

# ***LCR 2015/6 - Attribution Managed Investment Trusts: character flow through for AMITs***

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⚠ This document has changed over time. This is a consolidated version of the ruling which was published on *19 February 2018*



## Attribution Managed Investment Trusts: character flow-through for AMITs

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### Relying on this Ruling

This publication is a public ruling for the purposes of the *Taxation Administration Act 1953*.

This Ruling describes how the Commissioner will apply the law as amended by the *Tax Laws Amendment (New Tax System for Managed Investment Trusts) Act 2016*.

If you rely on this Ruling in good faith, you will not have to pay any underpaid tax, penalties or interest in respect of matters it covers if it does not correctly state how a relevant provision applies to you.

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### What this Ruling is about

1. If you are a member of an attribution managed investment trust (AMIT), the trustee of that AMIT may attribute various tax amounts to you. How those amounts are taxed to you depend on their character.
2. The amounts you have been attributed will be shown on the AMIT member annual statement (AMMA statement) issued to you. These may include various amounts of the AMIT's assessable income (net of relevant deductions), exempt income, NANE income and tax offsets.
3. This Ruling explains the rule which ensures that amounts attributed to you retain the character the amounts had in the hands of the trustee of the AMIT.

### Date of effect

4. This Ruling is a public ruling, effective for those who rely on it in good faith in respect of assessments for income years starting on or after:
  - 1 July 2016, or
  - if the trustee of the AMIT has made an irrevocable choice to apply the new tax system for its 2015-16 income year which starts on or after 1 July 2015 – 1 July 2015.

### Explanation

5. Under the AMIT regime<sup>1</sup>, amounts of 'determined trust components' are worked out by the AMIT and attributed to its members on a fair and reasonable basis, in accordance with the constituent documents (such as the constitution or deed) of the AMIT, based on their membership interests in the trust.<sup>2</sup> The amounts so attributed are the members' 'determined member components'. These amounts may include assessable income, exempt income, non-assessable non-exempt income, tax offsets, and credits of different characters.
6. Where an amount of a particular character is derived, received, made by or paid by an AMIT, and forms part of a determined trust component amount attributed to you as a member, you are treated as if that amount had been derived, received, made by or paid to you directly, rather than through the trust, and in the same circumstances as the trustee<sup>3</sup>, to the extent those circumstances gave rise to the particular character.<sup>4</sup>
7. As a result, you are taxable in respect of the attributed amounts in your own right, rather than as a member of the trust.
8. Under this rule, you can be described as 'standing in the shoes' of the trustee. The tax effects on you of being attributed amounts by the trustee are broadly what they would have been, had you been in the trustee's place, deriving, receiving, making or paying those amounts yourself.
9. The following explanation provides an overview of what character amounts that are attributed from AMITs may have, and how they may be treated in the hands of members generally. Not all parts of this explanation may be relevant to your own circumstances.

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<sup>1</sup> Contained in Division 276 of the *Income Tax Assessment Act 1997* (ITAA 1997). All legislative references in this Ruling are to the ITAA 1997 unless otherwise indicated.

<sup>2</sup> See Law Companion Ruling LCR 2015/7 *Attribution Managed Investment Trusts: attribution on a 'fair and reasonable' basis* for more information about this requirement.

<sup>3</sup> But ignoring the residence of the trustee of the AMIT and the place of the central management and control of the AMIT for these purposes (see subsection 276-85(7)).

<sup>4</sup> Subsections 276-80(2), (3), (5) and (6).

### **What are ‘characters’?**

10. ‘Character’ is not defined in the Act. The notion of character is a broad concept. In essence, an amount has a particular character if the Act requires that amount to be treated differently from other amounts, and its separate recognition affects the tax treatment of a member to whom the amount is attributed.

11. While subsections 276-80(1) and (4) give general descriptions of character that are consistent with the way the term ‘trust component’ is defined in subsection 276-260(1), those subsections do not restrict the types of character that the trustee of an AMIT can recognise. It is usually appropriate for the trustee to identify more specific types of character. The Act itself recognises examples of other types of character, such as discount capital gains<sup>5</sup>.

12. Under the heading ‘What is an amount of a particular character’, the Explanatory Memorandum to the Tax Laws Amendment (New Tax System for Managed Investment Trusts) Bill 2015 explains that:

- 3.17 An amount has a particular character for income tax purposes if the income tax law treats the amount in a way that is distinct to the way that it treats another kind of amount.
- 3.18 The character of a particular amount will depend on the activities of the attribution MIT that gave rise to the amount and the source of the amount.
- 3.19 Amounts of a particular character fall broadly into four main categories:
- assessable income;
  - exempt income;
  - non-assessable non-exempt income; and
  - tax offsets.
- 3.20 Examples of amounts of assessable income that are of a particular character which typically need to be identified by an attribution MIT include:
- discount capital gains;
  - non-discount capital gains;
  - dividends, interest or royalties that are subject to withholding tax; and
  - foreign source income.

13. In general, amounts of particular character relevant to the AMIT would be expected to be consistent with those used for the purpose of preparing members’ AMMA statements.

### **Example 1: Character for AMIT purposes**

14. In an income year, an AMIT derives Australian sourced and foreign sourced income. As amounts of these respective characters are treated differently by some taxpayers, each is a ‘character’ for AMIT purposes.

15. If, instead, the AMIT derived an amount of ordinary income in NSW, the fact that it was derived in that State (as distinct from another Australian state) is not in itself relevant for income tax purposes: the Act does not treat income derived in NSW differently to income derived in any other state. This distinction would not inform the character of the amount for the purposes of attribution under the rules in Division 276. Rather, its character for AMIT attribution would be that of Australian sourced ordinary income.

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<sup>5</sup> See subsection 276-85(3).

### **How does the character flow through to the member?**

16. Subsections 276-80(2) and (3) apply to determined member components which have a character relating to assessable income, exempt income or non-assessable exempt income.
17. The provisions ensure that the character of each attributed amount flows through to the relevant member. This is achieved, first, by assuming that the member derived, received, made or paid the relevant amount of a particular character in the member's own right, rather than as a member of the trust.<sup>6</sup> Then, each attributed amount is taken to flow to the member broadly in the same circumstances as it flowed to the AMIT, to the extent those circumstances gave rise to the particular character of that attributed amount.<sup>7</sup>
18. This two-fold approach not only has the effect of ensuring that the member is taxed on those attributed amounts, but also ensures that the member is taxed in the appropriate way, such as by ensuring that provisions of the Act relating to the taxation of specific income types are relevantly engaged.
19. Special rules apply where the determined member component has the character of a discount capital gain (see Example 5 of this Ruling).
20. Corresponding to subsections 276-80(2) and (3), analogous rules apply to determined member components that have characters related to tax offsets.<sup>8</sup>
21. Again, special rules apply in the context of tax offsets: determined member components relating to franking credit gross up amounts included in assessable income, and franking credit offsets, are dealt with separately.

### **Example 2: foreign source income**

22. *An AMIT member is attributed a \$50 determined member component with the character of foreign source income. The \$50 is included in the member's assessable income in the same way that foreign source income would be included, had the member made the gains in their own right. If the member is a foreign resident, this inclusion is limited by the rules in subsection 6-5(3).*

### **Example 3: unfranked distribution**

23. *A resident AMIT member is attributed a \$100 determined member component with the character of an unfranked distribution. The \$100 is included in the member's assessable income under section 44 of the Income Tax Assessment Act 1936, as this is the same way an unfranked distribution would be included in the member's assessable income had they derived the dividend directly in their own right and in the same circumstances as the AMIT trustee – here, as a member of the company paying the unfranked dividend.*

### **Example 4: franked distribution**

24. *The trustee of an AMIT receives a franked distribution from a company, of which it attributes \$100 (inclusive of attached franking credits) to a member. This is shown in the member's AMMA as determined member components with the character of: \$70 franked distribution, \$30 franking credit gross up, and \$30 franking credit.*

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<sup>6</sup> Paragraph 276-80(2)(a).

<sup>7</sup> Paragraph 276-80(2)(b).

<sup>8</sup> Subsections 276-80(5) and (6).

25. For the purpose of working out whether to include an amount in their assessable income, the member is considered to be the shareholder of the company paying the distribution. This is because the trustee received the distribution in the capacity as a shareholder and therefore these circumstances – which are relevant to the character of the amount as a dividend – flow through to the member. The rule in subsection 276-80(2) also results in the member's being deemed to have derived a franked distribution of \$70. The member is, accordingly, required to make the franking credit 'gross-up' of \$30 directly. The member includes both the franking credit and gross-up (totalling \$100) in their assessable income, and – if they are a qualified person in respect of the distribution<sup>8A</sup> and not otherwise disentitled<sup>8B</sup> – is allowed a \$30 tax offset.

26. The rule in subsections 276-80(5) and (6) results in the member being deemed to have received the franking credit directly.

27. In addition, a special rule in subsections 276-85(5) and (6) recognises that in some circumstances, the application of expenses may mean that the determined member component of a franking credit gross-up is less than the determined member component of a franking credit.

28. To deal with these circumstances, subsection 276-85(6) alters the normal imputation rules<sup>9</sup> so that the member's franking credit gross-up is limited to the amount of the determined member component that has the character of a franking credit gross up (rather than being equal to the amount of the franking credit otherwise attached to the franked distribution). The amount of the franking credit that may be available as a tax offset<sup>10</sup> will not be similarly limited – an offset will potentially be available in respect of the entire determined member component having the character of a franking credit.<sup>10A</sup>

#### **Example 4A: franking credit gross-up offset by deductions**

28A. The trustee of an AMIT receives a franked distribution of \$70,000 from a company. The franking credit on the distribution is \$30,000. In working out the trust components of amounts having the character of a franked distribution and franking credit gross up, the trustee allocates deductions against these two amounts<sup>10B</sup>. After subtracting the deductions, the trust components are \$63,000 and \$27,000 respectively. The trustee attributes \$6,300 (franked distribution) and \$2,700 (franking credit gross-up) to Member A. While the franking credit gross-up is \$2,700, the potential tax offset available to member A is \$3,000, representing the member's share of the franking credits on the distribution. The availability of the tax offset would depend on whether the tax offset conditions in Division 207 have been satisfied, such as the qualified person requirement.<sup>10C</sup>

<sup>8A</sup> See paragraph 29 of this Ruling.

<sup>8B</sup> See paragraphs 30-33 of this Ruling.

<sup>9</sup> Specifically, subsection 207-20(1).

<sup>10</sup> Subsection 207-20(2) – subject to relevant integrity rules such as those in Subdivision 207-F.

<sup>10A</sup> Subsection 276-85(6) applies if the member (not being a member in the capacity of trustee of another trust) has a determined member component of the character of assessable income under subsection 207-20(1). Where the AMIT is itself a beneficiary of another AMIT or non-AMIT trust which receives the franked distribution, the character of the trust component to the AMIT will be of a franked distribution and franking offset. Any franking credit gross up component attributable to this distribution will be of a character of assessable income under subsection 207-20(1).

<sup>10B</sup> Whether deductions are properly allocable against assessable income having a character of franked distributions and franking credits on the distribution must be determined by reference to the facts and circumstances. Rulings relating to the allocation of deductions are contained in Law Companion Ruling LCR 2015/8 *Attribution Managed Investment Trusts: the rules for working out trust components – allocation of deductions*.

<sup>10C</sup> See paragraphs 29 to 33 of this Ruling.

### **Flow through of qualified person status**

29. One of the requirements before a tax offset equal to the franking credit is available is that the member must be a qualified person in respect of the franked distribution.<sup>11</sup> If the trustee is a qualified person in relation to the distribution, the member will be deemed to be a qualified person in respect of the franked distribution because the member is deemed to have derived the franked distribution in the same circumstances as the trustee. This applies except when the Commissioner makes a determination under section 276-90 relating to the member.

### **Commissioner's determination on 'qualified person' status**

30. The Commissioner may make a determination in writing that a specified member or a specified class of members of a specified AMIT is not a qualified person in relation to the AMIT for an income year. If the Commissioner makes this determination, the member is not a qualified person in relation to a distribution(s) from the AMIT for the income year. Consequently, the member is not required to include the amount of the relevant franking credit gross-up in its assessable income, and is not entitled to a tax offset for the amount of the franking credits.

31. If the distribution flows indirectly through the member to another entity, the franking credit gross-up is not required to be included in the assessable income of the other entity, and the other entity is not entitled to a tax offset for the amount of the franking credits.

32. In deciding whether to make a determination, the Commissioner may consider:

- arrangements entered into by the member that directly or indirectly reduce the economic exposure of the member to changes in the value of their membership interests in the AMIT
- the lack of such arrangements
- the length of time the member has been a member, and
- any other matters the Commissioner considers relevant.<sup>12</sup>

33. The Commissioner may also consider whether the member had been a member for a continuous period of at least 45 days, at least one of which occurred in the relevant income year.

### **Further examples of character flow-through**

34. Examples 5 to 7 of this Ruling further demonstrate how character flow-through applies to amounts that are attributed to members and the taxation consequences that follow.

#### **Example 5: discount capital gains**

35. *In an income year, an AMIT makes a discount capital gain of \$600,000, and incurs a capital loss of \$100,000, both from assets that are taxable Australian property, resulting in a net capital gain of \$250,000 (( $\$600,000 - \$100,000$ ) x 50%).*

36. *A component with the character of a discount capital gain of \$250,000 is attributed to a resident beneficiary. The beneficiary is taken to have made a capital gain from a CGT event happening in relation to the relevant Australian property in their own right, and by subsection 276-85(4) the beneficiary's determined member component associated with the discount capital gain is treated as being double what it would otherwise be but for that subsection, that is double \$250,000, equalling \$500,000.*

<sup>11</sup> Paragraph 207-145(1)(a).

<sup>12</sup> Subsection 276-90(5).

37. Treating the member as making a capital gain of \$500,000, allows them to offset their own capital losses against the gain, and apply any CGT discount they are entitled to in their own right. Specifically, when applying the CGT discount, the member is treated as deriving the capital gain in the same circumstances as the AMIT: if the AMIT held the asset for more than 12 months before disposal, then the member will also be treated as having made a gain on an asset held for more than 12 months.<sup>13</sup> Therefore, providing the member is an entity that is eligible for the CGT discount (for example, an individual), they may be able to access the CGT discount.

#### **Example 6: foreign income tax offset**

38. The Docklands trust is an AMIT for an income year. In the income year, it derives \$1,000,000 foreign source income directly on which \$100,000 foreign tax has been paid by another entity. The Docklands trust's determined trust component with the character of foreign source income is \$1,000,000 (inclusive of a \$100,000 gross-up for the foreign tax that was paid)<sup>13A</sup>.

39. X Co is a resident beneficiary in the Docklands trust. X Co has a determined member component with the character of foreign source income equal to \$500,000. X Co also has attributed to it a determined trust component of a foreign income tax offset (FITO) character being its share (\$50,000) of the foreign tax paid of \$100,000.

40. Because of subsection 276-80(2), X Co includes in its assessable income the \$500,000 of foreign source income attributed to it.

41. Under subsections 276-80(5) and (6), X Co may also be entitled to the benefit of the attributed FITO.

#### **Example 7: FITO – AMIT treated as a transparent entity under foreign law**

42. Assume the same facts as Example 6, except that the Docklands trust is treated as a transparent entity under foreign law, and foreign tax has been paid in respect of the members of the trust.

43. Because of subsection 276-80(2), X Co includes the amount of the foreign source income attributed to it in its assessable income for the income year.

44. X Co will be treated as having an arrangement to pay foreign tax under subsection 770-130(2). Under section 770-10, X Co may be entitled to a tax offset for the income year to the extent of the foreign income tax paid in respect of the amount included in X Co's assessable income for that year.

#### **Further implications of character flow-through**

##### **Scrip roll-overs**

45. In determining the tax effect of an amount being attributed to a member, issues can arise as to whether relevant elections and thresholds are to be tested at the level of the AMIT or at the level of the member. The scrip for scrip roll-over rules provide a useful case study.

<sup>13</sup> Subsection 276-80(2).

<sup>13A</sup> Determined trust components with a character of foreign source income on which no foreign tax is paid also have a character of foreign source income. This may be relevant to the calculation of a foreign income tax offset limit under section 770-75.

46. The scrip for scrip roll-over provisions in paragraph 124-780(3)(d) permit the interest holder to choose whether to roll over a gain. In an AMIT context, choosing to apply the roll-over means there is no amount of gain made by the trust to attribute to a member in the first place. It follows that the choice can only be made by the AMIT (and not the member). The fact that a member holds their interest in the AMIT on revenue account does not preclude the AMIT from making the choice to access the roll-over.

47. Relevant to the application of the roll-over is whether there is a significant or common stakeholder for the arrangement.<sup>14</sup> As the choice to apply the roll-over is one for the trustee of the AMIT, rather than a member, it is the AMIT (not the member) that is subjected to the significant or common stakeholder test.

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**Commissioner of Taxation**

5 May 2016

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**References**

ATOlaw topic(s)	Income tax -- Trusts -- Other
Legislative references	ITAA 1997 ITAA 1997 6-5(3) ITAA 1997 124-780(3)(d) ITAA 1997 124-782 ITAA 1997 124-783 ITAA 1997 Div 207 ITAA 1997 Subdiv 207-F ITAA 1997 207-20(1) ITAA 1997 207-20(2) ITAA 1997 207-145(1)(a) ITAA 1997 Div 276 ITAA 1997 276-80(1) ITAA 1997 276-80(2) ITAA 1997 276-80(2)(a) ITAA 1997 276-80(2)(b) ITAA 1997 276-80(3) ITAA 1997 276-80(4) ITAA 1997 276-80(5) ITAA 1997 276-80(6) ITAA 1997 276-85(3) ITAA 1997 276-85(4) ITAA 1997 276-85(5) ITAA 1997 276-85(6) ITAA 1997 276-85(7) ITAA 1997 276-90 ITAA 1997 276-90(5) ITAA 1997 276-260(1) ITAA 1997 770-10 ITAA 1997 770-75

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<sup>14</sup> Sections 124-782 and 124-783.

	ITAA 1997 770-130(2) Tax Laws Amendment (New Tax System for Managed Investment Trusts) Act 2016
Related Rulings/Determinations	Law Companion Ruling LCR 2015/7 <i>Attribution Managed Investment Trusts: attribution on a 'fair and reasonable' basis</i> Law Companion Ruling LCR 2015/8 <i>Attribution Managed Investment Trusts: the rules for working out trust components – allocation of deductions</i>
Other references	<a href="#">Explanatory Memorandum</a> to the Tax Laws Amendment (New Tax System for Managed Investment Trusts) Bill 2015