2013-2014

THE PARLIAMENT OF THE COMMONWEALTH OF AUSTRALIA

HOUSE OF REPRESENTATIVES

TAX AND SUPERANNUATION LAWS AMENDMENT (2014 MEASURES No. 4) BILL 2014

EXPLANATORY MEMORANDUM

(Circulated by the authority of the  
Treasurer, the Hon J. B. Hockey MP)

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Glossary

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

|  |  |
| --- | --- |
| Abbreviation | Definition |
| ACNC | Australian Charities and Not-for-profits Commission |
| ACNC Act | *Australian Charities and Not-for-profits Commission Act 2012* |
| ADI | authorised deposit-taking institution |
| AFRSA Act | *Aviation Fuel Revenues (Special Appropriation) Act 1988* |
| CFC | controlled foreign company |
| CGT | capital gains tax |
| Commissioner | Commissioner of Taxation |
| Customs Act | *Customs Act 1901* |
| ETA | *Excise Tariff Act 1921* |
| GST | goods and services tax |
| GST Act | *A New Tax System (Goods and Services Tax) Act 1999* |
| IFRS | international financial reporting standards |
| ITAA 1936 | *Income Tax Assessment Act 1936* |
| ITAA 1997 | *Income Tax Assessment Act 1997* |
| MEC | multiple-entry consolidated group |
| MEC group | multiple-entry consolidated group |
| NANE | non-assessable non-exempt |
| non-ADI | not an authorised deposit-taking institution |
| non-TARP | assets that are not taxable Australian real property |
| TAA 1953 | *Taxation Administration Act 1953* |
| TARP | taxable Australian real property |
| TIES | Tax Issues Entry System |

General outline and financial impact

## Thin capitalisation and Foreign dividends

Schedule 1 to this Bill:

* tightens the debt limit settings in the thin capitalisation rules to ensure that multinationals do not allocate a disproportionate amount of debt to their Australian operations;
* increases the *de minimis* threshold to minimise compliance costs for small businesses; and
* introduces a new worldwide gearing debt test for inbound investors.

Schedule 2 to this Bill reforms the exemption for foreign non‑portfolio dividends.

Date of effect: Schedules 1 and 2 to this Bill commence on the day after Royal Assent. Schedule 1 to this Bill applies to income years commencing on or after 1 July 2014 and Schedule 2 to this Bill applies to distributions and non-share dividends made after the day the Bill receives Royal Assent.

Proposal announced: The Treasurer and Assistant Treasurer announced in a joint Media Release titled ‘Restoring integrity in the Australian tax system’ of 6 November 2013 that it would proceed with reforms to the thin capitalisation and foreign dividend rules to prevent erosion of the Australian tax base.

Financial impact: The changes to the thin capitalisation rules and the exemption for foreign non-portfolio dividends (Schedule 1 and 2 respectively) are expected to provide an increase in revenue of $755 million over the forward estimates period.

Human rights implications: Schedules 1 and 2 to this Bill do not raise any human rights issues. See *Statement of Compatibility with Human Rights* — Chapters 1 and 2, paragraphs 1.100 to 1.103 and 2.39 to 2.42 respectively.

Compliance cost impact: Low.

## Improving the integrity of the foreign residents capital gains tax regime

Schedule 3 amends the *Income Tax Assessment Act 1997* (ITAA 1997) to ensure that the foreign residents capital gains tax (CGT) regime operates as intended by preventing the double counting of certain assets under the Principal Asset Test. A technical correction is also made to the meaning of ‘permanent establishment’ in section 855-15 of the ITAA 1997.

Date of effect: The amendments to the Principal Asset Test will apply to CGT events that occur to different entities on:

* 7.30pm on 14 May 2013; and
* 13 May 2014.

The technical correction to section 855-15 will apply from the commencement of Division 855 (12 December 2006).

These changes are of a technical nature and do not affect any other aspect of the definition of taxable Australian property. They do not negatively affect any taxpayer because the scope of the definition of taxable Australian property aligns with the intention of the original provisions.

Proposal announced: The Principal Asset Test amendments were announced on 14 May 2013. The technical correction was announced on 26 May 2014.

Financial impact: The amendments to the Principal Asset Test are expected to raise an additional $10 million per annum from 2014-15:

|  |  |  |  |
| --- | --- | --- | --- |
| 2013-14 | 2014-15 | 2015-16 | 2016-17 |
| Nil | $10 million | $10 million | $10 million |

The technical correction to the meaning of ‘permanent establishment’ does not have a financial impact as it fixes a technical defect in the legislation in order to align with the existing policy intent of the regime.

Human rights implications: This Schedule engages the right to equality and non-discrimination but does not raise any human rights concerns. See *Statement of Compatibility with Human Rights* — Chapter 3, paragraphs 3.72 to 3.76.

Compliance cost impact: The amendments will have a minor regulatory cost to foreign residents disposing of interests in ‘land rich’ entities.

## Personalised tax receipts

Schedule 4 to this Bill amends the tax law to provide greater transparency to taxpayers about how their tax money is spent, by requiring the Commissioner of Taxation to issue a tax receipt to individuals for the income tax assessed to them.

Date of effect: The amendments will apply with respect to assessments for the 2014-15 income year and future income years.

Proposal announced: The amendments give effect to a 2013 election commitment.

Financial impact: Nil. The Australian Taxation Office will absorb the costs of preparing the receipts.

Human rights implications: This Schedule engages the right to take part in the conduct of public affairs. See *Statement of Compatibility with Human Rights* — Chapter 4, paragraphs 4.11 to 4.15.

Compliance cost impact: Nil.

## Miscellaneous amendments

Schedule 5 to this Bill makes a number of miscellaneous amendments to the taxation and superannuation laws. These amendments are part of the Government’s commitment to the care and maintenance of the taxation and superannuation systems.

These amendments include style changes, the repeal of redundant provisions, and the correction of anomalous outcomes and corrections to previous amending Acts.

***Date of effect***: The amendments have various application dates that are explained in detail in this explanatory memorandum. While some of these amendments have retrospective application, taxpayers will not be adversely impacted.

***Proposal announced***: The amendments were announced in the 2014‑15 Budget.

***Financial impact***: These amendments are expected to have a minimal or nil revenue impact. However, some of the amendments are integrity measures that protect what could be significant amounts of revenue.

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| 2013-14 | 2014-15 | 2015-16 | 2016-17 | 2017-18 |
| Nil | .. | .. | .. | .. |

.. not zero, but rounded to zero

***Human rights implications***: This Schedule does not raise any human rights issue. See *Statement of Compatibility with Human Rights* — Chapter 5, paragraphs 5.117 to 5.120.

***Compliance cost impact***: Negligible.

1. Thin capitalisation

## Outline of chapter

* 1. Schedule 1 to this Bill tightens the statutory limit settings in the thin capitalisation rules to ensure that multinationals do not allocate a disproportionate amount of debt to their Australian operations. Schedule 1 also increases the *de minimis* threshold to minimise compliance costs for small businesses, and introduces a new worldwide gearing debt test for inbound investors.

## Context of amendments

* 1. The current thin capitalisation rules were introduced in 2001 following the Review of Business Taxation. It was intended to prevent multinationals from profit shifting by allocating a disproportionate amount of debt in their Australian operations, and claiming excessive debt deductions in Australia, thereby reducing their Australian taxable income. If the Australian operations are funded by excessive debt, they are said to be ‘thinly capitalised’.
  2. Multinationals have the commercial flexibility to determine where international financing can occur and how debt will be allocated within the group, through intra-group funding arrangements. This provides them with the opportunity to effectively choose the jurisdiction that deductions for interest are claimed in. For example, multinationals can allocate a greater proportion of debt to higher taxing jurisdictions where debt deductions are often more valuable. This behaviour can effectively reduce or negate Australian income tax while increasing after tax profits for the multinational group.
  3. The thin capitalisation rules operate by disallowing a proportion of otherwise deductible debt related expenses where the debt allocated to a multinational’s Australian operations exceeds certain limits (or where there is a capital shortfall in the case of authorised deposit-taking institutions (ADIs)). These limits are determined by reference to the greater of a ‘safe harbour’ debt amount, an ‘arm’s length’ debt amount and, currently for certain outbound investors, the ‘worldwide gearing’ debt amount. This does not prevent the Australian operations from assuming higher levels of debt; however, the debt deductions will be denied where the relevant statutory debt limits are exceeded. For ADIs (principally banks), the tests are framed as a minimum requirement for equity capital based on prudential regulatory requirements.
  4. Setting these statutory debt limits involve balancing a number of factors, including minimising unnecessary compliance costs for multinationals, ensuring that the debt limits do not impede the efficient allocation of capital, and maintaining the integrity of the revenue base.
  5. When first introduced, the statutory debt limits were intended to provide broad coverage to accommodate commercial gearing levels across a range of industries. While gearing practices vary, recent data suggests these limits are now higher than the normal gearing levels of most corporates with independent financing arrangements, which is often less than 1:1 on a debt-to-equity basis.
  6. The gap between the statutory debt limits and the actual gearing levels of most companies can have a distorting effect on debt allocation decisions for the Australian operations of domestic and foreign multinationals. It may encourage multinationals to allocate excessive debt to Australia for tax purposes, rather than for commercial reasons.
  7. To address this, the Government announced on 6 November 2013 that it would proceed with reforms to tighten the thin capitalisation limits. It also announced that it would increase the *de minimis* threshold to minimise compliance costs for small businesses, and introduce a new worldwide gearing debt test for inbound investors.

## Summary of new law

* 1. The thin capitalisation rules will be tightened to prevent erosion of the Australian tax base by:
* reducing the maximum statutory debt limit from 3:1 to 1.5:1 (on a debt-to-equity basis) for general entities and from 20:1 to 15:1 (on a debt-to-equity basis) for non-bank financial entities;
* reducing the ‘outbound’ worldwide gearing ratio from 120 per cent to 100 per cent with an equivalent adjustment to the worldwide capital ratio for ADIs; and
* increasing the safe harbour capital limit for ADIs from 4 per cent to 6 per cent of their risk weighted Australian assets.
  1. To minimise compliance costs for small businesses, the *de minimis* threshold for the thin capitalisation limits will be increased from $250,000 to $2 million of debt deductions.
  2. To provide greater flexibility for inward investing entities, a new ‘inbound’ worldwide gearing debt test will be introduced. This test imports the commercial limits of the financial markets to gearing, and mirrors market outcomes for businesses that, as a whole, have naturally higher gearing levels. This will provide a further option to inward investing entities, where they do not fall within the safe harbour limit, and do not meet the arm’s length debt test. To minimise compliance costs, this test will utilise the audited consolidated financial statements that are already required to be prepared by the worldwide parent entity.

Comparison of key features of new law and current law

| New law | Current law |
| --- | --- |
| The safe harbour debt limit for general entities (not an authorised deposit-taking institution (non-ADI)) is 1.5:1 on a debt-to-equity basis. | The safe harbour debt limit for general entities (non-ADI) is 3:1 on a debt-to-equity basis. |
| The safe harbour debt limit for financial entities (non-ADI) is 15:1 on a debt-to-equity basis. | The safe harbour debt limit for financial entities (non-ADI) is 20:1 on a debt-to-equity basis. |
| The safe harbour capital limit for an ADI is 6 per cent of its risk weighted Australian assets. | The safe harbour capital limit for an ADI is 4 per cent of its risk weighted Australian assets. |
| The worldwide debt limit for outward investing entities (non-ADI) allows the Australian operations, in certain circumstances, to be geared at up to 100 per cent of the gearing of the entity’s worldwide group. | The worldwide debt limit for outward investing entities (non-ADI) allows the Australian operations, in certain circumstances, to be geared at up to 120 per cent of the gearing of the entity’s worldwide group. |
| The worldwide capital amount for ADIs allows the entity’s Australian operations to be capitalised at 100 per cent of the capital ratio of the Australian entity’s worldwide group. | The worldwide capital amount for ADIs allows the entity’s Australian operations to be capitalised at 80 per cent of the capital ratio of the Australian entity’s worldwide group. |
| The *de minimis* threshold is debt deductions of $2 million or less. | The *de minimis* threshold is debt deductions of $250,000 or less. |
| A new worldwide gearing debt limit will be available to inward investing entities (and inward investment vehicles that are also outward investing), to be applied if the entity chooses, subject to an assets threshold. | There is currently no equivalent test. |

## Key concepts and summary of current framework

* 1. There are a number of statutory debt limits (or in the case of ADIs a capital limit) currently set out in Division 820 of the *Income Tax Assessment Act 1997* (ITAA 1997) (all section references are to the ITAA 1997 unless otherwise specified). These statutory limits vary depending on whether the entity is inward investing or outward investing, and the type of entity — general, financial or ADI.

### Outward and inward investing entities

* 1. Different statutory debt limit tests apply depending on whether an entity is an inward investing entity or an outward investing entity.
  2. An inward investing entity is a foreign controlled Australian resident entity, and any foreign entity that carries on business at or through an Australian permanent establishment, or has direct investments within Australia.
  3. An outward investing entity is an Australian resident entity that controls any foreign entity or carries on business at or through an overseas permanent establishment, and an Australian associate entity of another outward investor.

### ADI or non-ADI (general and financial)

* 1. An ADI is an authorised deposit-taking institution for the purposes of the *Banking Act 1959*.
  2. In the case of non-ADIs, debt deductions will be disallowed where the maximum allowable debt is exceeded. In the case of ADIs, debt deductions will be disallowed where the minimum capital requirement is not met.
  3. A non-ADI entity is further classified as being either a financial entity or a general entity. A financial entity is defined in section 995-1. A general entity is any entity that is neither a financial entity nor an ADI.

### Summary of current debt limits

#### Maximum allowable debt (non-ADI)

* 1. A taxpayer’s maximum allowable debt for both inward investing entities (non-ADI) and outward investing entities (non-ADI) is the greater of the following amounts:
* the safe harbour debt limit: different limits apply depending on whether the entity is a general entity or a financial entity; or
* the arm’s length debt limit: this limit seeks to benchmark commercial or independent debt outcomes.
  1. Outward investing entities (non-ADI) may also elect to apply the worldwide gearing debt limit, which allows gearing of the Australian operations based on the debt-to-equity ratio of the worldwide group.

#### Minimum capital amount (ADIs)

* 1. An ADI’s minimum capital amount for both inward and outward investing entities is the lesser of the following amounts:
* the safe harbour capital amount: this limit is based on the entity’s risk-weighted Australian assets; or
* the arm’s length capital amount: this limit seeks to benchmark what would be the minimum amount of equity capital required by the bank to undertake its Australian business.
  1. Outward investing entities (ADI) may also elect to apply the worldwide capital amount.

## Detailed explanation of new law

### Safe harbour debt limit (non-ADI)

* 1. The thin capitalisation rules, when first introduced, were intended to provide broad coverage to accommodate commercial gearing levels across a range of industries.
  2. However, the gearing ratio allowed in the safe harbour debt limits is now much higher than the normal gearing levels of most corporates with independent arrangements.
  3. To address this, the safe harbour debt limit for:
* outward investors (general);
* inward investors (general); and
* inward investment vehicles (general),

are reduced from 3:1 to 1.5:1 on a debt-to-equity basis.

[Schedule 1, Part 1, items 1, 3 and 5, method statements in sections 820-95, 820-195, and 820-205]

* 1. The safe harbour debt limit for:
* outward investors (financial);
* inward investors (financial); and
* inward investment vehicles (financial),

are reduced from 20:1 to 15:1 on a debt-to-equity basis.

[Schedule 1, Part 1, items 2, 4 and 6, method statements in subsections 820‑100(2), 820‑200(2), 820-210(2)]

* 1. The new safe harbour debt limit more closely aligns with commercial debt levels, and for financial entities the new safe harbour debt limit brings debt levels more closely into line with prudential standards as amended under Basel III.

### Safe harbour capital amount (ADIs)

* 1. In contrast to non-ADIs, the safe harbour capital test for ADIs is determined by reference to a minimum capital amount (rather than a maximum allowable debt). Debt deductions claimed by the ADI may be disallowed if the minimum capital requirement is not met.
  2. Under the current law, an inward investing ADI is required to have capital equal to 4 per cent of its Australian risk‑weighted assets. An outward investing ADI is subject to the same minimum requirement, but must also have capital to match certain other Australian assets.
  3. Under the new law, the safe harbour capital limit for inward and outward investing ADIs will be increased from 4 per cent to 6 per cent of their risk-weighted Australian assets. [Schedule 1, Part 4, items 15 to 17, method statement in subsections 820-310(1) and 820-615(3), and section 820-405]
  4. The ‘risk‑weighted assets’of the entity means the sum of the assessed risk exposures of assets as calculated in accordance with the prudential standards determined by the prudential regulator in the jurisdiction of the foreign bank or by the Australian Prudential Regulation Authority.

### Worldwide gearing debt limit for outward investing entities (non-ADI)

* 1. Currently, an outward investing entity (non-ADI) which is not also an inward investment vehicle may exceed the safe harbour debt amount without having debt deductions denied if it does not exceed the worldwide gearing debt amount.
  2. The effect of the worldwide gearing rule is to allow the Australian operations, in certain circumstances, to be geared at up to the level of the gearing of the Australian entity’s worldwide group.
  3. The worldwide gearing ratio applying to general and financial outward investors, will be reduced from 120 per cent of the gearing of the entity’s worldwide group to 100 per cent of the gearing of the entity’s worldwide group. [Schedule 1, Part 2, items 11 and 12, method statements in section 820‑110]
  4. For the purposes of this test, the gearing of the entity’s worldwide group is determined by reference to method statements contained in section 820-110.
  5. A new worldwide gearing debt test will also be introduced for inward investing entities (non-ADI). The new test is explained below.

### New worldwide gearing debt limit for inward investing entities (non-ADI)

* 1. The worldwide gearing debt test, currently only available to outward investing entities that are also not foreign controlled, will be extended to inward investing entities that are not an ADI [Schedule 1, Part 6]. The new test will also be available to an entity that is both an inward investment vehicle (non-ADI) and also an outward investing entity (non-ADI) [Schedule 1, Part 2, item 9, paragraph 820-90(2)(c)].
  2. This will provide further flexibility to inward investing entities (non-ADI) that do not meet the safe harbour test or the arm’s length debt test.
  3. Allowing a worldwide gearing debt test to be available to inward investing entities (non-ADI) also, in the typical case, better reflects the policy intent of the thin capitalisation rules to prevent the disproportionate allocation of debt to Australia for income tax purposes. This is achieved by allowing the Australian operations to claim deductions on their debt where they are geared to the same level as the global group.
  4. As a result, the new worldwide gearing debt test for inward investing entities (non-ADI) will provide greater flexibility by effectively importing the commercial considerations of financial markets to limit gearing in cases where the statutory safe harbour limits are exceeded.
  5. Under the new law, the maximum allowable debt for an inward investing entity (non-ADI) in an income year will be the greatest of the following amounts:
* the safe harbour debt amount;
* the arm’s length debt amount; or
* the worldwide gearing debt amount unless:
  + the entity’s statement worldwide equity, or statement worldwide assets is nil or negative;
  + audited consolidated financial statements do not exist; or
  + an assets threshold is satisfied.

[Schedule 1, Part 6, item 19, section 820-190]

#### Which types of entities can choose to apply the new test?

* 1. The new worldwide gearing debt test will be available to inward investing entities (non-ADI). That is, any of the following entities can choose to apply the new test, provided that certain requirements are met:
* inward investment vehicles (general);
* inward investment vehicles (financial);
* inward investors (general); and
* inward investors (financial).

[Schedule 1, Part 6, item 20, sections 820-216 to 820-219]

* 1. If an inward investment vehicle (non-ADI) is also an outward investing entity (non-ADI), then it can also choose to apply the new worldwide gearing debt test, provided that certain requirements are met. That is, the new worldwide gearing debt test will apply to:
* an entity that is an inward investing entity (non-ADI); and
* an entity that is both an inward investment vehicle (non-ADI) and also an outward investing entity (non‑ADI) (unless it is the head of a consolidated group or multiple-entry consolidated (MEC) group, in which case, the worldwide gearing debt test in section 820-110 for outward investing entities would apply).

[Schedule 1, Parts 2 and 6, items 9 and 19 respectively, paragraphs 820‑90(2)(c) and 820-190(1)(c)]

* 1. This ensures that an entity that is both an inward investment vehicle and an outward investing entity has access to the new inbound worldwide gearing debt test, as they cannot use the existing outbound worldwide gearing debt test under subsection 820-90(2) (other than the head of a consolidated or MEC group).
  2. An entity cannot use the new worldwide gearing debt test unless it satisfies an assets threshold. Broadly, this threshold requires that the entity’s Australian assets represent no more than 50 per cent of the consolidated group’s worldwide assets.
  3. That is, if the result of the following formula is greater than 0.5, the entity is not eligible to apply the new worldwide gearing debt test:
  4. The intention of this asset threshold is to ensure that the thin capitalisation rules remain effective. Where the entity’s Australian assets are greater than 50 per cent of the consolidated group’s worldwide assets, the Australian operations can drive the worldwide gearing levels of the worldwide group. For this reason, a maximum threshold level of 50 per cent of Australian assets is considered appropriate to access the new worldwide gearing debt test.
  5. The assets threshold test removes access to the worldwide gearing debt test for high gearing structures, such as private equity investment schemes, where a foreign entity with high levels of related party debt (often provided by shareholders) acquires an Australian target company, being the worldwide group’s main asset.
  6. The numerator (‘average Australian assets’ of the entity) is calculated as follows:
* For inward investment vehicles that are also outward investing entities, the average Australian assets of the entity is the average value of all the assets of the entity, other than:
  + any assets attributable to the entity’s overseas permanent establishments;
  + any debt interests held by the entity, to the extent to which any value of the interests is all or a part of the controlled foreign entity debt of the entity; or
  + any equity interests or debt interests held by the entity, to the extent to which any value of the interests is all or a part of the controlled foreign entity equity of the entity.

[Schedule 1, Part 2, item 9, subsection 820-90(3)]

* For inward investment vehicles that are not also outward investing entities, the average Australian assets of the entity is the average value of all the assets of the entity, other than:
  + any debt interests held by the entity, to the extent to which any value of the interests is all or a part of the controlled foreign entity debt of the entity; or
  + any equity interests or debt interests held by the entity, to the extent to which any value of the interests is all or part of the controlled foreign entity equity of the entity.

[Schedule 1, Part 6, item 19, section 820-190, paragraph (a) of the definition of average Australian assets]

* For inward investors, the average Australian assets of the entity is the average value of all the assets of the entity that are:
  + located in Australia;
  + attributable to the entity’s Australian permanent establishments;
  + debt interests held by the entity, that were issued by an Australian entity and are on issue; and
  + equity interests held by the entity, in an Australian entity.

[Schedule 1, Part 6, item 19, paragraph 820-190(2)(c), paragraph (b) of the definition of average Australian assets]

* 1. The denominator (‘statement worldwide assets’) is the amount of assets shown in the audited consolidated financial statements referred to in section 820-935. These financial statements must, among other things, be the consolidated financial statements of the worldwide parent entity, comply with specified accounting standards, and be audited (see paragraphs 1.69 to 1.88 below for a further explanation about these requirements).
  2. It is relevant to note that the numerator is calculated using Australian tax concepts (based on the definition of average Australian assets currently contained in section 820-37, with modifications) and the denominator is calculated using audited consolidated financial statements prepared in accordance with accounting concepts (which are relied upon further for the purposes of the applying the new worldwide gearing debt test — see below). These amounts have been chosen to provide an indicative assessment of the relative Australian to global assets of the group whilst minimising the compliance costs of applying the asset threshold test for the worldwide gearing debt test.
  3. Pragmatically, it will be necessary to identify the period that the audited consolidated financial statements relate to and then calculate the average Australian assets for that same period, to ensure that both the numerator and denominator apply in relation to the same period [Schedule 1, items 9 and 19, subsections 820-90(4) and 820-190(3)]. Further, both the numerator and denominator must be expressed in Australian dollars.

JMP is an overseas hedge fund which has investments in several countries, including Australia. JMP’s average Australian assets (which are calculated using Australian tax law) are $3 billion, and its statement worldwide assets (which are calculated using the specified audited consolidated financial statements) are $10 billion. As JMP’s asset threshold ratio is 0.30, it is eligible to use the new worldwide gearing debt test for inward investing entities (provided that its statement worldwide equity is a positive amount).

MRP is an overseas private equity fund that has investments in several countries, including Australia. MRP’s average Australian assets (which are calculated using Australian tax law) are $3 billion, and its statement worldwide assets (which are calculated using the specified audited consolidated financial statements) are $4 billion. As MRP’s asset threshold ratio is greater than 0.50, it is not eligible to use the new worldwide gearing debt test for inward investing entities. MRP will need to apply either the ‘safe harbour’ debt test or the ‘arm’s length’ debt test, to determine whether any debt deductions will be denied.

* 1. The asset threshold test is supported by an integrity rule that is intended to ensure that the asset threshold test is not circumvented.  The purpose of the rule is to prevent scenarios where an entity might acquire, hold or otherwise deal with its statement worldwide assets in a way that increases the amount of its worldwide assets for the purpose of circumventing the asset threshold test.  The rule ensures that such actions or arrangements undertaken with a purpose, other than an incidental purpose, of inflating the amount of an asset included in the statement worldwide assets will result in that inflated amount being disregarded.
  2. This means that the amount of the statement worldwide assets of the entity for the income year is reduced by the inflated amount where the asset was held, acquired or otherwise dealt with for a purpose, other than an incidental purpose, of avoiding the application of the asset threshold test.

#### Is the new test mandatory to apply?

* 1. An inward investing entity does not need to apply the new test. For example, if an inward investing entity applies the relevant safe harbour debt limit and determines that it has not exceeded its maximum allowable debt, then it does not need to also apply the new worldwide gearing debt test.

#### How does the new test work?

* 1. The calculation of the worldwide gearing debt amount differs depending on the type of entity:
* For an inward investor (general), the worldwide gearing debt amount is calculated using the steps outlined in paragraph 1.57 (also see section 820-218).
* For an inward investor (financial), the worldwide gearing debt amount is calculated using the steps outlined in paragraph 1.58 (also see section 820-219).
* For an inward investment vehicle (general) that is not also an outward investing entity, the worldwide gearing debt amount is calculated using the steps outlined in paragraph 1.59 (also see section 820-216).
* For an inward investment vehicle (financial), that is not also an outward investing entity, the worldwide gearing debt amount is calculated using the steps outlined in paragraph 1.60 (also see section 820-217).
* For an inward investment vehicle (general) that is also an outward investing entity (general), the worldwide gearing debt amount is calculated using the steps outlined in paragraph 1.62 (also see subsection 820-211(1)).
* For an inward investment vehicle (financial) that is also an outward investing entity (financial), the worldwide gearing debt amount is calculated using the steps outlined in paragraph 1.64 (also see subsection 820-211(2)).
* For an outward investing entity (non-ADI), that is also not an inward investment vehicle (general or financial), the worldwide gearing debt amount continues to be calculated under section 820‑110.
  1. For an entity that is an inward investor (general), the worldwide gearing debt amount is calculated as follows:

Step 1: Divide the entity’s statement worldwide debt for the income year by the entity’s statement worldwide equity for that year (see further below for an explanation of statement worldwide debt and statement worldwide equity).

Step 2: Add 1 to the result of step 1.

Step 3: Divide the result of step 1 by the result of step 2.

Step 4: Multiply the result of step 3 above by the result of step 4 in the method statement in section 820-205.

Step 5: Add to the result of step 4 the average value, for that year, of the entity’s associate entity excess amount. The result of this step is the worldwide gearing debt amount.

[Schedule 1, Part 6, item 20, section 820-218]

* 1. For an entity that is an inward investor (financial), the worldwide gearing debt amount is calculated as follows:

Step 1: Divide the entity’s statement worldwide debt for the income year by the entity’s statement worldwide equity for that year (see further below for an explanation of statement worldwide debt and statement worldwide equity).

Step 2: Add 1 to the result of step 1.

Step 3: Divide the result of step 1 by the result of step 2.

Step 4: Multiply the result of step 3 above by the result of step 5 in the method statement in section 820-210(2).

Step 5: Add to the result of step 4 the average value, for that year, of the entity’s zero capital amount (that has arisen because of the Australian investments mentioned in step 1 of the method statement in subsection 820-210(2)).

Step 6: Add to the result of step 5 the average value, for that year, of the entity’s associate entity excess amount. The result of this step is the worldwide gearing debt amount.

[Schedule 1, Part 6, item 20, section 820-219]

* 1. For an entity that is an inward investment vehicle (general) that is not also an outward investor (general), the worldwide gearing debt amount is calculated as follows:

Step 1: Divide the entity’s statement worldwide debt for the income year by the entity’s statement worldwide equity for that year (see further below for an explanation of statement worldwide debt and statement worldwide equity).

Step 2: Add 1 to the result of step 1.

Step 3: Divide the result of step 1 by the result of step 2.

Step 4: Multiply the result of step 3 above by the result of step 4 in the method statement in section 820-195.

Step 5: Add to the result of step 4 the average value, for that year, of the entity’s associate entity excess amount. The result of this step is the worldwide gearing debt amount.

[Schedule 1, Part 6, item 20, section 820-216]

* 1. For an entity that is an inward investment vehicle (financial) that is not also an outward investor (financial), the worldwide gearing debt amount is calculated as follows:

Step 1: Divide the entity’s statement worldwide debt for the income year by the entity’s statement worldwide equity for that year (see further below for an explanation of statement worldwide debt and statement worldwide equity).

Step 2: Add 1 to the result of step 1.

Step 3: Divide the result of step 1 by the result of step 2.

Step 4: Multiply the result of step 3 above by the result of step 5 in method statement in subsection 820-200(2).

Step 5: Add to the result of step 4 the average value, for that year, of the entity’s zero-capital amount.

Step 6: Add to the result of step 5 the average value, for that year, of the entity’s associate entity excess amount. The result of this step is the worldwide gearing debt amount.

[Schedule 1, Part 6, item 20, section 820-217]

* 1. For the purposes of the calculations in sections 820-216 to 820‑219, references to an income year are taken to be a reference to a part year period (if applicable), as these calculations are contained in method statements that are covered by table item 1 in subsection 820‑225(3).
  2. For an entity that is an inward investment vehicle (general) that is also an outward investor (general), the worldwide gearing debt amount is calculated as follows:

Step 1: Divide the entity’s statement worldwide debt for the income year by the entity’s statement worldwide equity for that year (see further below for an explanation of statement worldwide debt and statement worldwide equity).

Step 2: Add 1 to the result of step 1.

Step 3: Divide the result of step 1 by the result of step 2.

Step 4: Multiply the result of step 3 above by the result of step 6 in the method statement in section 820-95.

Step 5: Add to the result of step 4 the average value, for that year, of the entity’s associate entity excess amount. The result of this step is the worldwide gearing debt amount.

[Schedule 1, Part 2, item 13, section 820-111]

* 1. For the purposes of this calculation, references to an income year are taken to be a reference to a part year period (if applicable), as this calculation is contained in a method statement that is covered by table item 1 in subsection 820‑120(4).
  2. For an entity that is an inward investment vehicle (financial) that is also an outward investor (financial), the worldwide gearing debt amount is calculated as follows:

Step 1: Divide the entity’s statement worldwide debt for the income year by the entity’s statement worldwide equity for that year (see further below for an explanation of statement worldwide debt and statement worldwide equity).

Step 2: Add 1 to the result of step 1.

Step 3: Divide the result of step 1 by the result of step 2.

Step 4: Multiply the result of step 3 above by the result of step 7 in method statement in subsection 820-100(2).

Step 5: Add to the result of step 4 the average value, for that year, of the entity’s zero-capital amount (other than any zero‑capital amount that is attributable to the entity’s overseas permanent establishments).

Step 6: Add to the result of step 5 the average value, for that year, of the entity’s associate entity excess amount. The result of this step is the worldwide gearing debt amount.

[Schedule 1, Part 2, item 13, section 820-111]

For the purposes of this calculation, references to an income year are taken to be a reference to a part year period (if applicable), as this calculation is contained in a method statement that is covered by table item 1 in subsection 820‑120(4).

#### Further explanation of the steps in the method statements

* 1. Steps 1 to 3 under each of the calculations set out above is intended to obtain a gearing ratio for the entity (further explanation of step 1 is below).
  2. Step 4 is intended to apply that gearing ratio to the amount of the entity’s Australian adjusted assets, as determined by reference to entity’s equivalent safe harbour gearing amount.
  3. For financial entities, an additional step has been included to add the entity’s zero capital amount to permit higher levels of gearing where the financial entity has assets that are effectively allowed to be fully debt funded.
  4. For both general and financial entities, the associate excess amount is added to determine the worldwide gearing debt amount. Associate entity equity is deducted from an entity’s assets as an integrity measure to prevent over-gearing from the cascading of equity through chains of entities. The associate entity equity rule can produce harsh outcomes where the value of the associate entity equity is not used to fully leverage debt in the associate. In order to address this, the ‘associate entity excess amount’ allows excess debt capacity of an associate entity to be carried back to the entity with the equity investment.

‘Statement worldwide debt’ and ‘statement worldwide equity’ under step 1

* 1. For step 1 (under the worldwide debt limit calculations set out above), the ‘statement worldwide debt’ and ‘statement worldwide equity’ will, for the purposes of the new test, be determined by reference to amounts shown in the audited consolidated financial statements that are prepared in relation to the ‘worldwide parent entity’, provided the statements satisfy specified requirements. [Schedule 1, Part 6, item 21, section 820-933]
  2. That is, for the purposes of the new test for inward investing entities (non-ADI), accounting concepts are used to determine:
* the amount of the ‘statement worldwide debt’;
* the amount of the ‘statement worldwide equity’;
* the amount of the ‘statement worldwide assets’ for the purpose of determining whether the assets threshold (explained above) is satisfied; and
* the entities that are to be included in the consolidated group, as the inclusion of entities in the audited consolidated financial statements are based on the accounting concept of control.
  1. The reliance on accounting concepts is intended to minimise compliance costs, as the calculation of the maximum allowable debt will be based on figures that are already required to be calculated as part of the worldwide parent’s consolidated financial reports.
  2. The consolidated financial statements must be prepared in accordance with any of the following standards:
* international financial reporting standards (IFRS) that are made or adopted by the International Accounting Standards Board; or
* the accounting standards that are made or adopted in any of the following jurisdictions:
  + the European Union;
  + the United States of America;
  + Canada;
  + Japan;
  + New Zealand; or
  + any other jurisdiction that the Minister specifies by legislative instrument.

[Schedule 1, Part 6, item 21, subsection 820-935(3)]

* 1. These jurisdictions are broadly based on those that are currently accepted for the separate existing requirement for inward investing entities to prepare financial statements for their permanent establishments (see subsections 820-960(1C) and (1D)). However, allowance has been made to permit other jurisdictions to be included where the Minister specifies.
  2. This requirement does not mean that the worldwide parent entity needs to be resident in a listed jurisdiction. Rather, the entity’s foreign parent must have complied with all applicable accounting standards that are required or permitted in a listed jurisdiction in preparing its audited consolidated financial statements.
  3. The audited consolidated financial statements must have been prepared in relation to the ‘worldwide parent entity’. A ‘worldwide parent entity’ is an entity that is not controlled by another entity according to the standards that were used to prepare the statements.

Austco is an Australian entity with a parent in Singapore, Singco. Singco is itself controlled by another entity in Japan, Japco. Japco is not controlled by another entity according to the accounting standards that it uses to prepare its audited consolidated financial statements.

For the purposes the new worldwide gearing debt test, Japco is the worldwide parent entity. Austco cannot use Singco’s audited consolidated financial statements (if any). Austco can use Japco’s audited consolidated financial statements for determining the statement worldwide debt and statement worldwide equity amounts.

* 1. If more than one set of financial statements satisfy the requirements relating to the audited consolidated financial statements, then the entity can choose the financial statements it would like to use for the purpose of the new worldwide gearing debt test [Schedule 1, Part 6, item 21, paragraph 820-935(1)(b)]. However, if an entity chooses to use a particular set of audited consolidated financial statements, those same statements must be used for the purpose of calculating the following amounts for a particular period:
* the ‘statement worldwide debt’;
* the ‘statement worldwide equity’;
* the ‘statement worldwide assets’ for purpose of determining whether the assets threshold (explained above) is satisfied; and
* control for the purpose of determining the ‘worldwide parent entity’.
  1. For example, an entity could not use one set of statements prepared using US GAAP for the purpose of determining it’s statement worldwide equity, and use another set of statements prepared using IFRS for the purpose of determining its statement worldwide debt, for a particular period.
  2. The audited consolidated financial statements must also show certain amounts that are relevant to the calculation of the new test. These amounts include the following (however described):
* liabilities;
* provisions;
* liabilities in relation to distributions to equity participants;
* trade payables;
* deferred tax liabilities;
* liabilities relating to employee benefits;
* current tax liabilities;
* deferred revenue;
* liabilities relating to insurance;
* net assets;
* assets; and
* any other amount specified by legislative instrument.

[Schedule 1, Part 6, item 21, paragraph 820-935(2)(c)]

* 1. It is not necessary for these amounts to be separately presented in the statements if this type of presentation is not required by the relevant accounting standards. For example, it would not be necessary to separately disclose liabilities relating to employee benefits as a separate line item on the statement of financial position, if a relevant accounting standard allowed this amount to be presented as part of a more general category of liabilities. However, it is necessary for these amounts to be calculated in accordance with the relevant accounting standards on a consolidated basis, and for these amounts to be reflected in the financial statements in a way those standards permit (albeit aggregated with other amounts).
  2. To calculate the amount of statement worldwide debt under step 1 of the method statements mentioned above, the entity must start with the total amount of liabilities for the period, and deduct the following amounts:
* provisions;
* liabilities in relation to distributions to equity participants;
* trade payables;
* deferred tax liabilities;
* liabilities relating to employee benefits;
* current tax liabilities;
* deferred revenue;
* liabilities relating to insurance; and
* any other amount specified by legislative instrument.

The result of this calculation is the statement worldwide debt for the period.

[Schedule 1, Part 6, item 21, subsection 820-933(1)]

* 1. This calculation is intended to better reflect the amount of ‘debt’ for the consolidated group. As accounting standards generally use the concept of liability, which is broader than the concept of debt, various adjustments are made to the consolidated liabilities to deduct certain amounts of liabilities that are non-debt in nature. For example, liabilities relating to employee benefits (including retirement benefit obligations) and those that relate to provisions, trade payables and current and deferred tax liabilities. This requirement is intended to provide a closer ‘proxy’ for debt, although it does not seek to deduct all types of liabilities that are non-debt in nature, in recognition that this would impose undue compliance burden on entities.
  2. For a relevant period, the audited consolidated financial statements that are to be relied upon for the purposes of the test must be the statements for the most recent period ending:
* no later than the end of the relevant period; and
* no earlier than 12 months before the start of the relevant period.

[Schedule 1, Part 6, item 21, paragraph 820-935(2)(e)]

* 1. The relevant period is the income year for an entity (or a part year period, if applicable).
  2. The consolidated financial statements need not relate to an annual period — part year financial statements could be used if they satisfy the other relevant requirements. Similarly, an entity would not necessarily be precluded from using the new worldwide gearing debt test if it has a newly incorporated worldwide parent entity whose first set of financial statements cover a period of more than 12 months (provided the other relevant requirements are satisfied).
  3. This would allow the new test to be calculated for a relevant period using the audited consolidated financial statements prepared by the entity’s worldwide parent entity for the most recent accounting period.
  4. This requirement is intended to balance the need to ensure that the most recent financial statements are used (to increase the relevance and reliability of the amounts used in the test) whilst recognising that the audited consolidated financial statements are prepared on a historical basis and may lag the income year in which the new test is being applied.

ABC Limited is an Australian entity, with an income year of 1 July 2014 to 30 June 2015. ABC Limited has a worldwide parent entity, XYZ Limited, in the United States. XYZ Limited has a balance date of 31 December, and prepares an audited consolidated financial statement using US GAAP.

In applying the worldwide gearing debt test, ABC Limited must determine the ‘statement worldwide debt’ and ‘statement worldwide equity’ by reference to the XYZ Limited’s financial statements for the period commencing 1 January 2014 to 31 December 2014.

ABC Limited is an Australian entity, with an income year of 1 July 2014 to 30 June 2015. ABC Limited has a worldwide parent entity, STE Limited, in the UK. STE Limited has a balance date of 31 March, and prepares an audited consolidated financial statement using IFRS.

In applying the worldwide gearing debt test, ABC Limited must determine the ‘statement worldwide debt’ and ‘statement worldwide equity’ by reference to the STE Limited’s financial statements for the period commencing 1 April 2014 to 31 March 2015.

ABC Limited is an Australian entity, with an income year of 1 July 2014 to 30 June 2015. ABC Limited has a worldwide parent entity, POW Limited, in New Zealand. POW Limited has a balance date of 30 June, and prepares an audited consolidated financial statement using IFRS.

In applying the worldwide gearing debt test, ABC Limited must determine the ‘statement worldwide debt’ and ‘statement worldwide equity’ by reference to the POW Limited’s financial statements for the period commencing 1 July 2014 to 30 June 2015.

* 1. To ensure the integrity of the new worldwide gearing debt test, the consolidated financial report will need to be audited in accordance with a law of a jurisdiction mentioned in subsection 820-935(3), or another jurisdiction that has adopted IFRS. [Schedule 1, Part 6, item 21, paragraph 820‑935(2)(d)]
  2. The auditor’s report must also be unqualified [Schedule 1, Part 6, item 21, paragraph 820-935(2)(d)]. This is intended to enhance the reliability and integrity of the financial information being relied upon for the purposes of the new test.

### Worldwide capital amount for outward investing entities (ADIs)

* 1. Outward investing entities that are ADIs can currently use the worldwide capital amount test in section 820-320, if they are also not a foreign controlled Australian entity throughout the income year.
  2. Currently, the worldwide capital amount allows an Australian ADI with foreign investments to fund its Australian investments with a minimum capital ratio equal to 80 per cent of the Tier 1 capital ratio of its worldwide group.
  3. Under the new law, the worldwide capital amount will require an Australian ADI with foreign investments to fund its Australian investments with a minimum capital ratio equal to 100 per cent of the Tier 1 capital ratio of its worldwide group. [Schedule 1, Part 3, item 14, method statement in subsection 820-320(2)]
  4. For the purposes of this test, the Tier 1 capital ratio (and more broadly, the worldwide capital amount) is determined by reference to the method statements contained in section 820-320.

### De minimis threshold

* 1. Currently, the thin capitalisation rules do not disallow any debt deductions of an entity, if the entity and all its associate entities have debt deductions of $250,000 or less (the *de minimis* threshold).
  2. To reduce compliance costs and ensure that small businesses are protected from the effects of the thin capitalisation debt tests, the current *de minimis* threshold will be increased from debt deductions of $250,000 or less, to $2 million or less. [Schedule 1, Part 5, item 18, section 820-35]
  3. For the purpose of paragraph 815-140(1)(a), an entity under the de minimis threshold is still considered to be applying Division 820. An entity can only qualify under the de minimis threshold if it has applied Subdivision 820-A and determined that its debt deductions fall under the threshold under section 820-35.

## Consequential amendments

* 1. As a result of the changes to the thin capitalisation debt limits, several consequential amendments have been made to update figures and calculations contained in various examples throughout Division 820. [Schedule 1, Part 7, items 24 to 25, 27, 30, 33, 35 to 36, 38 to 40, 42, 44 to 45 and 47].
  2. Consequential amendments have also been made to update cross-references to the revised debt limits, in various method statements throughout Division 820. [Schedule 1, Part 7, items 26, 37, 41, 49 and 50 ]
  3. As the *de minimis* threshold has increased from $250,000 of debt deductions to $2 million of debt deductions, various cross‑references to the threshold amount have been updated to reflect the new threshold amount. [Schedule 1, Part 7, items 23, 34, 43, 46, 48 and 51]

## Application provision

* 1. These amendments apply for income years starting on or after 1 July 2014 [Schedule 1, Part 8, item 56]. The amendments were announced by the Government on 6 November 2013, and taxpayers will be required to apply them to assessments completed after the end of that income year. Consequently, no taxpayer will be required to calculate their tax liabilities for the 2014-15 income year until after the Bill receives Royal Assent.

## STATEMENT OF COMPATIBILITY WITH HUMAN RIGHTS

## Prepared in accordance with Part 3 of the *Human Rights (Parliamentary Scrutiny) Act 2011*

### *Tax and Superannuation Laws Amendment (2014 Measures No. 4) Bill 2014 — Thin capitalisation*

* 1. This Bill is compatible with the human rights and freedoms recognised or declared in the international instruments listed in section 3 of the *Human Rights (Parliamentary Scrutiny) Act 2011*.

### Overview

* 1. The Bill:
* tightens the debt limit settings in the thin capitalisation rules to ensure that multinationals do not allocate a disproportionate amount of debt to their Australian operations;
* increases the *de minimis* threshold to minimise compliance costs for small businesses; and
* introduces a new worldwide gearing debt test for inbound investors.

### Human rights implications

* 1. This Bill does not engage any of the applicable rights or freedoms.

### Conclusion

* 1. This Bill is compatible with human rights as it does not raise any human rights issues.

1. Foreign dividends

## Outline of chapter

* 1. Schedule 2 to this Bill reforms the exemption for foreign non‑portfolio dividends.
  2. All references in this Chapter are to the *Income Tax Assessment Act 1997* (ITAA 1997) unless otherwise specified.

## Context of amendments

* 1. Currently, a non-portfolio foreign dividend (that is, a dividend on a voting interest of at least 10 per cent in a foreign resident company) is non‑assessable non-exempt (NANE) income when paid to an Australian resident company (see section 23AJ of the *Income Tax Assessment Act 1936* (ITAA 1936)).
  2. The intention of this exemption is to make non-portfolio returns on equity to Australian resident companies exempt of Australian income tax, to remove the Australian tax burden from active business income earned by a foreign subsidiary of an Australian owned company. This helps ensure that the foreign subsidiaries are able to compete on an equal footing with other businesses located in that foreign country.
  3. However, under the current rules, the exemption can also apply in circumstances where the investment instrument is treated as a debt instrument, for example, in the case of redeemable preference shares. This has led to unintended consequences arising from the interaction of the thin capitalisation rules, the core tax rules for determining what is debt and what is equity (the debt equity rules) and the exemption. This arises in circumstances where an Australian company uses a ‘debt instrument’ which also qualifies for the exemption to fund an offshore expansion. Offshore acquisitions effected in this way are currently unconstrained by the thin capitalisation rules contrary to the initial policy intent.
  4. Also, the exemption in section 23AJ of the ITAA 1936 only applies in instances where the dividend is received directly by the Australian company from the foreign company. That is, where a dividend from a foreign company passes through a trust or partnership it is no longer eligible for the exemption. There is, however, no economic difference between holding the equity interests directly or indirectly through a trust or partnership.

## Summary of new law

* 1. The exemption for foreign dividends has been modernised and re-written into the *Income Tax Assessment Act 1997* (ITAA 1997) to:
* ensure that it applies to returns on instruments treated as ‘equity interests’ under the debt-equity rules. This is intended to exclude any returns on ‘debt interests’ from the exemption and also allow the exemption to apply in respect of a broader range of equity-like interests, rather than interests that involve significant voting rights;
* allow it to apply where a distribution flows through interposed trusts and partnerships other than corporate tax entities;
* allow it to apply where it is received by a corporate tax entity, rather than a company; and
* allow it to apply in respect of distributions of a non-share dividend, which is not included in the definition of a distribution.
  1. In addition, the ability to pool portfolio dividends (that is, where the interest is less than 10 per cent) in an offshore entity in order to qualify for an exemption under section 23AJ of the ITAA 1936 will be removed. This type of arrangement is contrary to the intention of the exemption, which is intended to apply to non-portfolio dividends where the interest is at least 10 per cent.

Comparison of key features of new law and current law

| New law | Current law |
| --- | --- |
| The exemption will apply where an Australian corporate tax entity holds a participation interest of at least 10 per cent in a foreign company. | The exemption for non-portfolio dividends applies where an Australian company holds a voting interest of at least 10 per cent (the non-portfolio test). |
| The exemption will apply where the foreign equity distribution is made in respect of an equity interest in the foreign company.  This will ensure that the exemption is not available in respect of returns on debt interests. It will also allow the exemption to apply in respect of a broader range of equity interests, not only voting interests. | The exemption for non-portfolio dividends applies where the dividend is made in respect of a voting interest in the foreign company.  As a result, some returns on debt-like interests (such as redeemable preferences shares) may currently be eligible for the exemption. |
| The exemption will apply in respect of distributions of a non-share dividend. | The exemption for non-portfolio dividends does not apply in respect of a non‑share dividend. |
| The exemption will apply where a dividend is received by a corporate tax entity (including public trading trusts, corporate unit trusts, and corporate limited partnerships). | The exemption for non-portfolio dividends applies only where the dividend is received by a company. |
| The exemption for foreign dividends will apply where a dividend flows through an interposed trust or partnership, other than a corporate tax entity. | The exemption for non-portfolio dividends does not apply to dividends that flow through interposed trusts or partnerships. |
| The ability to pool portfolio dividends in an offshore entity to qualify for the non-portfolio dividend exemption will be removed. | It is possible to pool portfolio dividends in an offshore entity in order to qualify for the non-portfolio dividend exemption. |

## Detailed explanation of new law

### Foreign equity distributions on participation interests

* 1. The new exemption for foreign equity distributions on participation interest replaces the existing test in section 23AJ of the ITAA 1936 for non-portfolio dividends.
  2. If an Australian corporate tax entity holds a participation interest of at least 10 per cent in a foreign company, and receives a foreign equity distribution from the foreign company either directly or indirectly through one or more interposed trusts and partnerships, the distribution is NANE income for the Australian corporate tax entity. [Schedule 2, Part 1, item 4, Subdivision 768-A]

#### Participation interest test

* 1. As noted above, for the distribution to be NANE income, the Australian corporate tax entity must satisfy the participation test [Schedule 2, Part 1, item 4, paragraph 768-5(1)(b)]. This participation test needs to be satisfied at the time the foreign equity distribution is made [Schedule 2, Part 1, item 4, paragraph 768-5(1)(b)].
  2. The participation interest includes both direct and indirect participation interests [Schedule 2, Part 1, item 4, section 768-15]. Direct and indirect participation interests are existing concepts which are calculated by reference to rules set out in Subdivision 960-GP.
  3. However, for the purposes of the new NANE exemption for foreign equity distributions, any rights that the Australian corporate tax entity may have on winding-up are disregarded in determining the participation interest [Schedule 2, Part 1, item 4, section 768-15]. The rights on winding-up may vary considerably from other interests and can therefore distort the participation test.

#### Foreign equity distribution

* 1. The exemption applies where a foreign resident company makes a foreign equity distribution to an Australian corporate tax entity. [Schedule 2, Part 1, item 4, paragraph 768-5(1)(a)]
  2. A foreign equity distribution is a distribution or non-share dividend made by a company that is a foreign resident in respect of an equity interest in the company. [Schedule 2, Part 1, item 5, definition of ‘foreign equity distribution’ in subsection 995-1(1)]
  3. A key feature of the new law is that the distribution will only be NANE income where the distribution is made in respect of an equity interest [Schedule 2, Part 1, item 4, section 768-5]. This is intended to:
* modernise the exemption by aligning it to the concepts of ‘debt interests’ and ‘equity interests’ as defined in Division 974;
* ensure that the exemption is not available in respect of returns on debt interests, such as redeemable preference shares;
* allow the exemption to apply in respect of a broader range of equity interests, not only voting interests; and
* ensure that the deduction under section 25-90 operates as intended, by ensuring that any debt ‘on-lent’ to an offshore entity will give rise to assessable interest income in Australia, with any funding costs of the Australian company being deductible under the general deduction provision in section 8-1, rather than section 25-90.
  1. A foreign equity distribution also includes a non-share dividend [Schedule 2, Part 1, item 4, section 768-10], which is a dividend on a non-share equity interest. A non-share equity interest is an equity interest in a company that is not in legal form solely a share in the capital of the company. For example, certain convertible notes may be classified as a non-share equity interest for tax purposes.
  2. As a non-share equity interest is an equity interest, it is appropriate that returns on this equity interest are included in the definition of a foreign equity distribution and are covered by the exemption for foreign dividends (provided the other relevant requirements are satisfied).

#### Australian corporate tax entities

* 1. Another feature of the new law is that the exemption will be expanded to apply where the foreign equity distribution is received by an Australian corporate tax entity, whereas previously, the exemption only applied where it was received by an Australian company. [Schedule 2, Part 1, item 4, section 768‑5]
  2. This will allow an Australian public trading trust, corporate unit trust and corporate limited partnership to access the exemption where it satisfies the other requirements for the exemption.
  3. This will broaden the exemption to other types of entities that are treated as a company for tax purposes.

#### Interposed trusts and partnerships

* 1. Under the new law, a foreign equity distribution can be NANE income for an Australian company, even if it passes through interposed trusts and partnerships (including trusts that are commonly referred to as ‘nominee’ or ‘custodian’ arrangements), provided that the interposed trusts and partnerships are not corporate tax entities. [Schedule 2, Part 1, item 4, subsection 768-5(2)]
  2. This represents a change from the current law, which allows a dividend to be NANE under section 23AJ of the ITAA 1936 only in instances where the dividend is received directly by the Australian company from the foreign company.
  3. Allowing the exemption to apply where a foreign equity distribution has flowed through interposed trusts and partnerships is intended to reflect the fact that there is no economic difference between holding equity interests directly or indirectly through a trust or partnership.
  4. The new law provides that an amount will be NANE income for an Australian beneficiary or partner where:
* the amount is ultimately received by an Australian corporate beneficiary of a trust, or an Australian corporate partner in a partnership;
* the amount would otherwise be included in the trust or partnership’s assessable income under Division 5 or 6 of Part III of the ITAA 1936;
* the amount can be attributed, either directly or indirectly through one or more interposed trusts and partnerships that are not corporate tax entities, to a foreign equity distribution;
* at the time distribution is made, the trust or partnership satisfies the participation test explained above; and
* the Australian beneficiary or partner does not receive the distribution in the capacity of a trustee (unless it is received in the capacity of a trustee of a corporate unit trust or public trading trust).

[Schedule 2, Part 1, item 4, subsection 768-5(2)]

* 1. The distribution will not be NANE where it flows through an interposed trust or partnership that is a corporate tax entity [Schedule 2, Part 1, item 4, paragraph 768-5(2)(c)], as a corporate tax entity is not a flow‑through vehicle.

#### Interaction with rules about controlled foreign companies

* 1. Currently, section 389A of the ITAA 1936 provides that the debt and equity rules contained in Division 974 are to be disregarded in calculating the attributable income of an eligible controlled foreign corporation (CFC).
  2. However, given the new foreign distribution exemption relies on the concept of an equity interest, as defined in Division 974 of the ITAA 1997, the law has been clarified to provide that section 389A of the ITAA 1936 is to be disregarded for the purpose of applying the new foreign distribution exemption in Subdivision 768-A. [Schedule 2, Part 2, item 6, section 404 of the ITAA 1936]
  3. Section 389A of the ITAA 1936 is only to be disregarded for the purposes of applying the foreign distribution exemption in Subdivision 768-A, and not more broadly. This ensures that CFCs can continue to access the foreign distribution exemption.

### Repeal of portfolio dividend exemption for controlled foreign companies

* 1. The initial policy rationale for section 404 of the ITAA 1936 was to allow certain dividends to remain NANE income if they did not meet the requirements in section 23AJ of the ITAA 1936. This situation might arise where, for example, the regulatory requirements in some foreign jurisdictions limit the voting interests able to be held by foreigner investors because those jurisdictions do not attach voting rights to equity (and therefore the test in section 23AJ of the ITAA 1936 would not be satisfied).
  2. However, the need for section 404 of the ITAA 1936 has diminished, given the exemption for foreign equity distributions (explained above) will no longer rely upon the concept of voting rights.
  3. In addition, section 404 of the ITAA 1936 poses an integrity risk. Currently, the operation of section 404 of the ITAA 1936, and its interaction with section 23AJ of the ITAA 1936, can result in Australian taxpayers paying no Australian tax on dividends derived from their (in substance) foreign portfolio share holdings when received through an interposed CFC.
  4. This occurs where a CFC receives portfolio dividends from its offshore investments that can be pooled together and repatriated back to Australia as a non-portfolio dividend, which is currently NANE income under section 23AJ of the ITAA 1936. This result arises because all dividends (both portfolio and non-portfolio) paid to a CFC resident in a listed or section 404 country are treated as being exempt if the paying entity is also a resident of a listed or section 404 country.
  5. In contrast, dividends received directly from foreign portfolio holdings are taxable in Australia.
  6. To address these issues, section 404 of the ITAA 1936 will be repealed, together with the associated regulations which set out the section 404 countries. [Schedule 2, Part 2, item 6, section 404]
  7. Section 404 will be replaced with a requirement that is intended to ensure that CFC’s continue to have access the foreign dividend exemption — see paragraphs 2.27 to 2.29 above.

## Consequential amendments

* 1. Several consequential amendments have been made to:
* update various cross-references to section 23AJ of the ITAA 1936, and replace these with references to the new revised exemption in section 768-5 [Schedule 2, Part 3, items 7 to 9 and 14 to 22]; and
* remove various cross-references to section 404 of the ITAA 1936, given it will be repealed [Schedule 2, Part 3, items 10, 12 and 13].

## Application provision

* 1. The amendments apply to distributions and non-share dividends made after the day the Act receives Royal Assent. [Schedule 2, Part 4, item 23]

## STATEMENT OF COMPATIBILITY WITH HUMAN RIGHTS

## Prepared in accordance with Part 3 of the *Human Rights (Parliamentary Scrutiny) Act 2011*

### *Tax and Superannuation Laws Amendment (2014 Measures No. 4) Bill 2014 — Foreign dividends*

* 1. This Bill is compatible with the human rights and freedoms recognised or declared in the international instruments listed in section 3 of the *Human Rights (Parliamentary Scrutiny) Act 2011*.

### Overview

* 1. This Bill reforms the exemption for foreign non‑portfolio dividends.

### Human rights implications

* 1. This Bill does not engage any of the applicable rights or freedoms.

### Conclusion

* 1. This Bill is compatible with human rights as it does not raise any human rights issues.

1. Improving the integrity of the foreign residents capital gains tax regime

## Outline of chapter

* 1. Schedule 3 amends the *Income Tax Assessment Act 1997* (ITAA 1997) to ensure that the foreign residents capital gains tax (CGT) regime operates as intended by preventing the double counting of certain assets under the Principal Asset Test.
  2. A technical correction is also made to the meaning of ‘permanent establishment’ in section 855-15 of the ITAA 1997. The correction ensures that foreign residents are subject to CGT in relation to CGT assets that they have used in carrying on a business through a permanent establishment located in Australia.

## Context of amendments

### Australia’s Foreign Resident CGT Regime

* 1. Australia’s current foreign resident CGT regime was introduced in 2006, with the insertion of Division 855 into the ITAA 1997.
  2. Consistent with international practice and Australia’s international tax treaties, this regime promotes foreign investment in Australia. Subdivision 855-A operates to disregard a capital gain or capital loss made by a foreign resident provided the relevant CGT asset is not:
* a direct or indirect interest in Australian real property; or
* an asset used in carrying on a business through a permanent establishment in Australia.
  1. All references in this Chapter are to the ITAA 1997 unless otherwise specified.

### Permanent establishments

* 1. Section 855-15 of the ITAA 1997 provides that the term ‘permanent establishment’ has the same meaning as it does in section 23AH of the *Income Tax Assessment Act 1936* (ITAA 1936).
  2. The use of that definition was intended to apply any applicable treaty definition for permanent establishment. Alternatively, if no applicable treaty definition existed, the default meaning of permanent establishment in subsection 6(1) of the ITAA 1936 would apply.
  3. Section 23AH, however, deals with outbound investment. The section 23AH definition applies in relation to ‘listed or unlisted countries’, which, by definition, are countries other than Australia. A strict application of this definition in the context of Division 855 precludes a CGT asset from ever being taxable Australian property. This outcome is clearly unintended as it would mean that part of the definition of taxable Australian property has no operation.

### Indirect Australian Real Property Interests and the Principal Asset Test

* 1. The objects of the foreign resident CGT regime include ensuring that interests in an entity remain subject to Australia's capital gains tax laws if the entity's underlying value is principally derived from Australian real property (section 855-5).
  2. This is achieved by ensuring that a capital gain realised by a foreign resident on an ‘indirect Australian real property interest’ (see section 855-25) cannot be disregarded.
  3. An ‘indirect Australian real property interest’ includes a significant interest (generally a stake of 10 per cent or more) in an entity whose underlying value is principally derived from ‘Australian real property’.
  4. The Principal Asset Test in section 855-30 is used to determine whether an entity's underlying value is principally derived from Australian real property. The Principal Asset Test requires a comparison of the sum of the market values of the entity’s taxable Australian real property (TARP) assets with the sum of the market values of its assets that are not taxable Australian real property (non-TARP) assets.
  5. Sections 855-20 and 855-25 provide that a CGT asset is TARP if it is:
* real property situated in Australia (including a lease of land situated in Australia); or
* a mining, quarrying or prospecting right (to the extent that it is not real property), if the minerals, petroleum or quarry materials are situated in Australia.
  1. If the sum of the market values of the entity's assets that are TARP exceeds the sum of the market values of the assets that are non‑TARP, any capital gain or capital loss is not disregarded and may be included in the assessable income of the foreign resident.
  2. The Principal Asset Test applies to the assets of the entity in which the foreign resident had a direct interest (thetest entity). Where an asset of the test entity is an interest in another entity the test may operate to also assess the assets of those other entities. That is, the Principal Asset Test applies recursively to the assets of other entities in which the test entity has a significant interest, directly or indirectly, provided that the foreign resident has an indirect interest of at least 10% in that other entity.
  3. This is achieved, under subsection 855-30(3), by converting the membership interests held by one entity in another as notional TARP and non-TARP assets according to the first entity’s proportional stake in the other entity’s underlying assets.

### Asset Duplication

* 1. The Principal Asset Test only has regard to the market value of the assets of the relevant entities (it does not have regard to the liabilities or the source of the assets). Where the assets of multiple entities are assessed under the Principal Asset Test, and those entities have assets and liabilities arising out of transactions between themselves, this can affect the outcome of applying the Test in that the value of certain non-TARP assets can be effectively duplicated.
  2. Transactions between these entities may create assets that lead to certain assets of the group effectively being valued multiple times, once in the hands of each entity. The issue is best illustrated by way of example.
     + 1. : Asset duplication under the current law



Emily, a foreign resident, wishes to dispose of her 15 per cent interest in Mineral Dynamics International (MDI).

MDI owns 100 per cent of the shares in Regular Resource Industries (RRI), a mining company with operations in Australia.

MDI also has $100 million cash on hand (all examples in this Chapter use amounts denominated in Australian currency). RRI’s only asset is a mining licence with a current market value of $150 million.

If Emily were to sell her shares when these were MDI’s only assets, the Principal Asset Test would be satisfied as the test entity, MDI, would have a TARP asset worth $150 million (derived from the mining licence held by RRI) and a non-TARP asset worth $100 million.

Before Emily sells her shares, MDI loans $100 million to RRI on commercial terms. MDI thereby acquires a right to receive funds under the loan agreement. This right has a market value of $100 million. Under the arrangement, RRI uses the funds advanced to purchase non-TARP assets, equipment worth $100 million.

The same underlying store of economic value, the $100 million, is effectively counted twice under the Principal Asset Test, once as a loan asset in the hands of MDI and again as equipment in the hands of RRI.

As a result, the sum of the market values of MDI’s non-TARP assets equals $200 million (derived from the loan asset of MDI and the equipment in the hands of RRI) and exceeds the value of the TARP asset ($150 million derived from RRI’s mining licence). The Principal Asset Test is not satisfied. Therefore, any capital gain or capital loss that Emily would make on the disposal of her shares in MDI would be disregarded. The underlying value of MDI, however, has not changed.

* 1. Subsection 855-30(5) is an integrity rule that provides that the market value of an asset acquired with a purpose of failing the Principal Asset Test is disregarded. This integrity rule will not operate to prevent all instances of asset duplication, which may arise through legitimate commercial arrangements.
  2. The treatment of inter-company loans under the Principal Asset Test is discussed in [ATO Interpretative Decision 2012/14](http://law.ato.gov.au/atolaw/view.htm?docid=%22AID%2FAID201214%2F00001%22). The potential for the Principal Asset Test to result in asset duplication is discussed in [Taxpayer Alert 2008/20](http://law.ato.gov.au/atolaw/view.htm?DocID=TPA/TA200820/NAT/ATO/00001).

### Announced Changes to the Principal Asset Test

* 1. On 14 May 2013, the previous government announced amendments to the Principal Asset Test in the 2013-14 Budget. The amendments, as announced, would:
* value mining, quarrying or prospecting information and goodwill together with the mining rights to which they relate; and
* remove the ability to use transactions between members of the same consolidated group to create and duplicate assets.
  1. On 4 November 2013, the Government announced that it would proceed with the changes to the Principal Asset Test.

#### The valuation of mining information and goodwill

* 1. The previous government’s announcement of the valuation amendment appears to be a response to issues arising from the decision of the Federal Court in R*esource Capital Fund III LP v Commissioner of Taxation* [2013] FCA 363, which was handed down on 26 April 2013.
  2. Following additional judicial consideration, the courts have recently provided their final decision in relation to this issue (see in particular the decision of the Full Federal Court in *Commissioner of Taxation v Resource Capital Fund III LP* [2014] FCAFC 37 (3 April 2014)). The Government has decided to defer the enactment of the amendment until the effect of the decision has been analysed.

#### The scope of the anti-duplication amendment

* 1. The amendments to address asset duplication, as announced by the previous government, focused on interactions between members of a consolidated group or Multiple-Entry Consolidated (MEC) group.
  2. However, the potential for assets to be effectively duplicated is not restricted to assets being created from transactions between members of a consolidated group; rather it arises from the operation of the Principal Asset Test itself.

## Summary of new law

* 1. Part 1 of Schedule 3 amends the law to prevent the double counting of certain non-TARP assets that can distort the application of the Principal Asset Test.
  2. Where the assets of two or more entities are included in the Principal Asset Test, the market value of new non-TARP assets arising from certain arrangements between those entities will be disregarded for the purposes of the Principal Asset Test.
  3. If the group has consolidated financial accounts, the asset would not be recognised because it would be offset by the existence of the liability in the other entity. The amendments are necessary because the corresponding liability is not included in the Principal Asset Test calculations.
  4. These amendments are broader than those announced by the previous government. In particular, the scope of the amendments is not restricted to entities that are members of the same consolidated group or MEC group.
  5. Part 2 of Schedule 3 makes a technical correction to section 855‑15. This amendment ensures that, in determining whether an asset is ‘taxable Australian property’, the test in respect of CGT assets that are used in carrying on a business through a permanent establishment in Australia is applied appropriately.
  6. This change replaces the reference to a permanent establishment within the meaning of section 23AH of the ITAA 1936 with specific tests. Consistent with section 23AH, these tests take into account an entity’s status as a resident of a country with which Australia has an international tax agreement in determining whether it has a permanent establishment in Australia.

Comparison of key features of new law and current law

|  |  |
| --- | --- |
| New law | Current law |
| Where the assets of two or more entities are included in the Principal Asset Test, the market value of new non-TARP assets arising from certain arrangement involving those entities will be disregarded.  In particular, certain assets that relate to liabilities located elsewhere in the corporate group will not be counted because they do not represent the group’s underlying economic value. | The application of the Principal Asset Test can be distorted by transactions between certain related entities that create new non-TARP assets, for example loan assets. These agreements can result in double counting of the same market value under the Principal Assets Test.  This can result in situations where the Principal Asset Test is not satisfied even though the underlying value of the relevant entity is principally derived from Australian real property. |
| For the purposes of working out whether a foreign resident has used a ‘permanent establishment’ in carrying on a business in Australia, the expression will have its meaning under any relevant tax treaty or, if no treaty exists, the default statutory definition. | The meaning of permanent establishment in section 855-15 of the ITAA 1997 relies on the definition of the term in section 23AH of the ITAA 1936, which does not apply to Australian permanent establishments. |

## Detailed explanation of new law

### Part 1: Principal Asset Test Amendments

* 1. Part 1 of Schedule 3 prevents the double counting of non-TARP assets when applying the Principal Asset Test. [Schedule 3, item 4, subsection 855-32(1)]

#### The entities to which the amendments apply

* 1. The amendments apply to any assets arising from transactions between entities that have their assets valued for the purposes of the Principal Asset Test as a result of a CGT event occurring to a foreign resident. [Schedule 3, item 4, subsection 855-32(3)]
  2. The amendments can apply to all entities within an economic structure regardless of whether the entities are members of the same consolidated group or MEC group for tax purposes.
  3. The amendments bring entities within the scope of the provision is two ways. Where one of the parties to the arrangement has a direct interest in the other (see Example 3.1), paragraph 855-32(3)(a) will apply. Where there are entities interposed between the two parties but the parties are still within the same relevant ownership chain, paragraph 855‑32(3)(b) will apply. [Schedule 3, item 4, subsection 855-32(3)]
  4. In applying the Principal Asset Test, arrangements involving related parties and group members that result in the creation of new assets will not be affected if the assets of only one of the parties to the arrangement are taken into account in applying the Test. See the following example involving multiple chains of ownership.
     + 1. : Groups with multiple chains of ownership



Bridget, a foreign resident, has interests in two investment firms. One of the firms, Ardenia Capital finances an Australian mining company, Bikra Mining Co, through the purchase of shares. The other, Khutai Capital, makes an investment by way of a loan agreement with Bikra.

If Bridget disposed of her interest in Khutai Capital, the amendments would not apply to the loan asset created in the hands of Khutai Capital. This is because the assets of Bikra are not taken into account for the purposes of applying the Principal Asset Test in relation to Bridget’s disposal of the membership interests in Khutai Capital.

Similarly, if Bridget were to dispose of her interest in Ardenia Capital, the amendments would not apply to the cash asset in the hands of Bikra because Khutai Capital’s loan asset would not be assessed under the Principal Asset Test.

If Bridget were to sell both interests contemporaneously, she had significant control over the affairs of each entity, and both entities had significant TARP assets, it may be necessary to consider whether the loan asset was acquired for a purpose that satisfies the condition in subsection 855-30(5). The present amendments, however, would not apply.

* 1. The amendments will also only apply to entities in which the foreign resident has a sufficient interest. Table item 2 of subsection 855‑30(4) only applies to entities in which the foreign resident has a total participation interest of at least 10 per cent and where the entity with the direct interest has at least a 10 per cent interest.
  2. The amendments do not apply to entities that do not meet the interest thresholds because the Principal Asset Test assesses the net market value of these interests (and includes this in the value of the non‑TARP assets) (see table item 1 in subsection 855-30(4)).

#### The arrangements to which the amendments apply

* 1. The amendments only apply to arrangements that result in the creation of new non-TARP assets and corresponding liabilities. [Schedule 3, item 4, subsection 855-32(2)]
  2. The amendments are not designed specifically to target aggressive tax planning techniques but rather to overcome shortcomings in the existing regime. Accordingly, the amendments are not punitive but may apply to long-standing and legitimate commercial transactions.
  3. The amendments apply where a new asset is created, for example, a financial asset or a new interest in a pre-existing asset of another entity. The amendments ensure that, where a new asset is created and its market value is derived from a liability owed by another relevant entity, the market value of the new asset is disregarded. Assets acquired by the entity with the corresponding liability, however, are not affected.
     + 1. : Application of the amendments

Further to Example 3.1, the amendments would apply to disregard the loan asset in the hands of MDI for the purposes of the Principal Asset Test. The corresponding liability is RRI’s liability to repay the loan.

The underlying equipment asset will be valued in the hands RRI. The equipment and the corresponding liability to repay the loan are both held by RRI, which does not satisfy paragraph 855-32(2)(b).

* 1. The liability must be a ‘corresponding liability’ to satisfy subparagraph 855-32(2)(b)(ii). The corresponding liability will ordinarily be the liability that, in substance, requires the payment of the receivable, for example, the liability to repay a loan. A liability that bears no commercial relationship to the asset, or that is merely a contingent liability, is not a corresponding liability if another corresponding liability can be identified.
  2. The amendments will not apply to a transaction involving the simple transfer of pre-existing assets between relevant entities. Where no new asset is created or where there is no corresponding liability in another party to the arrangement, no potential for duplication arises.

##### Third Parties

* 1. The amendments also apply to arrangements that involve third parties, provided at least two of the parties to the arrangement meet the conditions outlined above.
     + 1. : Arrangements involving third parties



Daniel, a foreign resident, is disposing of his interest in Glee Capital Ltd.

Glee Capital’s assets consist of its interest in its wholly-owned subsidiary, Kurtz Coltan Pty Ltd, and a $100 million loan asset.

The loan asset arose from an arrangement whereby Glee Capital lent funds to an unrelated third party, Loris Finance Group, which on lent the funds to Kurtz Coltan. Kurtz Coltan’s liability to repay the loan to Loris is the corresponding liability to Glee Capital’s loan asset. The amendment will apply to ensure that the market value of the loan asset in the hands of Glee Capital is disregarded for the purposes of applying the Principal Asset Test in relation to Daniel’s disposal of his membership interests.

##### Intra-group membership interests

* 1. The amendments will also not apply to membership interests that relevant entities hold in one another. The market value of these assets is never taken into account due to the operation of subsection 855‑30(3).
  2. Rather, the membership interest asset becomes two notional TARP and non-TARP assets based on the underlying assets of the subsidiary. It is not intended that the amendments should apply to these notional assets directly, although their market value may be reduced (even to nil) because certain underlying assets were disregarded.

#### Limitation where only partial duplication exists

* 1. In the context of wholly-owned groups, assets may be fully duplicated. In these circumstances, it is appropriate to disregard the entire market value of the new asset. Where the arrangement involves parties that are not wholly-owned, however, it is appropriate that the effect of the amendments be limited to reflect the partial duplication of an asset.
  2. Accordingly, the amendments only apply to disregard the market value of the new asset to the extent of the test entity’s total participation interest in the entity in which the corresponding liability is created. [Schedule 3, item 4, subsection 855-32(4)]
  3. Consistent with the operation of the Principal Asset Test, the relevant total participation interest is assessed at the time of the CGT event occurring for the foreign resident.
     + 1. : Partial duplication



Simon, a foreign resident, owns a significant stake in Blaze Capital. Blaze Capital owns 25 per cent of the membership interest in Hello! Telecommunications.

To finance its operations, Hello has secured a $100 million loan from Blaze Capital.

Simon wishes to dispose of a portion of his interest in Blaze Capital. Under the current law, the original $100 million would be valued, to the test entity, Blaze Capital, 1.25 times or as $125 million.

Under the amendments, the market value of the loan asset in the hands of Blaze Capital is reduced proportionally to Blaze Capital’s interest in Hello (by 25 per cent). This outcome reflects the underlying value of the group, which is comprised of Blaze Capital’s interest in the advanced funds ($25 million) and a receivable with respect to the loan advanced to the non-owned portion of Hello ($75 million).

* 1. Where the relevant liability is created in the test entity, the market value of the new asset is disregarded entirely. [Schedule 3, item 4, subsection 855-32(4)]

#### ***Sequencing of provisions***

* 1. The amendments apply at the start of each application of subsection 855-30(3) and table item 2 in subsection (4). This means that relevant assets are disregarded prior to those assets contributing to the value of notional TARP and non-TARP assets created under subsection 855-30(3).
  2. This is consistent with the operation of the existing integrity rule in subsection 855-30(5).
     + 1. : Sequencing of Provisions

Further to Example 3.5, the outcome in that example is achieved through the following mechanical steps in sections 855-30 and 855‑32.

The first step is to consider the assets of the lowest tier company, Hello (see Note 1 to subsection 855-30(4)).

Hello’s only asset is the $100 million advanced under the loan. It is necessary to consider whether either integrity rule (subsection 855‑30(5) or section 855-32) applies to disregard the market value of the asset.  Neither rule applies to the asset.

Next, subsections 855-30(3) and (4) apply to Blaze Capital’s (the first entity) membership interest in Hello (the other entity).  The membership interest is valued as a non-TARP asset with a market value of $25 million ($100 million × 25%) and a TARP asset valued as nil (Hello does not have any TARP assets).

It would then be necessary to consider whether either integrity rule applied to the other assets of Blaze Capital.  As outlined in Example 3.5, $25 million of the market value of Blaze Capital’s loan asset would be disregarded.

### Part 2: Permanent Establishment Amendments

* 1. Part 2 of Schedule 3 makes a technical correction to the definition of taxable Australian property. A CGT asset is taxable Australian property if it is used at any time in carrying on a business through a permanent establishment in Australia.
  2. To ensure the definition of taxable Australian property applies as originally intended, these amendments replace the reference to the section 23AH definition of permanent establishment with an equivalent test that applies in respect of Australian permanent establishments. Consistent with the section 23AH definition, this new test applies any applicable treaty definition of permanent establishment.
  3. In determining whether a CGT asset is taxable Australian property of a kind that is used in carrying on a business through a permanent establishment in Australia, the residency status of the entity that uses the CGT asset determines the way in which the permanent establishment is defined.
  4. Where an entity is a resident in a country with which Australia has an international tax agreement that contains a permanent establishment article, the definition of permanent establishment in the agreement is used in determining whether the entity has a permanent establishment in Australia. [Schedule 3, items 6 and 8, section 855‑15, paragraph (a) of the cell at table item 3, column headed ‘Description’ and subsection 855‑35(1)]
  5. An international tax agreement is defined in subsection 995‑1(1) as an agreement within the meaning of, and given the force of law by, the *International Tax Agreements Act 1953*. To ensure that this aspect of the test is appropriately targeted, these amendments also introduce a definition of ‘permanent establishment article’.
  6. A permanent establishment article is defined as Article 5 of the UK convention, or a corresponding agreement of another international tax agreement. [Schedule 3, items 7 and 9, section 855‑16 and definition of ‘permanent establishment article’ in subsection 995‑1(1)()]
  7. Article 5 of the UK convention sets out the definition of permanent establishment for the purposes of that convention. An article in another agreement that has the same effect for the purposes of that agreement is also a permanent establishment article. This approach to defining permanent establishment articles is consistent with the definitions of associated enterprises article, business profits article, and residence article, which each refer to the corresponding article in the UK Convention.
  8. Where an entity is not a resident in a country with which Australia has an international tax agreement, the general definition of permanent establishment in subsection 995-1(1) is used in determining whether the entity has a permanent establishment in Australia (this definition refers to the definition in subsection 6(1) of the ITAA 1936). [Schedule 3, item 6, section 855‑15, paragraph (a) of the cell at table item 3, column headed ‘Description’]
  9. These amendments apply only to the way in which a permanent establishment is defined, and do not otherwise affect the test for whether a CGT asset is taxable Australian property.

## Consequential amendments

* 1. Two notes are inserted into section 855-30 to inform the reader that, under section 855-32, certain asset may be disregarded for the purposes of the Principal Asset Test. [Schedule 3, items 1 to 3, section 855‑30]

## Application Provisions

### Part 1: Principal Asset Test Amendments

* 1. Where the entities involved in the creation of the new non‑TARP asset are members of the same tax consolidated group, or MEC Group, the amendments in Part 1 of Schedule 3 apply to CGT events that occur after 7.30pm on 14 May 2013 (Budget Night).
  2. For all other entities, the amendments will apply to CGT events occurring on or after 13 May 2014. [Schedule 3, item 5]
  3. The application dates reflect the dates on which it was announced that the amendments would apply to particular entities.
  4. The retrospectivity of these amendments to the date of their announcement is warranted as the amendments correct a defect in the operation of the Principal Asset Test that would otherwise prevent it from operating as intended. The amendments also ensure greater integrity for Australia’s foreign resident CGT regime.

### Part 2: Permanent Establishment Amendments

* 1. The amendments made by Part 2 of Schedule 3 apply from the commencement of Division 855. [Schedule 3, item 10]
  2. These changes are of a technical nature and do not affect any other aspect of the definition of taxable Australian property. They do not negatively affect any taxpayer because the scope of the definition of taxable Australian property aligns with the intention of the original provisions.
  3. Division 855 was introduced in the *Tax Laws Amendment (2006 Measures No. 4) Act 2006* and applies to CGT events that happen on or after 12 December 2006, which aligns with the commencement of Division 855.
  4. Applying the amendments to Division 855 made by this Schedule from the commencement of Division 855 ensures the references to an Australian permanent establishment in the Division apply as originally intended.

## STATEMENT OF COMPATIBILITY WITH HUMAN RIGHTS

## Prepared in accordance with Part 3 of the *Human Rights (Parliamentary Scrutiny) Act 2011*

### *Tax and Superannuation Laws Amendment (2014 Measures No. 4) Bill 2014 — Improving the integrity of the foreign residents capital gains tax regime*

* 1. This Schedule is compatible with the human rights and freedoms recognised or declared in the international instruments listed in section 3 of the *Human Rights (Parliamentary Scrutiny) Act 2011*.

### Overview

* 1. This Schedule amends the *Income Tax Assessment Act 1997* (ITAA 1997) to ensure that the foreign residents capital gains tax (CGT) regime operates as intended by preventing the double counting of certain assets under the Principal Asset Test.
  2. A technical correction is also made to the meaning of ‘permanent establishment’ in section 855-15 of the ITAA 1997. The correction ensures that foreign residents are subject to CGT in relation to CGT assets that they have used in carrying on a business through a permanent establishment located in Australia.

### Human rights implications

* 1. These amendments improve the integrity of Australia’s foreign resident CGT regime. This ensures that foreign residents cannot obtain favourable treatment that is not justified under the regime’s policy framework. This promotes the rights to equality and non-discrimination in Article 26 of the *International Covenant on Civil and Political Rights* and the *International Convention on the Elimination of All Forms of Racial Discrimination.*

### Conclusion

* 1. This Schedule is compatible with human rights as it promotes, but does not inhibit, the fulfilment of human rights.

1. Personalised tax receipts

## Outline of chapter

* 1. Schedule 4 to this Bill amends the tax law to provide greater transparency to taxpayers about how their tax money is spent, by requiring the Commissioner of Taxation (Commissioner) to issue a tax receipt to individuals for the income tax assessed to them.
  2. This measure is part of the Government’s commitment to ensuring greater transparency of how taxpayers’ money is spent.

## Context of amendments

* 1. Prior to the 2013 Federal Election, the Government announced that it would improve transparency on taxes, by introducing a tax receipt for taxpayers. Individual taxpayers will receive a receipt that will inform them about how their taxes are notionally spent, as well as information on the level of Australian Government debt and its interest cost.
  2. This initiative will ensure that governments are held accountable for whether tax revenues are spent wisely and for the levels of government debt they maintain.
  3. For the 2013-14 income year, the Commissioner will issue tax receipts under his existing administrative powers. These amendments will make tax receipts an ongoing feature of the tax system.

## Summary of new law

* 1. For the 2014-15 income year and future income years, the Commissioner will be required to provide every applicable taxpayer with a tax receipt, setting out the notional distribution of the individual’s assessed income tax liability to different types of government expenditure.
  2. The receipt will also show the current level of gross government debt compared with the previous financial year, and the amount of interest paid on that debt.

Comparison of key features of new law and current law

|  |  |
| --- | --- |
| New law | Current law |
| The Commissioner will be required to provide every applicable taxpayer with a tax receipt, setting out the notional distribution of the individual’s assessed income tax liability to different types of government expenditure, and information on the level of Australian Government debt and its interest cost. | For the 2013-14 income year, the Commissioner will issue tax receipts under his existing administrative powers. |

## Detailed explanation of new law

* 1. The amendments are designed to impose a general obligation on the Commissioner to issue tax receipts that inform taxpayers about how their tax money is notionally spent and other information relevant to the financial performance of the Government.
  2. The amendments are intended to give the Commissioner a sufficient degree of flexibility to prepare the tax receipts in a way that best meets these objectives.
  3. In utilising this flexibility and subject to the other requirements of the amendments, the Commissioner must consult with the Treasurer on the form of the tax receipt and take into account the Treasurer’s views. [Schedule 4, item 2, subsection 70-5(5)]

### Requirement to issue a receipt

* 1. The amendments apply to every individual (natural person) taxpayer assessed to have an income tax liability for an income year that exceeds a threshold determined by the Commissioner. [Schedule 4, item 2, paragraphs 70-5(1)(b) and (c) and subsection 70-5(2)]
  2. The Commissioner has this discretion not to provide tax receipts to certain taxpayers where, because of the low level of income tax assessed to them, the tax receipt is likely to be confusing. Under the Commissioner’s current administrative arrangements, and until the Commissioner makes an alternative determination, the threshold is $100.
  3. The tax receipt will be issued to around 10 million individual taxpayers.
  4. An individual’s ‘income tax liability’ is the result of applying the method statement in subsection 4-10(3) of the *Income Tax Assessment Act 1997* (ITAA 1997) and generally reflects the total amount of the individual’s income tax liability for the year. This is to be distinguished from the taxpayer’s outstanding liability at the end of the year as the annual liability is reduced by credits, including amounts withheld during the year that are not refunded.
  5. Where an individual receives multiple assessments for an income year, a receipt will be provided only for the first assessment. Subsequent assessments with respect to the same income year will not trigger the requirement to issue a receipt. [Schedule 4, item 2, paragraph 70‑5(1)(a)]
  6. The Commissioner will not be required to issue a receipt where the assessment is made more than 18 months after the end of the relevant income year. This limitation is intended to ensure that receipts are issued with timely information, which may not be possible where there has been a delay in making the assessment, for example where the individual has lodged their tax return late. [Schedule 4, item 2, paragraph 70-5(1)(d)]
  7. The Commissioner is also not required to issue a tax receipt where assessment is made prior to the end of the income year. In these rare instances, the administrative cost of producing the tax receipt is likely to be excessive. [Schedule 4, item 2, paragraph 70-5(1)(d)]
  8. Where the Commissioner is required to issue a tax receipt to an individual, the receipt must be provided as soon as practicable after the income tax assessment is made. It is envisaged that, for the majority of applicable taxpayers, the receipt will be issued at the same time as the notice of assessment; however, the receipt does not form part of the notice. [Schedule 4, item 2, subsection 70-5(6)]

### Contents of the receipt

#### Government Expenditure

* 1. The primary purpose of the receipt is to convey information on the different categories of government expenditure, expressed in a way that relates to the individual’s income tax liability. To achieve this, the receipt will generally show the notional dollar amounts of the individual’s income tax distributed to a number of categories of government expenditure. [Schedule 4, item 2, subsection 70-5(3)]
  2. Expenditure in the form of payments to the States and Territories that notionally relates to goods and services tax revenue is excluded from the notional distribution calculation. Other, less significant, items of government expenditure that are notionally hypothecated, in whole or in part, to revenue sources other than personal income tax, are not excluded. [Schedule 4, item 2, paragraph 70-5(3)(c)]
  3. The calculation of the notional distributions will based on aggregate budget expenditure figures for the relevant financial year. For example, an individual who receives an income tax assessment for the 2014-15 income year in November 2015 would receive a tax receipt based on the Budget estimates for the 2014-15 financial year released in May 2015. In the 2014-15 Budget, Australian Government general government sector expenses were reported by function in Statement 6 of *Budget Paper No. 1*.
  4. The calculation would not be updated to reflect subsequent budget updates or the final budget outcome even if those statements are released prior to the preparation of a receipt.

#### Government Debt

* 1. The receipt will include information on the level of Australian Government general government sector gross debt (total face value of Commonwealth stock and securities on issue) for the relevant financial year and the previous financial year. [Schedule 4, item 2, paragraphs 70-5(3)(d) and (e)]
  2. The receipt will also show the estimated level of interest to be paid on government debt during the relevant year. [Schedule 4, item 2, paragraph 70-5(3)(f)]
  3. Again, these figures will be based on estimates published in the Budget before the end of the relevant year. In the 2014-15 Budget, the level of government debt and interest to be paid were published in Statement 7 of Budget Paper No. 1. [Schedule 4, item 2, subsection 70-5(4)]

## Consequential amendments

* 1. A consequential amendment is made to include the definition of a ‘tax receipt’ in the dictionary to the ITAA 1997. [Schedule 4, item 1, ITAA 1997 , definition of ‘tax receipt’ in subsection 955-1(1)]

## Application and transitional provisions

* 1. The amendments made by Schedule 4 commence on the date this Bill receives Royal Assent.
  2. The amendments apply to notices of assessment issued from 1 July 2015 with respect to assessments for the 2014-15 income year and future income years. [Schedule 4, item 3]

## STATEMENT OF COMPATIBILITY WITH HUMAN RIGHTS

## Prepared in accordance with Part 3 of the *Human Rights (Parliamentary Scrutiny) Act 2011*

### *Tax and Superannuation Laws Amendment (2014 Measures No. 4) Bill 2014 — Schedule 4: Personalised tax receipts*

* 1. This Schedule is compatible with the human rights and freedoms recognised or declared in the international instruments listed in section 3 of the *Human Rights (Parliamentary Scrutiny) Act 2011*.

### Overview

* 1. This Schedule to this Bill amends the tax law to provide greater transparency to taxpayers about how their tax money is spent, by requiring the Commissioner of Taxation to issue a tax receipt to individuals for the income tax assessed to them.

### Human rights implications

* 1. This Schedule engages the right to take part in the conduct of public affairs provided for in Article 25 of the *International Covenant on Civil and Political Rights*.
  2. By providing additional information to taxpayers on the decisions and fiscal performance of government, individuals’ capacity to engage in public debate is increased. This supports the right in Article 25.

### Conclusion

* 1. This Schedule is compatible with human rights as it promotes, but does not inhibit, the fulfilment of human rights.

1. Miscellaneous amendments

## Outline of chapter

* 1. Schedule 5 to this Bill makes a number of miscellaneous amendments to the taxation and superannuation laws. These amendments are part of the Government’s commitment to the care and maintenance of the taxation and superannuation systems, and the Government’s broader deregulation agenda.
  2. These amendments include style changes, the repeal of redundant provisions, and the correction of anomalous outcomes and corrections to previous amending Acts.

## Context of amendments

* 1. Miscellaneous amendments to the taxation and superannuation laws such as those contained in Schedule 5 are periodically made to remove anomalies, correct unintended outcomes and clarify the operation of the law. Progressing such amendments gives priority to the care and maintenance of the tax system, a process supported by a 2008 recommendation from the Tax Design Review Panel.
  2. A number of the amendments in Schedule 5 relate to issues lodged on the Tax Issues Entry System (TIES), a platform for members of the community to raise issues regarding the care and maintenance of the Australian Government’s tax and superannuation systems. For more information, please visit the TIES website (www.ties.gov.au).

## Summary of new law

* 1. These miscellaneous amendments address technical deficiencies and legislative uncertainties within several taxation and superannuation provisions.
  2. The table below lists the various parts of this Schedule.

| ***Part*** | ***Title*** |
| --- | --- |
| 1 | Amendments to the style of references to specific Ministers, Departments and Secretaries, and the repeal of redundant provisions. |
| 2 | Excise-related amendments |
| 3 | Renumbering of sections to correct errors in previous amending Acts |
| 4 | Other technical amendments to principal Acts |
| 5 | Other corrections to previous amending Acts |

## Detailed explanation of new law

### Part 1: References to Ministers and Departments

* 1. Part 1 of Schedule 5 makes a number of amendments to the way the tax laws refer to government ministers and departments. These amendments are made as part of a whole-of-government process to standardise drafting practices.
  2. The amendments are intended to increase readability and reduce the need for legislative changes to be made following machinery of government changes, ministerial changes and changes to the Administrative Arrangements Order.

#### References to Treasurer and Treasury

* 1. Part 1 amends the tax laws to replace references to ‘the Treasurer’ with references to ‘the Minister’ and replaces references to ‘the Treasury’ with references to ‘the Department’. Consequential amendments are also made to clarify references to other portfolios. [Schedule 5, items 1 to 6, 8, 12 to 28, 30, 31 and 69 to 72, section 79-100 of the GST Act, sections 6, 79B, 82CB, 82CD, 82CE and 128AE of the ITAA 1936, sections 30‑36, 30‑80, 30-85, 30-265, 30-280,30-285, 30-289, 30-289B, 30-289C, 30-300, 30-305, 30-310, 34-55, 207-115 and 842-105 of the ITAA 1997, and sections 355-50 and 355-65 of Schedule 1 to the TAA 1953]
  2. Section 19A of the *Acts Interpretation Act 1901* provides that generic references to a minister or a department are taken to be references to the ministers and departments of state responsible for administering the relevant provision.
  3. The current law aligns with the current Administrative Arrangements Order. There is no change to the ministerial or departmental responsibilities for any of the amended provisions.

#### Repeal of redundant definitions

* 1. A review of the current tax law definitions that relate to ministers and departments outside the Treasury portfolio revealed that a number of the definitions are no longer in use or could be rationalised.
  2. Consequently, Part 1 repeals redundant definitions and updates related definitions as necessary. [Schedule 5, items 7, 9 to 11, 29, 32 to 68 and 73, sections 6 and 73A of the ITAA 1936, sections 52‑131 and 955-1 and 995-1 of the ITAA 1997, subsection 2(1) of the TAA 1953 and paragraph 355-70(8)(a) of Schedule 1 to the TAA 1953]

#### Transitional and commencement provisions

* 1. Transitional provisions ensure that things done, including decisions taken, under the current law are preserved and continue in force as if they were done under the amended provisions. [Schedule 5, item 74]
  2. The amendments also provide that the Treasurer may make rules to deal with transitional matters arising under Part 1 of the Schedule. [Schedule 5, item 75]
  3. Division 2 of Part 1 repeals the redundant definitions of ‘Transport Department’ and ‘Transport Minister’. However, these definitions will be amended if the Land Transport Infrastructure Amendment Bill 2014 receives Royal Assent. Therefore, the repeals only take effect following the commencement of the other Act. [Schedule 5, item 76, section 955-1 of the ITAA 1997]

### Part 2: Excise-related amendments

* 1. Part 2 makes a number of amendments to the *Aviation Fuel Revenue (Special Appropriation) Act 1988* (AFRSA Act) to remove references to the indexation of rates of duty on aviation fuel under the *Excise Tariff Act 1921* (ETA)*.*
  2. The AFRSA Act grants power to the Minister to fix a rate of duty for aviation fuel by using the method of indexation in the ETA. However, indexation of rates of duty on aviation fuel ceased in August 2001. Accordingly, the provision relating to indexation concepts in the ETAis repealed as it is redundant. [Schedule 5, item 83]
  3. Determinations based on indexation concepts in the ETA continue to apply in circumstances where the determinations were in force at the time the duty was imposed on the aviation fuel. [Schedule 5, item 80, section 3, paragraph(a) of the definition of statutory rate in the AFRSA Act]
  4. Part 2 also makes a number of consequential amendments to reflect the repeal of the indexation measures in the ETA. [Schedule 5, items 77 to 79 and 81 to 82]

### Part 3: Renumbering of previous amendments

* 1. Part 3 makes a number of amendments to renumber provisions in the *Income Tax Assessment Act* 1997 (ITAA 1997) to correct errors identified in recent amending Acts. This Part also corrects cross‑referencing between provisions. [Schedule 5, items 84 to 91, sections 12-5, 26‑100, 40-235, 110-38 and 110-55 of the ITAA 1997]

### Part 4: Other amendments to principal Acts

#### Creditable acquisitions relating to reimbursements

* 1. Subsection 111-5(3) of the GST Act states the situations where a taxpayer is not entitled to claim an input tax credit, notwithstanding that the taxpayer reimbursed an employee for expenses that were directly related to the employee’s duties.
  2. Taxpayers are disentitled from claiming input tax credits if they satisfy any of the paragraphs in subsection 111-5(3) and it is not necessary for all of the paragraphs to be satisfied. In fact, it is impossible for taxpayers to satisfy all of the paragraphs as subparagraph (a)(i) and paragraph (b) are mutually exclusive.
  3. Prior to the amendment, subsection 111-5(3) had the potential to create confusion as it used the word ‘and’ between the paragraphs. Accordingly, the wording of subsection 111-5(3) of the GST Act is amended to clarify that taxpayers are disentitled from claiming input tax credits if they satisfy one or more of the paragraphs. [Schedule 5, item 92, subsection 111-5(3) of the GST Act]
  4. This amendment applies to acquisitions made on or after 1 July 2000. Although the amendment applies retrospectively, it does not alter the substance or operation of the section. [Schedule 5, item 93]

#### Consolidation of the definitions of tax and income tax

* 1. The *Income Tax Assessment Act 1936* (ITAA 1936) uses the terms ‘tax’ and ‘income tax’ interchangeably — they mean the same thing. However, the only entry in that Act’s general definition section appears under ‘income tax or tax’. That makes it difficult to locate the definition for the term ‘tax’; the reader has to know that it is listed under ‘I’.
  2. Accordingly, the amendments split the existing definition into two: one for ‘income tax’; and one for ‘tax’. Each definition appears in its correct alphabetical order, making it simpler to find. There is no change to the meaning of either term. [Schedule 5, items 95 to 97, subsection 6(1) of the ITAA 1936]

#### Correct error in the new special conditions for deductible gift recipients as a result of the introduction of the ACNC

* 1. Division 30 of the ITAA 1997 sets out the rules for working out the deductions a taxpayer may claim for certain gifts or contributions that they make.
  2. Division 30 sets out general categories of deductible gift recipients, for example, welfare and rights recipients, and contains special conditions which must be met by the fund, authority or institution for it to receive gifts that are eligible for a tax deduction. For example, item 4.1.4 in the table in subsection 30-45(1), lists public funds on the register of harm prevention charities, whose special conditions require the funds to be registered under the *Australian Charities and Not-for-profits Commission Act 2012* (ACNC Act).
  3. Similar to the harm prevention charities example in paragraph 5.29, the most common of these conditions deals with the interaction between the Australian Charities and Not‑for‑profits Commission (ACNC) regulatory framework and the tax law endorsement framework for deductible gift recipients that are charities. Consequential amendments were legislated along with the ACNC Act, adding new special conditions for deductible gift recipients that required charities endorsed as deductible gift recipients to also be registered under the ACNC Act in order to remain endorsed to access tax deductibility for gifts provided to them. A 12-month transitional arrangement gave charities time to make any necessary changes to existing arrangements should a small number of them not be eligible for transitional automatic registration.
  4. There are three categories of ACNC-related special conditions — those requiring the endorsed deductible gift recipient to be a registered charity in all instances, those requiring the endorsed deductible gift recipient to be a registered charity if it is *not* an Australian government agency, and those requiring the endorsed deductible gift recipient to be a registered charity if it is not an ACNC type of entity (that is, those deductible gift recipients that aren’t within the charitable sector or aren’t entities in their own right, (for example, sports groups or certain public funds that are merely bank accounts of another charity). In most cases, where the public fund is not an ACNC type of entity but is operated by a charity, that operating charity must be registered.
  5. The special conditions were developed based on the Australian Taxation Office endorsement database and the characteristics of the organisations and funds currently endorsed. However, there are cases where the incorrect category of ACNC-related special conditions was applied to some general categories because the database contained some minor errors or the wrong set of special conditions was allocated to be the deductible gift recipient category.
  6. This incorrect allocation of category is now incorrectly requiring certain organisations to restructure existing arrangements even though they are already covered by the ACNC regulatory framework, adding unintended compliance costs and red tape outside of the original policy intent.
  7. In relation to the public funds listed in item 4.1.4 in the table in subsection 30‑45(1), which currently requires the public fund to be a registered charity, Schedule 5 to this Bill amends the special conditions to instead require the public fund to be a registered charity or be operated by a registered charity. [Schedule 5, item 99, subsection 30‑45(1) of the ITAA 1997]
  8. As the register of harm prevention charities already requires a registered charity to operate the public fund, there was no intention to also require the fund (which might just be a bank account) to also be a registered charity.
  9. In relation to public funds listed in item 5.1.2 in the table in subsection 30‑50(1), which currently requires the public fund to be a registered charity or an Australian government agency, Schedule 5 to this Bill amends the special conditions to instead require the public fund to be an Australian government agency, a registered charity or operated by an Australian government agency or a registered charity. [Schedule 5, item 100, subsection 30‑50(1) of the ITAA 1997]
  10. The error with the special conditions in item 5.1.2 arose because the item covers both public institutions and public funds. Only public institutions were intended to be subject to the stricter special conditions introduced with the ACNC Act, while the new amended conditions are more appropriate for public funds.
  11. In relation to public funds listed in item 5.1.3 in the table in subsection 30‑50(1), which currently requires the public fund to be a registered charity or an Australian government agency, Schedule 5 to this Bill amends the special conditions to instead require the public fund to be an Australian government agency, a registered charity or operated by an Australian government agency or a registered charity. [Schedule 5, item 101, subsection 30‑50(1) of the ITAA 1997]
  12. In relation to public funds listed in item 8.1.1 in the table in subsection 30‑70(1), which currently requires the public fund to be a registered charity or an Australian government agency, Schedule 5 to this Bill amends the special conditions to instead require the public fund to be a registered charity or operated by a registered charity. [Schedule 5, item 102, subsection 30‑70(1) of the ITAA 1997]
  13. In relation to public funds listed in item 8.1.2 in the table in subsection 30‑70(1), which currently requires the public fund to be a registered charity or an Australian government agency, Schedule 5 to this Bill amends the special conditions to instead require the public fund to be a registered charity or operated by a registered charity. [Schedule 5, item 102, subsection 30‑70(1) of the ITAA 1997]
  14. In relation to public funds listed in item 2.1.2 in the table in subsection 30‑25(1), which currently requires the public fund to be a registered charity or an Australian government agency, Schedule 5 to this Bill amends the special conditions to instead require the public fund to be an Australian government agency, a registered charity or operated by an Australian government agency or a registered charity. [Schedule 5, item 98, subsection 30‑25(1) of the ITAA 1997]
  15. The original amendments misallocated these deductible gift recipient public funds to the wrong category of special conditions.

##### *Application provisions*

* 1. These amendments commence on the day this Bill receives Royal Assent and would apply to gifts received on or after 3 December 2012, which is the day the ACNC Act commenced. [Schedule 5, item 103]
  2. No deductible gift recipient will be adversely affected by these changes.

#### Clarifying the continuity of ownership test following the death of a beneficial owner of shares

* 1. Under the company loss recoupment rules, a company is able to deduct prior year losses, or apply capital losses, only if it satisfies the continuity of ownership test or the same business test.
  2. A company satisfies the continuity of ownership test if it satisfies the primary test or the alternative test in respect of voting power, rights to dividends and rights to capital distributions during the ownership test period.
* The primary test is satisfied if, broadly, the same persons beneficially own shares that carry more than 50 per cent of the voting power in the company, and carry rights to more than 50 per cent of the dividend and capital distributions made by the company.
* The alternative test is satisfied if, broadly, it is reasonable to assume that the same persons (none of whom are companies or trustees) control the voting power in the company and have rights to receive more than 50 per cent of the dividends and capital distributions made by the company.
  1. For the purpose of applying the continuity of ownership test after a shareholder dies, the shares that were beneficially owned by the deceased person at the time of death are treated as continuing to be owned by that person so long as the shares are owned by either the trustee of the deceased person’s estate or by a beneficiary of the estate. As a result, a company will not fail the continuity of ownership test simply because a shareholder dies.
  2. This concessional treatment for deceased estates operates appropriately where the primary test applies as the focus is on the beneficial ownership of shares in a loss company. However, it is not clear that the concession operates effectively for the purpose of applying the alternative continuity of ownership test.
  3. The amendments ensure that the concessional treatment for deceased estates operates appropriately for the purposes of applying both the primary test and the alternative test. [Schedule 5, item 106, section 165-205 of the ITAA 1997]
  4. The amendments apply to assessments for the 1997-98 income year and later income years. In this regard, the amendments clarify that the continuity of ownership tests operate as intended and are beneficial to taxpayers. [Schedule 5, item 107]
  5. This amendment addresses TIES issue 31/2010.

#### Removing technical defects in the franking deficit tax offset rules

* 1. Franking deficit tax arises when an entity has a deficit in its franking account at the end of an income year. The payment of franking deficit tax gives rise to a tax offset which can be applied to reduce an entity’s income tax liability.
  2. The franking deficit tax offset rules are modified for life insurance companies to ensure that the franking deficit tax offset applies only to reduce an income tax liability of a life insurance company that is attributable to its shareholders (as distinct from its policyholders).
  3. Division 63 of the ITAA 1997 contains rules that prioritise the order in which tax offsets are applied. When the Division was inserted in 2006, consequential amendments were made to the franking deficit tax offset rules in section 205‑70. As a result, the modified franking deficit tax offset rules for life insurance companies do not operate effectively.
  4. To overcome this concern, the amendments modify sections 219‑70 and 219‑75 to ensure that, for the purposes of applying section 205-70 to a life insurance company, the section applies as if the reference to the company’s basic income tax liability in section 63‑10 were a reference to the part of such an amount in respect of the company that is attributable to its shareholders. [Schedule 5, items 108 to 111, sections 219‑70 and 219‑75 of the ITAA 1997]
  5. Further, if an entity joins a consolidated group holding excess franking deficit tax offsets, Subdivision 709‑C of the ITAA 1997 applies to ensure that, broadly:
* if the joining entity has excess franking deficit tax offsets at the joining time, that excess is transferred to the head company; and
* if an entity leaves a consolidated group, any excess franking deficit tax offsets are retained by the head company.
  1. The amendments make some technical corrections to Subdivision 709‑C to ensure that it reflects the 2006 amendments to the franking deficit tax offset rules. [Schedule 5, items 115 to 118, sections 709‑185 and 709‑190 of the ITAA 1997]
  2. The amendments apply from the 2006-07 income year, that is, from the commencement of Division 63. In this regard, the amendments make technical corrections to clarify that the franking deficit tax offset provisions operate as intended and are beneficial to taxpayers. [Schedule 5, items 112 and 119]
  3. This amendment addresses TIES issue 11/2011.

#### Clarifying the operation of the consolidation tax cost setting rules for depreciating assets

* 1. When an entity joins a consolidated group, the consolidation tax cost setting rules apply to reset the tax costs of its assets. If a depreciating asset receives an increased tax cost under those rules, and the joining entity used the prime cost method to work out its depreciation deductions, paragraph 701‑55(5)(d) of the ITAA 1997 requires the head company to choose an effective life for that asset in accordance with subsections 40‑95(1) and (3) for the purpose of determining future depreciation deductions.
  2. However, for certain intangible depreciating assets, the effective life is specified in subsection 40‑95(7) (rather than being determined under subsections 40‑95(1) and (3)). The effective lives of certain other depreciating assets (such as indefeasible rights to use telecommunications cables, and mining, quarrying and prospecting rights) are specified under subsections 40‑95(8) to (10).
  3. Therefore, the amendments make a technical correction to paragraph 701‑55(2)(d) to ensure that, for relevant assets, the effective life of the asset can be worked out under subsections 40‑95(7) to (10). [Schedule 5, item 114, paragraph 701‑55(5)(d) of the ITAA 1997]
  4. This amendment addresses TIES issue 22/2011.

#### Clarifying the operation of the consolidation provisions for deducting bad debts

* 1. Subdivision 709‑D of the ITAA 1997 specifies the circumstances in which an entity can deduct a bad debt that is brought into a consolidated group by a joining entity, or that is taken out of the group by a leaving entity — that is, the Subdivision applies where, for part of the period that the bad debt exists, the debt has been owed to a member of a consolidated group.
  2. The object of the Subdivision is to, broadly, ensure that the claimant can deduct a debt, or part of a debt, only if an entity that was owed the debt for a debt test period could have deducted the debt if it had been written off as bad at the end of that period.
  3. Where a debt is taken to be owed to the head company of a consolidated group (because of the single entity rule), a debt test period for the head company ends when the subsidiary member of the consolidated group that is actually owed the debt leaves the group and joins another consolidated group (item 4 of the table in subsection 709‑215(4)).
  4. However, item 4 does not apply when the subsidiary member of a consolidated group that is actually owed the debt leaves the group but does not join another consolidated group. As a result, in these circumstances the former subsidiary member cannot deduct the debt when it is subsequently written off as bad.
  5. To address this concern, the amendments modify the table in subsection 709‑215(4) to clarify that, where a debt is taken to be owed by the head company of a consolidated group (because of the single entity rule), a debt test period for the head company ends when the subsidiary member of the consolidated group that is actually owed the debt leaves the group but does not join another consolidated group. [Schedule 5, item 120, item 4A of the table in subsection 709‑215(4) of the ITAA 1997]
  6. The amendment applies in relation to debt test periods starting on or after 1 July 2002. In this regard, the amendment makes a technical correction to clarify that the relevant provisions operate as intended and is beneficial to taxpayers. [Schedule 5, item 121]
  7. This amendment addresses TIES issue 21/2011.

#### Benefit certificates for defined benefit superannuation schemes

* 1. A benefit certificate is a certificate provided by an actuary relating to a defined benefit superannuation scheme and specifies the rate that is the notional employer contribution rate in relation to a specified class of employees that are members of a scheme.
  2. Paragraph 10(3)(a) of the *Superannuation Guarantee (Administration) Act 1992* requires superannuation funds to obtain a new benefit certificate when there is a change to the scheme in a way that affects the level or method of calculation of benefits provided by the scheme for the class of employees specified in the certificate.
  3. The provision may impose unwarranted administrative costs on superannuation funds in that they must obtain a new certificate in circumstances when the minimum benefits of members has not changed.
  4. The amendment provides that superannuation funds must obtain a new benefit certificate only when there has been a change to the minimum benefits of a class of employees. [Schedule 5, item 122, paragraph 10(3)(a) of the Superannuation Guarantee (Administration) Act 1992]

#### Note to subsection 8AAZLGA(7)

* 1. A Chair’s amendment to Schedule 7 to the *Tax and Superannuation Laws Amendment (2012 Measures No. 1) Act 2012* changed some of the section and paragraph numbers in the TAA 1953. The paragraph number in the note to subsection 8AAZLGA(7) of theTAA 1953 was overlooked and never updated. Accordingly, the paragraph number in the note to subsection 8AAZLGA(7) is amended so that it correctly refers to paragraph 14ZW(1)(aad). [Schedule 5, item 123, the note to subsection 8AAZLGA(7) of the TAA 1953]

#### Amendments to withholding matters and declarations

* 1. Section 15-30 of Schedule 1 to the TAA 1953 requires the Commissioner to have regard to particular matters when making a withholding schedule for the purpose of calculating a withholding payment or an alienated services payment to which Division 13 applies. One of the matters that the Commissioner must have regarded, under paragraph 15-30(d), is ‘prescribed tax offsets’. Prescribed tax offsets are individually listed in Regulation 24 of the *Taxation Administration Regulations 1976*. These amendments remove the requirement to prescribe specific ‘tax offsets’. [Schedule 5, item 126, paragraph 15-30(d) of Schedule 1 to the TAA 1953]
  2. Removing the requirement to first prescribe the tax offset before the Commissioner must have regard to it will allow the Commissioner to have regard to new tax offsets when making a withholding schedule, from the time the tax offset is effective, and not only after it has been prescribed.
  3. This is more administratively efficient and flexible.
  4. In addition, section 15-50 of Schedule 1 to the TAA 1953, requires individuals to give a declaration to an entity if they expect to receive a withholding payment or an alienated services payment from that entity, and they want that entity to take a prescribed matter into account when making the payment. This declaration is required to be in the approved form (see generally section 388-50 of Schedule 1 to the TAA 1953). Prescribed matters are individually listed in Regulation 26 of the *Taxation Administration Regulations 1976*.
  5. These amendments remove the need to ‘prescribe’ specific matters that can be included in these declarations. Instead, the Commissioner can have regard to any relevant matters when preparing the approved form(s). This is also more administratively efficient and flexible. [Schedule 5, items 127 to 132, section 15-50 of Schedule 1 to the TAA 1953]
  6. Currently, there are a number of prescribed matters in Regulations 24 and 26 of the *Taxation Administration Regulations 1976*. After these amendments, these regulations will become redundant and will be repealed from the *Taxation Administration Regulations 1976* at the first convenient opportunity.

#### Lodgement of returns under the Customs Act

* 1. The amendments in Schedule 5 provide that lodgement of particular returns in relation to taxable importations under paragraphs 69(8)(a), to (d) of the *Customs Act 1901* (Customs Act), result in a deemed assessment. [Schedule 5, item 134, subsection 155-15(1) in Schedule 1 to the TAA 1953]
  2. In 2012, changes were made to section 69 of the Customs Act to insert paragraphs 69(8)(a), to (d) which deal with returns relating to the importation of goods. Prior to this amendment returns relating to the importation of goods were dealt with under paragraph 69(5)(c). The amendment in Schedule 5 amends the table of self‑assessed amounts in subsection 155-15(1) to accurately reflect the current provision in the Customs Act under which assessable amounts arise concerning importations.
  3. This amendment applies to GST payable on or after the day following Royal Assent. [Schedule 5, item 135]
  4. This amendment addresses TIES issue 12/2012.

#### Machinery provisions for penalties

* 1. The uniform penalty rules in Division 298 of Schedule 1 to the TAA 1953 contain a range of machinery provisions for various penalties, which allow the Commissioner to impose, enforce and collect penalties. Section 298-5 of Schedule 1 to the TAA 1953 sets out the administrative penalties that are subject to these provisions. No penalties are established under Division 298. [Schedule 5, item 137, subsection 298-5 in Schedule 1 to the TAA 1953]
  2. Regulations have recently been made under Division 420 of Schedule 1 to the TAA 1953 that prescribe various quarterly reporting obligations for entities in the building and construction services industry. Entities that fail to comply with these reporting obligations are liable to an administrative penalty of 20 penalty units. To ensure that the Commissioner is able to collect and enforce these penalties a reference to section 420 is added to section 298-5. [Schedule 5, item 137, subsection 298-5 in Schedule 1 to the TAA 1953]

#### Hardship discretion and the general interest charge

* 1. Division 340 of Schedule 1 to the TAA 1953 allows the Commissioner to release certain taxpayers from certain liabilities in the case of serious hardship.
  2. Section 340-10 of the Schedule refers to the general interest charge imposed under a now-repealed provision of the ITAA 1936.
  3. The amendment corrects this and clarify that the Commissioner’s discretion applies to charges imposed under the old provision. [Schedule 5, item 138, section 340-10 in Schedule 1 to the TAA 1953]

#### Disclosure of protected taxpayer information to Centrelink

* 1. Table item 5A of subsection 355-65(2) of Schedule 1 to the TAA 1953 allows taxation officers to disclose protected information relating to taxpayers to the Chief Executive Officer of Centrelink for the purposes of administering the *Paid Parental Leave Act 2010*.
  2. On 1 July 2011, the title of ‘Chief Executive Officer of Centrelink’ changed to become ‘Chief Executive Centrelink’. This amendment updates the reference to reflect the change. [Schedule 5, item 139, subsection 355-65(2) to Schedule 1 to the TAA 1953]
  3. The amendment applies retrospectively from 1 July 2011. This clarifies that disclosures made after 1 July 2011 are permitted notwithstanding the change in the recipient’s title. [Schedule 5, item 140]

#### Style, spelling, grammatical and typographical errors

* 1. The following amendments are made to correct minor style, spelling and typographical errors:
     + - 1. : Style, spelling, grammatical and typographical errors

| Item(s) | Provision Affected |
| --- | --- |
| Schedule 5, item 94 | Paragraph 43-7(2)(a) of the *Fuel Tax Act 2006* |
| Schedule 5, items 104 and 105 | Section 104-255 of the ITAA 1997 |
| Schedule 5, item 113 | The note to section 355-400 of the ITAA 1997 |
| Schedule 5, item 125 | Paragraph 14ZW(1AABA)(b) of the TAA 1953 |
| Schedule 5, item 133 | Section 45-235 of Schedule 1 to the TAA 1953 |
| Schedule 5, item 136 | Section 280-170 of Schedule 1 to the TAA 1953 |

### Part 5: Corrections to previous amending Acts

* 1. Part 5 of Schedule 5 makes a number of corrections to previous amending Acts to ensure that the amendments made under the earlier Acts are effective.
  2. With the exception of the amendments made to the Superannuation Legislation Amendment (Stronger Super) Act 2012, the amendments in this Part commence immediately following the commencement of the provisions they amend. This retrospectivity is necessary to ensure the amending Acts operate as intended.
  3. The amendments to the Superannuation Legislation Amendment (Stronger Super) Act 2012 introduce new provisions, which commence from 1 July 2014.

#### New Business Tax System (Consolidation, Value Shifting, Demergers and Other Measures) Act 2002

* 1. Schedule 13 of the *New Business Tax System (Consolidation, Value Shifting, Demergers and Other Measures) Act 2002* inserted components of the simplified imputation system relating to the treatment of exempting entities into the ITAA 1997.
  2. Schedule 15 of the Act inserted control and common ownership rules relevant to the operation of the value shifting rules into the ITAA 1997.
  3. These amendments make some drafting corrections to ensure that minor technical consequential amendments made by Schedules 13 and 15 of the *New Business Tax System (Consolidation, Value Shifting, Demergers and Other Measures) Act 2002* are effective. [Schedule 5, items 141 to 143, item 34 of Schedule 13 and item 19 of Schedule 15 to the New Business Tax System (Consolidation, Value Shifting, Demergers and Other Measures) Act 2002]

#### ***Superannuation Legislation Amendment (Stronger Super) Act 2012 — Clarifying the date that employers are subject to the superannuation data and payment standards***

* 1. The Superannuation Legislation Amendment (Stronger Super) Act 2012 amended the *Superannuation Industry (Supervision) Act 1993* and the *Retirement Savings Accounts Act 1997* to introduce data and payment standards relating to certain superannuation transactions undertaken by superannuation entities, retirement savings account providers and employers.
  2. The application provision in Schedule 1 to the *Superannuation Legislation Amendment (Stronger Super) Act 2012* included a point in time test based on the number of employees an employer has on 1 July 2014. A ‘medium to large’ employer (with 20 or more employees) will apply the data and payment standards from 1 July 2014, and a ‘small’ employer (with less than 20 employees) will apply the data and payments standards from 1 July 2015. The application provision omitted to explain what happens where an entity commences business as a medium or large employer in the period 2 July 2014 to 30 June 2015.
  3. The amendments provide that an entity that starts to be an employer during the period 2 July 2014 to 30 June 2015 will apply the data and payment standards at the time it becomes a medium to large employer. The amendments also clarify that all employers will be subject to the data and payment standards from 1 July 2015 onwards. [Schedule 5, items 144 and 145, subitems 20(1A) and (3A) of Schedule 1 to the Superannuation Legislation Amendment (Stronger Super) Act 2012]

#### Tax Laws Amendment (2009 Budget Measures No. 2) Act 2009

* 1. Schedule 1 to *Tax Laws Amendment (2009 Budget Measures No. 2) Act 2009* contained amendments relating to the taxation treatment of employee share schemes. Item 55 of that Schedule made a consequential technical correction to a note to subsection 707‑325(1) of the ITAA 1997 (which is part of the consolidation provisions in the law).
  2. The amendment makes a minor technical correction to clarify that the amendment made by item 55 of the Act is to note 1 to subsection 707‑325(1). [Schedule 5, item 146, item 55 of Schedule 1 to the Tax Laws Amendment (2009 Budget Measures No. 2) Act 2009]

#### Tax Laws Amendment (2012 Measures No. 9) Act 2012 — Failures to Provide information to the Commissioner

* 1. An error concerning the commencement dates of certain amendments prevented them from operating as intended.
  2. The amendments clarify that an offence under paragraph 8C(1)(a) of the TAA 1953, which concerns failures to provide information to the Commissioner, is not limited to failures to furnish an approved form. [Schedule 5, items 124 and 147, paragraph 8C(1)(a) of the TAA 1953 and item 29 of Schedule 6 to the Tax Laws Amendment (2012 Measures No. 9) Act 2012]

#### Tax Laws Amendment (2011 Measures No. 9) Act 2012 — Guide Material

* 1. Amendments correct two minor description errors in the 2012 amending Act, ensuring that the amendments made by that Act operate as intended.
  2. These amendments commence retrospectively from 21 March 2012, the date of commencement for the amended provisions. [Schedule 5, items 148 and 149, items 83 and 140 of Schedule 6 to the Tax Laws Amendment (2011 Measures No. 9) Act 2012]

#### Tax Laws Amendment (2012 Measures No. 3) Act 2012 — Seasonal Labour Mobility Program

* 1. An error concerning the location of certain amendments prevented them from operating as intended.
  2. The amendments will correct a cross-referencing error to the Seasonal Labour Mobility Program withholding tax provisions. [Schedule 5, item 150, item 12 of Schedule 1 to the Tax Laws Amendment (2012 Measures No. 3) Act 2012]

#### Tax Laws Amendment (2012 Measures No. 6) Act 2013 — Farm management deposits

* 1. The *Tax Laws Amendment (2012 Measures No. 6) Act 2013*, amended Division 393 of the ITAA 1997 (the farm management deposit provisions) to clarify, with retrospective effect, that the 12-month period in which amounts withdrawn from a farm management deposit would be taken never to have been part of a farm management deposit ended before, not on, the one year anniversary of the deposit.
  2. These amendments ensure that assessments may be amended to give effect to this clarification even where the amendment period for the taxpayer might otherwise have passed. [Schedule 5, items 151 and 152, section 4 of the Tax Laws Amendment (2012 Measures No. 6) Act 2013]

#### Tax Laws Amendment (Research and Development) Act 2011

* 1. Amendments correct two minor description errors in the 2011 amending Act, ensuring that the amendments made by that Act operate as intended. [Schedule 5, items 153 and 154, items 49 and 50 of Schedule 5 to the Tax Laws Amendment (Research and Development) Act 2011]

#### Tax Laws Amendment (Temporary Budget Repair Levy) Act 2014

* 1. Section 3 of the *Tax Laws Amendment (Temporary Budget Repair Levy) Act 2014* provides for the amendments contained in the Act’s Schedules to apply according to their terms as far as they amend other Acts, as intended.
  2. An amendment is made to ensure the correct operation of section 3 and to provide a standard clarification that the Governor-General may continue to amend, or repeal, the 1976 Regulations. [Schedule 5, items 155 and 156, section 3 of the Tax Laws Amendment (Temporary Budget Repair Levy) Act 2014]

## STATEMENT OF COMPATIBILITY WITH HUMAN RIGHTS

## Prepared in accordance with Part 3 of the *Human Rights (Parliamentary Scrutiny) Act 2011*

### Tax and Superannuation Laws Amendment (2014 Measures No. 4) Bill 2014 — Schedule 5: Miscellaneous amendments

* 1. This Schedule is compatible with the human rights and freedoms recognised or declared in the international instruments listed in section 3 of the *Human Rights (Parliamentary Scrutiny) Act 2011*.

### Overview

* 1. This Schedule makes a number of miscellaneous amendments to the taxation and superannuation laws. These amendments are part of the Government’s commitment to the care and maintenance of the taxation and superannuation systems.
  2. These amendments include style changes, the repeal of redundant provisions, and the correction of anomalous outcomes and corrections to previous amending Acts.

### Human rights implications

* 1. These amendments make a number of minor and machinery changes to the taxation and superannuation provisions to ensure the provisions are consistent with their original policy intent. As such, this Schedule does not engage any of the applicable rights or freedoms.

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