

LCR 2020/3 - The superannuation fund for foreign residents withholding tax exemption and sovereign immunity

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The superannuation fund for foreign residents withholding tax exemption and sovereign immunity

❶ Relying on this Ruling

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

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

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What this Ruling is about

1. This Ruling addresses Schedules 3 and 4 to the *Treasury Laws Amendment (Making Sure Foreign Investors Pay Their Fair Share of Tax in Australia and Other Measures) Act 2019* (the Act), which limit the withholding tax exemption for superannuation funds for foreign residents and codify and limit the scope of the sovereign immunity tax exemption.¹
2. All legislative references in this Ruling are to the *Income Tax Assessment Act 1997* unless otherwise indicated.

Date of effect

3. This Ruling is effective from 1 July 2019. The amendments in the Act apply in relation to income derived in the 2019–20 income year and later income years.²

Outline of the law

Superannuation funds for foreign residents

4. Previously, superannuation funds for foreign residents were not liable to withholding tax on income consisting of interest, or income consisting of dividends or non-share dividends paid by an Australian company, where the requirements of paragraph 128B(3)(jb) of the *Income Tax Assessment Act 1936* (ITAA 1936) were satisfied.
5. Schedule 3 to the Act introduced extra requirements that must now be satisfied for paragraph 128B(3)(jb) of the ITAA 1936 to apply. Specifically:
 - the superannuation fund for foreign residents must satisfy the portfolio interest test in subsection 128B(3CC) of the ITAA 1936 in relation to the entity that paid the interest, dividend or non-share dividend³
 - the superannuation fund for foreign residents must not, at the time the income was derived, have influence of a kind described in

¹ See the General outline and financial impact section of the Revised Explanatory Memorandum to the Treasury Laws Amendment (Making Sure Foreign Investors Pay Their Fair Share of Tax in Australia and Other Measures) Bill 2018 and related Bills.

² Noting transitional provisions may apply.

³ The portfolio interest test must be satisfied at the time the income is derived and for at least 12 months in the 24 months preceding that time: paragraph 128B(3CA)(a) of the ITAA 1936. If subsection 128A(3) of the ITAA 1936 applies in relation to a resident trust estate, the portfolio interest test must be satisfied in relation to that trust: subsection 128B(3CB) of the ITAA 1936.

- subsubsection 128B(3CD) of the ITAA 1936 in relation to the payer of the interest, dividend or non-share dividend⁴, and
- the income cannot otherwise be non-assessable non-exempt income of the superannuation fund for foreign residents because of
 - Subdivision 880-C, or
 - Division 880 of the *Income Tax (Transitional Provisions) Act 1997*.⁵

Sovereign immunity

6. Schedule 4 to the Act introduced Division 880 which codifies and restricts the previous ATO administrative practice⁶ of providing sovereign immunity in certain circumstances.

7. Broadly, an amount of ordinary income or statutory income of a sovereign entity is non-assessable non-exempt income if:

- the sovereign entity is covered by section 880-125⁷
- the amount is a return on a membership interest, debt interest or non-share equity interest held by the sovereign entity in another entity (described as the 'test entity')⁸
- the test entity is an Australian resident company or a managed investment trust (MIT) at the relevant times⁹
- the sovereign entity group of which the sovereign entity is a member satisfies the portfolio interest test in subsection 880-105(4) in relation to the test entity at the relevant times¹⁰, and
- the sovereign entity group of which the sovereign entity is a member does not have influence of a kind described in subsection 880-105(6) in relation to the test entity at the income time.¹¹

8. There are additional provisions which deal with deductions¹², capital gains and capital losses¹³, and income from consular functions.¹⁴

Specific issues for guidance

The influence test

9. The influence tests introduced by Schedule 3 and Schedule 4 to the Act, and contained in subsection 128B(3CD) of the ITAA 1936 and subsection 880-105(6), are almost identical.¹⁵ There are two distinct sub-tests within the influence test.

⁴ Paragraph 128B(3CA)(b) of the ITAA 1936. If subsection 128A(3) of the ITAA 1936 applies in relation to a resident trust estate, the influence test must be satisfied in relation to that trust: subsection 128B(3CB) of the ITAA 1936.

⁵ Paragraph 128B(3CA)(c) of the ITAA 1936.

⁶ See ATO Interpretative Decision ATO ID 2002/45 *Withholding Tax Sovereign Immunity* (Withdrawn).

⁷ Paragraph 880-105(1)(a).

⁸ Paragraph 880-105(1)(b).

⁹ Paragraph 880-105(1)(c).

¹⁰ Paragraph 880-105(1)(d).

¹¹ Paragraph 880-105(1)(e).

¹² Section 880-110.

¹³ Sections 880-115 and 880-120.

¹⁴ Section 880-205.

¹⁵ Noting that subsection 128B(3CD) of the ITAA 1936 considers the influence of the superannuation fund for foreign residents itself, whereas subsection 880-105(6) considers the influence of the sovereign entity group (as modified by subsection 880-105(8)).

Identity of decision makers sub-test

10. The first sub-test¹⁶ assesses whether the relevant entity is able to determine the identity of at least one of the persons who, individually or together with others, make (or might reasonably be expected to make) the decisions that comprise the control and direction of the test entity's operations.

11. Whether the relevant entity is able to determine the identity of (to settle or decide upon, to choose or appoint) one of those persons is a question of fact. The phrase 'able to' focuses on the relevant entity's capacity or power. The sub-test is therefore not limited to situations where the entity has already determined, or intends to determine, the identity of one of the relevant decision makers. A right to determine will be sufficient for the requisite level of influence to exist.

12. The relevant entity will not be 'able' to determine, as a matter of fact, where it has irrevocably and unconditionally waived its rights by way of a legally enforceable agreement.

13. This sub-test also extends to situations where the relevant entity has the indirect capacity to determine the identity of one of the relevant decision makers. This may occur, for example, where the relevant entity controls another entity and that other entity holds the right to determine the decision-maker's identity.

Example 1 – indirect influence

14. *A superannuation fund for foreign residents (SFFR) holds a minority direct interest in Aus Co Limited. This minority direct interest does not provide SFFR with the capacity to determine the identity of any person who makes the decisions that comprise the control and direction of Aus Co Limited.*

15. *SFFR also wholly owns Sub Pty Ltd, an Australian resident subsidiary of SFFR. Sub Pty Ltd holds an interest in Aus Co Limited which comes with the right to appoint a director to the Board of Directors of Aus Co Limited. The Board of Directors makes decisions in relation to the control and direction of Aus Co Limited.*

16. *As SFFR controls Sub Pty Ltd, it is indirectly able to determine the identity of one of the directors who, together with others, makes the decisions that comprise the control and direction of Aus Co Limited's operations.*

17. *SFFR has influence of a kind described in subsection 128B(3CD) of the ITAA 1936.*

18. The requisite level of influence will also exist where the relevant entity 'in acting in concert with others' is directly or indirectly able to determine one of those persons.¹⁷ The phrase 'acting in concert' was considered by Finkelstein J in *Papua New Guinea Dockyard Limited v Adams* [2005] FCA 413 at [13]:

... Many of the important cases that discuss the meaning of "acting in concert" are helpfully collected by Barrett J in *Bateman v Newhaven Park Stud Ltd* (2004) 49 ACSR 597. These cases show that a person, A, will be acting in concert with another person, B, if A engages in conduct (act or omission) in consequence of an agreement or understanding between A and B and the conduct is in pursuance of an objective or purpose which is common to both. It is not as is sometimes suggested necessary to show that the common objective or purpose "has some pejorative element [such as] to circumvent the letter, or perhaps even the spirit, of some other statutory obligation or requirement" ...

19. Whether the relevant entity 'in acting in concert with others' is able to determine the identity of one of the relevant decision makers requires an examination of all of the relevant facts and circumstances. There must be some form of arrangement or

¹⁶ Paragraph 128B(3CD)(a) of the ITAA 1936 and paragraph 880-105(6)(a).

¹⁷ Subparagraph 128B(3CD)(a)(ii) of the ITAA 1936 and subsection 880-105(6).

understanding, whether explicit or otherwise, under which they are acting (or have agreed to act) in pursuing a common objective.

Example 2 – acting in concert

20. *A superannuation fund for foreign residents (SFFR) and a sovereign entity (SE) utilise a common investment manager (IM) to invest in an Australian MIT (Aus Trust).*

21. *While neither individual investment would give SFFR or SE a right to a seat on an Advisory Board to Aus Trust, the constituent documents of Aus Trust operate such that IM is able to appoint a member to the Advisory Board based on the aggregate investment of SFFR and SE. IM has entered into agreements with both SFFR and SE which govern how IM will appoint the Advisory Board member.*

22. *The Advisory Board is required to approve decisions in relation to the control and direction of Aus Trust's operations.*

23. *In this scenario, both SFFR and SE have the requisite level of influence for the purposes of the respective influence tests.*

24. The persons who, individually or together with others, make (or might reasonably be expected to make) the decisions that comprise the control or direction of the test entity's operation will depend on the specific facts and circumstances.

25. In the context of a company¹⁸, the key element in the control and direction of the company's operations is the making of high-level decisions that set the company's general policies and determine the direction of its operations and the type of transactions it will enter. This could include setting the investment or operational policy, appointing key management personnel, matters of finance or entering into of key business contracts.

26. Normally, where a company is run by its directors in accordance with its constitution and the relevant company law rules which give its directors the power to manage the company, the company's directors will control and direct its operations.¹⁹

27. However, the class of persons included within the group of relevant decision makers is not restricted to the directors (and shadow directors) of a company. Any person who has a role in the high-level decision-making processes or governance of the company may satisfy the relevant criteria. This could include, for example, a member of an advisory or investment committee where such committee is required to approve decisions in relation to the control and direction of the operation of the company.²⁰

Influence through decision makers sub-test

28. The second sub-test²¹ assesses whether at least one of the relevant decision makers is accustomed or obliged to act, or might reasonably be expected to act, in accordance with the directions, instructions or wishes of the relevant entity.²²

¹⁸ Noting the concepts would be similar for a trust as far as is relevant to the influence test.

¹⁹ This approach follows similar reasoning to that in Taxation Ruling TR 2018/5 *Income tax: central management and control test of residency*.

²⁰ See Example 3.4 in the EM.

²¹ Paragraph 128B(3CD)(b) of the ITAA 1936 and paragraph 880-105(6)(b).

²² A similar test was the subject of *Commissioner of Taxation v BHP Billiton Limited* [2019] FCAFC 4 (*BHP Billiton – Full Federal Court*) and the subsequent appeal to the High Court in *BHP Billiton Limited v Commissioner of Taxation* [2020] HCA 5 (*BHP Billiton – High Court*). The Courts considered the phrase 'accustomed or under an obligation (whether formal or informal), or might reasonably be expected, to act in accordance with the directions, instructions or wishes of' which is used in subsection 318(6) of the ITAA 1936 to explain the meaning of 'sufficiently influenced' for the purposes of identifying 'associates' of a company.

29. The three matters ('accustomed', 'obliged' or 'might reasonably be expected to') are not a composite phrase denoting a single test; they comprise different considerations each of which is sufficient to establish influence²³:

- Whether a person is 'accustomed' to act in accordance with the directions, instructions or wishes of the relevant entity requires an analysis of past facts. This necessitates an examination of any discernible pattern of the person following the directions, instructions or wishes given by the relevant entity.
- Whether a person is 'obliged' to act in accordance with the directions, instructions or wishes of the relevant entity depends upon a formal or informal obligation existing at the relevant time.
- Whether a person 'might reasonably be expected' to act in accordance with the directions, instructions or wishes of the relevant entity requires a prediction as to future events and a consideration as to the objective likelihood of those future events occurring. This requires a consideration of all of the facts and circumstances impacting upon the relationship between the two parties.

30. Determining whether a person acts 'in accordance with' directions, instructions or wishes requires consideration of the degree to which those directions, instructions or wishes contribute to the action, or any other link between them.²⁴ The link that is required is informed by statutory context.²⁵ In the context of these provisions, an action will be in accordance with directions, instructions or wishes if it is in harmonious correspondence, agreement or conformity with them.²⁶ The sub-test requires something more than mere coincidence, and it is not enough that the relevant decision maker is purely acting in their own interests in a way that happens to align with the wishes of another.²⁷ However, the sub-test does not require control²⁸, nor is it necessary to establish a causal link if there is some other basis to conclude that the person acts, or might reasonably be expected to act, in accordance with the relevant directions, instructions or wishes.²⁹ This is a factual inquiry and will depend on the circumstances in each case.

Example 3 – influence through an advisory committee

31. *A sovereign entity (SE) holds a 7% investment in Aus Co Pty Ltd, a closely-held Australian company. The Board of Directors makes decisions in relation to the control and direction of Aus Co Pty Ltd.*

32. *The Board of Directors is required to consult with an Advisory Committee on decisions in relation to the control and direction of Aus Co Pty Ltd. The Advisory Committee consists of a representative from each of the four largest shareholders and a representative on behalf of minority shareholders. Any recommendation of the Advisory Committee is non-binding on the Board of Directors, however, the Board of Directors has habitually complied with the recommendations (both positive and negative) of the Advisory Committee.*

33. *As one of the four largest shareholders, SE has appointed a member to the Advisory Committee.*

34. *In this scenario, the Board of Directors is accustomed or obliged to act, or might reasonably be expected to act, in accordance with the directions, instructions or wishes of*

²³ *BHP Billiton* – Full Federal Court at [85]; *BHP Billiton* – High Court at [35].

²⁴ *BHP Billiton* – High Court at [39].

²⁵ *BHP Billiton* – Full Federal Court at [87]; see also *BHP Billiton* – High Court at [40].

²⁶ *BHP Billiton* – Full Federal Court at [13].

²⁷ *BHP Billiton* – Full Federal Court at [87]; *BHP Billiton* – High Court at [7] and [37].

²⁸ *BHP Billiton* – Full Federal Court at [15]; *BHP Billiton* – High Court at [7] and [40–42].

²⁹ *BHP Billiton* – High Court at [39].

SE. These directions, instructions or wishes are expressed by SE through acting in concert with the other members of the Advisory Committee.

35. *This being the case, SE holds the requisite level of influence for the purposes of subsection 880-105(6).*

36. Rights to appoint an observer to a Board or Committee, the provision of a side letter, or the existence of additional rights/variations specific to the relevant entity are all factors which would potentially indicate that one of the relevant decision makers is accustomed or obliged to act, or might reasonably be expected to act, in accordance with the directions, instructions or wishes of the relevant entity.

Example 4 – influence through additional rights

37. *A sovereign entity (SE) holds a 7% investment in Aus Co Pty Ltd, a closely held Australian company. The Board of Directors makes decisions in relation to the control and direction of Aus Co Pty Ltd.*

38. *SE has negotiated with the Board of Directors for certain rights to be provided to SE which are not present for other shareholders. These rights include the right to be consulted in respect of decisions in relation to the control and direction of Aus Co Pty Ltd made by the Board of Directors and the right to receive additional information about the financial affairs of Aus Co Pty Ltd. A side letter has been issued to SE confirming this arrangement.*

39. *Any recommendation of SE is non-binding on the Board of Directors, however, historically the recommendations of SE (both positive and negative) have been followed by the Board of Directors.*

40. *In this scenario, the Board of Directors is accustomed or obliged to act, or might reasonably be expected to act, in accordance with the directions, instructions or wishes of SE. This being the case, SE holds the requisite level of influence for the purposes of subsection 880-105(6).*

Sovereign entity group

41. Section 880-20 provides the definition of ‘sovereign entity group’ for the purposes of Division 880. Broadly, sovereign entities of the same foreign country will be members of the same sovereign entity group³⁰ and sovereign entities of the same part of a foreign country will be members of the same sovereign entity group.³¹

Example 5 – identifying a sovereign entity group

42. *Country A has three levels of government – federal, state and provincial. State Investment Company is an investment company which is wholly owned by a state government department of Country A.*

43. *In determining the sovereign entity group of which State Investment Company is a member, subsection 880-20(1) has no application as this is directed at sovereign entities of the federal government of Country A.*

44. *Subsection 880-20(2) will apply such that any sovereign entity of that state is a member of the sovereign entity group alongside State Investment Company. Subsection 880-20(2) will only group sovereign entities of that particular state. Sovereign*

³⁰ Subsection 880-20(1).

³¹ Subsection 880-20(2).

entities of other states or provinces of Country A will not be grouped with State Investment Company.

45. Given the various structures and levels of government that exist in different countries, it is not possible to provide a uniform approach to determining the separate parts of a foreign country for the purposes of subsection 880-20(2). That being said, generally there are internationally recognised divisions within each country which will readily assist the enquiry.

Government-administered superannuation funds

46. Section 880-15 provides the definition of a sovereign entity. Relevantly, this definition includes certain entities in which a foreign body politic or foreign government agency holds a total participation interest of 100%.³²

47. Whether this is satisfied in relation to a government-administered superannuation fund will depend on the facts. However, in most cases, the participation interests in the fund will be held by the individual members rather than the body politic or government agency. In such cases, the government-administered superannuation fund will not satisfy the definition of a sovereign entity.

Example 6 – government-administered superannuation fund

48. *Foreign Government Company is the trustee of the Foreign Government Superannuation Fund, a superannuation fund for the employees of a particular government department. Foreign Government Company is a sovereign entity for the purposes of section 880-15.*

49. *The Foreign Government Superannuation Fund is funded by a combination of employee and employer contributions. The total participation interests³³ in the Foreign Government Superannuation Fund are held by the individual employee members.*

50. *In this scenario, the Foreign Government Superannuation Fund is not a sovereign entity. While Foreign Government Company is, in its own right, a sovereign entity, the Foreign Government Superannuation Fund does not meet the requirements of section 880-15 because it is not an entity in which the foreign government has a total participation interest of 100%.*

‘Return on’

51. For an amount of ordinary income or statutory income of a sovereign entity to satisfy paragraph 880-105(1)(b), it must be a ‘return on’ a membership interest, debt interest or non-share equity interest held by the sovereign entity in the test entity.

52. As detailed in paragraph 4.37 of the EM, a ‘return on’ for the purposes of paragraph 880-105(1)(b) will include (but is not limited to):

- dividends – including non-share dividends and dividends that pass through a MIT
- interest – including interest that passes through a MIT

³² Paragraph 880-15(c).

³³ In any given case the conclusion of whether total participation interests are held by individual employee members or the government-administered superannuation fund will depend on the application of section 960-180 in the context of the relevant fund. The application of section 960-180 is beyond the scope of this Ruling.

- fund payments made by a MIT – other than fund payments to the extent that they are attributable to non-concessional MIT income³⁴, or fund payments to the extent that they are attributable to amounts that would be non-concessional MIT income if certain provisions were disregarded³⁵, and
- revenue gains made on the disposal of an interest in the test entity, including revenue gains that pass through a MIT.

Public monies

53. In order to be a ‘covered sovereign entity’, a sovereign entity must satisfy the requirements of section 880-125. Paragraphs 880-125(a) and (b) require the sovereign entity to be funded solely by public monies and all returns on the sovereign entity’s investments to be public monies.

54. In the context of Division 880, the Commissioner considers that the phrase ‘public monies’³⁶ means monies of a foreign government (or part of a foreign government) held for a public purpose. These public monies would often be accounted for in the foreign government’s (or part of the foreign government’s) equivalent to Australia’s Consolidated Revenue Fund.³⁷ This would ordinarily include general tax revenue, proceeds from the issue of government bonds, and the proceeds of privatisations. In this context, public monies includes the relevant sovereign entity’s returns from investing public monies which are then held for reinvestment.

Example 7 – public monies requirement satisfied

55. *Foreign Government Co is a special-purpose investment company established and controlled by a Foreign Government for the purpose of investing in a broad portfolio of listed investments in Australia. Foreign Government Co is funded out of the Budget of Foreign Government (the equivalent to Australia’s Consolidated Revenue Fund). All returns on investments made by Foreign Government Co form part of the Budget and are available for appropriation by the Foreign Government.*

56. *Foreign Government Co will meet the requirements of paragraphs 880-125(a) and (b).*

Example 8 – public monies requirement satisfied

57. *Foreign Government Fund is an investment fund established by a Foreign Government specifically to meet the Foreign Government’s unfunded future pension liabilities. Foreign Government Fund is funded out of prior-year budget surpluses of the Foreign Government. All investment returns of Foreign Government Fund form part of the Budget of the Foreign Government (the equivalent to Australia’s Consolidated Revenue Fund).*

58. *Foreign Government Fund will meet the requirements of paragraphs 880-125(a) and (b).*

Government-administered superannuation funds – public monies

59. As outlined at paragraph 47 of this Ruling, a government-administered superannuation fund would not generally meet the definition of ‘sovereign entity’ in section 880-15. In any event, it is likely to be a ‘public financial entity’ in accordance with

³⁴ Paragraph 880-105(3)(a).

³⁵ Paragraph 880-105(3)(b).

³⁶ An undefined term.

³⁷ See *Roy Morgan Research Pty Ltd v Commissioner of Taxation* [2011] HCA 35.

subsection 880-130(2) and therefore not a covered sovereign entity (see paragraphs 77 to 79 of this Ruling).

60. Further, it is relevant to note that the phrase ‘public monies’ would not ordinarily extend to monies which fund government-administered superannuation funds or returns on investments of government-administered superannuation funds. These monies are commonly held and invested for a private purpose being, in substance, deferred remuneration of individuals in respect of their current or past employment and/or additional retirement savings for those individuals.

61. This situation traditionally arises where a foreign government or foreign government department administers a superannuation fund for its employees.³⁸ The superannuation fund is usually funded by a combination of employee and employer contributions (with the foreign government or foreign government department making contributions in its capacity as employer). Investment returns of the superannuation fund are unable to be diverted for any purpose other than meeting obligations under the current statute or trust deed. The assets and income of the superannuation fund sit separate to the foreign government’s equivalent to Australia’s Consolidated Revenue Fund.

62. In this scenario, it cannot be concluded that the superannuation fund is funded solely by public monies and all returns on its investments will be public monies.

Example 9 – public monies requirement not satisfied

63. *Foreign Government Company is the trustee of the Foreign Government Superannuation Fund, a superannuation fund for the employees of a particular government department.*

64. *The Foreign Government Superannuation Fund is funded by a combination of employee and employer contributions. The assets and income of the Foreign Government Superannuation Fund sit separate to the Budget of the Foreign Government (the equivalent to Australia’s Consolidated Revenue Fund).*

65. *While investments are legally held by a sovereign entity (Foreign Government Company in its capacity as trustee of the Foreign Government Superannuation Fund) the requirements of paragraphs 880-125(a) and (b) are not met. The Foreign Government Superannuation Fund is not funded solely by public monies and all returns on its investments are not public monies.*

Example 10 – public monies requirement not satisfied

66. *Foreign Government Company is the trustee of the Foreign Government Superannuation Fund, a superannuation fund established by statute for employees of a particular government department. Foreign Government Company is a sovereign entity for the purposes of section 880-15.*

67. *The Foreign Government Superannuation Fund is a defined-benefit superannuation fund. As a consequence of employment with the government department, employees become members of the Foreign Government Superannuation Fund and become entitled to a defined-benefit pension upon reaching retirement age. The defined-benefit pension is calculated based on a formula which includes years of service, final average salary and other factors.*

68. *Based on actuarial calculations, the Foreign Government transfers monies out of its Budget (the equivalent to Australia’s Consolidated Revenue Fund) to the Foreign Government Superannuation Fund as required. Once transferred out of the Budget, the monies are unable to be diverted for any purpose other than being invested to meet obligations owed to members under the relevant statute (save for a residual right for the*

³⁸ Noting that such an entity is also a public financial entity under paragraph 880-130(2)(c).

Foreign Government to be paid any actuarial excess which arises). Once transferred, the assets and income of the Foreign Government Superannuation Fund sit separate to the Budget of the Foreign Government.

69. *In this scenario, the requirements of paragraph 880-125(b) are not met. Returns on the investments held by Foreign Government Company in its capacity as trustee of the Foreign Government Superannuation Fund are not public monies. Rather, the returns on investments accrue to the benefit of the members of the Foreign Government Superannuation Fund.*

Third-party debt

70. Paragraph 880-125(a) will not be satisfied where a sovereign entity obtains third-party debt funding. In this scenario, it cannot be concluded that the sovereign entity is funded solely by public monies. The sovereign entity will, at least in part, be funded by the third-party debt.

Example 11 – third-party debt

71. *Foreign Government Co is a special-purpose investment company established and controlled by a Foreign Government for the purpose of investing in a broad portfolio of listed investments in Australia. Foreign Government Co is funded, in part, out of the Budget of Foreign Government (the equivalent to Australia's Consolidated Revenue Fund). Foreign Government Co is also funded, in part, by a loan from Global Bank, a third-party commercial bank.*

72. *Foreign Government Co will not meet the requirements of paragraph 880-125(a). Foreign Government Co is not solely funded by public monies as it is also funded by a commercial loan from Global Bank.*

Public non-financial entity

73. A sovereign entity cannot be a covered sovereign entity where it is a public non-financial entity.³⁹

74. In accordance with subsection 880-130(1), an entity is a public non-financial entity if its principal activity is:

- producing or trading non-financial goods, and/or
- providing services that are not financial services.

75. 'Principal' is not defined and, as such, takes its ordinary meaning having regard to the purpose and context in which it appears. The *Macquarie Dictionary* defines principal as '1. first or highest in rank, importance, value, etc.; chief; foremost ...'.⁴⁰ The principal activity of an entity, for the purposes of subsection 880-130(1), is therefore its chief or foremost activity.

76. Whether an entity is producing or trading non-financial goods and/or providing services that are not financial services is a question of fact. Common examples of public non-financial entities include:

- airline corporations
- postal authorities
- state water corporations

³⁹ Subparagraph 880-125(d)(i).

⁴⁰ Macmillan Publishers Australia, *The Macquarie Dictionary* online, www.macquariedictionary.com.au, viewed 8 December 2020.

- port authorities
- hospitals
- schools
- colleges
- state electricity corporations, and
- state mining corporations.

Public financial entity

77. A sovereign entity cannot be a covered sovereign entity where it is a public financial entity (other than a public financial entity that only carries on central banking activities).⁴¹

78. In accordance with subsection 880-130(2), an entity is a public financial entity if any of the following requirements are satisfied:

- it trades in financial assets and liabilities⁴², and/or
- it operates commercially in the financial markets⁴³, and/or
- its principal activities include providing any of the following financial services
 - financial intermediary services, including deposit taking and insurance services, and/or
 - financial auxiliary services, including brokerage, foreign exchange and investment management services, and/or
 - capital financial institution services, including financial services in relation to assets or liabilities that are not available on open financial markets.⁴⁴

79. Common examples of public financial entities⁴⁵ include:

- banks
- deposit taking corporations
- captive financial institutions
- pension/superannuation funds
- insurance corporations
- entities in the business of investment management
- entities in the business of share trading, and
- entities in the business of money lending.

⁴¹ Subparagraph 880-125(d)(ii).

⁴² Paragraph 880-130(2)(a).

⁴³ Paragraph 880-130(2)(b).

⁴⁴ Paragraph 880-130(2)(c).

⁴⁵ See International Monetary Fund, 2014, *Government Finance Statistics Manual 2014*, International Monetary Fund Publication Services, Washington; Australian Bureau of Statistics 2015, *Australian System of Government Finance Statistics: Concepts, Sources and Methods, 2015*, Australian Bureau of Statistics, Canberra.

Central banking activities

80. A public financial entity under subsection 880-130(2) is excluded from subparagraph 880-125(d)(ii) where it only carries on central banking activities.

81. Based on principles drawn from *Government Finance Statistics Manual 2014* and *Australian System of Government Finance Statistics: Concepts, Sources and Methods, 2015*⁴⁶, the following are considered 'central banking activities':

- monetary policy development
- issuing national currency
- acting as custodian of international reserves, and
- providing banking services to government.

82. The Reserve Bank of Australia is Australia's central bank. The activities of the Reserve Bank of Australia are consistent with those outlined in paragraph 81 of this Ruling and provide a useful reference point in considering whether a public financial entity is undertaking central banking activities.

83. Whether a public financial entity is 'only' carrying on central banking activities is a question of fact. It is important to note that a public financial entity may carry on both central banking activities and non-central banking activities (for example, commercial banking). Where this is the case, the public financial entity is not excluded from subparagraph 880-125(d)(ii).

Consular functions

84. Section 880-205 provides that an amount of ordinary or statutory income of an entity is not assessable income and is not exempt income if the income arises from the entity's consular functions.

85. Examples of consular functions which may result in ordinary or statutory income include:

- issuing passports and travel documents
- helping and assisting nationals
- acting as a notary and civil registrar and in capacities of a similar kind
- certain functions of an administrative nature, and
- transmitting judicial and extrajudicial documents.

Commissioner of Taxation
16 December 2020

⁴⁶ Paragraph 4.26 of the EM.

References

Previous draft:

Previously released in draft format as LCR 2019/D4

ATOlaw topic(s)	International issues ~~ Sovereign immunity Withholding tax ~~ Royalties / interest / unfranked dividends ~~ Foreign resident
Legislative references	ITAA 1936 128A(3) ITAA 1936 128B(3)(jb) ITAA 1936 128B(3CA)(a) ITAA 1936 128B(3CA)(b) ITAA 1936 128B(3CA)(c) ITAA 1936 128B(3CB) ITAA 1936 128B(3CC) ITAA 1936 128B(3CD) ITAA 1936 128B(3CD)(a) ITAA 1936 128B(3CD)(a)(ii) ITAA 1936 128B(3CD)(b) ITAA 1936 318(6) ITAA 1997 Div 880 ITAA 1997 Subdiv 880-C ITAA 1997 880-15 ITAA 1997 880-20 ITAA 1997 880-20(1) ITAA 1997 880-20(2) ITAA 1997 880-105(1)(a) ITAA 1997 880-105(1)(b) ITAA 1997 880-105(1)(c) ITAA 1997 880-105(1)(d) ITAA 1997 880-105(1)(e) ITAA 1997 880-105(3)(a) ITAA 1997 880-105(3)(b) ITAA 1997 880-105(4) ITAA 1997 880-105(6) ITAA 1997 880-105(6)(a) ITAA 1997 880-105(6)(b) ITAA 1997 880-105(8) ITAA 1997 880-110 ITAA 1997 880-115 ITAA 1997 880-120 ITAA 1997 880-125 ITAA 1997 880-125(a) ITAA 1997 880-125(b) ITAA 1997 880-125(d)(i) ITAA 1997 880-125(d)(ii) ITAA 1997 880-130(1) ITAA 1997 880-130(2) ITAA 1997 880-130(2)(a)

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Case references	BHP Billiton Limited v Commissioner of Taxation [2020] HCA 5; 2020 ATC 20-735; [2020] ALMD 1519; 376 ALR 43; 94 ALJR 326 Commissioner of Taxation v BHP Billiton Limited [2019] FCAFC 4; 263 FCR 334; 2019 ATC 20-680; 366 ALR 206; [2019] ALMD 3663 Papua New Guinea Dockyard Limited v Adams [2005] FCA 413; 215 ALR 742; [2005] ALMD 6098; [2005] ALMD 6112 Roy Morgan Research Pty Ltd v Commissioner of Taxation [2011] HCA 35; 244 CLR 97; 2011 ATC 20-282
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