


# ***TA 2023/3 - Franking credit refunds - income tax exempt entities receiving franked distributions in the form of property other than money***

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## Taxpayer Alert

# Franking credit refunds – income tax exempt entities receiving franked distributions in the form of property other than money

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### **📌 About Taxpayer Alerts**

Alerts provide a summary of our concerns about new or emerging higher risk tax or superannuation arrangements or issues that we have under risk assessment.

While an Alert describes a type of arrangement, it is not possible to cover every potential variation of the arrangement. The absence of an Alert on an arrangement or a variation of an arrangement does not mean that we accept or endorse the arrangement or variation, or the underlying tax consequences.

Refer to [PS LA 2008/15](#) for more information about Alerts. See [Alerts](#) issued to date.

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### **Description**

1. We are currently reviewing arrangements involving franked distributions in the form of property other than money (in specie distributions) that are made to income tax exempt entities, including registered charities, deductible gift recipients, scientific institutions and public educational institutions.
2. Under these arrangements:
  - an in specie franked distribution is made (or flows indirectly) to an income tax exempt institution, and
  - there are restrictions on the ordinary incidents of ownership of the distributed property that
    - are imposed as part of the terms and conditions for the making of the franked distribution, and

- prevent the income tax exempt entity from receiving immediate custody and control of that property.
3. We are concerned that income tax exempt entities may be entering into these arrangements without being aware that these restrictions may make them ineligible for a refund of the franking credits attached to the franked distribution.
4. All legislative references in this Alert are to the *Income Tax Assessment Act 1997*.

### Legislative context

5. Pursuant to subparagraph 207-122(b)(i), an entity that receives a franked distribution in the form of property other than money will not be eligible for a refund of franking credits where the terms and conditions on which the franked distribution is made are such that the entity 'does not receive immediate custody and control of the property'.
6. Our position is that subparagraph 207-122(b)(i) requires the recipient entity to receive, from the moment of distribution, control of the distributed property to the same extent as an absolute owner. In this context, ownership control commensurate with being the absolute owner involves having unrestricted authority over the ordinary incidents of ownership of that property.
7. Given that the operation of subparagraph 207-122(b)(i) may result in the recipient of the in specie distribution being ineligible for a refund of any attached franking credits, it is important for taxpayers and advisers to be aware of the potential implications when entering into these types of arrangements.

### Examples

8. The examples in paragraphs 9 to 15 of this Alert, while not exhaustive, are illustrative of arrangements where subparagraph 207-122(b)(i) may apply.

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#### **Example 1: Restrictions resulting in ineligibility for franking credit refund**

9. *The Distributing Entity makes an in specie distribution of shares held by it in the Company (the Company Shares) to the Recipient Entity. The distribution is fully franked.*
10. *Prior to the in specie distribution being made, the Distributing Entity and the Recipient Entity enter into a formal agreement that prohibits the Recipient Entity from selling, transferring or disposing of the Company Shares to another entity for a period of time, without the consent of the Distributing Entity.*
11. *The restrictions set out in the formal agreement mean the Recipient Entity does not have the required immediate custody and control of the Company Shares and is not eligible for a refund of franking credits.*

#### **Example 2: Variation of example 1 where restrictions are imposed by a third party**

12. *The Distributing Entity makes an in specie distribution of shares held by it in the Company (the Company Shares) to the Recipient Entity. The distribution is fully franked.*
13. *A third party, the Consenting Entity, also holds shares in the Company. The Consenting Entity is not a related party or associate of the Distributing Entity.*

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14. *Prior to the in specie distribution being made, a formal agreement is entered into by the Consenting Entity, the Distributing Entity and the Recipient Entity. Under the formal agreement:*

- *the Distributing Entity requires the consent of the Consenting Entity before making the in specie distribution of the Company Shares to the Recipient Entity, and*
- *the Recipient Entity is prohibited from selling, transferring or disposing of the Company Shares to another entity for a period of time, without the consent of the Consenting Entity.*

15. *The restrictions set out in the formal agreement mean the Recipient Entity does not receive the required immediate custody and control of the Company Shares and is not eligible for a refund of franking credits.*

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#### **What are our concerns?**

16. In respect of the arrangements covered in this Alert, we are concerned that income tax exempt entities may be incorrectly seeking refunds of franking credits.

#### **What are we doing?**

17. We are monitoring applications for franking credit refunds by income tax exempt entities where the claim is in respect of an in specie franked distribution.

18. By issuing this Alert, we are making the community aware of the need to take into consideration the operation of subparagraph 207-122(b)(i) before entering into arrangements involving in specie franked distributions of shares and other property due to the potential consequences on eligibility for a refund of franking credits.

19. We are also looking to identify an appropriate case to test our views on the application of subparagraph 207-122(b)(i).

#### **What should you do?**

20. If you have entered, or are contemplating entering, into an arrangement of this type, we encourage you to:

- phone or email us using the contact details provided at the end of this Alert
- ask us for our view through a [private ruling](#)
- seek independent professional advice
- make a [voluntary disclosure](#) to reduce penalties that may apply.

**Do you have information?**

21. To provide information about this type of arrangement, you can:

- phone us on **1800 060 062**
- contact the officer named in this Taxpayer Alert.

Contact officer: Glenn Cooper

Email: [Glenn.Cooper@ato.gov.au](mailto:Glenn.Cooper@ato.gov.au)

Phone: **03 994 69177**

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**Commissioner of Taxation**

8 December 2023

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**References**

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*Legislative references:*

- ITAA 1997 207-122(b)(i)
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## ATO references

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