



## ATO Interpretative Decision


ATO ID 2005/23

### Income Tax

### Research and Development Tax Offset: legal ownership of interests in a company by an exempt entity

FOI status: may be released

Status of this decision: Decision Current

 **CAUTION:** This is an edited and summarised record of a Tax Office decision. This record is not published as a form of advice. It is being made available for your inspection to meet FOI requirements, because it may be used by an officer in making another decision.

#### **This ATOID provides you with the following level of protection:**

If you reasonably apply this decision in good faith to your own circumstances (which are not materially different from those described in the decision), and the decision is later found to be incorrect you will not be liable to pay any penalty or interest. However, you will be required to pay any underpaid tax (or repay any over-claimed credit, grant or benefit), provided the time limits under the law allow it. If you do intend to apply this decision to your own circumstances, you will need to ensure that the relevant provisions referred to in the decision have not been amended or repealed. You may wish to obtain further advice from the Tax Office or from a professional adviser.

## Issue

Does an exempt entity legally own interests in a company within the meaning of subsection 73J(2) of the *Income Tax Assessment Act 1936* (ITAA 1936), where the *Corporations Act 2001* requirements for membership of a company have not been met?

## Decision

No. The exception in subsection 73J(2) of the ITAA 1936 will not operate to preclude a company from choosing a tax offset under section 73I of the ITAA 1936 where the exempt entity is not a member of the company under the Corporations Act.

## Facts

Section 231 of the Corporations Act states that a person is a member of a company if they are a member of the company on its registration.

Under section 120 of the Corporations Act, a person becomes a member of a company on registration if the person is specified in the application with their consent as a proposed member of the company.

Section 175 of the Corporations Act, provides that a register of members kept under section 168 of the Corporations Act, is only evidence of the matters contained in it, in the absence of evidence to the contrary.

On the company's Application for registration as an Australian company, lodged with the Australian Securities and Investment Commission (ASIC), an exempt entity was included as member of the company, with an interest totalling more than 25% of shares in the company.

The exempt entity was also recorded as a member of the company in its register of members kept under the Corporations Act.

The company is an eligible company within the definition in subsection 73B(1) of the ITAA 1936. It incurred research and development expenditure during the year of income and satisfied the eligibility requirements of subsection 73J(1) of the ITAA 1936.

The exempt entity had not at any time consented to become a member of the company, and nor had it authorised any payment from its own funds as consideration for the shares registered in its name.

## Reasons for Decision

Section 73J of the ITAA 1936 provides that an eligible company will be eligible to choose a tax offset instead of a deduction for research and development expenditure if it satisfies the requirements of subsection 73J(1) of the ITAA 1936.

However, even though the requirements of subsection 73J(1) of the ITAA 1936 may be satisfied, subsection 73J(2) of the ITAA 1936 prevents an eligible company from choosing the tax offset for the relevant year, if an exempt entity, the affiliates of an exempt entity, an exempt entity together with its affiliates, or two or more exempt entities, at any time during the tax offset year, legally or beneficially own, or have the right to acquire, the legal or beneficial ownership of:

- (a) interests in the company that carry between them the right to exercise or control the exercise of, at least 25% of the voting power in the company; or
- (b) interests in the company that carry between them the right to receive at least 25% of any distribution of income or capital by the company.

For the purpose of subsection 73J(2) of the ITAA 1936, 'interest' is used in the ordinary sense to denote 'a legal concern, title or right (in property)'. To fall within the exception, the relevant entity or entities must 'legally or beneficially own . . .' the prescribed interests. In this case those interests are the shares in the eligible company.

Legal owners of shares in a company are referred to as 'members' under the Corporations Act. Under section 231 of the Corporations Act, a person is member of a company if they are a member of the company on its registration.

Section 120 of the Corporations Act provides that a person becomes a member of a company on registration if the person is specified in the application **with their consent** as a proposed member of the company. (emphasis added)

Under section 176 of the Corporations Act, in the absence of evidence to the contrary, a register kept under section 168 of the Corporations Act, is proof of the matters shown in the register.

The exempt entity was specified in the company's Application for registration as a member holding more than the 25% stipulated by subsection 73J(2) of the ITAA 1936. The contemporaneous register of members also shows the exempt entity as the legal owner of more than 25% of shares in the company.

However, the exempt entity had not consented to become a member of the company. Therefore, sections 231 and 120 of the Corporations Act did not operate to make the exempt entity a member of the company upon registration.

Therefore, at the relevant times, the exempt entity did not legally own a relevant interest in the company for the purposes of subsection 73J(2) of the ITAA 1936.

On the facts there is also no basis on which to conclude that any exempt entity beneficially owned any such relevant interests.

Subsection 73J(2) of the ITAA 1936 therefore, does not preclude the eligible company from claiming the research and development tax offset.

**Date of decision:** 17 December 2004

**Year of income:** Year ended 30 June 2004

**Legislative References:**

*Income Tax Assessment Act 1936*

section 73I

section 73J

*Corporations Act 2001*

section 231

section 168

section 169

section 120

section 117

section 175

section 176

**Keywords**

Deductions & expenses

Research & development expenses

R&D tax offset

**Date of publication:** 21 January 2005

**ISSN:** 1445-2782

---

**Copyright notice**

© Australian Taxation Office for the Commonwealth of Australia

You are free to copy, adapt, modify, transmit and distribute material on this website as you wish (but not in any way that suggests the ATO or the Commonwealth endorses you or any of your services or products).

---