



THE TAX INSTITUTE

17 November 2021

Fiona Dillon
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Tax Counsel Network
Australian Taxation Office

By email: fiona.dillon@ato.gov.au

Dear Ms Dillon,

Guidance on the meaning of affiliate and withdrawn Taxation Ruling TR 2002/6

Based on feedback from our members, and their concerns about the lack of technical guidance on the meaning of affiliate following the withdrawal of former Taxation Ruling TR 2002/6 *Income tax: Simplified Tax System: eligibility – grouping rules (STS affiliate, control of non-fixed trusts) (the Ruling)*, The Tax Institute is writing to highlight the need for practical guidance from the Australian Taxation Office (**ATO**) on this subject.

The Ruling provided guidance on the application of the non-fixed trust control rule and simplified tax system (**STS**) affiliate under former Division 328 of the *Income Tax Assessment Act 1997 (ITAA 1997)*. Following the repeal of the STS, the Commissioner withdrew the Ruling without replacement on the basis that it related to a now-repealed regime and had no ongoing relevance.

Although we agree that the original basis for the Ruling is obsolete, The Tax Institute considers that the withdrawn guidance about STS affiliates provides useful and contemporary guidance generally about the definition of an affiliate which remains a relevant concept in the current tax law.

Technical analysis

Some aspects of the current tax laws relying on the definition of an affiliate include the following:

- A range of small tax concessions in Division 328 of the ITAA 1997 and the FBT, GST, PAYG instalment, superannuation and various administration provisions;
- The base rate entity rules in s 23AA of the *Income Tax Rate Act 1986*;
- The small business CGT concessions in Division 152 of the ITAA 1997;
- The calculation of aggregated turnover for determining eligibility for a range of Commonwealth and State COVID-19 economic support measures, including JobKeeper, temporary full expensing and loss carry back;
- The vacant land rules in s 26-102 of the ITAA 1997; and
- The meaning of an 'eligible investor' in an 'early-stage innovation company' pursuant to s 360-15 of the ITAA 1997.

We acknowledge that s 328-130 of the ITAA 1997 defines an 'affiliate' for tax purposes and note that the wording in that provision is almost identical to its predecessor, repealed s 328-380 of the ITAA 1997. However, we consider that contemporary guidance on the meaning of affiliate, drawing from and updating the principles and examples in the Ruling, would give taxpayers greater clarity and certainty when determining whether an entity is an affiliate in a range of circumstances.

Although the definitions of 'affiliate' and the former term 'STS affiliate' are not identical, they are sufficiently similar that the guidance in the Ruling about STS affiliates remains relevant to the meaning of an affiliate. The only distinction between s 328-130(1) (on affiliates) and s 328-380(8) (on STS affiliates) is that an STS affiliate may have included a company, individual, partnership or trust, whereas an affiliate is limited to an individual or company. The two definitions are otherwise identical in all other respects.

While the meaning of affiliate is not new, there remains widespread confusion across the tax profession and the taxpaying community about how to identify whether an individual or a company is an affiliate of another entity. In particular, more comprehensive and practical guidance on the meaning of '... acts, or could reasonably be expected to act, in accordance with your directions or wishes, or in concert with you, ...' would benefit taxpayers and practitioners who, in many cases, are challenged by how to interpret this term in practice.

Further, the original purpose of the meaning of 'STS affiliate' was to operate as an integrity measure for small businesses to determine whether their aggregated turnover was less than the (then) legislated threshold of \$2 million to access the repealed Simplified Tax System. It was similar in operation to repealed s 152-25 of the ITAA 1997 (about 'small business CGT affiliate') that also operated as an integrity measure for small businesses to determine whether their net assets were less than the (then) legislated threshold of \$5 million to access the small business CGT concessions in Division 152.

Today, the scope of 'affiliate' is far broader than these two measures, as can be seen from the indicative list on page 1 of this submission of provisions that rely on the meaning of 'affiliate'. An extended list of provisions throughout the tax law that utilise the meaning of 'affiliate' is set out at **Appendix A** of this submission. Further, from a policy perspective, what was once an integrity measure for very small businesses (less than \$2 million of aggregated turnover) has been applied as an integrity measure to much larger businesses, as high as (less than) \$5 billion of aggregated turnover. Accordingly, the relevance of the meaning of affiliate is far greater and applies to more taxpayers than ever before.

Another example of where guidance on the meaning of 'affiliate' would assist is in the context of the public entity exception to the indirect control test discussed in TD 2021/D4 *Income tax: aggregated turnover – application of the public entity exception to the indirect control test (TD 2021/D4)*. Subsection 328-125(8) of the ITAA 1997 provides that, where certain types of entities (**holding entities**) are interposed between a listed entity and the test entity, the listed entity is not taken to control the test entity merely because of its control over the interposed holding entity.

However, paragraph 41 under Example 2 of TD 2021/D4 notes that the example does not consider whether the interposed holding entity is an affiliate of the listed entity, such that the listed entity directly controls the test entity through its affiliation with the interposed holding entity, pursuant to s 328-125(2).

This issue is of particular concern to listed corporate groups. As the facts and circumstances of each corporate group may mean that some subsidiaries in the group are not taken to be indirectly controlled by the listed entity by virtue of the public entity exception, it is unclear whether other subsidiaries in the group would be taken to be affiliates of a listed parent entity.

We consider that further guidance on this issue would assist these types of taxpayers to calculate their aggregate turnover, given the number of tax concessions available to groups of this size.

Case for contemporary guidance

Accordingly, although it would not be appropriate to re-issue the Ruling in its entirety, we consider that comprehensive and contemporary guidance on the meaning of affiliate is warranted, that could readily draw on the Ruling. In particular, we consider that paragraphs 31 to 65 (including the full table at paragraph 65) of the Ruling contain valuable content to assist taxpayers in applying the definition of an affiliate in practice. We request that the ATO review, refresh and include these aspects in contemporary guidance suitable for the current law.

The abovementioned paragraphs address the following issues:

- Paragraphs 31 to 35 provide guidance about the scope of when an entity may be considered to be an affiliate of another. This includes ad-hoc dealings and foreign resident entities.
- Paragraphs 38 to 43 provide guidance about applying the first limb of the STS affiliate definition – i.e. whether the entity acts or has acted according to the directions, wishes or in concert with the other entity.
- Paragraphs 44 to 48 provide guidance about applying the second limb of the STS affiliate definition – i.e. whether the entity could reasonably be expected to act according to the instructions, wishes or in concert with the other entity.
- Paragraphs 49 to 56 provide guidance about the meaning of ‘can reasonably be expected’.
- Paragraphs 57 to 65 (including the full table at paragraph 65) provide guidance around the meaning of ‘in concert’.

We consider that the content from the above paragraphs would enable taxpayers to understand how to properly apply s 328-130(1). Many of the terms in this provision are not defined in the legislation and the proper application is dependent on the facts and circumstances of the taxpayer. For example, different considerations are involved where the potential affiliate is an individual or company. These nuances are not apparent in s 328-130.

Closing comments

For completeness, the paragraphs in the Ruling that we have not included relate to concepts that were specific to the repealed STS rules or are irrelevant to the definition of an affiliate in s 328-130(1).

We wish to consult with you about the form the guidance may be able to take to remain relevant, useful and not overly prescriptive for ATO officers, taxpayers and advisers.

We would be pleased to continue to work with the ATO on any future plans or guidance products relating to the meaning of affiliate.

Further, The Tax Institute will be conducting a series of guided workshops with our members in early 2022 to gather common scenarios of concern and identify cases where practitioners find the application of s 328-130 challenging in practice. These common scenarios will be shared with the ATO to assist in developing guidance.

The Tax Institute is the leading forum for the tax community in Australia. We are committed to shaping the future of the tax profession and the continuous improvement of the tax system for the benefit of all. In this regard, The Tax Institute seeks to influence tax and revenue policy at the highest level with a view to achieving a better Australian tax system for all. Please refer to **Appendix B** for more about The Tax Institute.

If you would like to discuss any of the above, please contact our Senior Advocate, Robyn Jacobson, on (03) 9603 2008.

Yours faithfully,

A handwritten signature in black ink, appearing to read 'Peter Godber', with a long horizontal flourish extending to the right.

Peter Godber

President

APPENDIX A

Aggregated turnover threshold	Measure	Provision(s)
—	Active asset test	s 152-35 of the ITAA 1997
—	Vacant land rules	s 26-102 of the ITAA 1997
\$2 million	Small business CGT concessions including:	s 152-10(1AA)
	• 15-year exemption	Subdiv 152-B of the ITAA 1997
	• Small business 50% reduction	Subdiv 152-C of the ITAA 1997
	• Retirement exemption	Subdiv 152-D of the ITAA 1997
	• Small business roll-over	Subdiv 152-E of the ITAA 1997
\$5 million	Small business income tax offset	Subdiv 328-F of the ITAA 1997
\$6 million	Maximum net asset value test	s 152-15 of the ITAA 1997
\$10 million	Small business entity rules and small business tax concessions, including:	Div 328 of the ITAA 1997
	• Simplified depreciation for small business entities	Subdiv 328-D of the ITAA 1997
	• Small business restructure roll-over	Subdiv 328-G of the ITAA 1997
	• Paying PAYG instalments based on GDP-adjusted notional tax	s 45-120 to Sch 1 of the <i>Tax Administration Act 1953 (TAA)</i>
	• 2-year amendment period for income tax returns	ss 170(1) of the <i>Income Tax Assessment Act 1936 (ITAA 1936)</i>
	• Simplified BAS reporting	s 45-130 to Sch 1 of the TAA
	• Accounting for GST on a cash basis	s 29-40 of the <i>A New Tax System (Goods And Services Tax) Act 1999 (GST Act)</i>
	• Annual apportionment of GST input tax credits	s 131-5 of the GST Act
	• Paying GST by instalments	s 162-5 of the GST Act

Aggregated turnover threshold	Measure	Provision(s)
\$10 million	<ul style="list-style-type: none"> Excise concessions 	s 69(1) of the <i>Customs Act 1901</i> ; s61C(1) of the <i>Excise Act 1901</i>
	<ul style="list-style-type: none"> FBT car parking exemption 	s 58GA of the <i>Fringe Benefits Tax Assessment Act 1986 (FBTA)</i>
	<ul style="list-style-type: none"> FBT work-related devices exemption 	s 58X(4) of the FBTA
	<ul style="list-style-type: none"> Payment of superannuation contributions to an approved superannuation clearing house 	s 23B of the <i>Superannuation Guarantee (Administration) Act 1992</i>
	<ul style="list-style-type: none"> Contribution of small business concession amounts to superannuation 	s 292-90 of the ITAA 1997
	<ul style="list-style-type: none"> Exemption from making adjustments under indirect value shifting rules 	s 727-15(8) of the ITAA 1997
\$20 million	R&D – eligibility to receive refundable tax offsets	s 355-1 of the ITAA 1997
\$10 million – \$50 million	Instant asset write-off	s 40-82 of the ITAA 1997
\$50 million	Immediate deduction of eligible prepayments	ss 82KZM and 82KZMD of the ITAA 1936
	Base rate entity – determining the corporate tax rate and the corporate tax rate for imputation purposes	s 23AA of the <i>Income Tax Rates Act 1986</i>
	Cash flow boost	s 5 of the <i>Boosting Cash Flow For Employers (Coronavirus Economic Response Package) Act 2020</i>
\$100 million	Mandatory application of the Taxation of Financial Arrangements (TOFA) rules	s 230-5 of the ITAA 1997
\$5 billion	Loss carry-back rules	s 160-1 of the ITAA 1997

Aggregated turnover threshold	Measure	Provision(s)
\$5 billion	Temporary full expensing	ss 40-155, 40-160, 328-181 of the ITAA 1997; See also Schedule 7 to the <i>Treasury Laws Amendment (A Tax Plan For The COVID-19 Economic Recovery) Act 2020</i> <i>Subdiv 40-BB of the Income Tax (Transitional Provisions) Act 1997</i>
Various	JobKeeper	<i>Coronavirus Economic Response Package (Payments and Benefits) Amendment Rules (No. 2) 2020</i>

APPENDIX B

About The Tax Institute

The Tax Institute is the leading forum for the tax community in Australia. We are committed to representing our members, shaping the future of the tax profession and continuous improvement of the tax system for the benefit of all, through the advancement of knowledge, member support and advocacy.

Our membership of more than 11,000 includes tax professionals from commerce and industry, academia, government and public practice throughout Australia. Our tax community reach extends to over 40,000 Australian business leaders, tax professionals, government employees and students through the provision of specialist, practical and accurate knowledge and learning.

We are committed to propelling members onto the global stage, with over 7,000 of our members holding the Chartered Tax Adviser designation which represents the internationally recognised mark of expertise.

The Tax Institute was established in 1943 with the aim of improving the position of tax agents, tax law and administration. More than seven decades later, our values, friendships and members' unselfish desire to learn from each other are central to our success.

Australia's tax system has evolved, and The Tax Institute has become increasingly respected, dynamic and responsive, having contributed to shaping the changes that benefit our members and taxpayers today. We are known for our committed volunteers and the altruistic sharing of knowledge. Members are actively involved, ensuring that the technical products and services on offer meet the varied needs of Australia's tax professionals.