ATLASSIAN

Mark Reading <mreading@atlassian.com>

FW: [redacted] (Pledge 1% Gift) - our preliminary position [SEC=OFFICIAL:Sensitive, ACCESS=Legislative-Secrecy]

[redacted] com.au> Mon, May 9, 2022 at 3:49 PM
To: Mark Reading <mreading@atlassian.com>
Cc: [redacted] com>, [redacted] com>

Mark, [redacted] and [redacted]

I hope you are all well. Please see the email below from the ATO. This is becoming quite a saga.

The good news is that the ATO have quite a bit of sympathy for the arguments I put to them in my last email. However the bad news is that they are effectively now saying that they don't think they can issue a ruling without knowing the relationship, discussions and negotiations between the company and the relevant charity. So while we might be able to get a particular scenario across the line, I think each company wanting to use the structure would also be required to seek a ruling, and it would not be "rubber-stamped" – rather each company would need to convince the ATO about the concerns they have expressed below.

[redacted] – your point about the shareholders agreement was well made, and to the extent possible it would make sense for the charity not to sign it – it may be that the protections in the constitution are enough to not require the charity to sign the shareholders agreement.

To be honest, I am not quite sure where we go from here. I would be happy to jump on a call with you if that made sense.

Regards

[redacted]

From: [redacted] @ato.gov.au>
Sent: Monday, 9 May 2022 12:07 PM
To: [redacted] com.au>
Cc: [redacted] @ato.gov.au>
Subject: RE: [redacted] (Pledge 1% Gift) - our preliminary position [SEC=OFFICIAL:Sensitive, ACCESS=Legislative-Secrecy]

[EXTERNAL]

H[redacted]

We've considered your extra comments.

While you've made some good points, we don't think the scenario is precise enough for us to rule on the exact consequences for a value shift. We're not confident we could rule favourably (ie, no value shifting consequences), because of the risks we've discussed below. The client will need to assess those risks if it seeks a revised ruling or self-assesses on a similar arrangement.

We'll respond to a few of your comments.

Value shift for a cash donation before cash subscription

You asked:

> *Just so I am clear – I think the effect of what you are saying is that even if, for example, the company made a cash donation to the charity and subsequently the charity subscribed for shares in an equal amount, and paid cash for the shares, your view would still be that value shifting would apply?*

We think the answer is still **yes,** there would be a value shift. It could depend on the circumstances, but we think shares would most likely be issued at a discount. We'll briefly explain our thinking:

As an aside, we realise that if the company and the charity did go through the 'form and ceremony' of handing money back and forth, the set-off question wouldn't be directly relevant.

- Section 725-150 says equity interests are issued at a discount if the market value exceeds the amount of the **payment** the issuing entity receives. 'Payment' or 'pay' would usually mean giving something (usually money) to discharge a debt or obligation.
- We can see a *theoretical* possibility that there'd be no discount if the charity made a genuine independent decision to subscribe for shares. That would be the outcome if the donation and the cash payment were properly characterised as separate, independent transactions.
- But we don't think that's the proper characterisation. We think the company and the charity would come to some agreement or understanding that the charity would only use the money to subscribe for shares. If there wasn't, we think an independent charity acting at arm's length would apply the cash to charitable purposes, rather than invest in a private company.
- Therefore, we don't think the two transactions (cash donation and subsequent share subscription) can be looked at separately. The two transactions are linked. It's really one transaction to issue shares to a charity for no 'net' payment.

Active participant

We think you've made some good arguments about 'active participant'. We understand your point that a merely passive recipient of shares shouldn't be an active participant. Thanks for drawing our attention back to the EM: we overlooked some paragraphs which support that view.

However, we still think there's significant risk that a charity would be an active participant under this scenario.

1. We still think it's arguable that entering a shareholders agreement is enough to be at least 'directly facilitating' a scheme. It's a positive act which might be enough to take it out of the 'passive recipient' category. If it's a question of fact whether a participant is an active participant (see EM paragraph 11.119), it could depend on the terms of that shareholders agreement. Some shareholders agreements might be a meaningless formality, but others might limit the shareholder's freedom or impose positive obligations.
2. In practice, we think the scenario could only happen where the charity has been involved in discussions and planning. The charity wouldn't subscribe for shares without some sort of side agreement or arrangement, reached after discussion and negotiation. We think those discussions would be relevant to determining whether the charity is an 'active' participant. For example, if the charity agreed to subscribe after receiving some assurance that the company would shortly have an IPO or sell, that might be enough.
3. If the charity is connected to the pledge 1% movement, we think it would be even more likely to be an active participant. The EM at paragraph 11.126 notes that encouraging, counselling or pressure might be 'active participation.' Promoting, affiliating itself with, or asking companies to join the pledge 1% movement might be enough to qualify.

None of that's to say that the charity would necessarily be an active participant: rather, we see significant risk and uncertainty. The outcome could turn on very fine details. For example:

- the identity of the charitable recipient
- any connections the charity had to the company, shareholders, or the pledge 1% movement
- the circumstances and timing of the donation and the share subscription
- whether the donation was contingent (formally or practically) on the charity subscribing
- any discussions between the parties, including any informal understandings or assurances (whether direct or through intermediaries).

We doubt we could rule on the 'active participation' question without more information about those things.

We'll briefly address some of your specific points:

- *Simply accepting a gift can't be enough to be an active participant.*

That seems like a sound argument, noting the EM's comment about a 'fortuitous recipient'. Accepting shares alone probably isn't enough, not much different to cashing a cheque. But signing a shareholder deed is more of a positive step – see our earlier comments.

- *The deed's unilateral, the charity isn't participating in that part of the scheme.*

While entering the deed is unilateral, the scheme would include any later discussions with the charity. We think there'd need to be at least some consultation before the charity agreed to subscribe and sign the deed. Would the company make a cash donation without receiving any assurance or commitment (from the charity) on that point?

- *Our reference to 'facilitation through omission' isn't relevant here.*

We were just making the point that 'direct facilitation' is a broad concept and the threshold might be low. For example, we think it's a relevant factor that the scheme couldn't happen if the charity wasn't prepared to sign the shareholder deed. Perhaps that's a bit like failing to exercise a veto power? But that point isn't central to our thinking.

Other comments

There might be other variables and issues apart from the 'discount' and 'active participant' issues. We've thought about two, but there might be more.

- *Market value*

Whether there's any significant decrease in market value for the 'diluted' original shares. Here we understand the original shareholders will retain 99% control. Arguably, that could be relevant when determining market value. However, there's some controversy about whether (and if so, to what extent) control premiums or discounts should be allowed when determining market value. (See the *Miley* case.)

- *The associate issue*

As you've noted, even if the charitable recipient wasn't an 'active participant,' it could still be an affected owner (of up interests) if it was an associate of the controller. The client would need to determine that once it has identified a charitable recipient.

Thanks,

[redacted]
Private Wealth |Technical Leadership & Advice
Australian Taxation Office
P 07[redacted] | M [redacted]

From: [redacted]pdm.au>
Sent: Wednesday, 4 May 2022 2:36 PM
To: [redacted]@ato.gov.au>
Cc: [redacted]@ato.gov.au>
Subject: RE: [redacted] (Pledge 1% Gift) - our preliminary position [SEC=OFFICIAL:Sensitive, ACCESS=Legislative-Secrecy]

EXTERNAL EMAIL: EXERCISE CAUTION

H[redacted]

Thanks for your note – I appreciate your input.

I have made some comments in your email below in **CAPITALS**.

I was also just having another look at your letter, particularly regarding the "active participant" aspect.

I think where I get to overall is that I am not convinced the charity would be an active participant, even given the terms of the EM. The deed is unilateral (i.e. the charity is not party to it) and accordingly it cannot be said that the charity is an active participant in that part of the scheme.

You make a reference to facilitation through omission – I agree that, hypothetically, an entity can facilitate through omission (e.g. failing to exercise a veto power etc – see example 11.10 in the EM), however I am not sure that is relevant here. Until the charity becomes a shareholder, it has no role to play at all. In making the comment about omission, did you have some particular issue in mind?

I also find it a little hard to accept that merely accepting the shares and signing the shareholders agreement makes the charity's involvement more than passive. As the EM notes at 1.127, the policy of the law is to apply the value shifting provisions because it cannot be said that the entity is merely a fortuitous recipient of the benefits of the value shift. See also 1.129. If the position were otherwise, then it would not be possible to have a situation where a recipient shareholder was not an active participant.

Here, the company is making a unilateral decision to make a donation to the charity, albeit satisfying the donation by issuing shares. The charity plays no part in that decision, and nor can it – it cannot be aware of the existence of the decision to donate (i.e. to enter into the deed) until the decision is made. I accept that the charity must accept the shares and sign the shareholders agreement, but that is really no different from, for example, a charity cashing a cheque for a donation. Surely the fact that the charity must accept the gift in order to perfect it is not sufficient for it to become an active participant?

As the EM notes at 1.120, the Macquarie Dictionary defines active as "in a state of action, in actual progress or motion *and capable of exerting influence*" (emphasis added). See also 1.22 in this regard. In the present circumstances, the charity is unable to exert any influence at all – it is merely a charitable recipient under a scheme arranged by the company.

See also section 6.5.1 of the ATO's guide to the general value shifting regime.

Further, the EM notes at 1.123 that the importance of the act to the success or effect of the scheme, whether great or slight, is not a relevant consideration.

Once you put the above factors together, it appears to me that the scheme here is the arrangement under which the company determines to issue shares to the charity. While the charity may be involved in the scheme in the sense that, contractually, it must accept the gift because the gift is being delivered in the form of shares, it played no part, and exerted no influence over (and nor could it) the scheme or its implementation. The fact that the charity must participate (in the sense of accepting the gift) is, per 1.123, not a relevant consideration.

On this basis, it seems to me the charity is not an active participant and therefore not an affected owner of up interests (provided it is not an associate of the controller).

Could you perhaps give some final consideration to this, and let me know your thoughts?

Regards

[redacted]

From: [redacted]@ato.gov.au>
Sent: Wednesday, 4 May 2022 1:04 PM
To: [redacted]com.au>
Cc: [redacted]@ato.gov.au>
Subject: RE: [redacted] (Pledge 1% Gift) - our preliminary position [SEC=OFFICIAL:Sensitive, ACCESS=Legislative-Secrecy]

[EXTERNAL]

H[redacted]

Thanks for the email.

We understand you're asking whether we can suggest alternatives which could allow the company to issue shares to a charity without any adverse tax consequences.

We appreciate your comments on Pledge 1% and the client's motivations, but we don't have (and can't make) any recommendations.

1. We've thought about revisions to the scheme, but can't see how the company could issue shares to a charity without causing a value shift under the direct value shifting rules. Conceivably the deed could be revised so that the company had an unconditional obligation to pay cash to a charity (rather than a choice between cash or issuing shares). But we are thinking set-off could only work if the charity had a genuine obligation (under a separate agreement) to subscribe for shares by paying cash. We don't think there'd be a genuine obligation if there was some understanding that the charity wouldn't have a practical obligation to pay cash for the share subscription. In substance, that revised scheme would still be a share issue for no consideration.

YES – I ACCEPT THIS IS A DIFFICULTY. IT WAS AN APPROACH WE CONSIDERED BUT FELT (CORRECTLY, AS IT TURNS OUT BASED ON YOUR COMMENTS HERE) THAT THE ATO MAY NOT ACCEPT IT.

AND JUST SO I AM CLEAR – I THINK THE EFFECT OF WHAT YOU ARE SAYING IS THAT EVEN IF, FOR EXAMPLE, THE COMPANY MADE A CASH DONATION TO THE CHARITY AND SUBSEQUENTLY THE CHARITY SUBSCRIBED FOR SHARES IN AN EQUAL AMOUNT, AND PAID CASH FOR THE SHARES, YOUR VIEW WOULD STILL BE THAT VALUE SHIFTING WOULD APPLY?

2. We see practical problems as well. Has the client identified a charity which would be willing to subscribe for shares in a private company? Our feeling is that a charity may be reluctant to (or unable under its constitution) become a shareholder and accede to a Shareholders Agreement. While the company's proposed action seems very generous, holding shares in a private company mightn't be the most appropriate investment for a charity, given its charitable object and obligations. For example, we think it would be difficult for the charity to sell shares in a private company to raise cash to support its activities.

I THINK THAT IN PRACTICE WHAT WILL HAPPEN IS THAT A FOUNDATION WOULD BE CHOSEN THAT ITSELF HAS SOME TIES TO THE PLEDGE 1% MOVEMENT AND SO WOULD BE HAPPY TO HOLD SHARES IN A PRIVATE COMPANY. IT MAY ALSO BE THE CASE THAT THE SHARE ISSUE OCCURS ONCE THERE IS A REASONABLE LIKELIHOOD THAT A SALE MAY OCCUR, SO THE CHARITY MAY PRACTICALLY ONLY BE A SHAREHOLDER FOR A RELATIVELY SHORT PERIOD OF TIME.

3. For completeness, we remind you about section 725-70. Broadly, there will only be Division 725 consequences for *down interests* affected by a value shift if the sum of all decreases in market value of those down interests are at least $150,000. We appreciate the company is unlikely to know what the market value of its shares will be when the liquidity event happens.

THANKS, AND YES I AM AWARE OF THE PROVISION. THIS ALSO RAISES THE POSSIBILITY THAT IF THE SHARES ARE ISSUED AT AN EARLY STAGE IN THE COMPANY'S EXISTENCE, THE DE MINIMIS THRESHOLD WOULD NOT BE BREACHED. BUT THAT MAY NOT BE THE CASE IF THE SHARE ISSUE OCCURS CLOSER TO THE LIQUIDITY EVENT.

4. Having said that, our function as law interpretation staff is to apply the ATO view of the law to known facts or proposed schemes, and that's the limit of our authority. Given these limitations we can't directly give 'planning' type advice to help taxpayers achieve desired tax outcomes, regardless of the client's motivations.

UNDERSTOOD AND EXPECTED THAT TO BE YOUR POSITION, BUT I THOUGHT IT WAS WORTH ASKING THE QUESTION IN THE CIRCUMSTANCES.

5. We can give still advice about how the law might apply to a revised arrangement if you or the client wish to suggest something. As we explained before, any advice we give outside a formal private ruling request wouldn't be binding.

If we don't hear back from you we'll treat the ruling request as withdrawn. We're happy to consider alternative arrangements – but for ATO administrative purposes, we'd treat those discussions as a new advice 'case'. (Preliminary discussions would probably be recorded as general guidance or early engagement.) We're happy for you to send any request for advice about a revised arrangement direct to us.

For completeness, we gather you're comfortable with the tax outcome if the shareholders donate cash on exit, and aren't asking for reassurance on that point? (Please let us know if we've misunderstood.)

YOUR UNDERSTANDING IS CORRECT – WE ARE NOT LOOKING FOR REASSURANCE ON THIS POINT.

Thanks,

[redacted]

Private Wealth |Technical Leadership & Advice
Australian Taxation Office
P 07[redacted] M[redacted]

From: [redacted]com.au>
Sent: Monday, 2 May 2022 5:02 PM
To: [redacted]@ato.gov.au>
Cc: [redacted]@ato.gov.au>
Subject: RE: [redacted] (Pledge 1% Gift) - our preliminary position [SEC=OFFICIAL:Sensitive, ACCESS=Legislative-Secrecy]

EXTERNAL EMAIL: EXERCISE CAUTION

Dea[redacted]

Thank you for your note.

As you may be aware, Pledge 1% is a movement aimed at encouraging corporate philanthropy. Generally speaking, participation will occur at the shareholder level, whereby the shareholder will enter into a deed similar to the one we submitted for your consideration. Where the shareholder participates, no issue of value shifting arises, and the shareholder will likely be entitled to a tax deduction in respect of the charitable donation made. I understand that the private ruling with authorisation number 1051807655739 deals with this situation.

In our experience, some companies themselves have a desire to encourage philanthropy, and for that reason we have been engaged (on a pro bono basis) to assist with the design of an arrangement that would allow a company to participate in the Pledge 1% movement without any adverse tax consequences. To be clear, the arrangement was not structured so as to deliver a tax deduction to the company (we consider one would not be available) but rather, to prevent shareholders from suffering a tax consequence as a result of the company's philanthropic pursuits.

If it is not possible to structure it in that way, then I suspect the shareholders may themselves make the donation on an exit event, and obtain a tax deduction (and potentially quite a significant one) at that point in time.

In that context, and given that we consider this is an important initiative, we would appreciate the opportunity to explore other options with you that might allow a favourable ruling to be issued.

I look forward to hearing from you in this regard.

Regards

[redacted]

From [redacted]@ato.gov.au>
Sent: Friday, 1 April 2022 11:36 AM
To [redacted]com.au>
Cc [redacted]@ato.gov.au>
Subject: [redacted] Pledge 1% Gift) - our preliminary position [SEC=OFFICIAL:Sensitive, ACCESS=Legislative-Secrecy]

[EXTERNAL]

Hi [redacted]

We've discussed your email with our regional director and it has been raised with our Assistant Commissioner.

[redacted] my manager, called you this morning to discuss this and left a voicemail for you to return his call. In brief, we acknowledge the shortcomings with the Early Engagement advice, however for reasons explained below we need to continue with the Private Ruling in the normal way and apply the ATO view of the law.

1. **The nature of Early Engagement advice**

The main purpose for Early Engagement is to help clients identify relevant facts and issues while preparing a Private Ruling application. It's preliminary and indicative, not binding advice about how we might later rule. We aim to highlight problems, but can't guarantee we'll identify all issues relevant to the final ruling. See our website: Early engagement for advice, QC 50061.

2. **Our approach in this private ruling**

Now you've applied for a Private Ruling, we're bound to apply the ATO view of the law.

- We identified TR 2008/5 which explains the ATO view on set-off.
- Applying TR 2008/5, we don't think this arrangement demonstrates the conditions for a valid set-off. Our letter explained our preliminary reasoning.
- In a ruling, ATO officers can't ignore an ATO view or apply it incorrectly just because previous non-binding advice might have taken a different view.

3. **Comments on our Early Engagement advice**

We're disappointed our Early Engagement advice didn't capture all the issues raised by your submission, but we don't think that undermines the process.

- Clearly the Early Engagement advice would have been more useful if it had identified and applied TR 2008/5.
- Having said that, our Early Engagement advice did raise some questions about whether the deed created a binding obligation to pay. We don't read it as an unqualified endorsement of your position.
- In any event, sometimes we need to change our thinking between Early Engagement and private rulings. We generally devote more resources (research, analysis, consultation, approval) to private rulings because they have more serious consequences.
- We've shared and discussed your feedback with our superiors.

4. **Next steps for this private ruling**

We're happy to receive submissions if you:

- disagree with our understanding or application of the principles in TR 2008/5, or
- don't think those principles apply here.

We'll allow you another 28 days **(Monday 2 May 2022)** to respond.

Otherwise, we'll work towards issuing a ruling. It's possible we'll ask for more facts, or alternatively make assumptions, before we can issue the final ruling. However, our decision will need to be consistent with TR 2008/5.

Thanks,

[redacted]

Private Wealth |Technical Leadership & Advice
Australian Taxation Office
P 07[redacted] | M [redacted]

From: [redacted]com.au>
Sent: Wednesday, 23 March 2022 11:36 AM
To: [redacted]@ato.gov.au>
Cc: [redacted]@ato.gov.au>
Subject: RE: [redacted] (Pledge 1% Gift) - our preliminary position [SEC=OFFICIAL:Sensitive, ACCESS=Legislative-Secrecy]

*****EXTERNAL EMAIL ALERT – EXERCISE CAUTION*****

Hi [redacted]

I have been mulling this over for a little while now. I have not spent any time considering your technical arguments. Instead, I am finding it very difficult to reconcile how your letter can reach the opposite conclusion reached in [redacted]s email dated 18 January. The only piece of information that has changed is the identity of the taxpayer seeking the ruling and even then, the taxpayer was identified as the majority shareholder in the original application, so this can hardly been seen as a material change.

I had understood that the purpose of the early engagement product was to provide taxpayers with a level of certainty when entering into commercial transactions. If the answer changes from that product to the private ruling product (which is the natural progression in these matters), then it seems to me that there is a real risk the integrity of the product is undermined, with the consequence that taxpayers lose confidence in it, which also reduces consultation.

I therefore request that you arrange a meeting or call between the relevant assistant commissioner and me.

Please let me know if you wish to discuss.

Regards

[redacted]

From: [redacted]@ato.gov.au>
Sent: Tuesday, 1 March 2022 2:49 PM
To: [redacted]om.au>
Cc: [redacted]@ato.gov.au>
Subject: [redacted] (Pledge 1% Gift) - our preliminary position [SEC=OFFICIAL:Sensitive, ACCESS=Legislative-Secrecy]

[EXTERNAL]

Hi [redacted]

We're reviewed this private ruling request for the 1% Pledge.

At this point, we think that Division 725 **will apply** if GGH issues shares to a charity to meet the pledge.

See the attached letter which summarises our reasoning on your submissions.

Let us know if you have questions or concerns, or further submissions, and whether the client still needs the ruling. We can also arrange a phone conference if you would like one. We're asking you to get back to us by **COB Wednesday 23 March 2023**.

Thanks,

[redacted]
Private Wealth |Technical Leadership & Advice
Australian Taxation Office
P 07[redacted] M[redacted]

From: [redacted]com.au>
Sent: Wednesday, 16 February 2022 8:13 AM
To: [redacted]@ato.gov.au>
Cc: [redacted]@ato.gov.au>; [redacted]@ato.gov.au>
Subject: RE: Application for PBR - Pledge 1% Company Deed of Equity Gift [SEC=OFFICIAL:Sensitive, ACCESS=Legislative-Secrecy]

*****EXTERNAL EMAIL ALERT – EXERCISE CAUTION*****

H[redacted]

Thanks for your note. I now **attach** the previous correspondence in relation to this matter, and you will see that [redacted] and [redacted] reached a view under the early engagement program. You will also note that we changed the taxpayer on whose behalf the ruling application was lodged given that the value shifting issue affects the shareholder rather than the target entity.

And yes – I appreciate the indefinite period may cause a problem, Happy to discuss that with you.

Anyway, I look forward to hearing from you in due course.

Regards

[redacted]

From: [redacted]@ato.gov.au>
Sent: Wednesday, 16 February 2022 9:07 AM
To: [redacted]com.au>
Cc: [redacted]@ato.gov.au>; [redacted]@ato.gov.au>
Subject: Application for PBR - Pledge 1% Company Deed of Equity Gift [SEC=OFFICIAL:Sensitive, ACCESS=Legislative-Secrecy]

[EXTERNAL]

Hi [redacted]

Just letting you know that this private ruling request for [redacted] and Pledge 1% Deed has been assigned to me – [redacted] has moved to another team in theATO.

It might take me some time to work through. We'll be in touch if we need more information or would like to discuss.

I'll just flag that we don't usually give rulings for indefinite periods – but this is something we can discuss after we've reviewed and reached a tentative view.

Thanks,

[redacted]
Private Wealth |Technical Leadership & Advice
Australian Taxation Office
P 07[redacted] M[redacted]

From: [redacted]com.au>
Sent: Tuesday, 15 February 2022 3:30 PM
To: [redacted]@ato.gov.au>
Cc: [redacted]@ato.gov.au>
Subject: RE: Application for PBR - Pledge 1% Company Deed of Equity Gift [SEC=OFFICIAL:Sensitive]

EXTERNAL EMAIL ALERT – EXERCISE CAUTION

H[redacted]

Please find **attached** private ruling application.

Regards

[redacted]

From: [redacted]@ato.gov.au>
Sent: Tuesday, 30 November 2021 12:23 PM
To: [redacted]com.au>
Cc: [redacted]@ato.gov.au>
Subject: RE: Application for PBR - Pledge 1% Company Deed of Equity Gift [SEC=OFFICIAL:Sensitive]

[EXTERNAL]

Thanks [redacted] received.

We won't need the signed ATO form until you're lodging it in final as a private ruling.

Regards,

[redacted]

Tax Specialist

Technical Leadership & Advice
Private Wealth
Australian Taxation Office
P 07[redacted]

From: [redacted]com.au>
Sent: Monday, 29 November 2021 3:40 PM
To: [redacted]@ato.gov.au>
Cc: [redacted]@ato.gov.au>
Subject: RE: Application for PBR - Pledge 1% Company Deed of Equity Gift [SEC=OFFICIAL:Sensitive]

EXTERNAL EMAIL ALERT – EXERCISE CAUTION

[redacted] and [redacted]

Please find attached the annexures to the draft ruling application and draft deed of gift. Please let me know if you also require the ATO ruling form.

Regards

[redacted]

From: [redacted]@ato.gov.au>
Sent: Friday, 26 November 2021 2:15 PM
To: [redacted]om.au>
Cc: [redacted]com>; [redacted]com>; Mark Reading <mreading@atlassian.com> [redacted]@ato.gov.au>
Subject: RE: Application for PBR - Pledge 1% Company Deed of Equity Gift [SEC=OFFICIAL:Sensitive]

[EXTERNAL]

H[redacted]

[redacted]and I are happy to assist with providing advice in relation to the proposed Company Deed of Equity Gift. As foreshadowed by Mark, you can send a copy of the draft application of your ruling to me if you prefer (this will take the form of 'early engagement advice'), before submitting a private binding ruling application in final.

Feel free to give me a call or email if you have any questions in the meantime.

We look forward to hearing from you.

Regards,

[redacted]

[redacted]

Tax Specialist

Technical Leadership & Advice
Private Wealth
Australian Taxation Office
P 07[redacted]

From: Mark Reading <mreading@atlassian.com>
Sent: Friday, 26 November 2021 9:29 AM
To: [redacted]@ato.gov.au>; [redacted]@ato.gov.au>
Cc: [redacted]com.au>; [redacted]om>; [redacted]com>
Subject: Application for PBR - Pledge 1% Company Deed of Equity Gift

*****EXTERNAL EMAIL ALERT – EXERCISE CAUTION*****

Dear[redacted]and[redacted]

In the spirit of Thanksgiving, I'd like to once again thank you for the way in which you so professionally processed the application for a Pledge 1% related private binding ruling by [redacted]founder of [redacted]early this year.

As you are aware, the Deed of Equity Gift to which the ruling related is a Deed executed by an individual taxpayer.

Since the PBR was issued, I have been working with[redacted]and [redacted]the founders of another Pledge 1% member,[redacted]and their adviser [redacted]from [redacted](who I believe is providing support pro bono), to finalise a Deed of Equity Gift executed by a company, rather than by an individual.

[redacted]is planning to issue, on behalf of[redacted]an application for a private binding ruling relating to the Company Deed of Equity Gift.

As you are familiar with Pledge 1% and the background to the Deed, I am hoping it might be possible for[redacted]to work with you.

Please respond directly to [redacted] copying [redacted] and I, advising whether or not [redacted] should coordinate with you.

Recalling that when the team from [redacted] worked with you, they shared a draft application and deed with you, before formally submitting the application, I'd also be interested in knowing if you would recommend a similar approach this time.

Kind regards

Mark

MARK READING
Head of Foundation
mreading@atlassian.com
Level 6, 341 George Street, Sydney NSW 2000, Australia

GPO BOX 9990 SYDNEY NSW 2001

Australian Government
Australian Taxation Office

[redacted] AS TRUSTEE FOR [redacted]
[redacted] TRUST
ATTENTION [redacted]
C/- [redacted]
[redacted]
SYDNEY NSW 2000

Our Reference: [redacted]
Contact officer: [redacted]
Phone: (07) [redacted]
Client ID: [redacted]

1 March 2022

Our preliminary position on your private ruling

Dear [redacted]

We've reviewed the private ruling request that we received on 15 February 2022.

We think that Division 725[1] will apply if GGH issues shares to a charity to meet the pledge. Shares will be issued at a discount, and the market value for existing shares will be reduced through dilution. We've considered your submissions, and another issue, but we think that the requirements for a value shift will be met.

You made two submissions. Your main submission was that subsection 725-145(2) won't apply: there's no discount because [redacted] is issuing the shares to set-off against a separate obligation to pay cash to the charitable recipient. You've also suggested that this arrangement should be outside the scope of the direct value shifting rules because it isn't a scheme designed to achieve a value shift. We disagree for reasons explained in the **Attachment.**

Next steps for the ruling

Let us know if you have questions or concerns or further submissions, and whether the client still needs the ruling. We can arrange a phone conference if you think that would be helpful.

Please get back to us by **COB Wednesday 23 March 2023** with any submissions, or to confirm whether the client still needs a ruling.
If the client does still need a ruling, we might need to confirm a few facts (or agree on assumptions) before we can issue it.

Yours sincerely,
Louise Clarke
Deputy Commissioner of Taxation

NEED HELP?

If you have any questions, you can phone Edward Brackin on **(07) 314 95843**.

Alternatively, you can phone us on **13 28 69** between 8:00am and 5:00pm, Monday to Friday.

Ask for Edward Brackin on extension **95843**.

PRIVACY

The ATO is a government agency bound by the *Privacy Act 1988* in terms of collection and handling of personal information and tax file numbers (TFNs). Further information about our privacy policy is available at **ato.gov.au/privacy**

[1] All legislative references are to the *Income Tax Assessment Act 1997*.

Attachment – our responses to your submissions

Will [redacted] receive a payment by set-off?

Shares will be issued at a discount (see section 725-150) if their market value exceeds the payment **received** by [redacted] While [redacted] won't receive cash, property or services, we can see an argument that it will receive a payment if it discharges mutual obligations by set-off. Therefore, we've considered your suggestion that set-off could apply under this arrangement.

Relevant principles

We think TR 2008/5 is relevant here: it explains the ATO's view about when set-off would apply to a company issuing shares. To briefly paraphrase some points it makes:

- The principle of set-off is that if A owes a money debt immediately payable to B, and B owes an equal money debt immediately payable to A, the parties can agree to extinguish both debts in payment of the other. [paragraphs 38-39]
- Set-off may be available when a company has incurred a loss or outgoing for some other obligation, and the other party has subscribed for shares in the company. [paragraphs 4, 37]
- There must be cross-liabilities immediately payable, with an agreement (express, tacit or implied) that the liabilities can be set-off. [paragraphs 41-42]
- Obligations must exist **before** they can be discharged by a set-off agreement. Agreements to set-off present obligations against future obligations are ineffective when made, and aren't self-executing if those future obligations arise. [paragraph 46]
- Where there is only one agreement and amounts are stipulated for the property/services, and amount of the shares, whether cross obligations arise and can be discharged by set-off can't be concluded without case-by case examination of the contract and substance of transaction. [paragraph 54]

Applying these principles – are there mutual obligations to set-off?

We don't think the conditions for a set-off will be established in this scenario for at least three reasons.

1. We can only see one obligation under the deed. We think the combined effect of clauses 4.2 and 6.1 is that [redacted] can choose to meet the pledge by either paying cash or issuing shares. We don't think it should be characterised as creating two separate obligations – one for [redacted] to pay cash, and one for the charitable recipient to subscribe for shares by paying cash.

2. We question whether a unilateral deed can give rise to two separate, mutual obligations which can be set-off. Each party needs to have independent pre-existing obligations, and they need to agree to set them off. Here, the charitable recipient isn't a party to the deed. While it might have rights under the deed, the deed couldn't require the charity to do anything (like subscribe for shares by paying cash) without a separate agreement. We appreciate that the charity may need to enter any Shareholder's Agreement (if required) for the grant to take effect: see clause 2.4. However, we think the charity would need to independently subscribe for shares *in exchange for cash*.

3. In substance, we see this as being one arrangement to issue shares to a charitable recipient. We may take the same view even if:
   a) the legal form of the deed purported to create two separate obligations, or
   b) the parties signed a separate share subscription agreement before GGH issued shares.

   We think it unlikely that a charity (given their legal obligations) would make a genuine, independent decision to pay cash for shares in a private company. Any share subscription agreement could only be

explained as a step to help [redacted] complete the pledge. It would be part of a single arrangement to issue shares to a charity.

While we have reservations about the effect of the deed, we don't see that amending it would necessarily change the outcome for the reasons given in points 2 and 3.

Is this arrangement outside the scope of the value shifting rules?

You've suggested that this arrangement should be outside the scope of the value shifting rules. The objects clause in section 725-1 suggests the rules are directed at schemes which inappropriately shift value. You've submitted this is a charitable scheme, not a scheme intended to shift value inappropriately.

We disagree.

- The scope of the value shifting rules are set by substantive rules, including the definition of a value shift in section 725-145. The objects clause isn't operative, and isn't an exhaustive description of when the value shifting rules apply.

- We don't think purpose is relevant. The core rules don't require any participant to have a purpose of shifting value. Also, see the Explanatory Memorandum[2] at paragraph 8.13, which says there doesn't need to be any tax avoidance purpose for Division 725 to apply. We don't think an arrangement would be exempt just because it has a charitable purpose or effect.

Will the charitable recipient be an affected owner of up-interests?

One other issue we considered was whether the charitable recipient would be an affected owner of up-interests for the purposes of working out the consequences for a value shift. 'Affected owner' is defined in section 725-85, and broadly includes controllers, associates, and active participants. 'Active participant' includes any entity which directly facilitated the scheme: see subsection 725-65(2). We can see an argument that the charitable recipient's involvement is 'passive' rather than 'active'. However, an entity can still facilitate through omission: see the Explanatory Memorandum at paragraphs 11.113 to 11.141. We think the charitable recipient will be directly facilitating the scheme by a) accepting shares, and b) signing the shareholder agreement. Therefore, the charitable recipient would be an active participant, and an affected owner of up-interests.

[2] Explanatory Memorandum (Senate) to the New Business Tax System (Consolidation, Value Shifting, Demergers and Other Measures) Bill 2002.