TD 2005/D42 - Income tax: consolidation: imputation: will the benchmark rule in section 203-25 of the Income Tax Assessment Act 1997 apply in a franking period to the provisional head company of a MEC consolidated group if it is a 100% subsidiary of a foreign parent company that has more than one class of membership interest on issue?

This document has been finalised by TD 2006/20.

Draft Taxation Determination

Income tax: consolidation: imputation: will the benchmark rule in section 203-25 of the *Income Tax Assessment Act 1997* apply in a franking period to the provisional head company of a MEC consolidated group if it is a 100% subsidiary of a foreign parent company that has more than one class of membership interest on issue?

Preamble

This document is a draft for industry and professional comment. As such, it represents the preliminary, though considered views of the Australian Taxation Office. This draft may not be relied on by taxpayers and practitioners as it is not a ruling for the purposes of Part IVAAA of the ***Taxation Administration Act 1953****. It is only final Taxation Determinations that represent authoritative statements by the Australian Taxation Office.*

1. Yes, unless the foreign parent company satisfies the criteria set out in paragraph 203-20(1)(a) of the *Income Tax Assessment Act 1997* (ITAA 1997).

2. The foreign parent company will satisfy the criteria set out in paragraph 203-20(1)(a) of the ITAA 1997 if it is a listed public company that cannot make a distribution on one membership interest during the franking period without making a distribution under the same resolution on all other membership interests. If the foreign parent company is a New Zealand (NZ) resident that is an NZ franking company within the meaning of section 220-30 of the ITAA 1997, it must also satisfy a further requirement. The further requirement is that it must be unable to frank a distribution made on one membership interest during the franking period without franking distributions made on all other membership interests under the same resolution to the same extent.[1]

3. If the foreign parent company satisfies the criteria set out in paragraph 203-20(1)(a) of the ITAA 1997 so that the provisional head company is not subject to the benchmark rule, the provisional head company is still subject to the anti-streaming rules in Division 204 of the ITAA 1997 and section 177EA of the *Income Tax Assessment Act 1936* (ITAA 1936). The application of these rules will depend on the relevant facts and circumstances of each case.

[1] Subparagraph 203-20(1)(a)(iii) of the ITAA 1997.

Background and explanation

4. The benchmark rule in section 203-25 of the ITAA 1997 provides that an entity must not frank a distribution during a franking period at a franking percentage that is different from the benchmark franking percentage for that period.

5. Subsection 203-20(1) of the ITAA 1997 provides that the benchmark rule does not apply in a franking period to a company that satisfies the following criteria:

- at all times during the franking period, the company is a listed public company;
- the company cannot make a distribution on one membership interest during the franking period without making a distribution under the same resolution on all other membership interests; and
- the company cannot frank a distribution made on one membership interest during the franking period without franking distributions made on all other membership interests under the same resolution to the same extent.

6. A 100% subsidiary (as defined in subsection 995-1(1) of the ITAA 1997) of a company that satisfies the criteria in paragraph 5 is also exempt from the benchmark rules.[2]

7. Ordinarily the foreign parent company would not meet the Australian residency requirements and so would not be able to frank any distributions to its members.[3] Therefore, the third criterion in paragraph 5 would automatically be satisfied. However, a NZ franking company can frank certain distributions and therefore it would need to independently satisfy that criterion.

8. If the second criterion in paragraph 5 is also satisfied, the application of the benchmark rule to the provisional head company of the MEC (multiple entry consolidated) group will depend on whether its foreign parent company is a listed public company.

9. A listed public company is defined in subsection 995-1(1) of the ITAA 1997 as one whose shares (other than shares that carry a right to a fixed dividend) are listed for quotation in the official list of an approved stock exchange, unless specifically excluded by the definition having regard to who controls, or can benefit from, the company.

10. An approved stock exchange is one specified in Schedule 12 to the Income Tax Regulations 1936.[4]

Example

11. *Top Co is a public company listed on an approved United States stock exchange.[5] It otherwise satisfies the definition of a listed public company.*

[2] Paragraph 203-20(1)(b) of the ITAA 1997.
[3] Paragraph 202-5(a) of the ITAA 1997.
[4] See the definition of an approved stock exchange in subsection 995-1(1) of the ITAA 1997, section 470 of the ITAA 1936 and regulation 152I of the Income Tax Regulations 1936.
[5] Schedule 12 to the Income Tax Regulations 1936.

12. *Top Co has two classes of membership interests on issue. However, it cannot:*

- *make a distribution on one membership interest during a franking period without making a distribution under the same resolution on all other membership interests; or*
- *frank a distribution made on one membership interest during a franking period without franking distributions made on all other membership interests under the same resolution to the same extent.*

13. *A Co and B Co, Australian resident companies, are 100% subsidiaries of Top Co. A Co and B Co qualify as eligible tier-1 companies and they jointly choose to form a MEC group with A Co as the provisional head company.*

14. *Top Co would not be subject to the benchmark rule because it satisfies the criteria set out in paragraph 203-20(1)(a) of the ITAA 1997.*

15. *A Co, the provisional head company of the MEC group, would not be subject to the benchmark rule because it is a 100% subsidiary of a company that is itself not subject to the benchmark rule.*

16. *Whilst A Co is not subject to the benchmark rule, differential franking of its frankable distributions, or the frankable distributions of B Co which are taken to be distributions by A Co under section 719-435 of the ITAA 1997, may, depending on the relevant facts and circumstances, result in a breach of the anti-streaming rules in Division 204 of the ITAA 1997 or section 177EA of the ITAA 1936.*

Date of Effect

17. When the final Determination is issued, it is proposed to apply both before and after its date of issue. However, the Determination will not apply to taxpayers to the extent that it conflicts with the terms of settlement of a dispute agreed to before the date of issue of the Determination (see paragraphs 21 and 22 of Taxation Ruling TR 92/20).

Your comments

18. We invite you to comment on this draft Taxation Determination. Please forward your comments to the contact officer by the due date.

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Commissioner of Taxation
12 October 2005

Previous draft:

Not previously issued as a draft

Related Rulings/Determinations:

TR 92/20; TD 2005/D43

Subject references:

- company tax
- consolidation – franking
- consolidation – multiple entry consolidated group
- dividend streaming arrangements
- frankable dividends
- franking year
- imputation credits
- imputation system
- provisional head company

Legislative references:

- TAA 1953 Pt IVAAA
- ITAA 1997 202-5(a)
- ITAA 1997 203-20(1)
- ITAA 1997 203-20(1)(a)
- ITAA 1997 203-20(1)(a)(iii)
- ITAA 1997 203-20(1)(b)
- ITAA 1997 203-20(2)(a)
- ITAA 1997 203-25
- ITAA 1997 Div 204
- ITAA 1997 220-30
- ITAA 1997 719-435
- ITAA 1997 975-505
- ITAA 1997 995-1(1)
- ITAA 1936 177EA
- ITAA 1936 470
- ITR 1936 152I
- ITR 1936 Sch 12

ATO references

NO: 2005/14325
ISSN: 1038-8982
ATOlaw topic: Income Tax ~~ Consolidation ~~ companies
Income Tax ~~ Consolidation ~~ international
Income Tax ~~ Consolidation ~~ multiple entry consolidated groups
Income Tax ~~ Tax integrity measures ~~ dividend streaming and demerger benefits