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Let's chat

Division 7A: Some of the lesser-known provisions – April 2026

With:

Darius Hii – Tax and estate planning lawyer; Chartered Tax Advisor; and Director at Chat Legal

Information provided is general in nature; precise application depends on specific circumstances



The deal





What doesn't work

Section 109R ITAA 1936

- “(2) A payment must not be taken into account if:
- (a) a reasonable person would conclude (having regard to all the circumstances) that, when the payment was made, the entity intended to obtain a loan or loans from the private company of a total amount similar to, or larger than, the payment; or
- (b) both of the following subparagraphs apply:
 - (i) the entity obtained, before the payment was made, a loan or loans from the private company of a total amount similar to, or larger than, the amount of the payment;
 - (ii) a reasonable person would conclude (having regard to all the circumstances) that the entity obtained the loan or loans in order to make the payment



What's excluded from 109R

- A dividend payable to the borrower by the lender
- Assessable payments for work (PAYG income) payable to the borrower
- Payment subject to voluntary withholding payable to the borrower
- Market value of property transferred to the lender company by the borrower entity less amounts paid by the company for that property
- Where Division 7A loan is subordinated to another loan or is refinanced from a 7 year to 25 year loan



The case study

Not so sneaky

- Individual borrows \$250,000 from Trading Company to repay home loan via Division 7A loan agreement during financial year ending 30 June 2024
- MYR of \$50,000 required prior to the end of the following financial year
- Individual deposits \$50,000 just before end of 30 June 2025
- Individual subsequently borrows \$50,000 on 2 July 2025

Trying to be sneaky

- Individual extends the period of the arrangement (e.g. repaying in early June and borrowing in mid August) – still captured
- Identified by Board of Taxation in 2012
- *Building Company Owner v FCT* [2012] AATA 755 where reborrowing occurred within 14 days



Repayment by set-off

- Liabilities must exist at time
- Liabilities should be supported by contemporaneous evidence (i.e. dividend statements and offset agreements)
- Where tri-party arrangements are in place – then additional documentation required (i.e. trustee resolutions as well)
- ATO noting *'a journal entry, without other supporting evidence and contemporaneous action, won't be effective to offset a minimum yearly repayment obligation'*
- Backdating not an appropriate strategy



Interposed entity loans

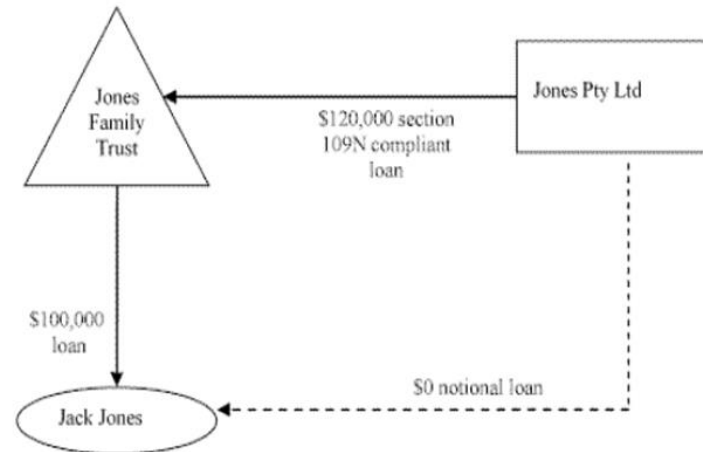
- Section 109T designed to ensure Division 7A applies to loans made by a company through interposed entities
- 'Reasonable person' would conclude that the private company made the payment or loan solely or mainly as part of an arrangement involving a payment or loan to the target entity
- Consider Trading Company loan to Dormant Company (with no Distributable Surplus) who then lends to target individual/trust
- Does not apply if target entity is a company (TD 2001/2) and where payment or loan deemed to be a dividend due to Division 7A



Example

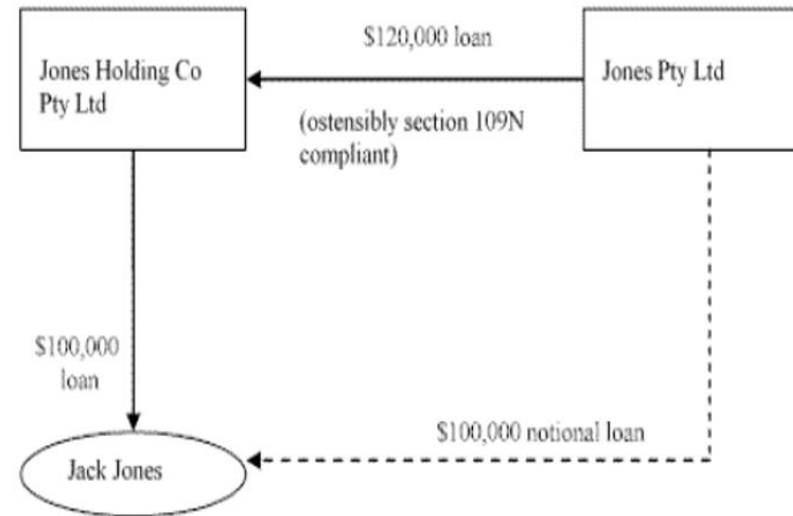
11. For the purposes of determining the amount of the notional loan under subsection 109W(1) the Commissioner will have regard to the fact the loan between Jones Pty Ltd and Jones Holding Co Pty Ltd as trustee for the Jones Family Trust complies with section 109N. As such the amount that would otherwise have been the amount of the notional loan, for section 109W purposes, will be reduced by \$100,000 and resulting in a notional loan with a value of nil (see Diagram 3).

Diagram 3





Example



109T and commercial transactions

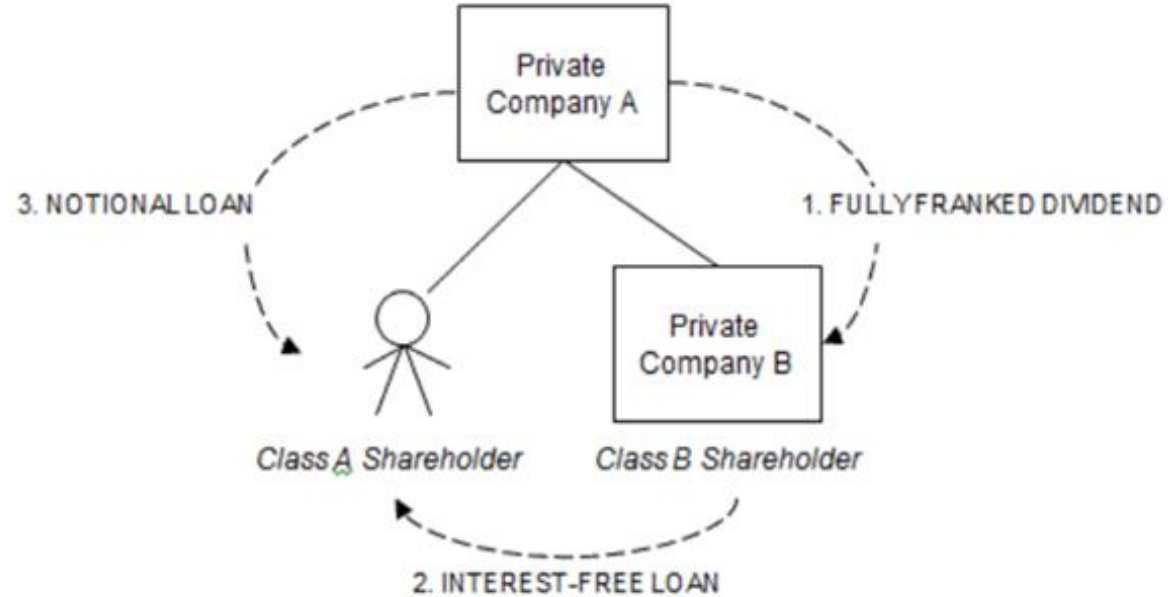


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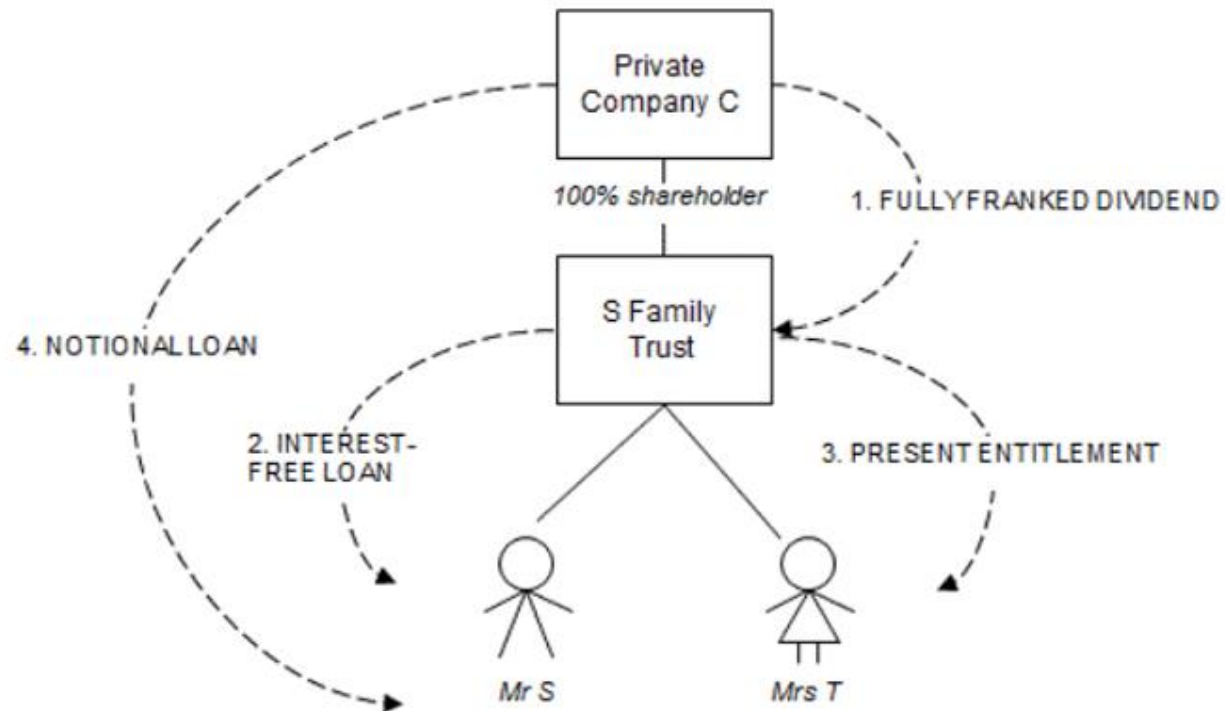
- Trading Company invest in unrelated Unit Trust. Units issued at market value, however, Unit Trust made loans back to trading Company (not compliance with Section 109N).
- TR 2018/13 – 109T can apply where transaction to interposed entity is a commercial transaction
- [78]....*Division 7A could be overcome by private company subscribing for an equity interest in another entity (for example, units in a unit trust...)*
- Notional loan amount factors in overall tax payable (item 5 of Compendium to TD 2018/13)



Example

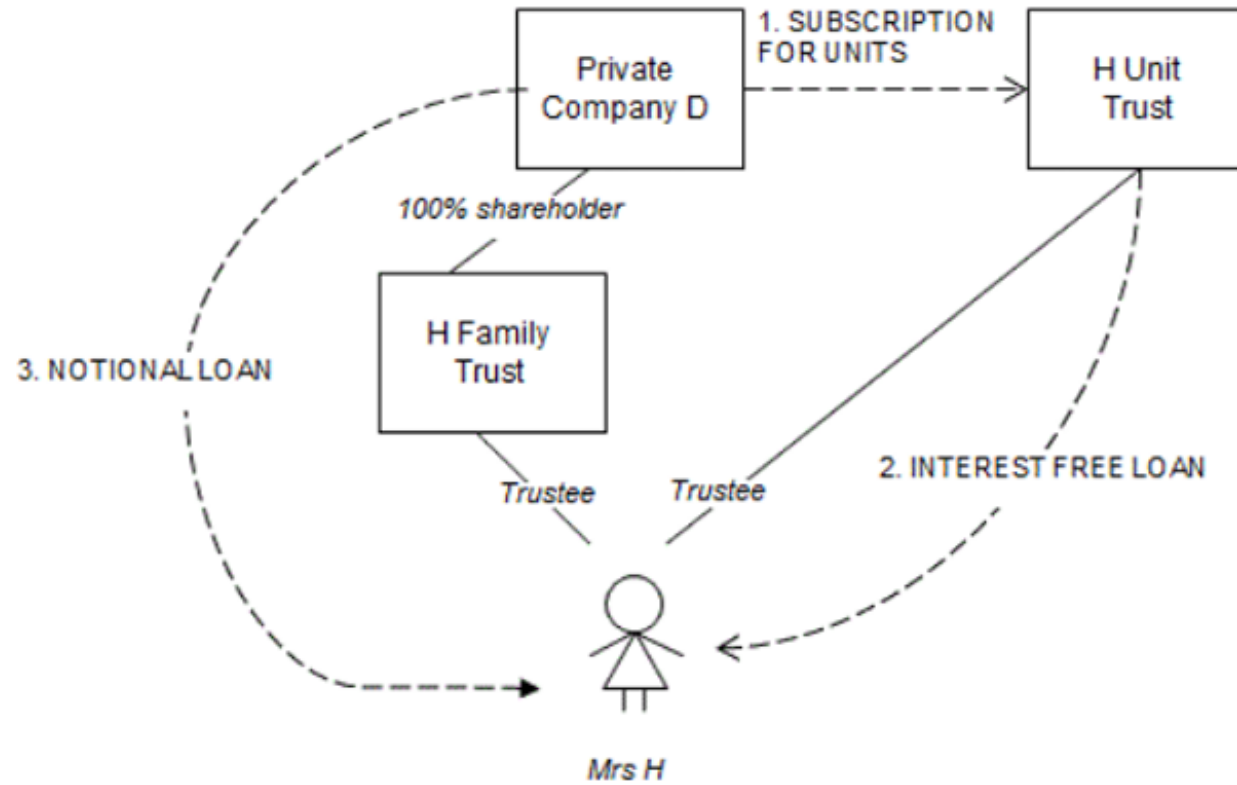


Example – non-resident beneficiaries



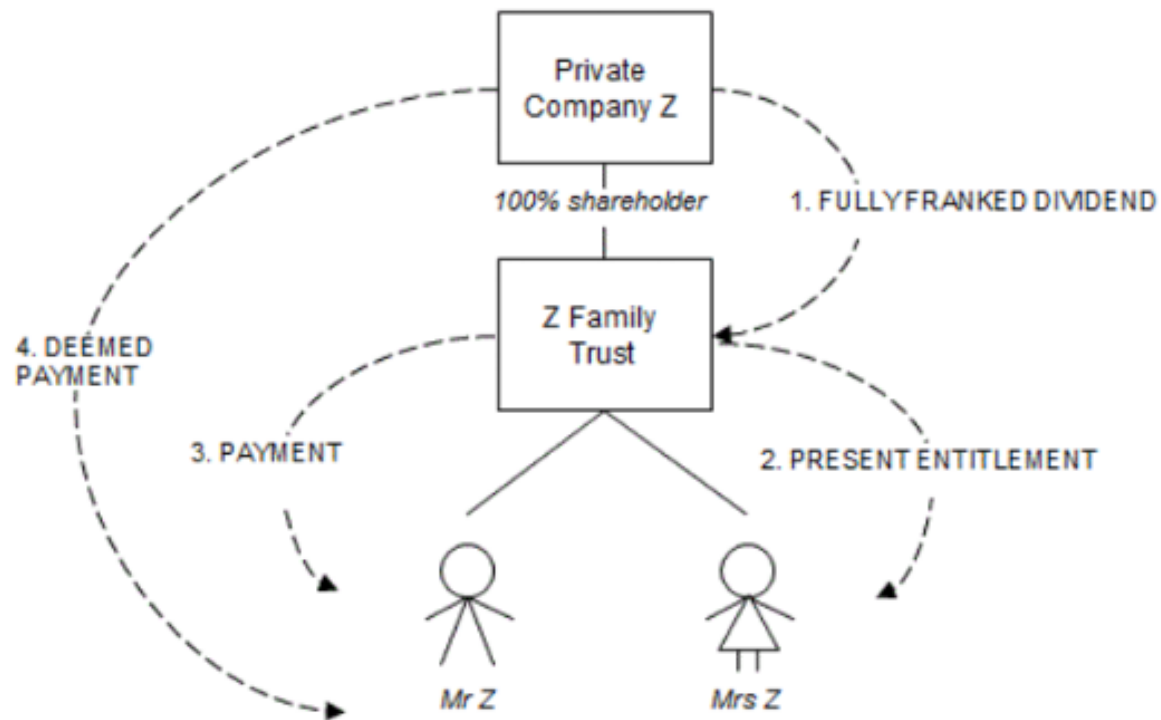


Example



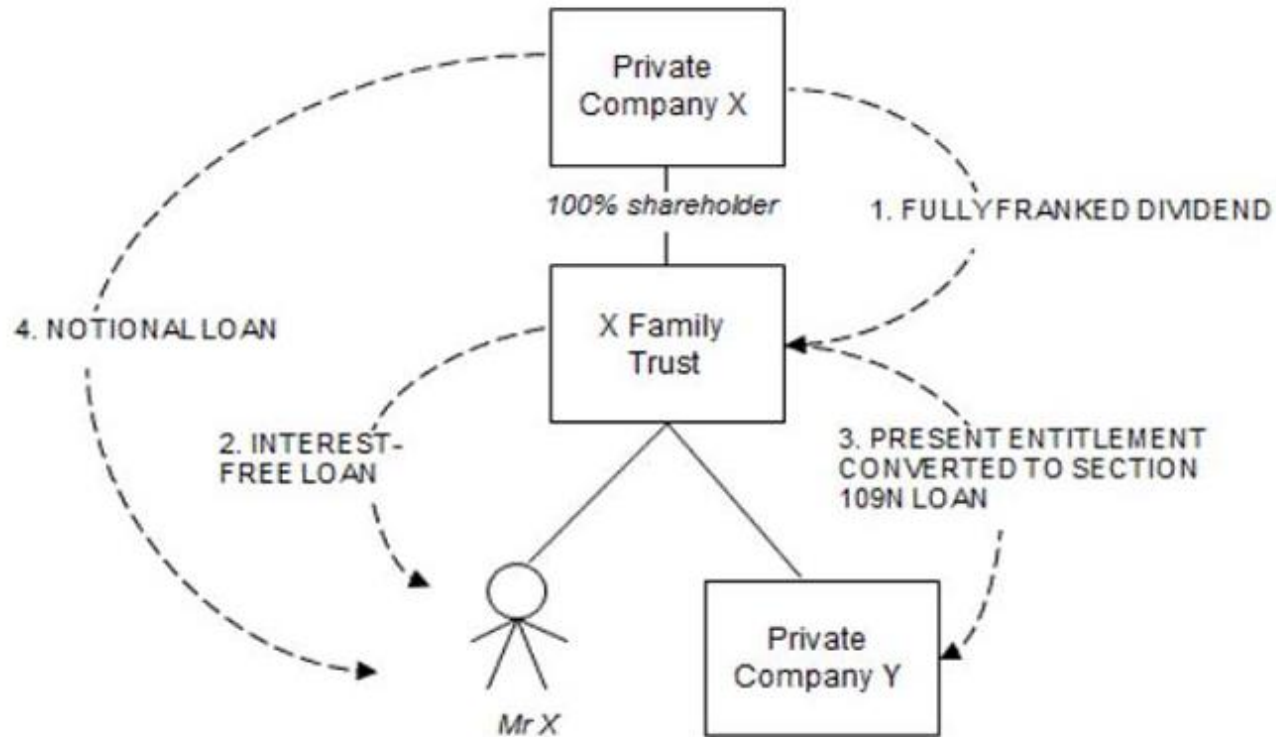


Example



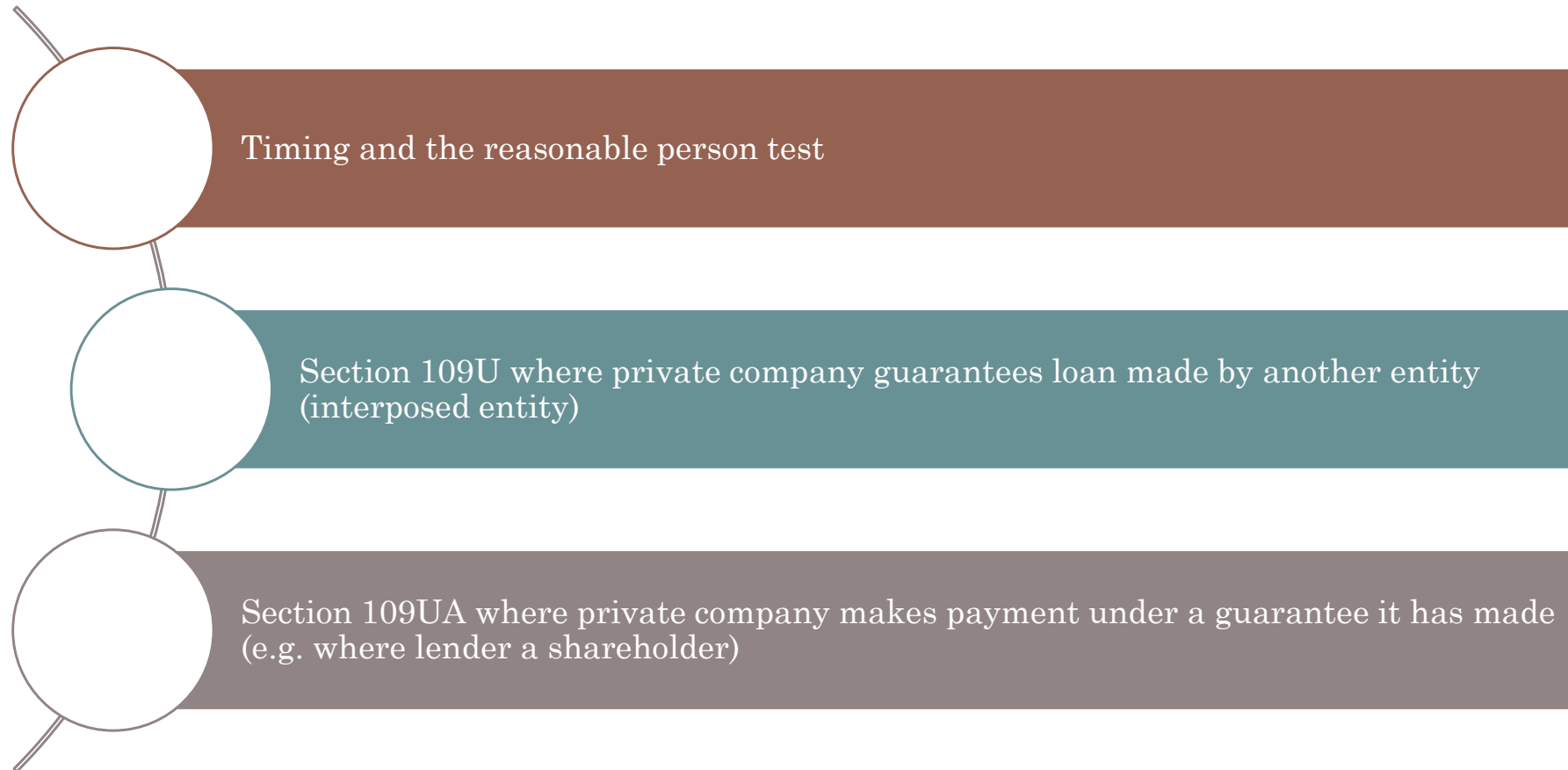


Example



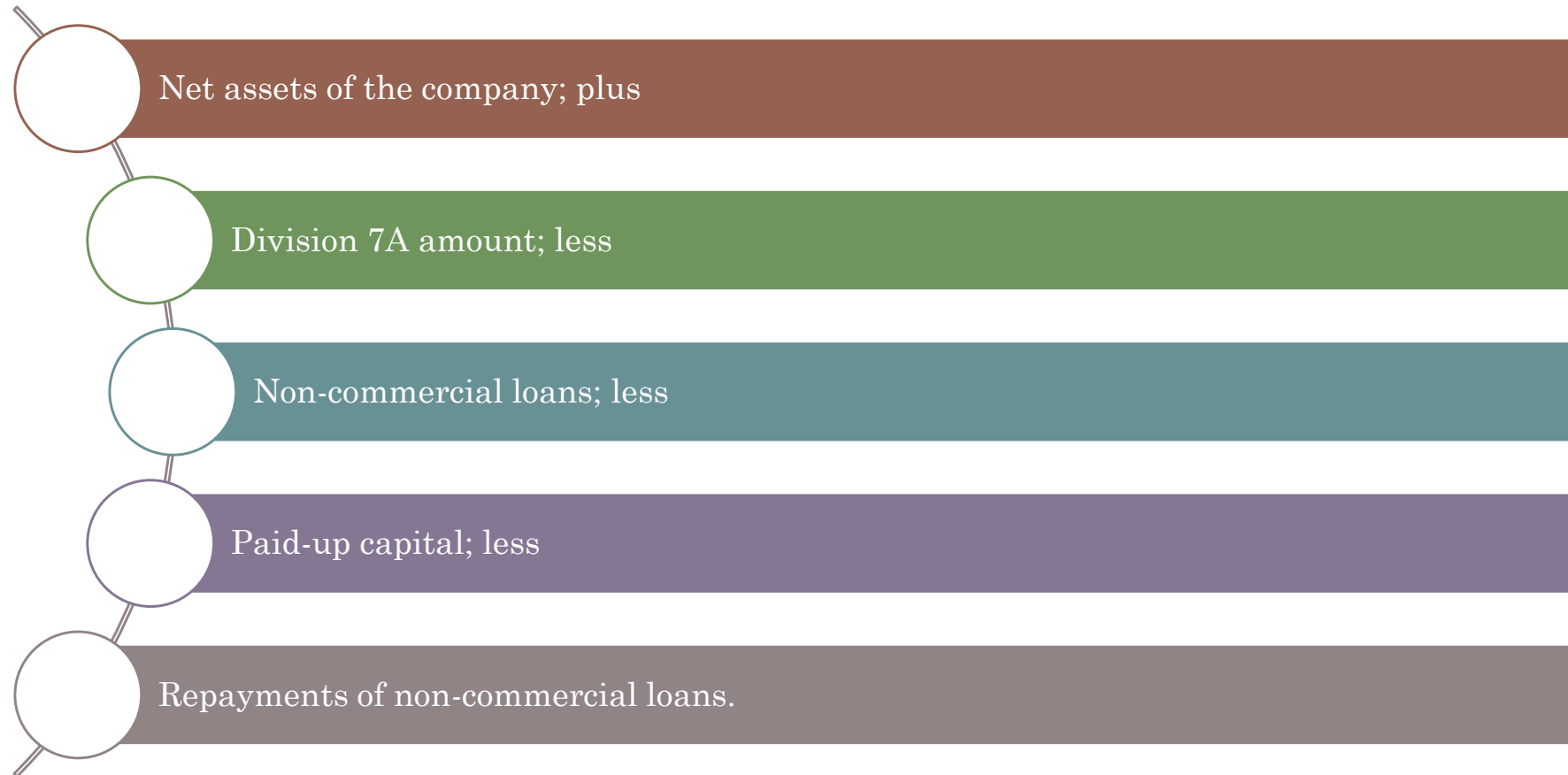


Interposed entity loans



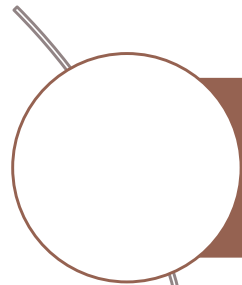


Distributable Surplus – 109Y

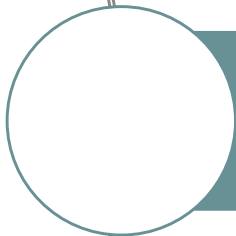




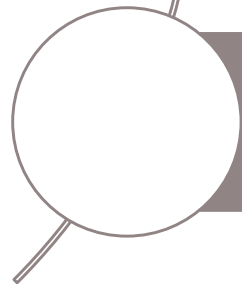
Net assets



Book value of the assets of the company exceeding the sum of



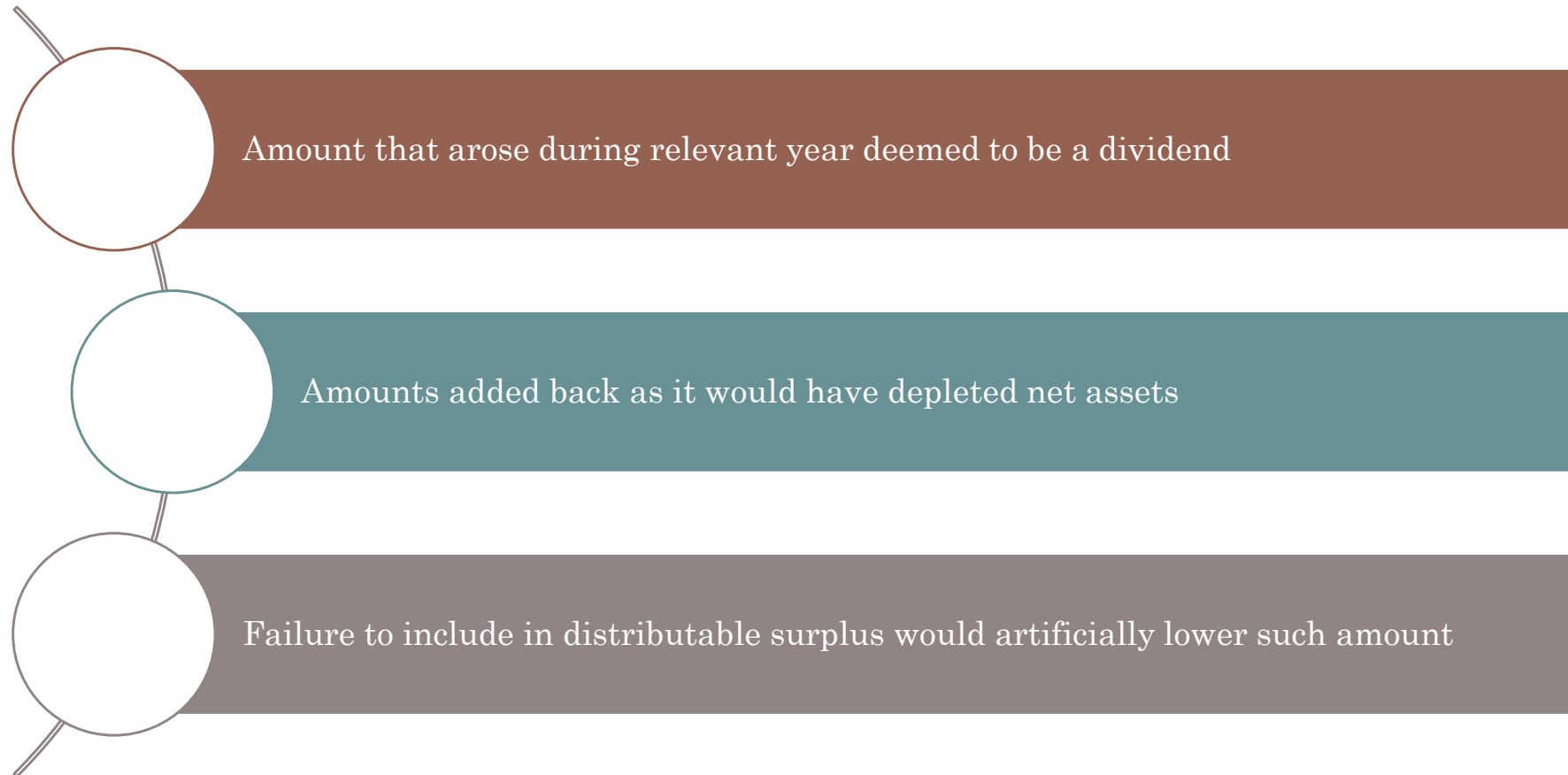
Present legal obligations owed to entities and provisions for depreciation (e.g. leave and amortisation of intellectual property)



Net assets cannot be less than nil

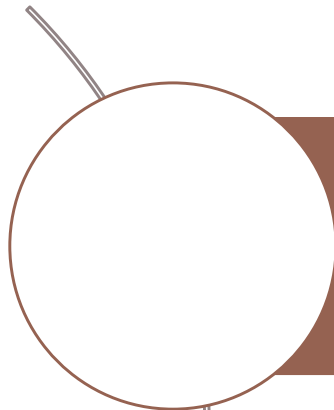


Division 7A amounts

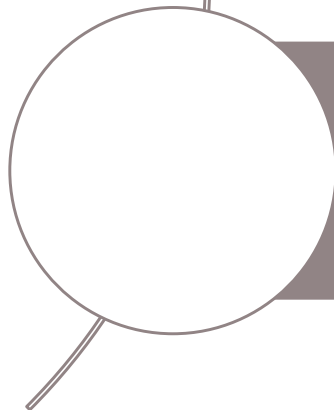




Non-Commercial loans



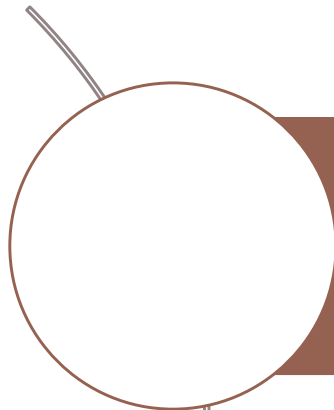
Includes prior year Division 7A loans



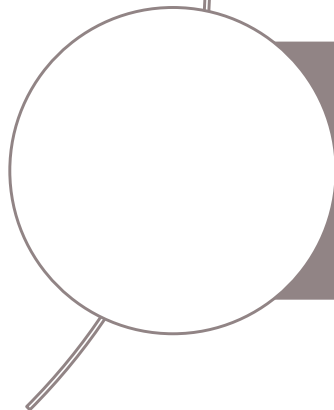
Also other non-commercial loans (including those without complying loan agreement)



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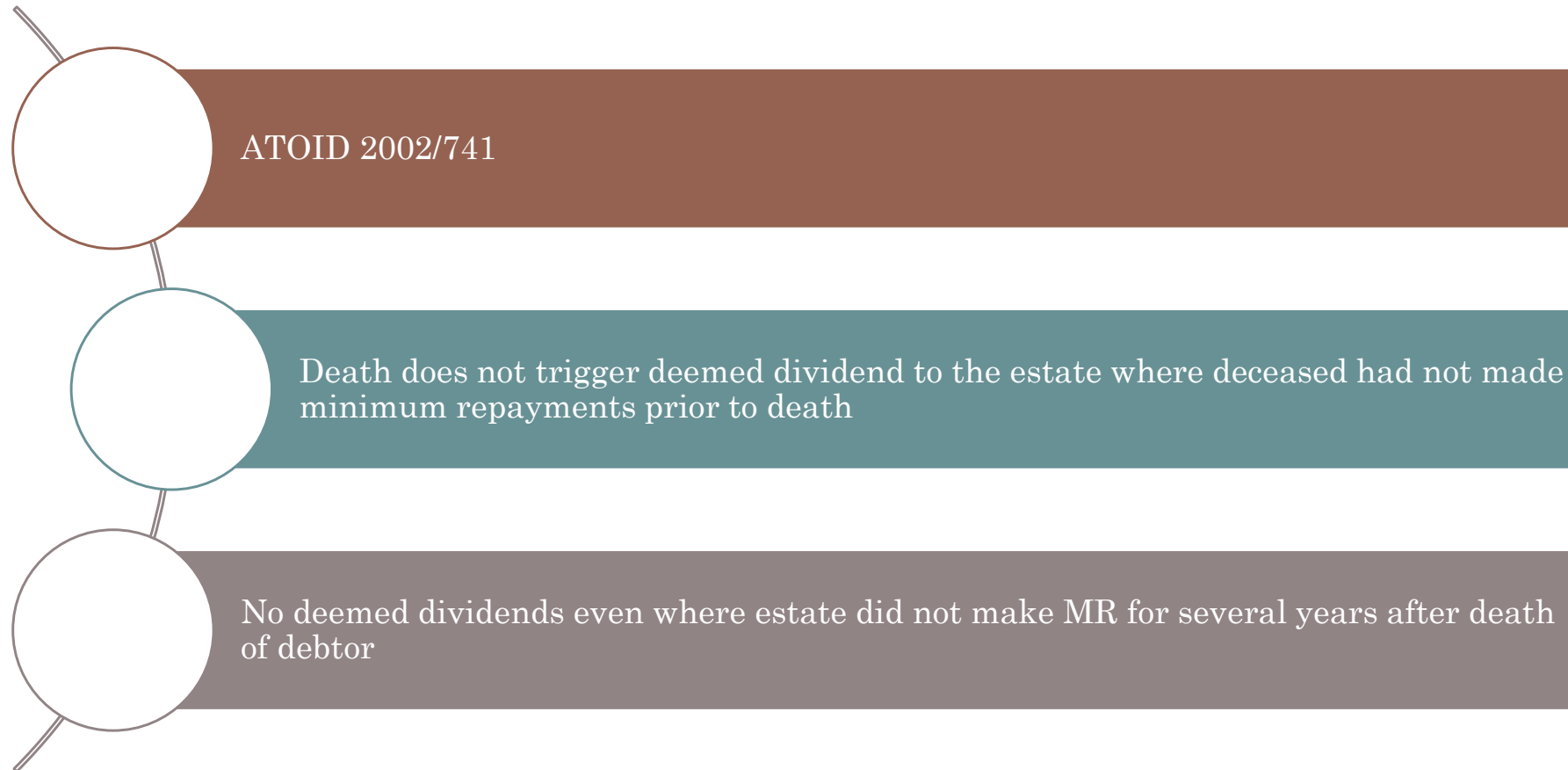


Out of time deemed dividends

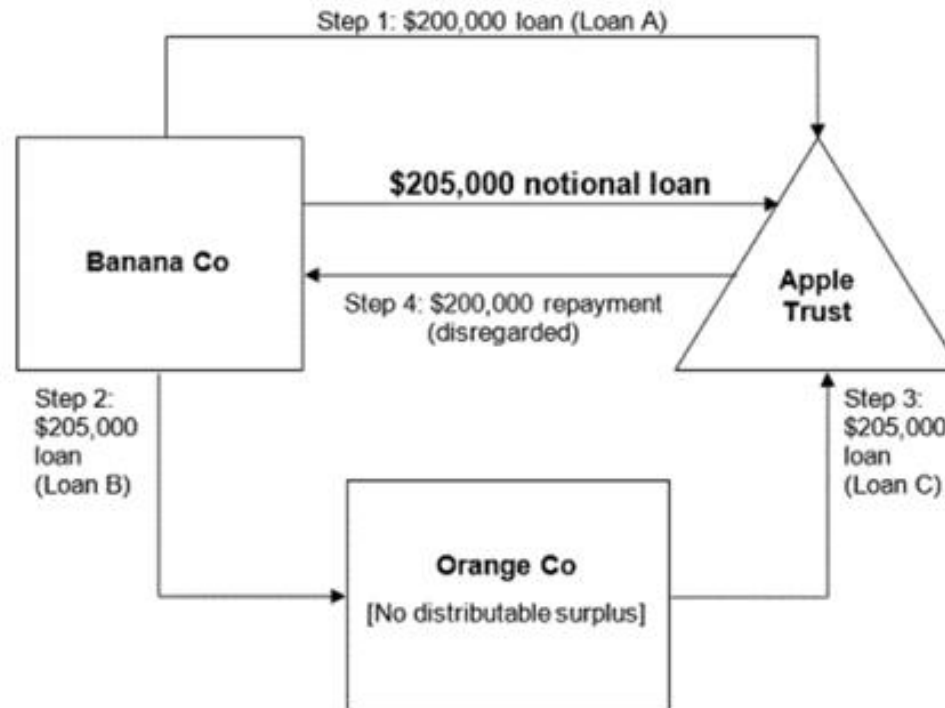
- What do you do if outside the 4-year amendment period
- Not advocating to put head in sand
- But genuine circumstances: (a) repay loan; or (b) forgive the loan
- Exemption of forgiveness of a loan from a deemed dividend
- FBT or commercial debt forgiveness rules (?)



Death of the Borrower and MYR



TD 2025/5 – 109R and notional loans

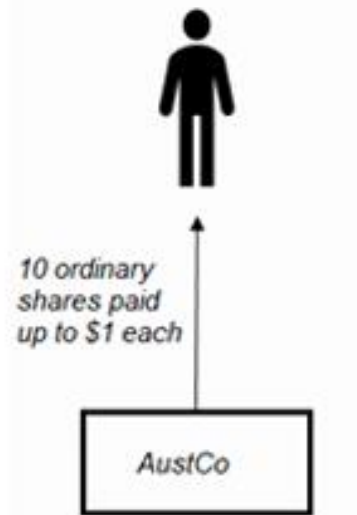




TA 2023/1

Pre-interposition

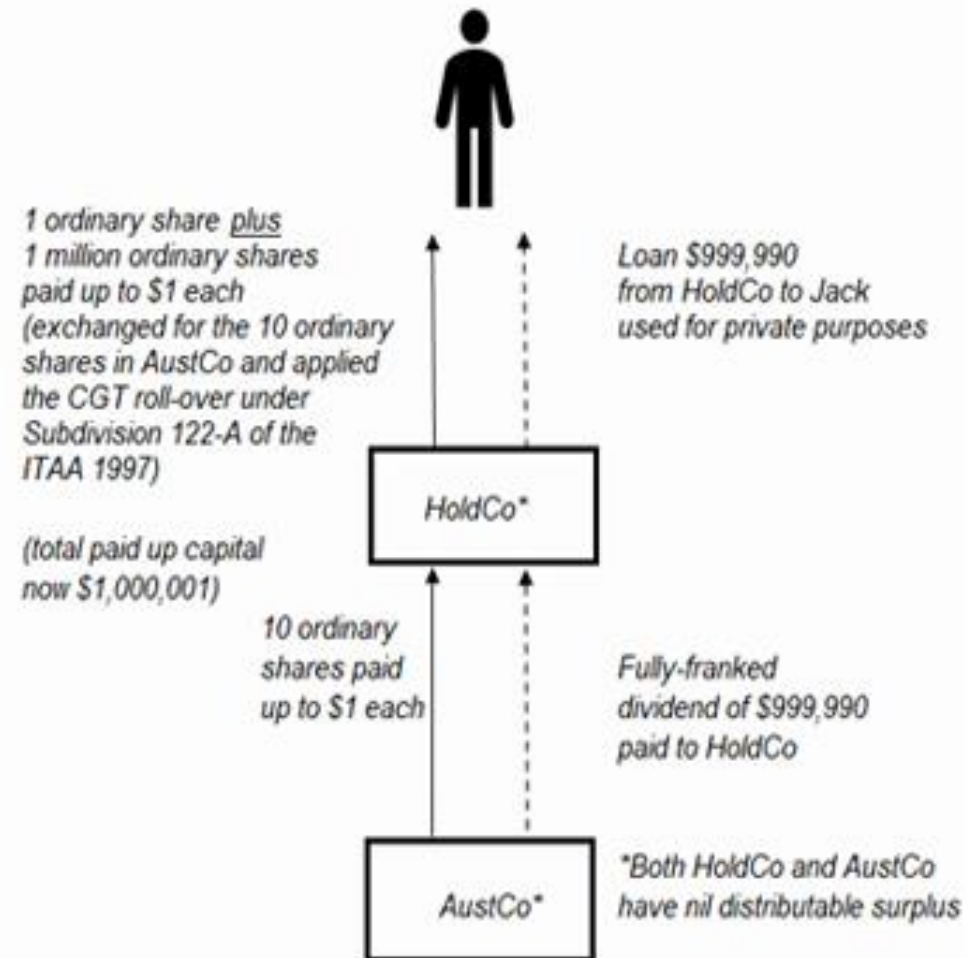
Jack (sole director and shareholder)



Retained profits of \$999,990
Cash at bank \$1,000,000

Post-interposition

Jack (sole director and shareholder)



1 ordinary share plus
1 million ordinary shares
paid up to \$1 each
(exchanged for the 10 ordinary
shares in AustCo and applied
the CGT roll-over under
Subdivision 122-A of the
ITAA 1997)

(total paid up capital
now \$1,000,001)

Loan \$999,990
from HoldCo to Jack
used for private purposes

10 ordinary
shares paid
up to \$1 each

Fully-franked
dividend of \$999,990
paid to HoldCo

*Both HoldCo and AustCo
have nil distributable surplus



Bendel

- Where Trust distributes to a company and leaves present entitlement unpaid
- Does not end all of the Division 7A issues
- Subdivision EA still applies
- Practical thoughts
- The one scenario where taxpayers 'win' with Bendel (assuming no further changes)

Contact details

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