

# TAX BULLETIN

*An update publication for our clients*

22 June 2011

## 30 June 2011 'Drop-dead' Requirements

With 30 June 2011 rapidly approaching it is important that action is taken to implement a range of tax measures. The purpose of this Tax Bulletin is to highlight what we regard as the most crucial of these requirements so that you can ensure that the appropriate action is taken before midnight on 30 June 2011.

We have identified the following requirements as being crucial 'drop-dead' ones:

- Division 7A:
  - 30 June 2010 unpaid present entitlements ("UPEs") need to be placed on Sub-trusts;
  - minimum yearly repayments on prior year loans must be made;
- Tax Consolidation:
  - elections to maintain a 100% pre-CGT proportion for shares in pre-CGT consolidated groups must be made;
- Trusts:
  - beneficiary TFNs must be collected;
  - resolutions to stream capital gains and franked distributions need to be made;
  - resolutions to ensure access to the CGT small business concessions must be made;
- Private Ancillary Funds ("PAFs"):
  - sufficient distributions must have been made to eligible recipients;
- Thin Capitalisation:
  - capital injections to avoid breaching the required debt/equity ratios need to be made;
- Taxation of financial arrangements ("TOFA"):
  - election to use the 'hedging financial arrangements method' must be made.

### Division 7A

#### 30 June 2010 UPEs

Last year the ATO announced in PSLA 2010/4 that to avoid a UPE due from a trust to a private company beneficiary for the year ended 30 June 2010 being regarded as a loan from that company to the trust for Division 7A purposes, a trustee has until midnight on 30 June 2011 to decide to place that UPE on a Sub-trust. An appropriate investment option must also be chosen for that Sub-trust.

The best way of evidencing the fact that the 30 June 2011 deadline has been met will be to have a trustee pass a resolution - i.e. to have a written minute of a meeting of the trustee(s) resolving to place the UPE on a Sub-trust for the exclusive benefit of the beneficiary using one of the investment options. In light of discussions between Pitcher Partners and the ATO it would also be prudent to have the trustee document the terms of whatever investment option is chosen by that date.

## Minimum yearly loan repayments

To avoid a deemed dividend arising, the required minimum yearly repayment must be made on/by 30 June 2011 for all prior year complying Division 7A loans.

## Tax Consolidation

Due to recent amendments to the tax consolidation regime a number of elections must be made, in writing, by 30 June 2011. Of these elections, the one regarding pre-CGT shares is particularly important and must not be overlooked - i.e. maintaining the pre-CGT status of assets within a tax consolidated group can be crucial in the event of a sale and adverse commercial consequences may arise if the appropriate action to preserve that status is not taken.

The elections that must be made in writing by 30 June 2011 include:

- electing to have a pre-CGT proportion for shares in pre-CGT consolidated groups;
- treating certain foreign exchange gains and losses on debts that were reset (e.g. foreign currency debts) on CGT account;
- applying the retrospective MEC conversion rules;
- applying the anti-double up rule for tax cost calculations retrospectively;
- treating cash management trust investments as retained cost base assets retrospectively;
- applying the exception to CGT event L3 for certain doubtful debts retrospectively; and
- retrospectively removing the double negative adjustment for convertible notes on entry and exit into consolidation.

## Trusts

### TFN withholding rules for trusts

Under the TFN withholding rules for trusts, trustees must have actually collected by 30 June 2011 all of the TFN details for beneficiaries to whom distributions have been/will be made for the year ending 30 June 2011 - if they have not, they will be liable for withholding tax plus penalties and interest on those distributions when they are made.

It is crucial therefore, that the TFN details for beneficiaries are actually collected by trustees before 30 June 2011. A beneficiary quotes their TFN when they provide the trustee with their:

- TFN;
- full name;
- date of birth (individuals only);
- postal address;
- residential address for individuals (not a PO Box or private mailbag); and
- business address for non-individuals (not a PO Box).

There is no prescribed format for the provision of this information. Beneficiaries may provide this information either verbally or in writing (including an electronic format) to the trustee to meet the requirements.

## Streaming capital gains

Under a Bill that is currently before Parliament, a taxpayer will not be able to stream capital gains and/or franking credits through a trust for 2010/11 unless the beneficiaries of that trust:

1. are made specifically entitled to those capital gains and/or franking credits; and
2. have their entitlements to those capital gains and/or franking credits documented in the accounts/records of the trust, before midnight on 30 June 2011.

The following approach must therefore, be taken to planning for the current tax year:

- Identify before 30 June 2011 whether the streaming of capital gains and/or franked distributions from a trust may be required;
- If "Yes", check the trust deed to confirm that streaming is not prohibited. (Note: if streaming is prohibited under the trust deed then it cannot occur for tax purposes and the trust deed may need to be amended before 30 June 2011); and
- Complete a written record before midnight on 30 June 2011 that makes beneficiaries specifically entitled to the capital gains and/or franked distributions from the trust.

## CGT small business concessions

If a taxpayer has sold shares in a company or units in a unit trust and wishes to access the small business CGT concessions, it is critical that a significant individual is established. To establish whether an entity has a significant individual, the distributions made from a trust in the ownership structure during a year may be relevant. Accordingly, it is important to ensure that the appropriate distributions are made by 30 June 2011.

## PAFs

PAFs need to have met their 2011 distribution requirements (i.e. made sufficient distributions out to eligible recipients) by 30 June 2011 - a failure to do so exposes the trustee (or its directors) to administrative penalties and the PAF to the potential risk of losing its concessional tax treatment.

## Thin capitalisation

To avoid to avoid breaching the 'safe harbour' debt test of 75% of the average net value of its assets, a taxpayer should (if it has not already done so) review its thin capitalisation position as soon as possible and ensure that any capital injections that need to be made are done by 30 June 2011.

## TOFA

Under the TOFA rules a taxpayer can elect to use the 'hedging financial arrangements method' to work out their gains and losses on certain derivative financial arrangements and foreign currency hedges. To be eligible to use this method, a taxpayer must satisfy the recording requirements in the Tax Act. Broadly, the records must include both of the following:

- details that are required under the accounting standards; and
- details of the basis for allocating gains and losses from the hedging financial arrangement for income tax purposes.

Whilst these records must technically be in place at or soon after the time the hedging financial arrangement is created, regulations have been made that extend the time for recording details of the basis for allocating gains and losses from hedging financial arrangements until 30 June 2011.

## Further Information

Please ask either your regular Pitcher Partners tax contact or any of the contacts in the Pitcher Partners firms below for further details on the issues raised in this Tax Bulletin:

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