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THE PARLIAMENT OF THE COMMONWEALTH OF AUSTRALIA

HOUSE OF REPRESENTATIVES

TAX AND SUPERANNUATION LAWS AMENDMENT (2013 MEASURES NO. 1) BILL 2013

EXPLANATORY MEMORANDUM

(Circulated by the authority of the
Deputy Prime Minister and Treasurer, the Hon Wayne Swan MP)

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Glossary

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

Abbreviation	*Definition*
ASIC	Australian Securities and Investments Commission
ATO	Australian Taxation Office
CGT	Capital Gains Tax
Commissioner	Commissioner of Taxation
DASP	Departing Australia Superannuation Payment
FBT	Fringe Benefits Tax
FBTAA	*Fringe Benefits Tax Assessment Act 1986*
IIO	Irrigation infrastructure operator
IT(TP)A 1997	*Income Tax (Transitional Provisions) Act 1997*
ITAA 1936	*Income Tax Assessment Act 1936*
ITAA 1997	*Income Tax Assessment Act 1997*
MEC group	multiple entry consolidated group
MRRT	Minerals Resource Rent Tax
MRRT(CATP)A 2012	*Minerals Resource Rent Tax (Consequential Amendments and Transitional Provisions) Act 2012*
MRRTA 2012	*Minerals Resource Rent Tax Act 2012*
MYEFO	Mid-Year Economic and Fiscal Outlook
NANE	Non-assessable non-exempt
PAYG	Pay-as-you-go
PRRT	Petroleum Resource Rent Tax
PRRTAA 1987	*Petroleum Resource Rent Tax Assessment Act 1987*
RBA	running balance account
Review	Super System Review

Abbreviation	***Definition***
RIS	regulation impact statement
S(DASPT) Act	*Superannuation (Departing Australia Superannuation Payment Tax) Act 2007*
S(UMLM) Act	*Superannuation (Unclaimed Money and Lost Members) Act 1999*
SIS Act	*Superannuation Industry (Supervision) Act 1993*
SIS Regulations	*Superannuation Industry (Supervision) Regulations 1994*
SMSF	self managed superannuation fund
SRWUIP	Sustainable Rural Water Use and Infrastructure Program
TAA 1953	*Taxation Administration Act 1953*
The Commissioner	Commissioner of Taxation
TIOEPA 1983	*Taxation (Interest on Overpayments and Early Payments) Act 1983*
Water Department	Department of Sustainability, Environment, Water, Population and Communities
Water Minister	Minister for Sustainability, Environment, Water, Population and Communities
Working Group	Business Tax Working Group

General outline and financial impact

Taxation of interest on unclaimed money

Schedule 1 to this Bill amends the income tax and superannuation law to ensure that income tax is generally not payable on the interest paid by the Commonwealth on unclaimed money from 1 July 2013.

Date of effect: 1 July 2013.

Proposal announced: In the 2012-13 Mid-Year Economic and Fiscal Outlook (MYEFO), the Government announced reforms to unclaimed money and lost superannuation. As part of these reforms, interest will accrue and be payable on unclaimed money that is reclaimed from 1 July 2013.

The *Treasury Amendment (Unclaimed Money and Other Measures) Act 2012* was enacted to give effect to these reforms. This Act did not deal with the taxation of interest paid on unclaimed money.

During the Parliamentary consideration of this legislation, the Government advised the Senate Standing Committee on Economics of its intention that this interest would be exempt from tax and this was included in the Senate Committee's report released on 19 November 2012.

Financial impact: Nil. The Government's intention to ensure that interest paid by the Commonwealth in respect of unclaimed money is not subject to income tax was reflected in the financial impact of the Treasury Amendment (Unclaimed Money and Other Measures) Bill 2012.

Human rights implications: This Schedule does not raise any human rights issues. See *Statement of Compatibility with Human Rights* — Chapter 1, paragraphs 1.43 to 1.51.

Compliance cost impact: Nil. This measure is a minor consequential amendment. It will only affect a very small proportion of the business and not-for-profit sector in very limited circumstances. As it is a tax exemption it prevents affected businesses from needing to undertake compliance activities, avoiding costs.

Fringe benefits tax — reform of airline transport fringe benefits

Schedule 2 to this Bill amends the *Fringe Benefits Tax Assessment Act 1986* to align the special rules for calculating airline transport fringe benefits with the general provisions dealing with in-house property fringe benefits and in-house residual fringe benefits.

The method for determining the taxable value of airline transport fringe benefits is also updated to simplify the practical operation of the law and to better reflect the economic value of the benefit.

Date of effect: 7:30 pm by legal time in the Australian Capital Territory on 8 May 2012.

Proposal announced: This measure was announced in the 2012-13 Budget and in the Treasurer and Assistant Treasurer's Joint Media Release No. 034 of 8 May 2012.

Financial impact: Unquantifiable.

Human rights implications: This Schedule does not raise any human rights issues. See *Statement of Compatibility with Human Rights* — Chapter 2, paragraphs 2.82 to 2.86.

Compliance cost impact: Nil.

Sustainable Rural Water Use and Infrastructure Program

Schedule 3 to this Bill amends the *Income Tax Assessment Act 1997* to allow participants in the Sustainable Rural Water Use and Infrastructure Program (SRWUIP) to choose to make payments they derive under the program free of income tax (including capital gains tax), with expenditure relating to the infrastructure improvements required under the program then being non-deductible.

Date of effect: Applies to payments made by the Commonwealth under a SRWUIP program on or after 1 April 2010, to reflect the date on which the Commonwealth signed the first contracts under the NSW Private Irrigation Infrastructure Operators Program (a major element of SRWUIP). Because irrigators enter into a SRWUIP program voluntarily and have the right to choose the new income tax treatment or to continue with the existing treatment, they suffer no disadvantage from this measure.

Proposal announced: 18 February 2011

Financial impact:

2012-13	***2013-14***	***2014-15***	***2015-16***
-$35m	-$30m	$5m	$15m

Human rights implications: This Schedule is compatible with human rights. See *Statement of Compatibility with Human Rights* — Chapter 3, paragraphs 3.87 to 3.95.

Compliance cost impact: This measure may impose some initial compliance costs on irrigators in choosing between the existing and new treatments. It may involve lower ongoing compliance costs for those who choose the new treatment because that removes SRWUIP amounts and related expenditure from the tax system.

Self managed superannuation funds — acquisitions and disposals of certain assets between related parties

Schedule 4 to this Bill amends the *Superannuation Industry (Supervision) Act 1993* to prescribe requirements for acquisitions and disposals of certain assets between self managed superannuation funds (SMSFs) and related parties. These requirements ensure that these transactions are conducted with transparency and are not used to circumvent the requirements of the superannuation law.

Date of effect: This measure applies to transactions occurring on or after 1 July 2013.

Proposal announced: This measure was announced in the then Assistant Treasurer and Minister for Financial Services and Superannuation's Stronger Super Reforms Media Release, No. 024 of 16 December 2010. In September 2011, the Minister released the Stronger Super Information Pack, outlining key aspect of the Stronger Super Reforms. The Minister for Financial Services and Superannuation, Employment and Workplace Relations announced further details of these reforms in Media Release No. 044 of 13 July 2012.

Financial impact: Nil.

Human rights implications: Schedule 4 to the Bill does not raise any human rights issues. See *Statement of Compatibility with Human Rights* — Chapter 4, paragraphs 4.76 to 4.87.

Compliance cost impact: Low.

Summary of regulation impact statement

Regulation impact on business

Impact: A regulation impact statement for the measure contained in Schedule 4 to this Bill has been assessed as adequate by the Office of Best Practice Regulation.

Main points:

- Currently SMSF trustees are permitted to dispose of assets to related parties. They are prohibited from acquiring assets from related parties, subject to certain exceptions for assets such as listed securities and business real property.
- Related party transactions lack transparency and are open to abuse because the buyer and seller are often the same person, or are otherwise closely related. This is particularly the case where the transaction is conducted outside a formal market. The most common example of this is transfers of listed securities.
- There is a risk that related party transfers that occur 'off-market' or outside a formal market may involve transaction date or asset value manipulation to illegally benefit the SMSF or related party, for example, by circumventing the contribution caps and avoiding tax liabilities.
- Given the risk of abuse, new rules requiring transfers to be conducted through an underlying market or supported by an independent valuation were recommended.
- All stakeholders in the SMSF working group supported the recommendation to require transfers of assets between SMSFs and related parties to be supported by an independent valuation where there is no underlying market. Views regarding the recommendation for transfers to be conducted through an underlying market where one exists were mixed.
- It was concluded that the costs associated with these new rules would be low and affect only a small number of funds.

Loss carry-back

Schedules 5 and 6 amend the income tax law to allow corporate tax entities that have paid tax in the past, but are now in a tax loss position, to carry their loss back to those past years to obtain a refund of some of the tax they previously paid.

This is done through the mechanism of a refundable tax offset. The tax offset the entity can get is the lowest of:

- the tax value of the amount of the loss the entity chooses to carry back;
- the tax payable on $1 million taxable income ($300,000 at the current corporate tax rate);
- the entity's franking account balance at the end of the current year; and
- the tax liability for the year(s) the entity carries the loss back to.

Date of effect: These amendments apply to assessments for the 2012-13 income year and later income years.

Proposal announced: The measure was announced in the Assistant Treasurer and Minister for Small Business' Joint Media Release No. 022 of 6 May 2012.

Financial impact: The revenue impact of this measure is as follows:

2012-13	*2013-14*	*2014-15*	*2015-16*
-	-$150m	-$250m	-$300m

Human rights implications: Schedules 5 and 6 do not raise any human rights issue. See *Statement of Compatibility with Human Rights* — Chapter 8.

Compliance cost impact: The compliance cost for taxpayers that will arise from making the choice to obtain a refundable loss carry-back tax offset will be insignificant. As the process of making a claim for most taxpayers will involve lodging the current year return, no additional compliance costs are expected to arise. Taxpayers are already required to keep records concerning their losses.

Summary of regulation impact statement

Regulation impact on business

Impact: Schedules 5 and 6 give a corporate tax entity the choice of carrying back all or part of a tax loss from the current income year, or from the preceding income year, against an unutilised income tax liability for either of the two years before the current year. The measure applies to assessments for the 2012-13 and later income years. A transitional carry-back period of only one year applies for the 2012-13 income year.

Main points:

- Loss carry-back predominantly affects existing businesses that have been profitable in the recent past and are considering what changes they need to make in order to remain competitive or return to profitability.
- The measure will support businesses, particularly small and medium businesses that are not able to take advantage of the consolidation regime's loss utilisation rules (where losses incurred by one member of the group can be offset against income earned by other members of the same group).
- Firms that have recourse to loss carry-back can benefit from the improved cash flow that results from more timely and certain access to tax losses.
- The measure reduces the tax system's bias against sensible risk taking and thereby supports investment in innovation and adapting to changing economic circumstances.
- Carrying losses back flattens taxable income peaks and troughs. Consequently, this can help the economy in a downturn and allow for faster recovery of government revenue when the economy rebounds.

Miscellaneous amendments

Schedule 7 makes a number of miscellaneous amendments to the taxation laws as part of the Government's commitment to uphold the integrity of the taxation system.

Date of effect: Unless otherwise indicated in Chapter 9 of this explanatory memorandum, the amendments in Part 1 will commence on

1 July 2012, and the amendments in Parts 2 and 3 will commence on Royal Assent. Notwithstanding the retrospective nature of many of these amendments, they will not adversely impact upon any taxpayers. See paragraphs 9.253 to 9.263 for more information about the commencement and application provisions.

Proposal announced: The amendments in Part 1 were publicly released for consultation on the Treasury website on 15 August 2012. The amendments in Parts 2 and 3 were publicly released for consultation on the Treasury website on 21 December 2012.

Financial impact: These amendments will have a minimal impact on revenue over the forward estimates.

Human rights implications: These amendments do not raise any human rights issues. See *Statement of Compatibility with Human Rights* — Chapter 9, paragraphs 9.266 to 9.270.

Compliance cost impact: Negligible.

Taxation of interest on unclaimed money

Outline of chapter

1.1 Schedule 1 to this Bill amends the income tax and superannuation law to ensure tax is not payable on interest paid by the Commonwealth in relation to unclaimed money reclaimed from 1 July 2013.

1.2 References in this chapter are to the *Income Tax Assessment Act 1997* unless otherwise specified.

Context of amendments

1.3 In the 2012-13 Mid-Year Economic and Fiscal Outlook (MYEFO), the Government announced reforms to the treatment of unclaimed money.

1.4 Unclaimed money is money held by an institution on behalf of an owner, where the institution has lost contact with and cannot locate the owner, and the money is held in:

- a bank account;
- a First Home Saver Account;
- a life insurance policy;
- superannuation; or
- corporate property.

1.5 Different rules apply to each type of unclaimed money.

1.6 Unclaimed superannuation is further divided into three classes:

- 'general' unclaimed superannuation;
- unclaimed superannuation of former temporary residents; and

- lost member accounts.

1.7 The reforms announced in the 2012-13 MYEFO widened the circumstances in which money is unclaimed money. Generally this has resulted in money being recognised earlier as lost or unclaimed and therefore required to be transferred to the Australian Taxation Office (ATO) (for superannuation) or the Australian Securities and Investments Commission (ASIC) (for all other forms of unclaimed money). This allows these agencies to take active steps to reconnect individuals with their funds sooner, helping to reunite people with their money and preventing the funds from being gradually eroded by fees and charges.

1.8 The reforms also provide for the payment of interest on the unclaimed money for the period it is held by the Government after 1 July 2013. The Government will pay interest at a rate linked to the Consumer Price Index to preserve the real value of the unclaimed money.

1.9 Under the current law, in most cases this interest paid by the Commonwealth on the unclaimed money would be subject to income tax. This is inconsistent with the Government's objective of ensuring the real value of unclaimed money is preserved, as individuals would receive the real value reduced by the relevant tax on the amounts of interest. To achieve its objective, the Government is legislating to ensure that interest paid by the Commonwealth on unclaimed money is generally not subject to income tax.

Summary of new law

1.10 Schedule 1 amends the law to ensure that income tax is not generally payable on interest paid by the Government in relation to unclaimed money reclaimed from 1 July 2013.

1.11 For unclaimed superannuation money, Part 1 of Schedule 1 makes a payment of interest a tax free component of a superannuation benefit. Consistent with other tax free superannuation benefits, these interest payments are non-assessable non-exempt income.

1.12 For other forms of unclaimed money, Part 2 of Schedule 1 makes a payment of interest on these forms of unclaimed money exempt income.

Comparison of key features of new law and current law

New law	***Current law***
Unclaimed superannuation	
Interest paid by the Commonwealth on payments of unclaimed superannuation from 1 July 2013, other than interest paid to former temporary residents, is a tax free component of a superannuation benefit.	The taxable treatment of interest paid by the Commonwealth on payments of unclaimed superannuation varies. Some payments of interest are a taxable component of a superannuation benefit. Others are not a superannuation benefit and are subject to income tax under ordinary principles. In some cases the treatment is ambiguous or unclear.
Unclaimed superannuation and Departing Australia Superannuation Payments	
Interest paid on the return of unclaimed superannuation to former temporary residents after 1 July 2013 is subject to Departing Australia Superannuation Payment (DASP) tax at a rate of 45 per cent. Interest paid to current residents of Australia in respect of unclaimed superannuation is not subject to DASP tax.	DASP tax applies to payments of amounts of superannuation, including payments of interest on unclaimed superannuation, to former temporary residents. Different rates of DASP tax apply to components of the superannuation benefit, depending on whether they are tax free or taxable and, if taxable, whether they have been taxed in the fund. DASP tax applies even where the former temporary resident is again an Australian resident.
Unclaimed bank accounts	
Interest paid by the Commonwealth in respect of unclaimed bank accounts is exempt from income tax.	Interest paid by the Commonwealth in respect of unclaimed bank accounts is subject to income tax.
Unclaimed corporate property	
Interest paid by the Commonwealth in respect of unclaimed corporate property is exempt from income tax.	Interest paid by the Commonwealth in respect of unclaimed corporate property is subject to income tax.
Unclaimed First Home Saver Accounts	
Interest paid by the Commonwealth in respect of unclaimed First Home Saver Accounts is exempt from income tax.	Interest paid by the Commonwealth in respect of unclaimed First Home Saver Accounts is subject to income tax.

New law	***Current law***
Unclaimed life insurance	
Interest paid by the Commonwealth in respect of unclaimed life insurance amounts is exempt from income tax.	Interest paid by the Commonwealth in respect of unclaimed life insurance amounts is subject to income tax.

Detailed explanation of new law

1.13 Schedule 1 ensures that income tax is not payable on interest paid by the Government after 1 July 2013 in relation to unclaimed money, with the exception of unclaimed money of former temporary residents. These amendments ensure that the application of income tax does not result in the real value of unclaimed money diminishing over time.

1.14 Where the interest is paid in relation to the unclaimed superannuation of a former temporary resident, Schedule 1 ensures that DASP tax applies appropriately to this payment.

1.15 This Schedule makes amendments in relation to three distinct areas: superannuation, general income tax and DASPs.

Superannuation amendments

1.16 Part 1 of Schedule 1 amends the ITAA 1997 to make interest paid by the Commonwealth in respect of unclaimed superannuation reclaimed after 1 July 2013 a tax free component of a superannuation benefit unless it is provided in relation to the unclaimed money of a former temporary resident. As a consequence of this treatment, the interest payments are non-assessable non-exempt income (see section 301-30).

1.17 This approach differs from that taken elsewhere in Schedule 1 for other forms of interest on unclaimed money. This alternative approach is required to ensure the payments of interest receive the appropriate treatment under the existing taxation and superannuation law.

1.18 Interest in respect of unclaimed superannuation relating to former temporary residents and lost member accounts was already included in the definition of ‘superannuation benefit’ (see item 5 of the table in subsection 307-5(1)). However, interest in respect of general unclaimed superannuation was not covered. These amendments extend the definition of ‘superannuation benefit’ to payments of interest under the general unclaimed superannuation provisions in subsections 17(2AB) and 17(2AC) of the *Superannuation (Unclaimed Money and Lost Members)*

Act 1999 (S(UMLM) Act). ***[Schedule 1, Part 1, items 4 and 5, subsection 307-5(1), table item 5, columns 2 and 3]***

1.19 Similarly, interest in respect of the unclaimed superannuation of former temporary residents and lost member accounts was also covered by the pre-existing rules for determining if a component of a superannuation benefit is tax free (see section 307-142). However, again interest in respect of general unclaimed superannuation provisions was not covered by these rules. Schedule 1 includes the rules for determining if and to what extent a superannuation benefit is tax free where the benefit includes a payment of interest under subsections 17(2AB) and 17(2AC) of the S(UMLM) Act. ***[Schedule 1, Part 1, items 6 and 7, paragraph 307-120(2)(e) and subsection 307-142(1)]***

1.20 Without the amendments in Schedule 1, this interest would generally have been considered a taxable component of a superannuation benefit. The amendments ensure that the payment of interest by the Commonwealth in respect of unclaimed superannuation reclaimed after 1 July 2013 is generally a tax free component of a superannuation benefit. ***[Schedule 1, Part 1, items 8, 11, 14 and 17, subsections 307-142(2) and (3B) and 307-300(2) and (3A)]***

1.21 The amendments also update the relevant guide material in the ITAA 1997 (including inserting new notes). ***[Schedule 1, Part 1, items 9, 10, 15 and 16, subsections 307-142(2) and 307-300(2)].***

1.22 Schedule 1 further amends item 5 of the table in subsection 307-5(1) of the ITAA 1997 to individually specify each provision under which unclaimed money or interest on unclaimed money may be paid. This ensures that it is clear that payments of unclaimed money and payment of interest on this unclaimed money are distinct superannuation benefits. To be consistent with this approach, similar amendments have been made to the other references to these provisions in the ITAA 1997, the *Superannuation (Departing Australia Superannuation Payment Tax) Act 2007* S(DASPT)) Act and the S(UMLM) Act. ***[Schedule 1, Part 1, items 1 to 3, 5 to 6, 12 to 13, 18 to 22 and 24 to 32, subsection 295-190(1A), section 301-125, subsections 301-170(2), (3) and (4), 307-5(1), 307-220(4), 307-300(1), 307-350(2B) of the ITAA 1997, subsection 5(2) of the S(DASPT) Act and subsection 17(2A), subparagraphs 20H(1)(b)(iii). (iv) and (vi), paragraphs 20H(1)(a) and 20M(1)(a), section 20P, subsections 24E(5) and 24G(4), paragraph 24L(1)(a) and subsection 29(4) of the S(UMLM) Act]***

1.23 These amendments additionally clarify that interest paid on prior amounts of unclaimed money does not affect the determination of any subsequent amounts of unclaimed money by a former temporary resident under section 20H of the ITAA 1997. ***[Schedule 1, Part 1, items 22 to 25, subparagraphs 20H(1)(b)(iii), (iv) and (vi), paragraph 20H(2B)(a)]***

1.24 Without this clarification, payments of unclaimed money to former temporary residents may have been reduced by the amount of any interest paid in relation to prior payments. This outcome would not have been consistent with the Government's intention to preserve the real value of unclaimed money.

General income tax amendments

1.25 For other types of unclaimed money, Part 2 of Schedule 1 inserts a new income tax exemption in Division 51 of the ITAA 1997.

1.26 This exemption provides that payments of interest are exempt from income tax where the interest relates to:

- unclaimed bank accounts ***[Schedule 1, Part 2, item 34, subsection 51-120(a)]***;
- unclaimed corporate property ***[Schedule 1, Part 2, item 34, subsection 51-120(b)]***;
- unclaimed First Home Saver Accounts ***[Schedule 1, Part 2, item 34, subsection 51-120(c) and (d)]***; and
- unclaimed life insurance amounts ***[Schedule 1, Part 2, item 34, subsection 51-120(e)]***.

1.27 Part 2 of Schedule 1 also makes amendments to the relevant guidance material in the Act. ***[Schedule 1, Part 2, items 33 and 34, sections 11-15 and 51-120]***

Departing Australia superannuation payments

1.28 Individuals residing outside Australia that are not Australian citizens, holders of a temporary or permanent visa, or current applicants for a permanent visa (former temporary residents — see section 20AA of the S(UMLM) Act) cease to be eligible for the tax concessions that apply to Australian superannuation.

1.29 The superannuation of former temporary residents is transferred to the Commonwealth as unclaimed superannuation (see sections 20C to 20G of the S(UMLM) Act).

1.30 Former temporary residents may claim these amounts back from the Commonwealth (section 20H of the S(UMLM) Act). As former temporary residents are generally no longer entitled to the tax concessions that apply to superannuation in Australia, the amount is returned as a DASP (see section 20H of the S(UMLM) Act and subsection 301-170).

1.31 Special tax arrangements apply to DASPs. These arrangements are intended to recover the tax benefits that applied while the money was held in the Australian superannuation system.

1.32 DASPs are specifically non-assessable and non-exempt income. However, recipients of a DASP are liable to pay income tax on the payment at a special rate (DASP tax) (section 301-175).

1.33 The rate of DASP tax is determined by the tax status of the particular components of the relevant superannuation benefit (see section 5 of the S(DASPT) Act). For amounts that are tax free components of the superannuation benefit, this rate is nil. For amounts that are taxable components, the rate of DASP tax is 35 per cent if they have been subject to tax in the fund, or 45 per cent if they were untaxed in the fund.

1.34 As with other types of unclaimed money, recipients of DASPs are entitled to receive interest from the Commonwealth from 1 July 2013.

1.35 As outlined above, as a result of these amendments, interest paid by the Commonwealth on unclaimed superannuation reclaimed after 1 July 2013 is generally a tax free component of a superannuation benefit.

1.36 However, for payments to former temporary residents, this would not be appropriate as the interest would have been calculated based on the pre-DASP tax amount without any adjustment to remove the benefit of the superannuation tax concessions.

1.37 To address this, the amendments provide that payments of interest on the unclaimed money of former temporary residents are not a tax free component of a superannuation benefit. ***[Schedule 1, Part 1, item 11, subsection 307-142(3C)]***

1.38 Instead, these payments are a taxable component of a superannuation benefit. Schedule 1 also specifically provides that these amounts are not taxed in the fund. ***[Schedule 1, Part 1, items 14 and 17, subsections 307-300(2) and (3A)***]

1.39 As a result of this change, payments of interest on the unclaimed money of former temporary residents reclaimed after 1 July 2013 are a taxable component of a superannuation benefit that has been untaxed in the fund and are subject to DASP tax at a rate of 45 per cent.

1.40 This treatment only applies to payments to individuals who are former temporary residents when the payment is made (or the estates of individuals who die while they are a former temporary resident). Individuals who were former temporary residents, but who obtain

Australian citizenship or a visa before reclaiming their unclaimed superannuation are treated in the same way as other Australian residents. The same treatment applies to payments to the estates of individuals who die while entitled to reside in Australia.

Application and transitional provisions

1.41 Part 1 of Schedule 1 (the superannuation and DASP amendments) commences from Royal Assent. This is consistent with the commencement date of the provisions providing for the payment of interest on unclaimed superannuation in the *Treasury Amendment (Unclaimed Money and Other Measures) Act 2012*. ***[Clause 2(1), Item 2 of the table]***

1.42 Part 2 of Schedule 1 (the general income tax amendments) commences from 1 July 2013. This is consistent with the commencement date of the provisions providing for the payment of interest on unclaimed money other than superannuation in the *Treasury Amendment (Unclaimed Money and Other Measures) Act 2012*. ***[Clause 2(1), Item 3 of the table]***

STATEMENT OF COMPATIBILITY WITH HUMAN RIGHTS

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

Taxation of interest on unclaimed moneys

1.43 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

1.44 Schedule 1 to this Bill amends the income tax and superannuation law to exempt from taxation the interest paid by the Commonwealth on unclaimed money from 1 July 2013.

Human rights implications

1.45 Consistent with other forms of interest, interest paid to former temporary residents under this measure is not subject to ordinary income tax. However, unlike other forms of interest it is subject to Departing Australia Superannuation Payments Tax.

1.46 This difference in treatment raises issues in relation to the right of equality and non-discrimination contained in Article 26 of the International Covenant on Civil and Political Rights, which prohibits discrimination on the basis of specified grounds, including race, colour, sex, language, religion, political or other opinion, national or social origin, property, birth or other status. 'Other status' is a broad category which can include grounds such as residence.

1.47 However, not all differences in treatment are contrary to the right of equality and non-discrimination. In particular, where differences in treatment are based on reasonable and objective criteria and are intended to achieve a legitimate purpose.

1.48 There is a well-established body of international law and practice recognising that taxation laws of a State can differentiate between the tax treatment of residents of that State and the tax treatment of non-residents. For example, treaties to prevent double taxation use residence status as a way to allocate taxing rights between States. At the same time, discrimination between residents of the same State on the basis of their nationality is prohibited.

1.49 Consistent with this body of law and practice, Australia's tax law includes a number of concessions for superannuation that are recovered in the event a person permanently departs Australia.

1.50 In light of this, there is no basis to conclude that this different treatment amounts to discrimination on the basis of 'other status' under the international instruments listed in section 3 of the *Human Rights (Parliamentary Scrutiny) Act 2011.*

Conclusion

1.51 This Schedule is compatible with human rights as it does not raise any human rights issues.

Assistant Treasurer, the Hon David Bradbury

Fringe benefits tax — reform of airline transport fringe benefits

Outline of chapter

2.1 Schedule 2 to this Bill amends the *Fringe Benefits Tax Assessment Act 1986* (FBTAA) to align the special rules for calculating airline transport fringe benefits with the general provisions dealing with in-house property fringe benefits and in-house residual fringe benefits.

2.2 The method for determining the taxable value of airline transport fringe benefits is also updated to both simplify the practical operation of the law and to better reflect the economic value of the benefit.

Context of amendments

Overview of the current law for airline transport fringe benefits

2.3 An airline transport fringe benefit arises under Division 8 of Part III of the FBTAA when an employee of an airline operator or a travel agent is provided with free or discounted air travel on a stand-by basis which is customary in the airline industry (including any related incidental services provided on board the aircraft).

2.4 Stand-by airline travel restrictions customarily apply in the airline industry and is travel in which seating on the aircraft is subject to availability and is not guaranteed for the employee or associate of the employee. This means that employees or associates of the employee may be displaced from a flight at any time up to the point of departure.

2.5 It is important to note that free or discounted airline travel that is provided to employees without stand-by restrictions is not an airline transport fringe benefit and is instead taxable under the ordinary in-house property or residual fringe benefit rules.

2.6 Division 8 of Part III of the FBTAA was originally introduced into the fringe benefits tax law in 1986 to provide industry-specific valuation rules for the airline industry in respect to free or discounted

airline travel provided to employees or associates of the employee on a stand-by basis.

2.7 These provisions were introduced at a time when the industry was heavily regulated and stand-by travel was also available to commercial passengers.

Working out the value of an airline transport fringe benefit

2.8 Currently, in working out the taxable value of an airline transport fringe benefit the provider must ascertain the value of the benefit, less the employee contribution.

2.9 For domestic travel, the value of the benefit is broadly 37.5 per cent of the lowest publicly advertised economy airfare charged by the provider (or a carrier where relevant), at or about the time of travel, over that route. However, the precise airfare to be used for the value depends on whether the transport is on a scheduled passenger air service or not and whether a carrier operates a scheduled passenger air service over that route or not.

2.10 For international travel, the value of the benefit is broadly 37.5 per cent of the lowest fare published in Australia as charged by any carrier, for travel over that route in the 12 months preceding the end of the year of tax. Again, the precise airfare to be used for the value depends on whether the transport is on a scheduled passenger air service or not and whether a carrier operates a scheduled passenger air service over that route or not.

2.11 The method of determining the taxable value of an airline transport fringe benefit was developed at a time when stand-by travel was a feature of commercial airline pricing which was available to members of the public.

Background to reform of the airline transport fringe benefits provisions

2.12 Stakeholders from the airline industry have raised concerns about the methodology for valuing stand-by airline travel. In particular, they were concerned about the amount of time spent and costs required to calculate the taxable value of the benefit, and the fact that the industry had evolved a great deal since the time the provisions were introduced in 1986.

2.13 These industry views also reflect a need to update the application of the provisions as the concept of stand-by travel, whilst still available to employees of airlines and travel agents, is no longer offered

by airlines commercially to members of the public, with airlines now using discounted pricing as a means to optimise passenger levels.

2.14 In response to these issues the Government announced in the 2012-13 Budget that it would reform the airline transport fringe benefits provisions in the fringe benefits tax (FBT) law so that the treatment of these benefits is aligned with the treatment of in-house benefits provided to employees in other sectors and the valuation method of the benefit is updated to simplify the practical operation of the law and better reflect the value of the benefit.

Summary of new law

2.15 Schedule 2 to this Bill reforms the special rules for calculating airline transport fringe benefits currently contained in Division 8 of Part III of the FBTAA with the result being that these benefits are aligned with the general provisions dealing with in-house property fringe benefits and in-house residual fringe benefits.

2.16 However, to reflect the restrictions that apply to employees or associates of employees travelling on a stand-by basis, the method for determining the taxable value of airline transport fringe benefits has been updated to simplify the practical operation of the law and better reflect the economic value of the benefit.

2.17 For airline transport fringe benefits provided after 7.30 pm by legal time in the Australian Capital Territory on 8 May 2012, the taxable value is calculated as 75 per cent of the stand-by airline travel value of the benefit.

2.18 Where the transport is on a domestic route the stand-by airline travel value is 50 per cent of the carrier's lowest standard single economy airfare for that route as publicly advertised during the year of tax.

2.19 Where the transport is on an international route, the stand-by airline travel value is 50 per cent of the lowest of any carrier's standard single economy airfare for that route as publicly advertised during the year of tax.

2.20 The reason for the 50 per cent discount, which provides a further concession against the value of the benefit compared with the use of notional value of other types of in-house fringe benefits, is that discounted employee travel is subject to a number of restrictions, for example, the travel is on a stand-by basis and the employees may be displaced from the flight, making a valuation more difficult and expensive.

2.21 The reforms to the airline transport fringe benefits complement the recent changes to the concessional treatment for in-house fringe benefits accessed by way of salary packaging arrangements as announced in the Mid-Year Economic and Fiscal Outlook 2012-13 and introduced into Parliament in Schedule 7 to the Tax Laws Amendment (2012 Measures No. 6) Bill 2012.

2.22 As a result, airline transport fringe benefits that are accessed by way of salary packaging arrangements will not receive the concessional in-house valuation and instead will be valued using the notional value.

Comparison of key features of new law and current law

New law	*Current law*
The taxable value of an airline transport fringe benefit is aligned with the in-house benefit valuation method and is calculated as 75 per cent of the stand-by airline travel value of the benefit, less the employee contribution. Where the transport is on a domestic route, the stand-by airline travel value is 50 per cent of *the* carrier's lowest standard single economy airfare for that route as publicly advertised during the year of tax. Where the transport is on an international route, the stand-by airline travel value is 50 per cent of the lowest of *any* carrier's standard single economy airfare for that route as publicly advertised during the year of tax.	The taxable value of an airline transport fringe benefit is the value less the employee contribution. For domestic flights this is is broadly 37.5 per cent of the lowest publicly advertised economy airfare charged by the provider (or a carrier where relevant), at or about the time of travel, over that route. For international flights this is broadly 37.5 per cent of the lowest fare published in Australia as charged by any carrier for travel over that route in the 12 months preceding the end of the year of tax.

Detailed explanation of new law

2.23 This measure reforms the airline transport fringe benefit rules by:

- aligning the airline transport fringe benefit rules with the in-house fringe benefit provisions; and

- updating the valuation methodology for airline transport fringe benefits.

Aligning the airline transport fringe benefit rules with the in-house fringe benefit provisions

2.24 In order to better align the treatment of the airline transport fringe benefits with other in-house benefits provided by employers in other industries, these reforms introduce a rewritten definition of ‘airline transport fringe benefit’, repeal Division 8 of Part III of the FBTAA and insert updated airline transport fringe benefit rules into the existing in-house property and in-house residual fringe benefit provisions.

2.25 This improves consistency across the FBT law and also assists in reducing the complexity of the law.

Introducing a new definition of an airline transport fringe benefit

2.26 To facilitate the alignment of the airline transport fringe benefit rules with the in-house fringe benefit provisions, this measure introduces a rewritten definition of ‘airline transport fringe benefit’.

2.27 The rewritten definition replaces the definition previously used for the purposes of Division 8 of Part III of the FBTAA to reflect modern airline industry airfare structures, and improve the clarity of the definition to simplify the practical operation of the law for airline operators and travel agents but does not alter its current scope. ***[Schedule 2, item 15, subsection 136(1) of the FBTAA]***

2.28 An airline transport fringe benefit under this measure includes an in-house property fringe benefit or an in-house residual fringe benefit to the extent that the benefit includes the provision of transport in a passenger aircraft operated by a carrier (including any related incidental services on board the aircraft) and is subject to the stand-by restrictions that customarily apply in the airline industry.

The meaning of ‘provision of transport in a passenger aircraft operated by a carrier and any incidental services on board the aircraft’

2.29 This term replicates (in a rewritten form) the relevant part of the existing definition of airline transport benefit (in section 32 of the FBTAA).

2.30 It describes the benefit that an airline or travel agent provides, which includes transport in a passenger aircraft operated by a carrier as well as other related incidental services.

The meaning of 'subject to stand-by restrictions that customarily apply for the provision of airline travel to employees in the airline industry'

2.31 An airline transport fringe benefit means the provision of transport that includes certain conditions or features and that are provided subject to stand-by restrictions.

2.32 Not all airlines and travel agents have the same corporate policies or staff remuneration policies in respect to stand-by travel for employees and associates of employees, so this definition is intended to identify the typical stand-by restrictions that apply across the airline industry (which is intended to include the travel agent industry).

2.33 Stand-by restrictions commonly mean that seating on the aircraft is not guaranteed for the employee or associate of the employee and transport on the aircraft is subject to seat availability up to the point of departure.

2.34 Stand-by restrictions also commonly mean that, whilst an employee or associate of the employee may be given a seat prior to departure, the employee or the associate of the employee may subsequently be asked to disembark for a commercial passenger.

2.35 Stand-by restrictions may also affect other incidental benefits such as meals and in-flight entertainment.

Inserting airline transport fringe benefit rules into the in-house fringe benefit provisions

2.36 The in-house fringe benefit provisions were inserted into the FBT law to provide special valuation methods for different types of benefits that may be provided in-house by employers in the business of providing the same goods and services to their clients.

2.37 An in-house fringe benefit is broadly a benefit that is provided either by the employer, an associate of the employer or a third party to an employee where the provider of the benefit carries on a business that consists of, or includes, providing identical or similar goods or services to customers at arm's length.

2.38 Employers in the airline and travel industry are in the business of providing airline travel or tickets for airline travel to customers. Where such an employer provides airline travel or tickets for airline travel to an employee (on a stand-by basis), they are not providing identical goods and services to the employee. However, they are providing similar goods or services which will nonetheless be in-house fringe benefits under the FBT law.

Example 2.1:

An airline, as employer, provides discounted travel on another airline to its employees pursuant to an interline agreement. This travel is subject to stand-by restrictions.

As the employer is in the business of providing airline travel, the provision of this benefit is an in-house residual fringe benefit as similar benefits are provided principally to outsiders.

2.39 To give effect to these reforms this measure inserts a modified form of the airline transport fringe benefits rules into the existing in-house property and residual fringe benefit provisions to deal with the unique valuation requirements for stand-by airline travel.

2.40 Where the airline transport fringe benefit is an in-house property fringe benefit, the taxable value of the benefit is an amount equal to 75 per cent of the stand-by travel value of the benefit at the time the transport starts. ***[Schedule 2, item 2, paragraph 42(1)(ab) of the FBTAA]***

2.41 Where the airline transport fringe benefit is an in-house residual fringe benefit, the taxable value of the benefit is an amount equal to 75 per cent of the stand-by travel value of the benefit at the comparison time (which is the time the transport starts). ***[Schedule 2, items 5 and 7, paragraphs 48(ab) and 49(ab) of the FBTAA]***

2.42 In both cases (whether it is an in-house property or in-house residual fringe benefit), the 25 per cent discount (that is, 75 per cent of the value) equals the standard discount applied in the FBT law for goods and services provided in-house by an employer or associate of the employer.

2.43 The reason for valuing the benefit at 75 per cent is that the discount reflects a traditional understanding that there is a lower cost for employers providing those benefits to their employees or associates of their employee than to their customers.

2.44 The reduction of aggregate taxable value of fringe benefits under section 62 of the FBTAA will continue to apply to airline transport fringe benefits as an in-house fringe benefit. ***[Schedule 2, items 10 to 12]***

2.45 A number of consequential amendments have also been made to the in-house fringe benefits provisions to update cross references and headings for the insertion of the reformed airline transport fringe benefits valuation rules. ***[Schedule 2, items 3, 4, 6, 8 and 10 to 12]***

Determining whether the airline transport fringe benefit is an in-house property fringe benefit or an in-house residual fringe benefit

2.46 In valuing the airline transport fringe benefit, employers may need to determine whether the benefit is an in-house property fringe benefit or an in-house residual fringe benefit. This depends on the particular facts and circumstances of the situation and is based on the way the benefit is provided.

In-house property fringe benefits

2.47 In general, a property fringe benefit includes:

- goods (including gas and electricity, unless provided through a reticulation system) and animals;
- real property, such as land and buildings; and
- rights to property, such as shares or bonds.

2.48 However, to be an in-house property benefit, the property benefit must satisfy a number of conditions including the requirement that the property must be tangible property. For this purpose, tangible property does not include such things as real estate, buildings or shares.

2.49 Different valuation rules apply to in-house property fringe benefits depending on whether the employer makes the goods or sells them as part of the employer's business.

Example 2.2:

A travel agent, as employer, provides an employee with a ticket for transport in a passenger aircraft subject to stand-by restrictions.

As the benefit the employer has provided to the employee is the ticket, it would be treated as an in-house property fringe benefit as the ticket is a property benefit that can be accepted as being tangible property.

In-house residual fringe benefits

2.50 Residual benefits on the other hand are those benefits that are not covered by a specific category of fringe benefit. Residual benefits often include benefits, such as services or use of property.

2.51 A benefit is an in-house residual fringe benefit if the employer (or an associate) provides an identical or similar right, service or facility to the public, in the ordinary course of business.

Example 2.3:

An airline, as employer, provides free travel to its employees, subject to stand-by restrictions.

As the benefit is a service (transport on the aircraft) the airline transport fringe benefit is an in-house residual fringe benefit.

2.52 The reforms in this measure mean that regardless of whether the airline transport fringe benefit is provided as an in-house property fringe benefit or an in-house residual fringe benefit, the airline transport fringe benefit will be valued consistently.

2.53 This will assist in reducing compliance costs for employers providing the benefit and ensures consistent treatment of airline transport fringe benefits across different employers that are able to provide these benefits to employees or associates of employees.

Interaction with the recent reform to in-house fringe benefits accessed through a salary packaging arrangement

2.54 Consistent with the recent reform to the in-house fringe benefits provisions in Schedule 7 to the Tax Laws Amendment (2012 Measures No. 6) Bill 2012, where an airline transport fringe benefit is accessed through a salary packaging arrangement, the benefit will not be taxed under the concessional in-house FBT valuation rules and instead will be valued using the notional value.

2.55 A salary packaging arrangement means an arrangement where the employee receives a benefit:

- in return for a reduction in salary or wages that would not have happened apart from the arrangement; or
- as part of the employee's remuneration package, and the benefit is provided in circumstances where it is reasonable to conclude that the employee's salary or wages would be greater if the benefit were not provided.

Repealing the existing airline transport fringe benefit rules

2.56 As the airline transport fringe benefit rules have been updated and inserted into the in-house fringe benefit provisions, this measure repeals Division 8 of Part III of the FBTAA in full as it is no longer needed. ***[Schedule 2, item 1, Division 8 of Part III of the FBTAA]***

2.57 There are also a number of consequential amendments across the FBTAA, and in particular in the interpretation section (section 136) of that

Act, that cross reference provisions or definitions in Division 8 of Part III of the FBTAA that are also repealed in order to give effect to this reform. ***[Schedule 2, items 9, 13, 14, 16 to 27 and 28 to 30]***

Updating the valuation methodology for airline transport fringe benefits

2.58 This measure updates the method for determining the taxable value of airline transport fringe benefits to simplify the practical operation of the law and better reflect the economic value of the benefit.

2.59 The economic value of the benefit (a proxy for its notional value) is defined as the stand-by airline travel value, which is slightly different depending on whether the transport is over a domestic route or an international route.

2.60 Where the transport is on a domestic route, the stand-by airline travel value is 50 per cent of *the* carrier's lowest standard single economy airfare for that route as publicly advertised during the year of tax. ***[Schedule 2, item 26, subsection 136(1) of the FBTAA]***

2.61 Where the transport is on an international route, the stand-by airline travel value is 50 per cent of the lowest of *any* carrier's standard single economy airfare for that route as publicly advertised during the year of tax. ***[Schedule 2, item 26, subsection 136(1) of the FBTAA]***

2.62 The 50 per cent reduction in the economic value of the benefit reflects the decreased value of the airline travel due to the stand-by restrictions that apply to the benefit.

2.63 This is consistent with the existing valuation method for domestic and international airline transport fringe benefits as the initial 25 per cent reduction that applies by way of the in-house fringe benefit concession coupled with the 50 per cent reduction by way of the stand-by airline travel value equates to the existing 37.5 per cent valuation currently applied.

2.64 The determination of the stand-by airline travel value is based on the employer determining the lowest standard single economy airfare for the particular route that the employee or associate of the employee is taking in respect to the benefit as publicly advertised during the year of tax in which the transport starts.

The difference between the valuation of stand-by airline travel value on domestic routes and international routes

2.65 The main difference between the stand-by airline travel value of domestic routes and international routes is what airfares can be used for the valuation method.

2.66 For domestic routes the valuation method is based on *the* carrier's lowest standard single economy airfare. This means the provider must use the lowest standard single economy airfare of the carrier that provided the transport.

2.67 For international routes the valuation method is based on the lowest of *any* carrier's standard single economy airfare. This means the provider can use the lowest standard economy airfare of any carrier that provides commercial airfares over the relevant route.

2.68 The ability to use any carrier for the valuation method in respect to travel over international routes reflects the existing law and assists providers who have to determine airfares over routes which they may not fly or service themselves.

2.69 For the purposes of clarity, a domestic route means a route in which the flight's departure and arrival are both within Australia. An international route on the other hand means a route in which the flight's departure or arrival (or both) are outside of Australia.

The meaning of standard single economy airfare

2.70 The term 'standard single economy airfare' is intended to take its ordinary meaning and reflect the economy airfare that an ordinary customer would be expected to pay in order to travel the same route in that year of tax.

2.71 The inclusion of the word 'single' is intended to preclude the use of discounted group booking fares as comparable fares in determining the stand-by airline travel value.

Example 2.4:

> An airline provider offers discounted fares where a group booking is made of more than 10 people. As this discounted fare is not a *single* economy airfare it cannot be used as a comparable airfare in determining the stand-by airline travel value.

2.72 The inclusion of the word 'standard' is also intended to preclude the use of discounted group booking fares or 'one-off' or heavily

discounted fares as part of a marketing campaign for determining the stand-by airline travel value.

Example 2.5:

GoCheap (an airline provider) is attempting to increase its market share and decides to set up a three month marketing campaign and as part of that, put out a select number of fares per flight over a couple of major routes during the off-peak season that are only $1.

The discounted fares are far below the cost price of the service and do not reflect the *standard* single economy airfare for that particular route and therefore cannot be used as a comparable airfare in determining the stand-by airline travel value.

Example 2.6:

A travel agent is determining the stand-by airline travel value for an airline transport fringe benefit provided to one of its employees. The airline transport fringe benefit provided to the employee was transport in a passenger aircraft from Sydney to Perth.

When determining the lowest standard single economy airfare, the travel agent finds a GoCheap airfare (as per the example above) that is only $1 over the Sydney to Perth route.

Even though the travel agent may not be aware that the flight is far below cost price, the travel agent is able to ascertain that the flight is heavily discounted as part of a marketing campaign because it is so far below the average range of fares for that route (which the travel agent determines is between $150 and $500 plus).

The travel agent then determines that the GoCheap airfare does not reflect a *standard* single economy airfare and it is therefore not a comparable airfare that can be used to determine the stand-by airline travel value.

The meaning of publicly advertised during the year of tax

2.73 In order to reduce compliance costs for employers in the airline industry, in determining the stand-by airline travel value, providers need only consider the relevant airfare that is publicly advertised during the relevant year of tax in which the transport began.

2.74 ‘Publicly advertised’ is intended to include mediums such as the internet, newspapers, television as well as any other medium in which a member of the public would be able to reasonably ascertain the cost of the fare.

2.75 This will make it easier for employers who need to determine the cost of a fare provided by an associate international airline under a code-share or interline arrangement.

2.76 'During the year of tax' is intended to ensure that the provider determines the stand-by airline travel value based on a contemporary fare and the relevant year of tax is determined by the year in which the travel starts. ***[Schedule 2, items 2, 5, 7 and 16]***

Example 2.7:

Axel, an employee of an Australian airline, is travelling on an international carrier that is in an interline arrangement with his employer.

Having waited for a few days to get onto a flight to travel home to Australia as part of the stand-by restrictions, Axel is finally able to get on flight on 31 March 2014.

Even though the flight lands in Australia on 1 April 2014 local time, the relevant year of tax in determining the stand-by travel value is the 2013-14 FBT year.

Example 2.8:

Assume the same facts as Example 2.7 except that Axel is unable to get onto the 31 March 2014 flight and instead boards on 1 April 2014. In that case the relevant year of tax is the 2014-15 FBT year.

Application and commencement

Application date

2.77 This reform applies to airline transport fringe benefits provided after 7.30 pm by legal time in the Australian Capital Territory on 8 May 2012.

Commencement date

2.78 Schedule 2 to this Bill commences on the latter of the date that this Bill receives Royal Assent and the day that the recent changes to the concessional treatment for in-house fringe benefits accessed by way of salary packaging arrangements commence.

2.79 This is to ensure that amendments, which are to the same area of law, do not conflict.

2.80 The reform to in-house fringe benefits accessed through salary packaging arrangements are in Schedule 7 to the Tax Laws Amendment (2012 Measures No. 6) Bill 2012.

Retrospectivity of measure

2.81 These amendments apply retrospectively to benefits provided after 8 May 2012, however, the amendments (in situations where the tax outcome differs) are of a beneficial nature to affected entities.

STATEMENT OF COMPATIBILITY WITH HUMAN RIGHTS

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

Schedule 2 Fringe benefits tax — reform of airline transport fringe benefits

2.82 Schedule 2 to 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

2.83 Schedule 2 amends the *Fringe Benefits Tax Assessment Act 1986* to reform the special rules for calculating airline transport fringe benefits so that these benefits are aligned with the general provisions dealing with in-house property fringe benefits and in house residual fringe benefits.

2.84 The method for determining the taxable value of airline transport fringe benefits is also updated to simplify the practical operation of the law and to better reflect the economic value of the benefit.

Human rights implications

2.85 Schedule 2 does not engage any of the applicable rights or freedoms.

Conclusion

2.86 Schedule 2 compatible with human rights as it does not raise any human rights issues.

Assistant Treasurer, the Hon David Bradbury

Sustainable Rural Water Use and Infrastructure Program

Outline of chapter

3.1 Schedule 3 to this Bill amends the *Income Tax Assessment Act 1997* to allow participants in the Sustainable Rural Water Use and Infrastructure Program (SRWUIP) to choose to make payments they derive under the program free of income tax (including capital gains tax (CGT)), with expenditure related to infrastructure improvements required under the program then being non-deductible.

3.2 References in this Chapter are to the *Income Tax Assessment Act 1997* unless otherwise specified.

Context of amendments

3.3 SRWUIP is a major component of the Commonwealth's *Water for the Future* program. SRWUIP payments from the Commonwealth are used to upgrade irrigation and other rural infrastructure in order to improve the efficiency and productivity of rural water use, to deliver substantial and lasting returns of water to the environment and to help secure a long-term sustainable future for irrigated agriculture.

3.4 SRWUIP consists of a broad suite of programs, often delivered in partnership with state/territory governments, who may provide supplementary funding.

3.5 SRWUIP payments are made under agreements between the Commonwealth and other parties, which may include state governments, irrigation infrastructure operators (IIOs) and individual irrigators. Project participants, who are the ultimate recipients of the payments, use that money to undertake specified works.

3.6 Where the increase in water use efficiency from those SRWUIP-funded projects means that less water needs to be used to achieve the existing amount of irrigated production, water entitlements can be transferred to the Commonwealth without causing a reduction in irrigated production. The Commonwealth can then use the transferred entitlements for environmental activities.

3.7 In the absence of these amendments, payments under SRWUIP would generally be taxable in the year they are derived, either as a subsidy or, to the extent that a payment is consideration for the transfer of water rights, as a capital gain. However, expenditure under the program would usually be recognised over a longer period:

- some of it might be deductible in the year it is incurred;
- some might be deductible over several years under the capital allowance provisions (three years in the case of primary production water facilities); and
- some might reduce a capital gain (or increase a capital loss) when a CGT asset is disposed of.

3.8 This difference in timing can mean that recipients of SRWUIP payments need to fund the gap between incurring tax liabilities and expenditure obligations and fully realising the tax effect of the expenditure that corresponds to the payments.

3.9 The Government announced on 18 February 2011 that it would amend the taxation law to eliminate the timing mismatch between when the SRWUIP payments are taxed and when deductions are available, and that a CGT exemption would form a part of the measure.

Summary of new law

3.10 This Schedule allows taxpayers to choose to make the water infrastructure improvement payments non-assessable non-exempt (NANE) income, and to disregard any capital gain or loss from transferring the water rights. If they do, expenditure that is made because of the payments is not deductible and does not form part of the cost of any asset it is spent on.

3.11 In effect, making the choice eliminates the need to fund the gap because removing the tax liability means that the remaining required outgoings (on improving water infrastructure) will equal the SRWUIP payments.

3.12 However, some taxpayers might not make this choice if their net tax outcome under the current law is better for them than the net outcome under the new approach. This might be because, while all of the expenditure will eventually reduce a tax liability under the current law, not all of the SRWUIP payments need be taxable (for example, the transfer of pre-CGT water rights will not produce a taxable capital gain).

Comparison of key features of new law and current law

New law	*Current law*
Taxpayers can choose either the existing treatment of their SRWUIP payments and related expenditure or: • make the subsidy part of their SRWUIP payments NANE income; • disregard any capital gains and losses arising from transferring their water rights under a SRWUIP program; • forgo their deductions for expenditure required under the SRWUIP program; and • exclude expenditure required under the SRWUIP program from the cost of any assets they acquire.	Taxpayers have no choice of tax treatment for their SRWUIP payments and related expenditure. Generally, part of a payment will be a subsidy included in assessable income and part will be capital proceeds for disposing of water rights. The expenditure on infrastructure improvements will usually be deductible over time.

Detailed explanation of new law

3.13 The *Sustainable Rural Water Use and Infrastructure Program* (SRWUIP) is a Commonwealth program designed to increase the efficiency of water use in rural Australia. In return for Commonwealth payments, participants agree to undertake improvements to their water infrastructure to reduce their water consumption and generally to transfer a set part of the water saved to the Commonwealth. The Commonwealth uses the water it acquires to improve environmental outcomes.

3.14 The Commonwealth payments are directed at infrastructure improvements which improve the efficiency of water use. The payment arrangements may include agreed values for the water rights transferred to the Commonwealth, which would usually give rise to a capital gain or loss for the entity transferring the rights. The other component of the payments is a subsidy for improving water infrastructure that would usually be assessable to the entity, either as ordinary income under section 6-5 or as statutory income under section 15-10.

3.15 Expenditure on the water infrastructure improvements would usually be deductible. Some of the expenditure could be deductible in the year it is incurred under section 8-1. Expenditure on a depreciating asset would be deductible under the capital allowance provisions of Division 40 over the life of the asset (or over three years in the case of water

facilities). Expenditure on a CGT asset would be recognised when the asset is subject to a CGT event, such as disposal.

3.16 For some taxpayers, the current law provides an adequate treatment. In particular, the amount included in their assessable income could be less than their deductions for expenditure on infrastructure improvements because they can access a CGT concession for the transfer of their water rights (for example, the rights might be a pre-CGT asset that is exempt from CGT or there might be a reduction in any capital gain on disposal of the rights, such as the 50 per cent discount available to individuals and trusts).

3.17 Other taxpayers could find themselves being taxed on the payments they receive in a year before they can deduct all the related expenditure. Because they are required to spend an amount equal to the Commonwealth payment on infrastructure improvements, having to pay the tax could create a financial gap that is only made good when the deductions are eventually available.

3.18 To help such taxpayers, the amendments allow them to choose to make the payments they derive NANE income and the expenditure they incur non-deductible.

Payments become NANE income

3.19 If a participant in a SRWUIP program makes that choice, the SRWUIP payments it derives from the Commonwealth, and the payments it derives that are reasonably attributable to Commonwealth SRWUIP payments, are NANE income so long as the program is on the Commonwealth's published list of SRWUIP programs for the day the particular payment is made. ***[Schedule 3, item 8, subsections 59-65(1) and 59-67(5)]***

3.20 NANE income is the same as exempt income, except that it does not reduce tax losses (see sections 6-23 and 36-10).

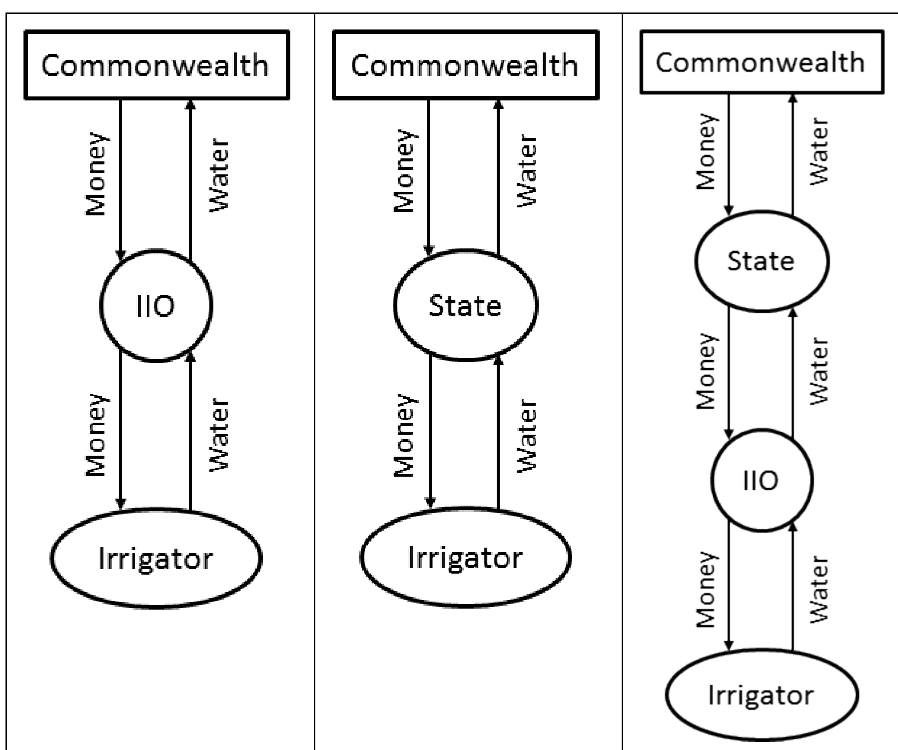
What is a SRWUIP program?

3.21 A ***SRWUIP program*** is a program under the umbrella of the Commonwealth's program known as the *Sustainable Rural Water Use and Infrastructure Program*. ***[Schedule 3, item 8, subsection 59-67(1)]***

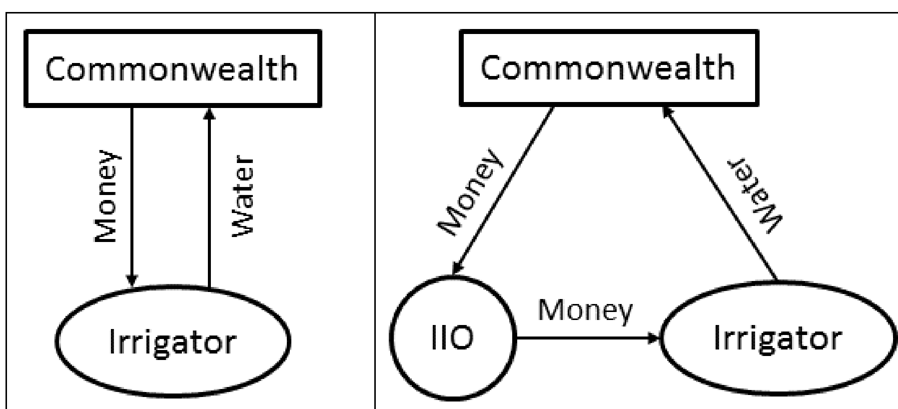
3.22 Each of the programs eligible for the special tax treatment is listed on the website of the Department of Sustainability, Environment, Water, Population and Communities. ***[Schedule 3, item 8, subsections 59-67(5) and 59-70(1)]***

3.23 A SRWUIP program could involve an arrangement between the Commonwealth and an individual irrigator. But most programs involve arrangements between the Commonwealth and a regional irrigation water provider or IIO. In a few cases, the Commonwealth enters into an arrangement with a State instead of with an IIO. The IIO or the State enters into agreements with the relevant irrigators. Those agreements are all entered into under a particular SRWUIP program.

Example 3.1: These are the more common SRWUIP arrangements:



Example 3.2: These are less common arrangements:



Who is a participant in a SRWUIP program?

3.24 The entity that enters into an agreement with the Commonwealth under a SRWUIP program is a participant in the program.

3.25 Entities that enter into agreements that will involve them improving their assets, or transferring their water rights, in order to satisfy an obligation under the head agreement with the Commonwealth are also participants because their involvement is necessary to achieve the program's objectives.

3.26 Mere agents of a participant are not themselves participants even though they might be performing work directed to achieving the program's objectives. For example, an irrigator's employees might actually make the improvements required under the program but they are not participants in the program because their actions are legally those of their employer.

3.27 Other entities performing work for a participant (such as a contractor who does the work or a lawyer who draws up the water transfer agreement) could be said to be participants because they perform work in their own capacity to achieve the program's objectives. However, even if they made a choice, it would not convert their payment into NANE income because they do not derive the payment as the owner of an asset to which the program relates. ***[Schedule 3, item 8, paragraph 59-65(1)(b)]***

What payments are covered?

An entity's choice to treat SRWUIP payments it derives as NANE income applies to all amounts paid by the Commonwealth to the entity under the particular SRWUIP program. These are called ***direct SRWUIP payments***. ***[Schedule 3, item 8, subsections 59-65(1) and 59-67(2) and (3)]***

The choice also applies to payments that are reasonably attributable to amounts paid by the Commonwealth under the program. These reasonably attributable payments are called ***indirect SRWUIP payments***. ***[Schedule 3, item 8, subsections 59-65(1) and 59-67(2) and (4)]***

However, a choice only applies to an indirect SRWUIP payment if the entity receives it because it owns an asset to which the program relates. That means that the entity must own water rights that will be transferred under the program or own land or other assets that are to be improved because of an obligation under the program. This could extend to assets that are merely rights to use things that are to be improved. ***[Schedule 3, item 8, paragraph 59-65(1)(b)]***

Example 3.3: Leaseholder makes a choice; contractor cannot

Beale Avocados leases land and related water rights for its irrigation activities. It agrees to upgrade the channels on the land in return for a payment from the landlord, who has received a payment from the Commonwealth. It engages Kevin to do the work.

Both Beale and Kevin have received indirect SRWUIP payments because they can be traced to a payment from the Commonwealth under a SRWUIP program. However, only Beale can make the choice because Kevin does not derive his payment as an owner of an asset to which the program relates. Beale's leasehold right to use the channels and the water rights is such an asset.

3.31 An entity that derives an indirect SRWUIP payment because it owns an asset to which the SRWUIP program relates cannot make that payment NANE income if it only owns that asset as part of a financial arrangement. This ensures that banks and other financiers cannot treat their interest earnings under the financial arrangement as NANE income simply because they might own a relevant asset for the purposes of securing a loan. ***[Schedule 3, item 8, paragraph 59-65(1)(b)]***

3.32 In some cases, Commonwealth payments will be topped up by a State. In those cases, only the part of the payment that is from the Commonwealth, or attributable to the payment from the Commonwealth, is covered by the choice. ***[Schedule 3, item 8, subsections 59-65(1) and 59-67(2) to (4)]***

Example 3.4: Payment from the State and the Commonwealth

The Blackwater Irrigation Alliance (an IIO) enters into agreements with the State Government and with the Commonwealth under which each will provide Blackwater with a payment to pass on to those of its members who have agreed to make water infrastructure improvements and transfer water entitlements to the Commonwealth.

Douglas Orchards has undertaken to spend $40,000 on making water infrastructure improvements and to transfer some of its water entitlements to the Commonwealth. It receives $40,000 from Blackwater, made up of $35,000 from the Commonwealth and $5,000 from the State.

Douglas chooses for the payment to be NANE income. $35,000 becomes NANE income because that part of the $40,000 is attributable to the Commonwealth payment to Blackwater. The remaining $5,000 is assessable income. A corresponding proportion of Douglas' $40,000 expenditure will be non-deductible.

When is a payment reasonably attributable to a Commonwealth SRWUIP payment?

In most cases, an irrigator does not receive a payment directly from the Commonwealth but receives it from an IIO or other delivery partner.

In those cases, the payment the irrigator derives is *reasonably attributable* to the payment the IIO has derived from the Commonwealth because the irrigator derives it as a consequence of the Commonwealth payment to the IIO. Further, the Commonwealth usually pays a particular amount to the IIO because the IIO and the irrigators under the program have agreed to spend that total amount on infrastructure improvements. The Commonwealth's payment will be divided up and passed on to the irrigators to match the expenditure each has committed to making. So, the payments they receive are usually mathematically, as well as consequentially, attributable to the payment the IIO derives from the Commonwealth.

Sometimes, an IIO receives payments from both the Commonwealth and a State Government to pass on to the irrigators. In such instances, only a portion of an amount the IIO pays to an irrigator is reasonably attributable to the Commonwealth's payment. How that portion is determined depends on the facts. In most cases, it would be done using a simple proportion for all the irrigators covered by the program. However, it could differ from one irrigator to another if the State has only agreed to subsidise the improvements of some of them.

Integrity rule for choices

In a few cases, a choice will only make a SRWUIP payment NANE income if certain associated entities also make the choice. This is an integrity rule to deal with cases where the associate that derives the SRWUIP payment wants to choose to treat it as NANE income and the associate that incurs the expenditure wants to retain the right to deduct it. If the SRWUIP payment does not flow between them (which is plausible because they are associates), these choices would not 'wash out' and the revenue could be disadvantaged.

For that reason, the amendments can prevent an amount being NANE income for a taxpayer, despite the taxpayer having made the choice, if its obligations under the SRWUIP program are satisfied because an associate incurred the required expenditure for it, rather than because it incurred the expenditure itself. In that case, the choice will only apply if the associate also makes the choice. ***[Schedule 3, item 8, subsection 59-65(4)]***

The integrity rule will not be relevant where the total amount the taxpayer receives is matched by the amount it expends on satisfying its SRWUIP obligations. It is not necessary for the total expenditure at *each* point in time to be matched by the SRWUIP payments it has derived to that time (indeed, that will seldom be the case because amounts will often only be paid after particular work has been undertaken). It is only necessary that the taxpayer's eventual SRWUIP expenditure will be matched by its eventual SRWUIP payments. ***[Schedule 3, item 8, subsection 59-65(4)]***

Example 3.5: Applying the integrity rule

Tom operates a market garden. The land, and the water rights that attach to it, are owned by the LDP trust, the beneficiaries of which are Tom and the members of his family. That means that Tom and the trust are associates.

The trust has entered into an agreement with its area water provider, under which it will receive a $100,000 SRWUIP payment and will spend $100,000 on making water infrastructure improvements. The trust does not make the improvements but arranges for Tom to do so. It lends Tom $100,000 to make the improvements. The trust makes the choice to treat its payment as NANE income.

The improvements resulting from Tom's expenditure will satisfy the trust's SRWUIP obligation but the trust will not incur the required $100,000 expenditure itself. The $100,000 loan Tom receives from the trust is not expenditure of the trust because it has to be repaid, so does not count. Accordingly, the trust's choice will only make its SRWUIP payment NANE income if Tom makes the choice too, in which case he will not be able to deduct the expenditure he makes.

Recovering Commonwealth SRWUIP payments

A payment is taken never to have been made under a SRWUIP program to the extent that the Commonwealth seeks to recover it. Payments that were reasonably attributable to the payment are therefore no longer attributable to a payment made under the program and so would no longer be an indirect SRWUIP payment. The result is that, when the Commonwealth seeks to recover a payment made under a SRWUIP program, neither that payment nor any of the payments reasonably attributable to it is NANE income. ***[Schedule 3, item 8, subsection 59-67(6)]***

If the Commonwealth seeks to recover part of a payment, the law applies as if the Commonwealth had never made that part of the payment under a SRWUIP program. ***[Schedule 3, item 8, subsection 59-67(6)]***

The provision refers to the Commonwealth *seeking* to recover an amount to deal with cases where the amount cannot actually be recovered (perhaps because the IIO has become insolvent).

If the Commonwealth voluntarily ceases its attempt to recover the amount, the payment would again be eligible to be covered by the irrigator's choice to treat it as NANE income.

If the Commonwealth does seek to recover a payment, an affected assessment can be amended at any time within two years after it does so, even if that would otherwise be outside the normal period for amending the assessment. ***[Schedule 3, item 8, paragraph 59-80(c)]***

The Secretary of the 'Water Department' (which is currently the Department of Sustainability, Environment, Water, Population and Communities) must keep the Commissioner of Taxation (Commissioner) informed about the Commonwealth's attempts to recover payments so that the Commissioner is able to properly determine the tax treatment of the payments and expenditure. ***[Schedule 3, item 8, section 59-75]***

Capital gains and losses are disregarded

Any capital gain or loss arising from a CGT event (whether from the transfer of the water right or otherwise) is disregarded if it relates to a Commonwealth payment that is NANE income because it is covered by a choice the taxpayer makes. ***[Schedule 3, item 11, paragraphs 118-37(1)(ga) and (gb)]***

That ensures that, as well as there being no tax consequences for the part of a Commonwealth payment that subsidises water infrastructure improvements, there are also no tax consequences for the part of a Commonwealth payment that relates to the transfer of water rights. ***[Schedule 3, item 11, paragraph 118-37(1)(ga)]***

To the extent that the payment is the capital proceeds for the disposal of a right to get the payment, there are also no tax consequences for the disposal of that right. ***[Schedule 3, item 11, paragraph 118-37(1)(gb)]***

SRWUIP expenditure not deductible

As well as making SRWUIP payments NANE income and disregarding capital gains and losses that arise in relation to those payments, making a choice also means that the taxpayer's expenditure in respect of a SRWUIP program is not deductible.

Making the choice means that expenditure a taxpayer incurs that satisfies an obligation under a SRWUIP program is not deductible if it is matched by a SRWUIP payment or if it is reasonable to expect that it will be matched by a SRWUIP payment. Such expenditure is called ***SRWUIP expenditure***. ***[Schedule 3, item 3, section 26-100]***

The 'reasonable expectation' element deals with cases where the expenditure precedes the SRWUIP payment. This could even include cases where the taxpayer incurs expenditure in anticipation of entering into an arrangement under a SRWUIP program, so long as that expenditure is eventually covered by such an arrangement.

If the expectation that the expenditure will be matched by a SRWUIP payment ceases to be reasonable, the expenditure is treated as if it had never been SRWUIP expenditure. So, if that expenditure was not deductible because the taxpayer had made a choice to treat the SRWUIP payment as NANE income, treating the expenditure as never having been SRWUIP expenditure means that it can be deducted. ***[Schedule 3, item 3, subsection 26-100(3)]***

Obligations under a SRWUIP program include making infrastructure improvements, but the affected expenditure is not limited to such obligations. It extends to all obligations under the relevant SRWUIP arrangement. For example, it could also apply to expenditure incurred to satisfy an obligation to transfer a water right.

Nor is the affected expenditure limited to direct expenditure to satisfy an obligation. Deductions are also not available for things like legal fees to effect a transfer of water rights and interest on money borrowed to undertake improvements, if that expenditure is matched by a SRWUIP payment included in the agreement.

Expenditure is only affected to the extent that it is matched by a SRWUIP payment. Expenditure in excess of the payment (for example, expenditure attributable to a supplementary State payment) can still be deducted. ***[Schedule 3, item 3, paragraph 26-100(2)(b)]***

Example 3.6: Expenditure exceeds Commonwealth payment

McMahon Orange Farms receives $120,000 from its area water provider to reduce leakage from its pumping and irrigation systems. $100,000 is attributable to a payment the water provider received from the Commonwealth. The other $20,000 is attributable to a supplementary payment from the State.

McMahon spends $150,000 making improvements to its systems. Since only $100,000 of its expenditure is matched by a Commonwealth payment, it is able to deduct the remaining $50,000.

Arrangements often include agreed values for the water rights that are to be transferred, and a portion of the total SRWUIP payments would normally be treated for income tax purposes as capital proceeds for the transfer rather than as a subsidy for infrastructure improvements. However, expenditure made by a participant in a SRWUIP program on making infrastructure improvements would still be 'matched' by its SRWUIP payments if it was obliged under the arrangement to spend the full amount of the payments on making those improvements.

Cost and cost base reduced

Some expenditure is deductible over time rather than for the year it is first incurred. This is the concept of a capital allowance (or depreciation), which recognises that wealth spent on an asset is not lost but is merely converted into another form. The loss actually arises over time and is recognised for tax purposes accordingly.

The amendments deal with most capital allowances by preventing the expenditure being included in the cost of the asset for tax purposes. Because tax depreciation is based on the cost of the asset, amounts excluded from its cost will never be deducted. ***[Schedule 3, items 4 and 7, section 40-222 and paragraph 43-70(2)(i)]***

Expenditure on water facilities is not recognised for income tax purposes in quite the same way as other depreciating assets. Instead of deducting a portion of the asset's cost (or an amount based on the asset's cost) a third of the capital expenditure on a water facility is recognised in the year it was incurred and in each of the following two years (see section 40-540). The amendments prevent SRWUIP expenditure covered by a choice from being counted as relevant capital expenditure in relation to a water facility. ***[Schedule 3, items 5 and 6, subsection 40-515(3) and section 40-540]***

Example 3.7: Expenditure not included in cost of assets

Byron Bay Tuber Products receives $125,000 to replace its water ejectors with vacuum pumps, to upgrade the machine that de-silts its irrigation channels and to reline its irrigation channels. It spends $10,000 replacing the water ejectors with vacuum pumps, $25,000 upgrading the de-silting machine and $90,000 relining its channels.

The vacuum pumps would normally be depreciated from their cost of $10,000 but, because Byron Bay has chosen to treat the payment as NANE income, they are treated as having a zero cost and so generate no capital allowance deductions.

Normally, the $25,000 would be added to the de-silting machine's base value as an improvement but, because of the choice, the $25,000

cannot be included in the second element of the cost of the machine and so is not added to its base value.

The $90,000 would normally be deductible over three years in equal instalments. However, because the of the choice, the capital expenditure on relining the channels (a water facility) is not counted for purposes of the capital allowance provisions and so is not deducted.

Some expenditure forms part of the cost base of a CGT asset and is not strictly deducted at all. Instead, it is taken into account in working out the amount of the capital gain (essentially, the excess of the proceeds from a CGT event (such as a disposal) over the asset's cost base). In effect, expenditure on a CGT asset is 'deducted' when a CGT event happens to that asset.

The amendments ensure that expenditure on a CGT asset is not taken into account in working out the asset's cost base (or its reduced cost base, which is used in working out capital losses). The effect is that expenditure on the asset is not 'deducted' when a CGT event occurs and any capital gain will therefore be larger and any capital loss smaller. ***[Schedule 3, items 9 and 10, subsections 110-38(7) and 110-55(9G)]***

Example 3.8: Expenditure not included in cost base of assets

Casey Station spends $10,000 of an amount it has received that is attributable to a Commonwealth SRWUIP payment to acquire some land on which to build a small water recycling plant. It supplements the purchase price with $35,000 from another source.

Casey Station makes the choice to treat its SRWUIP payments as NANE income. Therefore, the $10,000 of SRWUIP money is not included in the cost base (or reduced cost base) of the land. The extra $35,000 would still be included.

How to make the choice

An entity can only make the choice by the time it has to lodge its income tax return for the year that it:

- derives the *first* SRWUIP payment under a particular SRWUIP program; or
- incurs the *first* expense that satisfies an obligation under an arrangement entered into under the SRWUIP program.

[Schedule 3, item 8, subsection 59-65(2) and subparagraph 59-65(3)(b)(i)]

If the entity is assessed before it lodges its income tax return for that year, it has to make the choice before the assessment is made. This deals with the rare case where the Commissioner makes an assessment without a return having been lodged. ***[Schedule 3, item 8, subsection 59-65(2) and subparagraph 59-65(3)(b)(ii)]***

The Commissioner can always allow more time to make the choice. This discretion would usually be exercised where the taxpayer has a reasonable explanation for not making the choice by the standard time. One such case would be where it had to lodge its return before the relevant program was included on the list of SRWUIP programs. In such a case, it would usually be permitted to make the choice even though it was after its return was lodged. It would then seek to amend its assessment to give effect to the choice. ***[Schedule 3, item 8, subparagraph 59-65(3)(b)(iii)]***

A transitional rule provides for choices to be made that would otherwise have had to be made before the amendments commence. This rule is explained later.

Choices must be made in the form approved by the Commissioner. That ensures that the choice covers all necessary matters. ***[Schedule 3, item 8, paragraph 59-65(3)(a)]***

The choice does not have to be sent to the Commissioner — how the taxpayer's return is prepared will usually be sufficient evidence of the choice made. However, taxpayers will need to retain the document on which their choice is recorded to substantiate the choice they made if necessary. Such records would usually have to be retained for five years (see section 262A of the *Income Tax Assessment Act 1936*).

A choice once made cannot be revoked. That ensures that a consistent approach is applied to all SRWUIP payments the entity derives, and all SRWUIP expenditure it incurs, under the same program. ***[Schedule 3, item 8, subsection 59-65(3)]***

Eligible SRWUIP programs

Whether or not taxpayers can make a choice affecting the tax treatment of amounts derived and expenditure incurred for a particular program depends on whether the program is a SRWUIP program listed as such on the 'Water Department's' website. ***[Schedule 3, item 8, subsections 59-67(5) and 59-70(1)]***

A program is entered on the Department's list when the Secretary of the Department is jointly directed to do so by the Treasurer and the 'Water Minister' (who is currently the Minister for Sustainability,

Environment, Water, Population and Communities). They can so direct the Secretary if the Water Minister has previously notified the Treasurer that the program is a SRWUIP program that will generate efficiencies in water use through infrastructure improvements. ***[Schedule 3, item 8, subsections 59-70(2) and (3)]***

The Ministers' direction must be in writing and specify the period for which the program should be on the list (that period must also appear on the Department's website). The period can start at a time before the direction is given. ***[Schedule 3, item 8, subsections 59-70(1) and (4)]***

The Ministers can also jointly direct the Secretary in writing to extend the period for which a program is to be on the list (which can include a retrospective period) or to specify the last day for which a program is to be on the list (which must be a day after the direction is given). The Secretary must change the list accordingly. ***[Schedule 3, item 8, subsections 59-70(5) and (6)]***

In deciding whether to direct the Secretary to add a program to the list, or to change the relevant period for a program on the list, the Ministers must consider the policy and budgetary priorities of the government. ***[Schedule 3, item 8, subsection 59-70(7)]***

Amended assessments

Changes that affect the treatment of SRWUIP payments can occur after a relevant assessment is made. For example, a program might become a SRWUIP program with a retrospective operation, or the Commonwealth might seek to recover a payment it has made.

In such cases, the affected assessment can be amended at any time within two years after the change occurs, even if that is outside the normal period for amending the assessment. ***[Schedule 3, item 8, section 59-80]***

Application and transitional provisions

Application provision

The amendments commence on Royal Assent but apply in relation to payments made by the Commonwealth on or after 1 April 2010 under a SRWUIP program. ***[Schedule 3, item 18]***

The amendments do not apply to an indirect SRWUIP payment that is reasonably attributable to a Commonwealth payment made under a

SRWUIP program *before* 1 April 2010, even if the indirect SRWUIP payment itself is made on or after that date.

The amendments also do not apply to expenditure incurred on or after 1 April 2010 if the expenditure relates to a Commonwealth payment made under a SRWUIP program before that date.

On the other hand, they do apply to expenditure incurred before 1 April 2010 if that expenditure relates to a Commonwealth payment made under a SRWUIP program on or after that date.

3.79 1 April 2010 reflects the date on which the Commonwealth signed the first contracts under the NSW Private Irrigation Infrastructure Operators Program, a major element of the SRWUIP Program.

Transitional provision

3.80 Because the amendments apply to Commonwealth payments made from 1 April 2010, there will be some cases where payments have been derived and expenditure incurred for income years that ended before the amendments commence. Taxpayers will have already had to lodge returns for some of those years.

3.81 To ensure that taxpayers are able to make a choice for those years, a transitional provision allows taxpayers to make a choice that would otherwise need to have been made on or before the day of Royal Assent within two years after that day. The Commissioner can allow further time in appropriate cases. ***[Schedule 3, item 19]***

3.82 Unlike normal choices, these 'retrospective' choices must be provided to the Commissioner so he or she is in a position to make any amended assessments that may be necessary to give effect to the choice. ***[Schedule 3, subitem 19(2)]***

Consequential amendments

3.83 The dictionary for the *Income Tax Assessment Act 1997* is amended to include the defined terms 'direct SRWUIP payment', 'indirect SRWUIP payment', 'SRWUIP expenditure', 'SRWUIP payment', 'SRWUIP program' and 'Water Secretary'. ***[Schedule 3, items 12 to 17, subsection 995-1(1) (definitions of 'direct SRWUIP payment', 'indirect SRWUIP payment', 'SRWUIP expenditure', 'SRWUIP payment', 'SRWUIP program' and 'Water Secretary')]***

3.84 Amendments are made to the non-operative lists of provisions about NANE income and deductions to reflect the SRWUIP amendments. ***[Schedule 3, items 1 and 2, sections 11-55 and 12-5]***

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 (2013 Measures No. 1) Bill 2013

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

3.86 The Commonwealth provides amounts to irrigators under the Sustainable Rural Water Use and Infrastructure Program (SRWUIP) to help with upgrading their water infrastructure. The upgrades produce improvements in the efficiency of rural water use and some of the resulting water savings are transferred to the Commonwealth for use in environmental activities.

3.87 This Schedule amends the income tax law to provide irrigators with a choice between a new, and the existing, income tax treatment of the payments they derive under a SRWUIP program and the corresponding expenditure they make on upgrading their water infrastructure.

3.88 Under the new treatment, the SRWUIP payments are non-assessable non-exempt income (and so transparent to the income tax law) and the corresponding expenditure is not recognised by the law (either as a deduction or as part of the cost of any asset).

3.89 The new treatment ensures that irrigators do not have to fund the gap between the time the payments would be assessed to them and the time the income tax law would fully recognise the corresponding expenditure.

Human rights implications

3.90 This Schedule engages and promotes the right to health in Article 12 of the International Covenant on Economic, Social and Cultural Rights. The UN Committee on Economic, Social and Cultural Rights has interpreted Article 12 as extending to the underlying determinants of health, including a healthy environment.

3.91 This Schedule encourages irrigators to enter into a SRWUIP program and so improve the efficiency of their water use. That will free up more water for use in environmental activities, providing benefits that will secure the future of irrigation communities and protect or restore our environmental assets, such as wetlands and streams. Wetlands protect our shores from wave action, reduce the impacts of floods, absorb pollutants and provide critical habitat for animals and plants. River health is a crucial component of the sustainable management of our rivers, wetlands and groundwater basins.

3.92 Because irrigators enter into a SRWUIP program voluntarily and have the right to choose the new income tax treatment or to continue with the existing treatment, they suffer no disadvantage from this measure.

Conclusion

3.93 This Schedule is compatible with human rights. It promotes the right to health.

Assistant Treasurer, the Hon. David Bradbury

Self managed superannuation funds — acquisitions and disposals of certain assets between related parties

Outline of chapter

4.1 Schedule 4 to this Bill amends the *Superannuation Industry (Supervision) Act 1993* (SIS Act) to prescribe requirements for acquisitions and disposals of certain assets between self managed superannuation funds (SMSFs) and related parties. These requirements ensure that these transactions are conducted with transparency and are not used to circumvent the requirements of the superannuation law.

4.2 All references in this chapter are to the SIS Act unless otherwise stated.

Context of amendments

4.3 The *Super System Review* (Review) noted that SMSFs are closely held entities (as all members must also be trustees or directors of a corporate trustee) which may provide the opportunity for SMSF members to engage in behaviour that is inconsistent with the Government's retirement policy that superannuation savings should be invested for the sole purpose of providing an income in retirement.

4.4 While the Review acknowledged that some related party investments are consistent with Government policy, the Review was concerned that the current rules still provide avenues for potential abuse.

4.5 The Review was concerned that the off market acquisition and disposal of assets between related parties and SMSFs, where the guiding mind of both buyer and seller can effectively be the same person, lacks transparency, is inherently risky and is open to greater abuse than non-related party transactions.

4.6 The Review believed that the current provisions regulating related party acquisitions are insufficient to mitigate the risk of transaction date and asset value manipulation to illegally benefit the SMSF or a

related party. The Review did, however, conclude that SMSFs should retain the ability to conduct certain limited related party transactions.

4.7 The Review recommended that acquisitions and disposals of assets between related parties and SMSFs should be conducted through an underlying market where one exists, or where one does not exist, must be supported by a valuation from a suitably qualified independent valuer.

4.8 Schedule 4 to the Bill implements the Government's response to the Review's recommendations in relation to acquisitions and disposals of assets between SMSFs and related parties.

4.9 These amendments will provide greater transparency to related party acquisitions and disposals, enabling SMSF approved auditors and the Commissioner of Taxation (Commissioner), as Regulator, to monitor these transactions more effectively, which will enhance the integrity of the SMSF sector.

Summary of new law

4.10 Schedule 4 to the Bill:

- amends the existing prohibition on superannuation funds acquiring assets from related parties so that it applies to all regulated superannuation funds other than SMSFs;
- introduces a specific prohibition against trustees and investment managers of SMSFs acquiring assets from related parties, subject to certain exceptions;
- introduces new rules for SMSF trustees and investment managers when disposing of assets to related parties;
- introduces a new prohibition on schemes which avoid the operation of these new rules regulating SMSF related party transactions; and
- introduces administrative and civil penalties for contravention of these new rules.

Comparison of key features of new law and current law

New law	*Current law*
Acquisitions of certain assets	
A trustee or an investment manager of an SMSF must not acquire an asset from a related party of the fund, subject to certain exceptions.	A trustee or investment manager of an SMSF (as a regulated superannuation fund) must not intentionally acquire an asset from a related party of the fund, subject to certain exceptions.
Exceptions:	
The prohibition on acquiring an asset from a related party does not apply if the asset is a listed security acquired in the way prescribed by the regulations.	The prohibition on acquiring an asset from a related party does not apply if the asset is a listed security acquired at market value.
The prohibition on acquiring an asset from a related party does not apply if the asset is business real property of the related party acquired at market value, as determined by a qualified independent valuer.	The prohibition on acquiring an asset from a related party does not apply if the fund is a superannuation fund with fewer than five members and the asset is business real property of the related party acquired at market value.
The prohibition on acquiring an asset from a related party does not apply if the asset is acquired under a merger between regulated superannuation funds and at market value, as determined by a qualified independent valuer.	The prohibition on acquiring an asset from a related party does not apply if the trustee of a regulated superannuation fund acquired the asset under a merger between regulated superannuation funds.
The prohibition on acquiring an asset from a related party does not apply if the acquisition of the asset constitutes an investment that is covered by paragraph 66(2A)(a) (about certain in-house assets), is at market value as determined by a qualified independent valuer, and would not result in the level of in-house assets of the fund exceeding the level permitted by Part 8 of the SIS Act.	The prohibition on acquiring an asset from a related party does not apply if the acquisition of the asset constitutes an investment that is covered by paragraph 66(2A)(a) (about certain in-house assets), is at market value, and would not result in the level of in-house assets of the fund exceeding the level permitted by Part 8 of the SIS Act.
The prohibition on acquiring an asset from a related party does not apply if	No equivalent.

New law	***Current law***
the asset is acquired solely as a result of a change to the trustees of an SMSF.	
The prohibition on acquiring an asset from a related party does not apply if the asset is money.	The prohibition on acquiring an asset from a related party does not apply if the asset is money.
The prohibition on acquiring an asset from a related party does not apply if the asset is of a kind that the Regulator, by legislative instrument, determines may be acquired by SMSFs, or a class of SMSFs.	The prohibition on acquiring an asset from a related party does not apply if the asset is of a kind which the Regulator, by legislative instrument, determines may be acquired by any regulated superannuation fund, or a class of regulated superannuation fund in which the fund is included.
The prohibition on acquiring an asset from a related party of a SMSF does not apply if the asset is acquired in accordance with the requirements of subsections 66(2B) and 66(2C) (about the breakdown of relationships).	The prohibition on acquiring an asset from a related party of a regulated superannuation fund does not apply if the asset is acquired in accordance with the requirements of subsections 66(2B) and 66(2C) (about the breakdown of relationships).
A trustee or investment manager of an SMSF who acquires an asset from a related party otherwise than in accordance with an exception contravenes a civil penalty provision, to which civil or criminal penalties may be sought by the Regulator.	A trustee or investment manager or a regulated superannuation fund who intentionally acquires an asset from a related party where an exception does not apply is guilty of an offence punishable on conviction by imprisonment for a term not exceeding one year.
Disposals of certain assets:	
A trustee or an investment manager of an SMSF must not dispose of an asset to a related party of the fund, subject to certain exceptions.	No equivalent.
Exceptions:	
The prohibition on disposing of an asset to a related party does not apply if the asset is a listed security disposed of in the way prescribed by the regulations.	No equivalent.
The prohibition on disposing of an asset to a related party does not apply if the asset is one to which regulations in force for the purposes of section 62A (about collectables and personal use assets) apply.	No equivalent.

New law	***Current law***
The prohibition on disposing of an asset to a related party does not apply if the asset is money.	No equivalent.
The prohibition on disposing of an asset to a related party does not apply if the asset is of a kind that the Regulator, by legislative instrument, determines may be disposed of by SMSFs, or a class of SMSFs.	No equivalent.
The prohibition on disposing of an asset to a related party does not apply if the asset is disposed of solely as a result of a change to the trustees of an SMSF.	No equivalent.
The prohibition on disposing of an asset to a related party does not apply if the asset is not a listed security and is disposed of for market value, as determined by a qualified independent valuer.	No equivalent.
The prohibition on disposing of an asset to a related party of a SMSF does not apply if the disposal of the asset is to a trustee or investment manager of another SMSF, and the trustee or investment manager of the other fund may acquire the asset because of the operation of subsection 66A(4) (about relationship breakdowns).	No equivalent.
A trustee or investment manager of an SMSF who disposes of an asset to a related party otherwise than in accordance with an exception contravenes a civil penalty provision, to which civil or criminal penalties may be sought by the Regulator.	No equivalent.
A person must not enter into, commence to carry out, or carry out a scheme if the scheme results, or is likely to result, in a trustee or an investment manager of an SMSF acquiring or disposing of an asset in a manner that would avoid the prohibition on certain acquisitions and disposals.	A person must not enter into, commence to carry out, or carry out a scheme if the person entered into, commenced to carry out, or carried out the scheme or any part of the scheme with the intention that the scheme would result, or be likely to result in the acquisition of an asset by an SMSF (as a regulated superannuation fund) which would

New law	Current law
	avoid the prohibition on certain acquisitions.

Detailed explanation of new law

4.11 Schedule 4 prescribes requirements for acquisitions and disposals of certain assets between SMSFs and related parties. These requirements ensure that these transactions are conducted with transparency and are not used to circumvent the requirements of the superannuation law.

4.12 The requirements in section 66 relating to acquisitions of certain assets from members of regulated superannuation funds will continue to apply to regulated superannuation funds, except SMSFs. ***[Schedule 4, item 7, subsection 66(1)]***

Acquisitions of certain assets by self managed superannuation funds

A trustee or an investment manager of an SMSF must not acquire an asset from a related party of the fund, subject to a number of exceptions. ***[Schedule 4, item 13, subsection 66A(2)]***

An ***investment manager*** is a person appointed by a trustee of a fund or trust to invest on behalf of the trustee, or the trustees, of the fund or trust.

An ***asset*** is any form of property and, to avoid doubt, includes money (whether Australian currency or currency of another country). For the avoidance of doubt, acquisition of an asset includes *in specie* contributions to an SMSF by a related party of an SMSF.

A ***related party*** is any of the following:

- a member of the fund;
- a standard employer-sponsor of the fund; and
- an associate of one of those entities.

4.17 Part 8 of the SIS Act specifies who is an associate for different types of entities, including individuals and companies.

Exceptions

4.18 There are a number of exceptions to the prohibition on a trustee or investment manager acquiring an asset from a related party of the fund. ***[Schedule 4, item 13, subsections 66A(3) and (4)]***

Listed securities

A trustee or investment manager may acquire an asset from a related party if the asset is a listed security and it is acquired in a way prescribed by the regulations. ***[Schedule 4, item 13, paragraph 66A(3)(a)]***

4.20 A ***listed security*** is a security listed for quotation in the official list of:

- a licensed market within the meaning of section 761A of the *Corporations Act 2001* (defined as a financial market the operation of which is authorised by an Australian market licence);
- an approved stock exchange within the meaning of the *Income Tax Assessment Act 1997* (which are listed in Schedule 5 to the *Income Tax Assessment Regulations 1997*); or
- a market exempted under section 791C of the *Corporations Act 2001* (which lists exemptions from the requirement to be licensed).

Under the current section 66, SMSF trustees and investment managers have been able to acquire listed securities from related parties provided they are acquired at market value. The method by which these transactions have been effected has been dependent on the rules of the market the securities are traded on. For example, ownership of listed securities traded on the Australian Securities Exchange may be transferred off-market between parties through the use of a Transfer Form for Non-Market Transactions. The Review found that such transactions outside a formal market lack transparency and can be used to manipulate transaction dates and asset values to illegitimately benefit the SMSF or a related party.

Trustees and investment managers of SMSFs will not be prohibited from acquiring listed securities from related parties, provided that the appropriate method, as may be prescribed in the regulations, is used. The rules for acquiring listed securities are to be prescribed by regulation due to the broad definition of ‘listed securities’.

Business real property

4.23 A trustee or investment manager of an SMSF may acquire an asset from a related party if the asset is business real property acquired at market value, as determined by a qualified independent valuer. ***[Schedule 4, item 13, paragraph 66A(3)(b)]***

4.24 The terms 'business real property' and 'real property used in primary production business' are currently only defined for the purposes of section 66. Schedule 4 repeals these current definitions in subsection 66(5) and inserts a definition of 'business real property' into the definitions section (section 10), which incorporates the concepts of 'business' and 'real property used in primary production business'. The existing definitions have been moved and reworded to provide clarity, however it is not intended that this amendment will change their existing meanings. ***[Schedule 4, items 1 and 9 to 11, subsections 10(1) and 66(5]***

4.25 ***Business real property*** means:

- any freehold or leasehold interest of the entity in real property;
- any interest of the entity in Crown land, other than a leasehold interest, being an interest that is capable of assignment or transfer; or
- if another class of interest relating to real property is prescribed by regulations, any interest of that class held by the entity;

if the real property is used wholly and exclusively in one or more businesses (whether carried on by the entity or not).

[Schedule 4, item 3, subsection 21(1)]

Business real property does not include any interest held in the capacity of beneficiary of a trust estate. ***[Schedule 4, item 3, subsection 21(2)]***

4.27 For the purposes of the definition of 'business real property', real property used in one or more primary production businesses does not cease to be used wholly and exclusively in those businesses only because:

- an area of the real property, not exceeding two hectares, contains a dwelling used primarily for domestic or private purposes; and

- the area is also used primarily for domestic or private purposes;

provided that the use for domestic or private purposes is not the predominant use of the real property. ***[Schedule 4, items 3 and 12, subsections 21(3) and 66(6)]***

For the purposes of the definition of 'business real property', ***business*** includes any profession, trade, employment, vocation or calling carried on for the purposes of profit, including the carrying on of primary production and the provision of professional services, but does not include occupation as an employee. ***[Schedule 4, item 3, subsection 21(4)]***

Schedule 4 also inserts a definition of ***primary production business*** in subsection 10(1) as having the same meaning as in the *Income Tax Assessment Act 1997*. ***[Schedule 4, item 2, subsection 10(1)]***

To satisfy this exception, trustees and investment managers of SMSFs will be required to obtain a market valuation from a 'qualified independent valuer'. A valuer may be qualified either through holding formal valuation qualifications or by being considered to have specific knowledge, experience and judgment by their particular professional community. This may be demonstrated by being a current member of a relevant professional body or trade association.

The valuer must also be independent. Therefore, the valuer cannot be a member of the fund or a related party of the fund. They should be impartial, unbiased and not be influenced or appear to be influenced by others.

Independent and impartial valuation services are also offered by the Australian Valuation Office.

This exception is not intended to operate or apply in a different manner than the current exception in paragraph 66(2)(b) which applies to other regulated superannuation funds, except that the asset must be acquired at market value as determined by a qualified independent valuer.

Market value, in relation to an asset, means the amount that a willing buyer of the asset could reasonably be expected to pay to acquire the asset from a willing seller if the following assumptions were made:

- that the buyer and seller dealt with each other at arm's length in relation to the sale;
- that the sale occurred after proper marketing of the asset; and

- that the buyer and the seller acted knowledgeably and prudentially in relation to the sale.

Mergers between regulated superannuation funds

A trustee or investment manager may acquire an asset from a related party under a merger between regulated superannuation funds at market value, as determined by a qualified independent valuer. ***[Schedule 4, item 13, paragraph 66A(3)(c)]***

This exception is not intended to operate or apply in a different manner to SMSFs than the exception in the current paragraph 66(2)(c) which applies to regulated superannuation funds, except that the asset must be acquired at market value as determined by a qualified independent valuer.

In-house assets

A trustee or investment manager may acquire an asset from a related party if the acquisition of the asset constitutes an investment in certain in-house assets (those covered by paragraph 66(2A)(a)), is at market value as determined by a qualified independent valuer, and would not result in the level of in-house assets of the fund (within the meaning of Part 8) exceeding the level permitted by that Part. ***[Schedule 4, item 13, paragraph 66A(3)(d)]***

This exception is not intended to operate or apply in a different manner to SMSFs than the exception in the current subsection 66(2A), except for the requirement for market value to be determined by a qualified independent valuer.

Change of trustees

A trustee or investment manager may acquire an asset from a related party if the acquisition is solely a result of a change to the trustees of an SMSF. ***[Schedule 4, item 13, paragraph 66A(3)(e)]***

Example 4.1:

Anthony, Ian, Jennifer and Edwina (all siblings) are individual trustees of Purple SMSF. Anthony and Jennifer cease to be members and trustees of Purple SMSF. Their interest in the trust property will transfer to the remaining trustees. This exception ensures that the prohibition on acquiring an asset from a related party does not apply to prevent such a change in trustees.

Money

4.40 A trustee or investment manager may acquire an asset from a related party if the asset is money. ***[Schedule 4, item 13, paragraph 66A(3)(f)]***

An ***asset*** includes money (whether Australian currency or currency of another country). This exception ensures that a trustee or an investment manager of an SMSF may accept money from a related party. This exception is not intended to operate or apply in a different manner to SMSFs than the way that the current section 66 allows a regulated superannuation fund to accept money from a related party, for example, in the form of contributions.

Determination by the Regulator

A trustee or investment manager of an SMSF may acquire an asset from a related party if the asset is of a kind that the Regulator, by legislative instrument, determines may be acquired by SMSFs. The Regulator may make a determination that specifies different kinds of assets for different classes of SMSFs. ***[Schedule 4, item 13, paragraph 66A(3)(g)]***

This exception will provide the Regulator with flexibility to determine that SMSFs may acquire certain assets in certain circumstances. The Regulator may or may not determine conditions in relation to the acquisition, including that the acquisition must occur at market value, as determined by a qualified independent valuer.

This exception is not intended to operate or apply in a different manner to SMSFs than the current exception in paragraph 66(2)(d) applies to regulated superannuation funds.

Breakdown of relationships

A trustee or investment manager of an SMSF may acquire an asset from a related party if certain requirements relating to the breakdown of relationships listed in subsections 66(2B) and (2C) are satisfied. ***[Schedule 4, item 13, subsection 66A(4)]***

This exception is intended to apply to acquisitions involving SMSFs and related parties, as it currently applies to acquisitions involving regulated superannuation funds. Referring to subsections 66(2B) and 66(2C) in subsection 66A(4) avoids unnecessary repetition of the legislation.

Disposals of certain assets by self managed superannuation funds

Schedule 4 also inserts requirements relating to disposals of certain assets by SMSFs to related parties.

A trustee or an investment manager of a SMSF must not dispose of an asset to a related party of the fund, unless an exception applies. ***[Schedule 4, item 13, subsection 66B(2)]***

For the avoidance of doubt, disposal of an asset includes *in specie* payments to a related party by an SMSF.

Exceptions

There are a number of specific exceptions and one general exception to the prohibition on a trustee or investment manager acquiring an asset from a related party of the fund.

Listed securities

A trustee or investment manager may dispose of an asset to a related party if the asset is a listed security and the disposal is in a way prescribed by the regulations. ***[Schedule 4, item 13, paragraph 66B(3)(a)]***

The regulations may prescribe the way in which SMSFs may dispose of listed securities to related parties of an SMSF. The rules for disposing of listed securities are to be prescribed by regulation due to the need to provide sufficient detail and flexibility for different types of ‘listed securities’.

Collectables and personal use assets

A trustee or investment manager may dispose of an asset if the asset is one to which regulations in force for the purposes of section 62A (about collectables and personal use assets) apply. ***[Schedule 4, item 13, paragraph 66B(3)(b)]***

This exception ensures that the existing detailed rules continue to apply when a trustee of an SMSF disposes of certain collectable and personal use assets to related parties for which regulations have been made.

Money

A trustee of investment manager may dispose of an asset to a related party if the asset is money. ***[Schedule 4, item 13, paragraph 66B(3)(c)]***

This exception ensures that a trustee or an investment manager of an SMSF may continue to make payments of money to a related party, for example, lump sum superannuation benefits and pensions.

Determination by the Regulator

A trustee or investment manager of an SMSF may dispose of an asset to a related party if the asset is of a kind that the Regulator, by legislative instrument, determines may be disposed of by SMSFs. The Regulator may make a determination that specifies different kinds of assets for different classes of SMSFs. ***[Schedule 4, item 13, paragraph 66B(3)(d)]***

This exception will provide the Regulator with flexibility to determine that SMSFs may dispose of certain assets in certain circumstances. The Regulator may or may not determine conditions in relation to the disposal, including that the disposal must occur at market value, as determined by a qualified independent valuer.

Change in trustees

A trustee or investment manager may dispose of an asset to a related party if the disposal is solely as a result of a change to the trustees of an SMSF. ***[Schedule 4, item 13, paragraph 66B(3)(e)]***

Example 4.2:

Ian and Edwina are trustees of Purple SMSF. Their siblings, Anthony and Jennifer become members and trustees of Purple SMSF. An interest in the trust property will transfer to the new trustees. This exception ensures that the prohibition on disposing of an asset to a related party does not apply to prevent such a change in trustees.

General exception — disposal for market value, as determined by a qualified independent valuer

4.60 If the asset is not a listed security, a trustee or investment manager may dispose of the asset to a related party if the asset is disposed of for market value, as determined by a qualified independent valuer. ***[Schedule 4, item 13, paragraph 66B(3)(f)]***

Breakdown of relationships

4.61 A trustee or investment manager of an SMSF may dispose of an asset to a related party if the disposal of the asset is to a trustee or investment manager of another self managed superannuation fund, and the trustee or investment manager of the other fund may acquire the asset because the requirements relating to the breakdown of relationships covered by subsections 66(2B) and (2C) are satisfied in relation to the

acquisition of the asset by the other fund. ***[Schedule 4, item 13, subsection 66B(4)]***

4.62 This exception ensures that where there is a disposal of an asset to a trustee or investment manager of another superannuation fund as a result of a relationship breakdown, an exception applies for disposals in the corresponding way that it applies to acquisitions.

Prohibition on avoidance schemes

4.63 Schedule 4 introduces a prohibition on avoidance schemes, similar to the prohibition contained in subsection 66(3) that applies to acquisition of certain assets by regulated superannuation funds. The prohibition specific to SMSFs is intended to apply in in relation to acquisitions and disposals of assets in a similar manner to the prohibition relating to acquisitions of certain assets by regulated superannuation funds.

4.64 This prohibition makes it clear that trustees and investment managers of SMSFs must not enter into schemes to circumvent the application of the prohibition on acquisition and disposal of certain assets between related parties.

4.65 A person must not enter into, commence to carry out, or carry out a scheme (within the meaning of section 66) if all the following are satisfied:

- the scheme results, or is likely to result, in a trustee or an investment manager of an SMSF:
  - acquiring an asset from an entity; or
  - disposing of an asset to an entity,
- the scheme avoids the prohibition from applying to the acquisition, or the disposal, (as appropriate) because the entity is not a related party of the fund;
- that subsection would so apply were the entity a related party of the fund; and
- the entity has a connection, directly or indirectly through one or more interposed entities, with a related party of the fund.

[Schedule 4, item 13, subsection 66C(1)]

4.66 ***Scheme*** means:

- any agreement, arrangement, understanding, promise or undertaking:
  - whether expressed or implied; or
  - whether or not enforceable, or intended to be enforceable by legal proceedings, and
- any scheme, plan, proposal, action, course of action or course of conduct, whether unilateral or otherwise.

Penalties

Administrative penalties

4.67 A trustee or director of a corporate trustee who contravenes the new prohibitions will be liable to an administrative penalty of 60 penalty units for each contravention. ***[Schedule 4, item 19, subsection 166(1)]***

4.68 The provisions relating to administrative penalties in Schedule 4 commence immediately after the commencement of item 23 of Schedule 3 to the Superannuation Legislation Amendment (Reducing Illegal Early Release and Other Measures) Bill 2012, which proposes the new administrative penalty framework. ***[Schedule 4, item 20]***

Civil penalties

4.69 The provisions relating to acquisitions and disposals of assets, and the prohibition of avoidance schemes are all civil penalty provisions. Part 21 of the SIS Act provides for civil and criminal consequences of contravening, or being involved in a contravention of these subsections.

4.70 The Regulator may seek a civil penalty order of up to 2,000 penalty units for contravention of a civil penalty provision. If a trustee or investment manager contravenes a civil penalty provision either dishonestly and intending to gain an advantage for a person, or intending to deceive or defraud a person, the trustee or investment manager is guilty of an offence punishable on conviction by imprisonment for not longer than five years. ***[Schedule 4, items 13 and 14, subsections 66A(2), 66B(2), 66C(1) and paragraph 193(b]***

Transitional provisions – in house assets

4.71 Schedule 4 inserts a new definition of 'business real property' into the definitions section of the SIS Act, which applies from the commencement date of 1 July 2013 (see paragraph 4.24).

4.72 Schedule 4 also provides for a transitional provision in relation to the current definition of 'business real property' in subsection 66(5). Item 9 of Schedule 1 to the *Superannuation Industry (Supervision) Amendment Act 2010* deleted of the words '(within the meaning of subsection 66(5))' following the reference to 'business real property' in paragraph 71(1)(g), which relates to the meaning of an in-house asset. Omitting this reference to the meaning of 'business real property' as it appears in paragraph 71(1)(g) may have created uncertainty as to the meaning of 'business real property' for the purposes of paragraph 71(1)(g). This transitional provision re-instates the words '(within the meaning of subsection 66(5))' after the reference to 'business real property' in paragraph 71(1)(g) from the date of enactment of the *Superannuation Industry (Supervision) Amendment Act 2010* to remove any uncertainty. ***[Schedule 4, item 4]***

Consequential amendments

4.73 Section 62A provides that regulations may prescribe rules in relation to trustees of SMSFs making, holding and realising investments involving certain collectables and personal use assets. Schedule 4 clarifies that subsection 62A(1) has effect subject to section 66A, relating to acquisitions of assets by SMSFs. ***[Schedule 4, items 5 and 6, subsections 62A(1) and 62A(2)]***

4.74 Schedule 4 also makes a minor amendment to subparagraph 66(2A)(a)(iv) to remove a reference to a paragraph which has been repealed. ***[Schedule 4, item 8, subparagraph 66(2A)(a)(iv)]***

4.75 Schedule 4 also inserts notes to clarify that an administrative penalty applies to a contravention of the prohibition on acquiring or disposing of an asset to a related party. ***[Schedule 4, items 15 to 18, subsections 66A(2) and 66B(2)]***

STATEMENT OF COMPATIBILITY WITH HUMAN RIGHTS

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

Tax and Superannuation Legislation Amendment (2013 Measures No. 1) Bill 2013

Schedule 4 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

Schedule 4 introduces requirements relating to acquisitions and disposals of certain assets involving self managed superannuation funds (SMSFs) and related parties.

SMSFs are closely held entities where there is a maximum of four members and all members must also be trustees of the superannuation fund.

The *Super System Review* (Review) noted that given the nature of SMSFs as closely held entities, related party transactions are inherently risky and open to greater abuse than non-related party transactions, as the buyer and seller are effectively the same person.

While the Review debated recommending prohibiting all related party transactions, it concluded that retaining the ability to conduct limited related party transactions was still a desirable feature.

Schedule 4 implements the Government's response by amending the current law to provide specific rules acquisitions and disposals between SMSFs and related parties, specifically Schedule 4:

- introduces a specific prohibition against trustees and investment managers of SMSFs acquiring assets from related parties, subject to certain exceptions;
- introduces new rules for SMSF trustees and investment managers when disposing of assets to related parties;

- introduces a prohibition on schemes which avoid the operation of these new rules regulating SMSF related party transactions; and

- introduces administrative and civil penalties for contravention of these new rules.

Schedule 4 imposes an administrative penalty for contravention of the new requirements relating to acquisitions and disposals. The administrative penalty is 60 penalty units. The level of administrative penalty is consistent with other civil penalty provisions in the *Superannuation Industry (Supervision) Act 1993* (see subsections 65(1), 67(1), 84(1) and 106(1)).

A civil penalty may only be imposed by a court, on application by the Regulator. Where a court is satisfied that a person has contravened a civil penalty provision, a court may impose a monetary penalty up to a maximum 2,000 penalty units.

Schedule 4 introduces a specific penalty regime for SMSFs in comparison to the current penalty regime for regulated superannuation funds under section 66 of the *Superannuation Industry (Supervision) Act 1993*. The new prohibition on acquisitions and disposals between SMSFs and related parties does not contain an element of 'intention'. This is appropriate for SMSFs as closely held funds where all members must also be trustees and any related party transactions should be apparent. It is also not appropriate to impose penalties under the new regime on a provision which contains and element of intention.

Contravention of a civil penalty provision may however constitute an offence where a court is satisfied a person has contravened a civil penalty provision either dishonestly and intending to gain an advantage for a person, or intending to deceive or defraud someone. An offence is punishable on conviction by imprisonment for a maximum of five years.

Human rights implications

Schedule 4 does not engage any of the applicable rights or freedoms.

Conclusion

Schedule 4 is compatible with human rights as it does not raise any human rights issues.

Minister for Financial Services and Superannuation, the Hon Bill Shorten

Introduction to loss carry-back

Outline of chapter

5.1 Schedules 5 and 6 amend the income tax law to allow corporate tax entities to carry-back losses to previous income years. This chapter provides an overview of the loss carry-back measure.

5.2 The loss carry-back measure allows corporate tax entities that have paid tax in the past, but are now in a tax loss position, to choose to obtain a refund of some of the tax they have previously paid.

5.3 The operative rules for the loss carry-back measure are primarily contained in Division 160 of the *Income Tax Assessment Act 1997* (ITAA 1997).

Context of amendments

5.4 Following the Tax Forum in October 2011, the Government established the independent Business Tax Working Group (Working Group) to consider what kind of business tax system would best support Australia's future growth prospects.

5.5 In its *Final Report on the Tax Treatment of Losses*, the Working Group recommended that loss carry-back would be a worthwhile reform in the near term. In particular, the Working Group proposed a model that:

- is limited to companies;
- provides a two-year loss carry-back period on an ongoing basis; and
- limits the amount of losses that can be carried back by applying a quantitative cap of at least $1 million.

5.6 On 6 May 2012, the Government announced that it would introduce loss carry-back to the income tax law for corporate tax entities.

5.7 The Government issued a consultation paper, *Improving access to company losses,* in July 2012.

5.8 The introduction of loss carry-back also implements Recommendation 31 of the 2010 *Australia's Future Tax System* Review, which says:

> '…companies should be allowed to carry back a revenue loss to offset it against the prior year's taxable income, with the amount of any refund limited to the company's franking account balance.'

5.9 Loss carry-back will encourage companies to adapt to changing economic conditions and take advantage of new opportunities through investment. Firms will be able to utilise their tax losses sooner and reduce the extent to which they risk never being able to use those losses.

The case for loss carry-back

5.10 Implementing a change of business strategy may involve new investment in machinery and equipment, in the development of new goods and services and in re-skilling of people. These new investment decisions involve taking risks.

5.11 Policies that facilitate changes in business strategies and support sensible risk taking will enhance productivity growth in all sectors of the economy by increasing the quantity and quality of investment.

5.12 Under the current tax law, the Commonwealth collects, as tax, a share of any profits a company makes in an income year but does not share directly in a company's loss. Instead, future tax may be reduced because the company can deduct that loss from its future profits. This means there is an asymmetric treatment of profits and losses.

5.13 This asymmetry can mean that a company that makes a profit in one year and a loss in the next year will pay a higher effective tax rate over the two year period than another company that makes the same overall profit in a more even fashion.

Example 5.1: Tax outcomes vary according to cash flow risk

> Tables 5.1 and 5.2 show the impact of the tax treatment of losses on the total tax of two companies whose net profits are identical. If a company makes the same total profit in a variable manner, by deriving a large profit followed by a loss (Table 5.1), it will pay more tax over the two year period than a company that makes the same overall profit in a more even manner, with two smaller profit years (Table 5.2).

Table 5.1: Tax treatment for higher risk profit company

	Year 1 *$*	*Year 2* *$*	*Total* *$*
Profit (loss)	200	-100	100
Tax @ 30%	60	0	60

Table 5.2: Tax treatment for lower risk profit company

	Year 1 *$*	*Year 2* *$*	*Total* *$*
Profit (loss)	50	50	100
Tax @ 30%	15	15	30

In this stylised example, two companies earn the same $100 total profit over two years but the company earning it in a more variable manner pays double the tax that the more conservative company pays. The risky company therefore experiences an effective tax rate of 60 per cent, compared with the statutory tax rate of 30 per cent.

5.14 The potential to incur a higher effective tax rate can lower the expected after-tax return on a potential investment. This can distort the relative attraction of competing projects from a firm's perspective, compared with their value to the economy as a whole.

Example 5.2: Tax treatment of losses can distort investment choices

Tables 5.3 and 5.4 show the impact of the tax treatment of losses for two possible investment choices that present different levels of risk. One option is a higher-risk investment, which has a 40 per cent chance of incurring a loss (20 per cent chance of incurring a loss of $60 and a 20 per cent chance of incurring a loss of $40). The other option is a lower-risk investment that has a certain profit outcome. For simplicity, the investments have one year lives.

Table 5.3: Tax treatment for a low risk investment

Possible before-tax return on an investment ($)	*Probability of return (%)*	*Before-tax expected return ($)*	*After-tax expected return ($)*
40	50	20	14
20	50	10	7
Total	**100**	**30**	**21**

Table 5.4: Tax treatment for a high risk investment

Possible before-tax return on an investment ($)	*Probability of return (%)*	*Before-tax expected return ($)*	*After-tax expected return ($)*
140	10	14	9.8
100	20	20	14
80	20	16	11.2
20	10	2	1.4
–40	20	–8	–8
–60	20	–12	–12
Total	**100**	**32**	**16.4**

In this example, the riskier investment has a higher expected before-tax return ($32) than the low-risk investment ($30). However, the expected after-tax return is greater for the low-risk investment ($21) than the high risk investment ($16.4). In practice, this outcome would generally be partially mitigated in future years by deducting the tax losses against future profits.

5.15 The asymmetric tax treatment of profits and losses can therefore give rise to a bias against riskier investments, which will tend to divert capital to investments that are of lower value for the economy as a whole.

5.16 Reducing the tax system's bias against corporate risk taking can be expected to increase the quantity and the quality of investment, improving the allocation of resources across the economy. This should have positive flow-on effects for productivity, which in turn will support growth in real wages and employment.

5.17 The introduction of loss carry-back gives profitable companies greater certainty that they will be able to utilise a loss that arises from an investment they make to adjust to changing economic circumstances. This reduces the asymmetry between the taxation treatment of profits and losses.

5.18 It also improves the cash flow of affected companies by allowing them to access their losses in a timelier manner. This promotes sensible risk taking by companies, helping them to adjust to changing economic conditions in a patchwork economy.

5.19 Restricting loss carry-back to those companies that have recently paid tax ensures that the measure is targeted to companies that have a history of conducting a profitable enterprise. The measure is not intended to provide a seed funding for starting a new enterprise.

The loss carry-back tax offset

Outline of chapter

6.1 This chapter explains how the loss carry-back tax offset rules operate.

6.2 All legislative references in this chapter are to *the Income Tax Assessment Act 1997* (ITAA 1997) unless otherwise indicated.

Summary of new law

6.3 The loss carry-back rules give a corporate tax entity the choice of carrying back all or part of a tax loss from the current income year, or from the preceding income year, against an unutilised income tax liability for either of the years before the current year. The measure applies to assessments for the 2012-13 and later income years. A transitional one year carry-back period applies for the 2012-13 income year.

6.4 If the loss carry-back conditions are satisfied, a corporate tax entity can get a refundable tax offset for the losses it chooses to carry back.

6.5 The tax offset the entity can get is the lowest of:

- the tax value of the amount of the loss the entity chooses to carry back;
- the entity's franking account balance at the end of the current year;
- $1 million multiplied by the corporate tax rate for the current year[1] (currently $300,000); and
- the entity's tax liability for the income year(s) it carries a loss back to.

[1] It is assumed throughout Chapters 6 to 8 that the corporate tax rate is 30 per cent, except where a different position is taken expressly.

6.6 A corporate tax entity that has net exempt income in an income year it carries a loss back to must reduce the loss it carries back by that net exempt income before it works out its offset for the remaining loss.

6.7 The loss carry-back rules deny entitlement to the tax offset where there is a scheme for the disposition of membership interests in the corporate tax entity that changes who controls or is able to control the entity. The offset will be denied only if a purpose of the scheme (whether or not the dominant purpose but not including an incidental purpose) is to obtain a financial benefit calculated by reference to a loss carry-back tax offset.

Comparison of key features of new law and current law

New law	*Current law*
Tax losses can either be: • carried forward and deducted against income derived in later income years; or • carried back against income of earlier income years to produce a refundable tax offset.	Tax losses can be carried forward and deducted against income derived in later income years.

Detailed explanation of new law

6.8 The loss carry-back refundable tax offset allows a corporate tax entity to carry back a tax loss against income tax payable for the two preceding income years.

6.9 The objective of loss carry-back is to reduce the tax disincentive for corporate tax entities to undertake sensible investment risks. It does this by providing a corporate tax entity with access to its tax losses sooner than is the case under the existing loss carry-forward arrangements. ***[Schedule 5, item 2, section 160-5]***

Entities eligible for loss carry-back

6.10 Loss carry-back is only available for corporate tax entities (broadly, entities that are taxed like companies). ***[Schedule 5, item 2, paragraph 160-10(a)]***

6.11 A 'corporate tax entity' is defined in section 960-115 to be an entity that is:

- a company;
- a corporate limited partnership;
- a corporate unit trust; or
- a public trading trust.

6.12 Some of those entities may be corporate tax entities at some times but not at others. An entity can claim the loss carry-back tax offset for an income year only if it was a corporate tax entity throughout that income year. ***[Schedule 5, item 2, paragraph 160-10(a)]***

6.13 It must also have been a corporate tax entity throughout the income year the loss is carried back to and throughout any intervening income year. ***[Schedule 5, item 2, section 160-25]***

Loss carry-back gives rise to a refundable tax offset

6.14 A corporate tax entity can choose to utilise a tax loss to obtain a loss carry-back tax offset if:

- it has an unutilised tax loss for the current income year or for the preceding income year (called 'the middle year');
- it has an unutilised income tax liability for the middle year or for the income year before that (called 'the earliest year'); and
- for the current income year and each of the previous five income years, it has lodged an income tax return, or was not required to lodge a return, or has been assessed for income tax purposes by the Commissioner of Taxation (Commissioner).

[Schedule 5, item 2, paragraphs 160-10(b) to (e)]

6.15 The loss carry back offset is a refundable tax offset. ***[Schedule 5, item 1, section 67-23]***

Losses eligible for loss carry-back

6.16 Corporate tax entities can carry their tax losses back to produce a tax offset as an alternative to carrying them forward as a deduction for future income years.

6.17 Only tax losses can be carried back. Capital losses cannot be carried back because the capital gains tax regime operates on a realisation basis. Allowing capital losses to be carried back to produce a tax offset would mean that entities could choose to realise their capital losses to get an offset but defer their capital gains.

6.18 Generally speaking, an entity makes a 'tax loss' for an income year if its deductions exceed its assessable income for that income year.

Tax losses of the current income year

6.19 The most common case involves an entity carrying back a tax loss it makes in the current income year. ***[Schedule 5, item 2, subparagraph 160-10(b)(i)]***

6.20 Such a loss can be carried back against a tax liability of either or both of the two previous years (the middle year or the earliest year). The entity could choose to carry back some of its current year tax loss to the middle year and some of it to the earliest year. ***[Schedule 5, item 2, paragraphs 160-10(c) and (e) and subsection 160-20(1)]***

Example 6.1: Losses of the current income year

Super Syed Pty Ltd has the following outcomes:

Income year	*Taxable income/ (loss)*	*Tax liability*	*Refundable offset*	*Loss carried forward*
2013-14	$500,000	$150,000		
2014-15	$2 million	$600,000	0	0
2015-16	($5 million)	0	$300,000	$4 million

In 2015-16, Super Syed incurs a $5 million tax loss. Super Syed carries back $1 million of the loss with a tax value of $300,000 against its 2014-15 income tax liability or against its 2013-14 liability, or some against one year and some against the other. It chooses to carry $500,000 back to each of those years, producing a maximum offset of $300,000 and leaving $4 million of its 2015-16 losses still unused.

Tax losses of the middle year

6.21 The less common case involves an entity carrying back an unutilised tax loss from the middle year against its tax liability from the earliest year. There is no choice about which year to carry such a loss back to because losses can only be carried back two years before the current year. ***[Schedule 5, item 2, subparagraph 160-10(b)(ii)]***

Example 6.2: Losses of the middle year

Continuing the previous example:

Income year	***Unused taxable income/ (loss)***	***Unused tax liability***	***Refundable offset***	***Loss carried forward***
2014-15	$1.5 million	$450,000	0	0
2015-16	($4 million)	0	$300,000	$3 million
2016-17	0	0	$300,000	

In 2016-17 Super Syed Pty Ltd can carry back $1 million of its remaining $4 million tax loss from 2015-16 (which is now the middle year) against its unused tax liability of 2014-15 (the earliest year) to gain the maximum $300,000 tax offset in 2016-17. It will still have $3 million of its 2015-16 loss left that it can carry forward to deduct against future income years' assessable income.

Tax losses from both years

6.22 A corporate tax entity can carry back losses from *both* the middle year and the current year at the same time. Both would have to be carried back to the earliest year. The entity would choose how much of each year's loss to carry back. ***[Schedule 5, item 2, subsection 160-20(1)]***

Example 6.3: Losses of both years

Kathryn Joyce Inc. has the following outcomes:

Income year	*Unused taxable income/ (loss)*	*Unused tax liability*	*Refundable offset*	*Loss carried forward*
2014-15	$2 million	$600,000	0	0
2015-16	($700,000)	0	0	0
2016-17	($2 million)	0	$300,000	$1.7 million

In 2016-17, Kathryn Joyce can carry back its loss from the current year, or its loss from 2015-16, or some from each year. It decides to carry back the whole loss from 2015-16 and $300,000 from 2016-17. That will produce the maximum $300,000 tax offset and leave it with $1.7 million of its 2016-17 loss to carry forward to deduct against the assessable income of future years.

6.23 Tax losses not used for loss carry-back in the current income year are available to reduce any taxable income in that income year or a future income year, according to the usual rules for deducting prior-year losses in Division 36.

Tax losses ineligible for carry-back

6.24 Some tax losses cannot be carried back.

6.25 An entity cannot carry-back losses that have been transferred under:

- Division 170 — transfers between companies in the same foreign banking group; or
- Subdivision 707-A — transfers to the head company of a consolidated group by an entity joining the group.

[Schedule 5, item 2, paragraph 160-30(a)]

6.26 In addition, the part of a tax loss that is deemed to exist when a corporate tax entity has excess franking offsets for an income year (see section 36-55) is not eligible for carry-back because it does not represent an economic loss. Allowing it to produce a tax offset would mean that a past payment of tax could give rise to a refund of that tax without any effect on the entity's willingness to take sensible investment risks. The

real part of the income year's tax loss would still be able to be carried back. ***[Schedule 5, item 2, paragraph 160-30(b)]***

The loss carry-back period

6.27 For the 2013-14 and later income years, a loss carry-back refund can be claimed against tax liabilities of either of the two income years preceding the current income year. ***[Schedule 5, item 6, section 160-1 of the Income Tax (Transitional Provisions) Act 1997 (IT(TP)A 1997)]***

6.28 As a transitional measure for the 2012-13 income year, a loss carry-back refund can only be claimed against the tax liability for 2011-12 income year. ***[Schedule 5, item 6, section 160-5 of the IT(TP)A 1997]***

The choice to carry-back losses

6.29 Loss carry-back is optional, mirroring the existing choice corporate tax entities have about whether to deduct their tax losses (see subsections 36-17(2) and (3)). An entity can choose to carry a tax loss back or not as it sees fit. That is, the entity can choose:

- how much of its tax loss for the current year is to be carried back to the earliest year;
- how much of its tax loss for the middle year is to be carried back to the earliest year; and
- how much of its tax loss for the current year is to be carried back to the middle year.

[Schedule 5, item 2, subsection 160-20(1)]

6.30 Therefore, as well as choosing whether or not to claim a loss carry-back tax offset, an entity can also choose which tax loss to carry back (if it has a loss in both the current year and the middle year). It could choose to carry back losses from both years.

6.31 It can also choose which years to carry a tax loss back to (if it has a tax liability for both the middle year and the earliest year). It could choose to carry its loss back to both of those years.

6.32 Finally, an entity can choose how much of a loss to carry back (subject to the limit on the total amount of the offset it can produce for any given year). An entity might normally choose to carry back the maximum amount it can but there could be some cases where it would not do so. For example, a company might only wish to debit its franking

account by less than the maximum refund in order to retain its capacity to pay a fully franked dividend.

6.33 The choice to claim a loss carry-back tax offset is made by notifying the Commissioner in the approved form. The choice must specify that the entity wishes to claim the offset and:

- each loss year that it wishes to carry an amount back from;
- the amount of the loss it wishes to carry back; and
- each year it wishes to carry the loss back to.

[Schedule 5, item 2, subsection 160-20(2)]

6.34 The choice must be made by the time that the entity lodges its tax return for the current income year, or within such further time as the Commissioner allows. ***[Schedule 5, item 2, subsection 160-20(2)]***

6.35 The approved form would usually be the corporate tax entity's income tax return, so the claim would normally be made at the same time as the tax return is lodged. However, there might be cases where the claim is not made in the return. For example:

- an entity that is not required to lodge a return might claim the offset in a separate form; or
- an entity might wish to claim the offset when one of its assessments is amended after it has lodged its return, making loss carry-back possible for the current year or changing the maximum amount of the offset available — in such a case, the Commissioner would have to allow the choice to be made after the date for lodging the income tax return.

How the loss carry-back tax offset is calculated

6.36 The amount of an entity's loss carry-back tax offset is worked out in a series of steps.

Step 1: Work out the amount of the loss to be carried back

6.37 The first step is to work out the amount of the tax loss that the entity is carrying back to each of the two years before the current year (the middle year and the earliest year). These will be the amounts the entity has chosen to carry back to those years. ***[Schedule 5, item 2, step 1 in subsection 160-15(2)]***

Example 6.4: Choosing the amounts to carry back

Quigley Enterprises Ltd makes a $400,000 tax loss in the 2016-17 income year. Its franking account balance at the end of that year is $120,000. In 2014-15, it had a tax liability of $48,000 and, in 2015-16, it had a tax liability of $21,000. It also had net exempt income of $4,000 in 2015-16. The corporate tax rate is 30 per cent in each of those years.

Quigley chooses to carry back $160,000 to 2014-15 and $74,000 to 2015-16. The remaining $166,000 is available to deduct against future taxable income.

Step 2: Reduce the step 1 amount by net exempt income

6.38 The second step reduces the step 1 amount by the net exempt income of the year the loss is carried back to. This ensures that, for the purposes of the loss carry-back tax offset, net exempt income is applied in the same way as it is applied when working out the amount of deductible losses in an income year. ***[Schedule 5, item 2, step 2 in subsection 160-15(2)]***

Example 6.5: Reduction for net exempt income

Continuing the previous example, the amount Quigley carried back to 2015-16 is reduced by the $4,000 net exempt income, leaving $70,000. The amount carried back to 2014-15 is not reduced because there was no net exempt income for that year.

Step 3: Convert the step 2 amount to a tax equivalent amount

6.39 The third step converts those reduced amounts into tax equivalent amounts by multiplying the step 2 amount by the corporate tax rate for the current year. ***[Schedule 5, item 2, step 3 in subsection 160-15(2)]***

Example 6.6: Converting amounts to 'tax equivalents'

Continuing the previous example, the $160,000 carried back to 2014-15 is converted into a tax equivalent amount by multiplying it by the 30 per cent corporate tax rate, producing a result of $48,000. The reduced amount carried back to 2015-16 is converted into a tax equivalent amount in the same way, producing a result of $21,000.

Step 4: Reduce the step 3 amount so that it does not exceed the relevant tax liability

6.40 The fourth step reduces the converted amount so that it does not exceed the amount of the tax liability available for the income year the loss was carried back to. The result of this step, for each income year an

amount is carried back to, is the ***loss carry back tax offset component*** for that income year. ***[Schedule 5, item 2, step 4 in subsection 160-15(2)]***

Example 6.7: Reducing amounts to reflect tax liability

Continuing the previous example, neither amount carried back, after conversion into its tax equivalent amount, exceeds the tax liability for the income year it was carried back to. Therefore, neither amount is reduced. The loss carry back tax offset component for 2014-15 is $48,000 and for 2015-16 is $21,000.

6.41 If amounts were carried back to both the earliest year and the middle year, the loss carry back tax offset components for those two years are added together to produce the amount of the tax offset. ***[Schedule 5, item 2, paragraph 160-15(1)(a)]***

Limits on the loss carry back tax offset

6.42 The loss carry back tax offset for the current income year cannot exceed:

- the balance in the entity's franking account at the end of that current income year; or
- the tax payable on $1 million taxable income ($300,000 at the current corporate tax rate).

[Schedule 5, item 2, paragraphs 160-15(1)(b) and (c)]

Example 6.8: Working out the offset amount

Continuing the previous example, the two loss carry-back tax offset components are added together to produce a total of $69,000. This is less than Quigley's franking account balance and less than the $300,000 maximum offset, so is not reduced. Therefore, Quigley's tax offset for 2016-17 is $69,000.

6.43 The maximum amount of an entity's loss carry-back tax offset for a year is limited by the surplus balance of its franking account at the end of the year so that the offset cannot exceed the value of past taxes paid that have not yet been distributed to shareholders as franking credits.

6.44 A company may have a surplus in its franking account because it has paid tax, or received franked dividends, and has retained its profits.

6.45 Limiting the loss carry-back tax offset to the amount in the franking account at the end of the current year avoids a double benefit arising from the past payment of tax. This double benefit could otherwise

arise because shareholders could receive an imputation credit in relation to company tax that, because of loss carry-back, had effectively no longer been paid.

6.46 Another reason that loss carry-back is limited by the surplus balance of the franking account is to minimise the possibility of an entity's franking account going into deficit (which would create a liability to franking deficits tax) when it gets a refund as a result of the offset. This reduces administrative churn in the tax system from companies that receive a refund from their loss carry-back offset having to return some or all of it as franking deficits tax.

6.47 Since the debit from getting a refund of tax will occur after the end of the relevant year, the balance in the entity's franking account may have changed, so the debit could still put the account into deficit. If that deficit is not made up by the end of the year, the entity would be liable for franking deficits tax to make good the excess of its franking debits over its franking credits.

6.48 The franking account balance limit does not apply to a foreign resident entity with a permanent establishment in Australia. This ensures that loss carry-back does not discriminate against foreign residents that are not within the Australian imputation system and so will usually not have a franking account balance to support the offset. ***[Schedule 5, item 2, subsection 160-15(4)]***

6.49 However, the franking account balance does limit the loss carry-back tax offsets of New Zealand franking companies. These are companies resident in New Zealand that have chosen to be within the Australian imputation system.

6.50 Payments of Australian income tax by a New Zealand franking company does result in a credit arising in the company's franking account. Accordingly, the franking account limit applies to those companies to prevent them from obtaining an effective refund of tax that they have already passed on as a credit to their shareholders by paying a franked dividend. ***[Schedule 5, item 2, subsection 160-15(4)]***

6.51 Any debit to the franking account of a foreign resident entity (other than an New Zealand franking company) for a refund of tax arising from a loss carry-back tax offset can only reduce the account balance to nil; it cannot put it into deficit. ***[Schedule 6, item 59, table item 2A in subsection 205-30(1)]***

There must be a tax liability in the middle or earliest year

6.52 A corporate tax entity can only get a loss carry-back tax offset if it has an income tax liability for the year it carries a loss back to. That is, the company must have been assessed as owing an amount of income tax for either the middle or earliest year. ***[Schedule 5, item 2, paragraph 160-10(c) and step 4 in subsection 160-15(2)]***

6.53 If a tax loss is carried back two years, the tax value of the amount carried back to each year is limited by the available tax liability of that year. A tax liability of one of the years cannot be used to support carrying back an amount to the other year. ***[Schedule 5, item 2, step 4 in subsection 160-15(2)]***

6.54 The 'income tax liability' is not the amount of *unpaid* tax for that year. Payments of tax (whether by pay-as-you-go (PAYG) instalments or otherwise) do not affect the tax liability used to work out the offset. Rather, the income tax liability is the amount of income tax assessed to the entity for the year the loss is carried back to. ***[Schedule 5, item 3, definition of 'income tax liability' in subsection 995-1(1)]***

6.55 The Commissioner's usual practice is to apply any refund amount arising from an offset towards paying another amount the entity owes to the Commissioner before an actual refund would be paid.

6.56 Each part of a tax liability can only be used once to support a loss carry-back. This ensures that the tax value of the loss carried-back utilises the corresponding amount of the tax liability of the year it is carried-back to. ***[Schedule 5, item 2, subsection 160-15(3)]***

Example 6.9: Difference between basic and final tax liability

Neversink Corp has the following outcomes:

Income year	*Taxable income/(loss)*	*Basic tax liability*	*Offsets*	*Final tax liability*
2014-15	$1 million	$300,000	$120,000	$180,000
2015-16	($1 million)	0	0	0

In the 2015-16 income year, Neversink can carry-back some of its loss against its 2014-15 tax liability. Even though Neversink's $300,000 basic tax liability for 2014-15 was the same as the tax value of the maximum $1 million it can carry-back, its final liability was reduced to $180,000 because it had available a $120,000 tax offset in that year for some R&D expenditure.

Therefore, Neversink only carries back $600,000 of its 2015-16 loss because the tax value of that loss ($600,000 x 30 per cent corporate tax rate = $180,000) matches the liability available. The remaining

$400,000 of Neversink's loss can be deducted against taxable income of later income years.

Example 6.10: Using up a tax liability — single year shock

Proudnose Pty Ltd has the following outcomes:

Income year	***Taxable income/(loss)***	***Tax liability***
2014-15	$600,000	$180,000
2015-16	($1 million)	0
2016-17	$3 million	$900,000

In the 2015-16 income year, Proudnose can carry-back some of its loss against its 2014-15 tax liability. It would not carry-back the maximum $1 million because the tax value of that amount ($300,000) is more than the 2014-15 tax liability. Instead, Proudnose might choose to carry-back $600,000, using the whole 2014-15 tax liability ($600,000 x 30 per cent = $180,000).

In the 2016-17 income year, the remaining $400,000 of the 2015-16 loss can be used as a deduction against the taxable income of that income year. It cannot be carried-back to 2014-15 because there is no unutilised tax liability left in that income year.

Example 6.11: Using up a tax liability — two year shock

Cavendish Pty Ltd has the following outcomes:

Income year	***Taxable income/(loss)***	***Tax liability***
2014-15	$5 million	$1.5 million
2015-16	($1.5 million)	0
2016-17	($2 million)	0

In the 2015-16 income year, Cavendish can carry-back up to $1 million of its loss for that year against its 2014-15 tax liability. It decides to do so, producing a loss carry-back tax offset of $300,000 ($1 million x 30 per cent corporate tax rate) and using up $300,000 of its 2014-15 tax liability. Since it has no tax liability for 2015-16, the $300,000 is refunded to it.

In the 2016-17 income year, Cavendish can carry-back the remaining $500,000 from 2015-16 or $1 million of its 2016-17 loss, or some of each (to a total of $1 million), against the remaining 2014-15 tax liability. It chooses to carry-back $500,000 from 2015-16 and another $500,000 from 2016-17. This again produces a $300,000 offset that is refunded to it.

The loss from 2015-16 is fully used up and there is still $1.5 million left of the 2016-17 loss that can be used as a deduction for later income years. The loss can no longer be used as a carry-back loss because there is no year left that it can be carried back to (2014-15 being more than two years back from 2017-18).

Effect of net exempt income

Net exempt income in the current year

6.57 In working out a year's tax loss, the raw loss is reduced by any amount of net exempt income in the year (see subsection 36-10(3)). 'Net exempt income' is a taxpayer's exempt income, less the amounts that would become deductible if the exempt income had been assessable income (see section 36-20). Loss carry-back does not alter this calculation.

6.58 If an entity has net exempt income in the current year and an unutilised loss from an earlier year, it must apply that unutilised loss against the current year's net exempt income (see subsection 36-17(7)). This reduces the unutilised amount of the loss. Loss carry-back does not alter this operation. However, it does mean that a tax loss from the middle year that might otherwise be available for loss carry-back might first have to be reduced by any net exempt income in the current year.

Example 6.12: Net exempt income in the current year

Bukowski Inc. has the following outcomes:

Income year	***Unused taxable income/(loss)***	***Net exempt income***	***Unused tax liability***
2014-15	$1 million	0	$300,000
2015-16	($1 million)	0	0
2016-17	$2 million	$40,000	$600,000

In the 2016-17 income year, Bukowski can carry-back some of its $1 million 2015-16 tax loss against its 2014-15 tax liability.

However, before it does so, Bukowski must first apply that loss against 2016-17's net exempt income. That reduces the loss by $40,000 to $960,000.

If Bukowski carries that amount back, it would produce a $288,000 tax offset in 2016-17 ($960,000 x 30 per cent = $288,000). The tax offset would reduce its 2016-17 tax liability to $312,000.

Example 6.13: Net exempt income in the current year with prior year losses from outside the carry-back period

Rimbaud Pty Ltd has the following outcomes:

Income year	*Taxable income/(loss)*	*Net exempt income*	*Tax liability*
2013-14	($50,000)	0	0
2014-15	$5 million	0	$1.5 million
2015-16	($1 million)	0	0
2016-17	$2 million	$100,000	$600,000

Rimbaud has a $50,000 tax loss in the 2013-14 income year, which it chooses not to utilise in 2014-15 to preserve its franking credits.

In the 2016-17 income year, Rimbaud wants to claim a loss carry-back offset using its 2015-16 tax loss. Rimbaud must first use its $50,000 2013-14 tax loss against its net exempt income in 2016-17. Then it must utilise $50,000 of its 2015-16 tax loss against the remaining 2016-17 net exempt income before it is able to carry-back the unutilised $950,000 of its 2015-16 tax loss to 2014-15. That will produce a tax offset of $285,000, reducing Rimbaud's 2016-17 tax liability to $315,000.

Net exempt income in the middle and earliest years

6.59 If an entity chooses to carry a loss back to a year in which it had net exempt income, the amount carried back is reduced by the net exempt income of that earlier year before being converted into an offset. ***[Schedule 5, item 2, step 2 in subsection 160-15(2)]***

Example 6.14: Net exempt income in a prior year

Dupont & Dupond Pty Ltd has the following outcomes:

Income year	*Taxable income/(loss)*	*Net exempt income*	*Tax liability*
2014-15	$5 million	$100,000	$1.5 million
2015-16	($3 million)	0	0
2016-17	$500,000	0	0

Dupont & Dupond's 2015-16 tax loss can be carried back to offset its tax liability for the 2014-15 income year. It can carry-back the maximum $1 million in this case because there is a large enough tax liability in 2014-15.

If Dupont & Dupond wants to obtain the maximum loss carry-back refundable tax offset, it will have to carry-back $1.1 million of tax

losses to 2014-15 ($100,000 to absorb the net exempt income, and the other $1 million to achieve the maximum $300,000 refundable tax offset).

In the 2016-17 income year, Dupont & Dupond could choose to carry-back another $1 million from 2015-16 because its unused tax liability in 2014-15 is $1.2 million ($1.5 million – $300,000). Therefore it could again get the full $300,000 offset because the net exempt income was utilised the previous year, so will no longer reduce the offset.

Dupont & Dupond also has $900,000 of its 2015-16 loss ($3 million – $1.1 million – $1 million) that can be *deducted* against taxable income, including for 2016-17. Because 2016-17 only has taxable income of $500,000, Dupont & Dupond can deduct $500,000 for the loss, reducing its tax liability to nil and leaving $400,000 to be deducted in future years.

6.60 If there is net exempt income in the middle year or the earliest year but not both, an entity may choose to carry a current year loss back to only the year without net exempt income. If it does so, the loss is not reduced by the other year's net exempt income.

The relationship between loss carry-forward and loss carry-back

6.61 Corporate tax entities must deduct losses from prior years in the order in which they arose (see subsection 36-17(7)). No similar ordering rules apply to using losses for the loss carry-back tax offset. That is, there is no requirement that an eligible loss must be carried back to the earliest year first, or that the earliest loss must be carried back first.

6.62 However, prior year tax losses are deducted *before* the loss carry-back refundable tax offset can be worked out because the deduction occurs as part of working out an entity's taxable income for the current year (see section 4-10). The loss carry-back tax offset is then applied after the corporate tax entity has calculated its basic income tax liability on that taxable income for the current year (see subsection 4-10(3)).

Utilising tax attributes

6.63 Each part of an entity's tax losses, its net capital losses, and its net exempt income, can only be used once in working out an amount for an entity under the income tax law (including an amount of the entity's loss carry-back tax offset). This has been a long standing principle in the income tax law but this measure makes it explicit. ***[Schedule 6, item 34, subsection 960-20(1)]***

Tax losses can only be utilised once

6.64 If some part of a tax loss is carried-back to an income year, that part of the loss (not just the amount remaining after reduction by net exempt income) cannot be carried-back again to that or any other income year. Nor can it be used as a deduction under Division 36. Similarly, if some part of a loss is used as a deduction under Division 36, that part of the loss cannot be carried-back to produce a loss carry-back tax offset. ***[Schedule 6, item 34, subsections 960-20(1) and (2)]***

Example 6.15: Loss utilisation

Bostle Co Pty Ltd has the following outcomes:

Income year	*Taxable income/(loss)*	*Tax liability*
2013-14	($1 million)	0
2014-15	$5 million	$1.5 million
2015-16	($3 million)	0
2016-17	$2 million	$0

In the 2015-16 income year, Bostle Co could choose to carry-back $1 million of its loss against its 2014-15 tax liability. It chooses to do so, producing a loss carry-back tax offset of $300,000 ($1 million × the 30 per cent corporate tax rate). Since it has no tax liability for 2015-16, that amount would be refunded to it.

In the 2016-17 income year:

- $1 million of the remaining $2 million of the 2015-16 loss could again be carried back; or

- the whole $2 million could be deducted in 2016-17 (or a later year).

Bostle Co chooses to carry-back $1 million to 2014-15, generating a $300,000 tax offset for 2016-17, and deducts $2 million of its prior year losses in that year.

Because of the ordering rule in subsection 36-17(7), Bostle Co has to deduct the carry-forward loss from 2013-14 first, leaving the last $1 million from 2015-16 to be deducted as well. It has reduced its 2016-17 taxable income to nil, so its tax liability is also nil, allowing its offset to be refunded.

If instead Bostle Co chose in 2016-17 not to carry anything back to 2014-15, it would not have got a refund but it would still have $1 million of its loss left from 2015-16 that could be deducted in future years. By 2017-18, it would be too late to use it as a carry-back loss.

6.65 An entity ***utilises*** a tax loss to the extent that it deducts the tax loss against an amount of assessable or net exempt income, carries it back to produce a loss carry-back tax offset, or reduces it by applying a total net forgiven amount under the commercial debt forgiveness provisions in Division 245. ***[Schedule 6, item 34, subsection 960-20(2)]***

Net exempt income and net capital losses can only be utilised once

6.66 An entity ***utilises*** net exempt income when it:

- is taken into account in calculating a tax loss;
- reduces the amount of a tax loss that can be deducted;
- reduces a loss carried back to a year; or
- reduces an amount under subsection 26-47(8) (about losses from boating activities), subsection 35-15(2) (about losses from non-commercial business activities) or subsection 65-35(3) (about tax offsets carried forward from earlier years).

[Schedule 6, item 34, subsection 960-20(4)]

6.67 An entity ***utilises*** a net capital loss when it applies it to reduce an amount of its capital gains or reduces it by applying a total net forgiven amount under the commercial debt forgiveness provisions. ***[Schedule 6, item 34, subsection 960-20(3)]***

Example 6.16: Utilising losses and net exempt income

Polymorph Industrial Designs Pty Ltd has the following outcomes:

Income year	*Taxable income/(loss)*	*Net exempt income*	*Tax liability*
2014-15	$1.5 million	$100,000	$450,000
2015-16	($3 million)	0	0
2016-17	$500,000	$50,000	0
2017-18	$2 million	$50,000	$210,000

In the 2015-16 income year, Polymorph chooses to carry back $1.1 million of its loss to 2014-15. The amount is reduced by the $100,000 net exempt income of that year, leaving $1 million to produce a $300,000 loss carry-back tax offset. $1.9 million of the 2015-16 loss remains unutilised. The net exempt income of 2014-15 is fully utilised, along with $300,000 of that year’s income tax liability.

In the 2016-17 income year, Polymorph has to utilise at least $50,000 of its remaining 2015-16 tax loss because of the 2016-17 net exempt income. It can then carry back some of that loss to 2014-15 to produce a loss carry-back tax offset. It chooses to carry back $500,000. It cannot carry back any more because the rest of the 2014-15 tax liability was utilised in the previous income year. The amount it carries back is not reduced by 2014-15's net exempt income because it was fully utilised in working out the previous income year's offset.

In the 2017-18 income year, Polymorph has to use up $50,000 of it unutilised 2015-16 loss because it has that much 2017-18 net exempt income. After taking into account that amount and the $550,000 utilised in 2016-17, it has $1.3 million of its 2015-16 tax loss that is unutilised and can be deducted against its 2017-18 taxable income.

Consolidated groups

6.68 Loss carry-back is available to the head company of a consolidated group or multiple entry consolidated group (MEC group), just like any other corporate tax entity.

6.69 Consolidated groups and MEC groups cannot access loss carry-back in relation to losses transferred to the group by a joining entity. To allow them do so would add considerable complexity to the loss carry-back measure and would be inconsistent with the overall principles of the tax consolidation regime. ***[Schedule 5, item 2, paragraph 160-30(a)]***

6.70 Similarly, when an entity with prior year tax liabilities joins a consolidated group or MEC group, the group cannot carry back any tax loss against tax liabilities previously assessed to the joining entity. An entity can only carry its losses back against its own tax liabilities.

6.71 Under the existing consolidation rules, the franking account balance of a joining entity accrues to the head company immediately upon joining. No special restrictions apply to the group using those franking credits for loss carry-back purposes. The group should however be aware of the anti-avoidance rules relating to a consolidated group obtaining an imputation benefit under section 177EB of the *Income Tax Assessment Act 1936* (ITAA 1936).

Transferred losses for non-consolidated groups

6.72 Loss carry-back is not available for losses transferred to an entity under Division 170. That Division allows losses to be transferred between entities in a corporate group where an Australian branch of a foreign bank is involved, so that it can compete on equal terms with consolidated groups.

6.73 The restriction on the use of these transferred losses for loss carry-back purposes ensures that loss carry-back has a consistent application to consolidated groups and to non-consolidated groups that have an Australian branch of a foreign bank, or a non-bank foreign financial entity. ***[Schedule 5, item 2, paragraph 160-30(a)]***

Loss carry-back integrity rule

6.74 When deducting losses of earlier income tax years, corporate tax entities are subject to integrity rules (known as the continuity of ownership test and the same business test). Applying the same integrity rules to entities that wish to carry their losses back to obtain a tax offset would have minimal impact on the entities where the existing owners continue to trade and wish to undertake planned and sensible risks.

6.75 However, potential new owners who wish to acquire an existing entity and introduce new technology, business practices and product lines that will better position it to meet the commercial challenges of the future may find that they do not satisfy the continuity of ownership and same business tests in some circumstances.

6.76 The specific integrity rule for loss carry-back denies a corporate tax entity a loss carry-back tax offset it would otherwise be entitled to where there has been a change in the control of the entity arising from a disposition of membership interests and, considering all of the relevant circumstances, one or more parties entered into a scheme to obtain the tax offset.

6.77 Losses that cannot be carried back as a result of the integrity measure can still be carried forward and claimed as a deduction against the income of future years provided the requirements for doing so are met.

What happens when the integrity rule is applied

6.78 When the integrity rule for loss carry back applies, the corporate tax entity cannot carry back a tax loss. Subject to meeting the ordinary requirements, the entity would still be able to deduct those losses in a future year.

6.79 There is no direct impact on an entity that disposed of a membership interest when the corporate tax entity is denied the tax offset.

6.80 There is also no direct impact on an entity that acquires the membership interest when the corporate tax entity is denied the tax offset.

When does the integrity rule apply

There must be a scheme

6.81 There must have been a scheme for the disposition of membership interests, or of an interest in membership interests, in

- the corporate tax entity; or
- an entity that had a direct or indirect interest in the corporate tax entity.

6.82 'Scheme' is a widely defined term used in other taxation provisions, including Part IVA of the ITAA 1936. Where there has been no disposition of membership interests, the loss carry-back integrity rule does not apply. ***[Schedule 5, item 2, paragraph 160-35(1)(a)]***

6.83 For these purposes:

- a non-share equity interest in a corporate tax entity is treated in the same way as a membership interest in a corporate tax entity; and
- an equity holder in a corporate tax entity is treated in the same manner as a member in a corporate tax entity.

This ensures that equity interests in corporate tax entities that are not shares are treated in the same manner as shares. ***[Schedule 5, item 2, subsection 160-35(3)]***

6.84 Where there has been a scheme that does not involve a disposition of membership interests, the Commissioner is able to consider the potential application of other integrity rules in the taxation law (such as Part IVA of the ITAA 1936).

6.85 The terms 'interest in membership interest' and 'scheme for a disposition' have the same meanings as in section 177EA of ITAA 1936. ***[Schedule 5, items 4 and 5, definitions of 'interest in membership interests' and 'scheme for a disposition' in subsection 995-1(1)]***

6.86 An 'interest in a membership interest' includes legal and equitable interests in a membership interest. Specific rules apply when the interest is held through a partnership or trust.

6.87 The term 'scheme for a disposition' includes dispositions that include issuing or creating membership interests, entering into contracts, arrangements, etc. that affect the legal or equitable interest in

membership interests and other means by which control or ownership of a membership interest can be changed.

6.88 The scheme must have been entered into or carried out between the start of the year the entity seeks to carry the loss back to and the end of the year it claims the loss carry-back tax offset. ***[Schedule 5, item 2, paragraph 160-35(1)(b)]***

The disposition must have resulted in a change in control

6.89 The disposition of membership interests must have resulted in a change in who controlled, or was able to control, (whether directly or indirectly through one or more interposed entities) the voting power in the corporate tax entity. ***[Schedule 5, item 2, paragraph 160-35(1)(c)]***

6.90 When determining whether control of the entity has changed, dispositions of membership interests and interests in membership interests can be considered. The magnitude of the disposition of membership interests is not decisive.

The entity would be entitled to a loss carry-back tax offset

6.91 The loss carry-back integrity rule will apply only where, in the absence of the integrity rule:

- an entity (other than the corporate tax entity) received or receives, in connection with the scheme, a financial benefit; and
- that financial benefit was calculated by reference to one or more loss carry back tax offsets to which it was reasonable, at the time the scheme was entered into or carried out, to expect the corporate tax entity would be entitled.

[Schedule 5, item 2 paragraph 160-35(1)(d)]

6.92 Therefore, the loss carry-back integrity rule will not apply if:

- the corporate tax entity does not have an income tax liability for a year that a loss can be carried back to, or
- the corporate tax entity does not have, or expect to have, a franking credit balance.

6.93 The company is not required to consider the application of the loss carry-back integrity rule if it does not wish to carry back an eligible loss.

Purpose and relevant circumstances

6.94 The loss carry-back integrity rule will apply only if, having regard to the relevant circumstances of the scheme, it would be concluded that one or more of the persons who entered into or carried out the scheme or any part of the scheme did so for a purpose (whether or not a dominant purpose but not including an incidental purpose) of the corporate tax entity obtaining a loss carry-back tax offset. ***[Schedule 5, item 2, paragraph 160-35(1)(e)]***

6.95 To determine this purpose requires an examination of the facts and reasonable expectations of the persons at the time that the scheme was entered into. Subsequent events are not relevant except to the extent that they clarify what the true purpose of the parties was.

6.96 If at the time of entering into the scheme the expectation was that the corporate entity would not meet the requirements for getting a loss carry-back tax offset because, for example, the entity was expected to be profitable, the purpose of the entity getting the loss carry-back tax offset would not have existed. A subsequent unexpected loss would not change this.

6.97 However, an expectation that the corporate tax entity would be entitled to get the loss carry-back tax offset will not always require that the offset be denied. Consideration must be given to the purpose of the persons who entered into or carried out the scheme. This is an objective question of fact that is established by looking at all the relevant circumstances.

What are the relevant circumstances?

6.98 To objectively establish what the purpose of the persons who entered into the scheme was, the relevant circumstances surrounding the scheme of disposition must be considered. None of these circumstances is decisive by itself. The circumstances should be considered collectively to determine whether the tax offset is denied.

6.99 The first relevant circumstance is the extent to which the corporate tax entity continues the same activities undertaken after the scheme for the disposition of membership interests has been implemented as prior to implementation. ***[Schedule 5, item 2, paragraph 160-35(2)(a)]***

6.100 Activities in this sense are referring to what the entity did to earn assessable income. The entity will be undertaking the same activities notwithstanding that it has expanded or varied its product lines. For example:

- a restaurant that specialised in Chinese cuisine which under new ownership and control specialised in Greek cuisine would still be undertaking the business activity of being a restaurant; and
- an entity that manufactured cosmetics that changed ownership and control would not be undertaking the same activity if it retooled to manufacture motor vehicle parts; and
- a shop that switched from selling clothing to selling compact discs would not be undertaking the same activity.

6.101 Both the number of activities and their relative importance to the entity need to be considered. An activity may have been undertaken to such an extent and been of such importance to the entity that its continuation after the change in control was clearly the dominant purpose behind the change in control of the company. Conversely, the ending of that activity may indicate that continuing the activities of the entity was a very minor purpose of acquiring control and the entity obtaining a loss carry-back tax offset was much more than an incidental purpose.

6.102 It is a matter of judgement as to whether the extent to which the same activities have been continued indicates whether the purpose of obtaining the loss carry-back tax offset was incidental or of greater importance.

6.103 The second relevant circumstance is the extent to which the corporate tax entity continues to use the same assets. ***[Schedule 5, item 2, paragraph 160-35(2)(b)]***

6.104 If the entity is acquired as a means to obtain control over assets of the entity, this may indicate that the purpose of the new owner was gaining control over the assets rather than the tax offset. This is more likely to be the case where the assets have unique characteristics that cannot be obtained other than through purchase of membership interests in the company. The assets do not need to be used for the same or a similar purpose as they were used by the former owners.

6.105 The extent to which the new controllers of the entity use the pre-existing assets does not preclude the replacement of those assets as part of the ordinary running of a business.

6.106 The third relevant circumstance is the matters referred in subparagraphs 177D(b)(i) to (viii) of the ITAA 1936. ***[Schedule 5, item 2, paragraph 160-35(2)(c)]***

6.107 These matters are:

- the manner in which the scheme was entered into or carried out;
- the form and substance of the scheme;
- the time at which the scheme was entered into and the length of the period during which the scheme was carried out;
- the result in relation to the operation of the income tax law that, but for the integrity rule, would be achieved by the scheme;
- any change in the financial position of the relevant taxpayer that has resulted, will result, or may reasonably be expected to result, from the scheme;
- any change in the financial position of any person who has, or has had, any connection (whether of a business, family or other nature) with the relevant taxpayer, being a change that has resulted, will result or may reasonably be expected to result, from the scheme;
- any other consequence for the relevant taxpayer, or for any person, of the scheme having been entered into or carried out; and
- the nature of any connection (whether of a business, family or other nature) between the relevant taxpayer and any person.

6.108 Whether a change in the membership interests in a company was done with the purpose of gaining access to a tax offset is a matter that can only be determined on its facts. Nonetheless, the more complex or artificial the arrangements that surround the change in membership interests, the more likely it is that the tax offset will not be allowed because the form and substance of the scheme and the manner in which it was entered into indicate a purpose of getting the tax offset rather than a normal commercial purpose.

6.109 Ordinarily, it would not be expected that a change of control that arises from generational change within family owned corporate tax entities would indicate that there was a purpose of obtaining a tax benefit. Considering the financial and other consequences for the vendors and purchasers and the nature of the connection between them, the handing over of the membership interests and control of the company as the older

generation retires is more likely to reflect family dynamics rather than any purpose of obtaining a tax offset. This would remain the situation notwithstanding that the younger generation may wish to introduce changes to the company's business that initially could be expected to lead to losses that could be carried back.

6.110 Similarly, the transfer of membership interests that arise from a marital breakdown is unlikely to have anything more than an incidental purpose of obtaining a tax offset. Nor is a transfer of membership interests arising from the breakdown of personal and business relationships between shareholders likely to involve anything more than an incidental purpose of obtaining a tax offset. Corporate tax entities in these situations may experience losses due to the disruption of working relationships and lack of focus on the operation of the business. In the absence of any other aggravating factors, losses could be carried back and the tax offset would be allowed.

How the integrity rule will be administered

6.111 Corporate tax entities will self-assess whether the integrity rule applies to their circumstances. In most instances, it will be clear that the integrity rule does not apply to their circumstances and they will then be able to prepare their tax return and claim the refundable tax offset from the Commissioner.

6.112 Entities that may have doubts are able to seek the advice of the Commissioner. Should the Commissioner publish a public ruling or provide a private ruling, the entities will be able to rely on it.

Examples

6.113 The following examples illustrate how the integrity rule applies.

Example 6.17: Entity conducting similar business

Visanna Flowers Pty Ltd is a profitable company. However, its profits are in long term decline. Its business activities are growing of flowers for sale of flowers from a shop. As required, flowers will be purchased from suppliers for sale from the shop.

All of the shares that provide control of the company are purchased by Andrew and Melinda for $2 million. At that time, Visanna Flowers has a franking account balance of $250,000. Recent sales of nearby properties that had been used for agricultural but not floral purposes suggest that a fair market value of the flower farm and shop would be $1.85 million. The properties available do not have the arterial road access that Visanna Flowers has and would need to have new flower beds planted.

In accordance with their business plan, Andrew and Melinda refurbish the shop and add a café. They also expand the products sold from the shop to include the work of local artists. Andrew and Melinda expect that Visanna Flowers will incur a loss of $800,000 in the first year of operation but become profitable afterwards. The expected availability of the loss carry-back tax offset is included in the cash flow projections provided to their banker.

On the evidence available, Andrew and Melinda's purpose is to implement changes that they expect will lead to Visanna Flowers being a more profitable business than it currently is. While Visanna Flowers is undertaking new business activities, it has also continued its initial business activities of growing and buying flowers for sale. The company has retained most of its pre-existing assets albeit that some have been refurbished.

While the cash flow benefit of the carry back of losses has been taken into account, in this particular instance, other factors such as the existing flower beds and arterial road access lead to the view that the carry-back of the loss was an incidental purpose of acquiring of Visanna Flowers Pty Ltd.

Example 6.18: Entity using existing assets in new business

Sergio's Barbershop Pty Ltd is a company that owns a business premise valued at $1 million, which is well located for passing traffic. The company has a franking account balance of $300,000. Business premises are tightly held in that location and rarely come to the market. Sergio wishes to retire and insists that the company must be sold with the premises as opposed to him selling the premises separately and liquidating the company. He also requires a price that reflects the value of the franking credits.

Kate has sought to purchase the few properties that have to come to market in the last year but been unable to match the prices offered by competing purchasers. Kate pays $1.15 million to Sergio for 100 per cent ownership and control of the company. Kate paid this price because Sergio had an offer of $1.1 million from a competing purchaser.

The company is renamed Kate's Fashion Pty Ltd and commences to trade. Kate expects the company to trade at a small loss of approximately $20,000 in the first year of operation as she builds up a new clientele.

The company under Kate's control is conducting a very different business to that when controlled by Sergio. The price paid for the company at least in part was calculated by Sergio's determination to obtain a financial benefit by reference to the franking credits. However, Kate has acquired a company where her primary objective

was to gain control over business premises that she could not otherwise obtain and was at risk of losing to a competing purchaser.

The relatively small loss that she expected the company to have in its first year of trading suggests that the potential loss carry-back tax offset was not a significant purpose in her planning.

While there are some circumstances that suggest that the tax offset should be denied, there are also circumstances that suggest it should be allowed. In this particular situation, balancing these circumstances, the tax offset would be allowed.

Example 6.19: Entity acquiring assets that are generic in nature

Ian's Consulting Pty Ltd has a five-year lease over premises in a country town with an option to renew the lease for a further five years. There are many similar premises located within 500 metres that are available on similar terms. The company has been returning profits in excess of $500,000 in recent years and has a franking account balance of $400,000. Other than the lease and office equipment, the company has no significant assets.

Jackie acquires all of the shares in the company for $150,000. Ian establishes a new company called Ian's Consulting Services Pty Ltd and trades from one of the available premises located across the road. As the office equipment is of limited value to Jackie, she permits Ian to buy what he wishes and take it with him.

Jackie renames the company Jackie's Promotions Pty Ltd and refurbishes the business premises to meet her needs. As expected from the business plan, Jackie's Promotions makes a loss of $800,000 in its first year of operation. Jackie insists that her primary purpose in purchasing the membership interest in what is now her company was to obtain a valuable long term lease.

Jackie is conducting a very different business to that of Ian. While the company under her control has continued to use the same leased premises, comparable alternative premises were readily available. Jackie's claim that she wanted a valuable long term lease is not convincing. The payment of $150,000 by Jackie is providing a financial benefit to Ian. Jackie will also receive a financial benefit in that the company now under her control can expect to receive a loss carry-back tax offset of $240,000 (30 per cent of $800,000) in its first year of operation and possibly a further loss carry-back tax offset should the second year's trading give rise to a loss.

Accordingly, the loss carry-back tax offset would be denied.

Example 6.20: Entity sells assets back to former owners

Kelly Transport Pty Ltd owns vehicles, plant and equipment valued at $10.5 million. The company has a franking account balance of $600,000. Members of the King family acquire 100 per cent of the membership interest in Kelly Transport for $10.8 million and rename the company King Plumbing Pty Ltd.

Within a matter of days, King Plumbing sells for $10.5 million all of the vehicles, plant and equipment to Kelly Transport Service Pty Ltd, a company wholly owned by the former shareholders of Kelly Transport.

King Plumbing then commences a new business that in its first year of operation is expected to incur a loss of $1.5 million and $1 million in its second year, before it becomes profitable.

The King family is conducting a very different business to that of the former owners of what is now King Plumbing. While very valuable assets were acquired with the company, the quick sale of those assets demonstrates that there was never any intention to use them in an income earning activity. The very substantial recoupment of the purchase price for the company by selling its assets has effectively led to a situation where the net cost to the King family was $300,000.

As the King family expects the company to have trading losses of $2.5 million, they can reasonably expect to be able to carry back losses so that King Plumbing will obtain tax offsets of $300,000 in both of the first two years of operation under their control.

It is probable that the availability of the tax offset over two years was a significant purpose of the transfer of membership interests. Both tax offsets would be denied.

Example 6.21: No expectation of loss

Thomson Pty Ltd has been a profitable company for many years and has a franking credit balance of $300,000. The market value of the underlying assets of the company is $2.8 million. The company's owner wishes to retire and the shares are acquired by two long standing employees for $2.9 million.

Following the change of ownership in the company, minimal changes are made to its operations or assets. The new owners based on their intimate knowledge of the company were confident that it would continue to be profitable. Some months after acquisition, due to a fire, the company loses a substantial amount of stock leading to a loss for the year.

Under its new owners, Thompson made minimal changes to its business and retained most of its business assets. The price for the membership interest could suggest that it was calculated with reference

to a financial benefit from the franking credit balance. However, as the price paid is fairly close to market value, it could also represent the respective bargaining strengths of the parties. The new owners had a reasonable expectation that the company would continue to be profitable.

As the fire could not be predicted and there was no expectation that the tax offset would be claimed, there would be no basis to deny the tax offset.

Example 6.22: Complex or artificial arrangement

Williamson Brothers Pty Ltd provides a wide range of technological services to local governments and small to medium sized business. As the successful tenderer for a major technological upgrade by a local government, Williamson Brothers has entered into eight inter-related contracts, of which seven are expected to be profitable and one will be unprofitable.

Williamson Brothers acquires 95 per cent of the shares of Dormant Pty Ltd and individuals associated with Williamson Brothers acquire the remaining 5 per cent for a total payment of $50,000. Dormant's assets are $100 cash in the bank and a franking account credit balance of $300,000. Dormant had paid a substantial amount of tax in the two years prior to its acquisition by the Williamson Group. Dormant's previous business was connected with the provision of technological services.

The unprofitable contract is to be performed by Dormant. The seven profitable contracts are to be performed by Williamson Brothers Pty Ltd. The long standing practice of Williamson Brothers Pty Ltd has been to undertake all the contracts and accept the losses on the unprofitable contracts as a necessary aspect of being able to obtain the profitable contracts.

Even though Dormant was continuing to undertake the same business activities as prior to the change in ownership, having regard to the price paid for Dormant and the company having no assets or contracts in progress until the unprofitable contract was allocated to it, the availability of the tax offset would be a significant factor in the decision to acquire the membership interest. Therefore, the tax offset is not available.

Example 6.23: Generational change in an entity

David and Son Tailors Pty Ltd is a company where two-thirds of the shares are owned by the trustee of David's family trust. The company has assets valued at $3 million a franking account balance of $420,000. David is ready to retire and sells all of his shares to the trustee of the family trust of his son Michael for $2.1 million, who then becomes the only owner of the company.

Michael becomes the managing director of the company and immediately changes the business focus of the company in a manner that David had previously resisted. This includes selling of most of the company's assets. Michael expects that the company will be unprofitable for one to two years as the changes that he considers necessary if the company is to be able to survive in the longer term are bedded down. Michael has factored in the availability of a loss carry-back tax offset in his business plans.

The business focus of the company has changed and very few of the assets have been kept. The price paid for two-thirds of the company not previously owned could suggest that a financial benefit was expected and calculated by reference to the loss carry-back tax offset. However, the generational change is a significant factor that suggests that the availability of the tax offset was at most an incidental purpose of Michael acquiring control of the company.

Example 6.24: Breakdown of marital and personal relationships

SPA Accountancy and Financial Planning Pty Ltd is one third owned by Sandra, Pep and Anthony. Sandra and Pep are a married couple and Anthony is a close friend of Pep. The company has a franking credit balance of $500,000.

Following a marriage breakdown and pursuant to a Family Court order, Pep transfers his one-third interest in the company to Sandra. Pep is permitted to take his clients with him to wherever he chooses to work in the future. Anthony is now very hostile to Sandra and is no longer willing to work with her. His one-third interest is cancelled and he is permitted to take his clients with him and is released from all obligations arising from his time with SPA.

Other than the goodwill associated with the client lists, much of which is lost when Pep and Anthony take their clients with them, the other valuable asset of the company is its business premises, which are subject to a substantial mortgage.

Sandra renames the company as Sandra's Financial Advice Pty Ltd and changes the focus of the company away from accountancy towards financial advice, her area of expertise. She also rents that part of the premises that were previously occupied by Anthony and Pep to unrelated tenants. Sandra expects that the business will initially be unprofitable as she rebuilds what is a smaller company with a different focus and services the interest expense related to the premises.

There have been significant changes in the nature of the business and other income earning activities of the company. However the two key causes for the change in control and ownership were marital breakdown and the personal hostility between Anthony and Sandra which led to the collapse of their business working relationship.

> Taking into account the hostile family and personal relationship, the available evidence does not indicate an intention to acquire shares so as to access franking credits via a carry back of losses. The company that is now Sandra's Financial Advice Pty Ltd would be permitted to claim the tax offset.

Other administrative rules

A corporate tax entity must have lodged returns over the past five years

6.114 A corporate tax entity must have lodged an income tax return for the current year and each of the five years immediately preceding it in order to claim loss carry-back. This covers the usual period for which the entity is required to retain its tax records under section 262A of the ITAA 1936 and the usual period in which the entity's assessments can be amended. It therefore provides a level of assurance that the entity's tax liabilities, tax losses and franking account entries for that period are likely to be accurate and able to be verified. ***[Schedule 5, item 2, subparagraph 160-10(d)(i)]***

6.115 In some cases, the entity might not have been required to lodge a return for a year (see section 161 of the ITAA 1936). Not lodging a return for such a year does *not* disentitle an entity to a loss carry-back tax offset. A common case where an entity is not required to lodge a return for a year would be where the entity did not exist in that year. ***[Schedule 5, item 2, subparagraph 160-10(d)(ii)]***

6.116 Corporate tax entities are subject to the full self-assessment regime under which an assessment is made automatically when they lodge their returns (section 166A of the ITAA 1936). However, it is still possible for the Commissioner to have assessed a corporate tax entity for an income year without it having lodged a return for that year (sections 167 and 168 of the ITAA 1936). In such cases, the Commissioner can rely on that assessment for the purposes of establishing the accuracy of the corporate tax entity's losses and liabilities, so not having lodged a return for that year also does *not* disentitle an entity to a loss carry-back tax offset. ***[Schedule 5, item 2, subparagraph 160-10(d)(iii)]***

Interest on overpayments and late payments

6.117 A loss carry-back tax offset forms part of the tax assessment of the current year. Loss carry-back alters neither the tax liability of the year to which a loss is 'carried back' nor the consequences of any failure to have paid that liability by the due date. It follows that claiming a loss carry-back tax offset by carrying a loss back to a particular year does not:

- give rise to a right to 'interest on overpayments' in relation to the tax liability assessed for that year; or

- reduce any general interest charge or shortfall interest charge arising from not paying the liability of that year.

Amended assessments

6.118 A refund arising from a loss carry-back tax offset is recoverable where a review of a corporate tax entity's tax affairs leads the Commissioner to conclude that the corporate tax entity was not entitled to it.

6.119 Where a corporate tax entity's assessment for the current or middle year is amended, then:

- if the amendment results in the corporate tax entity having a reduced loss or no loss (because it increases assessable income or reduces deductions) in the middle or current year, the amount of the loss carry-back tax offset that the corporate tax entity is entitled to for the current year may be reduced (potentially to nil); and/or

- if the amendment results in the corporate tax entity having an increased loss, the corporate tax entity may qualify for a loss carry-back tax offset (or an increased offset) for the current year.

6.120 Where a corporate tax entity's assessment for either the middle or earliest year is amended, then:

- if the amendment results in the corporate tax entity's tax liability being reduced, this could affect the loss carry-back amount for the current year and so may require the assessment for the current year to be amended to provide a lower loss carry-back tax offset; and/or

- if the amendment results in the corporate tax entity having a higher tax liability for that year, this could increase the maximum loss that can be carried back to that year and so may allow the current year's assessment to be amended to provide a higher loss carry-back tax offset.

6.121 Subject to the usual amendment periods, a corporate tax entity can seek an amendment of its assessment for the current year in order to claim a loss carry-back offset, or to increase the amount of its offset, if:

- it did not claim a loss carry-back offset for the current year when it could have done so once the amended assessment for the middle or earliest year is taken into account; or
- it claimed a smaller amount than it could have once that amended assessment is taken into account.

6.122 A corporate tax entity may also request an amendment where the amount of the loss it sought to carry back from one income year is reduced, but it could have chosen to carry a loss back from another year instead. The same can also be true if the unutilised income tax liability for a gain year is reduced by an amended assessment, but the loss could instead have been carried back to another gain year with a sufficient unutilised tax liability.

6.123 In all cases, the corporate tax entity's pool of carry-forward losses would be adjusted to reflect any increase or decrease in the amount of loss carry-back used in recalculating its loss carry-back tax offset.

Application and transitional provisions

Application

6.124 The loss carry-back measure applies to assessments for the 2012-13 income year and later income years. ***[Schedule 5, item 6, section 160-1 of the IT(TP)A 1997]***

Transitional arrangements for 2012-13

6.125 Tax losses can usually be carried back to either of the two years immediately before the year for which the tax offset is being claimed. However, they can never be carried back before the 2011-12 income year. Therefore, in the 2012-13 income year, tax losses can only be carried back for one year. ***[Schedule 5, item 6, section 160-5 of the IT(TP)A 1997]***

6.126 This transitional rule is consistent with the recommendation of the Business Tax Working Group's 2012 *Final Report on the Tax Treatment of Losses* that loss carry-back be phased in with an initial one year carry-back period.

Loss carry-back consequential amendments

Outline of chapter

7.0 This chapter explains consequential amendments to the income tax law that are necessary as a result of implementing the loss carry-back measure.

7.1 All legislative references in this chapter are to the *Income Tax Assessment Act 1997* (ITAA 1997) unless otherwise indicated.

Loss carry-back consequential amendments

Utilising tax losses and capital losses

7.2 The current law defines when tax losses and net capital losses are utilised. This definition is amended to cover other forms of utilising those things (including for loss carry-back purposes) and extends it to cover utilising net exempt income. The definition is also relocated. ***[Schedule 6, items 2, 30, 31 and 41, section 707-110, section 960-20 and the definition of 'utilise' in subsection 995-1(1)]***

7.3 As the measure introduces a general rule about utilising tax losses, net capital losses, and amounts of net exempt income, some existing rules that detail how things are utilised are repealed. Other provisions are amended to reflect the new definition. Some notes about the general utilising rule are added to help readers. ***[Schedule 6, items 1 to 29, 32, 33, and 42 to 48, section 45B of the ITAA 1936, sections 4-15, 26-47, 35-15, 36-1, 36-15, 36-17, 36-45, 65-10, 102-10, 102-15, 165-114, 165-115R, 170-20, 170-45, 170-115, 170-145, 707-100 and 707-115 of the ITAA 1997, section 707-30 of the Income Tax (Transitional Provisions)Act 1997 (IT(TP)A 1997), sections 45-330 and 45-480 of Schedule 1 to the Taxation Administration Act 1953]***

The general anti-avoidance rule

7.4 The amendments modify the income tax general anti-avoidance rule in Part IVA of the *Income Tax Assessment Act 1936* (ITAA 1936) so that it applies to schemes entered into with the purpose of obtaining a loss carry-back tax offset.

7.5 The general anti-avoidance rule works by identifying a scheme and a tax benefit that is produced for a taxpayer by the scheme. The Commissioner of Taxation (Commissioner) can cancel the tax benefit if it can be concluded (after examining eight listed factors) that someone entered into the scheme for the dominant purpose of providing the taxpayer with the tax benefit.

7.6 A 'tax benefit' is defined as being an amount not being included in the taxpayer's assessable income, a deduction or capital loss being incurred by the taxpayer, or a foreign income tax offset being allowable to the taxpayer. The amendments extend that definition to include a loss carry-back tax offset being available to the taxpayer. ***[Schedule 5, items 28 to 30, the definition of 'loss carry-back tax offset' in subsection 6(1), paragraphs 177C(1)(baa) and (ea) of the ITAA 1936]***

7.7 As with the existing tax benefits, the tax benefit from gaining a loss carry-back tax offset does not apply if the offset arises from making a choice expressly provided for by the income tax law unless the scheme was entered into for the purpose of enabling the choice to be made. ***[Schedule 5, items 31 to 34, subsections 177C(2) and (3) and of the ITAA 1936]***

7.8 If Part IVA is satisfied, the Commissioner can make a determination to cancel the tax benefit. The possible determinations, which separately cover each type of tax benefit, are extended to include determinations in relation to tax benefits from a loss carry-back tax offset. ***[Schedule 5, items 36 and 37, paragraphs 177F(1)(c) and (ca) of the ITAA 1936]***

7.9 When the Commissioner makes a determination to cancel a tax benefit, he or she can also make any compensating adjustments needed to put any taxpayers into the tax position they would have been in if the scheme had not been entered into. The amendments allow the Commissioner to make compensating adjustments to provide taxpayers with the loss carry-back tax offset that would have been available apart from the scheme. ***[Schedule 5, items 38, paragraph 177F(3)(ca) of the ITAA 1936]***

7.10 The Tax Laws Amendment (Integrity) Bill 2013 is contemporaneously amending the general anti-avoidance rule to address weaknesses revealed by some recent court cases. The amendments made by that Bill are extended to ensure that they also cover tax benefits by way of a loss carry-back tax offset being available to a taxpayer. That extension occurs only after those amendments commence. ***[Schedule 5, item 35, paragraph 177CB(1)(ca) of the ITAA 1936 and clause 2, table item 12]***

Pooled development funds

7.11 A company that makes a tax loss in an income year that it ends as a pooled development fund (a PDF) can only deduct that loss in a later income year in which it is a PDF for the whole year.

7.12 The amendments extend the same treatment to the loss carry-back tax offset. They prevent a corporate tax entity carrying back a tax loss that arose in a year it ended as a PDF, unless it was a PDF throughout both the current year and the year the loss was carried back to. ***[Schedule 6, items 52, 53 and 57, sections 36-25 and 192-37]***

7.13 As with the current law treatment of deductions for tax losses, there is no restriction on a PDF carrying back any tax loss that arose in a year it did not end as a PDF. Nor is there any restriction on carrying back a tax loss that arose in the part of a year before the company became a PDF. ***[Schedule 6, items 55 and 56, subsection 195-15(5)]***

Venture capital and similar limited partnerships

7.14 The current law prevents a limited partnership from deducting a tax loss in an income year in which it is a venture capital limited partnership, an early stage venture capital limited partnership, an Australian venture capital fund of funds, or a venture capital management partnership.

7.15 These entities cannot be corporate tax entities and so cannot claim the loss carry-back tax offset. However, if a limited partnership stops being one of these venture capital entities and becomes a corporate tax entity, it might claim the offset by carrying a loss back to a year in which it was one of those entities. That would provide the entity with an offset based on a year in which it was not a corporate tax entity and so would not have been able to deduct a tax loss. To preserve the symmetry with deducting tax losses, the amendments prevent a limited partnership carrying a tax loss back to a year in which it was a venture capital entity. ***[Schedule 6, items 54 and 58, sections 36-25 and 195-72]***

7.16 Each partner in a venture capital partnership usually gets his or her share of the partnership's loss (subsection 92(2) of the ITAA 1936). However, a limited partner can only deduct its share of partnership losses to the extent of its contributions to the partnership (subsection 92(2AA) of the ITAA 1936). The remaining part of a limited partner's share of partnership losses is its 'outstanding subsection 92(2AA) amount' (subsection 92A(2) of the ITAA 1936). That amount can be deducted under some circumstances but can never be used to produce a tax loss for the limited partner (subsections 92A(1) and (3) of the ITAA 1936).

7.17 As the outstanding subsection 92(2AA) amount of a limited partner in a venture capital partnership cannot be part of a tax loss for the partner, it cannot be used to produce a loss carry-back tax offset the limited partner might claim if it is itself a corporate tax entity. ***[Schedule 6, item 49, subsection 92A(3) of the ITAA 1936]***

Life insurance companies

7.18 For income tax purposes, life insurance companies carry on two broad categories of business: complying superannuation business and ordinary business. The earnings on complying superannuation business are taxed in broadly the same way, and at the same rate, as earnings made by complying superannuation funds. Earnings on the ordinary business are taxed at the corporate tax rate.

7.19 To ensure that the tax treatment of the complying superannuation business of life insurance companies continues to be the same way as that of complying superannuation funds, loss carry-back tax offsets are not available in respect of that complying superannuation business. They are available in respect of ordinary business. ***[Schedule 6, item 64, paragraph 320-149(2)(aa)]***

Foreign hybrids

7.20 Foreign hybrid limited partnerships are entities that are partnerships under foreign law but would normally be treated as companies for the purposes of Australia's income tax law. A special regime ensures that they are generally treated as ordinary partnerships for purposes of the income tax law (see Division 830).

7.21 Foreign hybrid limited partnerships are not eligible for loss carry-back tax offsets (which are only available to corporate tax entities). However, a partner in such a partnership would get a share of the partnership loss and could, if it were itself a corporate tax entity, seek to claim a loss carry-back tax offset. There are limits on the extent to which partners can claim a deduction for a tax loss flowing to them from a foreign hybrid limited partnership. To preserve symmetry with deducting tax losses, the amendments ensure that the same limits apply to the partner's use of that loss for loss carry-back. ***[Schedule 6, item 65, subsection 830-65(3)]***

Franking accounts

7.22 Generating a refund from a loss carry-back tax offset (or any other refundable tax offset) will result in the entity's franking account being debited by the amount of the refund (see subsection 205-30(1), table

item 2). The debit only applies to entities that are Australian residents because foreign residents are generally outside the Australian imputation system.

7.23 However, there are rare cases where a foreign resident entity does have an amount in its franking account. Therefore, a debit will arise in the franking account of foreign resident entities that get a refund. The debit is limited to the balance in the franking account. This ensures that the entity will not become liable for franking deficits tax as a result of obtaining the refund. Similar amendments extend the same treatment to foreign resident entities that are within the imputation regime for life insurance companies. ***[Schedule 6, items 59, 62 and 63, subsections 205-30(1), 219-30(1) and(2)]***

7.24 To avoid any doubt that an entity that gets a refund arising from a loss carry-back tax offset 'receives a refund of income tax' (and so attracts the debit to its franking account), the definition of that expression is amended to include income refunds arising from loss carry-back tax offsets. ***[Schedule 6, items 60 and 61, subparagraph 205-35(1)(b)(ii)]***

Working out PAYG instalments

7.25 A taxpayer's PAYG instalments are advance payments of income tax the taxpayer makes throughout a year. When that year's assessment is made, the instalments are credited towards payment of the year's tax liability.

7.26 The instalments are worked out by applying a rate to the gross amounts the taxpayer earns during the year. The rate used is usually that provided by the Commissioner, based on the tax payable on the taxable income for the previous year. In working out that taxable income, the Commissioner does not count one-off amounts (for example, capital gains) that are unlikely to be repeated. One such amount is any deduction for a tax loss (paragraph 45-330(1)(b) of Schedule 1 to the *Taxation Administration Act 1953*).

7.27 The amendments ensure that a reduction in tax in the previous year as a result of a loss carry-back tax offset is similarly not reflected in calculating the rate the Commissioner provides for the next year's PAYG instalments. ***[Schedule 6, item 66, paragraph 45-340(dc) of Schedule 1 to the Taxation Administration Act 1953]***

Assessments and objections

Refund from tax offsets is part of an assessment

7.28 A corporate tax entity that claims a loss carry-back tax offset should be able to object to the amount of any refund arising from the offset. Therefore, the amendments extend the definition of 'assessment' to include the amount of a refund arising from the taxpayer's refundable tax offsets. ***[Schedule 5, items 9, 11 and 12, definitions of 'assessment' and 'tax offset refund' in subsection 6(1) of the ITAA 1936 and definition of 'tax offset refund' in subsection 995-1(1) of the ITAA 1997]***

7.29 As a result, the right to object to an assessment is extended to cover objections to the amount of the refund from the taxpayer's refundable tax offsets (see subsection 175A(1) of the ITAA 1936). In addition, the amount of a tax offset can only be changed through the amendment of an assessment and must therefore occur within the time limits for amending an assessment (section 170 of the ITAA 1936).

7.30 A number of consequential amendments are made because of the change in the meaning of 'assessment' to include refunds arising from refundable tax offsets. ***[Schedule 5, items 14, 15 and 16, sections 166, 166A and 168 of the ITAA 1936]***

7.31 If, as a result of an amendment to an assessment, the total of a person's tax offset refunds is increased the Commissioner must apply the amount of the increase in accordance with the relevant part of the running balance account provisions. ***[Schedule 5, item 17, subsection 172A(1) of the ITAA 1936]***

7.32 Similarly, if, as a result of an amendment to an assessment, the total of a person's tax offset refunds is reduced, the person is liable to pay the amount of the reduction. The amount is due 21 days after the Commissioner gives the person notice of the amended assessment. ***[Schedule 5, item 17, subsection 172A(2) of the ITAA 1936]***

7.33 If the amount that the person is liable to pay remains unpaid after the time by which it is due to be paid, the person is liable to pay the general interest charge on the unpaid amount for each day in the period that:

- starts at the beginning of the day on which the amount was due; and
- finishes at the end of the last day on which the amount, or the general interest charge on the amount, remains unpaid.

[Schedule 5, items 17, 22 and 23, subsection 172A(3) of the ITAA 1936 and subsection 8AAB(4) and 250-10(1) in Schedule 1 to the Taxation Administration Act 1953]

Returns of full self-assessment taxpayers

7.34 The returns of full self-assessment taxpayers (mostly companies) are deemed to be assessments made by the Commissioner at the time they are lodged (subsection 166A(3) of the ITAA 1936). Therefore, it is important that their returns contain all the information that an assessment needs to include. At the moment, the required information includes an entity's taxable income and the tax payable on that income. The amendments ensure that the required information also includes the amount of the entity's refund arising from its refundable tax offsets (which the amendments make part of an assessment). ***[Schedule 5, item 13, paragraph 161AA(ba) of the ITAA 1936]***

Objections in 'nil' tax liability cases

7.35 If an entity is assessed as having no taxable income or no tax liability, taxpayers can object only if they are seeking to increase the liability. The amendments modify this approach by permitting objections which allow the taxpayer to increase a refundable tax offset. This ensures that taxpayers have a right to object to the amount of a refund where an entity has no tax liability. ***[Schedule 5, items 18, 19 and 20, subsections 175A(2) and (3) of the ITAA 1936]***

Burden of proof on appeal

7.36 A taxpayer who is dissatisfied with a decision the Commissioner makes on their objection can take their dispute to the Administrative Appeals Tribunal or the Federal Court. A taxpayer who does that has the burden of proving that the Commissioner's decision was 'excessive'. As a result of the High Court's decision in *FCT v Dalco* (1990) 168 CLR 614, the taxpayer must prove, not just that the assessment is too high, but what the correct amount of the assessment is.

7.37 This causes a difficulty to arise if a taxpayer wants to show that the assessment is not high enough, as will usually be the case with assessments of the amount of a refund arising from refundable tax offsets. Therefore, the amendments change the 'burden of proof' rules so that the taxpayer must prove that:

- in the normal case — the assessment is excessive; or
- where the taxpayer contends that the assessment should be higher — the assessment is incorrect.

7.38 In either case, the taxpayer must also prove what the correct amount of the assessment is, preserving the effect of the *Dalco* decision. ***[Schedule 5, items 25 and 26, paragraphs 14ZZK(b) and 14ZZO(b) of the Taxation Administration Act 1953]***

Delayed application of the assessment and objection amendments

7.39 Changes will need to be made to the Australian Taxation Office's systems to bring the calculation of the amount of a taxpayer's refunds arising from refundable tax offsets into the assessment regime. As this will take some time to implement, the amendments to the assessment provisions only apply to assessments for the 2013-14 and later income years made on or after 1 July 2013. ***[Schedule 5, items 24 and 27]***

7.40 For the period before the assessment provisions apply, taxpayers will receive a notice of the amount of their refund from refundable tax offsets. The calculation of the amount in the notice is not an assessment. However, taxpayers can object to the notice separately from their right to object to their normal income tax assessment. ***[Schedule 5, item 10, subsections 67-115(2) and 67-135(1) of the IT(TP)A 1997]***

7.41 The objection must be lodged within the same period that the taxpayer could lodge an objection to an assessment for the relevant income year. If there is no notice of assessment for the year, the objection period is as long as the period would have been if notice of an assessment had been given on the date of the notice. ***[Schedule 5, item 10, subsection 67-135(3) of the IT(TP)A 1997]***

7.42 The amendments empower the Commissioner to:

- provide taxpayers with a notice of the amount of their refund arising from refundable tax offsets; and
- include the notice in some other notice the Commissioner is providing the taxpayer (it would usually be included in the notice of assessment).

The Commissioner can provide the notice electronically if the taxpayer's return is lodged electronically. ***[Schedule 5, item 10, section 67-100 of the IT(TP)A 1997]***

7.43 The Commissioner is deemed to provide a notice, if the taxpayer is a full self-assessment entity, when the taxpayer lodges its return for the 2012-13 income year. The notice is deemed to specify the amount of the entity's tax offset refunds in accordance with the return. ***[Schedule 5, item 10, section 67-105 of the IT(TP)A 1997]***

7.44 If the Commissioner does not provide a notice, taxpayers can request the Commissioner to provide a notice during the period within which they can object to their assessment for that year, or within two years after the end of the income year if there is no notice of assessment. As with assessments, the Commissioner can allow more time to object. ***[Schedule 5, item 10, subsections 67-110(1) and (2) of the IT(TP)A 1997]***

7.45 If the Commissioner does not provide the notice within 60 days of the request, the Commissioner is taken to have provided a notice that the taxpayer is not entitled to a tax offset refund on the 60th day after the request. That will trigger the taxpayer's right to object to the notice. ***[Schedule 5, item 10, subsection 67-110(3) of the IT(TP)A 1997]***

7.46 The Commissioner can amend a notice. An amended notice is treated as any other notice except that the taxpayer's right of objection is limited to the extent of any change from the amendment. The taxpayer's right to object to the original notice still remains. ***[Schedule 5, item 10, section 67-120 and subsection 67-135(2) of the IT(TP)A 1997]***

7.47 The rules about the validity of assessments, and about the due making and correctness of assessments, apply equally to notices of the amount of the refund. ***[Schedule 5, item 10, sections 67-125 and 67-130 of the IT(TP)A 1997]***

7.48 If the Commissioner does not give notice of the amount of the refund, this does not affect either:

- a taxpayer's right to the refund; or
- the time by which the refund must be applied or refunded under the running balance account rules.

[Schedule 5, item 10, subsection 67-115(1) of the IT(TP)A 1997]

7.49 The existing right to object to the amount of a tax offset for research and development expenditure is repealed for objections made on or after 1 July 2013. An objection made after that date will be dealt with:

- if the tax offset is part of an assessment for the 2013-14 or a later income year — under the normal assessment provisions; or
- if the objection relates to an offset for an earlier income year — under the interim arrangements.

[Schedule 5, items 7, 8 and 21]

Defined terms

7.50 The amendments add a number of definitions to the income tax law for the purposes of the loss carry-back tax offset measure. In some cases, existing definitions are expanded and relocated to reflect their extra application to loss carry-back. ***[Schedule 5, items 3, 9, 11, 12 and 28, Schedule 6, items 34 to 41, definitions of 'assessment', 'loss carry back tax offset' and 'tax offset refund' in subsection 6(1) of the ITAA 1936, section 960-20 and definitions of 'carry back', 'current year', 'income tax liability', 'loss carry back choice', 'loss carry back tax offset', 'loss carry back tax offset component', 'tax offset refund', 'unutilised' and 'utilise' in subsection 995-1(1) of the ITAA 1997]***

Guide material

The non-operative lists of relevant provisions about tax offsets and tax losses are amended to include references to the loss carry-back tax offset. ***[Schedule 6, items 50 and 51, sections 13-1 and 36-25]***

Application and transitional provisions

Application

7.52 The amendments to the assessment provisions of the income tax law apply to an assessment if the assessment is made on or after 1 July 2013, and:

- if the assessment relates to an income year, the income year is the 2013-14 income year or a later income year; or
- if the assessment relates to another accounting period, the other accounting period commences on or after 1 July 2013.

[Schedule 5, item 27]

The other amendments commence on the day after Royal Assent.

Loss carry-back — Statement of Compatibility with Human Rights and Regulation impact statement

STATEMENT OF COMPATIBILITY WITH HUMAN RIGHTS

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

Schedules 5 and 6 Loss carry-back

Schedules 5 and 6 are 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

8.1 The current income tax law allows taxpayers to deduct their tax losses only against their assessable income of later years. This can mean that a company that makes a profit in one year and a loss in the next year will pay a higher effective tax rate over the two year period than another company that makes the same overall profit in a more even fashion.

8.2 This potential to incur a higher effective tax rate can lower the expected after-tax return on an investment that is under consideration and so can distort the relative attraction of competing projects from a firm's perspective, compared with their value to the economy as a whole.

8.3 To address that, this measure adopts a recommendation made by the Business Tax Working Group in its *Final Report on the Tax Treatment of Losses* by allowing 'corporate tax entities' (corporations, unincorporated associations, and some limited partnerships and trusts that are taxed like companies) to use their income tax losses to produce a refundable tax offset, effectively obtaining a refund of past tax paid.

8.4 At the entity's option, up to $1 million of a tax loss can be carried back to either of the preceding two income years in which it had

an income tax liability. The offset is equal to the amount carried back multiplied by the corporate tax rate but is limited both by the entity's tax liability for the year it is carried back to and by the balance in its franking account.

8.5 The amount of the offset directly reduces the entity's income tax liability of the year for which it claims the offset. Any excess is an amount owed to the entity.

8.6 A tax loss that is carried back cannot later be reused, either to produce another tax offset or as a deduction against future assessable income.

Human rights implications

8.7 Use of an entity's tax losses in the way the measure provides for can only advantage the entity. Further, the entity can choose whether or not to use its tax losses in that way. Accordingly, schedule 5 and 6 do not engage any of the applicable rights or freedoms.

Conclusion

Schedules 5 and 6 are compatible with human rights as it does not raise any human rights issues.

Assistant Treasurer, the Hon David Bradbury

REGULATION IMPACT STATEMENT

Introduction

8.9 This Regulation Impact Statement, which was prepared by the Department of the Treasury at the original decision-making stage, was assessed as adequate by the Office of Best Practice Regulation and publicly released on 18 May 2012.

8.10 A Regulation Impact Statement is a document prepared by departments, and as such this Regulation Impact Statement reflects the Department of the Treasury's assessment of the costs and benefits of each option at the decision-making stage and does not reflect changes arising

from further consultation during the legislative development of this measure.

Background

8.11 The *Income Tax Assessment Act 1997* provides the rules for calculating a taxpayer's assessable income, allowable deductions and offsets to arrive at their taxable income and consequential income tax liability. One of the consequences of the rules is that in an income year a taxpayer may experience a tax loss as a result of their business or investment activities. If allowable deductions are greater than assessable income then the taxpayer will incur a tax loss.

8.12 The current taxation system treats profits and losses asymmetrically. Profit is taxed in the year in which it is derived, but a loss must be carried forward (indefinitely) at its nominal value and be deducted against future assessable income. A perfectly symmetrical treatment of profits and losses would see the income tax value of the loss (that is, the value of the loss multiplied by the relevant tax rate) refunded to the taxpayer in the year that the loss is incurred.

8.13 At the present time, individual taxpayers, including businesses operating as sole traders, can offset current year business losses against other income sources such as salary and wages and investment income.

8.14 For large companies and consolidated groups that conduct a range of business activities, losses in one activity can be offset against profits from other activities, improving their ability to utilise current losses.

8.15 However, companies that undertake only one business activity do not have other sources of income against which to offset their losses. Companies that make a current year loss are therefore required to carry that loss forward.

8.16 Australia is not unique in this respect; it is common practice in other jurisdictions to require a loss to be carried forward, although various forms of loss carry-back are available in a number of OECD countries, including Canada, France, Germany, Ireland, Singapore, the United Kingdom and the United States.

8.17 The rules governing the utilisation of tax losses have evolved considerably over time, generally to allow companies greater access to prior year losses, but with additional integrity rules to prevent 'loss trafficking'.

8.18 Although tax losses can now be carried forward indefinitely, that is a relatively recent development. It was extended to primary producers in 1966 and was given general application in 1990. Before that time, most companies were only entitled to a deduction for losses from the preceding seven years. In the early decades of the federal income tax, losses could only be carried forward for four years.

8.19 Prior to 1944, the time limitations were the only restrictions that were imposed on the ability of companies to carry forward their tax losses to offset against future income. In 1944, the continuity of ownership test (COT) was established for private companies to address 'loss trafficking', that is, purchasing companies in order to gain a tax advantage from the carry forward losses. Loss trafficking was described by the Treasurer at the time as the practice 'of buying up shares in practically defunct companies and then operating those companies for purposes other than those for which they were originally registered'. The COT ensures that, broadly, a company cannot deduct its losses if there has been a change in the identity of 50 per cent or more of its ultimate owners in the period since the loss was incurred.

8.20 The same business test (SBT) was first introduced in 1965 at a time when the COT requirements were being strengthened. It was intended to serve as a concession to the COT, aimed at ensuring that the COT did not interfere with bona fide attempts to take over, and rehabilitate, ailing businesses.

8.21 These integrity rules limit the ability of companies to carry forward losses. Thus the benefit (cash flow) of the loss is potentially not realised until a significant period of time has elapsed from the circumstances that caused the loss to occur and in some circumstances, may not be realised at all. As a result, the real value of the loss can be eroded by the time it is utilised.

8.22 The current treatment of losses restricts companies' cash flow in an economic downturn as they cannot access the value of the loss until they return to profitability. It also acts as a bias against risk taking, by increasing the effective tax rate over the course of the investment if in some years it incurs a loss. The current rules can also limit the companies' ability to utilise past losses if they seek an equity injection or seek to make changes to their business to respond to changes in demand or broader economic circumstances. In summary, the current treatment of losses inhibits companies' ability to meet the challenges and opportunities from the structural changes that the Australian economy is experiencing.

Problem

8.23 The Australian economy is undergoing structural change in the wake of Mining Boom Mark II and its impact on the terms of trade and the Australian dollar. Businesses operating in the non-mining sectors of the economy, such as manufacturing, tourism, education, retail and construction, are facing challenging trading conditions.

8.24 Businesses facing these conditions need to be able to adapt and restructure. It is particularly important that companies that are experiencing losses be able to make changes to their business to return them to profitability. That may mean undertaking investment in plant and equipment or retraining staff. It is important that the tax system does not place impediments in the path of businesses that are seeking to engage in the sensible risk taking and investments that are necessary in order to adapt and restructure.

8.25 The current taxation treatment of losses can act as an impediment to sensible risk taking.

8.26 Company profits are taxed in the year in which they are earned but losses must be carried forward and be deducted against future profits.

8.27 This asymmetric treatment of profits and losses can have the effect of increasing the effective tax rate above the statutory rate for companies that incur losses over the course of the investment. This is because the tax system looks through a single financial year lens at an investment that generates returns over multiple years. For an investment that has less risk of a loss and so generates returns evenly over the investment period, the lens of a single financial year may have little impact. But for a riskier investment that may generate uneven returns, the lens of a single financial year can result in a higher effective tax rate over the period of the investment. This is set out in the tables below that show the effective tax rate on a low risk and high risk investment.

Tax impact on low-risk investment choice

Possible before-tax return on an investment ($)	Investment 1 (less risky)			
	Prob. of return (%)	Treasury	After-tax expected return ($)	Effective tax rate (%)
40	*50*	20	14	30
20	*50*	10	7	30
Total		**$30**	**$21**	**30%**

Tax impact on a higher-risk investment choice

Possible before-tax return on an investment ($)	Investment 2 (more risky)			
	Prob. of return (%)	Before-tax expected return ($)	After-tax expected return ($)	Effective tax rate (%)
120	*10*	12	8.4	30
100	*20*	20	14	30
80	*20*	16	11.2	30
20	*10*	2	1.4	30
-40	*20*	-8	-8	-
-60	*20*	-12	-12	-
Total		**$30**	**$15**	**50%**

8.28 Of the approximately 850,000 companies in Australia, nearly 60% were in a tax loss position in 2008-09 (see below for a breakdown by industry).

8.29 Options to assist loss making companies will vary in terms of the number of companies affected. For example to benefit from loss carry-back, companies must have paid tax in the carry-back period and have a positive franking accounting balance. Once these factors have been taken into account, only around 110,000 (12%) companies are expected to benefit from loss carry-back over the first four years of operation – the majority of which will be small businesses.

Non-taxable companies[1], by industry[2], 2008-09 income year[3]

	Number of non-taxable companies	Percentage of total companies
Industry	No.	%
Agriculture, forestry and fishing	11,565	68.6
Mining	2,973	71.1
Manufacturing	22,740	59.4
Electricity, gas, water and waste services	1,305	60.8
Construction	57,239	61
Wholesale trade	23,758	59.6
Retail trade	26,821	61.9
Accommodation and food services	14,728	69.9
Transport, postal and warehousing	21,568	64.5
Information media and telecommunications	6,025	69.2
Financial and insurance services	52,737	56.4
Rental, hiring and real estate services	50,676	48.8
Professional, scientific and technical services	62,483	60.8
Administrative and support services	14,571	60.5
Public administration and safety	1,951	60.9
Education and training	4,873	66
Health care and social assistance	15,535	58
Arts and recreation services	4,685	68.6
Other services	15,944	61.1
Other[4]	39,960	60.2
Total	452,137	59.3

Source: Taxation Statistics 2008-09, Table 3.13

Notes:

1. Non-taxable companies are defined as companies with net tax less than or equal to $0.
2. The industry groups are classified based on the Australian and New Zealand Standard Industrial Classification (ANZSIC) 2006 codes on the Australian Business Register.
3. Data for the 2008–09 income year includes data processed up to 31 October 2010.
4. Includes companies lodging under the 'nil company returns' code, which includes non-taxable companies or companies with nil company returns – no income, expense or balance sheet data present; companies that did not state their industry; and/or companies registered under the government administration and defence industry code.

8.30 Reducing the tax system's bias against sensible risk taking could be expected to increase both the quantity and quality of investment and

improve cash flow for companies that have experienced a tax loss, potentially improving the allocation of resources across the economy. This could have positive flow-on effects for productivity, which in turn can support growth in real wages and employment. Importantly, reducing the bias can also encourage businesses under pressure to adapt and restructure to make the necessary changes to their business.

8.31 The tax system's bias against sensible risk taking may divert capital to less risky, lower value investments. The bias against business risk taking is likely to be particularly detrimental to productivity in Australia's current circumstances that require businesses to be flexible and innovative, and to be able to take advantage of new opportunities presenting themselves in the changing global environment.

8.32 Companies are also required to meet integrity tests that impact on their ability deduct the current year loss against future years' assessable income. The company must satisfy the COT to utilise a prior year loss. The COT is satisfied if the same persons have more than 50 per cent of the voting power, rights to dividends and rights to capital distributions at all times during the ownership period. Therefore, if there is a change in ownership or a capital injection, the taxpayer will not pass the COT and will not be able to carry forward any losses.

8.33 In the event the COT is not satisfied, the company can still utilise the loss if it can satisfy the SBT. That is, the company must carry on the same business in the year they claim the loss as it carried on immediately before it failed the continuity of ownership test. That can mean that, faced with the need to restructure their business in the face of incurring losses, a business may face restrictions on how it can change its products or services if it is to deduct its losses against future profits.

8.34 Where a business passes the integrity tests, they can deduct their tax losses but at their nominal value. The real value of the loss can therefore be reduced by the time it can be claimed as a deduction against income.

8.35 The asymmetric treatment of profits and losses can also impact on a businesses' cash flow – they are required to remit tax in the year they earn the profit but have to wait until they return to profitability in order to benefit from deducting the loss. The current tax treatment of losses can be seen as the Government withholding its share of the cash flow impact of a loss, leaving businesses to bear the full impact of a loss in the year it is incurred. The current tax treatment of losses delays (and in the extreme case of zero future assessable income, denies) the cash flow benefit for businesses associated with accessing the tax value of a loss.

8.36 This cash flow impact can be detrimental to a business's future economic prospects, especially where the company requires short-term liquidity to meet day-to-day outgoings. It also reduces the ability of a business to make investments in new equipment, research and development, staff training and development and other activities that help to increase the viability of the business in the long-term and add to productivity. Poor cash flow can also limit its access to commercial funding through debt and equity markets.

Objectives of Government action

8.37 The objectives of introducing loss carry-back are:

- to reduce the bias in the tax system against innovation and sensible risk-taking;
- to assist businesses in the current economic climate; and
- to manage the impact of assistance measures on the Budget.

Options that may achieve objectives

Full loss refundability

8.38 The asymmetry in the treatment of profits and losses could be directly addressed by providing a tax refund, equal to the value of the loss multiplied by the statutory tax rate, to companies in the year in which they incur a loss.

8.39 This would assist businesses in the current economic climate by providing them with immediate cash flow benefits and removing the bias against sensible risk taking.

8.40 However, this would raise integrity concerns that some taxpayers may engage in tax planning to achieve a loss in order to access the refund. If the business subsequently ceased operating there would be little recourse for the Commissioner of Taxation to take action against the taxpayer to recover the refund.

8.41 Providing an immediate refund of tax losses would also only provide symmetry to the extent that business income is being measured consistently. For example, where losses are derived from access to accelerated depreciation, business income and deductions are not being consistently measured.

8.42 No tax system in the world provides full loss refundability (and the cost to revenue would be extremely high). Providing a refund for tax losses would have a significant impact on the budget. The aggregate carried forward loss balance for all companies was estimated to be around $170 billion in 2009-10. It therefore does not meet the objective of managing the impact on the budget.

8.43 However, full refundability does operate as an automatic stabiliser. It increases cash flows for previously profitable companies during economic downturns when they are needed. It also means that revenue would recover more quickly as the economy recovered as companies would not lower their taxable income during the recovery period by deducting prior year losses as currently occurs.

Loss carry-back

8.44 A second option is to provide a more limited form of refundability by allowing companies to carry-back losses incurred in one year against taxes paid in earlier years. This means that rather than applying a single financial year lens, the tax system would look at the returns to investment across a number of years, allowing profits and losses to be offset across the period.

8.45 If loss carry-back were unlimited it could raise similar integrity concerns to that raised by full refundability and result in significant costs to the budget.

8.46 However, a number of restrictions can be placed on loss carry-back to mitigate these risks.

8.47 Carry-back would allow losses to be offset against prior years' tax paid. Australia's imputation system credits company income tax against the personal tax of the shareholders. Under the imputation system, companies must keep a franking account. A credit arises in the franking account when a company pays income tax. A debit arises when the company receives a refund of the tax paid or when it attaches franking credits to dividends paid to shareholders. If a company has a negative franking account balance at the end of an income year then they must pay a franking deficit tax to bring the account balance to zero. This means, if a company was to receive a carry-back refund for losses incurred then they would have to pay the franking deficit tax to the extent the carry-back refund leads to a negative franking account balance. To avoid this, the benefits of loss carry-back are limited to the positive balance of the franking account. That is, the carry-back can never exceed the value of past taxes paid that have not been distributed to shareholders. This reduces the risk of fraudulent activity.

8.48 The number of years that taxpayers can carry-back a loss can be limited to limit the impact on the budget. However, a shorter carry-back period means that companies experiencing large losses or longer periods of loss may not be able to fully realise the value of their loss. Other jurisdictions that have adopted loss carry-back have opted for between one and three years.

8.49 The amount of loss that can be carried back can be limited. Placing a cap on the amount of the loss reduces integrity concerns by reducing the value of the deduction that is available and so reducing the incentive to engage in tax planning.

8.50 A cap on the amount of the losses that can be carried back also targets the option to small and medium businesses. For example, for a cap of $1 million, around 90 per cent of the 'cash' benefit will flow to medium, small and micro businesses (see impact analysis section for more detail).

Loss uplift

8.51 A third option is to uplift the value of the losses that are carried forward. This would maintain or partially maintain the value of the loss, depending upon the uplift factor chosen. The impact on the budget would also depend upon the uplift factor. The impact on the budget would also ramp up over time as more losses were carried forward.

8.52 This option would not assist companies to as great an extent as loss carry-back as it would not provide a cash flow benefit at the time that the company incurred a loss, but would provide a benefit only when the company was once again profitable.

8.53 Uplifted losses would also not provide assistance to companies that could not access their losses because of the application of the integrity tests – the COT and the SBT.

Relax the loss integrity rules

8.54 A fourth option is to amend the integrity rules. The current rules limit companies' ability to seek new equity or to alter the goods or services or business model.

8.55 This option would assist companies in the current economic climate by removing an impediment to adaptation and restructuring. However, any relaxation of the integrity rules would move the tax system towards full loss refundability (that is, refunding losses at the company tax rate in the year in which they are incurred). However, this would need to be weighed against the risk of significant costs to the budget from potentially undermining the integrity of the tax treatment of losses through encouraging loss trafficking.

Refundable loss carry-back tax offset – design options

8.56 Treasury proposes a refundable loss carry-back tax offset that:

- is only available to companies, or entities that are taxed like companies;
- is subject to the loss integrity rules (that is, the continuity of ownership and/or same business tests);
- is restricted to revenue losses only;
- has a limited carry-back period;
- limits the amount of current year losses that can be carried back; and
- is limited to the amount of credit in the company’s franking account.

Available to companies and entities taxed like companies

8.57 Businesses can operate as sole traders, partnerships, companies or trusts. The administrative and compliance costs of extending loss carry-back to trusts, partnerships and sole traders is significant and outweighs the possible benefits.

8.58 Sole traders have broader options for utilising losses, such as offsetting the business loss against salary and wage income, which are not available to companies and entities taxed like companies.

8.59 Trusts are flow through vehicles for tax purposes - the point of taxation is the beneficiary not generally the trust. In order to apply loss carry-back the trustee would need to be aware of the beneficiary's marginal tax rate and whether the beneficiary paid tax on the trust distributions. This would require potentially complex and costly

compliance arrangements. For discretionary trusts, the benefits of loss carry-back may flow to beneficiaries other than those that paid the tax on the profits.

8.60 The advantages of restricting the measure to company losses are that it will be administratively simple, and have a negligible compliance impact.

Loss integrity rules apply

8.61 The loss integrity rules serve a crucial role in preventing loss trading. The COT ensures that, broadly, a company cannot deduct its losses if there has been change in the identity of 50 per cent or more of its ultimate owners in the period since the loss was incurred. The SBT was intended to serve as a concession to the COT, aimed at ensuring that the COT did not interfere with bona fide attempts to take over, and rehabilitate, ailing businesses. The consolidation regime modifies the loss utilisation rules, recognising the potentially more diverse nature of businesses within a consolidated group.

8.62 The COT and SBT will continue to apply to carry-back losses, to ensure that the new measure does not encourage the creation of arrangements that lead to loss trading.

8.63 The advantages of applying the loss integrity rules to loss carry-back are consistency with the current company loss recoupment rules and protecting the revenue.

Revenue losses only

8.64 Providing loss carry-back for capital losses would effectively provide an opportunity for companies to circumvent the integrity rules (in Part 3-1 of the Income Tax Assessment Act 1997) which quarantine the use of capital losses to capital gains. Currently, capital losses may only be applied against capital gains. Allowing capital losses to be applied against taxable income, which is revenue in nature, would permit capital losses to be converted into revenue losses – with significant potential cost to revenue.

8.65 Accordingly, loss carry-back would only be available in respect of revenue losses.

Limited carry-back period

8.66 Shorter carry-back periods have the advantage of reducing administrative and compliance costs, as well as limiting the impact on

revenue. However, its primary disadvantage is that it limits the benefits that companies can receive during a loss period, especially where those losses are large or protracted.

8.67 Longer carry-back periods have the advantage of providing companies with greater access to the tax value and benefit of their losses. However, they increase administrative and compliance costs, as well as increasing the potential impact on revenue.

Reduces the pool of losses

8.68 As a matter of clarification, any loss (or part of a loss) that is carried back will not be able to be carried forward.

Cap on amount of losses that can be carried back

8.69 Small and medium sized incorporated businesses don't have the same access to losses as diversified businesses and corporate groups. Large companies and consolidated groups have profits from other activities that they can use to absorb losses. Carry-back of losses could be targeted to small business by using the definition of small business or through imposing a quantitative cap (the amount of losses that could be carried back). A quantitative cap has the advantage of ease of administration and reduced compliance burden. The cap also reduces the exposure of the Government to very large losses incurred by individual businesses. A quantitative cap can also be easily adjusted to meet the economic circumstances.

Limited to the balance of the company’s franking account

8.70 Loss carry-back would be limited to the balance of the company's franking account. This means that the benefit of the loss carry-back is limited by the amount of tax that has been paid in the past. This operates as an integrity measure and, together with the quantitative cap, minimises the impact on the budget.

Start date

8.71 The advantages of providing loss carry-back for losses incurred from the 2012-13 income year include allowing companies experiencing a downturn to benefit as promptly as possible. In addition, it provides impetus for companies considering innovation and investment to do so in 2012-13.

8.72 The advantages of a later start date are that the Australian Taxation Office would have significant lead in time to update systems and income tax returns. However, the Australian Taxation Office, in its consultation with the Treasury, has indicated that the changes required are not extensive. In addition, the legislation could be achieved within current priority lists, although there will be pressure due to other legislative priorities, and potential 'tight' spots experienced by the Australian Taxation Office in updating its systems and documents.

Delivery Method

8.73 There are the two methods for delivering loss carry-back:

- Amending prior year returns; and
- A refundable loss carry-back tax offset for the current income year.

8.74 There are significant disadvantages to amending prior year returns. The disadvantages of a refundable tax offset are relatively minor when compared to the disadvantages of amending prior year returns. In view of this analysis, Treasury support the implementation of loss carry-back via the mechanism of a refundable tax offset.

8.75 Providing loss carry-back through amending earlier tax returns would mean that previous tax assessments would be reopened and altered to reflect the reversal of tax paid in those periods due to carry-back. This delivery mechanism could be administratively costly as old tax returns would need to be maintained and updated as losses are utilised.

8.76 Additional compliance costs would arise if unrelated amendments are made to previous tax returns. A taxpayer's assessment for the year in which they incurred a loss (and received a carry-back refund) may subsequently be amended such that they were not entitled to loss carry-back or were entitled to a greater refund than was provided. Correcting this would require reopening and amending the tax return from the loss year as well as the tax returns over the carry-back period.

8.77 Further problems may also arise if some of the tax returns that need to be amended fall beyond the Commissioner's amendment period (currently four years for companies). To deal with this problem, additional income tax could be imposed on the taxpayer to claw back incorrect refunds or additional refunds could be provided if taxpayers are found to have been entitled to a greater refund. This would eliminate the need to reopen and amend previous tax returns in light of an audit by the

Commissioner, significantly reducing the administrative costs of reversing incorrect refunds.

8.78 Alternatively, loss carry-back could be achieved through the use of a refundable tax offset. For example, a company could become entitled to a refundable tax offset in a year it has negative taxable income and has paid income tax in at least one year over the carry-back period. So, in the case where carry-back is limited to a company's franking account balance and a quantitative cap, the amount of the refundable tax offset would be the lesser of:

- the tax value of the company's tax loss for the current year;
- the company's franking account balance;
- the tax value of any quantitative cap imposed on loss carry-back; and
- the amount of income tax paid over the carry-back period.

8.79 The relevant proportion of the company's tax loss would then be converted to a refundable tax offset and, subject to any outstanding tax liabilities, paid to the company. To substantiate a claim for the refundable tax offset, a company would need to provide details of previous claims (to ensure there is no double dipping). The refundable tax offsets would be counted as a debit in the franking account.

8.80 This delivery mechanism is administratively easier than amending tax returns, as it removes the need to reopen previous tax returns and reduces the risk of complications due to the Commissioner's allowable amendment period. However, previous tax returns would still need to be maintained and accessed to calculate the refundable tax offset that is available to taxpayers. Any review of the company's tax affairs which lead the Commissioner to conclude that the company was not entitled to a refundable tax offset in a previous year could lead to the offset being disallowed.

Impact analysis

8.81 This measure is not expected to impact on the economy in the broader sense; that is, there will be no measurable impact on Gross Domestic Product.

8.82 An aggregate macroeconomic analysis would be a blunt tool to use because the policy doesn't affect all firms or most firms or even most

firms within an industry. It is more of a microeconomic issue than a macroeconomic issue and the limited scope of the measure and data limitations mean that an aggregate macroeconomic analysis would not be helpful.

8.83 Nonetheless, there will be positive economic impacts at the microeconomic level:

- The measure provides assistance to companies that are struggling from the impact of the mining boom. This assists the economy to make the necessary structural adjustments.
- Eligible companies that incur a loss in 2012-13 would receive a cash flow benefit in 2013-14. This will facilitate further investment and other business decisions that are necessary to return the company to profit.
- There will be less risk averse investment as the measure supports investment aimed at innovation and adapting to changing economic circumstances.
- The measure will support businesses, particularly small and medium businesses that are not able to take advantage of the consolidation regime's loss utilisation rules (current year losses incurred by one member of the group can be offset against income earned by other members of the same group).
- Carrying back losses will flatten taxable income peaks and troughs. Consequently, the upswing/downswing cycle will be flatter, allowing for faster recovery of government revenue on the upswing.

8.84 Loss carry-back will predominantly benefit existing businesses that have been profitable in the past and are considering what changes they need to make in order to remain competitive. As highlighted earlier, it will do this because such decisions involve uncertainty and risk for companies and loss carry-back will lower the risk adjusted after-tax return on a range of potential new investments.

8.85 The measure will be of potential benefit to the 26 per cent of small businesses (around 700,000) that are incorporated, but not to the 74 per cent (around 2.0 million) that are not incorporated.

8.86 A worked example is provided below:

Worked Example: A company investing to upgrade its product line

Seven Beaches Resorts Pty Ltd (Seven Beaches) would benefit under a loss carry-back arrangement with a $1 million cap, a one year carry-back period, limited by franking account balance. Seven Beaches operates seven beach resorts in different states around Australia.

To attract greater numbers of international and domestic clients, Seven Beaches decides to undertake a substantial refurbishment of all its resorts. This will involve upgrading all resort bars, replacing all beds and other furniture, upgrading all in-room televisions and fridges and installing a new range of light fittings and lamps.

Seven Beaches is also looking to distinguish itself on the basis of its service, particularly to overseas visitors. Subject to available cash flow, it would like to use the period of refurbishment to offer some of its staff the opportunity to upgrade their skills (for example, by becoming qualified recreational activity instructors).

This plan is developed over the course of 2012-13 and 2013-14 where Seven Beaches has taxable income of $8.00 million and $7.00 million respectively. At the end of 2014-15 Seven Beaches has a franking account balance of $3 million.

The refurbishment is planned to commence in 2014-15 with the eastern states beach resorts and involves closing parts of the resort during the refurbishment. In April 2016, Seven Beaches plans to launch an advertising campaign promoting its revamped facilities.

Seven Beaches plans to refurbish its other beach resorts in 2015-16. A further advertising campaign would be rolled out once the refurbishment of all beach resorts is completed early in 2016.

As a result of the refurbishment Seven Beaches would have substantially less assessable income and larger deductions than in previous years. As a result, it would make a tax loss of $6.00 million in 2014-15 and $4.00 million in 2015-16.

Under the current income tax law, Seven Beaches would build up a stock of carry forward tax losses. Provided it doesn’t experience a change in majority ownership these tax losses can be used to reduce Seven Beaches’ taxable income in future years.

Current tax system						
Year	**2012-13**	**2013-14**	**2014-15**	**2015-16**	**2016-17**	**2017-18**
Assessable income	$30,000,000	$30,000,000	$14,000,000	$19,000,000	$25,000,000	$35,000,000
Expenses — excluding depreciation	($21,000,000)	($22,000,000)	($18,800,000)	($21,700,000)	($23,900,000)	($20,900,000)
Deductions — depreciation	($1,000,000)	($1,000,000)	($1,200,000)	($1,300,000)	($2,100,000)	($2,100,000)
Deductions — losses	$0	$0	$0	$0	$0	($11,000,000)
Taxable income	$8,000,000	$7,000,000	($6,000,000)	($4,000,000)	($1,000,000)	$1,000,000
Tax payable	***$2,400,000***	***$2,100,000***	***$0***	***$0***	***$0***	***$300,000***
Total carry forward losses	$0	$0	$6,000,000	$10,000,000	$11,000,000	$0

Seven Beaches would benefit from the loss carry-back due to the losses made during its refurbishments, but would not be able to utilise the full value of its tax losses. Note that Seven Beaches has a franking account balance of $3 million at the end of 2014-15.

Due to the reduced income and increased deductions involved with refurbishments, Seven Beaches is in its first tax loss position in 2014-15 so that Seven Beaches has;

- a loss with the tax value of $1.8 million ($6 million x 30%)

- a franking account balance of $3 million

- paid $2,100,000 in taxes over the carry-back period, and

- a quantitative cap with the tax value of $300,000 ($1 million x 30%)

As the tax value of Seven Beaches' loss is higher than the quantitative cap, Seven Beaches will only be able to carry-back $1 million against previously paid taxes. Seven Beaches' loss for 2014-15 will be carried back against tax paid in 2013-14 (the prior year). Seven Beaches will receive a loss carry-back refund of $300,000 for its loss in 2014-15. This reduces the franking account balance to $2.70 million

($3 million — $300,000). The remaining loss of $5 million is carried forward to 2015-16.

Seven Beaches then experiences a second year of loss in 2015-16 but cannot carry the tax value back as there were no taxes paid in the previous year. The full value of the loss is added to loss stock and carried forward to 2016-17.

Seven Beaches suffers a third year of loss in 2016-17 but cannot carry the tax value back as there were no taxes paid in the previous year. The full value of the loss is added to the loss stock and carried forward to 2017-18.

In 2017-18 Seven Beaches returns to profit and is able to use its carry forward stock to reduce its taxable income.

Loss carry-back

Year	2012-13	2013-14	2014-15	2015-16	2016-17	2017-18
Assessable income	$30,000,000	$30,000,000	$14,000,000	$19,000,000	$25,000,000	$35,000,000
Expenses — excluding depreciation	($21,000,000)	($22,000,000)	($18,800,000)	($21,700,000)	($23,900,000)	($20,900,000)
Deductions — depreciation	($1,000,000)	($1,000,000)	($1,200,000)	($1,300,000)	($2,100,000)	($2,100,000)
Deductions — losses	$0	$0	$0	$0	$0	($10,000,000)
Taxable income	$8,000,000	$7,000,000	($6,000,000)	($4,000,000)	($1,000,000)	$2,000,000
Tax payable	***$2,400,000***	***$2,100,000***	***$0***	***$0***	***$0***	***$600,000***
Loss carried back	$0	$0	$1,000,000	$0	$0	$0
Carry-back refund	***$0***	***$0***	***300,000***	***$0***	***$0***	***$0***
Total carry forward losses	$0	$0	$5,000,000	$9,000,000	$10,000,000	$0

8.87 A range of variables for a refundable loss carry-back tax offsets were considered by Treasury. The costings are provided below.

	2011-12 ($m)	2012-13 ($m)	2013-14 ($m)	2014-15 ($m)	2015-16 ($m)	Total ($m)
Option A: Working Group Proposal Option Phase in Loss Carry-back (applied to losses incurred in 2013-14, $1 million cap, with a 1 year carry-back phase-in for 1 year, then 2 year carry-back going forward, limited by franking account balance.)	0	0	0	-150	-300	**-450**
B. Variation: Phase in Loss Carry-back, (applied to losses incurred in 2012-13, $1 million cap, with an initial 1 year carry-back phase-in for one year, then 2 year carry-back going forward, limited by franking account balance.)	0	0	-150	-250	-300	**-700**
C. Variation: Phase in Loss Carry-back, (applied to losses incurred in 2012-13, $1 million cap, with an initial 1 year carry-back phase-in for 2 years, then 2 year carry-back going forward, limited by franking account balance.)	0	-0	-150	-150	-300	**-600**
D. Variation: Loss Carry-back (applied to losses incurred in 2012-13, $1 million cap, with a 1 year carry-back, limited by franking account balance.)	0	0	-150	-150	-150	**-450**
E. Variation: Loss Carry-back, (applied to losses incurred in 2012-13, $10 million cap, with a 1 year carry-back, limited by franking account balance.)	0	0	-200	-200	-250	**-650**

8.88 Treasury's analysis of loss carry-back is based on historical company tax return data from 2003-04 to 2009-10. The distributional analysis represents the industries that would have benefited if loss carry-back had been in place from 2003-04 but is nonetheless indicative of which industries are the most likely to benefit if carry-back were introduced in the future. Across all the options with a cap around $1 million 90 per cent of the 'cash' benefit will flow to medium, small and micro businesses.

Distributional Analysis of Loss Carry-back by Industry					
	Option A	**Option B**	**Option C**	**Option D**	**Option E**
Construction	15%	15%	15%	15%	10%
Manufacturing	15%	15%	15%	15%	15%
Finance and Insurance	15%	15%	15%	15%	25%
Prof and Tech Services	10%	10%	10%	10%	10%
Wholesale Trade	10%	10%	10%	10%	10%
All Other Industries	35%	35%	35%	35%	30%

Distributional Analysis of Loss Carry-back by Company Size					
	Option A	**Option B**	**Option C**	**Option D**	**Option E**
Micro	40%	40%	40%	40%	25%
Small	25%	25%	25%	25%	15%
Medium	25%	25%	25%	25%	25%
Large	5%	5%	5%	5%	10%
Very Large	5%	5%	5%	5%	25%

Business cost calculations

8.89 A nil to insignificant compliance cost for taxpayers will arise from making the choice to obtain a refundable loss carry-back tax offset. As the process of making a claim will involve the lodgement of the current year return, no additional compliance costs are expected to arise. Taxpayers are already required to keep records concerning their losses.

8.90 The ATO advises that its existing account management system is sufficient to manage the refunds (it already has the capacity to automatically generate refunds). Some minor work on the income tax calculators will be required to allow for the new tax offset, and minor changes may be required to the company income tax return form to allow for the choice to be made.

Consultation

8.91 The Business Tax Working Group has conducted consultation on loss carry-back. In addition, Treasury and the Business Tax Working Group Secretariat have consulted with the Australian Taxation Office on matters concerning the implementation of the measure, such as compliance and administration issues.

8.92 The Business Tax Working Group invited written submissions from businesses and the wider community on the issues and ideas discussed in their interim report. To assist interested parties in making submissions, some framing questions were provided in a separate consultation guide.

8.93 Submissions were requested by 3 February 2012. The Working Group received a total of 24 submissions in response to the interim report including two confidential submissions.

8.94 Over the course of March 2012, representatives of the Working Group conducted meetings with stakeholders in Melbourne, Sydney, Brisbane and Perth.

8.95 The stakeholders consulted were a mix of representative bodies and individual companies.

8.96 The Working Group conducted these meetings on a confidential basis to allow discussions between the Working Group and participants to be as open as possible.

8.97 The following views have been offered in response to the Business Tax Working Group's interim report - generally supportive of loss carry-back:

- Association of Mining and Exploration Companies: supports loss reform, however wants a targeted exploration credit instead of loss carry-back.
- Australian Chamber of Commerce and Industry: supports loss carry-back but want it extended to all businesses, not just companies.
- Australian Financial Markets Association: broadly supports loss carry-back.
- Australian Property Group: supports loss carry-back with a three year carry-back period because it isn't likely that a

business will have one year in loss followed by a year in profit and so on. Cap on loss carry-back is not mentioned.

- BDO: rank loss reform as its highest priority. It prefers a carry-back period of three years, with limit to carry-back determined by franking account balances.
- Associate Professor Dale Boccabella: refers to his article, "A loss carry-back rule for business losses in Australia: Some initial thoughts", Weekly Tax Bulletin, Thomson Reuters, No 47, 11 November 2011 at paragraph 1770.
- BusinessSA: supports loss carry-back with a three year carry-back period.
- Corporate Tax Association: support a one year loss carry-back, with exceptions for certain circumstances (eg, GFC) and supports a cap on the losses carried back as in the European model.
- CPA Australia: supports loss carry-back for a two year period, with a modest cap as businesses are not prepared to give up much to fund loss carry-back.
- Ernst & Young: support a loss carry-back limited to two years, but do not support a cap other than the franking account balance.
- Grant Thornton: supports loss carry-back with a two year carry-back period.
- Institute of Public Accountants: supports loss carry-back with a one to three year carry-back period. It supports a restriction to small businesses for the measure.
- Master Builders Association: support loss carry-back with a longer carry-back period to support large capital investments.
- National Tourism Alliance: supports loss carry-back with a carry-back period of more than one year.
- Pennam Partners: notes that loss carry-back will not benefit start-up companies.
- Property Council of Australia: strongly prefers a loss carry-back to other loss reforms, with a three year carry-back period and be available to all businesses.

- Real Estate Institute of Australia: supports loss carry-back with a carry-back period of three years.

- The Institute of Chartered Accountants Australia: supports loss carry-back, with a carry-back period of two years, as a measure to support smaller businesses in better accessing their losses and supporting them during downturns.

- The Tax Institute: support a limited loss carry-back as outlined in the Australia's Future Tax System report.

- Tourism and Transport Forum: strongly support loss carry-back, with a three year carry-back period, as it will provide a cushion against the shocks regularly experienced by this industry (weather and other natural events, transport shocks, etc).

- Tourism Accommodation Australia: support loss carry-back in some form as it will support capital investment in their industry.

- Yarrawa Management Pty Ltd: Broadly support a loss carry-back, with a three year carry-back period, as the horticultural industry have longer peaks and troughs.

8.98 Treasury also intends to consult extensively on the implementation of the measure, and is preparing a Discussion paper to begin its consultation. This will be followed by consultation on exposure drafts as well as separate consultation with the Australian Taxation Office on its administration of the measure.

Conclusion and recommended option

8.99 All the loss carry-back options identified will reduce the bias in the tax system against innovation and investment and will assist businesses in the current economic climate.

8.100 The various options involve trade-offs between the timing and size of the incentive to business, and cost to budget and the administrative feasibility of delivering the measure.

Timing

8.101 Options that start later will reduce the cost, but also delay the benefits to companies considering new innovations and/or investments.

8.102 Treasury expect that the pressures on business from the high terms of trade and multispeed economy will continue and this will result in ongoing calls for assistance from government.

8.103 Sector or firm specific assistance can, depending on the policy design, be counter-productive. While support to a particular sector or firm may save jobs in the short term, in the longer term it can condemn those workers to lower wages and business owners to lower profits. It can also become increasingly costly to government and difficult to quarantine to preferred firms or sectors.

8.104 In contrast economy-wide measures, such as loss carry-back, that address impediments to businesses adapting and changing through supporting sensible investment and risk taking will enhance productivity growth in all sectors of the economy, particularly those currently under pressure.

8.105 Therefore, Treasury supports the design of loss carry-back suggested by the Working Group, but recommends that it commence sooner to maximise the impact on prospective investment.

8.106 For example, under a loss carry-back arrangement that starts from 2012-13 with a $1 million cap, businesses that are currently profitable and paying tax, will know that if they undertake investments in 2012-13 that initially result in a loss, they will get a refund of up to $300,000 of tax they previously paid when they lodge their 2012-13 return.

8.107 A commencement date of 2012-13 will involve challenging legislative and administrative timeframes. However, on the basis that this measure is a high priority, passage of legislation in the winter sittings of 2013 (to enable companies to start claiming loss carry-back after the conclusion of the 2012-13 income year) is possible.

Carry-back Period

8.108 Different carry-back periods will increase or decrease the cost to revenue, but also reduce or increase the benefits to companies.

8.109 Countries that have a loss carry-back arrangement generally limit the carry-back period, often to between one and three years. This reduces the administrative costs and also places a limit on the impact of loss carry-back on government revenues.

8.110 A shorter carry-back period limits the Government's exposure to the revenue effects of loss utilisation as refunds would not be as large during economic downturns. However, it also limits the benefits that

companies can derive from loss carry-back during loss periods, and limits the automatic stabiliser effect.

8.111 Treasury supports an initial carry-back period of one year, moving to a two year period after that. Treasury also notes that once loss carry-back is in place, the carry-back period can be fairly easily amended in response to the economic environment. For example, after the Global Financial Crisis, in an effort to stimulate business activity the United States and the United Kingdom both extended the allowable time period over which losses could be carried back.

Cap

8.112 Different caps will increase or decrease the cost to revenue, but also reduce or increase the benefits to companies. A quantitative cap limits the amount of losses that taxpayers can carry-back against taxes paid in previous periods. Quantitative caps have been used, for example, in the carry-back systems of Germany and the United Kingdom.

8.113 A quantitative cap can also be used to target the benefits of loss carry-back to small and medium sized companies. The lower the cap, the greater the relative benefit of the measure to small and medium sized companies.

8.114 As highlighted in the section on the impact of the various loss carry-back options, under a $1 million cap around 90 per cent of the 'cash' benefit will flow to medium, small and micro businesses. This falls to 65 per cent under a $10 million cap.

Implementation and review

8.115 Amendments to the current tax law will be required to implement this proposal.

8.116 An initial consultation paper will be issued following the 2012-13 Budget. A period of between four and six weeks will be provided for interested members of the public to make a submission on the consultation paper. Meetings with key stakeholders may also occur during the consultation period.

8.117 Responses to the consultation paper will inform any further policy decisions by the Government and the preparation of draft legislation. Subject to Government's overall drafting priorities, the draft legislation could be exposed for public comment by the end of 2012.

8.118 As with the consultation paper, interested members of the public would have between four and six weeks to make a submission on the exposure draft legislation. Meetings with key stakeholders may occur during the consultation period.

8.119 Responses to the draft legislation will determine how quickly the legislation could then be finalised for introduction in the Parliament. However, the implementation process would be undertaken with a view to the legislation being introduced in the first half of 2013.

Miscellaneous amendments

Outline of chapter

9.0 Schedule 7 to this Bill makes a number of miscellaneous amendments to the taxation laws as part of the Government's commitment to uphold the integrity of the taxation system.

Context of amendments

9.1 Amendments to the taxation laws, such as these, are periodically made to correct technical or drafting defects, remove anomalies and correct unintended outcomes in the tax legislation. Progressing such amendments gives priority to the care and maintenance of the tax system, as supported by a 2008 recommendation from the Tax Design Review Panel.

Summary of new law

9.2 These miscellaneous amendments address minor technical deficiencies and legislative uncertainties within several taxation laws.

Detailed explanation of new law

Part 1—Amendments relating to resource rent taxation

Minerals Resource Rent Tax

9.3 The *Minerals Resource Rent Tax Act 2012* (MRRTA 2012) received Royal Assent on 29 March 2012. A number of amendments are needed to correct minor technical errors in the drafting of that Act and associated Acts.

9.4 All references to provisions in paragraphs 9.7 to 9.96 refer to the MRRTA 2012, unless otherwise indicated.

Resource marketing operations

9.5 In working out what part of the sale price of their taxable resources, or things they produced using taxable resources, is attributable to the form and location of the resources at their valuation point (and is therefore mining revenue), miners have to make a number of assumptions (see subsection 30-25(4)). One of those assumptions is that a distinct and separate entity carried on the miner's downstream mining operations, its transformative operations, and its resource marketing operations. That contributes to ensuring that miners ascribe a fair amount to the cost of their operations when working out their mining revenue.

9.6 ***Resource marketing operations*** (see subsection 30-25(7)) is defined to be operations that involve marketing, selling, shipping or delivering the taxable resources. The definition does not mention operations in relation to things produced using the taxable resources even though the assumption about resource marketing operations must also be made in working out the sale price of those things.

9.7 The amendments therefore extend the definition of 'resource marketing operations' to include operations that involve marketing, selling, shipping or delivering things produced using the taxable resources. That ensures that miners ascribe fair values to their resource marketing operations for things produced using taxable resources as well as to those operations for the resources themselves. ***[Schedule 7, item 5, subsection 30-25(7)]***

Recoupments of mining expenditure that has been adjusted

9.8 Mining revenue includes amounts that recoup, or offset, amounts of mining expenditure (section 30-40). The amount included is reduced to reflect the extent to which the original expenditure was included in mining expenditure. However, this does not take into account adjustments made under Division 160.

9.9 Under Division 160, if there is a change in the circumstances affecting the amount of a previous item of mining expenditure, an adjustment may be made so that, in net terms, the correct result is achieved. The amendments ensure that the amount of mining expenditure considered under subsection 30-40(2) is an amount that takes into account any adjustments that have been made under Division 160. Similarly, amendments are made to ensure that the amount of pre-mining expenditure considered under paragraph 40-70(2)(b) and subsection 30-40(2) is an amount that takes into account any adjustments that have been made under Division 160. ***[Schedule 7, item 49, subsections 160-15(5) and (6)]***

9.10 A note is also added to subsection 30-40(2) to explain its interaction with Division 160. ***[Schedule 7, item 6, note in subsection 30-40(2)]***

Treatment of revenue from supplies deemed not to be initial supplies

9.11 The MRRTA 2012 includes some amounts in mining revenue that do not relate to a particular mining revenue event (that is, to a particular supply, export or use of taxable resources). It does this so that amounts received under a 'take or pay' contract are included in mining revenue, even though the supply to which they relate has not yet occurred (or, indeed, might never occur).

9.12 One case where there might not be a particular mining revenue event is where a supply is made by a miner to another miner in the course of a mining venture in which each has a mining project interest. Such supplies are treated as not being initial supplies (see paragraph 30-20(2)(a)) and therefore cannot be mining revenue events (see subsection 30-15(1)). This can mean that each of those miners might have to include an amount in their mining revenue for the same taxable resources. That would be inconsistent with accounting for the full value of the resources at their valuation point, but not more.

9.13 Accordingly, these amendments ensure that an amount is not included in a miner's mining revenue if the reason the amount does not relate to a particular mining revenue event is that it is received for a supply that paragraph 30-20(2)(a) treats as not being an initial supply. ***[Schedule 7, items 7 and 8, subsections 30-55(1) and (2)]***

Example 9.1: Integration agreement

Brian has a coal mining lease adjacent to Anthony's coal mining lease. Brian's lease is estimated to contain about one and a half times the amount of coal that Anthony's lease contains but, for commercial and geological reasons, it makes sense to mine the coal on Anthony's lease first. Therefore, they enter into an agreement under which they agree to mine all the coal on both leases as a single mining venture under a single mine plan. Brian will take 60 per cent of the coal extracted in each year and meet 60 per cent of the costs; Anthony will get the other 40 per cent of the coal and meet the other 40 per cent of the costs.

To compensate Anthony for all the coal initially coming from Anthony's lease, they agree that each will pay $2 for each tonne extracted during the year from the other's lease.

The amounts Brian pays Anthony in the early years of extracting coal from their project will not be mining expenditure because they are private mining royalties (see subsections 35-40(1) and 35-45(2)).

These amounts are not mining revenue for Anthony, even though they do not relate to a particular mining revenue event (because the supplies from Anthony to Brian are treated as not being initial supplies).

Amounts included in expenditure due to changed use of starting base assets

9.14 A miner's mining expenditure is the sum of all the amounts under the MRRTA 2012. While most amounts of mining expenditure will be covered by Subdivision 35-A, some amounts of mining expenditure will arise under other parts of the MRRTA 2012.

9.15 A note at subsection 35-5(1) alerts readers that amounts arising as a result of adjustments under Division 160, specifying that these amounts can also be mining expenditure. However, amounts arising as a result of the changed use of starting base assets may also be mining expenditure and will be taken into account when calculating the sum of all mining expenditure to arrive at the miner's mining expenditure for a mining project interest.

9.16 An amendment is made to the note in subsection 35-5(1) to include a reference to amounts of mining expenditure arising as a result of the changed use of starting base assets under section 165-55. ***[Schedule 7, item 9, note in subsection 35-5(1)]***

9.17 Similarly, an amendment is made to the note in subsection 70-35(1) to include a reference to amounts of pre-mining expenditure arising as a result of the changed use of starting base assets under section 165-55. ***[Schedule 7, item 12, note in subsection 70-35(1)]***

The low-profit offset formula

9.18 Miners are not liable to pay MRRT if their mining profit for a year is under $75 million. This is achieved by way of an offset that reduces their liability to nil if their mining profit is under that amount (see section 45-10).

9.19 To avoid a miner's liability rising from nil to the full amount if its mining profit rises above $75 million by as little as $1, the offset phases-in its liability over the next $50 million in mining profits.

9.20 To phase-in a liability on $75 million in mining profits over a $50 million range, a factor of 3/2 was added to the end of the formula that works out the offset.

9.21 The formula also reduces the offset to account for MRRT allowances for the year (for example, allowances for starting base and State royalties). That ensures that the offset amount does not exceed the

liability the miner would have had after taking those allowances into account.

9.22 Including the 3/2 factor at the end of the formula means that, as well as increasing the phasing-in rate, it also increases how much the offset is reduced because of the miner's allowances. The miner's allowances are not themselves increased, so that increase in the reduction they produce means that the miner's offset can be too low.

9.23 The amendments correct that problem by moving the 3/2 factor so that it only modifies the phasing-in part of the formula, and not also the reduction for the miner's allowances. ***[Schedule 7, item 10, formula in subsection 45-10(1)]***

9.24 Consequential amendments are made to examples that rely on the formula. ***[Schedule 7, items 11 and 65 to 67, examples in subsections 45-10(2) and 190-20(2)]***

Starting base

Definition of 'starting base asset'

9.25 Currently, an asset can be a 'starting base asset' even if it is not held by a miner on 1 July 2012. However, an asset that starts to be held after 1 July 2012 will not have a value that can be depreciated for MRRT purposes. An unintended consequence of this is that the disposal of such an asset could be subject to a starting base adjustment that inappropriately includes an amount in mining revenue.

9.26 Amendments are made to limit the meaning of starting base asset to assets held immediately before 1 July 2012. ***[Schedule 7, item 14, subparagraphs 80-25(3)(b)(i) to (iv)]***

9.27 Further amendments are made to ensure that this change does not inappropriately exclude those rights or interests in a mining project interest that starts to exist on or after 1 July 2012 but originates from a pre-mining project interest that existed before that time. In these cases, the mining project interest is taken to be a continuation of the pre-mining project interest. The effect of this deeming means that the mining project interest is taken to have existed at the time the pre-mining project interest existed and that the rights and interests in the mining project interest are taken to have been held by the entity that held the equivalent rights and interests in the pre-mining project interest. ***[Schedule 7, item 15, subparagraph 80-25(3A)]***

Example 9.2: Mining project interest originating from a pre-mining project interest that existed before 1 July 2012

James holds a pre-mining project interest on 1 July 2012. On 1 July 2013, James starts to have a mining project interest that originates from that pre-mining project interest. Even though the rights and interests that constitute the mining project interest did not exist immediately before 1 July 2012, those rights and interests are taken to have existed for the time that the rights and interests in the pre-mining project interest existed and to have been held by James for the period that he held the rights and interests that constituted the pre-mining project interest.

9.28 Additionally, amendments are made to ensure that interim expenditure that is incurred in relation to a pre-mining project interest can be attributed to the mining project interest that originates from it. ***[Schedule 7, items 21 to 24, subsections 90-45(1), (1A) and (2) and subsection 90-55(5A)]***

Starting base adjustments and recoupments need to take into account reductions in starting base losses

9.29 The amount of a starting base adjustment is reduced to the extent that the decline in value of the asset has been ignored in working out a starting base loss for the mining project interest for that MRRT year or an earlier year. The reduction is calculated using the 'sum of reductions' formula in subsection 165-15(2). However, this formula fails to take account of some of the circumstances in which the decline in value has been ignored in working out a starting base loss.

9.30 Starting base losses are extinguished or prevented from arising in several situations. When a miner decides to combine their interests, they give up the opportunity to realise starting base losses. Similarly, if the miner elects to use the simplified MRRT method, starting base losses are extinguished. Finally, if the suspension day for the mining project interest happens, then starting base losses are also extinguished.

9.31 Amendments are made to section 165-15 to recognise the range of situations where the miner has given up their opportunity or is prevented from realising their starting base losses. ***[Schedule 7, items 50 and 51, subsections 165-15(1) and (2)]***

9.32 Similar to starting base adjustments, if a miner receives an amount for a starting base asset that is not part of a starting base adjustment event, then the base value of the asset is reduced to the extent that there is an economic recoupment of the asset's base value (section 90-65).

9.33 For the same reason that amendments are necessary to the starting base adjustments to account for the declines in value that have been ignored in working out a starting base loss, amendments are made to subsection 90-65 to ensure that the starting base recoupment rules recognise that some of the starting base may not have been realised by the miner. ***[Schedule 7, item 25, subsection 90-65(5)]***

The uplift of starting base losses

9.34 In a later MRRT year, the starting base loss includes any unused starting base loss for the mining project interest for the previous year, increased by an uplift factor. Under the market value approach to valuing the starting base, the uplift factor is based on index numbers that relate to quarters of the MRRT year.

9.35 However, under Division 190, a miner can have an MRRT year that is different from a financial year. That is, the miner is allowed to use a substituted accounting period for MRRT purposes. A consequence of this is that miners can have different uplift factors depending on their MRRT year. This is contrary to the approach taken in the income tax law and may cause unintended compliance and administration costs.

9.36 Amendments are made to the definition of 'uplift factor' in section 80-45(1) to replace 'MRRT year' with 'relevant financial year'. The relevant financial year is either the MRRT year (where the MRRT year is the financial year) or the financial year corresponding to the MRRT year (where the relevant financial year is not the MRRT year). ***[Schedule 7, item 17, paragraph (b) of the definition of 'uplift factor' in subsection 80-45(1)]***

Choosing the look-back method of valuing starting base assets

9.37 A miner can choose to value starting base assets using 'look-back' method. Like other choices about the way to value the starting base, the choice to use the look-back method may need to be made before the 'start time', which is the time at which assets begin to be recognised as 'starting base assets'. While other choices provide for this possibility, amendments are required to ensure that the look-back choice can apply to those assets that are not yet, but may become, starting base assets. ***[Schedule 7, item 56, subsection 180-5(1)]***

Pre-mining profits

9.38 A pre-mining project interest can be assessed on any profit it makes. This is achieved by deeming the pre-mining project interest to be a mining project interest for the purpose of working out an MRRT liability.

9.39 However, pre-mining losses are ordinarily only available to be applied in working out a pre-mining loss allowance if the mining project interest originates from the pre-mining project interest.

9.40 An amendment is made to ensure that the notional mining project interest is taken to originate from the pre-mining project interest, so that any pre-mining losses of the interest can be used to offset against its profit. ***[Schedule 7, item 38, paragraph 140-10(2)(c)]***

Transferred pre-mining losses and combined mining project interests

9.41 When a miner is seeking to transfer a pre-mining loss to or from a combined interest, the pre-mining loss cap may apply in relation to a constituent interest to limit that transfer.

9.42 There is some potential uncertainty as to the interaction between section 115-55 and the rule under which the pre-mining loss cap arises (in section 95-25). Section 115-55 seeks to limit the transfer of a pre-mining loss to or from a combined interest where the transfer would be capped if the interests had not been combined.

9.43 Currently section 115-55 operates on the basis of a pre-mining loss of the combined mining project interest being entirely non-transferable because of such a cap. However, a pre-mining loss cap can operate to prevent the transfer of a *part* of a loss.

9.44 Amendments are made to section 115-55 to limit the transfer of a pre-mining loss to or from a combined project interest *to the extent* that such a loss would have been limited in relation to the constituent interests, as if those constituent interests had not combined. Additionally, amendments are made to ensure that section 115-55 can apply to a pre-mining loss of a pre-mining project interest, in addition to that of a mining project interest. ***[Schedule 7, item 33, subsections 115-55(1) and (2)]***

Transfers and splits

9.45 The effect of transferring a mining project interest is that the mining project interest in the hands of the new miner is taken to be a continuation of the original miner’s interest. Amounts of mining revenue, mining expenditure, royalty credits and allowance components arising in earlier years are all taken to be amounts of the new miner and the new interest.

9.46 Consistent with this ‘continuation’ principle, an amendment is made to provide that where a mining project interest is taken to have been transferred because of the start of a mining venture (under section 120-25) the amount of the pre-mining loss cap (if any) for the original interest also

transfers to the new miner and the new interest. ***[Schedule 7, items 34 and 35, paragraph 120-10(4)(e) and note in subsection 120-10(4)]***

9.47 Similarly, the effect of splitting a mining project interest is that each split interest is taken to be a continuation of part of the original interest (according to a split percentage). Where a split occurs, and the new miner is the same entity as the original miner, an amendment is made to ensure that the amount of the pre-mining loss cap (if any) for the original interest continues to apply to the split interest (to the extent of the split percentage). ***[Schedule 7, item 36, paragraph 125-10(4)(e)]***

9.48 If the new miner is not the same entity as the original miner, a new pre-mining loss cap arises for the new interest under section 95-30 (the pre-mining loss cap). A note is added to notify readers of this outcome. ***[Schedule 7, item 37, note in subsection 125-10(4)]***

9.49 Equivalent amendments are also made to deal with the transfer and split of a pre-mining project interest. A note is also added to notify readers that when a mining project interest originates from a pre-mining project interest, the origination is taken to be a transfer of the interest. ***[Schedule 7, items 39, 40 and 43, paragraph 145-15(2)(e), note in subsection 145-15(2) and paragraph 150-15(2)(e)]***

Additional areas under changed or renewed exploration rights

9.50 Exploration rights are sometimes adjusted or renewed, in the course of which the area of the right can be changed. The MRRTA 2012 provides that if such changes add an additional area, then the additional area is treated as the project area for a separate pre-mining project interest. This ensures that the project area of a pre-mining project interest, to which certain losses are attached, does not expand.

9.51 There is an exception for additional areas that are insignificant. This avoids the need to incur the compliance costs that can be involved in accounting for a separate pre-mining project interest when the addition does not make much difference.

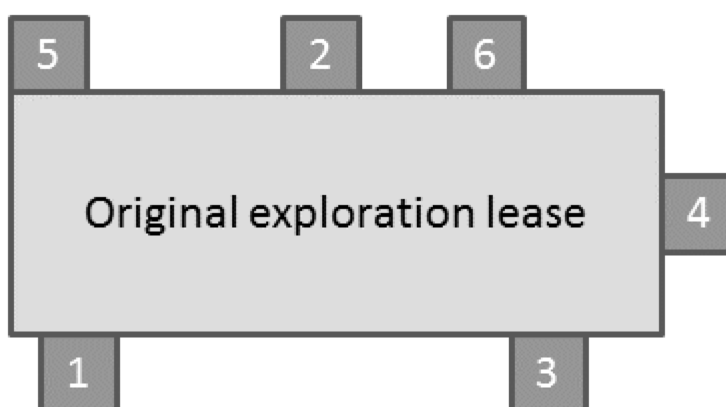
9.52 It is possible that an exploration right might be changed a number of times, each adding an insignificant area that, together, add up to a significant area. The MRRT deals with that by requiring that the significance of each additional area is judged taking into account all previously included insignificant additional areas.

9.53 However, the MRRT does not take into account any such already included area if it has previously prevented another additional area from being included. That produces unintended results because it allows the area of the exploration right to continue to grow even though the additional areas do add up to a significant addition.

9.54 The amendments remove the rule that prevents already added areas being taken into account in deciding whether another additional area is significant if they have already had that effect for an earlier additional area. ***[Schedule 7, item 48, subsection 155-10(3)]***

Example 9.3: Additional areas for an exploration right

Snakeoil Discoveries Pty Ltd is exploring for iron on an exploration lease. On six separate occasions, it sought and was granted minor extensions to the area of its exploration lease. Each of the additional areas is insignificant by itself but any three taken together would be significant.



Additional areas 1 and 2 are insignificant separately and together, so are added to the project area for the original pre-mining project interest. Additional area 3 is also insignificant on its own but, when taken together with areas 1 and 2, would be significant, so becomes the project area for a separate pre-mining project interest.

Additional areas 4 and 5 are again insignificant on their own, or taken together, but would be significant if taken together with already added areas 1 and 2. Under the current law, areas 1 and 2 could not be considered, so areas 4 and 5 would be added. Under the amendments, those areas are not added to the original project area.

Additional area 6 would be excluded under the current law because areas 4 and 5 would be taken into account in deciding that it is significant (even though areas 1 and 2 cannot be taken into account). The same result is achieved under the amendments because areas 1 and 2 are taken into account (areas 3, 4 and 5 are not because they were not added to the project area).

Combining mining project interests

9.55 Generally, a miner cannot combine mining project interests with starting bases unless it had each interest at all times from 2 May 2010 (section 115-35). This ensures that the starting base is not effectively transferrable between mining project interests.

9.56 However, a miner can choose to effectively extinguish its starting base assets in order to combine mining project interests. This is done by reducing the base value of all starting base assets to zero. However, this means that if a miner later sells such a starting base asset, the full sale proceeds will be included in mining revenue (under Division 165) even though the miner did not receive the full benefit of the starting base asset because its base value was reduced to zero.

9.57 Rather than reducing the base value of starting base assets, this amendment provides that the starting base *loss* of the combined interest for the relevant MRRT year or a later MRRT year will be reduced by the declines in value for the year of *any* starting base asset that does not comply with section 115-35. ***[Schedule 7, item 29, paragraph 115-15(2)(b)]***

9.58 Similarly, interests are only allowed to combine if their pre-mining losses comply with section 115-25. That is, combination can only occur if all the pre-mining losses of the constituent interests are fully transferable to each of the other integrated mining project interests. If the pre-mining losses are not available for transfer, the mining project interests can make the choice to cancel the pre-mining losses to enable combination. As noted above, a pre-mining loss cap may prevent the transfer of a *part* of a loss. Amendments are made to allow that part of a loss to be extinguished in order to combine mining project interests. ***[Schedule 7, items 30 to 32, subsection 115-15(3), paragraph 115-25(aa) and paragraph 115-25(b)]***

Counting the 10 million tonnes for the alternative valuation method

9.59 Miners can use a statutory method (the ‘alternative valuation method’) to work out what taxable resource value is to be included in their mining revenue if they and their associates produce under 10 million tonnes of taxable resources in the year.

9.60 The tonnes are measured when the resources have reached the form in which they are to be supplied or exported. However, resources that will be used up instead of being supplied or exported (for example, coal that is burned to produce electricity or iron ore that is turned into steel) are not dealt with under the current law.

9.61 The amendments provide that taxable resources are also measured when they reach the form in which they are to be used to produce something else. The first of the relevant events to occur (supply, export or use) determines which form is appropriate for the particular taxable resources. ***[Schedule 7, item 55, paragraph 175-15(1)(b)]***

Accounting profit for the simplified MRRT method

9.62 The simplified MRRT method allows miners a simple way to work out if they are to be liable for MRRT instead of having to go through the more complex process of working out if they are under the $75 million profit threshold where MRRT starts to be payable.

9.63 One of the tests asks whether the miner's accounting profit for the year (with certain adjustments) is under $75 million. This test relies on the likelihood that someone with an accounting profit under $75 million will have a mining profit well under $75 million.

9.64 However, that reasoning need not be sound where the miner has acquired a mining project interest during the year. The MRRT uses an 'inherited history' approach under which the miner who holds the interest at the end of the year is liable to pay MRRT on the full year's mining profits from the interest. The accounting profits from that interest will however have accrued in some part to the previous holder of the interest. Accordingly, it would be possible for a miner to have accounting profits under $75 million but mining profits well over $75 million.

9.65 The reverse problem is also possible. A miner who transfers a mining project interest during a year will include some part of the profits from the interest in its accounting profit but none of the mining profit. Accordingly, that miner could be denied access to the simplified MRRT method even though its mining profits are well under $75 million.

9.66 The amendments address these problems by adjusting the accounting profit of:

- a miner who *acquires* a mining project interest during a year (and still holds it at the end of the year) to include the profits it would have included had it held the interest for the whole year; and

- a miner who *transfers* a mining project interest during a year (and still does not hold it at the end of the year) to remove the profits it included for the part of the year it held the interest.

The same approach is used for transfers and acquisitions of partial interests in a mining project interest through the splitting rules. ***[Schedule 7, item 68, subsection 200-15(1A)]***

9.67 In most cases, miners will have the information they need to perform these adjustments because miners who transfer mining project interests must provide the transferee with the information it needs to work out its MRRT liabilities (see Division 121 of Schedule 1 to the *Taxation Administration Act 1953* (TAA 1953)). If all that information is not available, it will be necessary to make an estimate of the appropriate adjustment based on the best information that is available.

Starting base returns and assessments

9.68 A miner's annual MRRT returns must contain the information the Commissioner of Taxation (Commissioner) requires, including the miner's mining profit and the MRRT it must pay. If the Commissioner is not satisfied with the return, he or she can require the miner to provide a further or fuller return (see section 117-15 of Schedule 1 to the TAA 1953).

9.69 A miner's starting base return must also contain the information the Commissioner requires, including the base values of each starting base asset and each asset expected to become a starting base asset. However, unlike the annual returns, the Commissioner has no power to require a further or fuller starting base return if he or she is dissatisfied with the original.

9.70 The amendments provide the Commissioner with the same power to require a further starting base return as he or she has in relation to annual MRRT returns. ***[Schedule 7, item 177, subsection 117-20(6) of Schedule 1 to the TAA 1953]***

9.71 The *Minerals Resource Rent Tax (Consequential Amendments and Transitional Provisions) Act 2012* (MRRT(CATP)A 2012) amended the generic assessment provisions to apply them to annual MRRT assessments (see section 155-15 of Schedule 1 to the TAA 1953).

9.72 The MRRT(CATP)A 2012 did not directly amend those provisions to also apply them to MRRT starting base assessments, thus avoiding a permanent amendment to those provisions for what is only a one-off assessment. Instead, this Act applied them to starting base assessments in the same way that they apply to annual MRRT assessments. It did that by deeming the starting base value to be an assessable amount and the starting base return to be a relevant document.

9.73 However, the MRRT(CATP)A 2012 omitted to deem the Commissioner to be the recipient for that document. The amendments correct that omission. ***[Schedule 7, item 74, paragraph 15(1)(c) of Schedule 4 to the MRRT(CATP)A 2012]***

9.74 The values of starting base assets that are assessed by a starting base assessment are to be used to work out the starting base allowances for the whole life of those starting base assets. However, there is no explicit legislative connection between the values assessed in the starting base assessment and the asset values used to work out the allowances.

9.75 The amendments make that connection explicit. They do that by treating the starting base assessment (and therefore the asset values it assesses) as a part of each annual MRRT assessment. ***[Schedule 7, item 75, paragraph 15(3)(a) of Schedule 4 to the MRRT(CATP)A 2012]***

9.76 An annual MRRT assessment cannot be objected to in respect of matters that relate to the starting base assessment. Such objections would instead have to be made to the starting base assessment. ***[Schedule 7, item 75, paragraph 15(3)(b) of Schedule 4 to the MRRT(CATP)A 2012]***

9.77 An annual MRRT assessment can only be amended in relation to matters relating to the starting base assessment to give effect to amendments of the starting base assessment. An annual MRRT assessment can be amended to do that at any time. ***[Schedule 7, item 75, paragraph 15(3)(c) and subitem 15(4) of Schedule 4 to the MRRT(CATP)A 2012]***

9.78 Together, these amendments ensure that the starting base assessment is the only source for the values of starting base assets used in working out a mining project interest's annual starting base allowances. Notes to this effect are added to the body of the MRRTA 2012 to help readers. ***[Schedule 7, items 19 and 20, notes in subsections 90-25(1) and 90-40(1)]***

MRRT instalments

9.79 A miner must pay a quarterly MRRT instalment towards its annual MRRT liability for MRRT if it has mining revenue or pre-mining revenue for the quarter.

9.80 However, the Guide to Division 115 of the TAA 1953 (which deals with MRRT instalments) only refers to mining revenue. The amendments alter this Guide to include a reference to pre-mining revenue. ***[Schedule 7, item 176, section 115-1 of Schedule 1 to the TAA 1953]***

False or misleading statements about MRRT

9.81 Taxpayers are liable to a civil penalty for making statements to the Commissioner (and some others) about taxation laws that are

materially false or misleading (see Division 284 of Schedule 1 to the TAA 1953). The MRRT(CATP)A 2012 amended Division 284 to extend its scope to cover the MRRT.

9.82 To do that, it added references to the 'MRRT law', the 'MRRT payable' and the 'MRRT return'. It omitted to add a reference to the 'MRRT year'. The amendments correct that omission. ***[Schedule 7, item 183, subsection 284-90(1) of Schedule 1 to the TAA 1953 (cell in table item 4, column headed 'In this situation:')]***

9.83 The scope of the provisions relating to false or misleading statements is also extended to cover the PRRT, using the new definition of 'petroleum resource rent tax law'. ***[Schedule 7, items 178 to 182, paragraphs 284-75(2)(a) and (b) of Schedule 1 to the TAA 1953 and table items 3 and 4 in subsection 284-80(1) of Schedule 1 to the TAA 1953]***

Interest on overpayments of MRRT

9.84 The *Taxation (Interest on Overpayments and Early Payments) Act 1983* (TIOEPA 1983) provides for taxpayers to be paid interest on certain overpayments of tax. This Act was amended by the MRRT(CATP)A 2012 to extend it to cover MRRT amounts.

9.85 It was extended to apply to 'assessed MRRT' but the meaning of that term was extended to include MRRT instalments and the general interest charge payable on MRRT and MRRT instalments. The extension to cover MRRT instalments was unnecessary because the interest is payable on the primary MRRT liability and factors in the payment of instalments in working out the amount of the interest (see subsections 9(2) and (3) of the TIOEPA 1983). Therefore, the amendments remove the specific inclusion of MRRT instalments. ***[Schedule 7, item 185, subsection 3C(2) of the TIOEPA 1983]***

9.86 The amendments also make clear that amending an assessment to reduce a liability for assessed MRRT is a decision to which the TIOEPA 1983 applies. That ensures that miners can be eligible for the interest on overpayments covered by Part III of that Act. ***[Schedule 7, item 184, subsection 3(1) of the TIOEPA 1983, paragraph (d) of the definition of 'decision to which this Act applies']***

9.87 The amendments extend the current application of the TIOEPA 1983 to 'BAS provisions' to include the MRRTA 2012, the *Petroleum Resource Rent Tax Assessment Act 1987* (PRRTAA 1987), and Division 115 of Schedule 1 to the TAA 1953 (which covers MRRT instalments). It does that by also applying it to 'resource rent tax amounts', which are defined to mean those debits and credit arising under the MRRT law or the PRRT law other than under BAS provisions. ***[Schedule 7, items 3, 4, 167, 168 and 186 to 193, subsection 995-1(1) of the Income Tax Assessment Tax 1997 (ITAA 1997) (definitions of 'resource rent tax amount' and***

'resource rent tax provisions'), paragraph 8AAZLG(1)(b) and subsection 8AAZLH(1) of the TAA 1953, and heading in section 12AA, paragraph 12AA(a), note in section 12AA, paragraph 12AB(a), note in section 12AB, paragraph 12AC(b), note in section 12AC and definition of 'resource rent tax amount' in section 12AF of the TIOEPA 1983]

9.88 That extension means that interest can be payable to a miner on those MRRT amounts if they have been paid into an RBA (running balance account) of the miner and are refunded more than 14 days after the first opportunity for the refund (see Part IIIAA of the TIOEPA 1983).

9.89 It also means that the Commissioner is able to retain those MRRT amounts in an RBA (rather than refunding them) until the miner provides any required notification and nominates a financial institution account, if one is required (see sections 8AAZLG and 8AAZLH of the TAA 1953).

9.90 For the purpose of applying section 8AAZLH of the TAA 1953 in relation to the amounts that have been allocated to the RBA in relation to primary tax debts arising under any of the resource rent tax provisions, an amendment is made to include a new transitional provision to allow the Commissioner to use the existing details of taxpayers, even if they were not in the prescribed form. This transitional amendment ensures that taxpayers that have already provided their details to the ATO do not have to do so again. ***[Schedule 7, item 169, application of subsection 8AAZLH(2) of the TAA 1953]***

Substituted accounting periods

9.91 Only a miner can have a substituted accounting period under the MRRT. However, there are entities that have pre-mining project interests that may also be using substituted accounting periods.

9.92 Amendments are made to sections 190-1, 190-5, 190-10 and 190-15 to extend the use of a substituted accounting period to entities such as explorers. The words 'a miner' are omitted and replaced with 'entity or entities'. ***[Schedule 7, items 57 to 64 and 73, sections 190-1, 190-5, 190-10 and 190-15 of the MRRTA 2012 and paragraph 10(a) of Schedule 4 to the MRRT(CATP)A 2012]***

Clarifying ambiguities and correcting references

9.93 Some of the amendments remove ambiguities and referencing errors by making minor changes to the text of the MRRTA 2012:

- The first ensures that a starting base asset relates to the mining project interest on which it is used to carry on upstream mining operations rather than to some other mining project interest. ***[Schedule 7, item 13, subsection 80-25(1)]***

- The second clarifies that the declines in values of starting base assets, that are used to work out a starting base loss, are the declines of the year the loss relates to, not the year in which the loss is worked out. ***[Schedule 7, item 16, subsection 80-40(1)]***

- Corrections to cross-references between provisions. ***[Schedule 7, items 69 to 71, subsections 215-10(2), 255-20(1) and (2) and definition of 'MRRT year' in section 300-1]***

- An amendment is made to paragraph 80-50(1)(b) to improve the clarity of the paragraph, specifying that the starting base losses for the mining project interest for the year, not in the year, are applied in the order specified in subsection (4). ***[Schedule 7, item 18, paragraph 80-50(1)(b)]***

- Section 95-20 refers to a miner having a mining project interest. This is inconsistent with the wider language of the Act. An amendment is made to substitute 'has' with 'holds'. ***[Schedule 7, item 26, paragraph 95-20(2)(a)]***

- An amendment is made to improve the clarity of subsection 95-25(1). The words 'under that section' are inserted after 'cannot be applied'. The amendment ensures that it is clear that the section being referred to is section 95-20. ***[Schedule 7, item 27, subsection 95-25(1)]***

- 'Entity' is a defined term under the MRRTA 2012 and so should appear with an asterisk beside it. An amendment is made to include an asterisk in paragraphs 95-30(1)(a) and (2)(a). ***[Schedule 7, item 28, paragraphs 95-30(1)(a) and (2)(a)]***

- An amendment is made to correct an error at note 2 in subsection 150-30(2). 'Mining project transfer' is replaced with 'pre-mining project transfer'. ***[Schedule 7, item 47, note 2 in subsection 150-30(2)]***

- Where there is property transferred from one explorer to another as part of a pre-mining project transfer or split, special rules apply to ensure that no amount is included in the original explorer's pre-mining revenue or in the new explorer's pre-mining expenditure. Amendments are made to ensure that the deeming rules that achieve this outcome refer to all the relevant rules on which they rely, and to correct a mislabelled subsection heading. ***[Schedule 7, items 41, 42 and 44 to 46, subsections 145-20(2) and (3), heading in subsection 150-15(4) and subsections 150-20(2) and (3)]***

- Starting base adjustments that arise when a starting base asset is sold or disposed of can be expressed as a negative amount. When a negative starting base adjustment is included in mining revenue it is included as a positive amount that increases mining revenue. Similarly, when a negative starting base adjustment reduces a starting base loss the amount of the loss is reduced by the absolute value of the adjustment. Amendments are made to remove any ambiguity about the relationship between these positive and negative amounts. ***[Schedule 7, items 52 to 54, subsections 165-25(3), 165-30(1) and 165-30(2) and paragraph 165-30(2)(c)]***

Administration of the MRRT(CATP)A 2012

9.94 The Commissioner is given the general administration of Schedule 4 to the MRRT(CATP)A 2012. This Schedule has ongoing operation in relation to starting base assessments and some other transitional rules. The amendments ensure that the Commissioner has the necessary authority to administer those provisions in the same way that he or she administers other taxation laws. The amendments also ensure that Schedule 4 meets the definition of a 'taxation law', and is subject to the normal administrative provisions that apply to all taxation laws (such as administrative penalties for misleading the Commissioner). ***[Schedule 7, item 72, item 1A of Schedule 4 to the MRRT(CATP)A 2012]***

Petroleum Resource Rent Tax

9.95 The *Petroleum Resource Rent Tax Act 1987* (PRRTAA 1987) was amended by the *Petroleum Resource Rent Tax Assessment Amendment Act 2012*, which received Royal Assent on 29 March 2012. A number of amendments are needed to correct minor technical errors in the drafting of the PRRTAA 1987 and associated Acts.

9.96 All references to provisions in paragraphs 9.99 to 9.247 refer to the PRRTAA 1987, unless otherwise indicated.

Title

9.97 The long title of the Act is amended to reflect the existence of the three imposition acts that were enacted as part of the PRRT extension. ***[Schedule 7, item 76, title]***

Definition of 'acquisition'

9.98 The term 'acquisition' is used throughout the PRRTAA 1987 in relation to the determination of look-back starting base amounts in limited circumstances where interests in petroleum projects have been directly or

indirectly acquired (Schedule 2, clauses 18 and 19). It is also used in the definition of 'market value' (section 2).

9.99 Section 2 of the PRRTAA 1987 defines 'acquisition' to take its meaning as given by section 195-1 of the *A New Tax System (Goods and Services Tax) Act 1999* (GST Act). The definition in the GST Act generally refers to the acquisition of goods, services and rights. This definition is different from the ordinary meaning of 'acquisition' which is more appropriate when referring to the acquisition or part acquisition of projects and companies in relation to the look-back provisions.

9.100 The definition of 'acquisition' is amended to specify that in clauses 18 and 19 of Schedule 2 to the PRRTAA 1987, the definition of 'acquisition' has the meaning given by subclauses 18(7) and 18(8) of that Schedule, and in all other instances it takes the meaning given by section 195-1 of the GST Act. ***[Schedule 7, item 77, definition of 'acquisition' in section 2]***

Definition of 'created'

9.101 The term 'created' (see section 2) is a defined term which is used throughout the PRRTAA 1987 in relation to the creation of consolidated groups and multiple entry consolidated groups (MEC groups). The definition of created, depending on what type of group is being referred to, takes its meaning from various sections of the ITAA 1997.

9.102 The references to sections 703-15 and 719-25 of the ITAA 1997 within the definition of 'created' are incorrect.

9.103 The definition of 'created' is amended to correctly refer to the meaning given by subsection 995-1 of the ITAA 1997. ***[Schedule 7, item 78, definition of 'created' in section 2]***

Definition of notional tax amount

9.104 The term 'notional tax amount' is added to the list of definitions. The definition of 'notional tax amount' has the meaning given by section 97 of the Act. ***[Schedule 7, item 79, definition of 'notional tax amount' in section 2]***

Relationships between licences and permits

Holding an interest

9.105 Part II, section 4A of the PRRTAA 1987 details the circumstances under which a person is taken to have held an interest in a petroleum project, including a combined project (see subsection 4A(3)).

9.106 The current provisions do not operate correctly where an already combined project is combined with another project.

9.107 Amendments are made to Paragraphs 4A(3)(b) and 4A(3)(c) to ensure that the particular time at which a person is taken to have held an interest in relation to a combined project is the particular time when the earliest permit was granted. ***[Schedule 7, item 81, paragraphs 4A(3)(b)and (c)]***

Example 9.4: Holding an interest in a combined petroleum project

> Exploration permits WA-1, WA-2 and WA-3 were granted to Morris Petroleum in January, June and December 2013 respectively. Production licences PL-A, PL-B and PL-C correspond to exploration permits WA-1, WA-2, and WA-3 respectively. PL-A came into existence in 2014, PL-B came into existence in 2016 and PL-C came into existence in 2018.
>
> In 2016, Morris Petroleum applies to combine projects A and B into combined project AB. In 2018, Morris Petroleum applies to combine AB with project C to form combined project ABC.
>
> Morris Petroleum is taken to have held an interest in Project ABC from January 2013 onwards — the time when the earliest exploration permit was granted.

9.108 Additionally, minor amendments are made to subsections 4A(1), 4A(3) and 4A(4) and sections 4B and 4C to improve clarity. The words ‘in relation to’ are substituted with ‘in, or in relation to’ ***[Schedule 7, items 80, 82 and 84, subsections 4A(1), (3) and (4) and sections 4B and 4C]***

9.109 Similarly, subsection 4A(4) is amended with the words ‘any of’ inserted after the words ‘recovered from’. ***[Schedule 7, item 83, subsection 4A(4)]***

Translation of amounts into Australian currency

9.110 Part II, section 10 of the PRRTAA 1987 provides for the translation of an amount in foreign currency into Australian currency for the purposes of the Act. Subsection 10(4) details the translation rule with regard to an amount of deductible expenditure.

9.111 Deductible expenditure amounts are derived from ***eligible real expenditure*** amounts (see section 2). Consequently, amendments are made to substitute the references to ‘deductible expenditure’ in the heading in subsection 10(4) and paragraph 10(4)(a) with ‘eligible real expenditure’. ***[Schedule 7, items 85 and 86, heading in subsection 10(4) and paragraph 10(4)(a)]***

Combining PRRT Projects

9.112 Part IV, Division 20 of the PRRTAA 1987 sets out the rules relating to the combining of petroleum projects so that they are treated as a single project for the PRRT purposes. Petroleum projects may be combined within the qualifying period, subject to the approval of the Resources Minister.

9.113 Generally, the qualifying period in which the Resources Minister may issue a combination certificate is 90 days after the latter of either the time the licence came into force, the commencement of the Act, or, if the licence relates to an onshore petroleum project, the start of 1 January 2013 (see subsection 20(2)).

9.114 Amendments are made to the qualifying period in relation to onshore petroleum projects to provide persons new to the regime with additional time to lodge combination applications. Under the amendments, the commencement of the 90 day qualifying period still begins at the start of 1 January 2013 in cases where the project licence was granted on or after 1 July 2012, but is extended for those projects whose production licence was granted prior to 1 July 2012 to the start of 1 July 2013. ***[Schedule 7, item 87, subparagraphs 20(2)(a)(iii) and (iv)]***

Deductible expenditure

Resource tax expenditure

9.115 Resource tax expenditure is deductible against assessable receipts from a petroleum project if it is incurred in relation to the project (see section 35C).

9.116 Subsection 35C(5), which outlines how excess resource tax expenditure in the assessable year is to be uplifted, currently makes reference to subsections 35C(1), 35C(2) and 35C(3), when only subsections 35C(1) and 35C(2) are relevant.

9.117 Subsection 35C(5) is amended to remove the reference to subsection 35C(3). ***[Schedule 7, item 88, subsection 35C(5)]***

Starting base expenditure

9.118 Under the PRRT, a production licence must be in existence for a petroleum project to exist (see section 19). Subsection 19(1B) specifies that there is a single petroleum project for all production licences that are related to the 'North West Shelf exploration permits' (see section 2), that are in force from time to time.

9.119 As the North West Shelf exploration permits and/or retention leases derived from them are not treated as part of the North West Shelf project (only production licences are treated as part of the project), each exploration permit or retention lease that existed as at 1 May 2010 may have its own starting base amount from 1 July 2012 (see Schedule 2, clause 6). These starting base amounts only 'crystallise' to starting base expenditure when a production licence has been derived from the relevant permit or lease area.

9.120 Subsection 35E is amended to include a new subsection, subsection 35E(1A), to allow for the starting base expenditure of new production licences derived from the North West Shelf exploration permits to be added to the total starting base expenditure of the North West Shelf project. That starting base expenditure is taken to be incurred on the first day of the starting base financial year. ***[Schedule 7, item 89, subsections 35E(1A) and (1B)]***

9.121 A minor amendment is also made to subsection 35E to correct a wording error. ***[Schedule 7, item 90, subsection 35E(4)]***

Effect of procuring the carrying on of operations etc. by others

9.122 Part V, Division 3, Section 41 of the PRRTAA 1987 deals with the deductibility of expenditure in circumstances where project activities or operations are undertaken by a person other than the taxpayer in exchange for payment.

9.123 Broadly, where a liability to make such a payment is incurred, the expenditure is deemed to be incurred by the taxpayer, rather than by the person providing the operations. However, under subsection 41(2), this does not apply in cases where the person is providing the operations as part of the processing of 'internal petroleum' or 'external petroleum' (see section 2), in which case the expenditure is instead deductible under paragraph 37(1)(c) or 38(1)(d).

9.124 An amendment is made to clarify the operation of subsection 41(2). The amendment limits the reference to 'a petroleum project other than the project to which the operations, facilities, or other things referred to in subsection (1) relate', to external petroleum only, noting that there can only be one project in relation to internal petroleum. ***[Schedule 7, item 91, subsection 41(2)]***

Timing of incurred expenditure

9.125 Part V, Division 3, subsection 45(2) of the PRRTAA 1987 defines the time from which eligible real expenditure can be incurred in relation to onshore petroleum projects.

9.126 In relation to onshore petroleum projects (or the exploration permit or retention lease from which it is derived) that existed prior to 2 May 2010, paragraph 45(2)(a) provides that eligible real expenditure may be incurred at any time on or after the relevant starting base day as given by the table in subsection 45(5) for the person's interest in a project.

9.127 Paragraph 45(2)(b) provides that for onshore petroleum projects that came into existence on or after 2 May 2010, eligible real expenditure may be incurred from that time.

9.128 Amendments are made to address an ambiguity as to which paragraph applies in circumstances where a production licence is carved out of an exploration permit that existed prior to 2 May 2010, as both paragraphs could potentially apply.

9.129 The amendment makes clear that where paragraph 45(2)(a) can apply, it takes precedence over paragraph 45(2)(b). ***[Schedule 7, item 92, paragraph 45(2)(b)]***

9.130 The table in subsection 45(5) specifies the starting base days for interests in onshore projects or in the North West Shelf, which depend on the starting base valuation method chosen in relation to the project interest. The starting base day sets the time from which eligible real expenditure can be incurred in relation to the interest (subsections 45(2) and 45(4)).

9.131 Where a person acquired an interest in an onshore project between 1 July 2007 and 2 May 2010, the person may take account of the expenditure incurred in acquiring the interest under the look back valuation approach (Schedule 2, clauses 18 and 19). The time at which an acquisition is taken to have occurred is the time when the transaction was first entered into that, when complete had the effect of transferring the interest, or, in the case of an indirect acquisition, the time at which the agreement to enter into the transaction was entered into (Schedule 2, subclauses 18(7) and 18(8)).

9.132 Table item 2 in subsection 45(5) specifies the starting base day in such cases to be 'the day on which the acquisition occurred'. As an acquisition may occur (for the purposes of Schedule 2) prior to the acquisition actually being completed, an acquirer could unintentionally benefit from project expenditure incurred by the vendor between the time of acquisition and the time the acquisition was completed, being both taken into account in the acquisition price, and deductible as eligible real expenditure under subsection 45(5).

9.133 To address this issue, an amendment is made to the wording for the starting base day in table item 2 of subsection 45(5) to clarify that the

starting base day is the day the interest was transferred, and not an earlier date when an agreement to transfer the interest was reached. ***[Schedule 7, item 93, table item 2 in subsection 45(5)]***

Example 9.5: Acquisition of an interest in a project

> On 1 September 2007, Alex Co entered into an agreement with Ben Co to acquire a 10 per cent interest in project Boom (an onshore petroleum project) for $10 million. Alex Co. recognized the acquisition in its accounts on 31 December 2007 when it started to hold the interest. The starting base day for Alex Co's interest in the project is 31 December 2007 and any expenditure incurred by Alex Co from that date may be eligible real expenditure in relation to the project. Expenditure incurred in relation to the interest by Ben Co prior to that date would be expenditure incurred prior to the starting base day for Alex Co's interest in the project. Therefore, it cannot give rise to deductible expenditure of Alex Co by the application of section 48A.

9.134 For the avoidance of doubt, the amendments also clarify that, in circumstances where a person incurred eligible real expenditure in relation to an onshore petroleum project during the 'look-back period', and then transfers all or part of the interest to another person who chooses to use the look-back starting base approach (see Schedule 2, clause 3), that person is able to claim the eligible real expenditure incurred by the first person during the look-back period.

9.135 The new subsection 45(8) clarifies that eligible real expenditure that a person may incur in relation to a petroleum project may include expenditure that a person is taken to have incurred in relation to the project, before or after the commencement of that section, because of section 48 and 48A. ***[Schedule 7, item 94, subsection 45(8)]***

9.136 A person who acquired an interest between 1 July 2007 and 2 May 2010 and chooses the look back method as the starting base valuation approach (see Schedule 2, clause 3), is able to take account of the cost of the acquisition via that method (Schedule 2, clauses 18 and 19), with project expenditure incurred after the starting base day deductible subject to the normal PRRT rules (subsection 45(2)).

9.137 Where such an interest or part of the interest is subsequently transferred to another person following the choice of valuation approach, the acquisition expenditure is transferred with the interest through the operation of the PRRT transfer provisions (sections 48 or 48A).

9.138 In cases where the transfer of the interest occurs during the interim period (between 2 May 2010 and 1 July 2012), the second acquirer holding the interest is able to choose a starting base valuation approach. Amendments are made to clarify that, where the look-back

approach is chosen, clauses 18 and 19 of Schedule 2 apply, with the second acquirer able to take account of the expenditure incurred by the first acquirer in acquiring the interest. ***[Schedule 7, items 153, 154 and 161, subclauses 18(1), (3), (4) and (5) and paragraph 19(1)(b) of Schedule 2]***

Effect of certain transactions

Transfer of entire entitlement to assessable receipts and transfer on or after 1 July 1993 of part of entitlement to assessable receipts

9.139 Part V, Division 5, sections 48 and 48A of the PRRTAA 1987 detail the effect of a holder of an interest in a petroleum project transferring their interest in whole or in part to another person.

9.140 Subsections 48(1) and 48A(5) specify that the purchaser of an entitlement to assessable receipts shall be taken to have derived any assessable receipts, deductible expenditure and exploration expenditure incurred by the vendor in relation to the project.

9.141 Subparagraph 48(1)(a)(ib) is intended to ensure that, in circumstances where an interest in an exploration licence or retention lease with an associated starting base amount (which has not yet 'crystallised' into starting base expenditure) is transferred, the starting base amount transfers to the purchaser with the interest. It does this be specifying that, where section 35E (starting base expenditure) does not apply in relation to the year in which the transaction occurred, and the look-back method was not the valuation approach used by the vendor), the purchaser is taken to have incurred starting base expenditure equal to the vendor's starting base amount. Subparagraph 48A(5)(ca) operates in the same manner in relation to part transfer of an interests.

9.142 However, where an interest is transferred in the same financial year as the year in which the production licence is granted, subparagraphs 48(1)(a)(ib) and 48A(5)(ca) would not operate correctly as section 35E would apply to the interest in that year. As a consequence, the deeming function performed by these paragraphs would not apply.

Example 9.6: Problems with the transfer of starting base expenditure

> WPS Exploration holds an exploration permit over an area in the Joseph Bonaparte Basin which is transferred Eel Petroleum in a financial year. Eel Petroleum is granted a production licence in the same financial year. Section 35E applies to the interest in that year.
>
> Because section 35E applies to that interest in that year, the transfer provisions relating to starting base expenditure cannot apply for that year.

9.143 To address this issue, amendments are made to subparagraphs 48(1)(a)(ib) and 48A(5)(ca)(i) to remove the reference to 'the financial year in which the transaction was entered into' and 'in relation to the transfer year' respectively. These references are replaced by a reference to 'immediately before the transfer time'. ***[Schedule 7, items 95 and 98, subparagraphs 48(1)(a)(ib) and 48A(5)(ca)(i)]***

Transfer notices

9.144 The PRRTAA 1987 requires that the vendor of an interest provide the purchaser with a transfer notice within 60 days of the transfer time (see sections 48(3) and 48A(11)) after 1 July 2012. Amendments in this Bill remove this requirement transfers relating to onshore project or North West Shelf project interests made prior to 1 July 2012. ***[Schedule 7, item 94, subsection 45(9)]***

9.145 Further amendments are made as a transitional measure to provide onshore taxpayers and the North West Shelf project with more time to lodge their transfer notices if they have transfers that occur between 1 July 2012 and 30 June 2013. Taxpayers who have transactions in this period will have until 31 August 2013 to lodge their transfer notice. ***[Schedule 7, items 96, 97, 99 and 100, subsections 48(3) and 48A(11)]***

Anti-avoidance

Non arm's length receipts

9.146 Section 57 of the PRRTAA 1987 allows for the Commissioner to deem the amount of assessable receipts in the case of non-arm's length transactions. However, subsection 57(3) excludes the application of the section to receipts determined under subparagraph 24(1)(d)(i).

9.147 Paragraph 24(1)(d) specifies that, where any sales gas produced from petroleum from the project that becomes or became an excluded commodity by virtue of being sold, the assessable receipt is the amount worked out in accordance with the regulations. The intention of the exemption is to carve out the situation where the PRRTAA 1987 Regulations apply to a non-arm's length sale. Therefore, all subparagraphs of paragraph 24(1)(d) are relevant, not just the first subparagraph as currently drafted.

9.148 Amendments are made to subsection 57(3) to replace the reference to subparagraph 24(1)(d)(i) with a reference to paragraph 24(1)(d). ***[Schedule 7, item 101, subsection 57(3)]***

Functional currency

Translation rule — deductible expenditure

9.149 Division 7 of Part V of the PRRTAA 1987 allows taxpayers whose accounts are kept solely or predominantly in a particular currency to calculate their taxable profits and certain other amounts by reference to that functional currency. The Division provides a series of basic translation rules for situations where dealings occur that are not in the applicable functional currency.

9.150 Section 58F of the PRRTAA 1987 provides the translation rule for deductible expenditure. However, deductible expenditure is a derivation of 'eligible real expenditure' (see section 2). Amendments are made to substitute the references to 'deductible expenditure' with 'eligible real expenditure' in the heading in section 58F and paragraph 58F(a). ***[Schedule 7, items 103 and 104, heading in subsection 58F and paragraph 58F(a)]***

Certain expenditure incurred on the day when section 58B election takes effect

9.151 Section 58K and 58M specify categories of expenditure that should be converted to functional currency. These provisions also apply to the new categories of expenditure. That is, resource tax expenditure, acquired exploration expenditure, starting base expenditure and the starting base amount. These provisions are amended to include references to these new expenditure categories. ***[Schedule 7, items 111, 113, 114, 116, 118 and 119, heading in subsection 58K(1), paragraph 58K(1)(b), subparagraphs 58K(1)(b)(iv) to (vii), heading in subsection 58M(1), paragraph 58M(1)(c) and subparagraphs 58M(1)(c)(iv) to(vii)]***

9.152 Minor amendments are made to refer to a 'financial year' instead of a 'year of tax'. This is because a taxpayer who holds an interest in exploration permits as well as production licences will have a year of tax for the latter but not for the former. ***[Schedule 7, items 102, 105 to 110, 112, 115, 117, 120 and 121, subsections 58B(1) and (4) to (6), subsections 58C(1) and (2), subsection 58D(1), subsections 58J(1) and (3), paragraphs 58J(4)(b) and (c), subsection 58J(4), paragraphs 58J(5)(b) and (c), subsection 58J(5), subsections 58J(6) to (11), paragraphs 58K(1)(a) and (b), subsection 58K(2), subsections 58L(1) and (4), paragraphs 58M(1)(a) to (c) and subsections 58M(1) and (2)]***

Consolidated groups

Choice to consolidate

9.153 Section 58N allows the head company of a consolidated group or MEC group to consolidate for PRRT purposes if they choose. Subsection 58N(2) specifies, however, that the choice cannot be made if a

notice has not been given to the Commissioner under sections 703-58 or 719-76 of the ITAA 1997 in relation to the group.

9.154 Section 703-58 relates to the provision of the notice of the choice to consolidate for consolidated groups. Section 719-76 relates to the notice of the choice to consolidate for MEC groups. However, where a MEC group is formed as a result of a special conversion of a consolidated group in accordance with section 719-40, the notification of the conversion is required by section 719-78.

9.155 Amendments are made to subsection 58N(2) to replace the reference to section 719-76 with a reference to sections 719-76 or 719-78. This will allow MEC groups that come into existence as a result of a special conversion event to consolidate for PRRT purposes. ***[Schedule 7, item 122, subsection 58N(2)]***

Single entity rule

9.156 Under section 58P, subsidiary members of a consolidated group, or MEC group, that has consolidated for PRRT purposes, are treated as being parts of the group's head company (rather than separate entities) for the purposes of working out interests in projects, determining assessable receipts and deductible expenditure in relation to projects, and working out PRRT payable (see subsection 58P(2)).

9.157 Section 58P enables group companies which are participants in the same onshore project (including combined projects) to submit a single PRRT return, rather than a PRRT return for each group company interest in the project, without altering the broader operation of the PRRT law.

9.158 These amendments repeal and replace section 58P to clarify that the operation of the PRRT consolidation provisions extends only to those group companies holding onshore project interests, and not to group companies which do not. That is, only subsidiary members that hold an interest in the same petroleum project will be taken to be parts of the head company in relation to the project. ***[Schedule 7, item 123, section 58P]***

9.159 A transfer between members of the income tax consolidated group will only be disregarded if it involves a particular petroleum project and the members involved in the transaction hold an interest in the project.

Example 9.7: Sale of coal seam gas to an aggregator

Rich Coal, Quality Coal and Super Liquids are members of an income tax consolidated group whose head company (Fantastic Coal) has made a valid choice to consolidate for PRRT purposes. Rich Coal and

Quality Coal sell gas recovered from the Prize onshore petroleum project (Prize) to Super Liquids.

Pursuant to amended section 58P, Rich Coal and Quality Coal are taken to be parts of the head company for the Prize project but Super Liquids is not taken to be a part of the head company for this project.

Rich Coal and Quality Coal are subsidiary members of the PRRT consolidated group in relation to the Prize project. Any transaction relating to the Prize project between Super Liquids and Rich Coal or Super liquids and Quality Coal, including the sale of gas by Rich Coal and Quality Coal to Super Liquids will not be disregarded.

However, transactions between Rich Coal and Quality Coal in relation to the Prize project will be disregarded as they are both part of the head company (Fantastic Coal) for the purposes of the Prize project.

9.160 Since the PRRT is applied on a project basis, section 58P will consolidate the various project interests held by members of an income tax consolidated group on a project basis. This may result in there being a number of PRRT consolidated groups within the one income tax consolidated group.

Example 9.8: PRRT consolidated group in a wholly owned group

Assume the facts as stated in Example 1.7. The head company of the group acquires Gem Ltd that holds an interest in the Emerald onshore petroleum project. The PRRT consolidated group for the Prize project consists of the head company (Fantastic Coal) and Rich Coal and Quality Coal as subsidiary members. While, the PRRT consolidated group for the Emerald project consists of the head company (Fantastic Coal) and Gem Ltd as the subsidiary member.

Creation of new PRRT consolidated groups and cessation of groups

9.161 Since section 58P applies on a project basis, a new PRRT consolidated group may come into existence when an interest in an onshore project is acquired or a production licence is granted. A new PRRT consolidated group may also come into existence if a member of the income tax consolidated group acquires an entity that holds an interest in an onshore petroleum project.

9.162 Conversely, a PRRT consolidated group in relation to a project ceases to exist when the relevant onshore production licence is surrendered or the group ceases to hold an interest in that project.

Changes to the membership of a PRRT consolidated group

9.163 The membership of a PRRT consolidated group in relation to a petroleum project may change if a member of the income tax consolidated group acquires an interest in the project from an existing member of the PRRT consolidated group. A disposal of an interest in a project may also affect the membership of the PRRT consolidated group in relation to that project.

Example 9.9: Change in the membership of a PRRT consolidated groups

> Assume the facts as stated in Example 1.7. Quality Coal transfers all of its interest in the Prize project to Super Liquids. The PRRT consolidated group for the Prize project now consists of the head company (Fantastic Coal), Rich Coal and Super Liquids. After the transfer, any transactions between Super Liquids and Quality Coal in relation to the Prize project will be disregarded. Further, transactions between Quality Coal and Rich Coal will not be disregarded for PRRT purposes.

9.164 The new section 58P is also modified to include reference to provision head company interests, and clarifies the single entity rule applies to the calculation of PRRT instalments and the calculation of a tax credit in respect of closing-down expenditure.

Interests taken to be transferred to head company on joining

9.165 When a group consolidates for PRRT purposes, the onshore petroleum project interests of the group's subsidiary members are treated as having been notionally transferred to the head company or provisional head company of the group (section 58Q). This transfer is facilitated by the PRRT's existing transfer rules, described in Part V, Division 5, section 48.

9.166 The application of section 48 ensures any assessable receipts derived or any deductible expenditure incurred by these subsidiary members during the financial year are treated as being derived or incurred (as the case may be) by the head company. Any PRRT instalments paid by the subsidiary members during the financial year are also taken to have been paid by the head company of the group.

9.167 Section 48 requires that the transferee must give consideration to the transferor for the entitlement and the property (paragraph 48(1A)(c)). However, in the case of PRRT consolidation, there will be no consideration when the subsidiary members notionally transfer their entitlements to the head company.

9.168 Amendments are made to section 58Q to deem the head company or provisional head company to have given the consideration required by paragraph 48(1A)(c) at the transfer time to allow the transfer rules to operate as intended. ***[Schedule 7, item 124, section 58Q]***

9.169 A similar amendment is made to ensure that the transfer rules are able to operate in cases where a subsidiary member leaves a PRRT consolidated group and the entitlement to assessable receipts is notionally transferred from the head company or provisional head company back to the member. Subsection 58R(1) is amended to deem the subsidiary member to have given the consideration required by paragraph 48(1A)(c) at the transfer time. Subsection 58R(2) is also amended to deem the subsidiary member to have given the consideration required by paragraph 48A(11)(b) at the transfer time if the transfer is a partial transfer. ***[Schedule 7, items 125 to 128, subsections 58R(1) and (2)]***

Interests taken to be transferred when combined with offshore interests

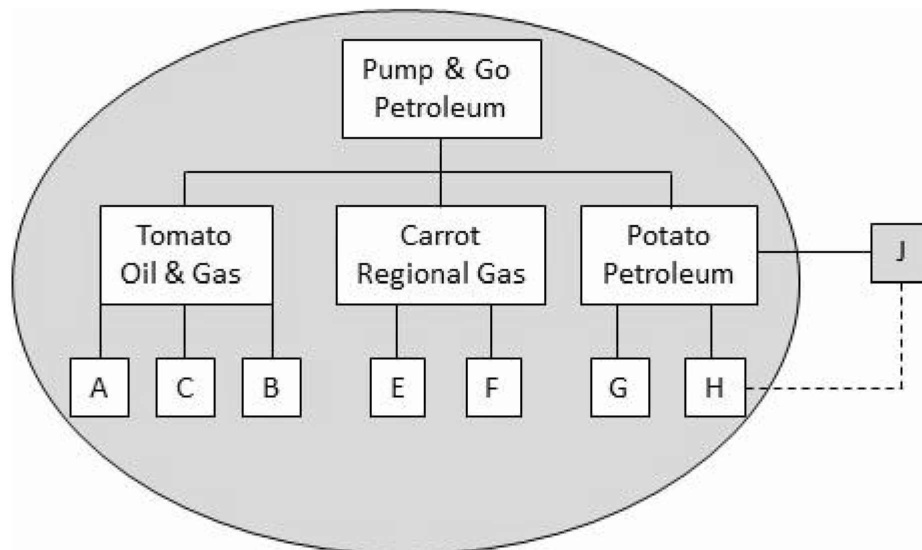
9.170 An onshore project is able to be combined with an offshore project provided the combination criteria in Part IV, section 20 are satisfied and the onshore project did not exist prior to 1 July 2012 (see subsection 20(1A)). Where the combination of an onshore and offshore project is approved by the Resources Minister, the combined project is treated as an offshore project.

9.171 In such circumstances, an issue arises in relation to the PRRT consolidation regime, which can only apply in relation to onshore petroleum project interests (paragraphs 58P(1)(b) and 58P(2)(a)).

9.172 Section 58R provides that onshore project interests held by a subsidiary group member are taken to transfer back to them from the head company in circumstances where the subsidiary member stops being part of the PRRT consolidated group. While this section will operate to correctly transfer the interest in the combined ‘offshore’ project from the head company back to the member company where the only onshore project interest held by the member relates to the onshore project that was combined, it will not operate where they have another onshore project interest and remain part of the PRRT consolidated group.

9.173 A new section, section 58RA, is added to provide that, in circumstances where an onshore project in which a subsidiary group member holds an interest is combined with an offshore, the interest in the combined ‘offshore’ project is notionally transferred back to the subsidiary member and must be accounted for by them and not the head company or provisional head company. ***[Schedule 7, item 129, section 58RA]***

Example 9.10: Interests taken to be transferred when combined with offshore interests



Pump & Go Petroleum is the head company of a consolidated group for PRRT purposes. Tomato Oil & Gas, Carrot Regional Gas and Potato Petroleum are subsidiary members of Pump & Go Petroleum.

Tomato Oil and Gas has an interest in onshore petroleum projects A, B and C. Carrot Regional Gas has an interest in onshore petroleum projects E and F. Potato Petroleum has an interest in onshore petroleum projects G and H. Project H did not exist prior to 1 July 2012.

On 16 March 2014, Potato Petroleum develops an offshore project, Project J. Potato Petroleum wishes to combine Project J and Project H. The Resources Minister accepts Potato Petroleum's combination request because the company satisfies the relevant combination criteria. The interest in project H is no longer treated as an interest held by Pump & Go Petroleum, and Potato Petroleum must separately account for it as part of the combined (offshore) project. The interest in project G is still treated as being held by Pump & Go Petroleum due to the application of the single entity rule in section 58P.

Effect of a change of head company or provisional head company of a MEC group

9.174 The PRRTAA 1987 does not use an asterisk for referencing defined terms. Instead, defined terms are referenced using bold type. Amendments are made to remove the asterisk before the term 'MEC group' in subparagraphs 58U(1)(a)(i) and 58U(1)(b)(i) and paragraph 58V(1)(a). ***[Schedule 7, items 130 to 132, subparagraphs 58U(1)(a)(i), 58U(1)(b)(i) and paragraph 58V(1)(a)]***

Effect of group conversions involving MEC groups

9.175 Section 58V of the PRRTAA 1987 applies in circumstances where a consolidated group is formed from a MEC group or vice versa. The section is intended to ensure that a choice to consolidate for PRRT purposes made before such a conversion continues to have effect after the conversion, with the 'new group' head company inheriting the history of things done by the former head company or provisional head company prior to the conversion.

9.176 However, section 58V does not operate correctly where there is a need for inheritance of the history from a consolidated group to a provisional head company of a MEC group.

9.177 Amendments are made to section 58V to remedy this situation. A new subsection 58V(3) is added, specifying that all references in paragraph 58V(2)(c) to the head company of the new group are taken to be a reference to the head company or provisional head company of the new group. ***[Schedule 7, item 133, subsection 58V(3)]***

Subsidiary members that are trusts

9.178 The term 'person', used in Division 8 of Part V of the PRRTAA 1987 which deals with consolidated groups, does not encompass trusts. This is problematic for the operation of the single entity rule (see section 58P) as a trust may be a subsidiary member of a consolidated group or MEC group.

9.179 Amendments are made to Division 8 of Part V to include a new section that deems a subsidiary member of a consolidated group or MEC group that is a trust, to be a person for the purposes of the Division. ***[Schedule 7, item 134, section 58W]***

9.180 An amendment is also made to carve out the trustee of a trust that is a subsidiary member of a consolidated group or MEC group, from the requirements imposed under section 109 of the PRRTAA 1987 which specifies that the agent (the trustee or 'representative') who derives assessable receipts in relation to a petroleum project is liable to pay the PRRT. ***[Schedule 7, item 139, subsection 109(5)]***

Collection by instalments

Interpretation

9.181 Section 93 of the PRRTAA 1987 specifies that, in section 85 (unpaid tax and charges), section 92 (person in receipt or control of money of a non-resident) and section 109 (agents and trustees) the term 'tax' (section 2) includes an instalment of tax payable under the Division.

9.182 Amendments are made to subsection 93(1) to include a reference to section 58P to ensure that the instalment provisions of Division 2 also apply to the tax payable by a PRRT consolidated group. ***[Schedule 7, item 135, subsection 93(1)]***

Notional tax amount

9.183 Section 97 of the PRRTAA 1987 sets out how notional tax amounts payable by instalment are determined. Paragraph 97(1A)(b) ensures that relevant deductible expenditures carried forward on the first day of the year of tax are only included in the calculation of the notional tax amount to the extent of their instalment percentages. The meaning of instalment percentage is defined in section 2.

9.184 Amendments are made to paragraph 97(1A)(b) to include references to subsections 35C(5), 35D(3), 35D(4) and 35E(3), which deal with the new deductible expenditure categories added to the PRRT from 1 July 2012 — that is, resource tax expenditure, acquired exploration expenditure and starting base expenditure. These deductible expenditures also need to be taken into account in the calculation of the notional tax amount for an instalment of tax. ***[Schedule 7, item 136, paragraph 97(1A)(b)]***

Notional tax amounts and sales gas

9.185 In situations where assessable petroleum receipts have been determined under subparagraph 24(1)(d)(i) or paragraph 24(1)(e), subsection 97(1AA) requires that the amounts so determined are to be excluded from determining the notional tax amounts and that, instead, the amount worked out in accordance with the PRRT 1987 regulations in respect of those assessable petroleum receipts is to be included.

9.186 An amendment is made to subsection 97(1AA) to replace the reference to subparagraph 24(1)(d)(i) with a reference to paragraph 24(1)(d) as the entire paragraph is relevant to subsection 97(1AA). The amendment also clarifies that notional tax amounts related to assessable receipts determined under paragraph 24(1)(f) are also determined in accordance with the regulations to the PRRTA 1987. ***[Schedule 7, item 137, subsection 97(1AA)]***

Amendments to Schedule 1 **to the** ***PRRTAA 1987 — provisions relating to incurring and transferring exploration expenditure on or after 1 July 1990***

Offshore information notices

9.187 Under section 264A of the *Income Tax Assessment Act 1936* (ITAA 1936), the Commissioner may serve an offshore information notice on a taxpayer, provided the Commissioner has reason to believe that

information from a source outside Australia is relevant to the assessment of a taxpayer. An offshore information notice requires that the taxpayer, within the period specified in the notice, provide the relevant information to the Commissioner.

9.188 An amendment is made to Part X of the PRRTAA 1987 to allow the Commissioner to issue offshore information notices in respect of PRRT in order to align the Commissioner's powers in respect of issuing offshore information notices with that of the MRRT (provided by section 353-17 of the MRRT(CATP)A 2012). ***[Schedule 7, item 138, section 108A]***

Defined terms

9.189 Clause 1 of Schedule 1 to the PRRTAA 1987 sets out the defined terms of the Schedule. Clause 1 includes a definition for 'relevant pre-commencement day' in relation to petroleum projects. The relevant pre-commencement day is used to determine the augmented bond rate expenditure year.

9.190 Under the definition, for petroleum projects that are *not* combined projects, and are *not* the Bass Strait project or the North West Shelf project, the relevant pre-commencement day is the day occurring five years before the earlier of either the day specified on the production licence notice, or the day the production licence was issued.

9.191 For combined projects, the Bass Strait project or the North West Shelf project, the definition specifies the relevant pre-commencement day to be the day occurring five years before the earlier of either the earliest day specified on the production licence notice in relation to the pre-combination project, or the earliest day the production licence notice was issued in relation to the pre-combination project. However, the Bass Strait project and the North West Shelf project are *not* combined projects but are instead defined under section 19 of the PRRTAA 1987 so there would be no pre-combination project, and consequently the relevant pre-commencement day cannot be determined.

9.192 Amendments are made to the definition of relevant pre-commencement day to address this anomaly. For the Bass Strait project and the North West Shelf project, the relevant pre-commencement day is the day occurring five years before the earlier of either the earliest day specified in a production licence notice in relation to the project, or the earliest day a production licence notice was issue in relation to the project. ***[Schedule 7, items 140 and 141, clause 1 of Schedule 1]***

Person must have held interest in relation to transferring entity and receiving project

9.193 Part 5 of Schedule 1 to the PRRTAA 1987 sets out the rules relating to the transfer of exploration expenditure. Clause 22 specifies that, in order to transfer expenditure a person must have held an interest in relation to both the transferring entity and the receiving project from the beginning of the financial year in which the expenditure was incurred to the end of the transfer year. This clause, together with clause 31, outlines the PRRT's common ownership test.

9.194 In 2006, clause 31 was repealed and replaced to allow unused exploration expenditure to be available for transfer between projects within group companies where there is continuity of group ownership of the transferring and receiving projects. These amendments were designed to allow internal corporate restructuring of a wholly-owned group to occur without losing the ability to transfer unused exploration expenditure.

9.195 However, clause 22 was not amended as part of the 2006 amendments, resulting in an anomaly whereby the PRRTAA 1987 gives rise to different outcomes dependent upon the way in which group restructures are undertaken. In essence, where a company owns multiple petroleum projects and incurs transferable exploration expenditure on those projects, the transferability of expenditure between said projects will only be preserved in the event that the restructure results in each of those projects being held by separate legal entities within the wholly owned group. However, where the restructure results in two or more projects being held by a single company such projects cease to be able to transfer exploration amongst themselves.

9.196 To address this anomaly, subclause 22(5) is inserted to allow the transfer of exploration expenditure between projects of a company where companies that have held those projects have at all times been group companies in relation to each other. However, subclause 22(5) does not apply unless, at the time of the transfer, the person holds an interest in *both* the transferring entity and the receiving project. ***[Schedule 7, item 142, subclause 22(5) of Schedule 1]***

Example 9.11: Group restructures and transferring exploration expenditure

Decay Resources is the head company of a consolidated group. Cobra Petroleum and Hero Oil are group companies of Decay Resources. Both group companies have operations in the Carnarvon Basin. Cobra Petroleum owns an exploration permit, EXP 100, and a petroleum project, Newport. Hero Oil owns a petroleum project, Finger Twist.

In January 2014, Cobra Petroleum incurs $6 million of exploration expenditure in EXP-100. Its Newport Project is making a loss and the exploration expenditure cannot be used by the project. In February 2014, Hero Oil and Cobra Petroleum merge and become a new entity within the Decay Resources group. The new entity is called Academy Petroleum.

Academy Petroleum is able to deduct the unused exploration expenditure from its EXP 100 permit against its profit making Finger Twist project.

General rules for transferring exploration expenditure between groups

9.197 Prior to the 2006 amendments, which repealed and replaced clause 31 in its entirety, the former subclause 31(2AB) allowed a company to transfer to other companies in the wholly-owned group, any unused exploration expenditures from a *relinquished* permit.

9.198 The new clause 31 does not contain a similar provision, meaning that a company could not transfer to other group companies the exploration expenditure associated with a relinquished permit as no company in the group will hold an interest in the transferring entity at the time of transfer.

9.199 Amendments are made to allow a company that has relinquished an exploration permit to transfer that exploration expenditure to another company in the same group. ***[Schedule 7, item 143, subclause 31(2A) of Schedule 1]***

Amendments to Schedule 2 of the PRRTAA 1987 — starting base for onshore petroleum projects and the North West Shelf project

Choosing a valuation approach

9.200 Amendments are made to paragraph 3(1)(b) of Schedule 2 to align the referencing used in this section with the terminology used in Part II, Section 4 of the PRRTAA 1987. The amendments replace references to 'projects' and 'interests in projects' being derived from an exploration permit or retention lease, and with references to the related production licence. ***[Schedule 7, item 144, paragraph 3(1)(b) of Schedule 2]***

9.201 Similar amendments are also made to align the terminology in paragraphs 5(b) and 7(3)(b), subparagraph 10(1)(a)(ii) and paragraph 15(5)(b). ***[Schedule 7, items 145, 146, 148 and 152, paragraphs 5(b) and 7(3)(b), subparagraph 10(1)(a)(ii) and paragraph 15(5)(b) of Schedule 2]***

The amount of the starting base amount

9.202 An amendment is made to correct a referencing error in the note in subclause 7(3). The reference to the 'subsection' is replaced with 'subclause'. ***[Schedule 7, item 147, note in subclause 7(3) of Schedule 2]***

Meaning of starting base asset

9.203 Clause 10 of Schedule 2 to the PRRTAA 1987 defines what constitutes a starting base asset for the purposes of determining starting base amounts in relation to those production licences (or retention leases and exploration permits from which a production licence is derived) which existed just before 2 May 2010.

9.204 Subclause 10(4) makes clear that starting base assets related to a person's interest in the retention lease or exploration permit become those of the first production licence derived from the lease or permit area, and cannot also be starting base assets of another project derived from the remaining area of the permit or lease in the future.

9.205 However, ambiguity arises as to where the starting base assets are assigned in circumstances where a retention lease is carved out of an exploration permit and the exploration permit continues to exist. Clarity on where the starting base assets are assigned in this situation is important if there is a transfer of the exploration permit (from which a retention lease was carved out) to another person, as both the vendor and the purchaser will be interested in which interest receives the starting base. In this case the starting base amount is assigned to the retention lease.

9.206 To better clarify the assignment of starting base assets (and consequently starting base amounts), subclause 10(4) is repealed and replaced, and the new subclause 10(4A) is inserted. ***[Schedule 7, item 151, subclauses 10(4) and 10(4A) of Schedule 2]***

9.207 These provisions only apply where there is one right in relation to an area as at 2 May 2010, but more than one right as at 30 June 2012.

Example 9.12: Assignment of starting base amounts

In August 2006, Bunting Petroleum was granted an onshore exploration permit over an area in the Gippsland Basin.

On 2 May 2010, Bunting Petroleum had several assets associated with the exploration permit area.

In October 2010, Bunting Petroleum took out a retention lease over a smaller area within the exploration permit area. The starting base assets of the exploration permit area are transferred to the retention lease.

In February 2011, Bunting Petroleum sells the exploration permit to Tepper Resources. No starting base assets transfer with the exploration permit.

9.208 Amendments are also made to correct referencing errors in clause 10. References to 'section' and 'subsection' are replaced with 'clause' and 'subclause' respectively. ***[Schedule 7, items 149 and 150, subparagraph 10(2)(b)(i) and subclause 10(3) of Schedule 2]***

Expenditure incurred in acquiring interests in petroleum projects

9.209 Part 4 of Schedule 2 to the PRRTAA 1987 deals with how the cost of acquiring project interests is treated under the look-back starting base approach, and operates in conjunction with section 45 of the PRRTAA 1987 which deals with the timing of expenditure.

9.210 Broadly, where a person has acquired an interest in a petroleum project between 1 July 2007 and 2 May 2010, and the person chooses the look-back approach in relation to the interest, they will be taken to have incurred 'acquisition expenditure' (see Schedule 2, clause 18). A project interest can be acquired directly (a direct acquisition), or via the acquisition of the company holding the interest (an indirect acquisition).

9.211 In circumstances where a person acquired an interest in a petroleum project after 1 July 2007, but sold part of that interest before 1 May 2010 and they choose the look-back approach, the person should only be entitled to take into account the *remaining* interest that they hold at 2 May 2010 in determining their acquisition expenditure, not the full amount of the consideration paid for the original acquisition.

Example 9.13: Interests acquired and partially sold during the look-back period

Fuller Resources acquires a 30 per cent interest in the Carpentaria Project in July 2007 for $30 million. In January 2010, Fuller Resources sells a 10 per cent interest in the project to County Electricity for $15 million.

Fuller Resources is entitled to $20 million under the look-back approach (two thirds of the original consideration).

9.212 Amendments are made to clause 18 to clarify that a person is only permitted to take into account the proportion of the consideration that relates to the interest that they hold at 2 May 2010. ***[Schedule 7, item 155, subclause 18(5A) of Schedule 2]***

9.213 Amendments are also made to subclause 18(7) to clarify that where a direct acquisition of a petroleum project occurs incrementally, the

person is able to take into account the total cost of acquisition in relation to the interest they held at 2 May 2010, and not just the cost of the first acquisition. ***[Schedule 7, item 158, subclause 18(7) of Schedule 2]***

9.214 A similar amendment is made to subclause 18(8) to ensure that a person is able to take into account the total cost of acquisition in the case of an incremental indirect acquisition of a petroleum project. ***[Schedule 7, item 160, paragraph 18(8)(c) of Schedule 2]***

Example 9.14: Incremental acquisitions

Liverpool Petroleum wishes to acquire a stake in Project A and Project B. Projects A and B are currently owned by Manchester Petroleum. Liverpool Petroleum can choose to acquire Manchester Petroleum and indirectly acquire the projects as a result, or it can directly acquire the projects from Manchester Petroleum.

Liverpool Petroleum decides that it will acquire its stake in the projects directly, rather than acquiring them via the acquisition of Manchester Petroleum.

In July 2007, Liverpool Petroleum pays $5 million for a 10 per cent stake in each of Projects A and B. In January 2010, Liverpool acquires a further 30 per cent in each of Projects A and B for $15 million.

Assuming that the acquisition expenditure was wholly for assets that reflect project activities, Liverpool Petroleum's total acquisition expenditure is $20 million.

9.215 Subparagraph 18(8)(b)(i) is also amended to improve clarity. The amendment removes the reference to 'first entered into' and includes the addition of the word 'company' after the word 'first'. ***[Schedule 7, item 159, subparagraph 18(8)(b)(i) of Schedule 2]***

9.216 Minor amendments are made to subclause 18(6) of Schedule 2 to correct a date error — '20 June 2007' is replaced with '1 July 2007'. ***[Schedule 7, items 156 and 157, heading in subclause 18(6) and paragraphs 18(6)(a) and (b) of Schedule 2]***

Acquired exploration expenditure amounts

9.217 Where a taxpayer has acquisition expenditure under Part 4 of Schedule 2 to the PRRTAA 1987, the person is taken to have an acquired exploration expenditure amount equal to the amount of acquisition expenditure allocated to exploration and evaluation assets as recorded in a financial report audited and prepared in accordance with accounting standards (clause 19).

9.218 Subclause 19(2) requires that the financial report must have been prepared in accordance with the accounting standards within the meaning of the *Corporations Act 2001*, which references Australian accounting standards.

9.219 An amendment is made to allow taxpayers to also use a financial report that has been prepared in accordance with the International Financial Reporting Standard 6 (or another international standard prescribed by the regulations), which is the basis for the Australian accounting standard relating to the treatment of exploration and evaluation assets. ***[Schedule 7, item 162, paragraph 19(2)(b) of Schedule 2]***

9.220 Where there is an indirect acquisition of a project interest, the acquisition date is taken to occur when the transaction (or the agreement to enter into the transaction) was first entered into which, when complete, had the effect of the company holding the interest becoming a subsidiary of the acquiring company (subparagraphs 18(8)(b)(i) and (ii)).

9.221 An issue may arise in circumstances where an acquisition is not completed in the same financial year as the acquisition date. This is because the financial report that must be relied upon in relation to determining acquisition expenditure must relate to the period that includes the day of the acquisition (subclause 19(2)), yet the acquisition will generally only recognised for accounting purposes when control passes to the acquirer. This will normally occur when the transaction is complete, not when the transaction was first entered into or an agreement to enter into the transaction was first entered into.

9.222 To address this, an amendment is made to paragraph 19(2)(c) to replace 'the day of acquisition' with 'the day the acquisition of the interest, or the acquisition of the company, was recognised in accordance with accounting standards'. ***[Schedule 7, item 163, paragraph 19(2)(c) of Schedule 2]***

Assessable property receipts

9.223 The new clause 21A in Schedule 2 of the PRRTAA 1987 addresses an anomaly in relation to the interaction of starting base amounts and assessable property receipts.

9.224 Onshore exploration permits and retention leases that existed as at 2 May 2010 can receive a starting base amount to recognise existing investment in the petroleum project. This amount 'crystallises' and becomes eligible real expenditure in the form of starting base expenditure, when a production licence is granted in relation to the permit or lease.

9.225 Where the value of a starting base asset was included in a starting base amount and the asset is sold after 1 July 2012, the PRRTAA 1987 does not reduce the starting base expenditure by the value of the asset. Instead, the receipt from its sale is intended to be recognised as an assessable property receipt under section 27.

9.226 However, this section does not operate correctly in relation to a post-1 July 2012 disposal of a starting base asset related to an exploration permit or retention lease. This is because paragraph 27(1)(a) requires eligible real expenditure of a capital nature to have been incurred in relation to the asset. This requirement will not be met in relation to the disposal of a starting base asset of an exploration permit or retention lease, because the starting base amount will not yet have 'crystallised' to be eligible real expenditure.

9.227 Without limiting section 27, clause 21A triggers on the disposal, loss or destruction of starting base assets by the person holding the interest after 1 July 2012, deeming eligible real expenditure of a capital nature to have been incurred by the person in relation to the asset to the extent it was used in carrying on the project activities. ***[Schedule 7, item 164 clause 21A of Schedule 2]***

Example 9.15: Disposals of starting base assets

On 2 May 2010, Brokenshire Resources has an interest in an onshore petroleum exploration permit in the Surat Basin. Brokenshire Resources has a starting base amount in relation to its interest in the project.

In October 2012, Brokenshire Resources makes a valid starting base election, selecting 'market value' as their starting base valuation method.

In March 2013, Brokenshire Resources sells two drill rigs used in the exploration of the permit area, the value of which were included in determining the starting base amount. As no production licence has yet been granted, eligible real expenditure is deemed to have been incurred through section 21A.

The consideration received from the sale of the drilling rigs is included as an assessable property receipt under section 27 of the PRRTAA 1987.

Starting base assessments

9.228 Section 66 of the PRRTAA 1987 outlines under what circumstances a person who is dissatisfied with their PRRT assessment may object to the assessment.

9.229 Under subsection 66(1), a person who is dissatisfied with an assessment may make an objection in the manner set out in Part IVC of the TAA 1953. However, a person cannot object against a nil assessment, unless they are seeking an increase in their tax liability (subsection 66(2)).

9.230 Clause 23 of Schedule 2 to the PRRTAA 1987 deems a 'starting base assessment' to be an assessment for the purposes of section 66. However, subsection 66(2) is not relevant to starting base assessments as there is no tax payable in relation to a starting base assessment, which only provides an amount that is submitted to be the person's starting base amount. Paragraph 23(4)(b) is amended to refer only to subsection 66(1). ***[Schedule 7, item 165, paragraph 23(4)(b) of Schedule 2]***

9.231 In addition, amendments are also made to subclause 23(5) to ensure that where a transfer in ownership occurs, future owners have rights relating to the starting base.

9.232 Subclause 23(4) deems the starting base assessment to be an assessment for the purposes of amendment of assessments, allowing objections and limiting the period of amendment to 4 years after notice of assessment is given (see section 67). Subclause 23(5) specifies that, while a starting base assessment is taken to be part of the person's general assessment, objections to general assessments by the taxpayer, and any amendment to general assessments, cannot relate to matters to which the starting base assessment relates.

9.233 Where a person transfers all or part of an interest for which a starting base assessment has been received, the right to request an amendment to an assessment, object against an assessment and the right to protection against amendment should transfer from the vendor to the purchaser from the date of purchase of the interest.

9.234 Subclause 23 is amended to insert the new subclause 23(5A), which specifies that, where a transfer of an interest occurs, the purchaser inherits the assessment rights and provided for under subclauses 23(4) and (5). The starting base rights may transfer multiple times to new purchasers. ***[Schedule 7, item 166, subclauses 23(5A) and (5B) of Schedule 2]***

PRRT consequential amendments

Liability for payment of tax where head company fails to pay on time

9.235 Division 721 of the ITAA 1997 relates to the payment of liabilities of the head company of a consolidated group in circumstances where the head company fails to meet all of those liabilities by the time they become due and payable.

9.236 Subsection 721-10(5) of the ITAA 1997 specifies that the members of a consolidated group or MEC group only become jointly and severally liable for PRRT liabilities that are listed at items 95, 100, 105 and 110 of the table if the group has chosen to consolidate for PRRT purposes. Companies are also jointly and severally liable to pay the general interest charge at item 40 of the table.

9.237 An amendment is made to subsection 721-10(5) of the ITAA 1997 to specify that where a consolidation choice has been made under section 58N of the PRRTAA 1987, all the members of the consolidated group are jointly and severally liable for those PRRT liabilities listed. If there is a provisional head company, subsection 721-10(5) of the ITAA 1997 also applies to the tax related liabilities of the provisional head company. Similar amendments are made to subsection 721-10(4) of the ITAA 1997. ***[Schedule 7, item 1, subsections 721-10(4), (5) and (6) of the ITAA 1997]***

Definitions in subsection 995-1(1) of the ITAA 1997

9.238 An amendment is made to subsection 995-1(1) of the ITAA 1997 to insert a definition of 'petroleum resource rent tax law'. The new definition is included to allow the administrative provisions in the tax law to apply to the PRRT consistently with its application to the MRRT. ***[Schedule 7, item 2, definition of 'petroleum resource rent tax law' in subsection 995-1(1) of the ITAA 1997]***

Objections, reviews and appeals

9.239 An amendment is made to section 14ZQ of the TAA 1953 to insert a definition for 'starting base assessment' into the general interpretive provisions. This addition facilitates other amendments to ensure that a person can make an objection against their starting base assessment. ***[Schedule 7, item 170, definition of 'starting base assessment' in section 14ZQ of the TAA 1953]***

9.240 Sections 14ZZK and 14ZZO of the TAA 1953 place the burden of proof on the taxpayer that an assessment is excessive. However, this is not relevant to starting base assessments, which do not establish a liability to pay an amount of tax payable.

9.241 Amendments are made to subparagraphs 14ZZK(b)(i) and (ii) and 14ZZO(b)(i) and (ii) of the TAA 1953 to refer to an assessment as being 'incorrect' rather than 'excessive' in the case of starting base assessments. This is similar to the treatment of franking assessments. ***[Schedule 7, item 171, subparagraphs 14ZZK(b)(i) and (ii) and 14ZZO(b)(i) and (ii) of the TAA 1953]***

Collection and recovery of income tax and other liabilities

9.242 Amendments are made to Schedule 1 to the TAA 1953 to align the treatment of withholding tax related to withholding from natural resource payments with that of the MRRT.

9.243 Entities that are foreign residents may have PRRT withheld from natural resource payments — that is, payments that are of a nature described in section 12-325 of Schedule 1 to the TAA 1953. ***[Schedule 7, item 173, paragraphs 12-330(1)(b) and 12-335(2)(a) of Schedule 1 to the TAA 1953]***

9.244 If an entity receives a natural resource payment from which an amount has been withheld for PRRT purposes, then the recipient of the natural resource payment is entitled to a credit equal to the amount withheld. ***[Schedule 7, items 174 and 175, note in subsection 18-10(3) and section 18-55 of Schedule 1 to the TAA 1953]***

9.245 'Petroleum resource rent tax' is also inserted in the objects of the PAYG withholding provisions dealing with the crediting of withheld amounts. ***[Schedule 7, item 172, paragraph 11-1(h) of Schedule 1 to the TAA 1953]***

Part 2—General amendments

Correcting a typographical error — dollar signs

Table 9.1: Amendments to the *A New Tax System (Medicare Levy Surcharge—Fringe Benefits) Act 1999*

Provisions being amended	*What the amendments do*
A New Tax System (Medicare Levy Surcharge—Fringe Benefits) Act 1999 15(1)(c) 16(2)(c) ***[Schedule 7, item 194]***	Insert the missing dollar sign before all references to '20,542'.

Updating references to a repealed provision

Table 9.2: Amendments to the *Crimes (Taxation Offences) Act 1980, New Business Tax System (Former Subsidiary Tax Imposition) Act 1999*, and *Taxation (Interest on Overpayments and Early Payments) Act 1983*

Provisions being amended	***What the amendments do***
Crimes (Taxation Offences) Act 1980 3(1) (paragraph (b) of the definition of 'income tax') ***[Schedule 7, item 195]*** ***New Business Tax System (Former Subsidiary Tax Imposition) Act 1999*** 4(2)(a) 4(2)(b) ***[Schedule 7, item 222]*** ***Taxation (Interest on Overpayments and Early Payments) Act 1983*** 3C(1) (table item 15 of the definition of 'relevant tax') 8A(1)(a)(vb) ***[Schedule 7, items 226 and 227]***	Ensure that remaining references in the tax laws to section 170AA of the ITAA 1936 refer to it as former section 170AA, as this provision has been repealed.

Relocating a Schedule

Table 9.3: Amendment to the *Excise Tariff Amendment (Condensate) Act 2011*

Provision being amended	***What the amendment does***
Excise Tariff Amendment (Condensate) Act 2011 Item 4 of Schedule 1 ***[Schedule 7, item 196]***	Relocates the new section 7 of the *Excise Tariff Act 1921* so it appears before the Schedule to this Act.

Removing a redundant definition

Table 9.4: Amendment to the *Fringe Benefits Tax Assessment Act 1986*

Provision being amended	***What the amendment does***
Fringe Benefits Tax Assessment Act 1986 136(1) (definition of 'Chief Executive Centrelink') ***[Schedule 7, item 197]***	Removes the definition of 'Chief Executive Centrelink' as it is no longer utilised by the Act. This amendment gives effect to a suggestion made via **TIES (issue 0003-2012)**.

Removing asterisks

Table 9.5: Amendments to the *Fuel Tax Act 2006*

Provisions being amended	***What the amendments do***
Fuel Tax Act 2006 43-10(11) 43-10(12) ***[Schedule 7, item 198]***	Remove asterisks which precede the expression 'road user charge', as this is not a defined term.

Contact lenses and the medical expenses rebate

Table 9.6: Amendments to the *Income Tax Assessment Act 1936*

Provisions being amended	***What the amendments do***
Income Tax Assessment Act 1936 159P(4) (subparagraphs (g)(i) and (ii) of the definition of 'medical expenses') ***[Schedule 7, item 199]***	Clarify that, consistent with existing administrative practice, payments relating to contact lenses are treated the same way as payments relating to spectacles for the purposes of the medical expenses rebate. These amendments give effect to a suggestion made via **TIES (issue 0010-2012)**.

Removing an unnecessary term

Table 9.7: Amendments to the *Income Tax Assessment Act 1997*

Provisions being amended	***What the amendments do***
Income Tax Assessment Act 1997 10-5 (table item headed 'balancing adjustment')	Remove all references to the term 'industrial property' in the assessable income Guide material, as this term is no longer relevant to assessable income.

Provisions being amended	What the amendments do
10-5 (table item headed 'industrial property') 10-5 (table item headed 'residual value') ***[Schedule 7, items 200 to 202]***	

Renumbering a note

Table 9.8: Amendment to the *Income Tax Assessment Act 1997*

Provision being amended	*What the amendment does*
Income Tax Assessment Act 1997 102-20 (Note 5, second occurring) ***[Schedule 7, item 203]***	Corrects the erroneously numbered second occurrence of 'Note 5', to 'Note 6'.

Amending the definition of 'tax preferred end user' in the ITAA 1997

9.246 This amendment will bring Australian residents within the definition of 'tax preferred end user' to the extent that they carry on a business at, or through, a permanent establishment in a foreign jurisdiction. In this regard the words 'to the extent' perform an important function in excising the foreign business operations of the entity. The Australian resident is then a 'tax preferred end user' in respect of those activities, in much the same way that a foreign resident is a 'tax preferred end user' in respect of all of its activities. Conversely, the entity will not be a 'tax preferred end user' in respect of its other business activities (for example its Australian business operations). ***[Schedule 7, item 204, paragraph 250-55(b)]***

9.247 The modification to the definition in this way is justified by the fact that income derived at or through the permanent establishment will generally be non-assessable non-exempt income because of section 23AH of the ITAA 1936. Appropriately, the modified definition will not apply to the entity that is subject to the Division's operation, because the 'end user' must be another entity.

9.248 Other than minor amendments to paragraph 250-155(3)(b) and subparagraphs 250-60(1)(b)(i) and (ii) of the ITAA 1997 to include the word 'business' after references to 'foreign resident', the modified definition will interact appropriately with the other provisions of Division 250 without any further modifications. For example, because the relevant part of the Australian resident's activities are picked up in the modified definition, subsections 250-60(1) and 250-60(2) will then

operate appropriately. These subsections set out when an asset will be put to a 'tax preferred use' and will only apply to the assets used by the Australian resident in carrying on a business at or through its foreign permanent establishment. ***[Schedule 7, items 205 to 207, subparagraphs 250-60(1)(b)(ii) and 250-60(2)(b)(ii), and paragraph 250-155(3)(b)]***

9.249 Because a permanent establishment is not a distinct legal entity (it is simply a part of an entity), even where the Australian resident has exclusive use of the asset it may be possible for the asset to be used both in the business the entity carries on at or through the foreign permanent establishment, and in its other activities more generally. In this context, and in conjunction with the 12 month requirement under section 250-20, the 'used wholly or principally outside Australia' tests in subparagraphs 250-60(1)(b)(ii) and 250-60(2)(b)(ii) will operate in a similar way to which they do in respect of a foreign resident who also has Australian business operations (that is an asset will only be found to have been put to a 'tax preferred use' where it has been predominantly used outside of Australia).

9.250 Given the operation of subsections 51AD(1A) and 159GH(1B) of the ITAA 1936, section 51AD and Division 16D will not apply to the extent that the modified definition of 'tax preferred end user' has effect in respect of an Australian resident that carries on a business at or through a foreign permanent establishment.

Clarifying an expression

Table 9.9: Amendment to the *Income Tax Assessment Act 1997*

Provision being amended	*What the amendment does*
Income Tax Assessment Act 1997 727-95(a) ***[Schedule 7, item 209]***	Rephrases the sentence so reference can be made to the defined term 'arm's length'.

Removing an extraneous definition

Table 9.10: Amendment to the *Income Tax Assessment Act 1997*

Provision being amended	*What the amendment does*
Income Tax Assessment Act 1997 995-1(1) (definition of 'natural resource', first occurring) ***[Schedule 7, item 210]***	Removes an extraneous definition of 'natural resource' from the Dictionary.

Simplifying the process for future changes to the phase-out thresholds in the Income Tax Rates Act 1986

Table 9.11: Amendments to the *Income Tax Rates Act 1986* and *Tax Laws Amendment (Income Tax Rates) Act 2012*

Provisions being amended	*What the amendments do*
Income Tax Rates Act 1986 3(1) (definition of 'net income phase-out limit') 3(1) (definition of ' non-resident phase-out limit') 3(1) (definition of 'resident phase-out limit') 13(2) 13(5)(b) 13(6)(c) 13(8)(b) 13(10) 14(2)(c) 14(3) 15(2)(b) 15(4)(d) 15(6)(b) 15(8) ***[Schedule 7, items 211 to 220]*** ***Tax Laws Amendment (Income Tax Rates) Act 2012*** 2(1) (table item 3) Part 2 of Schedule 1 ***[Schedule 7, items 234 and 235]***	Division 3 of Part II of the *Income Tax Rates Act 1986* (the Rates Act) sets the rates of tax payable on income of Australian resident minors (section 13), certain trusts (section 14), and foreign resident minors (section 15). These provisions contain fixed monetary thresholds that are implicitly linked to the statutory tax rates that apply to taxpayers more generally. For that reason, when there is a change in the tax rates, a corresponding change to the fixed monetary thresholds is also required. The recent reforms to the personal income tax rates that commenced on 1 July 2012 included an increase in the first tax rate for residents from 15 per cent to 19 per cent, and an increase of the first tax rate for foreign residents in the table in Part II of Schedule 7 to the Rates Act ('the first tax rate for non- residents') from 29 per cent to 32.5 per cent. While amendments have been made to section 15 to reflect these changes (the fixed monetary threshold was changed from $732 to $663), there was no corresponding consequential amendment to the concessional threshold in subsection 14(2). If the concessional threshold is not amended, trustees with annual, relevant trust income of $595 would pay around $24 more in tax than trustees with annual, relevant trust income of $594 — producing a very large and unintended effective marginal tax rate. To correct this missed consequential and to avoid the need to make future changes to the thresholds when there are changes to the relevant tax rates, these amendments replace references to these fixed monetary thresholds with the formulae that are used to produce the new monetary amounts that are used in the thresholds. With the introduction of the formulas,

Provisions being amended	***What the amendments do***
	legislated future changes to the thresholds to reflect legislated changes to the tax rates are also repealed, as they are no longer necessary.

Correcting a reference

Table 9.12: Amendment to the *New Business Tax System (Venture Capital Deficit Tax) Act 2003*

Provision being amended	***What the amendment does***
New Business Tax System (Venture Capital Deficit Tax) Act 2003 2(1) (table item 2) ***[Schedule 7, item 223]***	Corrects the reference to the *New Business Tax System (Consolidation and Other Measures) Act 2003*, by removing the '*(No.2)*'.

Rectifying a misdescribe — correcting an amending reference

Table 9.13: Amendment to the *Superannuation Laws Amendment (Capital Gains Tax Relief and Other Efficiency Measures) Act 2012*

Provision being amended	***What the amendment does***
Superannuation Laws Amendment (Capital Gains Tax Relief and Other Efficiency Measures) Act 2012 Item 1 of Schedule 2 ***[Schedule 7, item 224]***	Corrects an incorrect amending reference to those paragraphs in the *Superannuation Industry (Supervision) Act 1993* that confer the general administration of the Act on the Commissioner.

Public ancillary funds

Table 9.14: Amendment to the *Taxation Administration Act 1953*

Provision being amended	***What the amendment does***
Taxation Administration Act 1953 426-102(1)(a)(ii) of Schedule 1 ***[Schedule 7, item 225]***	Under reforms introduced in 2011, all public ancillary funds must have trustees which are constitutional corporations. However, a temporary concession was provided for a trustee prescribed by regulation. This mechanism permitted the granting of additional time for certain new public ancillary funds to comply with the requirement to have a trustee that is a constitutional corporation. The need for a limited exemption mechanism was identified during consultation and is intended

Provision being amended	***What the amendment does***
	to be exercised in limited number of cases where a need for additional transitional relief can be demonstrated. However, the regulation making power was unnecessarily limited to cases involving public ancillary funds with single trustees. This is inappropriate because in the exceptional cases contemplated in the explanatory materials, public ancillary funds without constitutional corporations will need to have more than one trustee to comply with the *Public Ancillary Guidelines 2011*. This amendment allows more than one trustee to be prescribed as exempt during the transitional period.

Allowing for the amendment of assessments

Table 9.15: Amendment to the *Tax Laws Amendment (2011 Measures No. 9) Act 2012*

Provision being amended	***What the amendment does***
Tax Laws Amendment (2011 Measures No. 9) Act 2012 4(4) ***[Schedule 7, item 228]***	Allows the Commissioner to amend assessments of those taxpayers who are entitled to apply the foreign income tax offset against the Medicare levy and Medicare levy surcharge back to 1 July 2008 (as a result of changes in Part 28 of Schedule 6 to the *Tax Laws Amendment (2011 Measures No. 9) Act 2012*).

Rectifying a misdescribe — hyphens

Table 9.16: Amendment to the *Tax Laws Amendment (2011 Measures No. 9) Act 2012*

Provision being amended	***What the amendment does***
Tax Laws Amendment (2011 Measures No. 9) Act 2012 Item 14 of Schedule 1 ***[Schedule 7, item 229]***	Removes the hyphen from the expression 'self-managed superannuation funds' in Item 14 of Schedule 1 to this Act, which amends a Note in the *Superannuation Industry (Supervision) Act* 1993. This is necessary to ensure that the subsequent amendment to the same Note (in Item 204 of Schedule 6 to this Act) will be effective, as it refers to the expression without a hyphen.

Rectifying a misdescribe — parentheses

Table 9.17: Amendments to the *Tax Laws Amendment (2011 Measures No. 9) Act 2012*

Provisions being amended	*What the amendments do*
Tax Laws Amendment (2011 Measures No. 9) Act 2012 Item 200 of Schedule 6 Item 201 of Schedule 6 Item 202 of Schedule 6 Item 203 of Schedule 6 ***[Schedule 7, item 230 to 233]***	Remove the parentheses in the references to the *Superannuation Industry (Supervision) Act 1993* in Items 200 to 203 of Schedule 6, which amend provisions in the ITAA 1997. This will ensure that Items 200 to 203 of Schedule 6 will be effective in amending these provisions, as the provisions in the ITAA 1997 did not originally have parentheses.

Part 3—Asterisking amendments

Table 9.18: Amendments to the *Income Tax Assessment Act 1997*

Provisions being amended	*What the amendments do*
Income Tax Assessment Act 1997 43-170(2)(b) 70-20(b) 70-30(1)(a) 70-110(1)(a) 70-120(6)(b) 87-40(2)(e) 112-20(1)(c) 112-20(2)(a) 116-30(2)(b)(i) 207-128(1)(e) 243-20(7) 243-25(1)(d) 420-30(c)(i) 620-40(2) 707-325(4)(b)(i) 775-120(a) 820-105(1)(b)(ii) 820-105(3)(h) 820-215(1)(b)(ii) 820-215(3)(h)	Ensure the terms 'arm's length' and 'quarter' are correctly asterisked, as they are defined terms.

Provisions being amended	***What the amendments do***
820-315(1)(d) 820-315(3)(f) 820-410(1)(d) 820-410(3)(f) 820-910(3)(d) 820-942(2)(g) 960-275(1) (formula) 960-275(1A) (formula) 960-275(2) (formula) 960-275(3) (formula) 960-280(1) 960-280(2) 960-280(4) 960-285(3A) (formula) 960-285(4) (formula) 960-285(6) ***[Schedule 7, items 236 to 242]***	

Commencement and application arrangements

9.251 All but one of the amendments in Part 1 of Schedule 7 commence on 1 July 2012, immediately after the commencement of the MRRTA 2012. They commence at this time to ensure the PRRT and MRRT laws will operate as intended from 1 July 2012, which is when the MRRT came into effect. These amendments are technical and machinery in nature, and will have no adverse impact on taxpayers.

9.252 The amendment made by item 137 is to commence immediately after the commencement of Part 2 of Schedule 2 to the *Petroleum Resource Rent Tax Assessment Amendment Act 2012* (on 29 September 2012). This ensures that paragraph 24(1)(f) of the PRRTAA 1987 will have always been considered a 'special calculation period' for the purposes of subsection 97(1AA) of the PRRTAA 1987.

9.253 All of the amendments in Part 2 of Schedule 7 commence on Royal Assent, unless otherwise indicated below. Further, if any of the amendments in Part 2 of Schedule 7 have specific application provisions, there are also identified below.

9.254 The amendment made by item 194 is to commence immediately after the relevant income amounts came into effect (on 1 July 2012). This ensures that the references to '20,542' will have always been regarded as including a dollar sign.

9.255 The amendment made by item 196 is to commence immediately after the *Excise Tariff Amendment (Condensate) Act 2011* came into effect (on 24 November 2011). This ensures that the new section 7 to the *Excise Tariff Act 1921* will have always been regarded as being located before the Schedule to this Act.

9.256 The amendments made by items 204 to 207 modify the definition of 'tax preferred end user' and apply to end users of assets on or after 1 July 2007. This application date is retrospective because the amendments give effect to the original policy intent of Division 250, and accompanying amendments to section 51AD and Division 16D of the ITAA 1936 (for Division 250 instead of section 51AD and Division 16D of the ITAA 1936 to apply to the use of certain assets by users who are exempt from Australian tax). ***[Schedule 7, item 208]***

9.257 The amendments made by items 211 to 220 apply in relation to the 2012-13 income year and all later income years. This ensures that no taxpayer is disadvantaged from a missed consequential not made as part of recent changes to the personal individual marginal tax rates. ***[Schedule 7, item 221]***

9.258 The amendment made by item 224 is to commence immediately after the commencement of item 1 of Schedule 2 to the *Superannuation Laws Amendment (Capital Gains Tax Relief and Other Efficiency Measures) Act 2012* (on 31 January 2013), which is when this Act inserted an additional paragraph in the *Superannuation Industry (Supervision) Act 1993*. This ensures that there will never have been an incorrect amending reference to the *Superannuation Industry (Supervision) Act 1993*.

9.259 The amendment made by item 229 is to commence immediately after the commencement of item 14 of Schedule 1 to the *Tax Laws Amendment (2011 Measures No. 9) Act 2012* (on 22 March 2012). This ensures that the expression 'self-managed superannuation funds' in item 14 of Schedule 1 will have always been regarded as not having a hyphen, thereby allowing the subsequent amendment in item 204 of Schedule 6 to be effective.

9.260 The amendments made by items 230 to 233 are to commence immediately after the commencement of items 200 to 203 of Schedule 6 to the *Tax Laws Amendment (2011 Measures No. 9) Act 2012* (on 21 March 2012). This ensures that the references to the *Superannuation Industry (Supervision) Act 1993* in items 200 to 203 of Schedule 6 will have always been regarded as not including parentheses (and will be effective), as the provisions they are amending in the ITAA 1997 did not originally have parentheses.

9.261 All of the amendments in Part 3 of Schedule 7 commence on Royal Assent, and none of them have specific application provisions.

STATEMENT OF COMPATIBILITY WITH HUMAN RIGHTS

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

Miscellaneous amendments to the taxation laws

9.262 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

9.263 This Schedule makes miscellaneous amendments to the taxation laws and regulations as part of the Government's commitment to uphold the integrity of the taxation system.

Human rights implications

9.264 Part 1 of this Schedule makes retrospective technical and machinery amendments to the MRRT and PRRT laws. As the MRRT and PRRT laws only directly affect commercial operations, Part 1 of this Schedule does not engage any of the applicable rights or freedoms.

9.265 Parts 2 and 3 of this Schedule make a variety of technical and machinery amendments to other taxation laws.

9.266 Item 199 in Part 2 of this Schedule promotes the rights to equality and non-discrimination as it clarifies that users of contact lenses are to be treated the same as users of spectacles regarding eligibility to the medical expenses rebate.

9.267 All of the other amendments in Parts 2 and 3 either do not direct affect individuals, or (to the extent they do) do not engage any of the applicable rights or freedoms.

Conclusion

9.268 This Schedule is compatible with human rights as it does not encroach upon any applicable rights or freedoms.

Assistant Treasurer, the Hon David Bradbury

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Schedule 1: Taxation of interest on unclaimed money

Bill reference	*Paragraph number*
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Part 1, items 8, 11, 14 and 17, subsections 307-142(2) and (3B) and 307-300(2) and (3A)	1.20
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Part 1, item 11, subsection 307-142(3C)	1.37
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Bill reference	*Paragraph number*
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Item 13, paragraph 66B(3)(a)	4.51
Item 13, paragraph 66B(3)(b)	4.53
Item 13, paragraph 66B(3)(c)	4.55
Item 13, paragraph 66B(3)(d)	4.57
Item 13, paragraph 66B(3)(e)	4.59
Item 13, paragraph 66B(3)(f)	4.60
Item 13, subsection 66B(4)	4.61
Item 13, subsection 66C(1)	4.65
Items 13 and 14, subsections 66A(2), 66B(2), 66C(1) and paragraph 193(b	4.70
Item 13, paragraph 66A(3)(a)	4.19
Item 13, paragraph 66A(3)(b)	4.23
Item 13, subsection 66A(2)	4.13
Items 15 to 18, subsections 66A(2) and 66B(2)	4.75
Item 19, subsection 166(1)	4.67
Item 20	4.68

Schedule 5: Introduction to loss carry-back

Bill reference	*Paragraph number*
Item 1, section 67-23	6.15
Item 2, paragraph 160-10(a)	6.10
Item 2, paragraph 160-10(a)	6.12
Item 2, section 160-25	6.13
Item 2, paragraphs 160-10(b) to (e)	6.14
Item 2, section 160-5	6.9
Item 2, subparagraph 160-10(b)(i)	6.19
Item 2, paragraphs 160-10(c) and (e) and subsection 160-20(1)	6.20
Item 2, subparagraph 160-10(b)(ii)	6.21
Item 2, subsection 160-20(1)	6.22
Item 2, paragraph 160-30(a)	6.25, 6.69

Bill reference	***Paragraph number***
Item 2, paragraph 160-30(b)	6.26
Item 2, subsection 160-20(1)	6.29
Item 2, subsection 160-20(2)	6.33
Item 2, subsection 160-20(2)	6.34
Item 2, step 1 in subsection 160-15(2)	6.37
Item 2, step 2 in subsection 160-15(2)	6.38
Item 2, step 3 in subsection 160-15(2)	6.39
Item 2, step 4 in subsection 160-15(2)	6.40
Item 2, paragraph 160-15(1)(a)	6.41
Item 2, paragraphs 160-15(1)(b) and (c)	6.42
Item 2, subsection 160-15(4)	6.48
Item 2, subsection 160-15(4)	6.50
Item 2, paragraph 160-10(c) and step 4 in subsection 160-15(2)	6.52
Item 2, step 4 in subsection 160-15(2)	6.53
Item 2, subsection 160-15(3)	6.56
Item 2, step 2 in subsection 160-15(2)	6.59
Item 2, paragraph 160-30(a)	6.73
Item 2, paragraph 160-35(1)(a)	6.82
Item 2, subsection 160-35(3)	6.83
Item 2, paragraph 160-35(1)(b)	6.88
Item 2, paragraph 160-35(1)(c)	6.89
Item 2 paragraph 160-35(1)(d)	6.91
Item 2, paragraph 160-35(1)(e)	6.94
Item 2, paragraph 160-35(2)(a)	6.99
Item 2, paragraph 160-35(2)(b)	6.103
Item 2, paragraph 160-35(2)(c)	6.106
Item 2, subparagraph 160-10(d)(i)	6.114
Item 2, subparagraph 160-10(d)(ii)	6.115
Item 2, subparagraph 160-10(d)(iii)	6.116
Item 3, definition of ‘income tax liability’ in subsection 995-1(1)	6.54
Items 3, 9, 11, 12 and 28, Schedule 6, items 34 to 41, definitions of ‘assessment’, ‘loss carry back tax offset’ and ‘tax offset refund’ in subsection 6(1) of the ITAA 1936, section 960-20 and definitions of ‘carry back’, ‘current year’, ‘income tax liability’, ‘loss carry back choice’, ‘loss carry back tax offset’, ‘loss carry back tax offset component’, ‘tax offset refund’, ‘unutilised’ and ‘utilise’ in subsection 995-1(1) of the ITAA 1997	7.51

Bill reference	***Paragraph number***
Items 4 and 5, definitions of 'interest in membership interests' and 'scheme for a disposition' in subsection 995-1(1)	6.85
Item 6, section 160-5 of the IT(TP)A 1997	6.28
Item 6, section 160-1 of the IT(TP)A 1997	6.124
Item 6, section 160-5 of the IT(TP)A 1997	6.125
Item 6, section 160-1 of the Income Tax (Transitional Provisions) Act 1997 (IT(TP)A 1997)	6.27
Items 7, 8 and 21	7.50
Items 9, 11 and 12, definitions of 'assessment' and 'tax offset refund' in subsection 6(1) of the ITAA 1936 and definition of 'tax offset refund' in subsection 995-1(1) of the ITAA 1997	7.29
Item 10, section 67-100 of the IT(TP)A 1997	7.43
Item 10, section 67-105 of the IT(TP)A 1997	7.44
Item 10, subsections 67-110(1) and (2) of the IT(TP)A 1997	7.45
Item 10, subsection 67-110(3) of the IT(TP)A 1997	7.46
Item 10, section 67-120 and subsection 67-135(2) of the IT(TP)A 1997	7.47
Item 10, sections 67-125 and 67-130 of the IT(TP)A 1997	7.48
Item 10, subsection 67-115(1) of the IT(TP)A 1997	7.49
Item 10, subsections 67-115(2) and 67-135(1) of the IT(TP)A 1997	7.41
Item 10, subsection 67-135(3) of the IT(TP)A 1997	7.42
Item 13, paragraph 161AA(ba) of the ITAA 1936	7.35
Items 14, 15 and 16, sections 166, 166A and 168 of the ITAA 1936	7.31
Item 17, subsection 172A(1) of the ITAA 1936	7.32
Item 17, subsection 172A(2) of the ITAA 1936	7.33
Items 17, 22 and 23, subsection 172A(3) of the ITAA 1936 and subsection 8AAB(4) and 250-10(1) in Schedule 1 to the Taxation Administration Act 1953	7.34
Items 18, 19 and 20, subsections 175A(2) and (3) of the ITAA 1936	7.36
Items 24 and 27	7.40
Items 25 and 26, paragraphs 14ZZK(b) and 14ZZO(b) of the Taxation Administration Act 1953	7.39
Item 27	7.53
Items 28 to 30, the definition of 'loss carry-back tax offset' in subsection 6(1), paragraphs 177C(1)(baa) and (ea) of the ITAA 1936	7.7
Items 31 to 34, subsections 177C(2) and (3) and of the ITAA 1936	7.8
Item 35, paragraph 177CB(1)(ca) of the ITAA 1936 and clause 2, table item 12	7.11

Bill reference	Paragraph number
Items 36 and 37, paragraphs 177F(1)(c) and (ca) of the ITAA 1936	7.9
Items 38, paragraph 177F(3)(ca) of the ITAA 1936	7.10

Schedule 6: The loss carry-back tax offset, consequential amendments

Bill reference	Paragraph number
Items 1 to 29, 32, 33, and 42 to 48, section 45B of the ITAA 1936, sections 4-15, 26-47, 35-15, 36-1, 36-15, 36-17, 36-45, 65-10, 102-10, 102-15, 165-114, 165-115R, 170-20, 170-45, 170-115, 170-145, 707-100 and 707-115 of the ITAA 1997, section 707-30 of the Income Tax (Transitional Provisions)Act 1997 (IT(TP)A 1997), sections 45-330 and 45-480 of Schedule 1 to the Taxation Administration Act 1953	7.4
Items 2, 30, 31 and 41, section 707-110, section 960-20 and the definition of 'utilise' in subsection 995-1(1)	7.3
Item 34, subsection 960-20(3)	6.67
Item 34, subsection 960-20(1)	6.63
Item 34, subsections 960-20(1) and (2)	6.64
Item 34, subsection 960-20(2)	6.65
Item 34, subsection 960-20(4)	6.66
Item 49, subsection 92A(3) of the ITAA 1936	7.18
Items 50 and 51, sections 13-1 and 36-25	7.52
Items 52, 53 and 57, sections 36-25 and 192-37	7.13
Items 54 and 58, sections 36-25 and 195-72	7.16
Items 55 and 56, subsection 195-15(5)	7.14
Item 59, table item 2A in subsection 205-30(1)	6.51
Items 59, 62 and 63, subsections 205-30(1), 219-30(1) and(2)	7.24
Items 60 and 61, subparagraph 205-35(1)(b)(ii)	7.25
Item 64, paragraph 320-149(2)(aa)	7.20
Item 65, subsection 830-65(3)	7.22
Item 66, paragraph 45-340(dc) of Schedule 1 to the Taxation Administration Act 1953	7.28

Schedule 7: Miscellaneous amendments

Bill reference	*Paragraph number*
Item 1, subsections 721-10(4), (5) and (6) of the ITAA 1997	9.239
Item 2, definition of 'petroleum resource rent tax law' in subsection 995-1(1) of the ITAA 1997	9.240
Items 3, 4, 167, 168 and 186 to 193, subsection 995-1(1) of the Income Tax Assessment Tax 1997 (ITAA 1997) (definitions of 'resource rent tax amount' and 'resource rent tax provisions'), paragraph 8AAZLG(1)(b) and subsection 8AAZLH(1) of the TAA 1953, and heading in section 12AA, paragraph 12AA(a), note in section 12AA, paragraph 12AB(a), note in section 12AB, paragraph 12AC(b), note in section 12AC and definition of 'resource rent tax amount' in section 12AF of the TIOEPA 1983	9.89
Item 5, subsection 30-25(7)	9.9
Item 6, note in subsection 30-40(2)	9.12
Items 7 and 8, subsections 30-55(1) and (2)	9.15
Item 9, note in subsection 35-5(1)	9.18
Item 10, formula in subsection 45-10(1)	9.25
Items 11 and 65 to 67, examples in subsections 45-10(2) and 190-20(2)	9.26
Item 12, note in subsection 70-35(1)	9.19
Item 13, subsection 80-25(1)	9.95
Item 14, subparagraphs 80-25(3)(b)(i) to (iv)	9.28
Item 15, subparagraph 80-25(3A)	9.29
Item 16, subsection 80-40(1)	9.95
Item 17, paragraph (b) of the definition of 'uplift factor' in subsection 80-45(1)	9.38
Item 18, paragraph 80-50(1)(b)	9.95
Items 19 and 20, notes in subsections 90-25(1) and 90-40(1)	9.80
Items 21 to 24, subsections 90-45(1), (1A) and (2) and subsection 90-55(5A)	9.30
Item 25, subsection 90-65(5)	9.35
Item 26, paragraph 95-20(2)(a)	9.95
Item 27, subsection 95-25(1)	9.95
Item 28, paragraphs 95-30(1)(a) and (2)(a)	9.95
Item 29, paragraph 115-15(2)(b)	9.59
Items 30 to 32, subsection 115-15(3), paragraph 115-25(aa) and paragraph 115-25(b)	9.60
Item 33, subsections 115-55(1) and (2)	9.46

Bill reference	***Paragraph number***
Items 34 and 35, paragraph 120-10(4)(e) and note in subsection 120-10(4)	9.48
Item 36, paragraph 125-10(4)(e)	9.49
Item 37, note in subsection 125-10(4)	9.50
Item 38, paragraph 140-10(2)(c)	9.42
Items 39, 40 and 43, paragraph 145-15(2)(e), note in subsection 145-15(2) and paragraph 150-15(2)(e)	9.51
Items 41, 42 and 44 to 46, subsections 145-20(2) and (3), heading in subsection 150-15(4) and subsections 150-20(2) and (3)	9.95
Item 47, note 2 in subsection 150-30(2)	9.95
Item 48, subsection 155-10(3)	9.56
Item 49, subsections 160-15(5) and (6)	9.11
Items 50 and 51, subsections 165-15(1) and (2)	9.33
Items 52 to 54, subsections 165-25(3), 165-30(1) and 165-30(2) and paragraph 165-30(2)(c)	9.95
Item 55, paragraph 175-15(1)(b)	9.63
Item 56, subsection 180-5(1)	9.39
Items 57 to 64 and 73, sections 190-1, 190-5, 190-10 and 190-15 of the MRRTA 2012 and paragraph 10(a) of Schedule 4 to the MRRT(CATP)A 2012	9.94
Item 68, subsection 200-15(1A)	9.68
Items 69 to 71, subsections 215-10(2), 255-20(1) and (2) and definition of 'MRRT year' in section 300-1	9.95
Item 72, item 1A of Schedule 4 to the MRRT(CATP)A 2012	9.96
Item 74, paragraph 15(1)(c) of Schedule 4 to the MRRT(CATP)A 2012	9.75
Item 75, paragraph 15(3)(b) of Schedule 4 to the MRRT(CATP)A 2012	9.78
Item 75, paragraph 15(3)(c) and subitem 15(4) of Schedule 4 to the MRRT(CATP)A 2012	9.79
Item 75, paragraph 15(3)(a) of Schedule 4 to the MRRT(CATP)A 2012	9.77
Item 76, title	9.99
Item 77, definition of 'acquisition' in section 2	9.102
Item 78, definition of 'created' in section 2	9.105
Item 79, definition of 'notional tax amount' in section 2	9.106
Items 80, 82 and 84, subsections 4A(1), (3) and (4) and sections 4B and 4C	9.110
Item 81, paragraphs 4A(3)(b)and (c)	9.109

Bill reference	***Paragraph number***
Item 83, subsection 4A(4)	9.111
Items 85 and 86, heading in subsection 10(4) and paragraph 10(4)(a)	9.113
Item 87, subparagraphs 20(2)(a)(iii) and (iv)	9.116
Item 88, subsection 35C(5)	9.119
Item 89, subsections 35E(1A) and (1B)	9.122
Item 90, subsection 35E(4)	9.123
Item 91, subsection 41(2)	9.126
Item 92, paragraph 45(2)(b)	9.131
Item 93, table item 2 in subsection 45(5)	9.135
Item 94, subsection 45(8)	9.137
Item 94, subsection 45(9)	9.146
Items 95 and 98, subparagraphs 48(1)(a)(ib) and 48A(5)(ca)(i)	9.145
Items 96, 97, 99 and 100, subsections 48(3) and 48A(11)	9.147
Item 101, subsection 57(3)	9.150
Items 102, 105 to 110, 112, 115, 117, 120 and 121, subsections 58B(1) and (4) to (6), subsections 58C(1) and (2), subsection 58D(1), subsections 58J(1) and (3), paragraphs 58J(4)(b) and (c), subsection 58J(4), paragraphs 58J(5)(b) and (c), subsection 58J(5), subsections 58J(6) to (11), paragraphs 58K(1)(a) and (b), subsection 58K(2), subsections 58L(1) and (4), paragraphs 58M(1)(a) to (c) and subsections 58M(1) and (2)	9.154
Items 103 and 104, heading in subsection 58F and paragraph 58F(a)	9.152
Items 111, 113, 114, 116, 118 and 119, heading in subsection 58K(1), paragraph 58K(1)(b), subparagraphs 58K(1)(b)(iv) to (vii), heading in subsection 58M(1), paragraph 58M(1)(c) and subparagraphs 58M(1)(c)(iv) to(vii)	9.153
Item 122, subsection 58N(2)	9.157
Item 123, section 58P	9.160
Item 124, section 58Q	9.170
Items 125 to 128, subsections 58R(1) and (2)	9.171
Item 129, section 58RA	9.175
Items 130 to 132, subparagraphs 58U(1)(a)(i), 58U(1)(b)(i) and paragraph 58V(1)(a)	9.176
Item 133, subsection 58V(3)	9.179
Item 134, section 58W	9.181
Item 135, subsection 93(1)	9.184
Item 136, paragraph 97(1A)(b)	9.186
Item 137, subsection 97(1AA)	9.188

Bill reference	***Paragraph number***
Item 138, section 108A	9.190
Item 139, subsection 109(5)	9.182
Items 140 and 141, clause 1 of Schedule 1	9.194
Item 142, subclause 22(5) of Schedule 1	9.198
Item 143, subclause 31(2A) of Schedule 1	9.201
Item 144, paragraph 3(1)(b) of Schedule 2	9.202
Items 145, 146, 148 and 152, paragraphs 5(b) and 7(3)(b), subparagraph 10(1)(a)(ii) and paragraph 15(5)(b) of Schedule 2	9.203
Item 147, note in subclause 7(3) of Schedule 2	9.204
Items 149 and 150, subparagraph 10(2)(b)(i) and subclause 10(3) of Schedule 2	9.210
Item 151, subclauses 10(4) and 10(4A) of Schedule 2	9.208
Items 153, 154 and 161, subclauses 18(1), (3), (4) and (5) and paragraph 19(1)(b) of Schedule 2	9.140
Item 155, subclause 18(5A) of Schedule 2	9.214
Items 156 and 157, heading in subclause 18(6) and paragraphs 18(6)(a) and (b) of Schedule 2	9.218
Item 158, subclause 18(7) of Schedule 2	9.215
Item 159, subparagraph 18(8)(b)(i) of Schedule 2	9.217
Item 160, paragraph 18(8)(c) of Schedule 2	9.216
Item 162, paragraph 19(2)(b) of Schedule 2	9.221
Item 163, paragraph 19(2)(c) of Schedule 2	9.224
Item 164 clause 21A of Schedule 2	9.229
Item 165, paragraph 23(4)(b) of Schedule 2	9.232
Item 166, subclauses 23(5A) and (5B) of Schedule 2	9.236
Item 169, application of subsection 8AAZLH(2) of the TAA 1953	9.92
Item 170, definition of 'starting base assessment' in section 14ZQ of the TAA 1953	9.241
Item 171, subparagraphs 14ZZK(b)(i) and (ii) and 14ZZO(b)(i) and (ii) of the TAA 1953	9.243
Item 172, paragraph 11-1(h) of Schedule 1 to the TAA 1953	9.247
Item 173, paragraphs 12-330(1)(b) and 12-335(2)(a) of Schedule 1 to the TAA 1953	9.245
Items 174 and 175, note in subsection 18-10(3) and section 18-55 of Schedule 1 to the TAA 1953	9.246
Item 176, section 115-1 of Schedule 1 to the TAA 1953	9.82
Item 177, subsection 117-20(6) of Schedule 1 to the TAA 1953	9.72
Items 178 to 182, paragraphs 284-75(2)(a) and (b) of Schedule 1 to	9.85

Bill reference	***Paragraph number***
the TAA 1953 and table items 3 and 4 in subsection 284-80(1) of Schedule 1 to the TAA 1953	
Item 183, subsection 284-90(1) of Schedule 1 to the TAA 1953 (cell in table item 4, column headed ‘In this situation:’)	9.84
Item 184, subsection 3(1) of the TIOEPA 1983, paragraph (d) of the definition of ‘decision to which this Act applies’	9.88
Item 185, subsection 3C(2) of the TIOEPA 1983	9.87
Item 194	Table 9.1
Item 195	Table 9.2
Item 196	Table 9.3
Item 197	Table 9.4
Item 198	Table 9.5
Item 199	Table 9.6
Items 200 to 202	Table 9.7
Item 203	Table 9.8
Item 204, paragraph 250-55(b)	9.248
Items 205 to 207, subparagraphs 250-60(1)(b)(ii) and 250-60(2)(b)(ii), and paragraph 250-155(3)(b)	9.250
Item 208	9.258
Item 209	Table 9.9
Item 210	Table 9.10
Items 211 to 220	Table 9.11
Item 221	9.259
Item 222	Table 9.2
Item 223	Table 9.12
Item 224	Table 9.13
Item 225	Table 9.14
Items 226 and 227	Table 9.2
Item 228	Table 9.15
Item 229	Table 9.16
Item 230 to 233	Table 9.17
Items 234 and 235	Table 9.11
Items 236 to 242	Table 9.18