

## Precedent: Div 7A loan agreement

[¶2500-220]

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This precedent loan agreement is drafted in light of Div 7A of Part III of the *Income Tax Assessment Act 1936*. Specific advice should be sought to ensure that the arrangements between the parties meet the requirements of a Div 7A loan.

### **Loan Agreement — Division 7A**

This agreement is made the day of , [insert year].

#### **PARTIES**

[insert name] of [insert address] ("**Company**")

[insert name] of [insert address] ("**Borrower**")

#### **BACKGROUND**

A. The Company has resolved to provide a Loan to the Borrower in accordance with this agreement.

#### **OPERATIVE PROVISIONS**

##### **1. Definitions**

###### **1.1 Definitions**

In this agreement:

"**Act**" means the *Income Tax Assessment Act 1936* (Cth), unless otherwise indicated.

"**Advance**" means any Loan made at any time to which this agreement applies (but 2 or more Loans made on the same day will be considered together as one Advance) and includes any loan deemed to have been made if a payment is converted to a loan in circumstances within section 109D(4A) of the Act.

"**Amalgamated Loan**", with respect to one or more Advances made or deemed to have been made in a Year of Income has the meaning provided by section 109E(3) of the Act, and section 109E(3A) and (3B) of the Act if applicable, where the reference in those sections to one or more "loans" termed "constituent loans" are taken to be references to one or more Advances ("constituent Advances") for the purposes of this agreement.

"**Corporations Act**" means the *Corporations Act 2001* (Cth).

"**Division 7A of the Act**" means Division 7A of Part III of the *Income Tax Assessment Act 1936* (Cth).

"**Excluded Loan**" means any payment or Loan that is not treated as a dividend by the Company by virtue of a provision of Division 7A of the Act other than section 109E, section 109N, section 109P or section 109Q of Division 7A of the Act. "**Event of Default**" has the meaning given in clause 7.1.

"**Insolvency Event**" means the occurrence of any one or more of the following events in relation to any person:

- (a) an application is made to a court for an order that it be wound up, declared bankrupt or that a provisional liquidator or receiver or receiver and manager be appointed, and the application is not withdrawn, struck out or dismissed within 21 days of it being made;
- (b) a liquidator or provisional liquidator is appointed;
- (c) an administrator or a receiver or receiver and manager is appointed to any of its assets;
- (d) it enters into an arrangement or composition with one or more of its creditors, or an assignment for the benefit of one or more of its creditors;
- (e) it proposes a winding-up or dissolution or reorganisation, moratorium, deed of company arrangement or other administration involving one or more of its creditors;
- (f) it is insolvent as disclosed in its accounts, or otherwise states that it is insolvent, or it is presumed to be insolvent under an applicable law;

- (g) it becomes an Insolvent under Administration (as defined in the Corporations Act) or action is taken which could result in that event and the proceeding is not dismissed within 21 days of the date that action is taken;
- (h) it is taken to have failed to comply with a statutory demand as a result of section [459F\(1\)](#) of the Corporations Act;
- (i) a notice is issued under sections [601AA](#) or [601AB](#) of the Corporations Act and not withdrawn or dismissed within 21 days;
- (j) a writ of execution is levied against it or a material part of its property which is not dismissed within 21 days;
- (k) it ceases to carry on business or threatens to do so, other than for reorganisation or restructuring in accordance with the terms of this agreement; or
- (l) anything occurs under the law of any jurisdiction which has a substantially similar effect to any of the above paragraphs of this definition.

**"Interest Rate"**, in relation to a Year of Income, means the rate determined under clauses 4.2 and 4.3.

**"Loan"** has the meaning provided by section [109D\(3\)](#) of the Act but does not include an Excluded Loan.

**"Loan Year"** is a Year of Income in which an Advance is made or is deemed to have been made, in accordance with clauses 2, 4 and 5.

**"Lodgement Day"** has the meaning provided by section [109D\(6\)](#) of the Act.

**"Payment Year"** is a Year of Income in respect of which a Repayment Amount is calculated and becomes payable in accordance with clause 5.

**"Principal Outstanding"** means, at any time, the outstanding aggregate principal amount of the constituent Advance or Advances of an Amalgamated Loan.

**"Prior Year"** is a Year of Income that immediately precedes a Payment Year, in accordance with clause 5.3.

**"Private Company"** has the meaning provided by section [995-1](#) of the *Income Tax Assessment Act 1997* (Cth).

**"Remaining Term"**, in relation to an Amalgamated Loan, has the meaning provided by clause 5.3.

**"Repayment Amount"** means the amount determined under clauses 5.3 and 5.5.

**"Term"**, in relation to an Advance, means the period of time determined under clause 3.

**"Year of Income"** means a year of income of the Company within the meaning of the Act.

## 1.2 Interpretation

In the interpretation of this agreement (unless the context indicates a contrary intention):

- (a) headings are for convenience only and do not affect interpretation;
- (b) if more than one person is identified as the Borrower, that expression refers to them, and the obligations of the Borrower under this agreement bind them, jointly and severally;
- (c) "person" includes an individual, the estate of an individual, a corporation, an authority, an association or a joint venture (whether incorporated or unincorporated), a partnership and a trust;
- (d) "power" in relation to the Company includes all powers, authorities, rights, remedies, privileges and discretions conferred on the Company by acceptance of this agreement, by any deed, agreement, document or instrument, by any statute or otherwise by law;
- (e) a reference to a party includes that party's executors, administrators, successors, and permitted assigns including persons taking by way of novation;
- (f) a word importing the singular includes the plural (and vice versa), and a word indicating a given gender includes every other gender.
- (g) a reference to a statute includes its delegated legislation and reference to a statute or delegated legislation or a provision of either includes consolidations, amendments, re-enactments or replacements;
- (h) a reference to a party, clause, schedule, exhibit, attachment or annexure is a reference to a party, clause, schedule, exhibit, attachment or annexure to or of this agreement, and a reference to this agreement includes all schedules, exhibits, attachments and annexures to it;
- (i) if a word or phrase is given a defined meaning, any other part of speech or grammatical form of that word or phrase has a corresponding meaning;
- (j) "includes" in any form is not a word of limitation; and
- (k) a reference to "\$" or "dollar" is to Australian currency.

## 2. Advances

### 2.1 Advances subject to this agreement

- (a) Any Advance by the Company to or for the Borrower is or will be made on, and is subject to, the terms set out in this agreement.
- (b) In the event that the Company has paid an amount to the Borrower at a time in a Loan Year, and the payment is converted to a loan before the end of the Company's Lodgement Day for the Loan Year in circumstances within section [109D\(4A\)](#) of the Act, the Loan resulting from that conversion will be deemed to constitute an Advance under this agreement and will be subject to all the provisions of this agreement as if it were an Advance made at the time of payment.
- (c) In the event that the Company has paid, lent or advanced amounts to the Borrower (other than an Excluded Loan) in a Loan Year before the date of this agreement with the intention that the terms of payment, Loan or advances be reduced

to writing in the terms of this agreement within the period permitted by section [109N](#) of the Act ending on the Lodgement Day for the Loan Year, such payments, Loans or advances constitute Advances under this agreement and are subject to all provisions of this agreement as if made after the date of this agreement.

## **2.2 Amalgamated Loan for an Income Year**

- (a) Where one or more Advances are made or are deemed to have been made during a Loan Year, the Advances made or deemed to have been made during the Loan Year comprise the constituent Advances of a separate Amalgamated Loan for the Loan Year to the extent that those Advances satisfy the statutory conditions in section [109E\(3\)](#) of the Act (together with section [109E\(3A\)](#) and [\(3B\)](#) if applicable).
- (b) Where, pursuant to clause 2.2(a) of this agreement, the Company has made or is deemed to have made an Amalgamated Loan during one or more Years of Income ("Loan Years"), the terms of this agreement apply separately to the Amalgamated Loan for each Loan Year and the Company will maintain appropriate records with respect to each Amalgamated Loan for each Loan Year, including the respective Repayment Amounts payable under clause 5 with respect to the Amalgamated Loan for each Loan Year.

## **3. Term**

### **3.1 Statutory maximum Term**

The Term for each Advance will be determined in accordance with the following:

- (a) if any regulations made under section [109N\(3\)](#) of the Act provide an applicable method for working out the maximum term, then the Term for the Advance will be the maximum term determined in accordance with those regulations;
- (b) subject to clause 3.1(a), if:
  - (i) 100% of the value of the Advance is secured by a mortgage over real property that has been registered in accordance with a law of a State or Territory; and
  - (ii) when the Advance is first made, the market value of that real property (less the amounts of any other liabilities secured over that property in priority to the loan) is at least 110% of the amount of the Advance,

then the Term for the Advance will be 25 years; and

- (c) subject to clause 3.1(a) and 3.1(b), the Term for the Advance will be 7 years.

### **3.2 Agreed term**

- (a) Despite clause 3.1, the parties may at any time agree to vary the Term for an Advance. The Term must never exceed the period determined in accordance with clause 3.1. Any variation of the Term must be in writing, signed by both parties.
- (b) If, at the time of making this agreement, the parties agree that the Term for any Advance will be shorter than the period determined in accordance with clause 3.1, the agreed Term will be specified in Attachment A.

### **3.3 Commencement of Term**

The Term for any Advance will commence on the date the Advance is made.

## **4. Interest**

### **4.1 Borrower must pay interest**

The Borrower must pay interest to the Company at the Interest Rate on the Principal Outstanding under this agreement, calculated annually in arrears on a daily basis.

### **4.2 Statutory Benchmark Interest Rate**

The Interest Rate for each Year of Income after the Year of Income in which the Term for an Advance commences will be determined in accordance with the following:

- (a) if any regulations made under section [109N\(2\)](#) of the Act provide an applicable method for working out the benchmark interest rate, then the Interest Rate for the Year of Income will be the benchmark interest rate determined in accordance with those regulations;
- (b) subject to clause 4.2(a), the Interest Rate for the Year of Income will be the Indicator Lending Rates — Bank variable housing loans interest rate last published by the Reserve Bank of Australia before the start of the Year of Income; or
- (c) where the Australian Taxation Office issues a public ruling or determination that prescribes the benchmark interest rate for the purposes of sections [109N](#) and [109E](#) of the Act with respect to a Year of Income, that rate will be taken to be the rate prescribed by clause 4.2(b).

### **4.3 Agreed Interest rate**

- (a) Despite clause 4.2, the parties may at any time agree to vary the Interest Rate for a Year of Income, but the Interest Rate must never be lower than the rate determined in accordance with clause 4.2. Any variation of the Interest Rate for a Year of Income must be in writing, signed by both parties.
- (b) If, at the time of making this agreement, the parties agree that the Interest Rate or Rates for one or more Years of Income will be higher than the rate determined in accordance with clause 4.2, the agreed Interest Rate or Rates will be specified in Attachment A.

## 5. Repayment

### 5.1 Repayment by expiry of Term

Any Advance must be fully repaid, with interest, by the expiry of its Term.

### 5.2 Yearly repayments

(a) Where:

- (i) the Company has made or is deemed to have made an Amalgamated Loan in any Loan Year; and
- (ii) the Amalgamated Loan or one or more constituent Advances of the Amalgamated Loan is or are not fully repaid at the end of either the Year of Income immediately after the Loan Year or at the end of any subsequent Year of Income,

in relation to the first Year of Income after the Loan Year in respect of which the Company would otherwise be deemed to pay a dividend under Division 7A of the Act with respect to the Amalgamated Loan, and in relation to each subsequent Year of Income, to the extent that the Amalgamated Loan (or one or more constituent Advances of the Amalgamated Loan) is or are not fully repaid at the end of any such Year of Income (each, a "Payment Year"), the Borrower must pay to the Company on or before the last day of each such Payment Year a Repayment Amount calculated in accordance with this clause.

(b) Where the Company has made or is deemed to have made an Amalgamated Loan to the Borrower in more than one Year of Income (that is, there is more than one Loan Year), the provisions of this clause 5 apply separately with respect to each Amalgamated Loan for each Loan Year, and the Repayment Amount or Amounts for each Payment Year.

(c) Where the Borrower pays an amount to the Company in relation to a constituent Advance of an Amalgamated Loan during any Year of Income after the Loan Year, the payment will be taken to be a repayment that relates the Amalgamated Loan that includes the constituent Advance.

### 5.3 Statutory minimum yearly repayment

The Repayment Amount payable on or before the last day of the Payment Year pursuant to clause 5.2 for an Amalgamated Loan for a Year of Income will be determined in accordance with the following:

- (a) if any regulations made under section [109E\(5\)](#) of the Act provide an applicable method for working out the amount of the minimum yearly repayment for an Amalgamated Loan for a Year of Income, then the Repayment Amount for the Payment Year will be the minimum yearly repayment for the Amalgamated Loan determined in accordance with those regulations;
- (b) subject to clause 5.3(a), the Repayment Amount payable on or before the last day of a Payment Year pursuant to clause 5.2 for an Amalgamated Loan for a Year of Income will be calculated in accordance with the formula;

$$\frac{OA \times IR}{1 - \left( \frac{1}{1 + IR} \right)^{RT}}$$

Where:

OA = the amount of the Amalgamated Loan which is not repaid by the end of the Year of Income (the "Prior Year") that immediately precedes the Payment Year, calculated in accordance with this clause 5.3.

IR = the Interest Rate for the Payment Year for which the Repayment Amount is being calculated; and

RT = the Remaining Term for the Amalgamated Loan.

(c) The Remaining Term for the Amalgamated Loan is the difference between:

- (i) the number of years in the longest Term of the constituent Advance or Advances comprising the Amalgamated Loan; and
- (ii) the number of years between the end of the Loan Year and the end of the Prior Year (beginning with zero where these Years are the same Year of Income);

rounded up to the next higher whole number if the difference is not otherwise a whole number.

(d) The amount of an Amalgamated Loan not repaid by the end of the Prior Year is determined as follows:

(i) where the Amalgamated Loan was made or deemed to have been made during the Prior Year (that is, the Loan Year and the Prior Year are the same Year of Income):

(A) by determining the amount of initial Principal Outstanding for the Amalgamated Loan and subtracting from it the total amount, if any, attributable to repayments of principal made during the Prior Year with respect to the constituent Advance or Advances of the Amalgamated Loan;

(ii) where the Amalgamated Loan was made or deemed to have been made during any Year of Income earlier than the Prior Year (that is, the Loan Year is a Year of Income earlier than the Prior Year):

(A) by determining the amount of the opening balance of the Principal Outstanding for the Amalgamated Loan at the beginning of the Prior Year;

(B) by determining the respective amount or amounts of any payments made during the Prior Year that are:

(I) attributable to interest payable for the Prior Year; or

(II) attributable to repayments of principal with respect to the constituent Advance or Advances for the Prior Year; and

(C) by subtracting from the opening balance determined under (A) the total of any payments made during the Prior Year attributable to repayments of principal with respect to the constituent Advance or Advances of the Amalgamated Loan.

(e) Notwithstanding the foregoing provisions of this clause, if the minimum repayment amount payable before the end of a Year of Income for an Amalgamated Loan for a Year of Income, calculated in accordance with Division 7A of the Act, would be an amount greater than, or less than, the Repayment Amount calculated in accordance with the foregoing provisions of this clause 5.3, then, subject to clauses 4.3 and 5.5, the Repayment Amount payable before the end of the Year of Income for that Amalgamated Loan will be the minimum yearly repayment amount calculated in accordance with Division 7A of the Act.

#### **5.4 Payments affected by the Act**

The Borrower may make repayments to the Company with respect to amounts outstanding under this agreement despite the fact that the repayments may be treated under Division 7A of the Act as repayments of a notional loan deemed to have been made to the Borrower by another entity.

#### **Agreed Repayment Amount**

(a) Despite clause 5.3, the parties may at any time agree to vary any Repayment Amount, but the Repayment Amount must not be lower than the amount determined in accordance with clause 5.3. Any variation of the Repayment Amount must be in writing, signed by both parties.

(b) If, at the time of making this agreement, the parties agree that the method for determining any Repayment Amount will be other than the method described in clause 5.3, the agreed method will be specified in Attachment A.

#### **5.6 [Early repayment on Company's demand]**

The Company may at any time serve a written notice, which must be expressed to be under this clause 5.6, stating that within 28 days or any other period as the Company may specify (which must not be less than 28 days) the Borrower is required to repay any or all of the amount owing under this agreement and any or all accrued but unpaid interest. The Borrower must comply with any notice received according to its terms.<sup>1</sup>

#### **5.7 Early repayment by Borrower**

The Borrower may at any time repay any or all of the amount owing under this agreement before repayment is otherwise required under this agreement.

#### **5.8 Set-off against dividends**

If at any time after the date of this agreement the Company pays or distributes a dividend where the Borrower is a shareholder, the Borrower and the Company may agree that all or part of the amount of the dividend paid or distributed to the Borrower, to the extent it is unfranked, may be set off against an amount owed by the Borrower to the Company under this agreement at the time of the payment or distribution of the dividend, to the extent that the amount owed by the Borrower to the Company under this agreement would, but for the set-off or application, be taken to be a dividend under Division 7A of the Act.

### **6. Guarantee**

#### **6.1 Liability arising in connection with a guarantee**

Where:

(a) the Company is a Private Company;

(b) the Company guarantees a loan made to the Borrower by another entity ("interposed entity"), whether or not the Company has provided an Advance to the Borrower and whether or not Division 7A of the Act applies to that guarantee;

(c) the Company incurs a liability (other than a contingent liability) under the guarantee to make a payment to the interposed entity;

- (d) all or part of the amount of the liability of the Company would otherwise be treated as a payment of the Company directly or indirectly to the Borrower under Subdivision E of Division 7A of the Act; and
- (e) as a result of the liability of the Company under paragraph (c) the Borrower incurs a liability (other than a contingent liability) to make a payment of an amount to the Company as guarantor,

the liability of the Borrower under paragraph (e) to the Company, to the extent of the amount of the deemed payment, if any, referred to in paragraph (d), will be treated as an Advance made by the Company to the Borrower to which this agreement applies and will be subject to all the provisions of this agreement as if it were an Advance made by the Company to the Borrower at the time the liability of the Borrower under paragraph (e) arises.

## **7. Event of Default**

### **7.1 Event of Default**

An Event of Default exists when:

- (a) the Borrower does not make a repayment in accordance with clause 5 of this agreement and does not rectify that failure within 7 days of receiving a written notice from the Company; or
- (b) an Insolvency Event occurs in relation to the Borrower.<sup>ii</sup>

### **7.2 Rights of the Company**

If an Event of Default occurs then, at the option of the Company and notwithstanding any delay or previous waiver of the right to exercise such an option, the Company may, by written notice, require the Borrower to immediately repay all outstanding borrowings and accrued but unpaid interest.

## **8. Continuing Effect**

This agreement and the liability of the Borrower under it will not be affected or discharged by:

- (a) the granting to any other person of any time or similar indulgence or consideration; or
- (b) any other laches, acquiescence, delay, act, omission or mistake on the part of the Company or any other persons.

## **9. Release of the Borrower from performance**

The Borrower will not be released from performing its obligations under this agreement, except in the following circumstances:

- (a) where the Borrower becomes bankrupt or where Part X of the *Bankruptcy Act* 1966 (Cth) applies;
- (b) where it is reasonable to consider that, within the meaning of section [109G\(4\)](#) of the Act:
  - (i) continued performance of its obligations under this agreement would cause the Borrower undue hardship;
  - (ii) at the time the Borrower incurred the debt, it had capacity to repay the debt; and
  - (iii) the Borrower has lost its ability to perform its obligations as a result of circumstances beyond its control; or
- (c) where or to the extent that the Commissioner of Taxation, pursuant to section [109Q](#), Subdivision DB or any other provision of Division 7A of the Act, exercises a discretion to modify the application or possible application of Division 7A of the Act to this agreement.

## **10. Governing law**

This agreement is governed by and must be construed according to the laws of the State or Territory specified in Attachment A.

## **11. Jurisdiction**

Each party irrevocably:

- (a) submits to the non-exclusive jurisdiction of the courts of the State or Territory specified in Attachment A, and the courts competent to determine appeals from those courts, with respect to any proceedings which may be brought at any time relating to this agreement; and
- (b) waives any objection it may now or in the future have to the venue of any proceedings, and any claim it may now or in the future have that any proceedings have been brought in an inconvenient forum, if that venue falls within the state or territory specified in clause 11(a).

## **12. Miscellaneous**

### **12.1 Assignments by the Borrower**

The Borrower cannot assign any of its rights under this agreement without the Company's prior written consent.

### **12.2 Time of essence**

Time is of the essence in respect of the Borrower's obligations under this agreement.

**12.3 Binding on each signatory**

This agreement is binding on each of the parties who sign this agreement, whether or not any one or more of the other named parties do not execute this agreement, or that there is any invalidity, forgery or irregularity touching any execution of this agreement, or that this agreement is or becomes unenforceable, void or voidable against another named party.

**12.4 Counterparts**

This agreement may be executed in any number of counterparts and by the parties on separate counterparts. Each counterpart constitutes an original of this agreement, and all together constitutes one agreement.

**ATTACHMENT A**

<b>Term</b> (Clause 3.2)	[insert] Years
<b>Interest Rate</b> (Clause 4.3)	[insert]
<b>Method of determining Repayment Amounts</b> (Clause 5.5)	[insert]
<b>Governing Law</b> (Clause 10)	The Laws of the State of [insert]
<b>Jurisdiction</b> (Clause 11)	[insert]

**EXECUTED AS AN AGREEMENT**

[insert execution blocks]

**Disclaimer:** This document must at all times be used cautiously and will need to be modified to reflect the particular circumstances in which it is proposed to be used. This document does not comprise legal, accounting or other professional advice. No person should rely on this document without first obtaining legal advice from a qualified lawyer and reviewing the document to ascertain if it is appropriate for the intended use. CCH does not warrant that this document is fit for any specific purpose, including without limitation compliance with any legal requirements that may be applicable to your organisation.

Last reviewed on 2 March 2018

**Footnotes**

- i This clause is optional, depending on whether the parties intend that the Company can call in the loan on demand.
  - ii An amending Act which is [expected to commence on 1 July 2018](#) will impose a stay on the enforcement of “ipso facto clauses”, which entitle a party to terminate or amend a contract (or which automatically terminate or amend the contract) merely because a company has entered into a formal insolvency process. The [Treasury Laws Amendment \(2017 Enterprise Incentives No 2\) Act 2017](#) received Royal Assent on 18 September 2017. The relevant part of the Amending Act is expected to take effect from 1 July 2018: Amending Act s 2; Media release, Kelly O'Dwyer MP, Minister for Revenue and Financial Services, “[Supporting innovation through insolvency law reform](#)”, Tuesday, 12 September 2017.
- These termination rights have been included in this precedent agreement because the ipso facto laws will not make them unlawful but rather unenforceable for certain periods. There is a provision that allows a court to order that the stay on enforcement of such rights does not apply if it is satisfied that it is “appropriate in the interests of justice”. If termination rights are not included in the agreement, then a party may be left in a precarious position. However, a party must be aware of the stay provisions before purporting to exercise the termination rights. The regulations which relate to these amendments are not yet available.
- The optional clause 5.6 gives the Company an independent right to demand early repayment within 28 days or any other specified period (which must not be less than 28 days).