been released for public comment. Further, it is noted for completeness that there will be no issue of any overlap of provisions for those UPEs arising in the circumstances that were the pretence for former section 109UB (that is, UPEs set aside on separate trust for the sole benefit of the private company beneficiary). This is because these UPEs will not be taken to be subsection 109D(3) loans in any event (see Example 8 of the final Ruling).
2.	When a UPE has been 'paid' such that Subdivision EA no longer applies	
	At paragraphs 24 to 26 of the draft Ruling, the Commissioner attempts to explain how Subdivision EA interacts with the main provisions of Division 7A to prevent double taxation. The draft Ruling explains that where a UPE is treated as a loan under Division 7A, the UPE will have been 'paid' leading to the conclusion that Subdivision EA could not also apply to an amount that has been treated as a deemed dividend under section 109D. The conclusion that a UPE that has been treated as a Division 7A loan (as opposed to a loan within the ordinary meaning) has been paid is incorrect. A UPE is defined in subsection 109XA(4) as an entitlement that 'remained unpaid' as at certain dates. The term 'unpaid' is not defined for the purposes of subsection 109XA(4) and should therefore take its ordinary meaning. The definition of 'payment' in section 109C is not relevant. Even if section 109C was the appropriate definition, not calling for a UPE would not amount to a 'payment' under the section. The UPE would therefore remain unpaid unless and until it is fully discharged. There is therefore potential for both section 109D and Subdivision EA to apply to the same amount, effectively resulting in triple taxation (since the operation of Division 7A itself leads to double taxation).	The final Ruling concerns itself only with whether a UPE can be or become a loan within the meaning of subsection 109D(3). The comments that a UPE may remain unpaid until it is legally discharged have been noted. As set out in response to issue 1 of this section of the compendium, given the legislative context of Division 7A, the Commissioner will not treat a UPE that is subject to the final Ruling and is considered to amount to a Division 7A loan as an unpaid entitlement for Subdivision EA purposes. This interaction between the final Ruling and Subdivision EA will be further clarified in a Law Practice Administration Statement, of which the draft has been released for public comment.
G: OTHER TECHNICAL ISSUES WITH THIS RULING		
1.	Timing of when a loan may arise	
	The draft Ruling does not address the issue of when a UPE may	Under the final Ruling, a Section two loan will arise when the ordinary loan is

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	be converted into a loan. Specifically, it is not clear whether the loan from the private company back to the trust comes into existence when the UPE is created or at a later point in time. It was recommended that the ATO should adopt a position that, in the event that a UPE is taken to be a loan for Division 7A purposes, the loan should be held to arise at the time of the actual appointment of the income by the trustee. This could be up to 31 August in accordance with the Commissioner's administrative concession in Taxation Ruling IT 329.	made (that is, when it is agreed or made by the trustee on behalf of the private company). A Section three loan will arise when factually the private company has provided financial accommodation or made an in-substance loan to the trustee, which generally will not be until such time as it knows about its UPE, knows that it is not being set aside or used for its sole benefit, and chooses not to call for payment of that UPE. Factually, it is difficult to see how this could be any earlier than the time of actual appointment. The final Ruling also notes that a Division 7A loan may not in fact arise in respect of a UPE until some time during the income year in which the UPE is recognised for income tax purposes. Subject to sufficient evidence to the contrary the Commissioner will accept that this is what has happened. It is acknowledged that the timing of the Division 7A loans dealt with by the final Ruling is a factual matter for which pinpointing a precise time may be most difficult. Accordingly, it is proposed that the Commissioner will administratively accept that: • a Section two loan is taken to be made at the time it is made under the relevant loan agreement or where there is no such agreement the time when it was recognised in the accounts, and • a Section three loan is not made until the end of the income year following the year in which the UPE is taken to have arisen for income tax purposes (that is, a UPE that is taken to have arisen for Division 6 purposes on 30 June 2010 that the private company allows to remain intermingled and used by the trustee for trust purposes will not be taken to be a Division 7A loan until 30 June 2011. Further details of this administrative concession will be set out in a Law Administration Practice Statement, of which the draft has been released for public comment.
2.	When will a UPE remain a UPE?	
	The draft Ruling is not clear on when a UPE will remain as a UPE.	Whilst it subsists in equity and has not been satisfied (for example by being paid) a UPE will remain a UPE. The position taken in the draft Ruling and the final Ruling does not change this. Subsisting UPEs are not ordinary loans and therefore will only be potentially subject to Section three of the final Ruling.
3.	When will the sub-trust act as the agent of the private company?	

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	In paragraphs 167 to 169 of the draft Ruling, it is suggested that if the private company beneficiary is an absolutely entitled beneficiary of the sub-trust and is able to direct the trustee of the sub-trust, the private company would be taken to have made a Division 7A loan, unless there is sufficient evidence to the contrary. It is not clear what evidence must be presented to demonstrate that the sub-trust does not make the loan as agent for the private company.	The creation of an agency relationship between the sub-trust and private company beneficiary requires the private company to consent to the sub-trust acting in such a representative capacity. Pursuant to ordinary agency principles, consent may be implied from acquiescence. However, in situations where the trustee also has authority to make such loans in its capacity as trustee of the sub-trust, the acquiescence by the private company to the actions of the trustee may merely amount to an acknowledgement of the trustee's authority to deal with the funds in that trust, rather than consenting to the trustee acting as its agent. For this reason, the question of fact as to whether or not the trustee of a sub-trust is acting as agent of the private company beneficiary will not often be a straightforward matter. Accordingly, it is proposed that administratively the Commissioner will require evidence of the private company's <i>express</i> consent in the form of unequivocal language or conduct before the trustee of the sub-trust will be taken to be acting as agent for the private company beneficiary. This administrative treatment be set out in a Law Administrative Practice Statement, of which the draft has been released for public comment.
4.	The application of Part IVA where a sub-trust makes a loan to the main trust other than as agent for the private company beneficiary	
	1. At paragraph 169, the draft Ruling suggests that even if a sub-trust is not acting as agent for a private company in making a loan to the main trust, Part IVA may be applied unless the loan complies with sections 109N and 109E. If the terms of the loan are strictly commercial, why would the arrangement attract Part IVA? 2. If Part IVA would ultimately apply to the arrangement, it would seem that the various examples in the draft Ruling are redundant because they all point to the conclusion that unless there is a complying Division 7A loan in place, either Division 7A or Part IVA would apply. If this is the Commissioner's position he should simply state this and apply the treatment only prospectively.	These issues are acknowledged. As it is not suggested that Part IVA should apply to the Examples in the final Ruling where a Division 7A loan does not arise on those facts alone, and any income of the sub-trust to which the private company beneficiary is paid out to the private company, the reference to its potential application has been removed from the final Ruling.
5.	Meaning of terms used in Ruling	
	Agreement	
	Whilst there are a number of references to the term 'agreement' in	When an agreement arises is to be determined by general principles and is not

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	the draft Ruling, there is no definition (or guidance provided as to the meaning of) that term for the purposes of the draft Ruling.	limited to circumstances where an ordinary agreement has been reduced to writing: see for example in paragraph 56 of the final Ruling.
	'Extinguished'	
	The draft Ruling refers to a UPE being 'extinguished' and converted into a loan back to the trust at paragraph 8 but does not explain how a UPE can be extinguished.	The reference to extinguished has been replaced with 'satisfied' for consistency and to better accord with general concepts regarding UPEs.
	Ordinary loan	
	The draft Ruling is not clear on what exactly will be considered an 'ordinary loan' under Section two.	Under Section two of the final Ruling an ordinary loan will arise where there is in fact a loan. This will be a question of fact, but an ordinary loan may arise for example where the parties have agreed for the private company to lend money to the trust (including where the trust has treated the private company's trust entitlements as having been paid and lent back and the private company has acquiesced with knowledge of this treatment), or where the trust has applied trust funds for the benefit of the private company and has done so by crediting a loan account in the private company's name. An outline of how the Commissioner will practically administer this question of fact will be detailed in a Law Administration Practice Statement, of which the draft has been released for public comment.
6.	No reference to the Explanatory Memorandum to the bill that introduced Subdivision EA	
	There are no references made to the Explanatory Memorandum to the <i>Taxation Laws Amendment (2004 Measures No. 1) Bill 2004</i> [the 2004 Explanatory Memorandum] which ultimately introduced Subdivision EA into Division 7A. Instead, references are only made to the Explanatory Memorandum to the <i>Taxation Law Amendment Bill (No. 3) 1998</i> [the 1998 Explanatory Memorandum], which introduce the now repealed section 109UB. As Subdivision EA is now the law, it would be more appropriate that any arguments to be raised in the draft Ruling about the current law should refer to the law in the context of the current terms of Division 7A (now inclusive of Subdivision EA).	The 2004 Explanatory Memorandum is referred to in paragraph 50 of the final Ruling (and paragraph 103 and 158 of the draft Ruling). References to the 1998 Explanatory Memorandum introducing Division 7A and former section 109UB are also made to explain the policy intent of Division 7A and the predecessor to Subdivision EA (the former section 109UB): see paragraph 58, 159 and 161 of the draft Ruling and paragraphs 31 and 173 of the final Ruling.
7.	Trustee is the legal entity, not the trust	
	The draft Ruling refers to actions of the 'trustee' and the 'trust'	The final Ruling now consistently refers to actions of the trustee of the trust.

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	interchangeably. The trustee is the relevant legal entity and should therefore be referred to consistently.	
8.	Fixed trusts	
	The draft Ruling is not clear that it applies to both discretionary and fixed trusts.	UPEs may arise other than as a result of an exercise of a discretion (for example, they may arise under the terms of a fixed unit trust). Paragraph 33 of the final Ruling has been modified to cater for these (non-discretionary arrangements).
H: STYLE AND FORMATTING ISSUES		
1.	Comments as to the form of the Ruling	
	1. The draft Ruling deals with at least five separate scenarios in which Division 7A could potentially apply in respect of a UPE but these scenarios are spread throughout the draft Ruling. It would be easier to understand if each of the scenarios was dealt with in a clearly defined separate section or sub-section. 2. It should be clearly evident which scenario each example is dealing with and what section of the final Ruling it addresses. 3. The passive voice is used extensively in the draft Ruling, which makes it more difficult to comprehend. 4. The draft Ruling contains unnecessary repetition, for example subsection 109D(3) is set out in its entirety four times. 5. The draft Ruling does not contain sufficient cross referencing between paragraphs. 6. The ATO has a general practice of including examples within the explanation section rather than within the body of the ruling. This practice was not followed in the draft Ruling. 7. The draft Ruling employs headings incorrectly or in the wrong position – see for example the heading 'loans within the ordinary meaning' located two paragraphs earlier than it should be located. 8. The draft Ruling does not address issues in a logical order.	1. The structure of the final Ruling has been improved to more clearly identify the types of loans being discussed in a logical and less repetitious manner. 2. The examples have been updated in the final Ruling to clearly identify which section of the Ruling they fall under and what scenario they are addressing. 3. The ATO has made an effort to improve this in the final Ruling. 4. Repetition has been reduced in the final Ruling. 5. Cross referencing has been improved in the final Ruling. 6. Current ATO practice is to generally include examples in the binding section of a taxation ruling. However due to numerous comments received in respect of this point and the need to further elaborate on them they have been moved to a separate appendix, Appendix 2, in the non-binding section of the final Ruling. 7. Use of headings has been improved in the final Ruling. 8. Ordering has been adjusted in the final Ruling.

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	9. The draft Ruling failed to adopt a clear methodology when exploring undefined words and terms. 10. Italics are used for effect in paragraph 9 of the draft Ruling where the same words are in bold for effect in paragraph 120. 11. The draft Ruling uses awkward constructions involving header clauses and tail clauses rather than simple English. 12. The draft Ruling uses both 'private company beneficiary' and 'corporate beneficiary' interchangeably. 13. The draft Ruling uses both 'sub-trust' and 'separate trust' interchangeably.	9. A clearer methodology for explaining the meaning of undefined words (including the use of dictionaries) has been adopted in the final Ruling. 10. Emphasis has been standardised in the final Ruling. 11. Constructions have been improved in the final Ruling. 12. The term 'private company beneficiary' has been used consistently in the final Ruling. Subsequent references to the private company beneficiary in the same sentence or paragraph generally abbreviated to 'the private company' as allowed by context. 13. The final Ruling defines the relevant sub-trust as a separate trust that is a sub-trust of the main trust. The term sub-trust is then used consistently.
I: ADMINISTRATIVE AND OTHER ISSUES		
1.	Potential for confusion	
	The draft Ruling adds significant complexity to Division 7A which is already a complex section of the Act. The ATO will need to devote significant resources to educating taxpayers and tax agents on the interpretation in the ruling and on its interaction with Subdivision EA.	The final ruling clarifies the ATO view in respect of the application of section 109D to and in respect of UPEs. Further administrative guidance will be provided in a Law Administration Practice Statement, of which the draft has been released for public comment.
2.	Interest on a Division 7A compliant loan	
	It should be made clear that interest paid on a UPE 'loan' which is put on Division 7A compliant terms will be deductible where the funds are being used as working capital in a business carried on by the trustee of a trust. Alternatively, a UPE may be refinanced using an external loan, so that the UPE can be repaid to the private company beneficiary. However, interest paid on those external loans may not be tax deductible in accordance with the principles contained in TR 2005/12. The Commissioner should therefore give full consideration to the issue of deductibility of interest on a loan which has been converted from a UPE.	The usual rules concerning the deductibility of interest will apply to any interest charged on a loan from a private company or an external lender. Nonetheless, for the avoidance of doubt it is proposed that the interaction of the final Ruling with TR 2005/12 in respect of such interest deductibility will be further clarified in a Law Administration Practice Statement, of which the draft has been released for public comment.
3.	Pre 16 December 2009 amounts and the impact of section 100A	

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	There is continuing uncertainty for taxpayers in relation to the treatment of UPEs pre 16 December 2009 (when the draft Ruling was released) as to whether they could be deemed to be something other than a UPE or to the potential application of section 100A. Without greater clarity on this both taxpayers and their advisers will continue in an uncertain position on any possible construction by the Commissioner on such UPEs.	The final Ruling considers Division 7A and does not address section 100A. Where the private company has been made entitled to an amount from a trust broadly as a result of a reimbursement agreement entered into for a purpose of paying less income tax, section 100A may apply according to its terms.
4.	High Court decision in <i>Bamford</i>	
	The draft Ruling fails to consider the impact of the definition of 'trust income' in the decision of <i>Commissioner of Taxation v Bamford</i> ; <i>Bamford v Commissioner of Taxation</i> [2010] HCA 10; 264 ALR 436; [2010] ATC 20-170 (30 March 2010).	The decision in <i>Bamford</i> is not relevant to the issue of whether a UPE may be a loan for Division 7A purposes. If the amount of a UPE is treated for tax purposes as a loan deemed to be a dividend paid by the private company to the trustee which is included in the net income of the trust estate then, broadly speaking, <i>Bamford</i> is authority for the beneficiaries of the trust (including the private company) including their proportionate share of that net income in their assessable income.
5.	Operation of PS LA 2007/20	
	The draft Ruling fails to consider the operation of PS LA 2007/20 (dealing with the Commissioner's discretion under section 109RB of Division 7A) and its recognition of issues arising under Subdivision EA.	PS LA 2007/20 only applies to certain transactions of actions in the 2002 to 2007 income years and 'corrective action' taken from 1 July 2007 to 30 June 2008. However, where a private company is taken to pay a dividend as a result of a loan made as set out in the final Ruling, the Commissioner may decide to exercise his discretion to disregard this dividend if it arose due to an honest mistake or inadvertent omission. It is proposed that the potential for the Commissioner's discretion to apply in respect of loans falling within the scope of the final Ruling will be confirmed in a Law Administration Practice Statement, of which the draft has been released for public comment.
6.	Payments of the private company beneficiary's tax liability	
	The draft Ruling fails to consider whether the Commissioner will treat payments of the private company's tax liability by the trustee as loan repayments and if so whether such payments can be apportioned between different loans.	This will be a question of fact. If the private company and trustee have entered into a loan agreement on section 109N compliant terms, they may agree that a repayment be directed towards payment of the tax bill of the private company. Alternatively, the payment of tax may be a result of the trustee deciding to apply additional trust funds for the benefit of the private company. The parties' treatment of the payment will likely be very relevant in deciding this.

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7.	'Fixed trust' loss rules in Schedule 2F	
	The ATO should provide administrative guidance on whether the 'fixed trust' loss rules in Schedule 2F apply to the sub-trust with the 'non-fixed trust' loss rules applying to the main trust, and whether the sub-trust may need to make its own family trust elections or interposed entity elections, or whether the elections made by the main trust also cover the sub-trust).	A sub-trust may be established in many different ways, and the trustees of sub-trusts may enjoy a wide range of discretions according to the terms of the relevant trust deed. The trust loss rules in Schedule 2F will apply according to their terms on the basis of the features of the relevant trust. A detailed consideration of Schedule 2F is beyond the scope of the final Ruling and also beyond the scope of this compendium of comments.
8.	Section 109R	
	There is a concern that section 109R will apply so that if a UPE that is treated as a Division 7A loan is paid out, and replaced with a loan back to the trust on 109N compliant terms, 109R would prevent the UPE treated as a Division 7A loan from being taken to have been paid. If correct, this would result in a deemed dividend arising in respect of the UPE in addition to a compliant Division 7A loan requiring minimum repayments etcetera in respect of the loan back.	It is not readily apparent that this situation will arise in practice, particularly where it is noted that the Commissioner proposes that where a UPE is treated as being a Division 7A loan, that loan will not be taken to have been made until the year after the year in which the UPE arose for tax purposes (see response to issue 1 of section G of this compendium of comments: 'Other technical issues with this Ruling'). Nonetheless, for the avoidance of doubt, it will be clarified in the proposed Law Administration Practice Statement that where a UPE is considered to be a loan for Division 7A purposes, if the UPE is paid out and replaced with a loan under a complying loan agreement before the lodgement day for the year of income when the Division 7A loan is taken to have been made, the ATO will treat the payment of the UPE as being a repayment and not seek to apply section 109R.