



TD 2010/D2 - Income tax: will the exemption in section 102NA of the Income Tax Assessment Act 1936 continue to apply to a unit trust that has become the interposed trust of a stapled group pursuant to Subdivision 124-Q of the Income Tax Assessment Act 1997 if the trustee of the unit trust later gains control (or the ability to control), either directly or indirectly, of operations of an entity that are in respect of a trading business within the meaning of section 102M of the Income Tax Assessment Act 1936 ?

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This document has been finalised by TD 2011/7.

 There is a Compendium for this document: **TD 2011/7EC** .



Draft Taxation Determination

Income tax: will the exemption in section 102NA of the *Income Tax Assessment Act 1936* continue to apply to a unit trust that has become the interposed trust of a stapled group pursuant to Subdivision 124-Q of the *Income Tax Assessment Act 1997* if the trustee of the unit trust later gains control (or the ability to control), either directly or indirectly, of operations of an entity that are in respect of a trading business within the meaning of section 102M of the *Income Tax Assessment Act 1936*?

❶ This publication provides you with the following level of protection:

This publication is a draft for public comment. It represents the Commissioner's preliminary view about the way in which a relevant taxation 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.

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Ruling

1. No. The unit trust that has become the interposed trust of a stapled group in circumstances to which rollover pursuant to Subdivision 124-Q of the *Income Tax Assessment Act 1997* (ITAA 1997) applied will not continue to be exempt under section 102NA of the *Income Tax Assessment Act 1936* (ITAA 1936)¹ from being a trading trust if the trustee of that unit trust later gains control (or the ability to control), either directly or indirectly, of operations of an entity that are in respect of a trading business within the meaning of section 102M of the ITAA 1936.

¹ All legislative references are to the ITAA 1936 unless otherwise indicated.

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Date of effect

2. 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 75 to 77 of Taxation Ruling TR 2006/10).

Commissioner of Taxation

18 August 2010

Appendix 1 – Explanation

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

Explanation

3. Division 6C of Part III (Division 6C) treats a public trading trust, its unitholders and its trustee as if the public trading trust is a company for some tax purposes. Subparagraph 102R(1)(a)(iii) requires a public trading trust to be a trading trust. Subsection 102N(1) means that a unit trust is a trading trust in relation to a year of income if, at any time during that year, its trustee is carrying on a trading business, or controls (or is able to control, directly or indirectly) the affairs or operations of another entity in respect of its carrying on a trading business.

4. Division 6C was amended when Subdivision 124-Q of the ITAA 1997 was introduced. Subdivision 124-Q of the ITAA 1997 provides CGT roll-over for holders of ownership interests in a stapled group when a unit trust is interposed between them and the entities in the stapled group. (The unit trust then becomes the 'head' trust of the other entities.) There are also rollover consequences for the interposed trust in its holding of ownership interests in the entities in the stapled group. The Explanatory Memorandum to the Tax Laws Amendment (2007 Measures No. 5) Bill 2007 (the Explanatory Memorandum) describes the purpose of Subdivision 124-Q of the ITAA 1997 as being:

...to allow for the reorganisation of stapled groups, and in particular Australian Listed Property Trusts. This will enable Australian Listed Property Trusts to rearrange their stapled structures and allow them to interpose a head trust so that they are treated as a single entity for the purposes of overseas acquisitions.

5. Section 102N of the ITAA 1936 treats a unit trust as a trading trust in relation to a year of income in which the trustee carries on a trading business (that is, has any activity that is not **eligible investment business** as defined in section 102M of the ITAA 1936 and modified by sections 102MA, 102MB and 102MC of the ITAA 1936), or is able to control the affairs or operations of another person in respect of their carrying on of a trading business. A unit trust interposed between equity holders and existing companies or trusts would wholly own those existing companies and trusts, and its trustee would be likely to control or be able to control, directly or indirectly, the activities of those existing companies and trusts and of any entities they control. So if any of those existing companies or trusts or any entities they control have any activity that is not **eligible investment business** the interposed unit trust would be a trading trust under section 102N of the ITAA 1936. In the circumstances to which Subdivision 124-Q of the ITAA 1997 applies the interposed head trust wholly owns stapled entities of which at least one was a trust not taxed like a company and at least one was either a company or a trust taxed like a company. Practically, almost all such stapling arrangements have a company or a trust taxed like a company which had or controlled activity that is not **eligible investment business**.

6. Subsection 102N(2) was inserted into Division 6C to ensure that unit trusts, including such a head trust, would be able in future to acquire control of the activities of foreign entities whose business consisted primarily of investing in land for the purpose, or primarily for the purpose, of deriving rent (even if the activities of the foreign entities also included some activity that would not be **eligible investment business**).

7. Section 102NA was inserted into Division 6C to ensure that the imposition of such a head trust by such a reorganisation will not lead to the head trust being treated as a public trading trust under Division 6C, even though it owns members of the stapled group which are companies or which are taxed like companies because they are public trading trusts under that Division or are corporate unit trusts under Division 6B of Part III, provided certain other conditions are met.

8. Subsection 102N(2) provides:

Despite paragraph (1)(b), a unit trust is not a trading trust only because it has acquired ownership interests (including a controlling interest) in, or controls:

- (a) a foreign entity whose business, when considered together with the businesses of entities that the foreign entity controls or is able to control, directly or indirectly, consists primarily of investing in land outside Australia for the purpose, or primarily for the purpose, of deriving rent; or
- (b) a foreign entity controlled, or able to be controlled, directly or indirectly, by an entity covered by paragraph (a).

9. Subsection 102NA(1) provides:

A unit trust is not a trading trust for the purposes of this Division in relation to a year of income if:

- (a) the trust is an interposed trust in relation to a scheme for reorganising the affairs of stapled entities referred to in Subdivision 124-Q of the *Income Tax Assessment Act 1997* in relation to the year of income or an earlier year of income; and
- (b) a roll-over was obtained by any entity under that Subdivision of that Act in relation to the scheme for the year of income or that earlier year of income; and
- (c) the condition in subsection (2) is satisfied.

10. Subsection 102NA(2) provides:

The trustee of the trust must not, at any time during the year of income:

- (a) carry on a trading business; or
- (b) control, or be able to control, directly or indirectly, the affairs or operations of another entity that carries on a trading business, other than:
 - (i) a company that was, before the scheme was completed, one of the stapled entities referred to in Subdivision 124-Q of the *Income Tax Assessment Act 1997*; or
 - (ii) a subsidiary of one of those stapled entities that is a company, or an entity that is controlled or able to be controlled, directly or indirectly, by that company; or
 - (iii) a trust whose trustee was, before the scheme was completed, assessed and liable to pay tax under Division 6B or this Division and that was, before the scheme was completed, one of those stapled entities; or
 - (iv) an entity that is controlled or able to be controlled, directly or indirectly, by the trust referred to in subparagraph (iii);

in relation to the year of income or an earlier year of income.

11. Section 102NA of the ITAA 1936 operates to exclude some interposed trusts from being trading trusts. They must be interposed in reorganisations for which rollover under Subdivision 124-Q of the ITAA 1997 is obtained. They must also meet the requirements of subsection 102NA(2) of the ITAA 1936 that their trustee neither carries on a trading business nor controls or is able to control, directly or indirectly, the activities of another entity that carries on a trading business, except stapled companies and trusts of which the interposed trust became the head company under the reorganisation and except subsidiaries or entities those stapled companies and trusts are able to control.

12. The intended effect of section 102NA and subsection 102N(2) is described at paragraph 8.2 of the Explanatory Memorandum in the following terms:

This Schedule also amends the *Income Tax Assessment Act 1936* (ITAA 1936) to ensure that such restructures do not result in the interposed head trust being taxed as if it were a company. In addition, public unit trusts will be able to acquire controlling interests in, or control, foreign entities whose business consists primarily of investing in land outside Australia for the purpose, or primarily for the purpose, of deriving rent.

The context for these amendments is further described at paragraph 8.5 of the Explanatory Memorandum:

To enable Australian Listed Property Trusts to acquire overseas vehicles in exchange for their own equity, it is often necessary for the acquirer to issue only its own equity. For example, it is only where equity in a US Real Estate Investment Trust is exchanged for equity in the acquirer that the holders of the Real Estate Investment Trust are able to obtain a tax deferral in the US. In this respect, a stapled Australian Listed Property Trust is at a competitive disadvantage to a single entity seeking to acquire US Real Estate Investment Trusts. This is because the interest holders of the target Real Estate Investment Trust would be entitled to a CGT roll-over in the US if the acquirer was offering only its own equity but not if the acquirer was offering a combination of its own equity with other equity. An Australian Listed Property Trust equity which is stapled can only offer proportionate equity in each of the stapled entities and so cannot offer as much tax deferral as an acquirer offering only its own equity.

Their intended effect is further described at paragraph 8.17 of the Explanatory Memorandum:

These proposed amendments will facilitate Australian public unit trusts acquiring property and property-holding entities offshore.

Their overall intended effect is summarised at paragraph 8.60 of the Explanatory Memorandum in the following terms:

Essentially, under these amendments a previously stapled company, owned or controlled by the interposed trust, will be able to continue to operate as it had before the restructure, without the interposed trust being taxed as a company. The interposed trust will be able to own, or control, any previously stapled public unit trusts on the basis that they are not carrying on a trading business.'

13. The amendments were designed to ensure that trusts can acquire control of foreign entities whose business is primarily that of investing in foreign land at least primarily for rent (taking into account all businesses of entities they are able to control directly or indirectly). They can do this whether they are interposed trusts, under a reorganisation to which Subdivision 124-Q of the ITAA 1997 applied, or not. The amendments continue to apply the same rules as before to any trust other than such an interposed trust, including trusts controlled or able to be controlled by such an interposed trust.

14. Statutory interpretation requires that legislation be considered in its context. As Brennan CJ, Dawson, Toohey and Gummow JJ noted in *CIC Insurance v. Bankstown Football Club Ltd* [1997] HCA 2; (1997) 187 CLR 384 at CLR page 408 (footnotes omitted):

[T]he modern approach to statutory interpretation (a) insists that the context be considered in the first instance, not merely at some later stage when ambiguity might be thought to arise, and (b) uses 'context' in its widest sense to include such things as the existing state of the law and the mischief which, by legitimate means such as those just mentioned, one may discern the statute was intended to remedy. Instances of general words in a statute being so constrained by their context are numerous. In particular, as McHugh JA pointed out in *Isherwood v. Butler Pollnow Pty Ltd*, if the apparently plain words of a provision are read in the light of the mischief which the statute was designed to overcome and of the objects of the legislation, they may wear a very different appearance. Further, inconvenience or improbability of result may assist the court in preferring to the literal meaning an alternative construction which, by the steps identified above, is reasonably open and more closely conforms to the legislative intent.

As McHugh, Gummow, Kirby and Hayne JJ noted in *Project Blue Sky Inc v. Australian Broadcasting Authority* [1998] HCA 28; (1998) 194 CLR 355 at paragraphs 69 to 71 (footnotes omitted):

69. The primary object of statutory construction is to construe the relevant provision so that it is consistent with the language and purpose of all the provisions of the statute. The meaning of the provision must be determined 'by reference to the language of the instrument viewed as a whole'. In *Commissioner for Railways (NSW) v. Agalianos*, Dixon CJ pointed out that 'the context, the general purpose and policy of a provision and its consistency and fairness are surer guides to its meaning than the logic with which it is constructed'. Thus, the process of construction must always begin by examining the context of the provision that is being construed.

70. A legislative instrument must be construed on the prima facie basis that its provisions are intended to give effect to harmonious goals. Where conflict appears to arise from the language of particular provisions, the conflict must be alleviated, so far as possible, by adjusting the meaning of the competing provisions to achieve that result which will best give effect to the purpose and language of those provisions while maintaining the unity of all the statutory provisions. Reconciling conflicting provisions will often require the court 'to determine which is the leading provision and which the subordinate provision, and which must give way to the other'. Only by determining the hierarchy of the provisions will it be possible in many cases to give each provision the meaning which best gives effect to its purpose and language while maintaining the unity of the statutory scheme.

71. Furthermore, a court construing a statutory provision must strive to give meaning to every word of the provision. In *The Commonwealth v. Baume* Griffith CJ cited *R v. Berchet* to support the proposition that it was 'a known rule in the interpretation of Statutes that such a sense is to be made upon the whole as that no clause, sentence, or word shall prove superfluous, void, or insignificant, if by any other construction they may all be made useful and pertinent'.

15. Considered together, the provisions of subsections 102N(2), 102NA(1) and 102NA(2) were designed to enable the acquisition by Australian public unit trusts such as Australian Listed Property Trusts of overseas vehicles by issuing their own equity in the public unit trusts, where those vehicles control, overall, a business primarily of investing in real property at least primarily for deriving rent. It was intended that such acquisitions should not cause the public unit trusts to become trading trusts. The legislative intent behind the enactment of section 102NA in this context was to help facilitate the reorganisation of stapled groups, particularly Australian Listed Property Trusts, to interpose a public unit trust which will not be a trading trust required to be taxed like a company by reason of the rollover. That interposed trust will then be able to acquire overseas vehicles with businesses primarily of investing in real property at least primarily for deriving rent, by issuing its own equity, which was expected to be more readily acceptable to vendors than stapled equity in each of the stapled entities existing before the reorganisation.

16. In this context, the provisions of subsection 102NA(2) are given full effect by ensuring that the previously stapled entities could continue their existing operations after reorganisation, without their existing trading business activity causing the interposed trust to be a trading trust taxed as a company. The Explanatory Memorandum explains at paragraph 8.60 that:

under these amendments a previously stapled company, owned or controlled by the interposed trust, will be able to continue to operate as it had before the restructure, without the interposed trust being taxed as a company. The interposed trust will be able to own, or control, any previously stapled public unit trusts on the basis that they are not carrying on a trading business.

17. The language and purpose of the amendments, taken together, would not be given intended effect were paragraph 102NA(2)(b) of the ITAA 1936 misunderstood as allowing an interposed trust owning stapled companies and stapled trusts taxed like companies to be able after a reorganisation to which Subdivision 124-Q of the ITAA 1997 applied then to come to control or be able to control new trading businesses, directly or indirectly, if that control arose through the stapled companies or stapled trusts taxed like companies.

18. The hierarchy of the provisions is clearly that paragraph 102NA(2)(b) of the ITAA 1936 is only instrumental to the overall intent of subsection 102N(2) of the ITAA 1936, of paragraph 102NA(2)(a) of the ITAA 1936 which precludes an interposed trust from itself coming to be able to control a trading business, directly or indirectly, and of the rollovers for a reorganisation to which Subdivision 124-Q of the ITAA 1997 applies.

19. The entities described in subparagraphs 102NA(2)(b)(i) to (iv) include entities that carry on trading businesses that were themselves or were controlled, directly or indirectly, by one of the stapled entities before the reorganisation. They do not include any entities that were not companies, or taxed like companies, before the reorganisation. They do not include any subsidiaries or other entities or other trading businesses that came to be controlled, directly or indirectly, by one of the stapled entities only after the reorganisation.

20. This means that if an entity and its trading business are directly or indirectly controlled by one of the stapled entities before the reorganisation was completed, the interposed trust will be taken not to be a trading trust under section 102NA.

21. However, if the trustee of the interposed unit trust gains control (or the ability to control), either directly or indirectly, after the interposition of the trust, of other operations of an entity that are in respect of a trading business, the unit trust will fail to satisfy paragraph 102NA(1)(c) and will therefore be a trading trust under section 102N. This is the same as the effect of the law if the trustee of the interposed unit trust begins to carry on a trading business after the reorganisation. It is the same as the effect of the law if a stapled trust that is not taxed like a company before the reorganisation begins to carry on a trading business after the reorganisation, or begins to control or to be able to control such a business, directly or indirectly, after the reorganisation.

22. Subparagraphs 102NA(2)(b)(i) to (iv) of the ITAA 1936 could be suggested as having a wider effect. Subparagraphs 102NA(2)(b)(i) and (iii) of the ITAA 1936 could be suggested as allowing one of the stapled entities taxed like companies for which the reorganisation interposed the unit trust to acquire any new trading business after the reorganisation, without making the interposed unit trust a trading trust taxed like a company under Division 6C. Similarly, subparagraphs 102NA(2)(b)(ii) and (iv) of the ITAA 1936 could be suggested as allowing one of the stapled entities taxed like companies for which the reorganisation interposed the unit trust to acquire control after the reorganisation of any trust or company and of any trading business carried on in that trust or company, without making the interposed unit trust a trading trust taxed like a company under Division 6C. These suggestions would not serve the overall purposes of the amendments or of the law, which clearly intended to retain the application of Division 6 of Part III of the ITAA 1936 to interposed trusts other than by reason of a reorganisation applying rollover under Subdivision 124-Q of the ITAA 1997 itself.

Appendix 2 – Your comments

23. You are invited to comment on this draft Determination. Please forward your comments to the contact officer by the due date.

24. A compendium of comments is also prepared for the consideration of the relevant Rulings Panel or relevant tax officers. An edited version (names and identifying information removed) of the compendium of comments will also be prepared to:

- provide responses to persons providing comments; and
- publish on the Tax Office website at www.ato.gov.au

Please advise if you do not want your comments included in the edited version of the compendium.

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References

Previous draft:

Not previously issued as a draft

Related Rulings/Determinations:

TR 2006/10

Subject references:

- public trading trusts
- stapled trusts
- trading trusts
- unit trusts
- widely held trusts

Legislative references:

- ITAA 1936
- ITAA 1936 Pt III Div 6
- ITAA 1936 Pt III Div 6B
- ITAA 1936 Pt III Div 6C
- ITAA 1936 102M
- ITAA 1936 102MA
- ITAA 1936 102MB
- ITAA 1936 102MC
- ITAA 1936 102N
- ITAA 1936 102N(1)
- ITAA 1936 102N(1)(b)
- ITAA 1936 102N(2)
- ITAA 1936 102NA
- ITAA 1936 102NA(1)

- ITAA 1936 102NA(1)(c)
- ITAA 1936 102NA(2)
- ITAA 1936 102NA(2)(a)
- ITAA 1936 102NA(2)(b)
- ITAA 1936 102NA(2)(b)(i)
- ITAA 1936 102NA(2)(b)(ii)
- ITAA 1936 102NA(2)(b)(iii)
- ITAA 1936 102NA(2)(b)(iv)
- ITAA 1936 102R(1)(a)(iii)
- ITAA 1997 Subdiv 124-Q

Case references:

- CIC Insurance v. Bankstown Football Club Ltd [1997] HCA 2; (1997) 187 CLR 384
- Commissioner for Railways (NSW) v. Agalianas (1955) 92 CLR 390
- Project Blue Sky Inc v. Australian Broadcasting Authority [1998] HCA 28; (1998) 194 CLR 355
- R v. Berchet (1690) 89 ER 480
- The Commonwealth v. Baume [1905] HCA 11; (1905) 2 CLR 405

Other references:

- Explanatory Memorandum to the Tax Laws Amendment (2007 Measures No. 5) Bill 2007

ATO references

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