

TD 2022/13 - Income tax: does Subdivision 855-A (or subsection 768-915(1)) of the Income Tax Assessment Act 1997 disregard a capital gain that a foreign-resident (or temporary-resident) beneficiary of a resident non-fixed trust has because of subsection 115-215(3)?

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Status: **legally binding**

Taxation Determination

Income tax: does Subdivision 855-A (or subsection 768-915(1)) of the *Income Tax Assessment Act 1997* disregard a capital gain that a foreign-resident (or temporary-resident) beneficiary of a resident non-fixed trust has because of subsection 115-215(3)?

📌 Relying on this Determination

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

If this Determination applies to you, and you correctly rely on it, we will apply the law to you in the way set out in this Determination. That is, you will not pay any more tax or penalties or interest in respect of the matters covered by this Determination.

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Ruling

1. No. Section 855-40 of the *Income Tax Assessment Act 1997* (ITAA 1997) only disregards a capital gain that a foreign-resident beneficiary has because of subsection 115-215(3) if the trust is a fixed trust.¹ Section 855-10 (or subsection 768-915(1)) does not disregard a capital gain that a foreign-resident (or temporary-resident) beneficiary of a resident trust has because of subsection 115-215(3).

¹ Subsection 995-1(1) defines a trust to be a 'fixed trust' if 'entities have fixed entitlements to all of the income and capital of the trust'. An entity is defined in subsection 995-1(1) as having a 'fixed entitlement' to a share of the income or capital of a trust if the entity has a fixed entitlement to that share within the meaning of Division 272 in Schedule 2F to the *Income Tax Assessment Act 1936* (ITAA 1936).

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2. All legislative references in this Determination are to the ITAA 1997, unless otherwise indicated.
3. This Determination does not deal with the application of Australia's double-tax agreements.

Example

4. *During the 2015–16 income year, the trustee of a resident discretionary trust derived income from a business.*
5. *The trustee also made non-discount capital gains from the sale of 5,000 listed shares that it had owned for less than 12 months. The shares were not 'taxable Australian property' (TAP).²*
6. *The trustee resolved to make a foreign-resident beneficiary presently entitled to all of the trust income (in this case, the business income).*
7. *On these facts, as there was no beneficiary specifically entitled to any of the trust gains, all of the gains will be attributable to the foreign-resident beneficiary.*
8. *Section 115-220 operates so that the trustee is assessed under section 98 of the ITAA 1936 on the beneficiary's attributable capital gain.*
9. *The foreign-resident beneficiary is also taken to have made capital gains under subsection 115-215(3). The beneficiary will receive a refundable tax offset under subsection 98A(2) of the ITAA 1936 for tax paid by the trustee.*
10. *As the trust is not a fixed trust, section 855-40 does not apply to disregard the foreign-resident beneficiary's capital gain attributable to the non-TAP trust assets, nor does section 855-10 apply to disregard the capital gain which the foreign-resident beneficiary is taken, by Subdivision 115-C, to have.*

Date of effect

11. This Determination applies 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 75 to 76 of Taxation Ruling TR 2006/10 *Public Rulings*).

Commissioner of Taxation
31 August 2022

² See section 855-15 for when a CGT asset is TAP.

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Appendix – Explanation

❶ ***This Explanation 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.***

Extra capital gains: section 115-215

12. If a trust's net income³ includes a net capital gain, subsection 115-215(3) may treat a beneficiary as having extra capital gains (that is, in addition to those capital gains that the beneficiary has made directly) which are included in the calculation of their net capital gain under the method statement in subsection 102-5(1).

13. Subsection 115-215(4A) makes it clear that the beneficiary is taken to have these capital gains even though no CGT event has happened directly to the beneficiary.⁴

Foreign-resident beneficiary exemption where there is a fixed trust: section 855-40

14. Section 855-40 disregards a capital gain that a foreign-resident beneficiary of a fixed trust is taken to have as a result of a CGT event happening to a CGT asset of that trust if, at the time of the event, the CGT asset was not TAP of the trust.⁵ The purpose of the provision is to provide comparable treatment to that which would have been available had the beneficiary directly owned the trust assets. It is apparent from the enactment that comparable treatment was not thought to be warranted in the case of a non-fixed trust.⁶

15. There is a clear policy justification for limiting relief to capital gains where beneficiaries have interests in fixed trusts. Prior to the changes made by the *New International Tax Arrangements (Managed Funds and Other Measures) Act 2005*, foreign-resident beneficiaries of resident trust estates received no relief in relation to trust capital gains attributed to them⁷, even though some gains would not have been assessed to the foreign-resident beneficiary if the asset were held directly. This was so, whether the resident trust estate was fixed or not.⁸

16. The rule now reflected in section 855-40 (and originally in section 768-605 of former Subdivision 768-H) was one of a number of changes aimed at removing tax impediments that discouraged foreign residents from investing in Australian trusts. In particular, the reform aimed to improve the international competitiveness of Australia's managed funds industry. Paragraph 1.3 of the Explanatory Memorandum to the *New International Tax Arrangements (Managed Funds and Other Measures) Bill 2004 (EM)* explained that the section was introduced to align the tax treatment of foreign residents

³ See subsection 95(1) of the ITAA 1936 for the meaning of 'net income'.

⁴ See also *Peter Greensill Family Co Pty Ltd (Trustee) v Commissioner of Taxation* [2021] FCAFC 99 (*Greensill*) at [35], per Davies, Moshinsky and Colvin JJ.

⁵ Section 855-40 also applies to disregard capital gains ultimately taken to be made by a foreign beneficiary through a chain of fixed trusts where the CGT event happens to a non-TAP CGT asset of the first-tier fixed trust.

⁶ See also *Greensill* at [55].

⁷ Unless the beneficiary was absolutely entitled to the CGT asset as against the trustee – see section 106-50.

⁸ Under the predecessor provisions in the ITAA 1936, the interaction between former sections 160L and 160T left open no argument that non-resident beneficiaries could obtain exemption in relation to capital gains made by trustees of resident trust estates. There is no evidence that any change to this outcome was intended to have been made by the Tax Law Improvement Project rewrite in 1998 or by the subsequent enactment in 1999 of Subdivision 115-C, which treated beneficiaries as having capital gains for the purposes of Division 102. Prior to 1999, capital gains treatment was afforded to beneficiaries by administrative practice; see paragraphs 12 to 16 of Taxation Ruling IT 2328 *Income tax: capital gains provision: interpretation and operation* (now withdrawn).

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investing in fixed trusts more closely with the tax treatment of foreign residents investing directly in assets in Australia. The EM also provided⁹:

1.9. These amendments apply to foreign residents that have interests in managed funds (or other fixed trusts) whose assets are without the necessary connection with Australia.

...

1.12 These amendments are not confined to foreign residents with interests in widely held unit trusts. The amendments will apply to interests in closely held trusts and trusts that are not unit trusts. This is to ensure the benefits of the measures apply as widely as possible, irrespective of the trust arrangements through which the foreign resident invests. However, the trust in which the foreign resident has invested and all relevant trusts in the chain must meet the definition of 'fixed trust' in the *Income Tax Assessment Act 1997* (ITAA 1997). ... This is important to the integrity of the amendments.

General foreign-resident exemption: section 855-10

17. Subsection 855-10(1) provides that a foreign resident can disregard a capital gain or capital loss from a CGT event if the event happens in relation to a CGT asset that is not TAP.

18. It has been suggested that this general exemption provision disregards a capital gain or capital loss which a foreign-resident beneficiary of a trust is taken to have as a result of a CGT event happening to non-TAP assets of the trust.

19. However, a capital gain that a foreign-resident beneficiary has because of the operation of subsection 115-215(3) is not a capital gain from a CGT event.¹⁰ According to its terms, subsection 855-10(1) can only apply to disregard a capital gain from a CGT event, which is defined as a CGT event described in Division 104.¹¹ The capital gain treated as the beneficiary's capital gain by subsection 115-215(3) is not a capital gain from a CGT event described in Division 104, but a capital gain that the beneficiary is deemed to have by operation of subsection 115-215(3).¹²

20. This construction is supported by the statutory context. The presence of a specific rule in section 855-40 enabling beneficiaries of fixed trusts to disregard certain trust capital gains is a strong indicator that beneficiaries of non-fixed trusts are not catered for by section 855-10.¹³

21. If subsection 855-10(1) could disregard trust capital gains attributed to foreign-resident beneficiaries, it would on its terms do so without regard to whether the trust was a fixed trust or a non-fixed trust, rendering that aspect of section 855-40 redundant.¹⁴ The statutory context strongly suggests that the intention is for foreign-resident beneficiaries of fixed trusts to have capital gains or losses disregarded in appropriate cases, but not foreign-resident beneficiaries of non-fixed trusts.¹⁵ Such an intention is consistent with the policy considerations set out in paragraphs 14 and 15 of this Determination.

22. Section 855-40 only disregards capital gains arising through a chain of fixed trusts in circumstances where each trust in the chain is a fixed trust. The purpose of these

⁹ See also *Greensill* at [63].

¹⁰ *Greensill* at [78].

¹¹ 'CGT event' is defined in subsection 995-1(1) to mean 'any of the CGT events described in Division 104.'

¹² See *Greensill* at [50].

¹³ See also *Greensill* at [55].

¹⁴ See also *Greensill* at [55].

¹⁵ See *Greensill* at [70].

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detailed rules would be frustrated if they could be bypassed through the application of section 855-10.

General temporary-resident exemption: section 768-915

23. Section 768-915 operates to disregard a capital gain or capital loss made by a temporary resident if, had the temporary resident been a non-resident, the capital gain or capital loss would have been disregarded under Division 855. However there is no counterpart in the provision to section 855-40. Therefore, a gain which a temporary resident is taken to have under Subdivision 115-C cannot be disregarded whether the trust is a fixed trust or non-fixed trust.

Status: **not legally binding**

References

Previous draft:

TD 2019/D6

Related Rulings/Determinations:

IT 2328 (Withdrawn); TD 2022/12; TR 2006/10

Legislative references:

- ITAA 1936 95(1)
- ITAA 1936 98
- ITAA 1936 98A(2)
- ITAA 1936 former 160L
- ITAA 1936 former 160T
- ITAA 1936 Div 272 Sch 2F
- ITAA 1997 Div 102
- ITAA 1997 102-5(1)
- ITAA 1997 Div 104
- ITAA 1997 106-50
- ITAA 1997 Subdiv 115-C
- ITAA 1997 115-215
- ITAA 1997 115-215(3)
- ITAA 1997 115-215(4A)
- ITAA 1997 115-220
- ITAA 1997 former Subdiv 768-H
- ITAA 1997 768-605 of former Subdiv 768-H

- ITAA 1997 768-915
- ITAA 1997 768-915(1)
- ITAA 1997 Div 855
- ITAA 1997 Subdiv 855-A
- ITAA 1997 855-10
- ITAA 1997 855-10(1)
- ITAA 1997 855-15
- ITAA 1997 855-40
- ITAA 1997 855-40(1)
- ITAA 1997 995-1(1)

Cases relied on:

- Peter Greensill Family Co Pty Ltd (Trustee) v Commissioner of Taxation [2021] FCAFC 99; 285 FCR 410

Other references:

- Explanatory Memorandum to the New International Tax Arrangements (Managed Funds and Other Measures) Bill 2004

ATO references

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