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THE PARLIAMENT OF THE COMMONWEALTH OF AUSTRALIA

HOUSE OF REPRESENTATIVES

TAX AND SUPERANNUATION LAWS AMENDMENT (2013 MEASURES No. 2) 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***
AAT	Administrative Appeals Tribunal
ACMA	Australian Communications and Media Authority
ATI	adjusted taxable income
BAS	Business Activity Statement
Commissioner	Commissioner of Taxation
Cooper Review	The Review into the Governance, Efficiency, Structure and Operation of Australia's Superannuation System
DGRs	deductible gift recipients
DIRS	Disaster Income Recovery Subsidy
DSTO	dependent spouse tax offset
FHSA	First Home Saver Accounts
GST	goods and services tax
GST Act	*A New Tax System (Goods and Services Tax) Act 1999*
ITAA 1997	*Income Tax Assessment Act 1997*
ITAA 1936	*Income Tax Assessment Act 1936*
LISC	low income superannuation contribution
MLA 1986	*Medicare Levy Act 1986*
MYEFO	Mid-Year Economic and Fiscal Outlook
NMETO	net medical expenses tax offset
PDS	product disclosure statement
QAPE	qualifying Australian production expenditure
SIS Act	*Superannuation Industry (Supervision) Act 1993*
SIS Regulations	*Superannuation Industry (Supervision) Regulations 1994*

Abbreviation	***Definition***
TIES	Taxation Issues Entry System
TOFA	Taxation of Financial Arrangements
TOFA Act	*Tax Laws Amendment (Taxation of Financial Arrangements) Act 2009*
TOFA regime	Taxation of Financial Arrangements regime

General outline and financial impact

Documentaries and film tax offsets

Schedule 1 to this Bill amends the *Income Tax Assessment Act 1997* (ITAA 1997) to define 'documentary'. It also clarifies that the exclusion of light entertainment programs from eligibility for the film tax offsets does extend to game shows.

Date of effect: The definition of 'documentary' applies to films that started principal photography on or after 1 July 2012. The exclusion of game shows from eligibility for the film tax offsets applies to films that start principal photography on or after the Royal Assent.

Proposal announced: 8 May 2012.

Financial impact: Nil.

Human rights implications: This Schedule is compatible with human rights. See *Statement of Compatibility with Human Rights* — Chapter 1, paragraphs 1.44 to 1.59.

Compliance cost impact: Low.

Tax exemption for ex-gratia payments for natural disasters

Schedule 2 to this Bill amends the *Income Tax Assessment Act 1997* to exempt from income tax the Disaster Income Recovery Subsidy for people who have lost income as a result of ex-Tropical Cyclone Oswald and related flooding in Queensland. It also exempts from income tax the ex-gratia payment for eligible New Zealand special category visa holders, equivalent to the Australian Government Disaster Recovery Payment, made in relation to the natural disasters occurring across Australia during the 2011-12 and 2012-13 financial years.

Date of effect: This measure applies to payments relating to disasters occurring in the 2011-12 and 2012-13 income years.

Proposal announced: Not previously announced.

Financial impact: Nil.

Human rights implications: This Schedule does not raise any human rights issues. See *Statement of Compatibility with Human Rights* — Chapter 2, paragraphs 2.27 to 2.30.

Compliance cost impact: Nil.

GST instalment system

Schedule 3 to this Bill amends the goods and services tax (GST) law to enable entities that are paying their GST by instalments, and that subsequently move into a net refund position, to continue to pay their GST by instalments if they choose to do so. This addresses an issue in the current law which leads to otherwise eligible entities being excluded from the GST instalment system when they move into a net refund position and therefore lose the compliance cost advantages of submitting their Business Activity Statements (BAS) annually.

Date of effect: The first 1 July after Royal Assent.

Proposal announced: In the 2011-12 Budget on 10 May 2011, the Government announced reforms to the GST instalment system.

Financial impact: The financial impact of this measure is unquantifiable but is expected to be minimal.

Human rights implications: This Schedule does not raise any human rights issues. See *Statement of Compatibility with Human Rights* — Chapter 3, paragraphs 3.20 to 3.23.

Compliance cost impact: This policy is minor in nature. The measure affects only a very small proportion of the business and not-for-profit sector. This measure reduces compliance costs for affected entities. These entities are able to remain in the GST instalment system and submit their BAS annually, rather than incur compliance costs when submitting their BAS quarterly.

There is a minor transitional impact, reflecting the need for some taxpayers to be aware of the amendment and apply it when paying GST by instalments.

Deductible gift recipients

Schedule 4 to this Bill amends the *Income Tax Assessment Act 1997* (ITAA 1997) to update the list of deductible gift recipients (DGRs) by adding six entities as DGRs.

Date of effect: The following dates of effect apply to each specifically listed entity:

- the listing of The Conversation Trust applies to gifts made after 21 November 2012;
- the listing of National Congress of Australia's First Peoples Limited applies to gifts made after 30 June 2013;
- the listing of National Boer War Memorial Association Incorporated applies to gifts made after 31 December 2012 and before 1 January 2015;
- the listing of the Anzac Centenary Public Fund applies to gifts made after 30 November 2012 and before 1 May 2019;
- the listing of the Australian Peacekeeping Memorial Project Incorporated applies to gifts made after 31 December 2012 and before 1 January 2015; and
- the listing of Philanthropy Australia Inc. applies to gifts made after 27 February 2013.

Proposal announced: The listings have not been previously announced.

Financial impact: The revenue implications of this measure are as follows:

Organisation	*2012-13*	*2013-14*	*2014-15*	*2015-16*
The Conversation Trust	Nil	–$0.3m	–$0.5m	–$0.5m
National Congress of Australia's First Peoples Limited	Nil	Nil	..	–$0.01m
National Boer War Memorial Association Incorporated	Nil	–$0.02m	–$0.05m	–$0.02m
The Anzac Centenary Public Fund	Nil	–$1.3m	–$3.5m	–$2.3m
The Australian Peacekeeping Memorial Project Incorporated	Nil	–$0.02m	–$0.04m	–$0.02m
Philanthropy Australia Inc.	Nil	..	–$0.01m	–$0.01m
Total	**Nil**	**–$1.64m**	**–$4.10m**	**–$2.86m**

..: denotes financial impact has been rounded to zero.

Human rights implications: This Schedule does not raise any human rights issue. See *Statement of Compatibility with Human Rights* — Chapter 4, paragraphs 4.21 to 4.25.

Compliance cost impact: Nil.

Merging multiple accounts in a superannuation entity

Schedule 5 to this Bill amends the *Superannuation Industry (Supervision) Act 199*3 (SIS Act) to expand the duties of trustees of particular superannuation funds to establish and implement procedures to consolidate accounts where a member of the fund has multiple accounts within a fund and consolidation is in the member's best interest.

This measure will facilitate a reduction in the number of unnecessary accounts. This will boost superannuation balances by ensuring members avoid paying unnecessary fees, including insurance premiums, on multiple accounts and reduce the number of lost accounts.

Date of effect: 1 July 2013.

Proposal announced: This measure was announced by the Minister for Financial Services and Superannuation in a media release No. 131 of 21 September 2011.

Financial impact: Nil.

Human rights implications: This Schedule raises human rights issues. See *Statement of Compatibility with Human Rights* — Chapter 5, paragraphs 5.50 to 5.56.

Compliance cost impact: This measure is expected to have a moderate compliance impact.

Summary of regulation impact statement

Regulation impact on business

Impact: This Schedule expands the duties of superannuation trustees to establish and implement procedures to identify and, where appropriate, merge multiple accounts of a member.

Main points:

- A regulation impact statement has been finalised for the implementation of the *Stronger Super* reforms and can be found on the Department of Finance and Deregulation website.
- The relevant information is contained in section 3 'Consolidation of Superannuation Accounts' within the SuperStream chapter of the regulation impact statement.
- Individuals are often not aware that they have multiple accounts. Where they are aware of the existence of multiple accounts they often fail to act to consolidate as this process can be time consuming and cumbersome.
- Consolidation generally will reduce the number of unnecessary accounts.

Superannuation Co-contribution

Schedule 6 to this Bill amends the *Superannuation (Government Co-contribution for Low Income Earners) Act 2003* to make changes to the superannuation co-contribution.

Date of effect: These amendments will commence from the date of Royal Assent and apply from the 2012-13 income year.

Proposal announced: This measure was announced in the 2011-12 Budget (additional one year freeze of the indexation of the lower income threshold) and in the 2011-12 Mid-Year Economic and Fiscal Outlook (MYEFO) (other changes).

Financial impact: This measure will have the following implications on the underlying cash balance:

2012-13	***2013-14***	***2014-15***	***2015-16***
$0m	$325m	$335m	$327m

Human rights implications: This Schedule does not raise any human rights issue. See *Statement of Compatibility with Human Rights* — Chapter 6, paragraphs 6.27 to 6.31.

Compliance cost impact: Minimal.

Consolidating the dependency tax offsets

Schedule 7 of the Bill amends:

- the *Income Tax Assessment Act 1997* to create a new consolidated dependency tax offset for taxpayers maintaining certain classes of dependants who are genuinely unable to work;

- the *Income Tax Assessment Act 1936* (ITAA 1936) to preserve the existing dependency tax offsets for taxpayers eligible for the zone, overseas forces and overseas civilian tax offsets; and

- the ITAA 1936 to reflect the impact of the consolidation of the dependency tax offsets on the net medical expenses tax offset.

Date of effect: These changes will apply for the 2012-13 and later income years.

Proposal announced: This measure was announced in the 2012-13 Budget.

Financial impact: This measure will have the following revenue implications:

2012-13	***2013-14***	***2014-15***	***2015-16***
–$2.9m	$24.9m	$24.9m	$20.0m

Human rights implications: This Schedule does not raise any human rights issue. See *Statement of Compatibility with Human Rights* — Chapter 7, paragraphs 7.71 to 7.83.

Compliance cost impact: Negligible.

Taxation of Financial Arrangements

Schedule 8 amends Division 230 of the *Income Tax Assessment Act 1997* and the *Tax Laws Amendment (Taxation of Financial Arrangements) Act 2009* to clarify and refine the operation of certain aspects of the Taxation of Financial Arrangements (TOFA) regime.

Date of effect: The amendments effectively apply from the commencement of the TOFA regime (that is, 26 March 2009). The TOFA regime applies for income years commencing on or after 1 July 2010, unless a taxpayer has elected to apply the Division for income years commencing on or after 1 July 2009.

These amendments are the outcome of the ongoing monitoring of the implementation of the TOFA reforms, and have been developed following extensive consultation with industry. The amendments are generally beneficial to taxpayers. They refine and clarify the operation of the TOFA provisions, lower compliance costs and provide additional certainty to affected taxpayers.

Proposal announced: These amendments were announced in the then Assistant Treasurer's Media Release No. 145 of 29 June 2010.

Financial impact: The revenue impact of these amendments is unquantifiable but is not expected to be significant. However, the amendments are expected to protect a significant amount of revenue which would otherwise be at risk.

Human rights implications: This Schedule does not raise any human rights issue. See *Statement of Compatibility with Human Rights* — Chapter 8, paragraphs 8.159 to 8.162

Compliance cost impact: Low.

Chapter 1
Documentaries and film tax offsets

Outline of chapter

1.1 Schedule 1 to this Bill amends the *Income Tax Assessment Act 1997* (ITAA 1997) to define 'documentary'. It also clarifies that the exclusion of light entertainment programs from eligibility for the film tax offsets does extend to game shows.

1.2 All references in this chapter are to the ITAA 1997 unless otherwise stated.

Context of amendments

1.3 The income tax law provides a number of tax offsets to encourage Australian investment in film production. There is:

- the 'producer offset' for Australian expenditure in making an Australian film;
- the 'location offset' for Australian expenditure in making any film; and
- the 'PDV offset' for Australian expenditure on post, digital and visual (PDV) effects production for any film.

1.4 The location offset and the PDV offset are not available for documentaries if they are feature films, telemovies or miniseries.

1.5 The producer offset is available for documentaries. It provides film makers with a refundable tax offset equal to 40 per cent of their 'qualifying Australian production expenditure' (QAPE) on feature films and 20 per cent of their QAPE on other films.

1.6 To be certified as eligible for the producer offset, a film must contain significant Australian content, must not be an excluded format, and must meet the relevant QAPE threshold for the format of the film. Excluded formats include news and current affairs programs, films for exhibition as advertising and light entertainment programs.

1.7 The QAPE threshold for a documentary series is lower than for other program formats. While a season of a drama has to have QAPE of at least $1 million, as well as a minimum of $500,000 per film hour, a documentary only needs QAPE of $500,000, with a minimum of $250,000 per film hour.

1.8 In addition, QAPE eligible expenditure on development and remuneration for the director, producers and principal cast ('above the line' expenditure) is normally capped for the purposes of the producer offset but the cap does not apply for a documentary.

1.9 Screen Australia is responsible for administering the producer offset, calculating a film's level of QAPE, determining whether it displays significant Australian content, and certifying its genre and format.

1.10 The term 'documentary' is not defined in the ITAA 1997. In the absence of a legislative definition of the term, Screen Australia has had regard to the Explanatory Memorandum that accompanied the introduction of the film tax offsets in 2007 and to the Australian Communication and Media Authority's (ACMA's) Guidelines: *Documentary Guidelines: Interpretation of 'documentary' for the Australian Content Standard*. The ACMA Guidelines define a documentary as 'a creative treatment of actuality other than a news, current affairs, sports coverage, magazine, infotainment or light entertainment program'.

1.11 In *EME Productions No. 1 Pty Ltd v Screen Australia* [2011] AATA 439 (the *Lush House* decision, decided on 24 June 2011), the Administrative Appeals Tribunal (AAT) considered Screen Australia's decision to refuse certification to *Lush House*, a six part television series. Applying the ACMA Guidelines, Screen Australia had determined that *Lush House* was an infotainment program, and not a documentary, and therefore had to meet the higher QAPE threshold to become eligible for the producer offset.

1.12 In the absence of a legislative definition of documentary, the AAT considered the ACMA Guidelines and the dictionary definition of a documentary before formulating its own definition. It concluded that, while close to the line, *Lush House* satisfied that definition.

1.13 The AAT's approach to determining the meaning of 'documentary' was upheld on 7 March 2012 by the Full Federal Court (although that Court did not consider the meaning of the term itself). The *Lush House* definition of documentary represents a departure from both the ACMA Guidelines and the long-held understanding of the term in the context of government regulation of, and support for, documentaries.

That has created uncertainty for Government and industry in relation to the film tax offsets.

Summary of new law

1.14 The amendments insert a meaning of 'documentary' that is consistent with the intended meaning, which is explained in the ACMA Guidelines and in the Explanatory Memorandum that accompanied the introduction of the tax offsets, and is understood by the screen production industry.

1.15 They do that by defining 'documentary' to be a creative treatment of actuality. It is also defined to exclude 'infotainment or lifestyle programs', and films that present factual information in multiple parts without an over-arching narrative structure or thesis (so called 'magazine programs').

1.16 The amendments also explicitly exclude game shows from eligibility for the film tax offsets to clarify the intended scope of the exclusion of light entertainment programs from eligibility.

1.17 The main amendments apply to a film if its principal photography commenced on or after 1 July 2012. The game show amendments apply to a film if its principal photography commences on or after the day the amendments receive the Royal Assent.

Comparison of key features of new law and current law

New law	***Current law***
Documentary is defined, in accordance with the ACMA Guidelines, as a creative treatment of actuality that is not an infotainment or lifestyle program or a magazine program.	There is no legislated definition of 'documentary'
Game shows are in the list of light entertainment programs explicitly excluded from eligibility for the film tax offsets.	There is a list of light entertainment programs that are currently excluded from eligibility for the film tax offsets (for example, panel and quiz shows) but it is not clear whether this is wide enough to exclude all game shows.

Detailed explanation of new law

Documentary definition

1.18 The income tax law provides three tax offsets for Australian expenditure on making a 'film':

- the 'producer offset' for Australian expenditure in making an Australian film;
- the 'location offset' for Australian expenditure in making any film; and
- the 'PDV offset' for Australian expenditure on post, digital and visual effects production for any film.

1.19 An entitlement to an offset depends upon obtaining a certificate from the Arts Minister or, in the case of the producer offset, from Screen Australia. The certificate can only be issued if the Minister or Screen Australia is satisfied that the film meets the relevant conditions. In the case of the location offset and the PDV offset, one condition is that a feature film, telemovie or a television miniseries cannot be a 'documentary'. In the case of the producer offset, a reality program or a film of a public event can only be eligible for the offset if it is a documentary. Different (and generally less demanding) rules apply to the producer offset for a documentary than for other films.

1.20 The amendments define 'documentary' as a film that is a creative treatment of actuality, other than an infotainment or lifestyle program or a film that presents factual information in multiple parts without an over-arching narrative structure or thesis (a 'magazine program'). The meaning given to 'documentary' is that described in the ACMA Guidelines. ***[Schedule 1, items 3 and 11, section 376-25 and subsection 995-1(1) (definition of 'documentary')]***

Creative treatment of actuality

1.21 To qualify as a documentary, a film needs to be a creative treatment of actuality. To do that, it has to analyse, explore or interpret its subject matter. The treatment of the material needs to be more than merely superficial and needs to enhance the viewer's understanding of the subject matter.

1.22 The treatment also needs to be creative through, for example, an innovative narrative structure or the manner in which the film is edited or constructed from a range of sources. That distinguishes a documentary from a factual program such as a news report.

Example 1.1: Documentaries versus news programs

Morbo's News and Weather Hour is Channel 314's nightly news show. It presents the day's news in short, factual segments, with limited analysis and minimal original expression. The superficial treatment of the issues and lack of creative or original presentation means this program would not fit the definition of a documentary.

Eliott's War is a program about the use of mercenaries and private military contractors in Afghanistan. It uses footage of a widely reported recent incident as a starting point, but incorporates additional elements, including interviews, dramatic reconstructions, and analysis of historical events and parallels, to increase the viewer's understanding of the origins and implications of the practice. This in-depth investigation and creative treatment means the program meets the definition of a documentary.

1.23 The requirement that a documentary be based on actuality means that the subject matter must be grounded in fact or real life. Therefore, the context for the program exists independently of the film itself. That is, the documentary is an exploration of something that would have happened whether someone was there to film it or not. However, it would be possible for a situation that was contrived by a filmmaker to give rise to actual events that are explored and analysed as part of a documentary program.

Example 1.2: Effect of producer-devised events

Denial Ain't Just, a program about access to the legal system in Ancient Egypt, uses dramatisations and reconstructions to provide insight into historical events and further the audience's understanding of the workings of the Ancient Egyptian legal system. It also examines historical documents and includes interviews with subject matter experts. Although the reconstructions are created for the purposes of the documentary, the program's grounding in historical reality and in-depth exploration of the theme mean it satisfies the definition of a documentary.

The Coff-Off Club asks a variety of coffee drinkers to give up coffee and record the mental and physical effects in order to answer the question of whether coffee's benefits outweigh its risks. The experiences of the participants are supplemented by information about how caffeine works, coffee's use across different eras and cultures, and the economic and social effects of producing coffee. Although giving up coffee is a contrivance, the results are factual and serve to illustrate the primary theme of the consequences of coffee use. When combined with the in-depth exploration of other factual material that also illuminates the primary theme, the program satisfies the definition of a documentary.

> *Burley Griffin Shore* puts a group of new university students in a Kingston share house and follows them as they go about their daily lives. The events depicted are predominantly outlandish and salacious and, while the edited footage is accompanied by narration, there is no attempt to explore a theme or idea. Because most of the events depicted would not have occurred without producer interference, and serve little purpose beyond entertainment, the program is not a documentary.

Relevant factors

1.24 When assessing whether a film is a creative treatment of actuality, and therefore a documentary, regard must be had to the extent and purpose of any contrived situation featured in the film, the extent to which it explores an idea or a theme, and the extent to which it has an overall narrative structure. These elements are drawn from the ACMA Guidelines. ***[Schedule 1, item 3, subsection 376-25(1)]***

1.25 A documentary's primary purpose is to creatively examine actual events. The greater the level of contrivance of the matters being depicted, the greater the likelihood that the film is not a documentary. However, films featuring dramatised sequences may be documentaries and some documentaries may start with contrivance and then record and analyse the resultant events to explore a theme. In such cases, consideration of the extent to which the contrivances explore an idea or theme would be relevant. ***[Schedule 1, item 3, paragraph 376-25(1)(a)]***

1.26 The extent to which a film explores an idea or theme is central to the definition of a documentary. Films that are superficial in their treatment of the subject matter would generally not be characterised as documentaries. The exploration or analysis of a topic or theme is also integral to the concept of documentary, accepting that the exploration or analysis need not be serious in tone. Films that have factual subject matter, but lack exploration or analysis, would be more likely to fall within the non-documentary categories of infotainment, lifestyle or magazine programs. ***[Schedule 1, item 3, paragraph 376-25(1)(b)]***

1.27 The narrative style of a program is very likely to have an impact on the way in which it treats its subject matter. A program without an over-arching narrative structure, such as one consisting of brief and unrelated aspects of a broad topic, is unlikely to be a program that explores and analyses its subject in some depth, which is a key characteristic of documentaries. ***[Schedule 1, item 3, paragraph 376-25(1)(c)]***

Example 1.3: The need for a narrative structure

> *Finding the Angle* reports developments in the world of fishing and angling. Segments are short, superficial and connected only by the

common subject matter of fishing. Facts are presented without question, analysis or wider context. The lack of in-depth consideration, narrative structure and over-arching theme means the program is a magazine or infotainment or lifestyle program rather than a documentary.

Doctor W's Death from the Skies! is an astronomy series that increases the viewer's understanding of the power of the galaxy by examining the different astronomical phenomena that could destroy life on Earth. Although each episode focuses on a different phenomenon (supernova, black holes, meteorite strikes and so on), each episode builds on the information discussed in previous episodes. The series is united by a common narrative theme: the weird and wonderful phenomena in the Milky Way and the implications they have for life on Earth. Each subject, and the galaxy as a whole, is examined in some depth, with a narrative structure that spans all the episodes. The program satisfies the definition of a documentary.

1.28 These are not the only factors that can be taken into account; anything else that is relevant should also be considered in deciding whether a film is a creative treatment of actuality. For example, relevant factors in appropriate cases might include the commercial arrangements underpinning the production, the likelihood of the film having enduring appeal, and the breakdown of the film's budget. ***[Schedule 1, item 3, paragraph 376-25(1)(d)]***

Infotainment, lifestyle and magazine programs

1.29 Documentaries do not include infotainment or lifestyle programs. ***[Schedule 1, item 3, paragraph 376-25(2)(a)]***

1.30 'Infotainment or lifestyle program' has the same meaning as in Schedule 6 to the *Broadcasting Services Act 1992*. There it is defined as a program, 'the sole or dominant purpose of which is to present factual information in an entertaining way, where there is a heavy emphasis on entertainment value'. ***[Schedule 1, item 3, paragraph 376-25(2)(a)]***

1.31 At the margin, it is this emphasis on entertainment that distinguishes an infotainment or lifestyle program from a documentary that presents facts but in a creative and entertaining way. In a documentary, the entertainment serves the more serious purpose rather than the other way around. Infotainment or lifestyle programs are also likely to share a number of observable characteristics that differentiate them from documentaries:

- The programs are usually episodic in nature, comprising a series of distinct or loosely connected segments rather than an overall story arc.

- The treatment of the material tends to be superficial and unquestioning. There is likely to be limited engagement with, or analysis of, the subject matter.
- The primary purpose of the program is often to highlight goods or services available to the viewer, or to give the viewer advice on 'how to' do something.

1.32 Documentaries also do not include films that present factual information in multiple discrete parts, each dealing with a different subject, or a different aspect of the same subject, but without an over-arching narrative structure or thesis. These are what the ACMA Guidelines call 'magazine programs'. ***[Schedule 1, item 3, paragraph 376-25(2)(b)]***

1.33 Like an infotainment or lifestyle program, a magazine program does not contain an over-arching narrative. It may deal with several subjects but, even if it deals with one broad subject matter, it will touch upon a number of aspects of the subject. Each part of the program is discrete from the others. It typically imparts superficial factual information without presenting an original thesis, exploration or interpretation.

1.34 Infotainment or lifestyle programs and magazine programs are not necessarily excluded from the producer offset. However, because they are not documentaries, they must meet the higher QAPE threshold and other existing criteria.

Example 1.4: Magazine program is not a documentary

> *Better House, Better Life* is a program that provides viewers with information on how to improve their living spaces. Each episode has a number of segments demonstrating how to complete a different do-it-yourself project.
>
> The superficial treatment, loosely connected segments and 'how to' nature of the program mean it is a magazine program and so not a documentary. It may still be eligible for the producer offset as a non-documentary program if it satisfies the higher QAPE threshold and different format criteria.

Excluded formats

1.35 When they were developed, the film tax offsets were intended to exclude light entertainment programs. This exclusion was achieved by providing that the necessary certificate cannot be issued for a film that is 'a discussion program, a quiz program, a panel program, a variety program, or a program of a like nature'.

1.36 There is some doubt whether game shows are covered by that description, although, as light entertainment programs, they were always intended to be excluded.

1.37 The amendments remove that doubt, and ensure that the original intention is achieved, by adding game shows to the list of formats that are ineligible for the film tax offsets. ***[Schedule 1, items 2, 5 and 6, subparagraphs 376-20(2)(c)(iii), 376-45(2)(c)(iii) and 376-65(2)(d)(ii)]***

Application and transitional provisions

1.38 Most of the amendments apply to films that commence principal photography on or after 1 July 2012. ***[Schedule 1, subitem 12(1)]***

1.39 Although this means that those amendments will have a retrospective operation, that operation restores the understanding of the provisions that was generally held in the context of government regulation of, and support for, documentaries before the recent *Lush House* decision. The amendments were also announced as part of the 2012-13 Budget and Screen Australia adopted the practice from July 2012 of advising applicants for the producer offset whether their film was a documentary under both the meaning adopted by the AAT and the meaning set out in the ACMA Guidelines. It follows that film makers would have embarked on making their films fully aware of the amendments that were proposed and of the consequences of those amendments for their film.

1.40 These amendments do not apply to films if their principal photography commenced *before* 1 July 2012. That ensures that they do not affect films on which significant expenditure had occurred by that date.

1.41 ‘Principal photography’ is the phase of film production where the film is actually shot. It can be distinguished from the pre-production phase, where scripts are finalised, suppliers and crew engaged and production planned. Principal photography is almost always the most expensive part of making a film.

Application rule for game show amendments

1.42 The amendments that ensure that the exclusion of light entertainment programs extends to game shows apply in relation to films that commence principal photography on or after the amendments receive Royal Assent. This reflects the fact that the clarification of this issue was not covered by the Government’s announcement about changes to the film tax offsets. ***[Schedule 1, subitem 12(2)]***

Consequential amendments

1.43 Consequential amendments insert asterisks before the term 'documentary' to indicate that it is defined. ***[Schedule 1, items 1, 4, and 7 to 10, subparagraphs 376-20(2)(c)(i), 376-45(2)(c)(i) and 376-65(2)(d)(iii); paragraph 376-65(3)(c) and subsections 376-65(6) and 376-170(4A)]***

STATEMENT OF COMPATIBILITY WITH HUMAN RIGHTS

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

Documentaries and film tax offsets

1.44 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

1.45 The income tax law provides a number of tax offsets designed to encourage expenditure on films in Australia if certain criteria are satisfied.

1.46 Some types of films are not eligible for the offsets at all unless they are a documentary and some of the criteria are easier to satisfy for documentaries than for other films. The producer offset, for example, requires a lower minimum level of qualifying expenditure for documentaries than for other films.

1.47 The law does not currently define what a documentary is. Screen Australia (which certifies whether a film is a documentary and whether it meets the minimum expenditure level for the producer offset) has used the definition from the Australian Communications and Media Authority's Guidelines since the offsets were enacted in 2007. That interpretation is consistent with the Parliamentary intention explained in 2007.

1.48 A decision of the Administrative Appeals Tribunal in 2011 used a different definition and found that the television program *Lush House* was a documentary that qualified for the producer offset. Programs of that sort were not intended to be eligible for the concessional tax offset treatment available to documentaries.

1.49 The Schedule amends the income tax law to add a definition of 'documentary' that is consistent with the definition that has been applied since 2007, ensuring that the provisions apply in the way they were understood before 2011. These amendments apply to films that start their principal photography on or after 1 July 2012.

1.50 The tax offsets also do not apply to light entertainment programs. The law achieves that by listing types of programs that are not eligible for the offsets. Some doubt has been raised about whether that list is wide enough to exclude all game shows. The amendments remove any doubt by stating that game shows are not eligible for the offsets. Those amendments apply to films that start their principal photography on or after Royal Assent.

Human rights implications

Cultural rights

1.51 Article 15 of the *International Covenant on Economic, Social and Cultural Rights* requires Australia, as a party, to recognise the right of everyone to take part in cultural life and to take steps to achieve the full realisation of the right, including those steps necessary for the conservation, development and diffusion of science and culture.

1.52 The *Committee on Economic, Social and Cultural Rights* noted in its General Comment 21 on the right of everyone to take part in cultural life (paragraph 13):

> The Committee considers that culture, for the purpose of implementing article 15(1)(a), encompasses, inter alia, ways of life, language, oral and written literature, music and song, non-verbal communication, religion or belief systems, rites and ceremonies, sport and games, methods of production or technology, natural and man-made environments, food, clothing and shelter and the arts, customs and traditions through which individuals, groups of individuals and communities express their humanity and the meaning they give to their existence, and build their world view representing their encounter with the external forces affecting their lives. Culture shapes and mirrors the values of well-being and the economic, social and political life of individuals, groups of individuals and communities.

1.53 Encouraging expenditure on films in Australia via tax offsets can be seen as an appropriate step for the development and diffusion of culture in Australia and documentaries are more likely than most films to do that because they try directly to help people understand cultural issues and cultural phenomena.

1.54 There being only limited funding available for promoting the right to culture, it is appropriate that the film tax offsets target those films where the funding will have the most effect. It is more likely to have a useful effect if used to encourage films, such as documentaries, that are more likely to promote the right to culture, and that are less likely to be made without the offsets than those that would be made anyway because of their greater commercial viability.

1.55 The limit on the scope of the tax offsets that Parliament intended to enact in 2007 is therefore both appropriate and consistent with implementing Australia's human rights obligations. Amending the law to restore that intention is therefore similarly appropriate and consistent.

Retrospectivity

1.56 The amendments to restore the intended meaning of 'documentary' apply to tax offsets for films that began their principal photography on or after 1 July 2012. They can therefore be argued to have a retrospective operation.

1.57 However, the amendments, and the application date for them, were announced in the 2012-13 Budget in May 2012. Further, since July 2012, Screen Australia, when providing certificates to applicants for the producer offset, on the basis of the Administrative Appeals Tribunal's understanding of the meaning of 'documentary', has also provided them with its view on whether their film is a documentary under the original understanding of that term. Film makers have therefore been aware when commencing their films that the Government proposed to change the law and what the consequences of that change would be for them. Consequently, the retrospectivity does not produce any disadvantage that film makers were unaware of.

1.58 The amendments to exclude all game shows from eligibility for the tax offsets apply to films that begin their principal photography on or after the day the amendments receive the Royal Assent. This reflects that fact that those amendments were not previously announced.

Conclusion

1.59 This Schedule is compatible with human rights. It promotes the right to take part in cultural life.

Assistant Treasurer, the Hon. David Bradbury MP

Chapter 2
Tax exemption for ex-gratia payments for natural disasters

Outline of chapter

2.1 Schedule 2 to this Bill amends the *Income Tax Assessment Act 1997* (ITAA 1997) to exempt from income tax ex-gratia payments made in relation to the disasters occurring across Australia during the 2011-12 and 2012-13 financial years.

Context of amendments

Ex-gratia payments to New Zealand Citizens

2.2 New Zealand citizens who arrived in Australia after 26 February 2001 are classified as non-protected special category visa holders and are not eligible for the Australian Government Disaster Recovery Payment.

2.3 The Australian Government Disaster Recovery Payment is a one-off payment which provides short-term financial assistance to individuals adversely affected by a major or widespread disaster, such as the floods that occurred in New South Wales, Queensland and Victoria in early 2012, the floods in New South Wales and Queensland in early 2013, and the bushfires in Tasmania in early 2013.

2.4 In light of the hardship these disasters may have caused New Zealand non-protected special category visa holders, the Government has agreed to make ex-gratia payments to affected eligible individuals.

2.5 The ex-gratia payment provides financial assistance to New Zealand citizens living in Australia who hold a non-protected special category visa (subclass 444) and who are adversely affected by disasters in the local government areas where the Australian Government Disaster Recovery Payment has been made available during the 2011-12 and 2012-13 financial years.

2.6 The ex-gratia payment is commensurate with the Australian Government Disaster Recovery Payment rates of $1,000 for eligible adults and $400 for eligible children.

2.7 The ex-gratia payment is administered by the Department of Human Services, and can generally be claimed for six months after the disaster has been declared by the Minister for Emergency Management.

2.8 Exempting from income tax the ex-gratia payment to New Zealand non-protected special category visa holders who have been affected by the recent disasters, and any other natural disasters that may occur before 30 June 2013, ensures that the payment receives the same taxation treatment as the Australian Government Disaster Recovery Payment made to eligible individuals.

2.9 It is also consistent with the exemption provided to New Zealand non-protected special category visa holders who received an ex-gratia payment because they were adversely affected by the disasters since the summer of 2010-11.

Disaster Income Recovery Subsidy

2.10 The Disaster Income Recovery Subsidy (DIRS) provides financial assistance to employees, small business persons and farmers that have lost their income as a result of natural disasters.

2.11 The DIRS is an ex-gratia payment which is made to eligible individuals who are residents for tax purposes, and to eligible New Zealand non-protected special category visa holders (subclass 444).

2.12 On 3 February 2013, the Prime Minister announced that the DIRS would be made available to eligible people who have lost income as a result of ex-Tropical Cyclone Oswald and associated flooding in the local government areas (LGAs) of Bundaberg, North Burnett, Fraser Coast, Gympie and Lockyer Valley.

2.13 On 13 February 2013, the Prime Minister agreed to extend the DIRS to people who lost income as a result of the ex-Tropical cyclone Oswald and associated flooding in Queensland that occurred in January 2013 in the Local Government Areas of Banana, Gladstone, Ipswich, Scenic Rim, Somerset, South Burnett, Southern Downs, Goondiwindi and Toowoomba.

2.14 Providing this payment with tax exempt status is consistent with previous activations of the DIRS.

Summary of new law

2.15 This measure amends the ITAA 1997 to list the assistance for New Zealand non-protected special category visa holders as exempt from income tax if it is claimed within the required time period.

2.16 This measure also amends the ITAA 1997 to list the DIRS as exempt from income tax if it is claimed within the required time period.

Detailed explanation of new law

2.17 Section 11-15 of the ITAA 1997 lists income which is exempt from income tax. This list will be amended to include disaster assistance for New Zealand non-protected special category visa holders, and the DIRS. ***[Schedule 2, item 1]***

2.18 Section 51-30 of the ITAA 1997 contains a table detailing welfare payments that are exempt from income tax and any exceptions and special conditions that must be met to qualify for the exemption.

2.19 Schedule 2 amends section 51-30 of the ITAA 1997 to repeal the current item 5.1C, and insert item 5.2 into the table, making the assistance for New Zealand non-protected special category visa holders for the disasters where the Australian Government Disaster Recovery Payment is activated during the 2011-12 income year exempt from income tax. ***[Schedule 2, item 2, item 5.2 in table in section 51-30]***

2.20 Schedule 2 amends section 51-30 of the ITAA 1997 to insert a new item 5.3 into the table, making the assistance for New Zealand non-protected special category visa holders for the disasters where the Australian Government Disaster Recovery Payment is activated during the 2012-13 income year exempt from income tax. ***[Schedule 2, item 2, item 5.3 in table in section 51-30]***

2.21 Schedule 2 also amends section 51-30 of the ITAA 1997 to insert a new item 5.4 into the table, making the ex-gratia payment known as DIRS for the flooding resulting from ex-Tropical Cyclone Oswald that occurred in Queensland during the period starting on 21 January 2013 exempt from income tax. ***[Schedule 2, item 2, item 5.4 in table in section 51-30]***

2.22 This Schedule also introduces a definition of Emergency Management Minister to assist with the readability of the legislation. The definition also allows disasters for the purposes of this section to be linked with an announcement by the relevant Minister. The definition is in line with the Administrative Arrangements Orders, and it is currently the Attorney-General who administers the *Social Security Act 1991*, insofar as

it relates to the Australian Government Disaster Recovery Payment. ***[Schedule 2, item 3]***

2.23 The special conditions inserted in the table in section 51-30 reflect the dates by which the payments must be claimed. This is generally six months after the disaster has been announced.

Application and transitional provisions

2.24 These amendments exempt from income tax ex-gratia payments made in relation to the disasters in Australia during the 2011-12 and 2012-13 financial years, provided these payments are claimed in accordance with the special conditions in the table in section 51-30 of the ITAA 1997.

2.25 These amendments will be repealed on 1 July 2016 in the case of the tax exemption for the 2011-12 financial year, and on 1 July 2017 in the case of the 2012-13 tax exemption, by which time the amendments would have become inoperative. ***[Schedule 2, items 6 to 9]***

Consequential amendments

2.26 The Schedule also repeals sections in the tax laws which dealt with disaster assistance payments which are no longer necessary following these amendments. ***[Schedule 2, items 4 and 5]***

STATEMENT OF COMPATIBILITY WITH HUMAN RIGHTS

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

Tax exemption for ex-gratia payments for natural disasters

2.27 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

2.28 Schedule 2 to this Bill amends the ITAA 1997 to exempt from income tax ex-gratia payments made in relation to the natural disasters occurring across Australia during the 2011-12 and 2012-13 financial years.

Human rights implications

2.29 This Schedule does not engage any of the applicable rights or freedoms, and the amendments are beneficial to taxpayers.

Conclusion

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

Assistant Treasurer, the Hon David Bradbury

Chapter 3
GST instalment system

Outline of chapter

3.1 Schedule 3 amends the *A New Tax System (Goods and Services Tax) Act 1999* (GST Act) to enable those entities that are paying their GST by instalments, and that subsequently move into a net refund position to continue to use the GST instalments option if they wish.

3.2 The amendments also provide that entities that move into a net refund position and wish to continue to pay GST by instalments have an instalment amount each quarter of zero.

3.3 Entities that are currently not using the instalment option and are in a net refund position continue to be ineligible to pay their GST by instalments while they remain in a net refund position.

Context of amendments

3.4 The GST instalment option, contained in Division 162 of the GST Act, allows an eligible entity to choose to pay GST by quarterly instalments worked out by the Australian Taxation Office or an alternative amount nominated by the entity. The entity then lodges an annual GST return in which it accounts for any difference between the actual GST liability and the total GST instalments paid for the year.

3.5 The instalment amounts are generally based on the previous year's GST liability, and are generally notified to the taxpayer by the Commissioner of Taxation.

3.6 The instalment option was introduced in 2001 to make it easier for small businesses to meet their tax reporting requirements. Specifically, the measure seeks to reduce compliance costs for those GST instalment payers by allowing them to lodge a BAS annually rather than quarterly or monthly.

3.7 Currently, the GST legislation excludes a taxpayer from choosing to pay GST by instalments if that entity is in a net refund position. Similarly, an entity that moves into a net refund position while using the instalment option is no longer able to use this option. A net refund position is one in which a business is entitled to receive more input

tax credits on its acquisitions than it is required to pay GST on its sales and other supplies during the relevant tax period.

3.8 In 2008, a small business representative advised through the Taxation Issues Entry System (TIES 022/2008), that the exclusion of businesses from the instalment system, because they move into a net refund position, may make compliance with the GST law more difficult for these businesses. This is because the increased compliance costs which is inconsistent with the intention of the instalments system.

3.9 The amendments allow entities that use the instalment option and move into a net refund position to choose to continue to pay GST by instalments and therefore retain the compliance cost advantages of reporting annually.

3.10 The choice to remain in the GST instalment system provides the entity with the compliance cost advantages of not having to complete quarterly BASs. The amendments result in those entities that decide to remain in the GST instalment system receiving their refund after they have submitted their annual GST return.

Summary of new law

3.11 Schedule 3 amends the GST Act to maintain access to the GST instalment option for those entities that have elected to pay their GST obligations by instalments (GST instalment payers) and move into a net refund position. Specifically, Schedule 3 removes the requirement that entities in the GST instalment system must not be in a net refund position.

3.12 Schedule 3 also amends the GST Act to provide that GST instalment payers that move into a net refund position and wish to continue to pay GST by instalments receive a zero instalment amount each quarter that they remain in a net refund position.

3.13 This measure applies to GST instalment quarters starting on or after the first 1 July that is on or after Royal Assent of this Schedule.

Comparison of key features of new law and current law

New law	*Current law*
GST instalment payers are allowed to continue using the GST instalment method, if they move into a net refund position.	Currently, the GST Act prevents an entity from paying GST by instalments if that entity is in a net refund position or moves into a net refund position.

Detailed explanation of new law

3.14 The amendments to Division 162 of the GST Act enable eligible entities that are already paying GST by instalments to choose to continue to use this method if they move into a net refund position.

3.15 The amendments ensure that an election by an entity to pay GST by instalments does not cease to have effect in the first tax period in which a net refund arises. Similarly, the timing rule which sets out when entities in a net refund cease to be entitled to be GST instalment payers is repealed. This enables these GST instalment payers in a net refund position to avoid the additional compliance costs associated with reverting to quarterly reporting. ***[Schedule 3, items 1 and 2, paragraph 162-30(1(d)) and subsection 162-30(6)]***

3.16 The consequence of choosing to remain in the GST instalment system for those entities that move to a net refund position is that they have an instalment amount each quarter of zero, and not less. No instalment amount is therefore paid unless an entity varies the instalment amount upwards. This is achieved by an amendment to the definition of estimated annual GST amount which requires this amount to be zero in net refund quarters if it would otherwise be less than zero. ***[Schedule 3, items 3 and 6, subsections 162-135(1) and 162-140(6)]***

3.17 Entities that are not paying GST by instalments and are already in a net refund position, remain ineligible to use the instalment option.

3.18 As a consequence of the amendments an additional note is added and the reference to the location of the definition of estimated annual GST amount in the GST dictionary is updated. ***[Schedule 3, items 4, 5 and 7, subsection, 162-140(4) and section 195-1]***

Example 3.1: Quarterly instalment system applies

Ashley operates a shop selling home wares and is eligible to pay GST by instalments.

She has paid GST by instalments continuously from the quarter ending September 2010. Ashley made a large equipment purchase in August 2015. On 31 July 2016 she lodges her annual GST return and receives a refund because she is entitled to more input tax credits on her purchases than she is required to pay GST on her sales.

Ashley wants to continue paying GST by instalments from the quarter ending September 2016 despite being in a net refund position when she lodged her most recent annual GST return.

As she was paying GST instalments in the previous year she is eligible to continue to use the GST instalment system. She is offered an instalment amount of zero in the quarter ending September 2016. Ashley may choose to vary the instalment amount upwards from zero to better reflect her trading conditions.

Example 3.2: Quarterly instalment system cannot be applied

Ricardo has been operating a small commercial development business for the past three years. Ricardo has not previously made an election to pay GST by instalments.

Due to the initial development costs and no sales to date, Ricardo’s business is in a net refund position, that is, Ricardo’s business is entitled to receive more input tax credits on its purchases than it is required to pay GST on its sales.

Prior to the new financial year Ricardo decides that he would like to pay GST by instalments. However, as his business is in a net refund position and he was not already using the GST instalment system, his business is ineligible to elect to pay GST by instalments under paragraph 162-5(1)(e) of the GST Act.

Application and transitional provisions

3.19 The amendments made by this Schedule apply in relation to GST instalment quarters starting on or after the first 1 July that occur on or after Royal Assent of this Bill. The amendments apply from this time to coincide with the beginning of the financial reporting year for many small businesses that may be affected by these amendments. ***[Schedule 3, item 8]***

STATEMENT OF COMPATIBILITY WITH HUMAN RIGHTS

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

GST instalment system

3.20 Schedule 3 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

3.21 Schedule 3 to this Bill amends the GST law to enable entities that are paying their GST by instalments, and that subsequently move into a net refund position, to continue to pay their GST by instalments if they choose to do so.

Human rights implications

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

Conclusion

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

Assistant Treasurer, the Hon David Bradbury

Chapter 4
Deductible gift recipients

Outline of chapter

4.1 Schedule 4 to this Bill amends the *Income Tax Assessment Act 1997* (ITAA 1997) to update the list of deductible gift recipients (DGRs) by adding six entities as DGRs.

Context of amendments

4.2 The income tax law allows income tax deductions for taxpayers who make gifts of $2 or more to DGRs. To be a DGR, an entity must fall within one of the general categories set out in Division 30 of the ITAA 1997 or be specifically listed by name in that Division.

4.3 DGR status helps eligible funds and entities attract public financial support for their activities.

Summary of new law

4.4 The amendments add The Conversation Trust, National Congress of Australia's First Peoples Limited, and Philanthropy Australia Inc. as specifically listed DGRs for an unlimited period. The amendments also add National Boer War Memorial Association Incorporated, the Anzac Centenary Public Fund and the Australian Peacekeeping Memorial Project Incorporated as specifically listed DGRs for a time limited period.

Detailed explanation of new law

The Conversation Trust (ABN 80 958 603 438)

4.5 Taxpayers may claim a deduction for gifts made to The Conversation Trust after 21 November 2012. ***[Schedule 4, item 1, item 2.2.42 in the table in subsection 30-25(2) of the ITAA 1997]***

4.6 The Conversation is a charity that publishes analysis and commentary on current affairs from the university and research sector,

written by experts and delivered directly to the public through its website, Twitter and Facebook.

National Congress of Australia's First Peoples Limited (ABN 47 143 207 587)

4.7 Taxpayers may claim a deduction for gifts made to National Congress of Australia's First Peoples Limited after 30 June 2013. ***[Schedule 4, item 2, item 4.2.42 in the table in subsection 30-45(2) of the ITAA 1997]***

4.8 National Congress of Australia's First Peoples Limited is a national representative organisation of Aboriginal and Torres Strait Islander peoples. It works for the recognition of Aboriginal and Torres Strait Islander rights, and towards securing a better economic, social, cultural and environmental future for these peoples.

National Boer War Memorial Association Incorporated (ABN 29 293 433 202)

4.9 Taxpayers may claim a deduction for gifts made to National Boer War Memorial Association Incorporated after 31 December 2012 and before 1 January 2015. ***[Schedule 4, item 3, item 5.2.33 in the table in subsection 30-50(2) of the ITAA 1997]***

4.10 National Boer War Memorial Association Incorporated is seeking donations to commemorate Australian service in the Boer War (1899 to 1902) by constructing a memorial on Anzac Parade in Canberra, ACT.

Anzac Centenary Public Fund (Operated by Department of Veterans' Affairs – ABN 23 964 290 824)

4.11 Taxpayers may claim a deduction for gifts made to the Anzac Centenary Public Fund after 30 November 2012 and before 1 May 2019. ***[Schedule 4, item 3, item 5.2.31 in the table in subsection 30-50(2) of the ITAA 1997]***

4.12 Donations collected in the Anzac Centenary Public Fund will be used to fund a range of Anzac Centenary initiatives and projects as agreed by Government, for the commemoration of the Anzac Centenary and Australia's involvement in World War One (1914 to 1918).

The Australian Peacekeeping Memorial Project Incorporated (ABN 56 102 846 791)

4.13 Taxpayers may claim a deduction for gifts made to Australian Peacekeeping Memorial Project Incorporated after 31 December 2012 and

before 1 January 2015. ***[Schedule 4, item 3, item 5.2.32 in the table in subsection 30-50(2) of the ITAA 1997].***

4.14 The Australian Peacekeeping Memorial Project Incorporated is seeking donations to build a memorial on Anzac Parade in Canberra, ACT to recognise the service of Australians who have served in peacekeeping missions.

Philanthropy Australia Inc. (ABN 79 578 875 531)

4.15 Taxpayers may claim a deduction for gifts made to Philanthropy Australia Inc. after 27 February 2013. ***[Schedule 4, item 5, item 13.2.19 in the table in section 30-105 of the ITAA 1997].***

4.16 Philanthropy Australia Inc. is a national membership body for the philanthropic sector, primarily servicing Australia's philanthropic trusts and foundations, and providing directory and information products on philanthropy.

Consequential amendments

4.17 An out-dated listing for the Australian Peacekeeping Memorial Project Incorporated has been removed. ***[Schedule 4, item 4, item 13.2.15 in the table in section 30-105 of the ITAA 1997].***

4.18 Changes have been made to update the index in Division 30 to add the new entities. ***[Schedule 4, items 6 to 11].***

4.19 Part 2 of Schedule 4 also provides for the repeal of the time limited DGRs after they cease to have effect.

4.20 Entries for National Boer War Memorial Association Incorporated and Australian Peacekeeping Memorial Project Incorporated will be repealed on 1 July 2019. The entry for the Anzac Centenary Public Fund will be repealed on 1 July 2023. ***[Schedule 4, items 12 to 15]***

STATEMENT OF COMPATIBILITY WITH HUMAN RIGHTS

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

Deductible gift recipients

4.21 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

4.22 This Schedule amends the list of DGRs in Division 30 of the ITAA 1997. The income tax law allows income tax deductions for taxpayers who make gifts of $2 or more to DGRs.

4.23 The amendments add The Conversation Trust, National Congress of Australia's First Peoples Limited and Philanthropy Australia Inc. as specifically listed DGRs for an indefinite period. The amendments also add National Boer War Memorial Association Incorporated, the Anzac Centenary Public Fund and the Australian Peacekeeping Memorial Project Incorporated as specifically listed DGRs for a time limited period.

Human rights implications

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

Conclusion

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

Assistant Treasurer, the Hon David Bradbury

Chapter 5
Merging multiple accounts in a superannuation entity

Outline of chapter

5.1 Schedule 5 to this Bill amends the *Superannuation Industry (Supervision) Act 1993* (SIS Act) to expand the duties of trustees of particular superannuation funds to establish and implement procedures to consolidate accounts where a member of the fund has multiple accounts within a fund and consolidation is in the member's best interest.

5.2 This measure will facilitate a reduction in the number of unnecessary accounts. This will boost superannuation balances by ensuring members avoid paying unnecessary fees, including insurance premiums on multiple accounts and reduce the number of lost accounts.

Context of amendments

5.3 Many Australians have multiple superannuation accounts and are paying multiple sets of administration fees and insurance premiums, within the same superannuation fund. This can happen, for instance, when the member has had a succession of different jobs within the same industry and has been enrolled in the same default fund on different occasions.

5.4 Lost and unnecessary superannuation accounts can increase fees and reduce the retirement savings of the individuals concerned. They can also add to fund administration costs.

5.5 Similarly, members may be paying multiple insurance premiums, even in cases where they are no longer eligible for a payout (for instance, because they are no longer employed), or they are not eligible for more than one payout. It is common for group insurance policies to specify that they will not pay out more than once, even if the member has been paying multiple premiums.

5.6 The Government's *Stronger Super* reforms include a range of measures designed to protect the retirement savings of the many Australians who choose not to take an active role in managing their superannuation. The *Stronger Super* package of reforms was announced

by the Government in response to the recommendations of the Cooper Review (the *Review into the Governance, Efficiency, Structure and Operation of Australia's Superannuation System*).

5.7 The requirement to consolidate multiple accounts within the same fund is one of several Government initiatives designed to support funds, individuals and the Australian Taxation Office to consolidate accounts and encourage people to save for their retirement.

5.8 The SIS Act requires trustees to perform their duties and exercise their powers in the best interests of their members.

5.9 The Office of the Australian Information Commissioner has been consulted on these amendments, and has indicated that trustees in identifying members with multiple accounts must do so with regard to the *Privacy Act 1988*, which regulates the privacy aspects of the handling of personal information including tax file numbers.

5.10 This change has been developed in consultation with industry and demonstrates the Government's commitment to increasing the future retirement savings of Australians.

Summary of new law

5.11 These amendments expand the duties of trustees of particular superannuation funds to require them to establish and implement procedures to consolidate accounts where a member of that superannuation fund has multiple accounts within a fund and consolidation is in the member's best interest.

5.12 This duty will require trustees of particular superannuation funds to establish procedures in relation to the consolidation of multiple member accounts within their fund on a periodic basis. A first round of consolidation must be undertaken by 30 June 2014. This will apply regardless of the balances of the accounts concerned.

5.13 However, defined benefit interest accounts, accounts supporting an income stream and First Home Saver Accounts will all be exempt from this measure. Similarly, this duty does not apply to trustees of pooled superannuation trusts or self-managed superannuation funds.

5.14 When considering whether to merge a member's superannuation accounts, the trustee must consider whether the consolidation is in the member's best interests. Additionally, trustees will not be required to merge member's accounts where it is considered impracticable to do so.

Comparison of key features of new law and current law

New law	***Current law***
Trustees of particular superannuation funds will have an overarching duty to identify the fund's members with multiple accounts within the same super fund and consider whether it is in the best interests of the member to merge those accounts. This is to happen at least annually.	There is no obligation placed on trustees to search for or merge multiple member accounts within the same super fund.

Detailed explanation of new law

Terminology

5.15 While this requires trustees to merge what are commonly thought of as 'accounts', the term 'account' does not have a well-defined meaning.

5.16 For this reason, Schedule 5 introduces 'superannuation account' as a new defined term. This term is intended to be used in the context of these amendments only.

5.17 The Bill makes clear that a FHSA is not a superannuation account and therefore will not be subject to these amendments. ***[Schedule 5, item 4, subsection 108A(3) of the SIS Act]***

5.18 A ***superannuation account*** is a record of a member's benefits, in relation to a superannuation entity in which the member has an interest, which is recorded separately:

- from other benefits of the member in relation to the entity (if any); and
- from other benefits of any other member in relation to the entity.

5.19 Schedule 5 uses the term 'benefit' because benefit is a concept used more broadly under the SIS Act (Parts 18 and 24) and the *Superannuation Industry (Supervision) Regulations 1994* (SIS Regulations) (see SIS Regulations 6.28 and 6.29).

Trustee's duty to identify and consolidate multiple superannuation accounts of members

5.20 These amendments will place a general duty upon trustees to establish rules setting out a procedure to identify members with multiple accounts within their fund, on an annual basis, and to consider whether it would be appropriate to merge them. This will apply regardless of the balances of the accounts concerned.

5.21 The amendments will require affected trustees to:

- establish rules setting out how they will find multiple accounts held by one member within their fund;
- search for multiple accounts at least once per financial year;
- merge the member's multiple accounts (except in the case of defined benefit and income stream accounts) where the trustee reasonably believes it would be in the member's best interest, regardless of the balances of the accounts; and
- ensure no fees are payable (other than buy/sell spreads) for any mergers of multiple accounts.

[Schedule 5, item 4, subsection 108A(1) of the SIS Act]

5.22 These amendments will impose a standard condition in the Registrable Superannuation Entity (RSE) licensee's RSE licence requiring the licensee to ensure compliance with this duty as set out as part of these amendments. This will require RSE licensees to ensure that the trustee complies with the new requirements. ***[Schedule 5, item 3, subsection 29E(6) of the SIS Act]***

5.23 Furthermore, under these amendments, trustees will be guilty of a strict liability offence if they fail to establish rules setting out the procedure for the consolidation of member's multiple superannuation accounts and execute the procedure annually. ***[Schedule 5, item 4, subsection 108A(5) of the SIS Act]***

5.24 'Strict liability' is defined in section 6.1 of the *Criminal Code*. The offence for failing to establish rules setting out the procedure for consolidation of a member's superannuation accounts and executing those procedures is a strict liability offence in order to ensure the integrity of the regulatory regime. Making it a strict liability offence is also necessary as the matter of whether the trustee has satisfied their duty under this measure is peculiarly within the knowledge of the trustee.

Exercising the trustee's duty

Considering whether to merge member's multiple accounts

5.25 In the first instance, the trustee must consider whether there is a need to merge the accounts. The duty to merge accounts will only apply to accumulation accounts, and not to defined benefit accounts or income streams. Nor will this duty apply to trustees of pooled superannuation trusts, self-managed superannuation funds or First Home Saver Accounts (FHSA). ***[Schedule 5, item 4, subsection 108A(1) and paragraph 108A(2)(b) of the SIS Act]***

5.26 The trustee must then consider whether or not merging the member's accounts is in the member's best interest. In deciding whether it is in the member's best interest to merge accounts, the trustee must take into account the possible savings in fees, charges and insurance premiums which will result if they merge two or more separate accounts creating a single account. ***[Schedule 5, item 4, Subsection 108A(4) of the SIS Act]***

5.27 In general, multiple fees, charges and insurance may not be in the member's best interest, and one set of fees and charges may be more appropriate (see further discussion below).

Example 5.1

Brendan has two superannuation accounts with ABC Fund. Both accounts are structured identically (they have the same rights and benefits, though their balances happen to differ). Both carry insurance, though Jack is only entitled to one payout in the event of a claim.

The fund has the ability to merge the two accounts into one, on the basis that the rights and benefits in both accounts are equivalent and it is therefore in Jack's best interest. Brendan no longer pays two sets of fees and charges, nor two insurance premiums.

Example 5.2

Niamh is 23 and has $7,000 in a standard account with insurance in XYZ fund, and another $1,000 in a higher risk/return account without insurance in the same fund. The trustee considers that the potential additional earnings expected on the higher risk account (based on the target earning rate) are smaller than the extra fees and charges Niamh incurs by having two accounts. The trustee accordingly merges the accounts and eliminates duplication in fees, costs and insurance. In doing so, the trustee either:

- merges the underlying benefits; or

- retains the separate classes of benefits but with reduced fees and charges (that is, the trustee charges one administration fee, but possibly two variable fees).

Example 5.3

Sonia is 51 and has $500,000 in a standard account, and $500,000 in a higher risk/return account. The trustee considers that Sonia is a fully engaged member, and that any potential savings in fees and charges is small compared to potential differences in the earnings rates on the two accounts. Accordingly, the trustee does not merge the two accounts into one, though the trustee may consider bringing them both under one 'account' with a single set of fees and charges.

Considering whether it is practical to merge a member's accounts

5.28 Trustees are not required to merge accounts where they consider it to be impracticable. ***[Schedule 5, item 4, paragraph 108A(2)(a) of the SIS Act]***

5.29 Impracticable circumstances may include where a member has an interest in a hybrid scheme, which may include a defined benefit and an accumulation benefit.

5.30 However, trustees should not ordinarily regard cases like the following as impracticable:

- where there is a cost associated with the implementation of the rules;
- where there are operational requirements that the fund determines to have a higher priority;
- where contributions have been paid into two or more accounts in the current reporting period; or
- where higher per account costs may arise as a result of the superannuation fund administering a smaller number of accounts.

Undertaking the process of merging a member's multiple accounts

5.31 The process of merging accounts covers two scenarios. In the first scenario, trustees can choose to retain separate benefits, reflecting different underlying investments, but record those benefits in a single 'account' with a single set of membership fees, charges and insurance. However, there would be no liquidation of the underlying investments in either account. The merged account would record the total balance of the different benefits.

- If trustees choose to maintain separate benefits as one account, the account would ordinarily include only one fee in respect of administration costs, though separate variable fees can be charged in relation to the separate benefits.

5.32 In the alternative scenario, a trustee would, in addition to consolidating records and rationalising costs, fees and insurance, decide to close one account, moving the member's funds into another benefit (the 'retained' account). In other words, the pre-merger accumulation accounts would be consolidated in to one kind of account.

5.33 When merging accounts, trustees should ensure the member has only one account balance, in respect of these accounts, following the merger. Although the account may also record sub-totals, relating to separate amounts of distinct underlying accumulation benefits, if those benefits have not themselves been merged. ***[Schedule 5, item 4, paragraph 108A(1)(c) of the SIS Act]***

5.34 The trustees must develop rules setting out how they will comply with these requirements. In developing these rules the trustee would have regard to base generic circumstances where the trustee would reasonably believe that it would be in the best interest of a member to merge or consolidate multiple accounts. Subject to the obligations and duties above, trustees may develop their own procedures for dealing with multiple accounts.

5.35 It is up to the trustee to decide whether to retain separate benefits under one account, or to merge the benefits within the one account (except in the case of defined benefit and income stream accounts). In the latter case, it is also up to the trustee to decide which class of benefits to retain (the 'retained' benefits), taking into account the best interests of the member.

5.36 The fact that a MySuper interest does not involve investment choice is not, in itself, evidence that it is in the member's best interest to retain a choice interest. The trustee would also need to consider the savings in fees, charges and premiums which come from having fewer accounts, and the savings in fees which attach to MySuper accounts in their own right.

5.37 Similarly, the fact that two accounts have different investment strategies is not, in itself, evidence that it is in the member's interest to retain separate accounts.

5.38 Where one of the accounts is an eligible rollover fund account, it should usually be closed and merged into another account within the same fund.

5.39 Where accounts carry separate insurance rights, the trustee must develop rules regarding the aggregation or extinguishing of existing insurance cover.

Transaction costs associated with exercising the trustee's duty

5.40 If a trustee incurs transaction costs associated with disposing of assets and reinvesting the proceeds as a result of consolidating accounts, the trustee may recover transaction costs by way of a buy/sell spread fee.

5.41 This will be relevant where the trustee decides not only to merge the accounts (in the sense of combining the relevant records) and rationalise fees, costs and insurance, but also merges the underlying benefits.

5.42 However, trustees must not charge other fees for merging accounts, for example an administrative fee for account closure. ***[Schedule 5, item 4, paragraph 108A(1)(d) of the SIS Act]***

Consent, privacy and disclosure

5.43 Trustees will not be required to obtain the consent of the member. However:

- if the separate accounts are significant, trustees could consider giving the member notice that the trustee plans to merge the accounts in order to seek their views; and
- the trustee will need to comply with any requirements set out by the Australian Securities and Investments Commission in relation to significant events.

5.44 Trustees must also consider the disclosure obligations in the *Corporations Act 2001* and the *Corporations Regulations 2001* when consolidating accounts.

5.45 Trustees will need to consider the circumstances of their particular fund and the individual involved in making decisions about appropriate disclosure, particularly with regards to ongoing disclosure of material changes and significant event disclosure pursuant to section 1017B of the *Corporations Act 2001*. Where a trustee makes a decision that fundamentally affects a member's investment, including a decision to transfer a member's benefits without notice or consent, the trustee must disclose this change or event to the member either before, or as soon as practicable (but not more than three months) after the decision.

5.46 Paragraph 7.9.20(b) of the *Corporations Regulations 2001* also requires specific disclosure of amounts of benefit rolled-over or otherwise transferred during the reporting period, to be included in a periodic statement for a member. Further, trustees will need to consider whether they include information in the periodic statements pursuant to section 1017D of the *Corporations Act 2001* about the effect of account consolidation, particularly if consolidation is a change in circumstance affecting the investment that has not been notified since the previous periodic statement (paragraph 1017D(5)(f) of the *Corporations Act 2001*).

5.47 Disclosing information about consolidation is not one of the specific requirements for the shorter Product Disclosure Statement (PDS) regime under Schedule 10D to the *Corporations Regulations 2001*. However, trustees can include additional information about the account consolidation processes in their PDS, including by incorporating this information by reference.

Consequential amendments

5.48 Consequential amendments have also been made to the interpretation section of the SIS Act to reflect the terms utilised in these amendments. This includes the terms ‘buy/sell spread’ and ‘superannuation account’ which are explained in further detail above. ***[Schedule 5, items 1 and 2]***

Application provisions

5.49 These amendments will commence from 1 July 2013 and trustees are required to establish rules and complete their first annual consolidation process by 30 June 2014. ***[Schedule 5, item 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. 2) Bill 2013

5.50 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

Schedule 5 expands the duties of particular superannuation trustees in the *Superannuation Industry (Supervision) Act 1993* to establish and implement procedures to consolidate accounts where a member of the fund has multiple accounts within that fund and consolidation is in the member's best interest.

5.51 Many Australians have multiple superannuation accounts, and are paying multiple sets of administration fees and insurance premiums, within the same superannuation fund. This can happen, for instance, when the member has had a succession of different jobs within the same industry and has been enrolled in the same default fund on different occasions.

5.52 Lost and unnecessary superannuation accounts can increase fees and reduce the savings of the individuals concerned. They can also add to fund administration costs.

5.53 These amendments require trustees to establish rules for identifying and merging multiple accounts within their fund — if the trustee reasonably believes it is in the best interests of the member to do so, and subject to a practicability test. This will facilitate a steady reduction in the number of unnecessary multiple accounts in the superannuation system.

5.54 These amendments apply to trustees of Australian Prudential Regulation Authority regulated superannuation funds and approved deposit funds.

Human rights implications

5.55 Schedule 5 to this Bill engages the right to privacy in Article 17 of the International Covenant on Civil and Political Rights (ICCPR) in so far as it affects a member's personal affairs, as superannuation trustees are not required to obtain consent from a member to merge multiple accounts.

5.56 Article 17 of the ICCPR provides that no one shall be subjected to unlawful or arbitrary interference with their privacy. Interferences with privacy may be permissible, provided they are authorised by law and not arbitrary. In order for the interference not to be 'arbitrary', the interference must be for a legitimate objective and be reasonable, necessary and proportionate to that objective.

5.57 The United Nations Human Rights Committee (UNHRC) has interpreted 'reasonableness' in this context to imply that 'any interference with privacy must be proportional to the end sought and be necessary in the circumstances of any given case'. While the views of the UNHRC are not binding as a matter of law, they are to be considered in good faith and considerable weight should be given to them by Government in the interpretation of Australia's obligations under the ICCPR.

5.58 While Schedule 5 interferes with a member's personal affairs, it does so in order to promote the right to just and favourable conditions of work in Article 7 of the International Covenant on Economic, Social and Cultural Rights (ICESCR), particularly Article 7(a)(ii) in relation to the provision of a decent living for workers and their families, which is what superannuation is designed to provide following retirement.

5.59 Where Australians have multiple superannuation accounts, they could be unnecessarily paying multiple sets of administration fees and insurance premiums, within the same superannuation fund. These fees reduce the savings of the individuals concerned.

5.60 The objective of Schedule 5 is to reduce the number of unnecessary multiple accounts by merging these accounts within the same superannuation fund. Consequently, the Schedule would reduce the amount affected members pay in multiple sets of administration fees and insurance premiums, and increase their retirement savings.

5.61 Members' privacy interests are protected through having specific conditions that are required to be satisfied prior to a trustee merging a member's accounts, namely that the trustee must reasonably believe that it is in the best interests of the member to merge the accounts. In determining whether it is in the member's best interest, the trustee must consider the total amount of fees and charges payable by the member.

5.62 While trustees will not be required to obtain the consent of the member before merging the separate accounts, if the separate accounts are significant, trustees could implement a model where members are given notice that the trustee plans to merge the accounts and the member's views are sought.

5.63 Trustees are also required to comply with the notice requirements set out by the Australian Securities and Investments Commission in relation to material changes or significant events. Where a trustee makes a decision that fundamentally affects a member's investment, including a decision to transfer a member's benefits without notice or consent, the trustee must disclose this change or event to the member either before, or as soon as practicable (but no more than three months) after the decision.

5.64 In identifying members with multiple accounts, the Office of the Australian Information Commissioner has recommended that trustees have regard to the *Privacy Act 1988*, which regulates the handling of personal information.

5.65 By providing these additional safeguards, the amendments introduced by Schedule 5 are reasonable and necessary in the circumstances and required to meet the objects of the law.

Conclusion

5.66 This Schedule limits the right to privacy in a reasonable and proportionate way and is therefore compatible with human rights.

Minister for Financial Services and Superannuation, the Hon, Bill Shorten MP

Chapter 6
Superannuation co-contribution

Outline of chapter

6.1 Schedule 6 to this Bill amends the *Superannuation (Government Co-contribution for Low Income Earners) Act 2003* by:

- reducing the rate of payment for the superannuation co-contribution from 100 per cent to 50 per cent;
- decreasing the maximum amount payable from $1,000 to $500;
- extending the freeze on the indexation of the lower income threshold for the 2012-13 income year; and
- setting the higher income threshold at $15,000 above the lower income threshold (down from $30,000).

Context of amendments

6.2 The superannuation co-contribution matches eligible personal superannuation contributions made to a superannuation fund up to a maximum amount.

6.3 An ***eligible personal superannuation contribution*** is a non-concessional contribution made to a superannuation fund. It does not include contributions that attract an income tax deduction. Other exclusions apply such as transfers from foreign superannuation funds and roll-overs.

6.4 Individuals eligible for the full rate of this payment have their total income at or below the lower income threshold. The superannuation co-contribution phases down for individuals with total income between the lower and higher income thresholds. The lower income threshold is indexed but has been frozen at $31,920 for the 2010-11 and 2011-12 income years.

6.5 ***Total income*** is the sum of an individual's:

- assessable income;

- reportable fringe benefits;
- reportable employer superannuation contributions; and
- is reduced by eligible deductions (if any) from carrying on a business.

6.6 In the 2011-12 Budget, the Government announced an extension of the freeze on the indexation of the lower income threshold of the superannuation co-contribution for the 2012-13 income year (remaining at $31,920 for the 2012-13 income year).

6.7 In the 2011-12 MYEFO, the Government announced that the rate at which this payment would be made would be reduced from 100 per cent (dollar for dollar matching) to 50 per cent. Other changes announced were that the maximum amount available would be reduced from $1,000 to $500. The higher income threshold would be set at $46,920 for the 2012-13 income year.

6.8 Eligible individuals with adjusted taxable income up to $37,000 will benefit from the low income superannuation contribution (LISC) which is a different payment available from the 2012-13 income year. Adjusted taxable income is a more comprehensive income definition to total income as it also included deductions, tax-free pensions and benefits and deductible child maintenance expenditure. This LISC pays an amount equivalent to the concessional contributions tax paid by superannuation funds in respect of low income individuals, up to a maximum of $500 each year.

6.9 The LISC is a better targeted payment, covering over an estimated five times as many individuals as the superannuation co-contribution as a result of these amendments. It also does not require that low income individuals make eligible personal superannuation contributions to their superannuation fund, which increases the coverage of assistance available to low income earners. Historically, only 20 per cent of the people eligible to receive the co-contribution make the voluntary contributions required to receive it.

Summary of new law

6.10 These amendments will reduce the amount of superannuation co-contribution available and apply to the 2012-13 income year and later income years.

6.11 There will be a reduction in the rate at which this payment is made, reducing from 100 per cent (dollar for dollar matching) to 50 per cent (50 cents matched for every dollar of eligible personal superannuation contributions by the individual).

6.12 The maximum amount payable will be reduced to $500 (previously $1,000).

6.13 The higher income threshold is being reduced to $15,000 above the lower threshold. In 2012-13, this threshold will be $46,920. The lower income threshold will continue to be $31,920 for the 2012-13 income year. Indexation of the lower income threshold will resume for 2013-14 and later income years.

Comparison of key features of new law and current law

New law	*Current law*
The rate at which this payment is made is 50 per cent (50 cents contributed by the Government for every dollar of eligible personal superannuation contributions made to a superannuation fund).	The rate at which this payment is made is 100 per cent (one dollar contributed by the Government for every dollar of eligible personal superannuation contributions made to a superannuation fund).
Maximum amount payable is $500.	Maximum amount payable is $1,000.
The higher income threshold is set at $15,000 above the lower income threshold.	The higher income threshold is set at $30,000 above the lower income threshold.
The lower income threshold has indexation frozen for an additional income year (2012-13), in addition to 2010-11 and 2011-12.	The lower income threshold had indexation frozen for 2010-11 and 2011-12.

Detailed explanation of new law

Payment rate and maximum amount payable

6.14 The income years where the amount of superannuation co-contribution payable is paid at a rate equal to 100 per cent of the sum of eligible personal superannuation contributions made during the income year (dollar for dollar matching) is limited to the 2009-10, 2010-11 and 2011-12 income years. ***[Schedule 6, item 1, paragraph 9(1)(c)]***

6.15 For the 2012-13 income year or a later income year, the amount of superannuation co-contribution payable is paid at a rate equal to 50 per cent of the sum of eligible personal superannuation contributions made during the income year.

6.16 The 50 per cent rate at which the payment is made means that the Government will contribute 50 cents for every dollar of eligible personal superannuation contributions. ***[Schedule 6, item 2, paragraph 9(1)(d)]***

6.17 The $1,000 maximum amount of superannuation co-contribution available is limited to payments made in respect of the 2009-10, 2010-11 and 2011-12 income years. ***[Schedule 6, item 3, paragraph 10(1B)]***

6.18 From the 2012-13 income year, the new maximum amount of superannuation co-contribution available is $500. Individuals with total income at or below the lower income threshold, (that is, $31,920 in 2012-13) are entitled to receive a payment up to this new maximum amount.

Example 6.1

> Verity has a total income of $28,000 and makes a $1,000 eligible personal superannuation contribution to her superannuation fund in the 2012-13 income year. As her total income is below the lower income threshold, her rate of payment for the superannuation co-contribution is 50 per cent and she is entitled to the maximum $500 amount.

6.19 Also, from the 2012-13 income year, the superannuation co-contribution will phase down for eligible individuals with total income between the lower and higher income thresholds. The superannuation co-contribution will be tapered by a rate of 3.333 cents for each dollar of total income for the year that exceeds the lower income threshold. ***[Schedule 6, item 4, paragraph 10(1C)]***

Example 6.2

> Andrew has a total income of $40,000 and makes a $1,000 eligible personal superannuation contribution to his superannuation fund in the 2012-13 income year. As Andrew 's total income is between the lower and higher income thresholds, he will be paid a superannuation co-contribution of $230.70.

6.20 Provisions relating to the minimum payment rules, the payment of interest on late or underpaid amounts and small underpayments also apply to the payment of the superannuation co-contribution from 2012-13 onwards. ***[Schedule 6, item 5, sub-section 10(2)]***

Freeze in the indexation of the lower income threshold

6.21 The freezing of the lower income threshold in 2010-11 and 2011-12, will continue for the 2012-13 income year, remaining at $31,920. ***[Schedule 6, item 6, paragraph 10A(1)]***

6.22 The mechanism by which indexation is frozen for 2012-13 income is setting by the indexation factor for this year at 1. ***[Schedule 6, item 9, paragraph 10A(5A)]***

Higher income threshold

6.23 The higher income threshold is set at $30,000 above the lower income threshold from the 2007-08 income year until the 2011-12 income year. ***[Schedule 6, item 7, paragraph 10A(3)(c)]***

6.24 The higher income threshold is set at $15,000 above the lower income threshold for the 2012-13 income year and later income years.

6.25 As the lower income threshold is frozen for the 2012-13 income year (remaining at $31,920), the higher income threshold will be $46,920. ***[Schedule 6, item 8, paragraph 10A(3)]***

Example 1.3

> Angela’s total income is $60,000 in 2012-13. Although previously entitled to the co-contribution in 2011-12, she is no longer eligible as her total income is above the higher income threshold.

6.26 These amendments apply from the 2012-13 income year. ***[Schedule 6, item 10]***

STATEMENT OF COMPATIBILITY WITH HUMAN RIGHTS

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

Superannuation Co-contribution

6.27 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

6.28 This Schedule amends the *Superannuation (Government Co-contribution for Low Income Earners) Act 2003*.

6.29 The purpose of this Schedule is to reduce the rate of payment for the superannuation co-contribution and the maximum payment. In addition, the freeze on indexation of the lower income threshold continues for the 2012-13 income year but will resume in 2013-14 and later income years. The higher income threshold is lowered to be set at $15,000 above the lower income threshold.

Human rights implications

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

Conclusion

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

Minister for Financial Services and Superannuation, the Hon, Bill Shorten MP

Chapter 7
Consolidating the dependency tax offsets

Outline of chapter

7.1 Schedule 7 of the Bill amends:

- the *Income Tax Assessment Act 1997* (ITAA 1997) to create a new, consolidated dependency tax offset for taxpayers maintaining certain classes of dependants who are genuinely unable to work;
- the *Income Tax Assessment Act 1936* (ITAA 1936) to preserve the existing dependency tax offsets for taxpayers eligible for the zone, overseas forces and overseas civilian tax offsets; and
- the ITAA 1936 to reflect the impact of the consolidation of the dependency tax offsets on the net medical expenses tax offset.

Context of amendments

7.2 The Government announced in the 2012-13 Budget that they would consolidate eight existing dependency tax offsets into a single offset that is only available to taxpayers who maintain a dependant who is unable to work due to invalidity or care obligations.

7.3 The dependency tax offsets are currently contained in the ITAA 1936 and are available for taxpayers who maintain certain classes of dependants, which are: invalid spouse, carer spouse, housekeeper, housekeeper (with child), child-housekeeper, child-housekeeper (with child), invalid relative and parent/parent-in-law.

7.4 In certain cases, taxpayers may receive more than one dependency tax offset provided that each dependency tax offset is claimed in respect of a different dependant. For example, a taxpayer who maintains an invalid spouse and an invalid parent-in-law may receive both the invalid spouse and the invalid parent-in-law tax offsets. By contrast, a taxpayer cannot receive a carer spouse and invalid spouse tax offset for the same spouse in the same income year.

7.5 The taxpayer is entitled to the maximum dependency tax offset if the dependant has an adjusted taxable income (ATI) of $282 or less for the period of dependency. ATI, for this purpose, has the meaning given by section 159J of the ITAA 1936 and includes taxable income, reportable employer superannuation contributions, deductible superannuation contributions, adjusted fringe benefits, certain tax-free government pensions or benefits, target foreign income and net investment losses, less child support payments paid to another individual.

7.6 The maximum amount of the dependency tax offset is reduced by $1 for every $4 the dependant's ATI exceeds $282. Based on the maximum amount available for the highest value dependency tax offset, this means that the dependency tax offset is fully phased out when the dependant's ATI exceeds $9,974 for the period of dependency during the 2012-13 income year.

7.7 The maximum amount of dependency tax offset is indexed each year with reference to the All Groups Consumer Price Index (CPI) published by the Australian Bureau of Statistics.

7.8 Taxpayers cannot receive a tax offset for an invalid spouse, carer spouse, housekeeper or child housekeeper for any part of the income year that they are a member of a family in receipt of Family Tax Benefit (Part B) (without shared care), or the taxpayer or their spouse receives parental leave pay.

7.9 Taxpayers cannot receive the dependency tax offset in respect of a spouse if the taxpayer's ATI is more than the income limit for Family Tax Benefit (Part B).

7.10 Taxpayers cannot receive the dependency tax offset in respect of any other class of dependant if the combined ATI of the taxpayer and taxpayer's spouse is more than the income limit for Family Tax Benefit (Part B).

7.11 The income limit for Family Tax Benefit (Part B) is defined in subsection 159J(6) of the ITAA 1936 as the amount specified in subclause 28B(1) of Schedule 1 to the *A New Tax System (Family Assistance) Act 1999*, and is indexed under Schedule 4 to that Act. In 2012-13, the income test for Family Tax Benefit (Part B) is ATI of $150,000.

Interaction with other concessional tax offsets

7.12 Eligibility for a dependency tax offset can be relevant for determining the amount of a taxpayer's other concessional tax offsets. These other offsets are the:

- zone tax offset (provided for in section 79A of the ITAA 1936), which is available to residents of remote or isolated locations in Australia that are prescribed in Schedule 2 to the ITAA 1936;
- overseas forces tax offset (provided for in section 79B of the ITAA 1936), which is available to Australian Defence Force personnel who have served at overseas locations specified by the Treasurer under subsection 79B(5) of the ITAA 1936; and
- overseas civilian tax offset (provided for in section 23AB of the ITAA 1936), which is available to personnel who have served under the control of the United Nations and are prescribed in the regulations.

7.13 The dependency tax offsets are used to calculate the base amount, which forms part of the zone, overseas forces and overseas civilian tax offsets.

7.14 If a taxpayer is entitled to receive one of these three offsets, there will be no change to their dependency tax offset entitlements as a result of these amendments. These taxpayers will continue to access the existing dependency tax offsets in their own right, and will also continue to receive a proportion of the dependency tax offsets as a component of their zone, overseas forces or overseas civilian tax offset.

Interaction with the net medical expenses tax offset and Medicare levy

7.15 Section 159P of the ITAA 1936 provides for taxpayers to claim a tax offset for eligible net medical expenses incurred in respect of certain dependants including those in respect of whom a taxpayer may receive a dependency tax offset.

7.16 The net medical expenses tax offset (NMETO) provides taxpayers with a 20 per cent non-refundable tax offset for eligible out of pocket medical expenses (that is, medical expenses less available reimbursements, such as Medicare and private health insurance refunds) above the claim threshold ($2,120 in 2012-13).

7.17 Similarly, a taxpayer may be entitled to a Medicare levy concession by accessing the family Medicare levy low income threshold if they have a spouse or a child, if they contribute to the maintenance of a child housekeeper, or if they engage a housekeeper.

Summary of new law

Consolidated dependency tax offset

7.18 From 2012-13, eight existing dependency tax offsets will be consolidated into a single, streamlined and non-refundable tax offset that is only available to taxpayers maintaining certain classes of dependants who are genuinely unable to work due to invalidity or carer obligations. This new offset will be called the 'Dependant (Invalid and Carer) Tax Offset'.

7.19 A taxpayer may only receive an amount of the Dependant (Invalid and Carer) Tax Offset if they contribute to the maintenance of their spouse, relative or spouse's relative, who is genuinely unable to work due to invalidity or carer obligations.

7.20 Consequently, a taxpayer may no longer receive a tax offset in respect of a housekeeper or child-housekeeper, as they may not meet the requirement of maintaining a dependant who is genuinely unable to work.

7.21 The Dependant (Invalid and Carer) Tax Offset is equal to the highest value existing dependency tax offset, which is $2,423 in 2012-13, and will be indexed annually in line with CPI .

7.22 A taxpayer may receive an amount of Dependant (Invalid and Carer) Tax Offset if the ATI of the taxpayer, the taxpayer's spouse and the dependant, in respect of whom the offset is being claimed, meet the respective income requirements.

7.23 A taxpayer may receive a reduced amount of Dependant (Invalid and Carer) Tax Offset if the taxpayer was a member of a family in receipt of Family Tax Benefit (Part B) (without shared care), or if the taxpayer or taxpayer's spouse received parental leave payments under the *Paid Parental Leave Act 2010* for only part of a year.

7.24 Taxpayers may receive multiple amounts of the Dependant (Invalid and Carer) Tax Offset, when it is in respect of more than one dependant (other than the taxpayer's spouse) who is genuinely unable to work.

Preserving the existing dependency tax offset for recipients of the zone, overseas forces and overseas civilian tax offsets and the dependent spouse tax offset

7.25 Taxpayers who are eligible for the zone, overseas forces or overseas civilian tax offsets, will experience no change to their current offset entitlement. These taxpayers: may maintain dependants who are able to work; engage housekeepers and maintain child housekeepers; and will continue to receive their dependency tax offset entitlements under existing arrangements, and as an additional component of their zone, overseas forces or overseas civilian tax offset entitlement. Eligibility for these offsets will continue to be determined under the ITAA 1936.

7.26 There is no change to the amount or the eligibility requirements for the dependent spouse tax offset (DSTO). Aside from recipients of the zone, overseas forces or overseas civilian tax offsets, eligibility for the DSTO is limited to taxpayers who contribute to the maintenance of a spouse born before 1 July 1952.

7.27 A taxpayer who maintains an invalid spouse or a carer spouse who was born before 1 July 1952 would be eligible to receive an amount of DSTO, rather than an amount of the Dependant (Invalid and Carer) Tax Offset, in respect of that spouse.

Interaction with the net medical expenses tax offset and Medicare levy

7.28 In determining the amount of NMETO a taxpayer may receive with respect to the 2012-13 and future income years, a taxpayer will be able to include the net medical expenses incurred in relation to a dependant who is a relative, spouse's relative, parent or spouse's parent who is genuinely unable to work due to invalidity or care obligations.

7.29 Similarly, a taxpayer may be entitled to a Medicare levy concession by accessing the family Medicare levy low income threshold if they have a spouse or a child.

7.30 Taxpayers eligible for the zone, overseas forces or overseas civilian tax offset will not experience any change to their NMETO entitlements or Medicare levy concession.

Comparison of key features of new law and current law

New law	*Current law*
The invalid spouse, carer spouse, invalid relative, and parent/parent-in-law offsets are consolidated into the Dependant (Invalid and Carer) Tax Offset. A taxpayer will only be able to receive the Dependant (Invalid and Carer) Tax Offset if they maintain a dependant who is genuinely unable to work due to invalidity or carer obligations during an income year. A taxpayer will no longer be able to receive a tax offset in respect of a child-housekeeper, child-housekeeper (with child), housekeeper or housekeeper (with child) as those dependants do not meet the requirement of being genuinely unable to work.	A taxpayer who maintains an individual within a set class of dependant (invalid spouse, carer spouse, housekeeper, housekeeper (with child), child-housekeeper, child-housekeeper (with child), invalid relative or parent/parent-in-law) during an income year may be able to receive an amount of dependency tax offset.
A taxpayer may receive more than one amount of Dependant (Invalid and Carer) Tax Offset, as long as each amount is in respect of a different dependant (but not in respect of multiple spouses).	A taxpayer may receive more than one dependency tax offset as long as each offset is received in respect of a different individual (but not in respect of multiple spouses).
The maximum amount of the Dependant (Invalid and Carer) Tax Offset for 2012-13 is $2,423.	The maximum offset amount varies depending on which dependency tax offset a taxpayer is entitled to.
A taxpayer is entitled to include the net medical expenses of a dependant who is a relative, spouse's relative, parent or spouse's parent who is genuinely unable to work due to invalidity or care obligations as part of their NMETO claim.	A taxpayer is entitled to include the net medical expenses of a dependant who is a relative, spouse's relative, parent, spouse's parent, child-housekeeper, child-housekeeper (with child), housekeeper or housekeeper (with child) as part of calculating an amount of NMETO.

New law	***Current law***
A taxpayer may be entitled to a concession by accessing the family Medicare levy low income threshold if they have a spouse or a child.	A taxpayer may be entitled to a Medicare levy concession by accessing the family Medicare levy low income threshold if they have a spouse or a child, if they contribute to the maintenance of a child housekeeper, or if they engage a housekeeper.
A taxpayer who maintains a dependant and who is eligible for the zone, overseas forces or overseas civilian tax offset will experience no change to any of their offset and concession entitlements or amounts.	A taxpayer who maintains a dependant and who is eligible for the zone, overseas forces or overseas civilian tax offset: can receive an amount of dependency tax, and can receive an additional amount of dependency tax offset as part of their zone, overseas forces or overseas civilian tax offset entitlement. They can also include the net medical expenses incurred in respect of eligible dependants in calculating their NMETO entitlement, and may be entitled to a Medicare levy concession by accessing the family Medicare levy low income threshold if they have a spouse or a child, if they contribute to the maintenance of a child housekeeper, or if they engage a housekeeper.

Detailed explanation of new law

Consolidated dependency tax offset

7.31 These amendments introduce a new tax offset, which will be available to eligible taxpayers maintaining individuals who fall within certain classes of dependants who are genuinely unable to work due to invalidity or care obligations. ***[Schedule 7, item 1, Subdivision 61-A of the ITAA 1997].***

7.32 This offset is called the Dependant (Invalid and Carer) Tax Offset.

Eligibility for the Dependant (Invalid and Carer) Tax Offset

7.33 A taxpayer may be entitled to this offset for an income year if, during that year, they contributed to the maintenance of an eligible dependant.

7.34 The circumstances whereby a taxpayer may be found to contribute to the maintenance of an eligible dependant are not limited. However, where the taxpayer and the dependant reside together, the taxpayer would generally be considered to have contributed to the maintenance of that dependant.

7.35 An eligible dependant may include:

- a taxpayer's spouse, parent, child (aged 16 years or over), brother or sister (aged 16 years or over) who is genuinely unable to work due to invalidity;
- the taxpayer's spouse's parent, brother or sister (aged 16 years or over), who is genuinely unable to work due to invalidity; or
- a taxpayer's spouse or parent/parent-in-law, who is genuinely unable to work due to carer obligations.

[Schedule 7, item 1, section 61-10 of the ITAA 1997]

7.36 A dependant is considered to be genuinely unable to work due to invalidity where that person receives: a disability support pension or a special needs disability support pension under the *Social Security Act 1991*; or an invalidity service pension under the *Veterans' Entitlements Act 1986*. ***[Schedule 7, item 1, subsection 61-10(2) of the ITAA 1997]***

7.37 A dependant is considered to be genuinely unable to work due to carer obligations if they are:

- receiving a carer payment or carer allowance under the *Social Security Act 1991*; or
- wholly engaged in providing care to a relative who receives: a disability support pension or a special needs disability pension under the *Social Security Act 1991*; or an invalidity service pension under the *Veterans' Entitlements Act 1986*.

[Schedule 7, item 1, subsections 61-10(3) and (4) of the ITAA 1997]

Example 7.1

> Peter and Loretta have a son called Adam who is over the age of 16 years and receives a part-rate disability support pension. Loretta does not work as she cares for Adam. Peter may be able to claim amounts of the Dependant (Invalid and Carer) Tax Offset in respect of Loretta, who is unable to work due to her carer obligations, and Adam who is unable to work due to invalidity.

7.38 An eligible dependant must be an Australian resident, unless they are the taxpayer's spouse or child. A foreign resident spouse or child is an eligible dependant if the taxpayer has a domicile in Australia. This condition replicates the eligibility in section 159J (rebates for dependants) of the ITAA 1936. ***[Schedule 7, item 1, paragraph 61-10(1)(c) of the ITAA 1997]***

7.39 A taxpayer may receive more than one amount of Dependant (Invalid and Carer) Tax Offset in an income year if they maintain more than one eligible dependant (except where they maintain more than one spouse) during that income year. ***[Schedule 7, item 1, subsection 61-10(5) of the ITAA 1997]***

7.40 Where a taxpayer maintains two or more spouses in respect of whom the taxpayer may be eligible for an amount of either the DSTO or the Dependant (Invalid and Carer) Tax Offset, the taxpayer may only receive an amount of offset in respect of the spouse with whom the taxpayer resides. ***[Schedule 7, item 1, subsection 61-15(1) of the ITAA 1997]***

7.41 Where the taxpayer does not reside with any of their spouses (who are genuinely unable to work due to invalidity or carer obligations), or where they reside with more than one of these spouses, the taxpayer would need to determine the amount of either the DSTO or the Dependant (Invalid and Carer) Tax Offset that they could receive in respect of each spouse. Their entitlement is the smallest of those amounts. ***[Schedule 7, item 1, subsection 61-15(2) of the ITAA 1997]***

Eligibility subject to income testing

7.42 Eligibility for the Dependant (Invalid and Carer) Tax Offset is income tested according to the 'income limit for family assistance purposes'. ***[Schedule 7, item 1, subsection 61-20(1) of the ITAA 1997]***

7.43 This income testing is based on the ATI of the taxpayer where the offset is claimed in respect of a spouse, or the combined ATI of the taxpayer and the taxpayer's spouse where it is claimed in respect of any other class of dependant.

7.44 ATI, for the purposes of this tax offset, has the meaning given by section 159J of the ITAA 1936 and includes taxable income, reportable

employer superannuation contributions, deductible superannuation contributions, adjusted fringe benefits, certain tax-free government pensions or benefits, target foreign income and net investment losses, less child support payments paid to another individual.

7.45 The relevant ATI threshold for income testing of the offset is $150,000 in 2012-13 under subclause 28B(1) of Schedule 1 to the *A New Tax System (Family Assistance) Act 1999*.

Example 7.2

> Mel and Yot are married and Yot has an ATI of $160,000 in 2012-13. Mel does not work as she cares for her father who receives an invalidity service pension. Yot is unable to claim the Dependant (Invalid and Carer) Tax Offset in respect of Mel, as his ATI is more than $150,000 in 2012-13.

7.46 If the taxpayer had a spouse for only part of the year, the spouse's ATI is pro-rated on the proportion of the year that the spouse was partnered with the taxpayer. ***[Schedule 7, item 1, subsection 61-20(2) of the ITAA 1997]***

7.47 If the taxpayer had different spouses during different parts of the year, the spouses' ATI are pro-rated on the proportion of the year that those spouses were partnered with the taxpayer. ***[Schedule 7, item 1, subsection 61-20(3) of the ITAA 1997]***

7.48 A taxpayer is not entitled to the Dependant (Invalid and Carer) Tax Offset in respect of a spouse for a period of the income year if they or their spouse received Family Tax Benefit (Part B) (without shared care). ***[Schedule 7, item 1, sections 61-25 and 61-40 of the ITAA 1997]***

Amount of the Dependant (Invalid and Carer) Tax Offset

7.49 For each eligible dependant, the maximum amount of the Dependant (Invalid and Carer) Tax Offset is $2,423. The amount is indexed annually in line with the CPI . ***[Schedule 7, item 1, subsection 61-30 of the ITAA 1997 and item 8, section 960-265 of the ITAA 1997]***

7.50 The Dependant (Invalid and Carer) Tax Offset uses the core indexation rules contained in Subdivision 960-M of the ITAA 1997.

7.51 Depending on whether certain circumstances arise, the amount of the Dependant (Invalid and Carer) Tax Offset that the taxpayer is eligible for may be reduced.

7.52 These reductions are determined in a particular order and none, some or all may apply, which are set out below.

Reduction for shared care arrangements

7.53 A taxpayer or their spouse may have shared care arrangements for a child. Under a shared care arrangement, two or more adults who care for a child, and who are not members of the same couple, may each be eligible for Family Tax Benefit (Part B) provided that each adult cares for the child between 35 per cent and 65 per cent of the care period.

7.54 Where a taxpayer or taxpayer's spouse had shared care arrangements for a child for which they are receiving Family Tax Benefit (Part B), then the amount of Dependant (Invalid and Carer) Tax Offset is reduced by multiplying the ratio of the shared care rate of Family Tax Benefit (Part B). This ensures that a taxpayer who only has a partial eligibility for Family Tax Benefit (Part B) has a partial eligibility for the Dependant (Invalid and Carer) Tax Offset. ***[Schedule 7, item 1, section 61-35 of the ITAA 1997]***

Example 7.3

> Morten and Suzanna are married. Suzanna maintains Morten as an invalid spouse who is in receipt of a part invalidity pension. Morten has a daughter, Manuja, from his previous marriage to Tachelle. Morten and Tachelle share care of Manuja. Morten and Tachelle are each eligible to receive an amount of Family Tax Benefit (Part B) for Manuja. Morten's share care rate is determined to be 40 per cent.
>
> Since Morten receives Family Tax Benefit (Part B) for a child with shared care, Suzanna may not receive the full $2,423 of the Dependant (Invalid and Carer) Tax Offset in respect of Morten. Instead, the amount is reduced by the 40 per cent (or $969) relevant to Morten's shared care of Manuja. As a result, Suzanna may receive 60 per cent of the Dependant (Invalid and Carer) Tax Offset for that income year, or $1,453 subject to meeting the other eligibility requirements.

Reduction for part year eligibility

7.55 After reducing the maximum amount of the offset for shared care arrangements (where relevant and applicable), the amount of the offset otherwise available is further reduced in situations where a taxpayer may only be entitled to an amount of the Dependant (Invalid and Carer) Tax Offset for part of an income year.

7.56 The reduction to the amount of the offset is that which the Commissioner of Taxation (Commissioner) considers to be a reasonable apportionment in the circumstances. ***[Schedule 7, item 1, section 61-40 of the ITAA 1997]***

7.57 In coming to this decision, the Commissioner must have regard to a number of factors including:

- whether the taxpayer or individuals other than the taxpayer contributed to the maintenance of the dependant during part of the year;
- the type of dependant that the taxpayer is claiming the offset in respect of for part of the year;
- whether the taxpayer is a member of a family in receipt of Family Tax Benefit (Part B) (without shared care) for part of the year; and
- whether parental leave pay is payable to them under the *Paid Parental Leave Act 2010* for part of the year.

[Schedule 7, item 1, subsection 61-40(2) of the ITAA 1997]

Example 7.4

Chris and Ash are in a de-facto relationship. Chris cares for their son Ollie who is 21 years of age, and who started to receive a disability support pension three months before the end of the income year. As Chris is only an eligible dependant for part of the year, Ash's maximum tax offset is apportioned accordingly: three months divided by twelve months multiplied by the full tax offset of $2,423, or $605.

Example 7.5

Fred is married to Susie who cannot work due to the full time care of her invalid father. For three months of the income year, Fred and Susie are members of a family in receipt of Family Tax Benefit (Part B) (without shared care). This represents 25 per cent of the full income year. Fred is not entitled to any tax offset for this part of the income year.

In determining the amount of tax offset to be allowed to Fred for the full income year, the Commissioner has regard to the circumstances that exist in the remaining part of the income year. In the absence of any other relevant factors, the Commissioner would likely determine the amount of the tax offset available to Fred for the income year to be $1,817, or 75 per cent of the maximum offset amount of $2,423, which is the full amount of tax offset available to Fred after disregarding that part of the income year in which he and Susie were members of a family in receipt of Family Tax Benefit (Part B).

Reduction where the adjustable taxable income of the dependant is over $282 for a particular period

7.58 After reducing the maximum amount of the offset for shared care arrangements and part year eligibility (where relevant and applicable), the amount otherwise available is then reduced by $1 for each $4 by which the eligible dependant's ATI for the period of dependency exceeds $282. ***[Schedule 7, item 1, subsection 61-45 of the ITAA 1997]***

7.59 The period of dependency means the time during the year that the taxpayer contributed to the maintenance of the other individual, which may be the whole year or part of the year.

Example 7.6

Mike and Sumita are married. Sumita does not work for the entire income year as she cares for her invalid brother Jarrod. Sumita has annual income of $5,000. Mike and Sumita's combined ATI is $105,000. Mike will be able to claim a Dependant (Invalid and Carer) Tax Offset of $1,244 in respect of Sumita. This is less than the maximum, as the offset is reduced by $1 of every $4 that Sumita's income exceeds $282.

Preserving the existing dependency tax offsets for recipients of the zone, overseas forces and overseas civilian tax offsets and the dependent spouse tax offset

7.60 There is no change to the dependency tax offset entitlements of taxpayers who are eligible for the zone rebate (section 79A of the ITAA 1936) the overseas forces (section 79B of the ITAA 1936) rebate or the overseas civilian rebate (section 23AB of the ITAA 1936) ***[Schedule 7, item 2, subsection 159(1F) of the ITAA 1936]***

7.61 Only taxpayers who are eligible for the zone, overseas forces or overseas civilian tax offsets may receive an amount of dependency tax offset in respect of a housekeeper or housekeeper (with child). ***[Schedule 7, item 5, subsection 159L(3C) of the ITAA 1936]***

7.62 Taxpayers who are eligible for the zone, overseas forces or overseas civilian tax offsets are not entitled to the Dependant (Invalid and Carer) Tax Offset. ***[Schedule 7, item 1, paragraphs 61-10(1)(d) and (c) of the ITAA 1997]***

7.63 Taxpayers maintaining a dependent spouse born before 1 July 1952 will still be able to receive the DSTO. ***[Schedule 7, item 2, subsection 159(1G) of the ITAA 1936]***

Example 7.7

Blair and Janine are in a de-facto relationship and reside in Townsville, which is in zone B for the purpose of the zone tax offset. Blair cares for his mother who is unable to work and who receives an invalid pension. Janine is precluded from claiming the Dependent (Invalid and Carer) Tax Offset, because she resides in a zone tax offset area. Janine is, however, able to claim an amount of DSTO under the existing provisions. Janine is also able to receive an additional 20 per cent of her DSTO entitlement as part of her zone tax offset entitlement.

Interaction with the net medical expenses offset and Medicare levy concession

7.64 These amendments expand the list of dependants for the purposes of determining the amount of NMETO a taxpayer may receive under section 159P of the ITAA 1936 to include a person in respect to which the taxpayer receives an amount of the new Dependant (Invalid and Carer) Tax Offset. ***[Schedule 7, item 6, paragraphs 159P(4)(e) and (f) of the ITAA 1936]***

7.65 The effect of these amendments will also mean that a taxpayer may be entitled to a concession by accessing the family Medicare levy low income threshold if they have a spouse or a child.

Definitions

7.66 These amendments amend the definition of 'invalid relative' and 'invalid spouse' in the ITAA 1936 to ensure there is consistency in the offsets between the ITAA 1936 and the ITAA 1997, and to remove the current requirement for an invalid relative or invalid spouse to be issued a certificate by a medical officer of the Health Department or by a medical practitioner appointed by the Families Secretary. ***[Schedule 7, item 3, subsection 159J(6) of the ITAA 1936 and Schedule 7, item 4, subsection 159J(6) of the ITAA 1936]***

7.67 This requirement is being removed because such certificates have not been issued in recent years and are no longer issued.

7.68 In order to ensure that the meaning of ATI is the same for the purposes of the ITAA 1997 and the ITAA 1936, these amendments also alter the definition of 'ATI for offsets' in subsection 995-1(1) of the ITAA 1997. ***[Schedule 7, item 9, subsection 995-1(1) of the ITAA 1997]***

7.69 The table of tax offsets set out in the ITAA 1997 is being updated to include a reference to the Dependant (Invalid and Carer) Tax. ***[Schedule 7, item 7, section 13-1 of the ITAA 1936]***

Application and transitional provisions

7.70 These amendments apply to assessments for the 2012-13 income year and later income years. ***[Schedule 7, item 10]***

STATEMENT OF COMPATIBILITY WITH HUMAN RIGHTS

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

Consolidating the dependency tax offsets

7.71 Schedule 7 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

7.72 Schedule 7 amends:

- the *Income Tax Assessment Act 1997* to create a new, consolidated dependency tax offset for taxpayers maintaining certain classes of dependant who are genuinely unable to work;
- the *Income Tax Assessment Act 1936* to preserve the existing dependency tax offsets for taxpayers eligible for the zone, overseas forces and overseas civilian tax offsets; and
- the *Income Tax Assessment Act 1936* to reflect the impact of the consolidation of the dependency tax offsets on the net medical expenses tax offset.

Human rights implications

7.73 This Schedule engages the following human rights:

Right to Social Security

7.74 Article 9 of the International Covenant on Economic, Social and Cultural Rights (ICESCR) recognises the right of everyone to social security, including social insurance.

7.75 Consolidating the dependency tax offsets better targets assistance to taxpayers contributing to the maintenance of dependants who are genuinely unable to work.

7.76 The consolidation of the dependency tax offsets complements the provision of direct assistance under the *Social Security Act 1991* and the *Veterans' Entitlements Act 1986.* It does not alter anybody's entitlement to direct assistance through the social security system, and does not affect anybody's right to social security.

7.77 Australian Government annual expenditure on social security and welfare is estimated to be around $130 billion for 2012-13. Improving targeting by consolidating the dependency tax offsets is one of a number of measures the Government has identified to ensure an equitable and sustainable social security system.

Right to Health

7.78 Article 12(1) of the ICESCR recognises the right to the enjoyment of the highest attainable standard of physical and mental health.

7.79 While the ICESCR contains no definition of health, the UN Committee on Economic, Social and Cultural Rights has stated that the right to health is not to be understood as a right to be healthy.

7.80 Limiting access to the net medical expenses tax offset and to the Medicare levy concessions does not reduce the availability or access to comprehensive medical services in Australia.

7.81 These limitations reduce a Government rebate for the out-of-pocket cost of medical expenses and increase the Medicare levy payable for some taxpayers maintaining dependants who do not work, but who are able to.

7.82 Australian Government annual health expenditure is estimated to be around $61 billion for 2012-13. Better targeting support through NMETO and Medicare levy concessions will ensure a strong and sustainable health care system.

Conclusion

7.83 This Schedule is compatible with human rights. It advances the protection of human rights in relation to health and social security by ensuring that assistance is better targeted, and does not raise any human rights issues.

Assistant Treasurer, the Hon David Bradbury

Chapter 8
Taxation of Financial Arrangements

Outline of chapter

8.1 Schedule 8 to this Bill amends Division 230 of the *Income Tax Assessment Act 1997* (ITAA 1997) and the *Tax Laws Amendment (Taxation of Financial Arrangements) Act 2009* (TOFA Act) to clarify and refine the operation of certain aspects of the Taxation of Financial Arrangements regime (the TOFA regime).

Context of amendments

8.2 The TOFA provisions, which include Division 230 and the TOFA Act, commenced on 26 March 2009. The TOFA regime applies for income years commencing on or after 1 July 2010; or on or after 1 July 2009 if a taxpayer has elected to apply the Division in that earlier income year.

8.3 The TOFA provisions modernise the finance taxation system by better reflecting the economic and commercial substance of financial arrangements. They represent a major legislative reform that affects a wide range of financial arrangements; including arrangements that are complex in nature.

8.4 These amendments are the outcome of ongoing monitoring of the implementation of the TOFA regime, and have been developed following extensive consultation with industry.

8.5 The amendments refine and clarify the operation of the TOFA provisions, lower compliance costs and provide additional certainty to affected taxpayers. Consequently, these amendments apply from the commencement of the TOFA regime.

8.6 All references to legislative provisions in this chapter are references to the ITAA 1997, unless otherwise stated.

Summary of new law

8.7 Schedule 8 to this Bill amends the TOFA provisions to clarify and refine the operation of certain aspects of the TOFA regime. The amendments relate to the:

- core rules;
- accruals and realisation tax timing methods;
- fair value tax timing method;
- hedging financial arrangements method;
- transitional balancing adjustment provisions; and
- eligibility requirements for making certain elections.

8.8 With respect to the core rules, the amendments clarify that, when determining whether a gain or loss arises from a financial arrangement:

- taxpayers must have regard to financial benefits that they are both certain and uncertain of providing or receiving; and
- financial benefits are generally not attributable to interest or interest-like amounts.

8.9 With respect to the accruals and realisation tax timing methods, the amendments ensure that:

- a gain or loss from a financial arrangement that arises from a particular event, such as the receipt or provision of a financial benefit or cessation of a right or obligation, (a particular gain or loss) can be sufficiently certain, even if the financial arrangement consists of other financial benefits that the taxpayer is not sufficiently certain of receiving or providing;
- if, at the start of a financial arrangement, a taxpayer has both a sufficiently certain overall gain or loss and sufficiently certain particular gains or losses, the accruals method applies to the particular gains and losses unless the taxpayer:
  - chooses to apply the accruals method to the overall gain or loss; or

  - cannot apply the accruals method to the particular gains and losses;

- a gain or loss arising from a prepayment is spread over the period to which it relates;

- taxpayers have regard to a notional principal when applying the accruals method to a gain or loss arising from a single financial benefit;

- a gain resulting from a reversal of an impairment that is to be spread across the period occurring after the reversal does not reflect losses resulting from the impairment that the taxpayer could not deduct;

- running balancing adjustments are not made upon an impairment, reversal of impairment or the writing off of a bad debt; and

- where the realisation method applies to a gain or loss from a financial arrangement, that gain or loss is realised when the last of the financial benefits taken into account actually:

  - are provided, or become due (whichever occurs earlier); or

  - the rights and obligations concerning them cease.

8.10 With respect to the fair value tax timing method, the amendments ensure that the fair value method can be applied to recognise, for tax purposes, some gains and losses from financial arrangements that are assets or liabilities treated as at fair value through profit or loss for accounting purposes. This is even if those assets or liabilities are not classified or designated in accordance with accounting principles as at fair value through profit or loss.

8.11 With respect to the hedging financial arrangements method, the amendments ensure that:

- the hedging financial arrangements election applies in a consistent manner to:

  - hedging financial arrangements that are hedging instruments for accounting purposes on a 'one-in all-in' basis; and

  - foreign currency hedges of anticipated dividends from a connected entity; and

- if a hedged item is a net investment in a foreign operation carried on through a subsidiary or a company in which the taxpayer holds shares, separate regard is had to each relevant interest, for tax classification purposes.

8.12 With respect to transitional balancing adjustments, the amendments ensure that an alternative method for calculating a transitional balancing adjustment can be used only if the amount of the balancing adjustment worked out under that method approximates the amount of the balancing adjustment worked out under the primary method.

8.13 With respect to requirements for certain TOFA elections, the amendments ensure that foreign banks may use an audited Statement of Financial Position and Statement of Financial Performance that they are required under the prudential standards to submit to the Australian Prudential Regulation Authority to satisfy eligibility requirements for making various TOFA elections.

8.14 Finally, some minor technical amendments are made to ensure language is used consistently in the TOFA provisions and to make some minor drafting corrections.

Comparison of key features of new law and current law

New law	*Current law*
Core rules	
In determining whether a gain or loss arises from a financial arrangement, taxpayers must also have regard to financial benefits that they are uncertain of providing or receiving.	In determining whether a gain or loss arises from a financial arrangement, taxpayers need only have regard to financial benefits that have been, or are to be, received or provided.
The general cost attribution rules determine whether financial benefits are attributable to one another when working out whether a gain or loss arises from a financial arrangement. Under those principles, financial benefits that are interest or interest-like amounts generally do not have other financial benefits attributable to them.	In determining whether a gain or loss arises from a financial arrangement, financial benefits are not attributable to interest or interest-like amounts.

New law	*Current law*
The accruals and realisation methods	
A particular gain or loss from a financial arrangement can be sufficiently certain even if the financial arrangement consists of both financial benefits that the taxpayer is and is not sufficiently certain of receiving or providing.	It is arguable that a taxpayer cannot have a sufficiently certain particular gain or loss from a financial arrangement if there are financial benefits under that arrangement (which are not taken in to account in determining the gain or loss) that are not sufficiently certain.
If a taxpayer has both a sufficiently certain overall gain or loss and sufficiently certain particular gains or losses at the start of a financial arrangement, the accruals method applies to the particular gains and losses unless the taxpayer: • chooses to apply the accruals method to the overall gain or loss; or • cannot apply the accruals method to the particular gains and losses.	If a taxpayer has both a sufficiently certain overall gain or loss and sufficiently certain particular gains or losses at the start of a financial arrangement, the accruals method applies to the particular gains or losses only if, as a whole, they adequately represent the overall gain or loss from that arrangement.
Taxpayers must spread a gain or loss arising from a prepayment over the period to which it relates.	Taxpayers either: • cannot spread a gain or loss arising from a prepayment; or • cannot spread a gain or loss arising from a prepayment over the period to which it relates.
Taxpayers must have regard to a notional principal when applying the accruals method to a gain or loss arising from a single financial benefit.	It is unclear how the accruals method applies to a gain or loss arising from a single financial benefit.
Upon a reversal of an impairment loss, positive amounts to be spread over the period after the reversal do not include losses resulting from the impairment that the taxpayer could not deduct, and were not given some other tax recognition.	Upon a reversal of an impairment loss, taxpayers must spread a re-estimated gain or loss. This re-estimated gain or loss may include losses resulting from impairment, even if the taxpayer could not deduct those losses.
A running balancing adjustment is not made upon impairment, reversal of impairment or the writing off of a bad debt.	It is arguable that a running balancing adjustment can be made upon impairment, reversal of impairment or the writing off of a bad debt.

New law	***Current law***
If the realisation method applies to a gain or loss from a financial arrangement, that gain or loss is realised when the last of the financial benefits taken into account actually: • are provided, or become due (whichever occurs earlier); or • the rights and obligations concerning them cease.	A gain or loss is worked out taking into account financial benefits or the cessation of related rights and obligations. If the realisation method applies to a gain or loss from a financial arrangement, that gain or loss is realised when the last financial benefit taken into account actually is provided or becomes due (whichever occurs earlier).
The fair value method	
The fair value method can be applied to financial arrangements that are assets or liabilities which have the same treatment of being as at fair value through profit or loss for accounting purposes. This is even if those assets or liabilities are not technically classified or designated in accordance with accounting standards as at fair value through profit or loss for accounting purposes.	The fair value method can apply to financial arrangements only if the financial arrangements are assets or liabilities that are classified or designated as at fair value through profit or loss for accounting purposes.
The hedging financial arrangements method	
A hedging financial arrangements election applies, in a consistent manner, to: • all financial arrangements that are hedging instruments for accounting purposes on a 'one-in all-in' basis; and • foreign currency hedges of anticipated dividends from a connected entity. Where a documentation requirement is failed after a hedging financial arrangements election has applied to a hedging financial arrangement, the election cannot apply to any financial arrangement that the taxpayer starts to have after the failure.	A hedging financial arrangements election may only apply to a hedging financial arrangement if, among other things, certain documentation requirements are satisfied in respect of the arrangement.

New law	*Current law*
If a hedged item is a net investment in a foreign operation carried on through a subsidiary or a company in which the taxpayer holds shares, for tax classification purposes, separate regard is to be had to each relevant interest.	If a hedged item is a net investment in a foreign operation carried on through a subsidiary or a company in which a taxpayer holds shares, for tax classification purposes, the hedged item is the interest in the shares of the company.
Transitional balancing adjustments	
The alternative method for calculating a transitional balancing adjustment can only be used if the relevant amount from the taxpayer's financial reports has been recognised in profit or loss in accordance with accounting principles.	Taxpayers may elect to apply the TOFA regime to financial arrangements that they hold before their first TOFA year. If such an election is made, a transitional balancing adjustment must be made with respect to these financial arrangements. The amount of the balancing adjustment must be calculated using either the primary method or the alternative method (which uses amounts from the financial reports of taxpayers).
Elective requirements	
Foreign banks that have branches in Australia may use the audited Statement of Financial Position and Statement of Financial Performance that they are required to provide to the Australian Prudential Regulation Authority, under the prudential standards, to satisfy the eligibility requirements for making various TOFA elections.	Foreign banks that have branches in Australia can only satisfy the eligibility requirements for making various TOFA elections if they have appropriately prepared and audited foreign financial reports.

Detailed explanation of new law

Core rules

8.15 Under the TOFA provisions, a gain or loss from a financial arrangement is worked out by offsetting costs (financial benefits provided) against proceeds (financial benefits received). The cost attribution rules determine which costs should be subtracted from which proceeds.

Attribution of costs

8.16 Currently, it is arguable that the cost attribution rules apply only to financial benefits that taxpayers have received or provided or are certain of receiving or providing. This is because, to work out the amount of a gain or loss from a financial arrangement, taxpayers are obliged to have regard only to financial benefits that they have provided or are to provide.

8.17 However, before determining whether a gain or loss is certain or not, taxpayers are required to determine what the gains and losses from a financial arrangement are. Therefore, taxpayers need to have regard to all financial benefits under the arrangement — both those they are certain and uncertain of receiving or providing.

8.18 Therefore, the amendments clarify that taxpayers should also have regard to financial benefits that they might receive or provide when determining whether they have a gain or loss from a financial arrangement. This ensures that taxpayers may attribute a financial benefit that they are uncertain of providing or receiving as a cost or proceed when determining whether they have a gain or loss from a financial arrangement. ***[Schedule 8, items 1, 2, 4 and 6, sections 230-70 and 230-75]***

Interest

8.19 Currently, the general cost attribution rules provide that one financial benefit may be attributable to another when working out whether a gain or loss arises from another financial benefit. This attribution must be reasonable and reflect appropriate and commercially accepted valuation principles.

8.20 Currently, there is a specific cost attribution rule that applies to financial benefits that are interest or interest-like amounts. An amount is an interest-like amount if it represents a return paid or provided on a debt interest, is something in the nature of interest or is something that could reasonably be regarded as being a substitute for interest.

8.21 The specific cost attribution rule provides that a financial benefit cannot be attributed to interest or an interest-like amount when working out whether a gain or loss arises from the interest or interest-like amount.

8.22 The rationale for the specific cost attribution rule is to clarify that interest and these interest-like amounts are effectively payments for the time value of money; not payments for the receipt of another financial benefit. Therefore, consistent with the general cost attribution rule, no financial benefit can be reasonably attributable to these interest or interest-like amounts.

8.23 However, in some circumstances, it may be unclear whether a financial benefit may be characterised as interest or an interest-like amount. For example, a financial benefit provided may consist of both interest and an amount of principal repaid. Alternatively, a financial benefit may be the interest component of an interest-strip security. In these circumstances, it may (though not necessarily) be appropriate to attribute a cost or proceed to these financial benefits under the general cost attribution rules.

8.24 Therefore, the amendments ensure that the general cost attribution rules apply to work out gains or losses arising from the receipt or payment of interest or interest-like amounts. This ensures that a financial benefit is attributable to interest or an interest-like amount in appropriate circumstances. However, consistent with the rationale for the current specific cost attribution rule, the application of the general cost attribution rules generally result in no financial benefits being attributable to interest or an interest-like amount. ***[Schedule 8, items 3 to 6, notes to sections 230-70 and 230-75]***

8.25 A consequential amendment also removes cross references to the specific attribution rule. ***[Schedule 8, item 7, subsection 230-200(2)]***

The accruals and realisation methods

8.26 The accruals and realisation methods are default tax timing methods for taxing financial arrangements under the TOFA provisions.

8.27 Currently, taxpayers apply the accruals method when they have a sufficiently certain overall or particular gain or loss from a financial arrangement. The tax system recognises parts of these gains and losses as they are spread over a period of time.

8.28 The realisation method may apply to all other gains and losses. The tax system recognises these gains and losses when they occur.

Sufficiently certain particular gains and losses

8.29 The accruals method applies to sufficiently certain overall or particular gains and losses from financial arrangements. A sufficiently certain overall gain or loss arises if:

- it is sufficiently certain, at the time a taxpayer starts to have a financial arrangement, that there is an overall gain or loss from the arrangement of at least a particular amount; and

- having regard to the risk that the receipt or provision of financial benefits under the arrangement that are not sufficiently certain may reduce that gain or loss.

8.30 A sufficiently certain particular gain or loss arises if:

- it is sufficiently certain that a gain or loss, of at least a particular amount, will be made upon the receipt or provision of a financial benefit, or upon the cessation of a right or obligation, under an arrangement; and
- having regard to the risk that the receipt or provision of financial benefits under the arrangement that are not sufficiently certain may reduce that gain or loss.

8.31 It is arguable that taxpayers must have a sufficiently certain overall gain or loss from a financial arrangement to have a sufficiently certain particular gain or loss. This is because taxpayers must have regard to all financial benefits under a financial arrangement when determining whether a particular gain or loss is sufficiently certain.

8.32 This is unintended. If a financial benefit that a taxpayer is not sufficiently certain of receiving or providing is not attributable in working out a particular gain or loss, it has no impact on whether that gain or loss is sufficiently certain. Taxpayers ought to be able to have a sufficiently certain particular gain or loss from a financial arrangement even if there are financial benefits under that arrangement that are not sufficiently certain.

8.33 Consequently, the amendments clarify that, when determining if a particular gain or loss is sufficiently certain, taxpayers need only have regard to financial benefits reasonably attributable to the financial benefit giving rise to that gain or loss. ***[Schedule 8, item 10, paragraph 230-110(2)(a)]***

Example 8.1

DeFran Co holds an equity-linked bond that pays an annual coupon. When the bond matures, DeFran Co will either pay or receive an additional amount based on the performance of the issuer's listed share price.

DeFran Co does not have regard to the additional contingent financial benefit that may become payable upon maturity when determining whether it has a sufficiently certain particular gain referable to the annual coupon. This is because that financial benefit is not a cost attributable to the receipt of the coupon payment.

Precedence of particular gains or losses

8.34 Currently, taxpayers may apply the accruals method to particular gains or losses from a financial arrangement only if they adequately represent the overall gain or loss from that arrangement.

8.35 Applying the accruals method, an overall gain or loss from a financial arrangement is spread over the period during which a taxpayer holds the arrangement. A particular gain or loss from a financial arrangement is spread over the period to which the gain or loss relates.

8.36 As such, the particular gain or loss approach more accurately reflects the compounding accruals method (which involves allocating gains and losses to the periods to which they relate). The overall gain or loss approach approximates the compounding accruals method and might be used to save compliance costs.

8.37 The amendments ensure that the particular gain or loss approach is the default approach. This means that if, at the time a taxpayer starts to have a financial arrangement, the taxpayer is sufficiently certain of both an overall gain or loss and particular gains or losses from the arrangement, the taxpayer can only apply the accruals method to the overall gain or loss if:

- they choose to do so; or
- they cannot apply the accruals method to the particular gains or losses arising from the financial arrangement.

[Schedule 8, items 11 and 14, paragraph 230-100(2)(c)]

8.38 Consequential amendments ensure that where the accruals method could apply to an overall gain or loss, but the taxpayer does not choose to apply it, the taxpayer can apply the accruals method to particular gains or losses that become sufficiently certain before the taxpayer starts to have the arrangement. ***[Schedule 8, item 12, subparagraph 230-100(3)(b)(i)]***

8.39 Consequential amendments also ensure that when a taxpayer is working out whether they have a sufficiently certain particular gain or loss, a financial benefit cannot be disregarded on account of its inclusion in the calculation of an overall gain or loss, unless the accruals method is applied to that overall gain or loss. ***[Schedule 8, items 13, paragraph 230-110(2)(b)]***

Example 8.2

On 1 July 2013, Fred Co provides a $10,000 loan at 10 per cent annual simple interest with the principal to be repaid on 30 June 2015. The interest is payable at the end of each income year.

At the time of entering into the financial arrangement, Fred Co has a sufficiently certain overall gain of $2,000.

Fred Co applies the accruals method to its financial arrangements and chooses to apply the accruals method to the overall gain from the loan.

Consequently, Fred Co spreads the overall gain of $2,000 over the period between 1 July 2013 and 30 June 2015.

As Fred Co applies the accruals method to the overall gain, it must disregard the interest payments in determining whether it has a sufficiently certain particular gain or loss from the loan. This effectively means that Fred Co has no sufficiently certain particular gains or losses from the loan.

Alternatively, if Fred Co does not choose to apply the accruals method to the overall gain, Fred Co would have two particular gains of $1,000 from the loan. Therefore, in applying the accruals method to those particular gains, it would spread:

- a gain of $1,000 between 1 July 2013 and 30 June 2014; and
- another gain of $1,000 between 1 July 2014 and 30 June 2015.

Spreading prepayments

8.40 A gain or loss arising from a prepayment generally relates to a period after it is made. For example, if a payment is made before it is otherwise due, the period to which the gain or loss arising from the payment typically spans the time between when the obligation to pay arose and the due date.

8.41 To more closely align the tax and commercial recognition of gains or losses, a gain or loss arising from a prepayment should be spread across the period to which it relates.

8.42 Currently, the accruals method cannot apply to spread a particular gain or loss arising from a prepayment if the gain or loss becomes sufficiently certain at the time the prepayment is made. This results in the gain or loss being recognised for tax purposes in the income year in which the prepayment is made.

8.43 In addition, even if the accruals method can apply to spread the gain or loss (that is, the gain or loss becomes sufficiently certain prior to the time the prepayment is made), the accruals method does not allow the spreading of the gain or loss:

- earlier than the time the gain or loss becomes sufficiently certain; or
- beyond the time the prepayment is made.

8.44 Consequently, apart from particular gains and losses arising from certain arrangements that the accruals method cannot apply to, the amendments ensure that the accruals method can apply to particular gains and losses that become sufficiently certain upon receipt or provision of a financial benefit and relate to a period occurring after that receipt or provision. ***[Schedule 8, items 15 to 18, subsections 230-100(3A) and (4), 230-110(1) and 230-115(1)]***

8.45 In addition, to ensure that taxpayers may spread gains or losses arising from prepayments over the period to which they relate, the amendments ensure that the period over which taxpayers spread gains or losses may:

- start earlier than when the gain or loss becomes sufficiently certain; and
- end as late as the time at which the taxpayer ceases to have the financial arrangement from which the gain or loss arises.

[Schedule 8, items 19 and 20, paragraph 230-130(4)(b) and subsection 230-130(5)]

8.46 The application of the accruals method to a gain or loss from a prepayment, which becomes sufficiently certain at the time the prepayment is made, may result in taxpayers allocating parts of the gain or loss to intervals preceding the time at which the gain or loss becomes sufficiently certain. This is inconsistent with the fact that the accruals method is forward-looking — from the time the gain or loss becomes sufficiently certain.

8.47 Consequently, the amendments deem the parts of the gain or loss, allocated to intervals ending prior to or during the income year in which the gain or loss became sufficiently certain, as being made in that income year. ***[Schedule 8, item 21, subsection 230-170(2A)]***

Example 8.3

On 1 July 2013, George Co provides a loan over 5 years; the terms of which include a right to interest and a contingent right to receive an

additional amount when a certain equity index exceeds a certain level on 30 June of each year. This amount is equal to sum of:

- the amount of interest that would have accrued if the contingency did not need to be satisfied for it to accrue; plus
- the present discounted value of interest that would have accrued if the amount had not also been prepaid.

Consequently, the gain arising from this amount relates to the period between 1 July 2013 and 30 June 2017.

On 30 June 2015, the equity index exceeds that level, and George Co receives an additional amount of $44.

The application of the accruals method results in a gain of $44 being allocated as follows:

- 1 July 2013 - 30 June 2014: $9.56;
- 1 July 2014 - 30 June 2015: $10.48;
- 1 July 2015 - 30 June 2016: $7.27;
- 1 July 2016 - 30 June 2017: $7.96; and
- 1 July 2017 – 30 June 2018: $8.73.

George Co's income years end on 30 June.

The part of the gain allocated to the interval spanning from 1 July 2013 to 30 June 2014 ends prior to the gain becoming sufficiently certain. The remaining parts are allocated to intervals ending after the income year in which the gain becomes sufficiently certain.

Consequently, George Co includes the following amounts in its assessable income:

- 2013-14 income year: $0;
- 2014-15 income year: $20.04 ($9.56 + $10.48);
- 2015-16 income year: $7.27;
- 2016-17 income year: $7.96; and
- 2017-18 income year: $8.73.

Spreading single payment

8.48 To apply the accruals method to a gain or loss, a taxpayer must determine an amount, to apply a rate of return to, for each interval over which the gain or loss is spread. Currently, when the gain or loss being spread arises from a single financial benefit, it is unclear as to what this amount should be.

8.49 Consequently, the amendments clarify that, in determining the amount to which taxpayers apply a rate of return, when the gain or loss being spread arises from a single financial benefit, taxpayers must have regard to a notional principal:

- from which the amount of the financial benefit giving rise to the gain or loss is calculated; or
- which is reasonably related to the financial benefit.

[Schedule 8, item 22, subsection 230-135(6A)]

8.50 In determining whether a notional principal is reasonably related to a financial benefit, the taxpayer should have regard to appropriate and commercially accepted valuation principles. For example, the notional principal could be an amount that is effectively invested in order for the taxpayer to make that gain or loss.

Re-estimations

8.51 Currently, taxpayers may only re-estimate gains or losses under the accruals method if circumstances materially affecting the timing and amount of those gains or losses arise.

8.52 However, the accruals method allows taxpayers to spread gains or losses under the accruals method in accordance with the effective interest method mentioned in accounting standard AASB 139, provided certain conditions are met. These accounting principles may require taxpayers to re-calculate the effective interest rate used in that method in the absence of circumstances materially affecting the timing or amount of gains or losses.

8.53 Consequently, if taxpayers re-calculate an effective interest rate for accounting purposes in the absence of such a circumstance, those calculations can no longer be used for tax purposes. This defeats the purpose of allowing taxpayers to use the effective interest method to spread their gains or losses — that purpose being to minimise compliance costs without opening up tax deferral opportunities.

8.54 Therefore, the amendments clarify that, when applying the effective interest method under the accruals method, taxpayers must re-estimate the gain or loss from a financial arrangement, irrespective of whether there is a material change in circumstances affecting the timing or amount of the gain or loss, if the re-calculation of the effective interest rate is consistent with the accounting principles. ***[Schedule 8, items 23 to 26, paragraph 230-190(1)(c) and subsections 230-190(2), (3A) and (3B)]***

Impairments and reversals

8.55 If there is an impairment (within the meaning of the accounting principles) of a financial arrangement (or a financial asset or financial liability that forms part of a financial arrangement), the taxpayer makes an impairment loss for accounting purposes. The amount of an impairment loss is calculated in accordance with AASB 139. Reversals of impairment losses reduce this amount. Both an impairment and a reversal of an impairment loss affect the amount of a gain or loss from a financial arrangement.

Losses resulting from impairments are not deductible

8.56 Currently, where financial benefits attributed to each other give rise to no gain or loss, there will be no gain or loss for the accruals method to apply to. This means that if a financial asset or liability, as represented by one of those financial benefits, is impaired, the resulting loss is a new loss to which the accruals method applies.

8.57 It is intended that a deduction is not allowed for losses resulting from impairment under the TOFA provisions. An impairment should only give rise to a deduction upon the writing off of a bad debt.

8.58 This amendment ensures that this loss is not able to be deducted. This is so that their treatment is consistent with existing gains or losses that are re-estimated as a result of impairment. ***[Schedule 8, item 28, subsections 230-172(1) and (2)]***

Reassessment upon reversal of an impairment

8.59 If a financial arrangement (or financial asset or financial liability that forms part of the financial arrangement is impaired), a taxpayer must reassess whether there is still a sufficiently certain gain or loss to which the accruals method can apply. If it is concluded that there is not a sufficiently certain gain or loss to which the accruals method can apply following this reassessment, the realisation method applies instead. Upon reversal of that impairment loss, the taxpayer must make another reassessment. As a result of this reassessment, it may be concluded that there is, once again, a sufficiently certain gain or loss to which the accruals method can apply.

8.60 However, that gain or loss may relate to a period preceding the gain or loss becoming sufficiently certain. As with prepayments, the current law does not allow the spreading of the gain or loss earlier than the time the gain or loss becomes sufficiently certain.

8.61 The amendment ensures that the taxpayer may spread the gain or loss over the period to which it relates, by allowing that period to start earlier than when the gain or loss becomes sufficiently certain. ***[Schedule 8, items 19 and 27, paragraph 230-130(4)(b) and subsection 230-130(4A)]***

8.62 Furthermore, as is done for prepayments, the amendments also deem the parts of the gain or loss allocated to intervals ending prior to or during the income year in which the gain or loss became sufficiently certain, as being made in that income year. ***[Schedule 8, item 21, subsection 230-170(2A)]***

Re-estimation upon reversal of an impairment

8.63 Currently, if an impairment of a financial arrangement (or financial asset or financial liability that forms part of the financial arrangement) occurs, and a re-assessment does not result in the conclusion that the realisation method should apply, taxpayers must re-estimate the gain or loss that changes due to the financial benefit being impaired. If that re-estimation results in taxpayers making a loss for an income year, that loss is not deductible.

8.64 Upon reversal of the impairment, re-estimation may result in taxpayers making a gain for an income year which is assessable in that income year. That gain may reflect to some extent the non-deductible loss resulting from the prior impairment. Although those losses are not deductible, the entire gain is assessable.

8.65 Therefore, to ensure closer alignment between the tax treatment of an impairment and a reversal of the impairment, the amendments specify how a taxpayer should re-estimate a gain or loss from a financial arrangement upon the reversal of an impairment loss for accounting purposes. ***[Schedule 8, item 30, paragraph 230-192(1)(b)]***

8.66 The amendments ensure that, where a deduction is not allowed for a loss resulting from an impairment and the re-estimation upon reversal of the impairment results in a taxpayer having to make a fresh allocation of a positive amount to intervals ending after the re-estimation, the amount to be reallocated does not take into account the non-deductible amount. ***[Schedule 8, item 30, subsection 230-192(5)]***

8.67 However, the amount to be reallocated should not be adjusted for losses resulting from impairment, where those losses have also been

written off as a bad debt (and deducted) through a balancing adjustment under the accruals method. ***[Schedule 8, item 30, subsection 230-192(6)]***

8.68 Where the non-deductible amount is greater than the amount to be reallocated, the amount actually reallocated is a loss. ***[Schedule 8, item 30, subsection 230-192(7)]***

8.69 Where the non-deductible amount is less than the amount to be reallocated, the amount actually reallocated is a gain. ***[Schedule 8, item 30, subsection 230-192(8)]***

8.70 The amendments also clarify that, if an impairment loss is partially reversed and the re-estimation results in the taxpayer still making a loss, the loss is not deductible to the extent that it is indirectly the result of the impairment. ***[Schedule 8, items 28 and 30, paragraph 230-172(3) and 230-192(3)(b)]***

8.71 In addition, the amendments ensure that where a taxpayer realises their impairment losses upon sale of a financial arrangement, the taxpayer recognises those losses under the balancing adjustment provisions. ***[Schedule 8, item 28 and 30, subsections 230-172(2) and 230-192(4)]***

8.72 Consequential amendments also group the existing provisions related to re-estimations upon impairment, with the amendments regarding reversal of impairment. ***[Schedule 8, items 29 and 30, subsections 230-192(1) to (3)]***

Example 8.4

On 1 July 2013, ABC Co lends $10,000. It expects to receive that $10,000, plus annual interest of 20 per cent compounding annually, on 30 June 2017. As a result, on 30 June 2017, ABC Co is sufficiently certain of:

- receiving $20,736 ($10,000$(1.2)^4$); and
- having an overall gain of $10,736 ($20,736 – $10,000).

Consequently, ABC Co allocates this gain as follows:

Year ending	*Gain or loss*	*Balance*
		$10,000
30 June 2014	$2,000 ($10,000 × 20 per cent) gain	$12,000
30 June 2015	$2,400 ($12,000 × 20 per cent) gain	$14,400
30 June 2016	$2,880 ($14,400 × 20 per cent) gain	$17,280
30 June 2017	$4,456 ($17,280 × 20 per cent) gain	$20,736
	$10,736	

However, on 1 July 2014, the loan is impaired, but ABC Co does not write it off as a bad debt. ABC Co now only expects to receive $8,748 on 30 June 2017. Therefore, ABC Co has an impairment loss of $6,937.50 ($12,000 – $8,748(1.2)$^{-3}$) for accounting purposes.

Consequently, ABC Co makes a re-estimation in relation to the overall gain from this financial arrangement. The fresh determination of that gain means that ABC Co now has an overall loss of $1,252 ($10,000 - $8,748).

ABC Co has already allocated $2,000 to intervals preceding the re-estimation — between 1 July 2013 and 1 July 2014. The part of the re-determined gain (which is now an overall loss of $1,252) that has not been allocated to intervals ending after 1 July 2014 is a $3,252 ($2,000 + $1,252) loss. Therefore, ABC Co applies the accruals method so as to spread the loss of $3,252 over the remaining three years.

To spread such a loss over three years, ABC Co must use a rate of return of 10 per cent (1 - $12,000/($12,000 - $3,252)$^{-3}$).

Year ending	*Gain or loss*	*Balance*
		$12,000
30 June 2015	$1,200 ($12,000 × 10 per cent) loss	$10,800
30 June 2016	$1,080 ($10,800 × 10 per cent) loss	$9,720
30 June 2017	$972 ($9,720 × 10 per cent) loss	$8,748
	$3,252 loss	

ABC Co cannot deduct these losses because they result from the impairment.

On 1 July 2015, the impairment of that loan is partially reversed. ABC Co now expects to receive $14,520 on 30 June 2017.

Consequently, ABC Co makes a re-estimation in relation to the overall loss from this financial arrangement. The fresh determination of that loss means that ABC Co now has an overall gain of $4,520 ($14,520 - $10,000).

ABC Co has already allocated a $2,000 gain and a $1,200 loss to intervals preceding the re-estimation — between 1 July 2013 and 1 July 2015. The part of the re-determined loss (which is now an overall gain of $4,520) that has not been allocated to intervals ending after 1 July 2015 is a $3,720 ($4,520 – $2,000 + $1,200) gain. ABC Co reduces this amount by $1,200 — the total of the losses that it could not deduct.

Therefore, ABC Co spreads a gain of $2,520 ($3,720 - $1,200), as follows:

Year ending	***Gain or loss***	***Balance***
		$12,000
30 June 2016	$1,200 ($12,000 × 10 per cent) gain	$13,200
30 June 2017	$1,320 ($13,200 × 10 per cent) gain	$14,520
	$2,520 gain	

Therefore, ABC Co includes the following amounts in its assessable income:

- 2013-14 income year: $2,000;
- 2014-15 income year: $0;
- 2015-16 income year: $1,200; and
- 2016-17 income year: $1,320.

On 1 July 2017, ABC Co sells the loan for $14,520. It makes a balancing adjustment. In doing so, it disregards the $1,200 loss resulting from impairment that it could not deduct, when calculating the amount of all the losses that would have been allowed to it as deductions if all losses could be deducted. Therefore, it makes a balancing adjustment of $0 as the Step 1 and Step 2 amounts are equal:

- Step 1(a): $14,520;
- Step 1(b) to (e): $0;
- **Step 1 amount: $14,520.**
- Step 2(a): $10,000;
- Step 2(b): $4,520;
- Step 2(c) to (e): $0;
- **Step 2 amount: $14,520.**

Running balancing adjustments

8.73 Under the running balancing adjustment provisions, taxpayers make a gain or loss if the amounts they receive or provide under a financial arrangement are different to the amounts they estimated they would receive or provide and those amounts have been taken into to account under the accruals method. This ensures that the gains and losses on a financial arrangement include any amounts not spread due to estimation errors.

8.74 Currently, it is arguable that a taxpayer may make a loss as a result of an impairment or the writing off of a bad debt, or a gain as a result of a reversal of an impairment, under the running balancing adjustment provisions. However, these events arise from changes in circumstances affecting the timing and amount of gains or losses (rather than being the result of estimation errors). It is intended that taxpayers should either re-estimate those gains or losses or re-assess whether the realisation method (instead of the accruals method) should apply to those gains or losses.

8.75 Consequently, the amendments clarify that a running balancing adjustment does not arise if:

- the amount of financial benefit received is less than the estimated amount, and the difference is the result of the writing off of a bad debt or an impairment; or

- the amount of financial benefit received is more than the estimated amount, and the difference is the result of a reversal of an impairment loss.

[Schedule 8, items 31 and 32, subsections 230-175(1A) and (2A)]

Ceasing of rights or obligations

8.76 Currently, taxpayers applying the realisation method to a gain or loss from a financial arrangement recognise the gain or loss in the income year during which the last financial benefit taken into account in working out that gain or loss is, or is due to be, provided.

8.77 However, in some cases, a right to receive a financial benefit or an obligation to provide a financial benefit under a financial arrangement may cease without the receipt or provision of the financial benefit. Under the realisation method, if a right or obligation is taken into account in working out a gain or loss from the financial arrangement and the cessation of the right or obligation occurs after the provision or receipt of the last financial benefit taken into account in working out the gain or loss, a taxpayer should recognise the gain or loss in the income year in which the cessation of that right or obligation occurs.

8.78 The amendments ensure that, under the realisation method, a gain or loss from a financial arrangement (except a loss from a financial arrangement resulting from the writing off of a bad debt) occurs:

- if the last of the financial benefits, rights and obligations taken into account in determining the amount of the gain or loss is a financial benefit:
  - at the time when that financial benefit is provided; or
  - if the financial benefit is not provided at the time when it is due to be provided and it is reasonable to expect that the financial benefit will be provided, at the time when that financial benefit is due to be provided; or
- if the last of the financial benefits, rights and obligations taken into account in determining the amount of the gain or loss is a right to receive a financial benefit or an obligation to provide a financial benefit:
  - if the right or obligation ceases before the financial benefit (to be received or provided) is provided, at the time when that right or obligation ceases; or

   – otherwise, at the time when the financial benefit is provided.

[Schedule 8, item 33, subsection 230-180(2)]

Example 8.5

On 1 July 2012, Henry Co buys a call option for a premium of $10, giving it the right to buy 100 shares for $1000 on 30 June 2015.

Henry Co could:

- make a gain equal to amount by which the market value of the 100 shares on 30 June 2015 exceeds the cost of the option ($10) plus the exercise price of the option ($1000); or
- make a loss:
  - if the option expires without Henry Co exercising it, equal to the cost of the option ($10); or
  - if the option is exercised and the cost of the option ($10) plus the exercise price ($1000) exceeds the market value of the 100 shares on 30 June 2015, equal to the excess.

If Henry Co allowed the option to expire on 30 June 2015 without exercising it, the last financial benefit to be provided would have been the premium paid on 1 July 2012.

However, Henry Co makes a loss of $10 on 30 June 2015, not 1 July 2012, even though the last financial benefit taken into account in working out that gain or loss was provided on 1 July 2012. This is because the right to buy 100 shares ceases on 30 June 2015.

The fair value method

8.79 When taxpayers make a fair value election, they must apply the fair value method to financial arrangements that are assets or liabilities being classified or designated as at fair value through profit or loss for accounting purposes.

8.80 Under the fair value method gains or losses are recognised for tax purposes in the same way they are recognised in profit or loss for accounting purposes.

8.81 This lowers compliance costs and improves the alignment of the recognition of gains or losses for tax and commercial purposes.

Financial arrangements to which the fair value election applies

8.82 Currently, the fair value method can only be applied to financial arrangements that are assets or liabilities that the accounting standards require to be classified or designated in the financial reports as at fair value through profit or loss.

8.83 However, changes in the fair value of hedging instruments and some hedged items in a fair value hedge may be recognised wholly or partly in profit or loss for accounting purposes, even if they are not assets or liabilities that are technically so classified or designated.

8.84 Consequently, taxpayers that have made a fair value election should also apply the fair value method to these gains or losses unless they have made a hedging financial arrangements election or reliance on financial reports election that applies to these financial arrangements.

8.85 However, the method should not apply to financial arrangements that are assets or liabilities that do not have gains or losses that arise from a change in fair value recognised through profit or loss. For example, gains or losses from available-for-sale assets, while fair-valued, are not treated as at fair value through profit or loss.

8.86 The amendments ensure that, for tax purposes, taxpayers may apply a fair value election to financial arrangements that are assets or liabilities that are otherwise treated as at fair value through profit or loss for accounting purposes, even if those assets or liabilities are not classified or designated as at fair value through profit or loss. ***[Schedule 8, item 35, paragraph 230-220(1)(c)]***

Gains and losses to which the fair value method applies

8.87 Currently, if a fair value election applies to a financial arrangement, in general, the gain or loss the taxpayer makes from the arrangement for an income year is the gain or loss that the accounting principles require to be recognised in profit or loss for the income year. This means that the election applies to recognise all gains or losses from the arrangement as opposed to gains and losses that reflect a change in fair value from the arrangement. This is appropriate for financial arrangements that are 'classified or designated as at fair value through profit or loss' for accounting purposes.

8.88 However, for financial arrangements that are not classified or designated, but are otherwise treated as at fair value through profit or loss, only certain gains and losses from the arrangement are treated as at fair value through profit or loss for accounting purposes. As such, the fair value method should only apply to gains or losses that arise from changes

in fair value of the arrangement and are recognised in profit or loss for accounting purposes, and allow other tax timing methods to apply to other gains and losses from the arrangement.

8.89 Consequently, the amendments ensure that a gain or loss that taxpayers make from a financial arrangement under the fair value method:

- is not the only gain or loss that they may make from that financial arrangement;
- is equal to the amount that they recognise in profit or loss for accounting purposes; and
- for financial arrangements that are otherwise treated as at fair value through profit or loss, is the gain or loss that is recognised as at fair value through profit or loss for accounting purposes.

[Schedule 8, items 36 and 37, subsections 230-230(1), (1A) and (4)]

8.90 Taxpayers should recognise all other gains or losses arising from those financial arrangements under another method. ***[Schedule 8, item 34, paragraph 230-40(4)(a)]***

8.91 A consequential amendment is made to the balancing adjustment provisions under the fair value method for financial arrangements that are otherwise treated as at fair value through profit or loss. Upon a fair value election ceasing to have effect or to apply to such an arrangement, only changes in fair value through profit or loss are relevant when working out a balancing adjustment.

8.92 Consequently, when working out a balancing adjustment, any changes in fair value that are not recognised as at fair value through profit or loss are subtracted from any amount that taxpayers are deemed to have disposed and reacquired the financial arrangement for. ***[Schedule 8, item 38, subsection 230-245(6)]***

Example 8.6

On 1 July 2012, Ursyn Co lends $1,000,000 for 10 years at a fixed interest rate of 5 per cent, paid annually in arrears to Bernard Co.

Ursyn Co hedges its exposure to changes in the fair value of the loan that is attributable to interest rate risks by entering into an interest rate swap on 1 July 2012 under which:

- a fixed interest rate of 5 per cent is paid on a notional principal of $1,000,000 for 10 years annually in arrears; and

- a floating rate of interest is received on a notional principal of $1,000,000 for 10 years annually in arrears.

This swap is entered into with an unrelated third party.

Ursyn Co designates the hedging relationship between the interest rate swap and the interest on the loan as a fair value hedge pursuant to AASB 139 on the date of its inception. Gains and losses from remeasuring the interest rate swap at fair value are recognised in profit or loss, and the gains or losses on the loan attributable to changes in interest rates are also recognised in profit or loss as at fair value.

The loan is otherwise carried at amortised cost for accounting purposes.

Ursyn Co has made a fair value election, but has not made a hedging financial arrangements election.

The fair value method applies to both the swap and the loan. However, in relation to the loan, the fair value method will only apply to the gain or loss attributable to changes in interest rates.

Any other gain or loss – for example, interest on the loan – is subject to the accruals or realisation tax timing method.

Between 1 July 2012 and 30 June 2014, interest rates are unchanged. No amounts are recognised in profit or loss in relation to the interest rate risk for the loan. However, during this period Bernard Co has its credit rating downgraded. The fair value movement of the loan that is attributable to the credit rating downgrade is not recognised in profit or loss nor does it cause the carrying amount of the loan to be affected.

Ursyn Co does not make a gain or loss under Subdivision 230-C in relation to the loan for the income years ended 30 June 2013 and 30 June 2014. Ursyn Co applies the accruals or realisation method to gains from its receipts of interest.

The hedging financial arrangements method

8.93 Taxpayers may use financial arrangements to hedge financial risks arising from the purchase, sale or production of commodities, and their financial assets or liabilities.

8.94 Hedging activity is ordinarily conducted on a pre-tax basis and is designed to manage, reduce or eliminate risk and uncertainty associated with the financial exposures of taxpayers created while anticipating the purchase, sale or production of commodities and other items or while having financial assets or liabilities. Derivative instruments (such as

swaps, options and forward contracts) are often the means used to hedge such exposures.

8.95 When taxpayers make a hedging financial arrangements election (the hedging election), they must apply the hedging financial arrangements method (the tax hedging method) to certain financial arrangements (hedging financial arrangements) that hedge risks in relation to certain items (hedged items). The method allows taxpayers to align the tax character and timing of gains and losses from a financial arrangement that is hedging another item, with that of gains and losses from that other item.

8.96 For tax purposes, hedging financial arrangements and hedged items are generally:

- financial arrangements that are designated as hedging instruments for accounting purpose (accounting hedges), and the items they hedge — that is, where the accounting standards allow a taxpayer to designate a hedging relationship between the hedging financial arrangement and hedged item;
- financial arrangements that would be designated as hedging instruments for accounting purposes, but for the fact that consolidated financial reports disregard the arrangement or the period of the hedge straddles two or more income years ('would-be' accounting hedges), and the items they hedge — that is, once again, where the accounting standards would allow a taxpayer to designate a hedging relationship between the hedging financial arrangement and hedged item; and
- financial arrangements that hedge a foreign currency risk in relation to certain anticipated dividends from a connected entity that is non-assessable non-exempt income (anticipated dividend hedges), and that anticipated dividend.

8.97 Taxpayers that elect to apply the tax hedging method are required to satisfy certain documentation requirements in relation to their hedging financial arrangements. Under these documentation requirements, taxpayers must, for each hedging financial arrangement they have, keep certain records, identify the basis for allocating gains and losses to income years, and assess the effectiveness of the hedge.

The 'one-in all-in' principle

8.98 A fundamental principle underlying the hedging election is that the election applies to all accounting hedges and 'would-be' accounting

hedges on a 'one-in, all-in' basis. The election also applies to anticipated dividend hedges in a consistent manner. Under this principle, taxpayers that make a hedging election must generally apply the hedging financial arrangements method to all of their hedging financial arrangements. These arrangements are:

- accounting hedges;
- ‘would-be’ accounting hedges; and
- anticipated dividend hedges provided they apply or have previously applied their election to an anticipated dividend hedge.

8.99 Under the current law, it is arguable that taxpayers can circumvent the 'one-in, all-in' principle by deliberately or accidentally failing to meet documentation requirements for particular hedging financial arrangements.

8.100 This is because satisfaction of the documentation requirements in relation to a hedging financial arrangement is a pre-condition for a hedging election applying to arrangements.

8.101 In addition, the current integrity measure that applies when a taxpayer ‘deliberately fails to meet a documentation requirement’ is not effective in preventing the circumvention of the ‘one-in, all-in’ principle. Currently, where taxpayers deliberately fail to meet a documentation requirement in relation to a hedging financial arrangement to which the hedging election applies, the consequence is that they cannot apply their election to any financial arrangement that they start to have after a failure to meet a documentation requirement. However, under current law, it is arguable that this consequence only arises, if the hedging election applied to the arrangement in the first place.

8.102 As such, the amendments ensure that a hedging election generally applies to all hedging financial arrangements, and failure to meet a documentation requirement in respect of a hedging financial arrangement may result in the hedging election not applying to all future hedging financial arrangements after the failure.

‘Would-be’ accounting hedges

8.103 Currently, the ‘would-be’ accounting hedges are hedging financial arrangements only if the taxpayer meets certain documentation requirements in relation to the arrangement. If the taxpayer fails to meet those documentation requirements, the arrangement is not, or will no longer be, a hedging financial arrangement and, as a result, the hedging

election ceases to apply to the arrangement. This contravenes the 'one-in, all-in' principle.

8.104 Consequently, the amendments ensure that these hedges are hedging financial arrangements, regardless of whether taxpayers meet the documentation requirements for these hedges. This ensures that a hedging election applies to these hedges. ***[Schedule 8, items 40 and 41, paragraphs 230-335(3)(d) and (e)]***

Example 8.7

> Heading Co elected in the 2011-12 income year to apply the hedging financial arrangements method. It prepares a consolidated report for accounting purposes with its subsidiary, Sub Co. However, Heading Co is not within the same consolidated group as Sub Co for tax purposes.
>
> During the 2011-12 income year, Heading Co enters ten cross-currency swaps and five interest rate swaps with Sub Co.
>
> Heading Co would have recorded all of these swaps as hedging instruments in a hedging relationship in their financial reports, if its consolidated report did not exclude its transactions with Sub Co.
>
> Therefore, regardless of whether Heading Co complies with any documentation requirements in relation to these swaps, all of these swaps are hedging financial arrangements for tax purposes and Heading Co must apply its hedging financial arrangements election to all of these swaps.

Anticipated dividend hedges

8.105 Currently, an anticipated dividend hedge is a hedging financial arrangement only if certain documentation requirements are met both initially and in subsequent years. This allows taxpayers to apply a hedging election to these hedges on an ‘arrangement by arrangement’ basis, which may result in inconsistent treatment of these hedges.

8.106 Consequently, the amendments remove the condition that certain documentation requirements must be satisfied (as a pre-condition of an anticipated dividend hedge being a hedging financial arrangement) if a hedging election applies, or applied, to that anticipated dividend hedge or to another anticipated dividend hedge. ***[Schedule 8, item 42, subsection 230-335(3A)]***

Example 8.8 (Continuation of Example 1.7)

> Heading Co also owns two foreign subsidiaries — X Co and Y Co, from whom it anticipates the payment of a dividend. On 1 July 2012

Heading Co enters into a forward contract hedging a foreign currency risk in relation to the anticipated dividend from X Co (the 'X Co forward contract').

Heading Co made a hedging financial arrangement election. The election applies to the X Co forward contract as it becomes a hedging financial arrangement when Heading Co complies with the initial documentation requirements in respect of the contract.

On 1 July 2013 Heading Co enters into another forward contract, hedging a foreign currency risk in relation to the anticipated dividend from Y Co (the 'Y Co forward contract').

As Heading Co applies the hedging financial arrangement election to the X Co forward contract, both forward contracts are hedging financial arrangements, regardless of whether Heading Co:

- meets the initial documentation requirements for the Y Co forward contract; or
- subsequently fails to meet those requirements for the X Co forward contract.

Taxpayers do not have to meet documentation requirements for an election to apply to a hedging financial arrangement

8.107 Currently, an election can apply to a hedging financial arrangement only if the documentation requirements are satisfied in respect of that arrangement. As a result, the satisfaction of documentation requirements in respect of some arrangements results in the election applying to some arrangements but not others. This contravenes the ‘one-in all-in’ principle.

8.108 Consequently, the amendments remove the condition that documentation requirements must be satisfied in relation to a hedging financial arrangement before an election can apply to that arrangement. This ensures that an election can apply to all hedging financial arrangements. ***[Schedule 8, item 39, section 230-325]***

An election may not apply to any hedging financial arrangement a taxpayer starts to have after failure to meet documentation requirements

8.109 A taxpayer should continue to satisfy their documentation requirements with respect to each hedging financial arrangement where the election would have applied to a financial arrangement if the taxpayer had not failed to meet that requirement in respect of an arrangement.

8.110 This is crucial for the administration of the hedging financial arrangements method.

8.111 Consequently, the amendments ensure that elections do not apply to a hedging financial arrangement, of any type, that a taxpayer starts to have:

- after the taxpayer deliberately or accidentally fails to meet the requirement to:
  - keep certain records;
  - determine the basis of allocating gains and losses to income years in an objective manner that fairly and reasonably corresponds with the tax treatment of the hedged item; or
  - assess of the effectiveness of the hedge; and
- before a date (if any) determined by the Commissioner of Taxation (Commissioner).

[Schedule 8, items 43, 44 and 47, paragraphs 230-365(c) and (d), and subsections 230-385(1), (2) and (4)]

8.112 The amendments also ensure that a determination can only be made, if the Commissioner is satisfied that at the time of making it, the taxpayer is unlikely to deliberately or accidentally fail to meet a requirement in relation to a hedging financial arrangement again. ***[Schedule 8, item 47, subsection 230-385(5)]***

8.113 This does not preclude taxpayers from having to rectify any failures to meet requirements for financial arrangements that they have at or prior to the time of failing a requirement.

The Commissioner may determine how gains or losses from a hedging financial arrangement should be allocated

8.114 The tax hedging method reduces post-tax mismatch by allocating gains and losses from hedging financial arrangements on a timing basis that is consistent with the tax recognition time for gains and losses made from the hedged item or items. In determining the basis of allocation, taxpayers must use a basis that:

- broadly, fairly and reasonably corresponds with the basis on which gains and losses on hedged items are allocated or recognised for income tax purposes;
- is objective; and

- is sufficiently precise and detailed so that the time at which the gain or loss from the hedging financial arrangement is to be taken into account for the purposes of the TOFA provisions, and the way in which the gain or loss will be classified for tax purposes, can be determined from the records that the taxpayer is required to keep in relation to the arrangement.

8.115 If a taxpayer does not satisfy these requirements, the amendments allow the Commissioner to determine the basis for allocating gains and losses for hedging financial arrangements (that a taxpayer has prior to the failure to satisfy the requirements) in a way that satisfies the requirements for determining the basis for allocating a gain or a loss in section 230-360. ***[Schedule 8, item 47, subsection 230-385(3)]***

8.116 However, even if the Commissioner makes such a determination, the hedging financial arrangements election does not apply to a hedging financial arrangement that the taxpayer starts to have after the failure to satisfy those requirements. This contrasts with an alternative determination that the Commissioner may make under subsection 230-380(6) which has the effect of deeming the taxpayer as having met the requirement.

Example 8.9 (Variation of Example 1.8)

Prior to 1 July 2012, Heading Co fails to allocate the gains and losses from one of its cross-currency swaps, on a fair and reasonable basis.

Heading Co must continue to apply the hedging financial arrangements method to the swap and any hedging financial arrangements that it started to have prior to the failure, including the swaps it acquired during the 2011-12 income year, if it still has them.

To continue applying the hedging financial arrangements election to the swap, the Commissioner determines what the fair and reasonable allocation of those gains and losses should be for tax purposes.

However, due to this failure, Heading Co may not apply the hedging financial arrangements method to:

- the X or Y Co forward contract (the hedging financial arrangements that hedges a foreign currency risk in relation to its anticipated dividend from its foreign subsidiaries, X Co and Y Co) which it acquired on 1 July 2013; or

- any other hedging financial arrangement that it starts to have after the failure, whether or not those financial arrangements are also cross-currency swaps.

Consequential amendments

8.117 Consequential amendments modify headings, correct cross references and make other minor changes to reflect these amendments. ***[Schedule 8, items 45 to 47, section 230-380 and subsections 230-385(4), (6) and (7)]***

Hedging net investments in foreign operations

8.118 Generally, the tax hedging method provides for gains or losses from hedging financial arrangements to be classified for income tax purposes in a way that corresponds with the way that income or losses from their corresponding hedged items are classified for income tax purposes. This corresponding classification is called tax character matching. For example, if the gain or loss on the hedged item is classified as a capital gain or loss for income tax purposes, the gains or loss from the hedging financial arrangement is also classified as a capital gain or loss.

8.119 Currently, if the hedged item is a net investment in a foreign operation (within the meaning of the accounting principles) which is carried on through a company in which a taxpayer holds shares or through a subsidiary company of the taxpayer, the hedged item is deemed to be the interest that the taxpayer has in the shares of the company for the purpose of tax classification.

8.120 However, a net investment in a foreign operation may comprise interests that are in addition to interests in the shares of the company. A hedging financial arrangement (a NIFO hedge) may hedge risks in relation of any one of those interests.

8.121 Consequently, the amendments ensure that, if the hedged item is a net investment in a foreign operation which is carried on through a company in which a taxpayer holds shares or through a subsidiary company of the taxpayer, then, for the purposes of determining the tax classification of the gains and losses from the NIFO hedge:

- to the extent that the NIFO hedge hedges a risk or risks in relation to the net investment in the foreign operation and that investment is held through shares in the company, the hedged item is taken to be the interest in those shares; and

- to the extent that the NIFO hedge hedges a risk or risks in relation to the net investment in the foreign operation that investment is held through another interest in the company, the hedged item is taken to be that other interest.

[Schedule 8, item 48, subsections 230-310(5) and (6)]

8.122 When taxpayers determine how to allocate gains and losses from a NIFO hedge, the allocation basis must fairly and reasonably correspond with recognition of gains and losses or amounts related to the share or other interests for tax purposes. Therefore, this determination will affect the extent to which those gains and losses are reasonably attributable to the share or other interests and the tax classification of those gains or losses.

Example 8.10

Aust Co has a net investment in a foreign operation carried on through its foreign subsidiary Fore Co. Its interests in Fore Co consist of shares and a long term debt interest. These interests are denominated in US dollars.

To hedge the foreign currency exchange risk in these interests, Aust Co enters into a foreign exchange forward contract.

Consequently, for the purpose of classifying the gains and losses from the forward contract, the hedged items are the interest in the shares, and the debt interest.

Transitional balancing adjustments

8.123 The TOFA provisions generally apply to financial arrangements that a taxpayer starts to have in the first income year commencing on or after 1 July 2010 (the first applicable income year).

8.124 To reduce compliance costs, taxpayers may elect to apply the TOFA provisions to financial arrangements that they started to have prior to the first applicable income year and which they still have at the beginning of this income year (existing financial arrangements). Where a taxpayer makes an election to bring existing financial arrangements into the TOFA regime, a transitional balancing adjustment is made to reconcile differences in tax treatments under other tax provisions and the TOFA provisions for the pre-TOFA holding period.

8.125 Taxpayers must calculate the transitional balancing adjustment using either the method under subitem 104(13) of Schedule 1 to the *Tax Laws Amendment (Taxation of Financial Arrangements) Act 2009* (the ‘primary method’) or the method under subitems 104(14) and (15) (the ‘alternative method’). This alternative method is only available to taxpayers who made the reliance on financial reports election under the TOFA provisions. The reliance on financial report method allows taxpayers to calculate the gains and losses from financial arrangements by reference to the relevant accounting standards, and was adopted following consultations as a way to reduce compliance costs.

8.126 The alternative method requires taxpayers to use amounts recorded in a deferred tax asset or deferred tax liability account for accounting purposes to calculate transitional balancing adjustments. The amount worked out using the alternative method should approximate the amount worked out using the primary method, where such an amount is recorded by the taxpayer in a deferred tax asset account or deferred tax liability account (respectively). A deferred tax asset or a deferred tax liability is recorded in a taxpayer's financial reports where the financial year in which a taxpayer recognises an amount of income or an expense for tax purposes is different to the year in which the taxpayer entity recognises the income or expense for financial accounting purposes.

8.127 However, adjustments calculated under the alternative method may not currently approximate those under the primary method. This is because the deferred tax effect amounts may represent the deferred tax effect of gains and losses that are not recognised in profit or loss in accordance with accounting principles. These include the deferred tax effect of gains and losses from cash flow hedges and available-for-sale assets.

8.128 Consequently, the amendments ensure that the alternative method is available only if:

- an amount recorded in a deferred tax asset and deferred tax liability account that is attributable to a financial arrangement wholly represents the deferred tax effect of a gain or loss from that financial arrangement; and

- that gain or loss has been recognised in profit or loss for accounting purposes.

[Schedule 8, items 49, 50, 52 and 53, paragraphs 104(14)(c), 104(14)(ca), 104(15)(c) and 104(15)(ca) of Schedule 1 to the Tax Laws Amendment (Taxation of Financial Arrangements) Act 2009]

8.129 In this regard, the deferred tax effect of a gain or loss from a financial arrangement should:

- be determined immediately before the start of the first applicable income year; and

- that determination must take into account any events occurring after this start, for example an amended assessment altering the tax treatment of the financial arrangement outside of Division 230, or a retrospective amendments to legislation.

[Schedule 8, items 51 and 54, notes to subitems 104(14) and (15) of Schedule 1 to the Tax Laws Amendment (Taxation of Financial Arrangements) Act 2009]

Example 8.11

Short Co must apply the TOFA provisions to financial arrangements it starts to have after 1 July 2010.

Short Co makes an election to apply the TOFA provisions to all the financial arrangements it has prior to, and that it still has, on 1 July 2010. Therefore, it must make a transitional balancing adjustment on account of these financial arrangements.

Short Co also makes the reliance on financial reports election. This election applies to all of these financial arrangements. Consequently, it uses the alternative method to make its transitional balancing adjustment.

However, on 30 June 2009, Short Co purchases some securities which it classifies as available-for-sale assets for accounting purposes. The fair value of these securities increases by $100 on 30 June 2010. This upwards revaluation is recognised in equity rather than in profit or loss.

Consequently, the amount in Short Co's deferred tax liability account on account of these purchased securities is equal to $30 ($100 x 30 per cent), representing the deferred tax effect of this upward evaluation.

As the amount does not represent the deferred tax effect of a gain from the securities that have been recognised in profit or loss, Short Co cannot apply the alternative method to make its transitional balancing adjustment in respect of these securities.

Elective requirements

8.130 Currently, taxpayers must satisfy certain criteria to be able to make the following elections under the TOFA provisions:

- the portfolio treatment of fees election;
- the fair value election;
- the foreign exchange retranslation election;
- the hedging financial arrangements election; and
- the reliance on financial reports election.

8.131 One criterion is that the taxpayer must have financial reports prepared in accordance with the accounting principles and auditing standards (the financial reports criterion).

8.132 However, practical difficulties arise in the use of these reports for Australian branches of foreign authorised deposit-taking institutions (foreign ADIs). For example, difficulties arise because of compliance costs associated with foreign currency translation, the absence of intra-bank transactions in these reports and the fact that these reports may not reflect some of the Australian branch transactions due to materiality.

8.133 To overcome these difficulties, the amendments enable foreign ADIs to satisfy the financial reports criterion using the Statement of Financial Performance and the Statement of Financial Position that foreign ADIs must provide to the Australian Prudential Regulation Authority for their Australian branch operations under section 13 of the *Financial Sector (Collection of Data) Act 2001*. ***[Schedule 8, item 55, section 230-527]***

8.134 Currently, these respective statements are the subject of Reporting Standard ARS 330.0 and Reporting Standard ARS 320.0.

8.135 These statements can be used by a foreign ADI to satisfy the financial reports criterion provided that three criteria are satisfied.

8.136 First, the statements must cover the activities of an Australian permanent establishment of the foreign ADI for the year. ***[Schedule 8, item 55, paragraph 230-527(1)(a)]***

8.137 Second, the statements must be prepared in accordance with the recognition and measurement standards under the accounting principles. In this regard, unlike their financial reports, these statements do not have to be prepared in accordance with the disclosure standards under the accounting principles. However, to ensure that the amount and timing of gains and losses are the same as what taxpayers would recognise if they used their financial reports, they must comply with the recognition and measurement standards. ***[Schedule 8, item 55, paragraph 230-527(1)(b)]***

8.138 Third, the statements must be audited in accordance with the auditing principles, as taxpayers would have had their financial reports audited. This is to ensure that there is a similar degree of integrity as to the amount and timing of gains or losses, regardless of whether taxpayers use their financial reports or these statements. ***[Schedule 8, item 55, paragraph 230-527(1)(c)]***

8.139 If these three criteria are satisfied, then taxpayers can use the statements to satisfy the eligibility requirements for certain elections in the TOFA provisions. ***[Schedule 8, item 55, subsection 230-527(2)]***

Miscellaneous amendments

Consistency of language

8.140 The TOFA provisions refer to two types of gains and losses. Taxpayers have the gains and losses that arise from financial arrangements. They allocate parts of these gains or losses to income years, according to the applicable tax-timing method. If the allocation of the gains and losses affect the assessable income or allowable deductions of a taxpayer in an income year, they are gains and losses that the taxpayer makes.

8.141 Currently, a number of provisions refer to a gain or loss that taxpayers make when the relevant gain or loss is one from a financial arrangement, rather than the gain or loss that affects assessable income or allowable deductions. These provisions relate to:

- requirements to treat certain gains or losses from financial arrangements consistently;
- identification of which gains or losses the accruals or realisation method should apply to; and
- the overview of how the accruals method applies to gains or losses from a financial arrangement.

8.142 Consequently, the amendments modify these provisions to refer to gains or losses that taxpayers 'have' rather than gains or losses that taxpayers 'make'. ***[Schedule 8, items 56, 57 and 58, paragraphs 230-80(2)(a) and (3)(a), subsections 230-100(2) to (5), and section 230-125]***

Other amendments

8.143 The amendments also make some minor drafting corrections. These corrections are grammatical in nature and do not change the operation of the provisions. ***[Schedule 8, items 59 to 64, subparagraph 230-5(2)(a)(iv), paragraph 230-85(a), subparagraph 230-140(3)(c)(ii), paragraph 230-190(7)(a), subsections 230-190(1) and (3) and paragraph 230-455(1)(d)]***

Application and transitional provisions

8.144 These amendments commence on 26 March 2009, immediately after the commencement of the provisions they are amending.

8.145 As a result, the amendments effectively apply from the commencement of the TOFA regime. The TOFA regime applies for

income years commencing on or after 1 July 2010, unless a taxpayer has elected to apply the Division for income years commencing on or after 1 July 2009.

8.146 The amendments were announced prior to the first income year of mandatory application of the TOFA provisions (see the then Assistant Treasurer's Media Release No. 145 of 29 June 2010).

8.147 The amendments are the outcome of the ongoing monitoring of the implementation of the TOFA reforms, and have been developed following extensive consultation with industry.

8.148 The amendments are generally beneficial to taxpayers. They refine and clarify the operation of the TOFA provisions, lower compliance costs and provide additional certainty to affected taxpayers.

Amendment of assessments

8.149 Generally, the Commissioner has the power to amend an assessment (including where a taxpayer requests an amendment) of a company, other than a small business entity, within four years from the date of the notice of assessment. However, as these amendments may apply to income years in respect of which the four year amendment period has wholly or partly expired, the period for amending assessments will be extended. An assessment can be amended if:

- the assessment was made before the date of commencement of the amendments (that is, the day on which the amendments receive Royal Assent);
- the amendment is made within two years after that date; and
- the amendment is made for the purpose of giving effect to these amendments.

[Section 4]

Consistency in working out gains and losses

8.150 Generally, a taxpayer who chooses to apply a method in a particular manner to one financial arrangement must use the same manner consistently for each financial arrangement that is essentially of the same nature (the consistency rule).

8.151 Some of the amendments in this Bill, or other amendments in the future, may allow taxpayers to make a choice not available under current law.

8.152 For example, under current law, taxpayers must apply the accruals method to overall gains or losses from financial arrangements. They are only allowed to apply the accruals method to particular gains or losses under certain circumstances. As such taxpayers may have applied the accruals method to overall gains or losses from financial arrangements they had prior to this Bill being enacted (pre-enactment arrangements).

8.153 This Bill changes the hierarchy between the application of the accruals method to an overall gain or loss and particular gains and losses from a financial arrangement. Taxpayers must apply the accruals method to particular gains and losses from a financial arrangement unless they choose to apply the method to the overall gain or loss from the arrangement. Therefore, the taxpayer may apply the accruals method to particular gains and losses from similar financial arrangements that it starts to have on or after this Bill is enacted (the post-enactment arrangement).

8.154 However, under the consistency rule, the taxpayer is prevented from applying the newly available choice to the post-enactment arrangement. Alternatively, the taxpayer can amend its prior year income tax assessments to apply the newly available choice to all the pre-enactment arrangements of essentially the same nature.

8.155 Consequently, the amendment ensures that in such circumstances (and provided that different manner is still allowed), the taxpayer can treat a post-enactment arrangement in a manner inconsistent with pre-enactment arrangements solely to apply a manner not available prior to the enactment of this Bill or a future amendment, to the post-enactment arrangement.

[Schedule 8, items 8 and 9, subsection 230-80(4)]

8.156 As a result, a taxpayer:

- does not have to amend their prior income tax assessment for a pre-enactment arrangement; and
- can use the different manner allowed as a result of the enactment of this Bill, or some future amendment for a post-enactment arrangement.

8.157 Therefore, a taxpayer must only apply a method consistently to all arrangements of essentially the same nature that they started to have on or after the enactment of the amendments.

8.158 Similarly, a taxpayer must still have applied the manner consistently for arrangements of essentially the same nature that they started to have prior to the enactment of the amendments.

STATEMENT OF COMPATIBILITY WITH HUMAN RIGHTS

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

Taxation of Financial Arrangements

8.159 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

8.160 Schedule 8 to this Bill amends Division 230 of the *Income Tax Assessment Act 1997* and the *Tax Laws Amendment (Taxation of Financial Arrangements) Act 2009* to clarify and refine the operation of certain aspects of the Taxation of Financial Arrangements regime.

Human rights implications

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

Conclusion

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

Assistant Treasurer, the Hon David Bradbury

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Item 7, paragraph 10A(3)(c)	6.24
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Item 9, paragraph 10A(5A)	6.23
Item 10	6.27

Schedule 7: Dependant (invalid and carer) tax offset

Bill reference	Paragraph number
Item 1, Subdivision 61-A of the ITAA 1997	7.31
Item 1, section 61-10 of the ITAA 1997	7.35
Item 1, paragraph 61-10(1)(c) of the ITAA 1997	7.38
Item 1, paragraphs 61-10(1)(d) and (c) of the ITAA 1997	7.62
Item 1, subsection 61-10(2) of the ITAA 1997	7.36
Item 1, subsections 61-10(3) and (4) of the ITAA 1997	7.37
Item 1, subsection 61-10(5) of the ITAA 1997	7.39
Item 1, subsection 61-15(2) of the ITAA 1997	7.41
Item 1, subsection 61-20(1) of the ITAA 1997	7.42
Item 1, subsection 61-20(2) of the ITAA 1997	7.46
Item 1, subsection 61-20(3) of the ITAA 1997	7.47
Item 1, sections 61-25 and 61-40 of the ITAA 1997	7.48
Item 1, subsection 61-30 of the ITAA 1997 and item 8, section 960-265 of the ITAA 1997	7.49

Bill reference	***Paragraph number***
Item 1, section 61-35 of the ITAA 1997	7.54
Item 1, section 61-40 of the ITAA 1997	7.56
Item 1, subsection 61-40(2) of the ITAA 1997	7.57
Item 1, subsection 61-45 of the ITAA 1997	7.58
Item 2, subsection 159(1F) of the ITAA 1936	7.60
Item 2, subsection 159(1G) of the ITAA 1936	7.63
Item 3, subsection 159J(6) of the ITAA 1936 and Schedule 7, item 4, subsection 159J(6) of the ITAA 1936	7.66
Item 5, subsection 159L(3C) of the ITAA 1936	7.61
Item 6, paragraphs 159P(4)(e) and (f) of the ITAA 1936	7.64
Item 7, section 13-1 of the ITAA 1936	7.69
Item 9, subsection 995-1(1) of the ITAA 1997	7.68
Item 10	7.70

Schedule 8: Taxation of financial arrangements

Bill reference	***Paragraph number***
Items 1, 2, 4 and 6, sections 230-70 and 230-75	8.18
Items 3 to 6, notes to sections 230-70 and 230-75	8.24
Item 7, subsection 230-200(2)	8.25
Items 8 and 9, subsection 230-80(4)	8.155
Item 10, paragraph 230-110(2)(a)	8.33
Items 11 and 14, paragraph 230-100(2)(c)	8.37
Item 12, subparagraph 230-100(3)(b)(i)	8.38
Items 13, paragraph 230-110(2)(b)	8.39
Items 15 to 18, subsections 230-100(3A) and (4), 230-110(1) and 230-115(1)	8.44
Items 19 and 27, paragraph 230-130(4)(b) and subsection 230-130(4A)	8.61
Items 19 and 20, paragraph 230-130(4)(b) and subsection 230-130(5)	8.45
Item 21, subsection 230-170(2A)	8.47, 8.62
Item 22, subsection 230-135(6A)	8.49
Items 23 to 26, paragraph 230-190(1)(c) and subsections 230-190(2), (3A) and (3B)	8.54
Item 28, subsections 230-172(1) and (2)	8.58

Bill reference	***Paragraph number***
Items 28 and 30, paragraph 230-172(3) and 230-192(3)(b)	8.70
Item 28 and 30, subsections 230-172(2) and 230-192(4)	8.71
Items 29 and 30, subsections 230-192(1) to (3)	8.72
Item 30, paragraph 230-192(1)(b)	8.65
Item 30, subsection 230-192(8)	8.69
Item 30, subsection 230-192(5)	8.66
Item 30, subsection 230-192(6)	8.67
Item 30, subsection 230-192(7)	8.68
Items 31 and 32, subsections 230-175(1A) and (2A)	8.75
Item 33, subsection 230-180(2)	8.78
Item 34, paragraph 230-40(4)(a)	8.90
Item 35, paragraph 230-220(1)(c)	8.86
Items 36 and 37, subsections 230-230(1), (1A) and (4)	8.89
Item 38, subsection 230-245(6)	8.92
Item 39, section 230-325	8.108
Items 40 and 41, paragraphs 230-335(3)(d) and (e)	8.104
Item 42, subsection 230-335(3A)	8.106
Items 43, 44 and 47, paragraphs 230-365(c) and (d), and subsections 230-385(1), (2) and (4)	8.111
Items 45 to 47, section 230-380 and subsections 230-385(4), (6) and (7)	8.117
Item 47, subsection 230-385(3)	8.115
Item 47, subsection 230-385(5)	8.112
Item 48, subsections 230-310(5) and (6)	8.121
Items 49, 50, 52 and 53, paragraphs 104(14)(c), 104(14)(ca), 104(15)(c) and 104(15)(ca) of Schedule 1 to the *Tax Laws Amendment (Taxation of Financial Arrangements) Act 2009*	8.128
Items 51 and 54, notes to subitems 104(14) and (15) of Schedule 1 to the *Tax Laws Amendment (Taxation of Financial Arrangements) Act 2009*	8.129
Item 55, section 230-527	8.133
Item 55, paragraph 230-527(1)(a)	8.136
Item 55, paragraph 230-527(1)(b)	8.137
Item 55, paragraph 230-527(1)(c)	8.138
Item 55, subsection 230-527(2)	8.139
Items 56, 57 and 58, paragraphs 230-80(2)(a) and (3)(a), subsections 230-100(2) to (5), and section 230-125	8.142
Items 59 to 64, subparagraph 230-5(2)(a)(iv), paragraph 230-85(a),	8.143

Bill reference	***Paragraph number***
subparagraph 230-140(3)(c)(ii), paragraph 230-190(7)(a), subsections 230-190(1) and (3) and paragraph 230-455(1)(d)	