

IT 2439 - Income tax: notification requirements for certain dividends paid by private companies under the phasing-out arrangements for Division 7

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TAXATION RULING NO. IT 2439

INCOME TAX : NOTIFICATION REQUIREMENTS FOR CERTAIN
DIVIDENDS PAID BY PRIVATE COMPANIES UNDER THE
PHASING-OUT ARRANGEMENTS FOR DIVISION 7

F.O.I. EMBARGO: May be released

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PREAMBLE With the introduction of the imputation system of company tax, which involves the alignment of the company tax rate with the maximum marginal rate of personal income tax, the additional tax on the undistributed income of private companies will last apply, in its traditional form, to profits of the 1985-86 year. However, to prevent a revenue loss through the retention by private companies of income of 1985-86 and earlier income years that would have been required to have been distributed to shareholders and taxed in their hands, under the previous "classical" system, the abolition of the undistributed profits tax will be subject to certain phasing-out arrangements.

2. Division 7 of Part III of the Income Tax Assessment Act 1936 was amended by the Taxation Laws Amendment Act (No. 2) 1987 to provide the necessary transitional rules for the phasing-out of the liability of private companies to the undistributed profits tax.

3. Under the transitional rules a private company will become liable for undistributed profits tax in respect of income of the 1986-87 and later income years only if it fails to distribute, as unfranked dividends, during the relevant prescribed period, an amount equal to the amount of phasing-out dividends included in its distributable income.

4. Unfranked dividends are dividends paid before 1 July 1987, and dividends paid on or after that date to the extent they are not franked with imputation credits.

5. The amount of phasing-out dividends included in a private company's distributable income is the aggregate of:

- (a) private company dividends to the extent to which they represent allocations of phasing-out amounts of the paying company as specified in notices issued by that company to the shareholder pursuant to subsection 105(3); and

- (b) private company dividends to which subsection 105(4) or (5) applies,

to the extent that the total of those amounts does not exceed the company's distributable income.

6. The purpose of this Ruling is to outline the administrative arrangements that are to apply in relation to the obligations of private companies to notify their shareholders of the extent to which dividends paid to them after 1 July 1985 represent amounts that, if derived by a private company during its 1986-87 or later income year, will be phasing-out dividends. Arrangements relating to the obligations of private companies to provide the Australian Taxation Office with the information contained in the notices to shareholders are also dealt with in this Ruling.

FACTS

7. Subsections 105(3), (4) and (5) specify the circumstances in which a private company is obliged to notify its shareholders that dividends it has paid after 1 July 1985:

- (a) are to be, or have been, taken into account in ascertaining whether the company has made a sufficient distribution for the purposes of Division 7; and
- (b) are potential phasing-out dividends.

Subsection 105(3)

8. Subsection 105(3) requires a private company to allocate its phasing-out amount for the 1985-86 or a later year of income (as determined by subsection 105(1) or (2)) among shareholders to whom it pays dividends that are taken into account in ascertaining whether the company has made a sufficient distribution in relation to the year of income. A company's phasing-out amount for the 1985-86 income year will be the difference between the company's distributable income and its retention allowance if it has made a sufficient distribution in relation to that income year. If it hasn't made a sufficient distribution, the company's phasing-out amount for that year will be the amount of unfranked dividends actually paid during the prescribed period relating to that year. A company's phasing-out amount for the 1986-87 and later years will be the phasing-out dividends included in its distributable income for the year concerned, or the amount of unfranked dividends paid during the prescribed period in relation to the year, whichever is the lesser.

9. The company is required to inform each shareholder, by notice in writing, of the phasing-out amount allocated to the shareholder in accordance with the subsection, and to give the Commissioner a copy of each such notice.

10. The subsection also prescribes the time limits within which the allocation and notification requirements are to be satisfied. Where the prescribed period within which the

dividends were paid ended before 5 June 1987, the allocation and appropriate notifications are required to be made before 3 July 1987. Where the prescribed period ended on or after 5 June 1987 the allocation and notifications are required to be made within 28 days of the end of the prescribed period. In either case, the Commissioner is authorised to allow further time for companies to comply with the requirements.

Subsection 105(4)

11. A 'retrospective dividend' is a dividend paid by a private company after the end of a prescribed period which is deemed to have been paid during that period by reason of the granting by the Commissioner, pursuant to section 105AA, of an additional period within which the dividend may be taken into account for the purpose of enabling the company to satisfy its sufficient distribution requirements in relation to the year of income to which the prescribed period relates.

12. Subsection 105(4) requires a private company to give a notice in writing to each shareholder to whom a 'retrospective dividend' is, or has been, paid after 1 July 1985 notifying the shareholder that the subsection applies to the dividend. The company is also required to provide the Commissioner with a copy of each such notice.

13. The subsection also prescribes time limits within which the company must issue the notices to shareholders and the Commissioner. Where the retrospective dividends were paid before 5 June 1987, the company is required to issue the notices before 3 July 1987. Where the retrospective dividends are paid on or after 5 June 1987, the company is required to issue the notices within 28 days of the date of payment. In either case, the Commissioner is authorised to allow companies further time to comply with requirements.

Subsection 105(5)

14. Subsection 105(5) requires a private company to give a notice in writing to each shareholder to whom a dividend is paid after 1 July 1985, where that dividend was:

- (a) taken into account in ascertaining whether the company had made a sufficient distribution in relation to the 1984-85 or an earlier income year; and
- (b) actually (rather than deemed to have been) paid during the prescribed period relating to the relevant income year.

The notice must contain advice notifying the shareholder that the subsection applies to the dividend, and must be given to the shareholder before 3 July 1987 or such later date allowed by the Commissioner.

15. Where a private company fails to comply with the requirements of subsections 105(3), (4) and (5), subsection

105(7) will operate to apply Division 7 in relation to the year of income concerned as if the company had not paid any dividends during the relevant prescribed period.

RULING

16. It was announced on 19 June 1987 that further time would be allowed to enable private companies to comply with the phasing-out amount allocation and notification requirements under subsections 105(3), (4) and (5). The further time to be allowed is as follows -

- (a) in respect of notices required under subparagraph 105(3)(a)(ii) in the case of all prescribed periods ended or ending before 3 August 1987 - until 31 August 1987;
- (b) in respect of notices required under paragraph 105(4)(a) in the case of all retrospective dividends paid before 3 August 1987 - until 31 August 1987; and
- (c) in respect of notices required under subsection 105(5) - until 31 August 1987.

17. A company which is unable to comply with the requirements of subsection 105(3), (4) or (5) within the extended time allowed as above and which requires a further extension should contact the Taxation Office where it normally lodges its returns. Such requests will be considered by the appropriate Deputy Commissioner on the basis of the facts of each particular case.

18. No particular format for the notices to be given to shareholders is prescribed. However, to enable shareholders to comply with their own requirements under Division 7 each notice should specify -

- (a) where subsection 105(3) applies, the date of payment of the dividend or dividends concerned (or, alternatively, the period during which the dividends concerned were paid) and the phasing-out amount allocated to the shareholder in respect of the dividends; and
- (b) where subsection 105(4) or (5) applies, the amount and the date of payment of the dividend or dividends to which the subsection relates.

Information to be given to the Commissioner

19. Further time will also be allowed to enable private companies to comply with the requirement, under subparagraph 105(3)(a)(iii), to provide the Taxation Office with a copy of notices issued to shareholders under subsection 105(3). Unless specifically required by the Commissioner to do otherwise, private companies will be allowed to provide the appropriate copies to the Taxation Office as follows -

- (a) in the case of allocations of phasing-out amounts relating to the 1985-86 year of income:

- (i) where the company income tax return for the 1986-87 year of income was lodged before 31 August 1987 - by 31 August 1987; or
- (ii) where the company income tax return for the 1986-87 year of income has not been lodged by 31 August 1987 - by the date of lodgment of that return; and
- (b) in the case of allocations of phasing-out amounts relating to the 1986-87 and later income years - by the date of lodgment of the company income tax return for the year of income following the income year to which the phasing-out amount relates.

20. For the purpose of satisfying the information requirements under subparagraph 105(3)(a)(iii), a schedule listing the name of each shareholder to whom a phasing-out amount is allocated and the respective amount allocated to each shareholder will be regarded as sufficient for that purpose.

21. Further time will also be allowed as follows to enable private companies to comply with the requirement, under subparagraph 105(4)(a)(ii), to provide the Commissioner with a copy of notices issued to shareholders under subsection 105(4) -

- (a) where the further period allowed under section 105AA to pay retrospective dividends ends on or before 1 August 1987 - until 31 August 1987; and
- (b) where the further period allowed under section 105AA ends after 1 August 1987 - until the thirtieth day after the end of that further period.

22. For the purpose of satisfying the information requirements under subparagraph 105(4)(a)(ii), a schedule listing for each retrospective dividend paid:

- (a) the date on which the dividend was paid;
- (b) the name of the shareholder to whom the dividend was paid; and
- (c) the amount paid to each shareholder,

will be regarded as sufficient for that purpose.

COMMISSIONER OF TAXATION
6 August 1987