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THE PARLIAMENT OF THE COMMONWEALTH OF AUSTRALIA

HOUSE OF REPRESENTATIVES

NATIONAL RENTAL AFFORDABILITY SCHEME (CONSEQUENTIAL
AMENDMENTS) BILL 2008

EXPLANATORY MEMORANDUM

(Circulated by the authority of the
Treasurer, the Hon Wayne Swan MP)

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Glossary

The following abbreviations and acronyms are used throughout this explanatory memorandum.

<i>Abbreviation</i>	<i>Definition</i>
ATO	Australian Taxation Office
the Consequential Bill	National Rental Affordability Scheme (Consequential Amendments) Bill 2008
CGT	capital gains tax
Commissioner	Commissioner of Taxation
Housing Secretary	Secretary of the Department that administers the NRAS
ITAA 1997	<i>Income Tax Assessment Act 1997</i>
ITAA 1936	<i>Income Tax Assessment Act 1936</i>
NRAS	National Rental Affordability Scheme

General outline and financial impact

National Rental Affordability Scheme: Refundable tax offset and other taxation issues

The National Rental Affordability Scheme (NRAS) is designed to encourage large-scale investment in affordable housing. The NRAS offers tax and cash incentives to providers of new dwellings on the condition that they are rented to low and moderate income households at 20 per cent below market rates. The National Rental Affordability Scheme Bill 2008 establishes the NRAS.

The National Rental Affordability Scheme (Consequential Amendments) Bill 2008 (the Consequential Bill) amends the *Income Tax Assessment Act 1997* (ITAA 1997) to enable entities participating in the NRAS to claim a refundable tax offset in their annual tax return, or through lodgment of a short form application by not-for-profit entities who would not ordinarily lodge a tax return. In addition, it amends the ITAA 1997 to ensure that state and territory contributions to entities participating in the NRAS, whether in cash or in-kind, are non-assessable and non-exempt income for taxation purposes, and to ensure that there are no capital gains tax consequences from the receipt of incentives under the scheme.

Date of effect: The NRAS commences on 1 July 2008. These amendments apply to income tax assessments for the 2008-09 income year and later years.

Proposal announced: The NRAS was announced on 13 August 2007 during the 2007 Federal election. The measure was also announced in the 2008-09 Budget on 13 May 2008. A detailed proposal was released by the Minister for Housing for public consultation on 2 May 2008 in a paper titled *National Rental Affordability Scheme — technical discussion paper*. A prospectus calling for expressions of interest in the scheme was released by the Treasurer and the Minister for Housing on 24 July 2008.

Financial impact: The amendments in the Consequential Bill, together with the National Rental Affordability Scheme Bill 2008, have a total fiscal cost of around \$622.6 million over five years (including administration costs).

Impact on fiscal balance

Expense

<i>2007-08</i>	<i>2008-09</i>	<i>2009-10</i>	<i>2010-11</i>	<i>2011-12</i>
–	\$23.5m	\$72.2m	\$170.1m	\$356.8m

Compliance cost impact: Compliance costs for entities participating in the NRAS could vary depending on the type of entity participating in the scheme. For most entities, these costs are likely to be low. The design of the law has sought to minimise compliance costs.

Chapter 1

National Rental Affordability Scheme: Refundable tax offset and other taxation issues

Outline of chapter

1.1 The National Rental Affordability Scheme (Consequential Amendments) Bill 2008 (the Consequential Bill) amends the *Income Tax Assessment Act 1997* (ITAA 1997) to enable entities participating in the National Rental Affordability Scheme (NRAS) to claim a refundable tax offset in their annual tax return. In addition, it amends the ITAA 1997 to ensure that state and territory contributions to entities participating in the NRAS, whether in cash or in-kind, are non-assessable and non-exempt income for taxation purposes, and to ensure that there are no capital gains tax (CGT) consequences from the receipt of incentives under the scheme.

Context of amendments

1.2 The NRAS is designed to encourage large-scale investment in affordable housing. It offers tax and cash incentives to providers of new dwellings on the condition that they are rented to low and moderate income households at 20 per cent below market rates.

1.3 The incentive comprises a Commonwealth contribution in the form of a refundable tax offset or payment to the value of \$6,000 per dwelling per year, and a state or territory contribution in the form of direct financial support or an in-kind contribution to the value of at least \$2,000 per dwelling per year. The incentive will be provided for a period of 10 years to complying participants, and will be indexed in line with the rental component of the Consumer Price Index.

1.4 The National Rental Affordability Scheme Bill 2008 establishes the NRAS. The explanatory memorandum to that Bill provides further information on the NRAS.

1.5 The National Rental Affordability Scheme (Consequential Amendments) Bill 2008 addresses the taxation aspects of the NRAS. In particular, this Bill specifies the entities entitled to claim the refundable

tax offset in their annual tax returns (or through lodgment of a short form application by not-for-profit entities who would not ordinarily lodge a tax return) and the methodology to determine the amount of their refundable tax offset. The Consequential Bill also ensures that assistance provided by the States and Territories, whether in cash or in-kind, is non-assessable and non-exempt income for taxation purposes, and ensures that there are no CGT consequences from the receipt of incentives under the scheme.

Summary of new law

1.6 The Consequential Bill addresses a number of scenarios that may arise under the NRAS including the following:

- An individual, corporate tax entity or a superannuation fund is entitled to a refundable tax offset provided that the Secretary of the Department that administers the NRAS (Housing Secretary) has issued the particular entity a certificate under the NRAS. The amount of the tax offset is the amount stated in the certificate.
- A party to a non-entity joint venture is entitled to a refundable tax offset provided that the Housing Secretary has issued the non-entity joint venture a certificate under the NRAS. The amount of the tax offset is the amount stated in the certificate shared between the parties of the non-entity joint venture according to their proportion of the NRAS rent of the non-entity joint venture for the NRAS year.
- The partners of a partnership and the beneficiaries of a trust are entitled to a refundable tax offset provided that the Housing Secretary has issued their partnership or trust (or a partnership or trust through which their interest is ultimately obtained) a certificate under the NRAS. The amount of the tax offset is the amount stated in the certificate shared between the partners of a partnership or the beneficiaries of a trust according to their proportion of the NRAS rent of the partnership or trust for the NRAS year.
- A trustee of a trust (rather than the trust's beneficiaries) is entitled to a refundable tax offset provided that the Housing Secretary has issued the trustee a certificate under the NRAS and this trust has no net income. Similarly, a trustee of a trust (rather than the trust's beneficiaries) is entitled to a refundable tax offset if the NRAS refundable tax offset flows to this trust from another entity (because the trust is a party to

a non-entity joint venture, the trust is a partner of a partnership, or the trust is a beneficiary of another trust which has net income) and the trust to which the offset flows has no net income. Trustees assessable on net income of the trust are also entitled to a share of the offset.

1.7 The Consequential Bill also ensures that payments made by a state or territory department or agency are non-assessable and non-exempt income for taxation purposes. It also ensures that there are no CGT consequences from the receipt of incentives under the scheme.

Detailed explanation of new law

Refundable tax offset

1.8 An amendment is made to subsection 67-25(2A) of the ITAA 1997 by inserting a new subsection indicating that the tax offset available under Division 380 of the ITAA 1997 is subject to the refundable tax offset rules. This makes the tax offset under the NRAS a refundable tax offset. *[Schedule 1, item 5, subsection 67-25(2A)]*

Claims made by individuals, companies and superannuation funds

1.9 An individual, corporate tax entity or a superannuation fund is entitled to claim a refundable tax offset provided that:

- the individual, corporate tax entity or superannuation fund has been issued with a certificate by the Housing Secretary under the NRAS; and
- the income year begins in the NRAS year to which the certificate relates.

[Schedule 1, item 7, subsection 380-5(1)]

1.10 The term **NRAS year** has the same meaning as in the National Rental Affordability Scheme Bill 2008 (ie, the period 1 July 2008 to 30 April 2009, or the period 1 May to 30 April each year commencing on 1 May 2009) *[Schedule 1, item 11, definition of 'NRAS year' in subsection 995-1(1)]*. The Housing Secretary means the Secretary of the Department that administers the NRAS *[Schedule 1, item 9, definition of 'Housing Secretary' in subsection 995-1(1)]*. Both these terms are used throughout the Consequential Bill.

1.11 The terms ‘individual’, ‘corporate tax entity’ and ‘superannuation fund’ are defined terms in section 995-1 of the ITAA 1997. The term **individual** means a natural person, while the term ‘superannuation fund’ has the same meaning as section 10 of the *Superannuation Industry (Supervision) Act 1993*. An entity is a **corporate tax entity** if the entity is a company, corporate limited partnership, corporate unit trust or a public trading trust at a particular point in time. Generally speaking, a not-for-profit organisation is likely to be a corporate tax entity. The Consequential Bill does not amend any of these definitions.

1.12 The amount of the refundable tax offset the individual, corporate tax entity or superannuation fund is entitled to claim in their annual income tax return is the amount stated in the certificate. [*Schedule 1, item 7, subsection 380-5(2)*]

Example 1.1

If the NRAS certificate is issued in June 2010 relating to the NRAS year ending 30 April 2010, the taxpayer’s income year is 1 July to 30 June and the taxpayer is a superannuation fund, then the amount in the certificate is the amount the superannuation fund claims in their tax return for the 2009-2010 income year.

1.13 The Housing Secretary may issue an amended certificate to the individual, corporate tax entity or a superannuation fund. If this occurs, then the amount of the refundable tax offset is the amount stated in the amended certificate. This means that the taxpayer will need to apply for an amended assessment with the Australian Taxation Office. [*Schedule 1, item 7, subsection 380-5(3)*]

Claims by a party to a non-entity joint venture

1.14 Circumstances may arise where an individual, a corporate tax entity, or a superannuation fund is a party to a non-entity joint venture. In this circumstance, these entities are entitled to claim a refundable tax offset provided that:

- NRAS rent is derived by the party to a non-entity joint venture in relation to the rental dwelling for an income year;
- the non-entity joint venture has been issued with a certificate by the Housing Secretary under the NRAS; and
- the income year begins in the NRAS year to which the certificate relates.

[*Schedule 1, item 7, subsections 380-10(1) and (3)*]

1.15 The amount of the refundable tax offset per dwelling that the individual, corporate tax entity, or superannuation fund who is a party in a non-entity joint venture is entitled to claim is the amount stated in the certificate for the rental dwelling apportioned by the NRAS rent derived by the entity from the dwelling for the income year and the total NRAS rent derived from the rental dwelling for the income year [*Schedule 1, item 7, subsection 380-10(4)*]. Generally speaking, it is likely that the ratio of the NRAS rent derived by the entity from the dwelling for the income year and the total NRAS rent derived from the rental dwelling for the income year will be one (because a participant in a non-entity joint venture will commonly be renting particular dwellings for NRAS rent exclusively of any other participants). If this is the case, the amount of the refundable tax offset per dwelling will be the amount stated in the certificate. The amounts per dwelling are summed to work out the total amount of the entity's (ie, the individual's, corporate tax entity's, or superannuation fund's) refundable tax offset. [*Schedule 1, item 7, subsection 380-10(2)*]

1.16 The term *non-entity joint venture* is a defined term in section 995-1 of the ITAA 1997. It means a contractual arrangement under which two or more parties undertake an economic activity that is subject to the joint control of the parties, and this arrangement is entered into to obtain individual benefits for the parties, in the form of a share of the output of the arrangement rather than joint or collective profits for all the parties. The term *derive* is also defined in section 995-1 of the ITAA 1997. The Consequential Bill does not amend these definitions.

1.17 The term *NRAS rent* is defined as the rent derived in respect of a rental dwelling from renting it on an affordable housing basis under the NRAS for an income year [*Schedule 1, item 11, definition of 'NRAS rent' in subsection 995-1(1)*]. This term is also used in sections 380-15 to 380-30.

1.18 Another circumstance is where a partnership or a trust is a party to a non-entity joint venture. In this circumstance, the partnership or trust is deemed to have been issued with the certificate for its income year which begins in the NRAS year, the rental dwellings covered by the certificate are those for which the partnership or trustee has derived NRAS rent and the amount in the certificate is the total of all the amounts worked out in relation to those rental dwellings as set out in subsection 380-10(4). The trust or partnership would then apply the framework set out in section 380-15 so that the refundable tax offset can flow through to the partners or beneficiaries receiving the NRAS rent indirectly (see below). Alternatively, if a trust has no net income, then section 380-20 will apply enabling the trustee to claim the refundable tax offset. [*Schedule 1, item 7, subsection 380-10(5)*]

Example 1.2

Assume that a non-entity joint venture comprises Company A having an interest in 70 dwellings (and receiving \$70,000 in rental income) and XYZ Trust having an interest in 30 dwellings (and receiving \$30,000 rental income). The Housing Secretary issued the non-entity joint venture a certificate in June 2010 relating to the NRAS year ending 30 April 2010 stating that the refundable tax offset is \$600,000.

Company A is entitled to claim a refundable tax offset of \$420,000 (ie, the aggregate amount of the formula in subsection 380-10(4): $\$600,000 \times (\$70,000 / \$100,000)$). This is claimable in its income year that begins in the NRAS year ending 30 April 2010.

XYZ Trust is not entitled to claim the tax offset using subsections 380-10(1) and (2) because it is not an individual, a corporate tax entity or a superannuation fund. However, subsection 380-10(5) deems for the purposes of applying section 380-15 the amount stated in the certificate referred to in the formula in subsection 380-15(4) to be the amount worked out under subsection 380-10(4). This amount is \$180,000 (ie, the aggregate amount of the formula in subsection 380-10(4): $\$600,000 \times (\$30,000 / \$100,000)$).

1.19 The Housing Secretary may issue an amended certificate to the non-entity joint venture in relation to a rental dwelling. If this occurs, then the amounts worked out under subsection 380-10(4) will need to be recalculated using the amended amount. As a result, the parties to a non-entity joint venture may need to apply for an amended assessment with the ATO. [*Schedule 1, item 7, subsection 380-75(3)*]

Claims made by entities who receive the tax offset indirectly

Background

1.20 Circumstances may arise where the certificate is issued under the NRAS to an entity (or is treated as being so issued) but the refundable tax offset is claimed by another entity. An example of this is where the certificate is issued to a trustee of a trust, and the refundable tax offset needs to be claimed by the beneficiaries of the trust rather than the trustee (although in some circumstances it is available to the trustee rather than to the beneficiaries). Another example is where the certificate is issued to a partnership, and the refundable tax offset needs to be claimed by the partners in the partnership.

1.21 Reflecting these circumstances, the Consequential Bill sets out a framework to enable entities that are indirect recipients of the NRAS rent to claim the NRAS refundable tax offset. This effectively allows for the

refundable tax offset to flow directly to those entities. This framework is based broadly on the current framework where a franking credit flows indirectly to an entity.

1.22 The principle is that an entity is entitled to claim its share of the refundable tax offset consistent with its share of rental income from its participation in the NRAS through trusts or partnerships. The rationale is that taxpayers should be entitled to the refundable tax offset if they receive a lesser amount of rental income from renting the dwellings out at 20 per cent below market rate. This ensures that only those entities participating in the NRAS, whether directly or indirectly through a trust, partnership or non-entity joint venture, are entitled to the refundable tax offset. Conversely, it ensures that those entities not participating in the NRAS by renting dwellings to NRAS tenants, whether directly or indirectly through a trust, partnership or non-entity joint venture, are not entitled to the refundable tax offset.

Claims by certain entities to whom NRAS rent flows indirectly

1.23 An entity that indirectly derives NRAS rent from a rental dwelling, as a partner of a partnership or as the trustee or a beneficiary of a trust is entitled to claim the refundable tax offset provided that:

- the trust or partnership which directly receives the rental income has been issued with a certificate by the Housing Secretary under the NRAS applicable to the dwelling; and
- the income year of that trust or partnership begins in the NRAS year to which the certificate relates.

[Schedule 1, item 7, subsection 380-15(1)]

1.24 The entity indirectly receiving the NRAS rent may be:

- an individual;
- a corporate entity (at the time the NRAS rent flows indirectly to it);
- the trustee of a trust that is liable to be assessed on a share of, or all or a part of, the trust's net income under section 98, 99 or 99A of the *Income Tax Assessment Act 1936* (ITAA 1936) for that income year;
- the trustee of a First Home Saver Account; or

- a superannuation fund, an approved deposit fund, or a pooled superannuation trust.

[Schedule 1, item 7, paragraph 380-15(1)(a)]

1.25 There are two observations that should be made about section 380-15. The first is that a beneficiary of a trust cannot receive NRAS rent indirectly in any year that the trust of which they are a beneficiary has no net income. In the circumstance where a trust has no net income, the trustee of such a trust may be able to claim the refundable tax offset under section 380-20.

1.26 Secondly, the NRAS rent flowing indirectly to the entity referred to in subsection 380-15(1) may be derived by the trust or partnership through which the NRAS rent ultimately flows (ie, the ‘top entity’) in an earlier income year than the income year in which the entity is entitled to the refundable tax offset (ie, the income year in which the entity is assessable on their share of the NRAS rent). This circumstance is contemplated by paragraph 380-15(1)(c), which identifies the income year of the top entity as the income year which begins in the NRAS year to which the certificate relates. NRAS years end on 30 April, before the end of the financial year on 30 June and may also not match an entity’s income year where that differs from the financial year. This point also applies to paragraph 380-20(1)(e) relating to the circumstance where the trustee of a trust can claim the refundable tax offset.

1.27 The amount of the refundable tax offset that the partner or beneficiary is entitled to claim is equal to the amount stated in the certificate apportioned by the partner’s or beneficiary’s share of NRAS rent derived from a dwelling for the income year and the total NRAS rent derived from rental dwellings covered by the certificate for the relevant income year *[Schedule 1, item 7, subsection 380-15(2)]*. While the numerator in the formula in subsection 380-15(2) refers to the entity’s share of NRAS rent for the dwelling, the formula obtains the same total result whether it is worked out per dwelling or in respect of total dwellings in the numerator.

1.28 The Housing Secretary may issue an amended certificate to the partnership or the trustee of a trust which receives the certificate. If this occurs, then the amount of the refundable tax offset in respect of the dwelling is the amount stated in the amended certificate. This means that the entities indirectly receiving NRAS rent will need to apply for an amended assessment with the ATO, because the claim is a share of the amount in the certificate. *[Schedule 1, item 7, subsection 380-15(3)]*

When NRAS rent flows indirectly to an entity

1.29 NRAS rent is taken to flow indirectly in an income year to a partner in a partnership or to a beneficiary of a trust or the trustee of a trust if:

- the NRAS rent is derived by the partnership or trustee of the trust, or flows indirectly to the partnership or to the trustee as a partner or beneficiary [*Schedule 1, item 7, paragraphs 380-25(2)(a), (3)(a) and (4)(a)*]; and
- one of the following conditions is satisfied:
 - the partner has an individual interest in the partnership’s net income for that year or is allowed a deduction for the partnership’s loss for that year under subsections 92(1)(a) or (b) and 92(2)(a) or (b) of the ITAA 1936 [*Schedule 1, item 7, paragraph 380-25(2)(b)*];
 - the beneficiary has a share of the trust’s net income for that year to which paragraph 97(1)(a) of the ITAA 1936 applies, or an individual interest in the trust’s net income for that year to which section 98A or 100 of the ITAA 1936 apply [*Schedule 1, item 7, paragraph 380-25(3)(b)*]; or
 - the trustee is liable to be assessed on a share of the trust’s net income in respect of a beneficiary under section 98 of the ITAA 1936, or assessed on all or part of the trust’s net income for that year under section 99 or 99A of the ITAA 1936 [*Schedule 1, item 7, paragraph 380-25(4)(b)*]; and
- the entity’s share of the NRAS rent as calculated in new section 380-30 is a positive amount (ie, the entity must have an entitlement to part or all of the NRAS rent) [*Schedule 1, item 7, paragraphs 380-25(2)(c), (3)(c) and (4)(c)*].

1.30 NRAS rent will be taken to flow indirectly to a beneficiary of a trust, or to the trustee of that trust, but the same NRAS rent cannot be taken to flow to both, because the conditions in paragraphs 380-25(3)(b) and (4)(b) are mutually exclusive.

NRAS rent flowing indirectly through an entity

1.31 For the purposes of working out an entity’s share of NRAS rent, it is also necessary to describe where NRAS rent flows indirectly through an entity. This occurs where there is an entity (intermediary entity) and

the NRAS rent flows through that entity to another entity (the focal entity) [Schedule 1, item 7, subsection 380-25(5)]. These terms are used in the table in subsection 380-30(3) to determine an entity's share of the NRAS rent where it flows indirectly.

The entity's share of NRAS rent

1.32 The concept of an entity's share of NRAS is set out in section 380-30. The entity's share of NRAS rent is taken to be a notional share because an entity may not actually derive its share of NRAS rent (ie, the concept is defined so that it is undiminished by deductions of the partnership or trustee of a trust in which the entity is a partner or a beneficiary or through which the NRAS rent flows). [Schedule 1, item 7, subsections 380-30(1) and (2)]

1.33 An entity's share of NRAS rent is determined under the table in subsection 380-30(3). This calculation is used to determine the entity's share of the NRAS rent where the NRAS rent flows indirectly to the entity. A focal entity's share of NRAS rent is calculated by referring to the share of the intermediary entity's share of the NRAS rent to which the intermediary entity is entitled. Column 2 in the table provides the intermediary entity's share and column 3 in the table provides the focal entity's share. The table operates so that an entity's share of NRAS rent can be calculated where the distribution flows indirectly:

- to a partner in a partnership, or to a beneficiary or trustee of a trust, where the partnership or trustee derives the NRAS rent; or
- to a partner in a partnership, or to a beneficiary or the trustee of a trust, where NRAS rent flows indirectly to the partnership or trustee through a chain of trusts or combination of trusts and partnerships.

1.34 An entity's share of NRAS rent is its share of the NRAS rent as the focal entity in column 3 of an item in the table. [Schedule 1, item 7, subsection 380-20(3)]

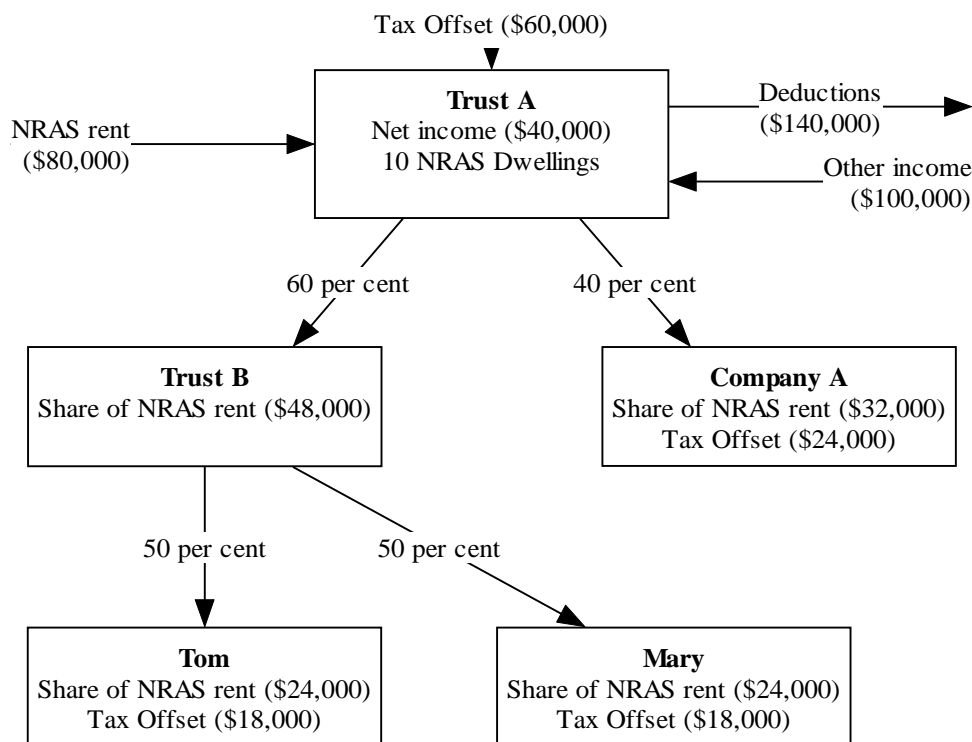
1.35 In the case of a trust, the table operates so that if deductions exceed assessable income (ie, the trust has no net income), there can be no amount which flows indirectly to a beneficiary or through it to another entity. [Schedule 1, item 7, column 2 in item 3 in the table in subsection 380-30(3)]

Example of claims made by a beneficiary of a trust who receives the NRAS rent indirectly

1.36 The following provides an example of the above framework in the case where the Housing Secretary issues a certificate to a trust and one of the beneficiaries of this trust is also a trust.

Example 1.3

Scenario



The following scenario is assumed (as illustrated in the diagram above):

- The top entity is a trust (called Trust A) and Trust A has two beneficiaries — Trust B which is entitled to 60 per cent of Trust A's income and Company A which is entitled to 40 per cent of Trust A's income. The beneficiaries of Trust B are two individuals (Tom and Mary) who are presently entitled to an equal share of the income of Trust B.
- Trust A holds 10 dwellings under the NRAS.
- All the entities income years are 1 July to 30 June. The income year is 2010-11.

- Trust A derives \$80,000 in NRAS rent and \$100,000 in income unrelated to Trust A's participation in NRAS, and claims \$140,000 deductions. This means that Trust A's net income is \$40,000, and Trust B's paragraph 97(1)(a) of the ITAA 1936 amount is \$24,000 (ie, 60 per cent of \$40,000) and Company A's paragraph 97(1)(a) amount is \$16,000 (ie, 40 per cent of \$40,000).
- Trust B's only assessable income is its \$24,000 entitlement referred to above. It has no tax deductions.
- The Housing Secretary issues a certificate to Trust A on 15 June 2011 stating that the refundable tax offset relating to Trust A's participation in the NRAS is \$60,000 for the NRAS year ending 2011.

The implications of this scenario are as follows.

Implications for Company A

- NRAS rent is taken to flow indirectly to Company A. This is because the conditions in subsection 380-25(3) are satisfied.
- Company A's share of the NRAS rent is \$32,000 (calculated under column 3 of item 3 in the table in subsection 380-30(3)). On an aggregate basis, this is the numerator of the fraction in the formula in subsection 380-15(2).
- Total NRAS rent derived by Trust A is \$80,000. This is the denominator of the fraction in the formula in subsection 380-15(2).
- Consequently, the amount of Company A's refundable tax offset is \$24,000 (ie, $\$60,000 \times (\$32,000 / \$80,000)$). This outcome is the result of applying the formula in subsection 380-15(2) (on an aggregate basis).

Implications for Trust B

- NRAS rent flows indirectly to Trust B. This is because the conditions in subsection 380-25(3) are satisfied.
 - It is noted that Trust B has a subparagraph 97(1)(a)(i) amount of \$24,000. This is because it is presently entitled to 60 per cent of income of Trust A and therefore 60 per cent of Trust A's \$40,000 net income even though, as a trustee, it does not pay tax on that amount. Moreover, Trust B is not entitled to an offset because it is not assessed under section 98, 99 or 99A of the ITAA 1936 (see subparagraph 380-15(1)(a)(iii)).

Implications for Tom and Mary

- NRAS rent is taken to flow indirectly through Trust B. This is because, in terms of subsection 380-25(5), Tom and Mary are the focal entities referred to in item 4 in the table in subsection 380-30(3) (see below) and their share of the NRAS rent is based on Trust B's share as an intermediary.
- NRAS rent is taken to flow indirectly to Tom. This is because the NRAS rent flows indirectly to Trust B (see above) and Tom, being presently entitled to 50 per cent of the income of Trust B, has a paragraph 97(1)(a) amount of 50 per cent of the \$24,000 net income of Trust B (ie, \$12,000), and his share of the NRAS rent is a positive amount (see below). As a result, the conditions in subsection 380-25(3) are satisfied.
- As explained above, the intermediary entity is Trust B and the focal entity is Tom for the purposes of section 380-30. The relevant item in the table in subsection 380-20(3) is item 4. Under column 3 of that item, \$24,000 of the amount worked out under column 2 (namely \$48,000, being Trust B's share of the NRAS rent, as calculated under column 3 of item 3 in the table — effectively 60 per cent of the \$80,000 NRAS rent derived by Trust A) is attributable to Tom, having regard to his 50 per cent share of Trust B's income (including the income attributable to the NRAS rent that flows indirectly to Trust B). In other words, Tom's share of the NRAS rent is \$24,000.
- Consequently, the amount of Tom's refundable tax offset is (on an aggregate basis) \$18,000 (ie, $\$60,000 \times (\$24,000 / \$80,000)$). This outcome is the result of applying the formula in subsection 380-15(2).
- Mary would work out her offset in the same way.

1.37 The above framework operates in an equivalent way if the top entity is a partnership.

1.38 An important implication of this framework is that three pieces of information need to pass down the chain. This information is the amount in the certificate, the entity's share of NRAS rent for the income year on an aggregate basis, and the total NRAS rent derived by the dwellings covered by the certificate for the income year. Taking the above example, Trust B needs this information to work out the amount of Tom's and Mary's refundable tax offset.

Claims by the trustee of a trust

1.39 Claims by the trustee of a trust indirectly entitled to NRAS rent can be made for the offset generally only in years that the trust has net income. Section 380-20 addresses the circumstance where a trust has no net income. This section operates by assuming that the trust has net income. In particular, a trustee of a trust is entitled to the NRAS refundable tax offset if the following conditions are satisfied:

- the trust does not have net income for the income year;
- NRAS rent for a rental dwelling would, on the assumptions stated in paragraph 380-20(1)(c), otherwise flow indirectly to the trustee of the trust;
- the Housing Secretary has issued a trust or a partnership with a certificate under the NRAS; and
- the income year of the trust or partnership that derived the NRAS rent begins in the NRAS year to which the certificate relates.

[Schedule 1, item 7, subsection 380-20(1)]

1.40 If the trustee of a trust is entitled to a refundable tax offset under subsection 380-20(1), a beneficiary of this trust, or a subsequent entity to whom the NRAS rent flows indirectly, is not entitled to the refundable tax offset. *[Schedule 1, item 7, subsection 380-20(4)]*

1.41 The amount of the refundable tax offset that the trustee of the trust is entitled to claim is the trust's relevant share of the amount stated in the certificate. This share is worked out in accordance with the formula in subsection 380-15(2) and is based on the assumption that the trust has net income. *[Schedule 1, item 7, subsection 380-20(2)]*

Example 1.4

ABC Trust has participated in the NRAS scheme and has received \$80,000 in rental income for the 2009-10 income year and no other income. The NRAS certificate is issued in June 2010 relating to the NRAS year ending 30 April 2010. The Housing Secretary issued the trustee of the ABC Trust with a certificate stating that the refundable tax offset is \$480,000. ABC Trust's income year ends on 30 June. For the 2009-10 income year, the ABC Trust has tax deductions of \$200,000.

ABC Trust has two beneficiaries, Trust B and Trust C. Trust B also has no net income for the 2009-10 income year.

Implications for the trustee of ABC Trust

- Section 380-20 provides that the trustee of ABC Trust will be entitled to the offset as ABC Trust does not have any net income for the income year and the other requirements in subsection 380-20(1) are satisfied.
- The amount of the tax offset is still worked out in accordance with the formula in subsection 380-15(2).
- In order to work out the offset amount the trustee will have to assume that ABC Trust did have net income and that the trustee had a share amount for the purposes of subsection 380-25(4) which equals the deemed net income of the trust.
- Using these assumptions, the trustee's share of the NRAS rent is determined under column 3 of item 3 in the table in subsection 380-30(3) as being \$80,000. This is because \$80,000 of the NRAS rent derived by ABC Trust would be taken into account in working out the deemed share amount (being the whole of the deemed net income).
- Therefore the amount of refundable tax offset is \$480,000 (ie, the aggregate amount of the formula in subsection 380-15(2): $\$480,000 \times (\$80,000 / \$80,000)$).
- The trustee will claim the offset in their 2009-10 income year.

Implications for Trust B and Trust C

- The trustee of ABC Trust is entitled to the offset. Therefore, neither Trust B nor Trust C would be entitled to claim the offset despite Trust B having no net income itself (see subsection 380-20(4)).

1.42 The Housing Secretary may issue an amended certificate. If this occurs, then the amount of the refundable tax offset in respect of a dwelling is determined by reference to the amended certificate. This means that the trustee of the trust will need to apply for an amended assessment with the ATO, because the trustee's entitlement is worked out by reference to the certificate. [*Schedule 1, item 7, subsection 380-5(1)*]

Exclusion of entitlements to NRAS incentives from capital gains tax

1.43 The Consequential Bill amends the ITAA 1997 to ensure that there are no CGT consequences arising from the provision to taxpayers of incentives or other benefits under the NRAS.

1.44 A capital gain or capital loss may arise from a CGT event happening to an entitlement to receive incentives from the Australian Government, or from state or territory governments, in relation to the NRAS. The application of CGT to these entitlements is inappropriate as it would reduce or remove the benefit that the incentives are intended to provide.

1.45 Consequently, the Consequential Bill inserts paragraph 118-37(1)(h) into the ITAA 1997 to disregard a capital gain or capital loss relating to an NRAS incentive a taxpayer claims under the ITAA 1997 as a tax offset. *[Schedule 1, item 6, paragraph 118-37(1)(h)]*

1.46 In addition, the Consequential Bill inserts paragraph 118-37(1)(i) in the ITAA 1997 to disregard a capital gain or capital loss relating to a variation, transfer or revocation of an allocation under the NRAS. Under the current CGT provisions, the sale of a dwelling, for example, in relation to which there is an allocation for NRAS incentives would trigger a CGT event in relation to the allocation. *[Schedule 1, item 6, paragraph 118-37(1)(i)]*

1.47 The Consequential Bill also inserts paragraph 118-37(1)(j) into the ITAA 1997 to disregard a capital gain or capital loss in relation to anything of economic value provided to a taxpayer by a department of a state or territory, or by certain bodies such as local government entities, in relation to their participation in the NRAS. For example, the provision would disregard any capital gain or capital loss arising from a payment, grant or subsidy or from a reduction of a liability, such as stamp duty, relating to a taxpayer's participation in the NRAS. *[Schedule 1, item 6, paragraph 118-37(1)(j)]*

1.48 The CGT provisions require an adjustment to the cost base and reduced cost base of a CGT asset when there is a recoupment of expenditure (eg, see subsection 110-40(3) of the ITAA 1997). These recoupment of expenditure provisions do not apply where a benefit under the NRAS is received as the relevant incentive is not received in respect of a loss or outgoing as required by subsection 20-25(1) of the ITAA 1997.

Contributions made by state or territory governments

1.49 Part of the assistance being provided under the NRAS comprises of grants or in-kind benefits provided by state and territory governments to the value of at least \$2,000. The Consequential Bill makes an amendment to the ITAA 1997 to ensure that such assistance is non-assessable non-exempt income for income tax purposes. This ensures that the after-tax treatment of assistance provided by state and territory

governments is equivalent to the refundable tax offset. [*Schedule 1, item 7, section 380-35*]

Consequential amendments

1.50 The Consequential Bill makes the following consequential amendments:

- Section 11-55 of the ITAA 1997 lists payments which are non-assessable non-exempt income under various provisions of the ITAA 1936 and the ITAA 1997. A consequential amendment is made to include payments, or non-cash benefits, made by a government in relation to participation in the NRAS in the list of payments which are non-assessable non-exempt income [*Schedule 1, item 1, section 11-55*].
- Section 13 of the ITAA 1997 lists tax offsets under various provisions of the ITAA 1936 and the ITAA 1997. A consequential amendment is made to add a reference to the NRAS and appropriate cross references in respect of partnerships and trusts [*Schedule 1, items 2 to 4, section 13-1*].
- Section 955-1 defines the term ‘flows indirectly’. References are added to this definition indicating that subsections 380-25(2) to (4) set out the circumstances where NRAS rent flows indirectly to an entity, and subsection 380-25(5) sets out the circumstances where NRAS rent flows indirectly through an entity [*Schedule 1, item 8, definition of ‘flows indirectly’ in section 995-1*].
- The term ‘National Rental Affordability Scheme’ has been added to the definitions in section 995-1 of the ITAA 1997. This term is defined as having the same meaning as in the National Rental Affordability Scheme Bill 2008 [*Schedule 1, item 10, definition of ‘National Rental Affordability Scheme’ in section 995-1*].
- Section 995-1 of the ITAA 1997 defines the term ‘share’. An amendment is made to the effect that the share of NRAS rent has the same meaning as given by section 380-30 [*Schedule 1, items 13, definition of ‘share’ in section 995-1*].

Application and transitional provisions

1.51 The amendments in Schedule 1 to the Consequential Bill will apply to assessments for the 2008-09 income year and later income years. This approach is consistent with the application of other income tax amendments. *[Schedule 1, item 14]*

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Item 6, paragraph 118-37(1)(j)	1.47
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