



Law Council  
OF AUSTRALIA

*Business Law Section*

Mr Peter Maher  
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Australian Taxation Office  
**Via email:** [peter.maher@ato.gov.au](mailto:peter.maher@ato.gov.au)

29 October 2015

Dear Peter,

### **Guidance paper: Negative Control and the application of Division 6C**

We refer to your email to Carol O'Sullivan of 3 September 2015 providing a draft of the above Guidance Paper, inviting comments or feedback.

We understand that the Guidance Paper is being prepared because "the issue of when a 'power of veto' can constitute 'negative control' for the purposes of section 102N of Division 6C of the [*Income Tax Assessment Act 1936*] was commonly raised as an area of uncertainty."

In our discussions on 19 March 2015, you further suggested that by resolving such uncertainty, it would reduce the need for parties involved in privatisation activity and infrastructure investment to seek rulings on these matters. To this extent, we understand it is consistent with the approach of the Australian Taxation Office (**ATO**) to give guidance to taxpayers to help them "swim between the flags".<sup>1</sup>

As a general observation, if our understanding of the purpose of the document is correct, then we are not certain that it will achieve its objective in its current form. This is because the language used throughout the document is hesitant, ie. "likely", "possibly", "depend[ing] on the particular facts of the arrangement", "depending on the materiality and threshold".

We appreciate the difficulties that the ATO faces in being more definitive, however question the value of the Guidance Paper if the purpose cannot be achieved.

If the Guidance Paper is to achieve the above purpose, we consider it needs to provide more certainty as to the ATO's views of particular arrangements or, at the minimum, the

<sup>1</sup> See <https://www.ato.gov.au/printfriendly.aspx?url=/General/Consultation/In-detail/Consultation-steering-group---minutes/Consultation-Steering-Group-meeting-minutes-15-August-2014/>

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circumstances where the ATO will definitively not take any active compliance. This kind of approach has been taken in other ATO guidance material.<sup>2</sup>

We also think the Guidance Paper could be enhanced by elaborating on the following matters:

- On page 12, the ATO acknowledges that the ability to control has to be more than a remote or hypothetical possibility. We consider that the inherent friction between the commercial realities of a minority, passive investor needing to have mechanisms in place to protect their investment (which you may argue are 'control' mechanisms) and the integrity concerns that Division 6C is seeking to address (including the "contrived arrangements" referred to on page 13) can be better addressed in Appendix 2 by acknowledging the unique nature of infrastructure projects. By way of example, Appendix 2 refers to vetoes over the management/business plans and annual budgets as well as entry into business contracts as two vetoes which would "likely" result in negative control. However, the nature of infrastructure projects and the underlying business in the infrastructure project is such that the budget is very unlikely to be materially changed from year to year and the veto is practically required to prevent any radical departure from the business into which the veto holder invested. It is submitted that this veto would consequently not be contrived and would be highly unlikely to be exercised given the nature of the business. There does not appear to be any consideration of these vetoes in the context of the industry. We recommend that the vetoes in the Guidance Material should be amended to take account of the nature of the infrastructure business – both in terms of the analysis included and the outcome on their 'ratings' (which we submit in relation to at least the third and fourth of the "likely" vetoes, should be changed).
- On page 13, the ATO “acknowledges that in cases where there are shared negative control rights between unrelated investors, there may be more of a presumption that such rights are in the nature of protective minority interest holder rights rather than the type of control rights to which [paragraph 102N(1)(b)] was directed”. It would greatly assist if the ATO were to elaborate on the facts and circumstances in which the ATO would accept this is the case.
- On pages 17 and 18, a number of control clauses are identified which are “likely” to give rise to negative control. Many of these include a dollar amount or percentage in square brackets. It is not clear whether the references to percentages and to dollar values means that if the veto existed but the thresholds were substantially higher, that the Commissioner would not consider that negative control would be "likely". This should be clarified.
- In the preamble in Appendix 2, it would assist if the ATO makes it clear whether each type of control clause is considered individually (eg. if you have control over the appointment and removal of the CEO, then negative control will be found to exist) or whether they will be looked at in combination (eg. negative control would exist if you had control over the CEO's appointment and removal as well as approval of budgets and one or more other veto rights).

We hope that these comments are constructive, and we would be happy to meet with you and Louise Andolfatto to discuss them in further detail, if that would be helpful.

For the avoidance of doubt, nothing in this letter should be taken as conceding that “negative control” amounts to “control” for the purposes of section 102N of the *Income Tax Assessment Act 1936*.

If you have any questions, in the first instance please contact Adrian Varrasso, Chair of the Taxation Committee of the Business Law Section of the Law Council of Australia.

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<sup>2</sup> See, for example, <https://www.ato.gov.au/business/starting-your-own-business/in-detail/professional-firms/assessing-the-risk--allocation-of-profits-within-professional-firms/>.

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Yours sincerely

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

**John Keeves, Chairman**  
Business Law Section