

# Unpacking the latest on UPEs, Corporate Beneficiaries & Div 7A

5 October, 2023



# Today's Speakers



**Brian Richards**

Taxation Advisor – Richards Advisory



**Emily Pritchard**

Chief Legal & Operating Officer – Acis

# TD 2022/11 Overview

- The Commissioner's most recent iteration of the Division 7A application to unpaid trust distributions (UPE's) to a corporate beneficiary was provided by TD 2022/11.
- The TD is to apply to a trustee's distribution of trust income after 1<sup>st</sup> July 2022 and inter alia provided that:
  - (i) A company's decision not to call for payment of the trust distribution was a 'loan' for the purposes of subsection 109D(3) – ie., the provision of financial accommodation:
  - (ii) That if the unpaid amount was put aside on a sub-trust arrangement, the UPE came to an end;
  - (iii) If the company 'consented' to the use its sub-trust amount to be applied or otherwise used by an entity who was either a shareholder of the company or associate of the shareholder – that application et al was the making of a loan for the purposes of section 109D; and
  - (iv) To the extent that the UPE ceased to exist as a consequence of the sub-trust arrangement, subdivision EA was not applicable

# TD 2022/11 Implications

- TD 2022/11 provided that:
  - The section 109D loan was made at and when the corporate beneficiary is taken to know the amount of the present entitlement (in the 2024 year of income for a June 2023 trust distribution);
  - To avoid the application of Division 7A, the relevant entities would need to rectify the 'loan' by various strategies including inter alia facilitating a section 109M complying loan agreement by the due date of lodgment of the company's 2024 taxation return (May 2025);
  - Where the company's sub-trust amount is applied for the benefit of a shareholder (or associate) of the company, it is necessary to 'trace' the specific application of the sub-trust amount to ascertain the section 109D treatment

# Bendel – the Facts

- The trust distributed trust income to the company;
- Pursuant to the terms of the trust deed, the amounts distributed and unpaid were set aside on a sub-trust arrangement (no specific trust asset was allocated to the sub-trust amount;
- No s.109M loan agreements or PSLA 2010/4 investment loans were put in place in relation to the unpaid trust distributions;
- As a consequence of a audit review of Bendel's tax affairs, the Commissioner assessed the Trust in relation to the unpaid trust distributions to the company as a deemed dividend pursuant to section 109D(1) (no franking allowed;
- Bendel also received trust distributions, however these distributions were offset against monies owed to him; and
- The trust made payments ('drawings') to Bendel during the relevant years.

# AAT Decision – Section 109D(3) Loan

That the term ‘loan’ in section 109D(3) does not include an UPE:

- The ‘provision of financial accommodation’ relied on by the Commissioner does not include equitable obligations – such as non-paid trust distributions;
- Rejected the Commissioner’s reference to other statutory contexts to define the meaning of ‘provision of financial accommodation’;
- Rejected the Commissioner’s argument that the existence of Subdivision EA does not exclude ‘consensual arrangements not to be paid’;
- There was no trustee power exercised to apply specific trust property, rather the original trust continued and the equitable obligation arose from the provisions of the trust deed – there was no new trust created. The unpaid amount was an equitable obligation
- The introduction of subdivision EA and the statutory context of the subdivision relative to section 1098D cannot be ignored.
- The Commissioner’s argument re subdivision EA raised the ‘spectre’ of taxing two people in respect of precisely the same under the same circumstance, namely the UPE”

## AAT Decision – Amounts set aside on sub-trust

- Pursuant to the terms of the trust deed, the trust distributions were set aside on a separate trust for the absolute benefit of the beneficiary.
- The setting aside of the trust distributions did not bring to an end the UPE
- The equitable obligation in relation to the unpaid distribution continued to exist
- Notwithstanding that the equitable obligation had been set aside on a sub-trust arrangement, subdivision EA would still be applicable if the trust made a loan to a shareholder (associate) and the unpaid obligation to the company was still in existence (section 109XA would apply)

# What now – The Commissioner?

It is early days however, in my opinion:

- The Commissioner will appeal – this decision contradicts the very essence that the former TR 2010/3 and TD 2022/11 relied in relation to:
  - The application of subsection 109D(3) to unpaid trust distributions;
  - The consequential implications where the unpaid amount is set aside on a sub trust arrangement (no specific trust fund allocation); and
  - The application of subdivision EA where the unpaid amount has been set aside on a sub-trust arrangement
- The Commissioner will respectfully ‘ignore’ the AAT decision and maintain that the TD 2022/11 status quo remains;
- Will perhaps try to hurry up the Government to introduce Treasury’s Division 7A recommendations (which include a specific recommendation that UPE’s be statutory included in the definition of a loan for the purposes of section 109D(3))



# What Now – the Advisor/Client

Based on TD 2022/11, the relevant decision-making time is the lodgment of the 2024 company tax return – so wait and do nothing in the interim;

Assume that the Commissioner will successfully appeal the matter and:

- Ignore the AAT decision based on that expected appeal outcome (best advise the client; or
- Put in place a section 109M complying loan agreement or pay the UPE by May 2025

**Note:** have regard to the section 100A implications (PCG 2022/2 – working capital exception) of putting the distribution on a loan agreement

Questions?

Acis.

P 1800 773 477  
acis@acis.net.au  
**acis.net.au**

**Acis.**

