TD 2017/25EC - Compendium

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Public advice and guidance compendium – TD 2017/25

This is a compendium of responses to the issues raised by external parties to draft Taxation Determination TD 2016/D2 *Income tax: can a foreign resident elect to treat their interest in a limited partnership as an interest in a foreign hybrid limited partnership under paragraph 830-10(2)(b) of the Income Tax Assessment Act 1997?*

This compendium of comments has been edited to maintain the anonymity of entities that have commented.

Summary of issues raised and responses

Issue No.	Issue raised	ATO response / action taken
1	**Draft Determination should be amended to restrict its application to inbound investment:** The draft Determination could be interpreted to apply to outbound investment scenarios to preclude an election being made by a partner in a foreign limited partnership that is either: • a CFC (with an Australian investor), or • a non-resident trust estate (with an Australian resident beneficiary). This would result in unintended and inappropriate outcomes that include: • inconsistent tax outcomes depending on the level of interest held by the Australian investor in the CFC and whether it results in an amount of attributable income, and • loss of partnership treatment under Division 5 of the *Income Tax Assessment Act 1936* (ITAA 1936) in determining the assessable income in relation to the interest.	Acknowledged. The final Determination has been amended to clarify that it does not apply: a) if the foreign resident is a CFC or was taken to be a Part XI Australian resident under former Part XI of the ITAA 1936, or b) for the purposes of calculating the net income of a partnership or trust estate. By way of explanation, a note to paragraph 11 now states that certain taxpayers were taken to be Part XI Australian residents (see former subsection 485(6) of the ITAA 1936). Also, the former FIF rules applied in the calculation of the notional income of a CFC (based on the assumption in section 383 of the ITAA 1936 that the CFC is a taxpayer and a resident), and in the calculation of the net income of a partnership or trust estate (see former section 485A of the ITAA 1936). Words have also been added to paragraph 14 of the Explanation (Appendix 1) to clarify that foreign residents 'who were not subject to the former FIF rules' cannot make the election under subsection 830-10(2) of the *Income Tax Assessment Act 1997*

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	The draft Determination should be amended to restrict its application to inbound investment or clarify that an election can only be made by a partner that is an Australian resident or an entity that is required under relevant Australian tax law to calculate the taxable income as if it were an Australian resident.	(ITAA 1997).
2	**Election under former section 485AA of the ITAA 1936 not as restrictive as draft Determination states:** The precursor to the election in paragraph 830-10(2)(b) of the ITAA 1997 (former section 485AA of the ITAA 1936) was not limited to Part XI Australian residents (see paragraph 11 of the draft Determination) on the basis that: • The effect of the foreign hybrid election was not merely to 'switch off' the operative provision in former section 529 of the ITAA 1936 but to also activate the foreign hybrid rules in Division 830 of the ITAA 1997 (refer to the Note to former subsection 485AA(5) of the ITAA 1936). There is nothing within former section 485AA of the ITAA 1936, stated or implied, which requires the taxpayer making the election to be a Part XI Australian resident. Rather, that condition is contained in former section 485 of the ITAA 1936 with respect to the activation of the operative FIF provisions, not its disengagement by election. Paragraph 830-10(2)(b) of the ITAA 1997 refers only to former section 485AA of the ITAA 1936. • Retention of the ability to make the election after the repeal of the FIF attribution rules supports the argument that the election had a dual purpose and	The two consequences of an election under former subsection 485AA(5) of the ITAA 1936 (disengaging the FIF attribution rules and activating partnership treatment under the foreign hybrid rules) were interrelated – partnership treatment was a dependent on, and a consequence of, disengaging the FIF rules. For the reasons set out in the final Determination, the Commissioner's view is that you could only choose under former subsection 485AA(5) of the ITAA 1936 to activate the foreign hybrid rules (and disengage the FIF rules) if you were a Part XI Australian resident that would otherwise be subject to the FIF rules. The Commissioner acknowledges that the election mechanism was retained despite the FIF rules being repealed. However this was to ensure that, regardless of whether there is another taxpayer that is an attributable taxpayer in relation to a CFC, 'normal tax treatment' would continue to apply to interests held by taxpayers that are not attributable taxpayers (they are excluded from partnership treatment unless they opt in). Importantly however, as paragraphs 12 to 13 of the final Determination provide, the conditions required for making the election are the same as those under former section 485AA of the ITAA 1936 (see also paragraph 1.36 of the Explanatory Memorandum to *Tax Laws Amendment (Foreign Source Income Deferral) Bill (No. 1) 2010*).

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	was not limited to disengaging attribution under former section 529 of the ITAA 1936.	
3	**Not necessary to satisfy the conditions of former section 485 of the ITAA 1936 to be eligible to make an election under former section 485AA of the ITAA 1936:** The Commissioner has previously allowed a complying superannuation fund the ability to make a section 485AA election, despite former subsection 519B(2) of the ITAA 1936 stating that the operative provision does not apply to a complying superannuation fund. The Commissioner has always applied the provisions in the following manner: (1) Was the interest a FIF interest? (2) If so, has the taxpayer made an election under former section 485AA of the ITAA 1936 for the purpose of Division 830 of the ITAA 1997? (3) If not, did the taxpayer meet the conditions in former section 485 of the ITAA 1936? (4) If so, did the taxpayer apply the exemption in former section 519B of the ITAA 1936? The effect of the Commissioner applying these provisions in this order is that for (2), when a taxpayer made an election, the interest was not held to be a FIF (per former subsection 485AA(5) of the ITAA 1936). Therefore, it was not possible to satisfy the requirements for (3) as the conditions in former section 485 of the ITAA 1936 cannot be satisfied. As such, it was never a requirement that a taxpayer must first be subject to the operation of the FIF rules before it is able to make	Consistent with the view in the final Determination, complying superannuation funds could only make the election under former section 485AA of the ITAA 1936 if they had an interest in a FIF to which Part XI applied (ie they satisfied the conditions in former section 485 of ITAA 1936). This included complying superannuation funds which held interests to which Part XI applies but were entitled to the exemption in former subsection 519B(2) of the ITAA 1936.

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	an election.	
4	**Incongruous that the draft Determination relies on object of Division 830 being to address unintended consequences of FIF attribution:** The draft Determination incorrectly states that a taxpayer can only make election in paragraph 830-10(2)(b) of the ITAA 1997 on the same restrictive interpretation as for former section 485AA of the ITAA 1936 (ie that limited to Part XI Australian residents). It is incongruous that the draft Determination's interpretation of paragraph 830-10(2)(b) of the ITAA 1997 relies on the object of Division 830 of the ITAA 1997 in relation to FIF attribution given that FIF attribution is irrelevant following the repeal of the FIF rules.	The context of Division 830 as set out in the final Determination is relevant to the interpretation of subsection 830-10(2) and in particular the interpretation of the phrase 'interest in a FIF' in subsection 830-10(4). As paragraphs 12 to 13 of the final Determination provide, despite the repeal of the FIF rules, the amendments to subsection 830-10(2) of the ITAA 1997 were not intended to (and did not) broaden the scope of the election. Parliament's intention was to preserve the same conditions that applied to the election under former section 485AA of the ITAA 1936 under paragraph 830-10(2)(b) of the ITAA 1997. Accordingly, when considered in context, an election for foreign hybrid treatment is only available to partners who have an interest in a FIF to which former Part XI of the ITAA 1936 applied, being partners who are Australian residents.
5	**Election in paragraph 830-10(2)(b) not as restrictive as draft Determination states:** Paragraph 14 of the draft Determination states that the Explanatory Memorandum to the *Tax Laws Amendment (Foreign Source Income Deferral) Bill (No. 1) 2010* provides that the conditions required to make an election under paragraph 830-10(2)(b) of the ITAA 1997 are the same as the repealed section 485AA of the ITAA 1936 to ensure that the election 'would operate as intended'. This has been read out of context. The exact quote at paragraph 1.34 is: 'Amendments to sections 830-10 and 830-15 of the	The footnote to the quote at paragraph 13 of the final Determination refers to paragraph 1.34 to 1.36 of the Explanatory Memorandum to the *Tax Laws Amendment (Foreign Source Income Deferral) Bill (No. 1)* 2010. In particular, the Explanatory Memorandum continues at paragraph 1.36 to provide that: '…this schedule inserts a new election mechanism so that, going forward, taxpayers will be able to elect for hybrid treatment (that is, treatment as a partnership) despite the repeal of section 485AA. The conditions required for making this election are the same as those required under the former section 485AA.' Subsection 830-10(4) of the ITAA 1997 adopted the language

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	ITAA 1997 (which treat certain entities as foreign hybrids and therefore taxed like partnerships) are made to ensure that: • following the repeal of the section 485AA, taxpayers can continue to rely on an election made under that section (before its repeal), and can make an election under subsections 830-10(2) or 830-15(5) (subsequent to the repeal of section 485AA), and • the interaction of subsection 830-10(1) and 830-15(1) (automatic treatment of an entity as a foreign hybrid) with the new election for foreign hybrid treatment continue to operate as intended.' The above passages do not state that the new election is intended to operate the same as the old election that was available. Rather, it refers to the *interaction* of the subsection referred to with the *new* election being continued to operate as intended.	previously used in former subsection 485AA(1) of the ITAA 1936 and as a result the wording of the provisions is the same in all relevant respects. Therefore the requirements for making an election under Division 830 of the ITAA 1997 are the same.
6	**Reference to former provision not indicative that narrower interpretation intended by Parliament:** Disagree with paragraph 19 of the draft Determination, which provides that it is improbable that Parliament would use specific language from the repealed FIF rules if the intention was simply to require the partner have an interest in a 'foreign company'. As the election had historical effect, the retention of the reference to the old provision was convenient, and simply infers the object of	Disagree. It is a principle of statutory interpretation that, as a starting point, a consistent meaning should ordinarily be given to a particular term wherever it appears in a suite of statutory provisions (for example, see *Tabcorp Holdings v. Victoria* [2016] HCA 4). As provided by the final Determination at paragraphs 12 to 13, it was intended that the same conditions would be required to make the election under paragraph 830-10(2)(b) of the ITAA 1997 as under former section 485AA of the ITAA 1936.

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	allowing elections to be made survives the repeal of the FIF attribution rule.	Furthermore, as paragraphs 15 to 18 of the final Determination provide, an interpretation that promotes a role and function for paragraph 830-10(4)(a) of the ITAA 1997 is to be preferred to one that does not.
7	**Purposive approach incorrectly applied in draft Determination:** Do not agree with the draft Determination's use of a purposive approach to an interpretation of paragraph 830-10(2)(b) of the ITAA 1997 based on a presumption of what it considers 'is improbable that Parliament' would have intended. In the decision of *Commonwealth Bank of Australia (ACN 123 123 124) v. Deputy Commissioner of Taxation* [2009] FCAFC 126 at paragraph 33 the Court cautioned strongly against such an approach: '*…[I]n the face of the clearly stated, but circumscribed, legislative intent…which opens with the unequivocal declaration: 'It is the intention of the Parliament' – it is not open to this court to make assumption as to whether and if so how, the legislature would wish as well to extend… what is meant…'* Furthermore, to the extent that the Commissioner perceives there to be an anomaly by allowing foreign residents access to the election, in the decision of *ConnectEast Management Ltd v. Federal Commissioner of Taxation* [2009] FCAFC 22 at paragraph 41 Sundberg, Jessup and Middleton JJ provided that: *Resort to the odd or anomalous consequences of a particular construction of legislation is to be approached with caution. In Esso Australian Resources Ltd v. Federal*	The reasons for the conclusion at paragraph 18 of the final Determination (that it 'is improbable that Parliament would use specific language (ie 'interest in a FIF') from the repealed FIF rules if the intention was simply to require the partner have an interest in a 'foreign company'), are explained in the preceding paragraphs – the conclusion is not based on a presumption of Parliament's intent.

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	Commissioner of Taxation (1998) 83 FCR 511 at 518-519, speaking of ss 118 and 119 of the Evidence Act 1995 (Cth), Black CJ and Sundberg J said: *'In our opinion the plain language of the sections is confirmed by the only directly relevant extrinsic material, which shows that Parliament intended the consequence that is said by the appellant to be anomalous. Especially when different views can be held about whether the consequence is anomalous on the one hand or acceptable or understandable on the other, the Court should be particularly careful that arguments based on anomaly or incongruity are not allowed to obscure the real intention, and choice, of the Parliament.'* *In Ganter v. Whalland [2001] NSWSC 1101 at [36], in connection with the caution just referred to, Campbell J highlighted the risk of the court 'taking over the function of making policy choices which properly belongs to the legislature'. See also Pearce and Geddes, Statutory Interpretation in Australia (6th ed, Butterworths, 2006) at [2.36].*	
8	**Current legislation does not limit a foreign hybrid (ie treated as a partnership) from making election:** The legislation as currently drafted does not include any limitation that would preclude a limited partnership that is a foreign hybrid (ie treated as a partnership for Australian tax purposes) from electing to treat their interest in another limited partnership as an interest in a foreign hybrid. The relevant taxpayer in the context of making that election should be the Australian resident partner	Paragraph 1 of the final Determination has been amended to clarify that it will not apply: a) if the foreign resident is a CFC or was taken to be a Part XI Australian resident under former Part XI of the ITAA 1936, or b) for the purposes of calculating the net income of a partnership (which would include a foreign hybrid) or

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	in the first limited partnership. Furthermore, the legislation does not preclude a CFC from electing to treat their interest in a limited partnership as an interest in a foreign hybrid.	trust estate. By way of explanation, a note has been added to paragraph 11 referring to the fact that: • former section 485A of the ITAA 1936 ensured that the operative provision applied in calculating the net income of a partnership as if the requirement in section 90 of the ITAA 1936 was to calculate assessable income as if the taxpayer were a Part XI resident, and • the former FIF rules also applied in calculating the notional income of a CFC (based on the assumption in section 383 of the ITAA 1936 that the CFC is a taxpayer and a resident). The issue of who can make an election on behalf of a partnership is beyond the scope of this Determination.
9	**No requirement under current legislation that entity making the election has to be an Australian resident:** Prior to the repeal of the FIF provisions only an Australian resident could elect to treat an entity (FIF) as a partnership for income tax purposes. Upon repeal of the FIF provisions, the link between the requirement to be an Australian resident and the ability of electing was also repealed.	The Commissioner agrees that only Australian residents could make a foreign hybrid election prior to the repeal of the FIF provisions. Similarly, however, an election under subsection 830-10(2) of the ITAA 1997 can only be made by Australian residents. Subsection 830-10(4) of the ITAA 1997 adopted the language previously used in former subsection 485AA(1) of the ITAA 1936 and as a result the wording of the provisions is the same in all relevant respects. Therefore the requirements for making an election under Division 830 of the ITAA 1997 are the same.
10	**Words in subsection 830-10(4) of the ITAA 1997 are clear and unambiguous:**	The Commissioner has explained his interpretation at paragraphs 12 to 18, and addressed the alternative view at

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	There is no basis at law, or according to the applicable principles of statutory construction, to interpret 'a partner that has an interest in a FIF that consists of a share in the FIF' in subsection 830-10(4) of the ITAA 1997 as 'an Australian resident partner that has an interest in a FIF that consists of a share in the FIF.' With respect to the resolution of the priority issue, in the decision in *Commissioner of Taxation v. Consolidated Media Holdings Ltd 2* [2012] HCA 55 the High Court provided that the task of statutory construction must begin and end with a consideration of the statutory text. As there is no ambiguity in the words of the relevant statutory text, it is impermissible to look further than those words in order to interpret them in a different manner. If there is a perceived policy concern with the outcome, then it is the role of Parliament to consider that policy concern.	paragraphs 19 to 24 of the final Determination.
11	**Heading of former section 485AA of the ITAA 1936 not required for clarification:** It is the heading of former section 485AA of the ITAA 1936 rather than the full text of the corresponding section that makes reference to excluding the operation of Part XI attribution. Headings cannot be used to give a different effect to clear words in the section where there cannot be any doubt as to their ordinary meaning. The words in former section 485AA of the ITAA 1936, just as those in subsection 830-10(4) of the ITAA 1997, are clear and unambiguous, meaning the heading is not required for clarification.	Section 13 of the *Acts Interpretation Act 1901* provides that headings in an Act are part of the Act. It is appropriate to consider the heading of former section 485AA of the ITAA 1936 as part of the relevant context. It is also noted that the wording in the heading was consistent with the effect of making the election: the 'operative provision' did not apply to the taxpayer's interest in the limited partnership, and as a result, no income would be attributed from the FIF to the taxpayer.
12	**Paragraph 830-10(2)(b) of the ITAA 1997 should be given its ordinary and grammatical meaning:**	See response to Issue 11.

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	The general statutory interpretation rule that taxation legislation is to be given a purposive construction (as provided by section 15AA of the *Acts Interpretation Act 1901*) may be displaced where the literal meaning of the words is clear and unambiguous (see *Marsh v. Federal Commissioner of Taxation* (1985) 85 ATC 4345 and *Federal Commissioner of Taxation v. Bill Wissler (Agencies) Pty. Ltd.* (1985) 85 ATC 4626). According to the relevant prevailing principles of statutory constructions, the statutory provision will be given its ordinary and grammatical meaning, if the language of a statutory provision is clear and unambiguous, and is consistent and harmonious with the other provisions of the enactment and can be intelligibly applied to the subject matter with which it deals. The clear meaning of the test in paragraph 830-10(2)(b) of the ITAA 1997 is that the limited partner can make an election if the partner is not an 'attributable taxpayer' in relation to a limited partnership and that the draft Determination has impermissibly relied on historical considerations and extrinsic material in reaching the view that the taxpayer must be an Australian resident taxpayer.	