TD 2012/12 - Income tax: Division 7A: do the rules in Subdivision D of Division 7A of Part III of the Income Tax Assessment Act 1936 which exclude certain payments or loans from being treated as dividends under Subdivision B of Division 7A of that Act necessarily affect the circumstances in which a deemed payment or notional loan arises under Subdivision E of Division 7A of that Act?

This cover sheet is provided for information only. It does not form part of *TD 2012/12 - Income tax: Division 7A: do the rules in Subdivision D of Division 7A of Part III of the Income Tax Assessment Act 1936 which exclude certain payments or loans from being treated as dividends under Subdivision B of Division 7A of that Act necessarily affect the circumstances in which a deemed payment or notional loan arises under Subdivision E of Division 7A of that Act?*

There is a Compendium for this document: **TD 2012/12EC** .

Generated on: 26 November 2026, 07:41:38 AM

Taxation Determination

Income tax: Division 7A: do the rules in Subdivision D of Division 7A of Part III of the *Income Tax Assessment Act 1936* which exclude certain payments or loans from being treated as dividends under Subdivision B of Division 7A of that Act necessarily affect the circumstances in which a deemed payment or notional loan arises under Subdivision E of Division 7A of that Act?

This publication provides you with the following level of protection:

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

A public ruling is an expression of the Commissioner's opinion about the way in which a relevant provision applies, or would apply, to entities generally or to a class of entities in relation to a particular scheme or a class of schemes.

If you rely on this ruling, the Commissioner must apply the law to you in the way set out in the ruling (unless the Commissioner is satisfied that the ruling is incorrect and disadvantages you, in which case the law may be applied to you in a way that is more favourable for you – provided the Commissioner is not prevented from doing so by a time limit imposed by the law). You will be protected from having to pay any underpaid tax, penalty or interest in respect of the matters covered by this ruling if it turns out that it does not correctly state how the relevant provision applies to you.

Ruling

1. No. Whether or not the rules in Subdivision D of Division 7A of Part III of the *Income Tax Assessment Act 1936* (ITAA 1936)[1] have any impact on the application of Subdivision E of that Division will depend upon the facts and circumstances of each case.

[1] All legislative references are to the ITAA 1936 unless otherwise stated.

Example 1

2. *A private company with current year profits and a large retained profits reserve (and a large distributable surplus) lends money to a related company that has no current year earnings and several years of carried forward losses (consequently it has no distributable surplus for the purposes of section 109Y).*

3. *The loss company subsequently makes a loan to a shareholder of the profitable company.*

4. *The shareholder does not make any repayment on the loan during the year of income.*

5. *There is no commercially justifiable reason to explain why the inter-company loan was made.*

6. *It can be concluded that the profitable company made the loan to the loss company solely or mainly as part of an arrangement to make a loan to the shareholder. Accordingly under section 109W the Commissioner determines an amount of a notional loan as if the private company had made a loan to the shareholder at the time the actual loan was made to the shareholder.*

7. *Section 109K does not prevent the private company from being taken to have paid a dividend in respect of the notional loan between the private company and the shareholder under section 109D because of the loan between the companies.*[2]

Example 2

8. *Private Company Pty Ltd makes a payment to Interposed Company Pty Ltd. Under an arrangement with Private Company Pty Ltd, Interposed Company Pty Ltd on lends that amount to one of Private Company Pty Ltd's shareholders – Aaron.*

9. *A loan agreement is in place between Interposed Company Pty Ltd and Aaron that meets the criteria in section 109N.*

10. *Subsections 109X(3) and (4) will treat the loan agreement between Interposed Company Pty Ltd and Aaron as the relevant agreement for the purpose of section 109N and a deemed dividend will not arise so long as minimum yearly repayments are made in accordance with section 109E in subsequent income years.*

Date of effect

11. This Determination applies to years of income commencing both before and after its date of issue. However, this Determination will not apply to taxpayers to the extent that it conflicts with the terms of a settlement of a dispute agreed to before the date of issue of this Determination (see paragraphs 75 and 76 of Taxation Ruling TR 2006/10).

Commissioner of Taxation
6 June 2012

[2] See subsection 109X(1).

Appendix 1 – Explanation

This Appendix is provided as information to help you understand how the Commissioner's view has been reached. It does not form part of the binding public ruling.

Explanation

Subdivision B – private company payments, loans and debt forgiveness are treated as dividends

12. Under Subdivision B, private company payments or loans made directly to an entity that is a shareholder (or an associate of a shareholder) are taken to be a dividend paid to the shareholder (or associate). Debts owed by the entity to a private company that are forgiven are also taken to be the payment of a dividend.

13. In this regard it may be said that Division 7A is an anti-avoidance or integrity measure aimed at ensuring that the profits of a private company are not effectively received in a non-dividend form.

14. There are, of course, occasions when it would be inappropriate to apply the broad rules in Subdivision B. Subdivision C sets out the rules that provide that a dividend does not arise under Subdivision B where certain debts are forgiven (for example, between companies). Subdivision D sets out rules about payments and loans that are also not treated as dividends under Subdivision B.

15. For example, payments of genuine debts to an entity, payments and loans to other companies and otherwise assessable payments or loans are excluded from the general rules in Subdivision B under sections 109J, 109K and 109L respectively. Loans made in the ordinary course of a private company's business on an arm's length basis are also not taken to be dividends (section 109M).

Subdivision E – payments and loans through interposed entities

16. A way of avoiding the operation of the primary rules in Subdivision B may be to cause an entity interposed between the private company and its shareholder (or their associate) to itself make a payment or loan to the shareholder (or their associate).

17. Subdivision E anticipates this kind of arrangement and sets out rules to treat payments and loans through interposed entities as giving rise to direct payments and loans under Subdivision B from a private company to a shareholder (or their associate) which are then taken to be dividends.

18. The kind of situation under consideration by section 109T of Subdivision E is where a private company makes a payment or loan to an interposed entity and a reasonable person would conclude that this was done solely or mainly as part of an arrangement involving a payment or loan (by the interposed entity or another interposed entity) to the shareholder or associate (described as the target entity). The fact that an arrangement may not have been entered into for the purpose of circumventing Division 7A is not relevant to the application of this provision.

19. In some cases Division 7A may apply to the transactions between the private company and the interposed entity and/or the transaction between the interposed entity and the target entity because the interposed entity is a shareholder (or an associate of a shareholder) or the interposed entity is a private company respectively.

20. To avoid double taxation, if an actual payment or loan made by the private company to an interposed entity results in the private company being taken to have paid a dividend to that interposed entity, then the private company will not be taken to have also made a payment or loan to the target entity.[3]

21. Once the mechanics of section 109T are satisfied, the amount that is taken to be the deemed payment or notional loan directly from the private company is determined by the Commissioner under section 109V or 109W respectively. Taxation Determination TD 2011/16 sets out some of the factors the Commissioner will take into account in determining, under these sections, the amount of any deemed payment or notional loan arising under section 109T.

22. Some of those factors mirror considerations set out in Subdivision D. For example, paragraph 2 of that Determination provides that the relevant factors the Commissioner will take into account include the extent to which any loan made from the private company to an interposed entity as part of the arrangement meets the criteria set out in section 109N (dealing with complying loan agreements) and the extent to which any actual loans made as part of the arrangement would be covered by section 109M (dealing with certain loans in the ordinary course of the private company's business). The extent to which a payment made under the arrangement being considered under section 109T is in fact consideration for anything may also be a relevant factor to take into account, which is not dissimilar to the focus of section 109J.

23. However, the consideration of what is the *amount* of any deemed payment or notional loan is separate to any consideration of the application of Subdivision D to any such deemed payment or notional loan that is taken to exist.

Subdivision D – payments and loans that are not treated as dividends

24. The rules in Subdivision D operate (or not) in respect of the deemed circumstances taken to exist by Subdivision E. For example, if the private company is taken to have made a loan to the target entity then section 109D has application to that notional loan. In determining whether the company is taken to pay a dividend the Subdivision D provisions relating to loans need to be considered.

25. Section 109X contains some rules about the interaction of Subdivisions D and E. For example, subsection 109X(1) provides that despite sections 109K and 109L, the fact that the interposed entity is a company or the fact that some, or all, of an amount paid or loaned to the interposed entity is included in the interposed entity's assessable income, will not prevent the private company having been taken to have made a payment or loan to the target entity.[4] Nonetheless, where the target entity is itself a company, section 109K will apply to exclude the deemed payment or loan to that company from the general rules in Subdivision B.[5]

26. Subsection 109X(3)[6] provides that the loan agreement under which the actual loan was made is treated for the purposes of section 109N as the agreement under which the notional loan was made.[7]

---

[3] Subsection 109T(3).
[4] Subsection 109X(1).
[5] See, for example, Taxation Determination TD 2001/2.
[6] which applies to assessments for the income year in which 1 July 2006 occurred and later income years
[7] Subsections 109X(2), (3) and (4) were substituted for subsection 109X(2) by *Tax Laws Amendment (2007 Measures No 3) Act 2007*. Subsection 109X(2) formerly read:

27. It is difficult to see that there is any further interplay between Subdivision D and the amount of a deemed payment or notional loan that has arisen under Subdivision E. For example, section 109J provides that a private company is not taken to pay a dividend under section 109C if the payment is made to discharge a pecuniary obligation and is not more than an arm's length amount. Because in Subdivision E the relevant payment is a deemed payment from the private company to the target entity it cannot in fact be a payment to discharge a pecuniary obligation**.**

28. Similarly, section 109M excludes from section 109D any loans made on ordinary commercial terms by a private company in the ordinary course of its business. Again, it is difficult to imagine how section 109M could apply to a notional loan between the private company and the target entity.

29. The point to be made is that the deemed circumstances from the operation of the interposed entity rules in Subdivision E can give rise to deemed dividends under Subdivision B notwithstanding the exclusion rules in Subdivision D. The interaction of all the various provisions contained in Division 7A need to be considered in the context of the particular circumstances under consideration.

Sections 109M and 109N do not apply to a notional loan under section 109W (so it must generally be taken into account for the purposes of working out whether the private company is taken under section 109D to have paid a dividend).

References

Previous draft:

TD 2011/D7

Related Rulings/Determinations:

TR 2006/10; TD 2001/2; TD 2011/16

Subject references:

- deemed dividends
- dividend income
- shareholder debt forgiveness
- shareholder loans
- shareholder payments

Legislative references:

- ITAA 1936
- ITAA 1936 Pt III Div 7A
- ITAA 1936 Pt III Div 7A Subdiv B
- ITAA 1936 109C
- ITAA 1936 109D
- ITAA 1936 109E
- ITAA 1936 Pt III Div 7A Subdiv C
- ITAA 1936 Pt III Div 7A Subdiv D
- ITAA 1936 109J
- ITAA 1936 109K
- ITAA 1936 109L
- ITAA 1936 109M
- ITAA 1936 109N
- ITAA 1936 Pt III Div 7A Subdiv E
- ITAA 1936 109T
- ITAA 1936 109T(3)
- ITAA 1936 109V
- ITAA 1936 109W
- ITAA 1936 109X
- ITAA 1936 109X(1)
- ITAA 1936 109X(2)
- ITAA 1936 109X(3)
- ITAA 1936 109X(4)
- ITAA 1936 109Y
- TAA 1953
- Tax Laws Amendment (2007 Measures No.3) Act 2007

ATO references
NO: 1-35RYRXS
ISSN: 1038-8982
ATOlaw topic: Income Tax ~~ Entity specific matters ~~ companies
Income Tax ~~ Tax integrity measures ~~ private company distributions