





# **Tax Laws Amendment (2005 Measures No. 5) Act 2005**

**No. 162, 2005**

**An Act to amend the law relating to taxation, and  
for related purposes**

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# **Tax Laws Amendment (2005 Measures No. 5) Act 2005**

**No. 162, 2005**

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## **An Act to amend the law relating to taxation, and for related purposes**

*[Assented to 19 December 2005]*

The Parliament of Australia enacts:

### **1 Short title**

This Act may be cited as the *Tax Laws Amendment (2005 Measures No. 5) Act 2005*.

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## 2 Commencement

- (1) Each provision of this Act specified in column 1 of the table commences, or is taken to have commenced, in accordance with column 2 of the table. Any other statement in column 2 has effect according to its terms.

<b>Commencement information</b>		
<b>Column 1</b>	<b>Column 2</b>	<b>Column 3</b>
<b>Provision(s)</b>	<b>Commencement</b>	<b>Date/Details</b>
1. Sections 1 to 3 and anything in this Act not elsewhere covered by this table	The day on which this Act receives the Royal Assent.	19 December 2005
2. Schedules 1 to 5	The day on which this Act receives the Royal Assent.	19 December 2005
3. Schedule 6, items 1 to 5	1 July 2005.	1 July 2005
4. Schedule 6, item 6	Immediately after the commencement of the <i>New Business Tax System (Debt and Equity) Act 2001</i> .	1 July 2001
5. Schedule 6, items 7 to 13	1 July 2005.	1 July 2005
6. Schedule 6, Part 2	Immediately after the commencement of the <i>New Business Tax System (Debt and Equity) Act 2001</i> .	1 July 2001
7. Schedule 6, Part 3	The day on which this Act receives the Royal Assent.	19 December 2005

Note: This table relates only to the provisions of this Act as originally passed by the Parliament and assented to. It will not be expanded to deal with provisions inserted in this Act after assent.

- (2) Column 3 of the table contains additional information that is not part of this Act. Information in this column may be added to or edited in any published version of this Act.

## 3 Schedule(s)

Each Act that is specified in a Schedule to this Act is amended or repealed as set out in the applicable items in the Schedule

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concerned, and any other item in a Schedule to this Act has effect according to its terms.

## Schedule 1—Modifications to exemption for foreign earnings

### *Income Tax Assessment Act 1936*

#### **1 After subsection 23AG(1)**

Insert:

- (1A) A person is taken, for the purposes of subsection (1), to have been engaged in foreign service for a continuous period of 91 days if:
- (a) the person died at a time when he or she was engaged in foreign service for a continuous period of less than 91 days; and
  - (b) he or she would have otherwise continued to be engaged in the foreign service; and
  - (c) his or her continuous period of engagement in the foreign service would have otherwise been a period of at least 91 days.

#### **2 After subsection 23AG(2)**

Insert:

- (2A) Subsection (2) does not apply in relation to foreign earnings to the extent that the person derived them from foreign service in Iraq after 31 December 2002 but before 1 May 2004.

#### **3 Subsections 23AG(6A) to (6E)**

Repeal the subsections, substitute:

- (6A) 2 or more periods in which a person has been engaged in foreign service are together taken to constitute a continuous period of foreign service until:
- (a) the end of the last of the 2 or more periods; or
  - (b) a time (if any), since the start of the first of the 2 or more periods, when the person's total period of absence exceeds  $\frac{1}{6}$  of the person's total period of foreign service;
- whichever happens sooner.

Example: Kate is engaged in foreign service for 20 days, is absent for 2 days and is then engaged in foreign service for 10 days. These 2 periods of

foreign service constitute a continuous period of foreign service, because the total period of absence is never more than  $\frac{1}{10}$  of the total period of foreign service.

Kate is then absent for 5 days before commencing a further period of foreign service. No matter how long the further period lasts, it can never constitute a continuous period of foreign service with the first 2 periods of foreign service, because on the fourth day of the second absence the total period of absence is  $\frac{1}{5}$  of the total period of foreign service.

(6B) In subsection (6A):

***total period of absence***, in relation to a particular time, means the number of days, in the period starting at the start of the first of the 2 or more periods and ending at that time, for which the person was not engaged in foreign service.

***total period of foreign service***, in relation to a particular time, means the number of days, in the period starting at the start of the first of the 2 or more periods and ending at that time, for which the person was engaged in foreign service.

#### **4 Subsection 23AG(6J)**

Repeal the subsection.

#### **5 Application**

- (1) The amendment made by item 1 is taken to have applied in relation to deaths that occurred on or after 1 July 2004.
- (2) The amendment made by item 2 is taken to have applied to assessments for the 2002-03 year of income and each subsequent year of income.
- (3) The amendments made by items 3 and 4 apply in relation to foreign service performed on or after the day on which this Act received the Royal Assent.
- (4) If, immediately before the day on which this Act received the Royal Assent (the ***commencement day***):
  - (a) a person had an absentee credit balance within the meaning of subsection 23AG(6A) of the *Income Tax Assessment Act 1936*; or
  - (b) would have had such a balance if that subsection allowed for an absentee credit balance to be a part of a day;

on the commencement day the person's total period of foreign service, under subsections 23AG(6A) and (6B) of that Act as amended by this Act, is increased by a number of days equivalent to:

- (c) if, immediately before the commencement day, the person was engaged in foreign service—the number of days, before that day, in that continuous period of foreign service; or
- (d) if paragraph (c) does not apply—the number of days in the last continuous period of foreign service in which the person was engaged before that day.

## **Schedule 2—Tax offset for Australian production expenditure on television series**

### *Income Tax Assessment Act 1997*

#### **1 Subparagraph 376-15(1)(d)(ii)**

Omit “; and”, substitute “; or”.

#### **2 At the end of paragraph 376-15(1)(d)**

Add:

- (iii) a \*television series that is not covered by subparagraph (i) or (ii); and

#### **3 Subparagraph 376-15(1)(e)(i)**

Repeal the subparagraph, substitute:

- (i) if the film is covered by subparagraph (d)(i) or (ii)—a documentary; or

#### **4 Subparagraph 376-15(1)(e)(v)**

Repeal the subparagraph, substitute:

- (v) if the film is covered by subparagraph (d)(i) or (ii)—a film forming part of a drama program series that is, or is intended to be, of a continuing nature; or

#### **5 After paragraph 376-15(1)(e)**

Insert:

- (ea) if the film is a \*television series that is not covered by subparagraph (d)(i) or (ii):
  - (i) for a television series that is predominantly a digital animation or other animation—the \*making of the television series (other than a pilot episode, if any, or activities mentioned in paragraph 376-25(3)(a)) takes place within a period of not longer than 36 months; or
  - (ii) otherwise—all principal photography for the television series (other than a pilot episode, if any) takes place within a period of not longer than 12 months; and

- (eb) if the film is a \*television series that is not covered by subparagraph (d)(i) or (ii)—the amount worked out for the film under subsection (3) is at least \$1 million; and

## 6 At the end of section 376-15

Add:

- (3) For the purposes of paragraph (1)(eb), the amount for a film is worked out by using the formula:

$$\frac{\text{Total QAPE}}{\text{Duration of film in hours}}$$

where:

*duration of film in hours* means the total length of the film, measured in hours.

*total QAPE* means the total of the company's \*qualifying Australian production expenditure on the film (worked out using Subdivision 376-C).

## 7 After section 376-15

Insert:

### 376-17 Television series

- (1) A *television series* is a \*film made up of 2 or more episodes that:
- are produced wholly or principally for exhibition to the public on television under a single title; and
  - contain a common theme or themes; and
  - contain dramatic elements that form a narrative structure; and
  - meet the requirement in subsection (2).

Note: A documentary can be a television series.

- (2) The requirement is that all of the episodes must be produced wholly or principally for exhibition together, for a national market or national markets.
- (3) To avoid doubt, and without limiting paragraph (1)(c), a \*film satisfies the requirement in that paragraph if:

- (a) the sole or dominant purpose of the film is to depict actual events, people or situations; and
  - (b) the film depicts those events, people or situations in a dramatic or entertaining way, with a heavy emphasis on dramatic impact or entertainment value.
- (4) A pilot episode to a television series is taken to be a part of the television series.

**8 Subsection 376-25(5)**

Omit “section 376-35”, substitute “subsection 376-35(1)”.

**9 Subsection 376-25(6) (note)**

Omit “section 376-35”, substitute “subsection 376-35(1)”.

**10 Section 376-35**

Before “Despite”, add “(1)”.

**11 At the end of section 376-35**

Add:

- (2) Despite sections 376-25 and 376-30, the expenditure of a company is not production expenditure of the company on a \*film if:
- (a) the film is a \*television series that is not covered by subparagraph 376-15(1)(d)(i) or (ii); and
  - (b) the expenditure is reasonably attributable to the production of a pilot episode to the television series; and
  - (c) the expenditure, apart from this subsection, would be production expenditure that was not \*qualifying Australian production expenditure.

**12 Subsection 995-1(1)**

Insert:

*television series* has the meaning given by section 376-17.

**13 Application**

The amendments made by this Schedule apply to production expenditure incurred on and after 1 July 2004.

## Schedule 3—Consolidation

### Part 1—Bad debts

#### Division 1—MEC groups

#### *Income Tax Assessment Act 1997*

#### 1 After Subdivision 719-H

Insert:

#### Subdivision 719-I—Bad debts

#### Guide to Subdivision 719-I

#### 719-450 What this Subdivision is about

The head company of a MEC group is taken to meet the conditions in section 165-123 (about maintaining the same ownership in an ownership test period to be able to deduct a bad debt) if and only if the top company for the group at the start of the period meets those conditions for the period.

#### Table of sections

##### **Maintaining the same ownership to be able to deduct bad debt**

- 719-455 Special test for deducting a bad debt because a company maintains the same owners
- 719-460 Assumptions about nothing happening to affect direct and indirect ownership of the test company
- 719-465 Assumptions about the test company failing to meet the conditions in section 165-123

## Maintaining the same ownership to be able to deduct bad debt

### 719-455 Special test for deducting a bad debt because a company maintains the same owners

- (1) This section has effect for the purposes of working out whether the \*head company of a \*MEC group:
- (a) can deduct a debt it writes off as bad; or
  - (b) could have deducted a debt as described in subsection 709-215(2).

Note: Whether the head company of the MEC group could have deducted a debt as described in subsection 709-215(2) is relevant under Subdivision 709-D to:

- (a) the question whether the head company can deduct the debt it writes off as bad, or the swap loss it makes in extinguishing the debt as part of a debt/equity swap, after the debt was owed to an entity while the entity was not a member of the MEC group; and
  - (b) the question whether an entity that was owed the debt after it was owed to the head company can deduct the amount of the debt the entity writes off as bad or the swap loss the entity makes in extinguishing the debt as part of a debt/equity swap.
- (2) The \*head company is taken to meet the conditions in section 165-123 (about the company maintaining the same owners) for the \*ownership test period if and only if the company (the *test company*) that was the \*top company for the \*MEC group at the start of the same period would have met those conditions for that period on the assumptions in the following sections (if applicable):
- (a) section 719-460 (which is about assuming that nothing happened in relation to certain things that would affect whether the test company would meet those conditions);
  - (b) section 719-465 (which is about assuming that the test company would have failed to meet those conditions in certain circumstances).

Note 1: Even though subsection (2) of this section raises the issue whether the test company meets the conditions in section 165-123, that is determined by reference to:

- (a) the ownership test period for the head company of the MEC group; and
- (b) the debt owed to the head company.

Note 2: If this section is applying for the purposes of working out whether the head company could have deducted a debt as described in subsection

**Schedule 3** Consolidation  
**Part 1** Bad debts

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709-215(2), section 709-215 affects what is the ownership test period for the purposes of section 165-123 as it applies for those purposes.

*Head company's failure to meet conditions in section 165-123*

- (3) The \*head company is taken to fail to meet a condition in section 165-123 only at:
- (a) the first time the test company would have failed to meet the condition on the relevant assumptions mentioned in subsection (2); or
  - (b) the \*test time described in section 166-40 for the test company, if:
    - (i) Division 166 is relevant to working out whether the test company met the conditions in section 165-123 on the relevant assumption mentioned in paragraph (2)(a); and
    - (ii) the test company is not assumed under section 719-465 to fail to meet the condition before the test time.

Note 1: If the head company is taken to fail to meet a condition in section 165-123, the head company will not be able to deduct the debt unless that company meets the condition in section 165-126 by satisfying the same business test. That test applies to the head company (and not the test company).

Note 2: Section 719-285 may affect whether the head company satisfies the same business test if there has been a change in the identity of the head company of the group during the ownership test period.

*Same business test for head company under Division 166*

- (4) If section 166-40 directly affects whether the \*head company can deduct the debt, the subsection of that section that requires the \*same business test be applied to a particular \*business operates as if it required that test to be applied to the business the head company carried on just before the time described in subsection (3) of this section.

Note: Section 166-40 has an *indirect* effect on whether the head company can deduct the debt so far as that section affects whether the *test* company meets the conditions in section 165-123 and therefore whether the head company is taken to meet those conditions.

**719-460 Assumptions about nothing happening to affect direct and indirect ownership of the test company**

- (1) This section sets out an assumption that must be made whenever there is a change in the identity of the \*top company for the \*MEC group during the \*ownership test period.
- (2) Assume that after the change nothing happens in relation to \*membership interests or voting power in the following entities that would affect whether the test company would meet the conditions in section 165-123:
  - (a) the company that was the \*top company for the \*MEC group before the change;
  - (b) an entity (if any) that at the time of the change was interposed between:
    - (i) the company that was the top company for the MEC group before the change; and
    - (ii) the company that became the top company for the MEC group as part of the change.

**719-465 Assumptions about the test company failing to meet the conditions in section 165-123**

- (1) Assume that the test company fails to meet the conditions in section 165-123 at the time an event described in subsection (2), (3) or (4) happens after the start of the \*ownership test period in relation to:
  - (a) the \*MEC group; or
  - (b) the \*potential MEC group whose membership was the same as the membership of the MEC group.

Note: If the test company is assumed to fail to meet the conditions in section 165-123, the head company of the MEC group is taken (under section 719-455) to have failed to meet those conditions.
- (2) One event is the \*potential MEC group ceasing to exist.
- (3) Another event is something happening that meets these conditions:
  - (a) the thing happens at a time in relation to \*membership interests in one or more of these entities:
    - (i) a company that was just before that time a \*member of the \*MEC group and an \*eligible tier-1 company of the \*top company for the MEC group;

- (ii) an entity interposed between a company described in subparagraph (i) and the company that was the top company for the group just before that time;
  - (b) the thing does not cause the \*potential MEC group to cease to exist but does cause a change in the identity of the top company for the potential MEC group.
- (4) Another event is the \*MEC group ceasing to exist because there ceases to be a \*provisional head company of the group.

*Other causes of failure to meet conditions in section 165-123*

- (5) To avoid doubt, this section does not limit the circumstances in which the test company would have failed to meet the conditions in section 165-123.

## **Division 2—Deducting debt/equity swap loss**

### ***Income Tax Assessment Act 1997***

#### **2 At the end of subsection 709-205(1)**

Add:

Note: This Subdivision affects similarly whether an entity that is or has been a member of a consolidated group and extinguishes a debt as part of a debt/equity swap may deduct a loss resulting from the swap. See section 709-220.

#### **3 At the end of Subdivision 709-D**

Add:

### **Extension of Subdivision to debt/equity swap loss**

#### **709-220 Limit on deduction of swap loss**

*Object*

- (1) The object of this section is to limit the circumstances in which an entity can deduct a swap loss (as defined in section 63E of the *Income Tax Assessment Act 1936*) resulting from a debt/equity swap (as defined in that section) to circumstances similar to those in which this Subdivision lets an entity deduct a debt it writes off as bad.

*Modified operation of sections 709-205, 709-210 and 709-215*

- (2) Sections 709-205, 709-210 and 709-215 (except subsection 709-215(2)) apply in relation to the extinction (however described) of a debt as part of a debt/equity swap in the same way as they apply in relation to the writing off of a debt as bad.
- (3) Subsection 709-215(1):
  - (a) applies in relation to a swap loss from a debt/equity swap in the same way as it applies in relation to a debt, or part of a debt; and
  - (b) applies as if paragraph 709-215(1)(a) referred to subsection 63E(3) of the *Income Tax Assessment Act 1936* instead of sections 8-1 and 25-35.
- (4) This section has effect despite subsection 63E(5) of the *Income Tax Assessment Act 1936*.

### **Division 3—Consequential amendments**

#### ***Financial Corporations (Transfer of Assets and Liabilities) Act 1993***

##### **4 Subsection 22(2)**

Omit “and 175-C”, substitute “, 175-C, 709-D and 719-F”.

##### **5 Paragraph 22(3)(d)**

Omit “Subdivision 165-C or 175-C, or both,”, substitute “any one or more of Subdivisions 165-C, 175-C, 709-D and 719-F”.

##### **6 Subsection 22(3)**

Omit “neither Subdivision 165-C nor 175-C of that Act”, substitute “none of those Subdivisions”.

##### **7 Subsection 22(3) (at the end of the note)**

Add:

Subdivision 709-D of that Act is about the conditions that must be met for an entity to deduct a bad debt that has for a period been owed to a member of a consolidated group and has for another period been owed to an entity that was not a member of that group for the period.

Subdivision 719-I of that Act is about the conditions that must be met for an entity to deduct a bad debt that has for a period been owed to a member of a MEC group.

## ***Income Tax Assessment Act 1936***

### **8 Paragraph 427(b)**

Omit “and 175-A”, substitute “, 175-A, 709-D and 719-I”.

### **9 Subsection 266-35(1) in Schedule 2F (note)**

Repeal the note, substitute:

Note: Subdivisions 709-D and 719-I of the *Income Tax Assessment Act 1997* also affect when a trust that used to be a member of a consolidated group or MEC group may deduct a debt that used to be owed to a member of the group and that the trust writes off as bad.

### **10 Subsection 266-85(3) in Schedule 2F (note)**

Repeal the note, substitute:

Note: Subdivisions 709-D and 719-I of the *Income Tax Assessment Act 1997* also affect when a trust that used to be a member of a consolidated group or MEC group may deduct a debt that used to be owed to a member of the group and that the trust writes off as bad.

### **11 Subsection 266-120(1) in Schedule 2F (note)**

Repeal the note, substitute:

Note: Subdivisions 709-D and 719-I of the *Income Tax Assessment Act 1997* also affect when a trust that used to be a member of a consolidated group or MEC group may deduct a debt that used to be owed to a member of the group and that the trust writes off as bad.

### **12 Subsection 266-160(2) in Schedule 2F (note)**

Repeal the note, substitute:

Note: Subdivisions 709-D and 719-I of the *Income Tax Assessment Act 1997* also affect when a trust that used to be a member of a consolidated group or MEC group may deduct a debt that used to be owed to a member of the group and that the trust writes off as bad.

### **13 Subsection 267-25(1) in Schedule 2F (note)**

Repeal the note, substitute:

Note: Subdivisions 709-D and 719-I of the *Income Tax Assessment Act 1997* also affect when a trust that used to be a member of a consolidated

group or MEC group may deduct a debt that used to be owed to a member of the group and that the trust writes off as bad.

**14 Subsection 267-65(1) in Schedule 2F (note)**

Repeal the note, substitute:

Note: Subdivisions 709-D and 719-I of the *Income Tax Assessment Act 1997* also affect when a trust that used to be a member of a consolidated group or MEC group may deduct a debt that used to be owed to a member of the group and that the trust writes off as bad.

**15 Paragraph 271-60(5)(a) in Schedule 2F**

After “165-C”, insert “, 709-D or 719-I”.

***Income Tax Assessment Act 1997***

**16 Section 12-5 (table item headed “bad debts”)**

Omit:

debt/equity swaps.....	<b>63E, 63F</b>
deduction of a debt that used to be owed to a member of a consolidated group by an entity that used to be a member of the group .....	Subdivision 709-D

substitute:

debt/equity swaps.....	<b>63E, 63F, 709-220</b>
deduction of a debt that used to be owed to a member of a consolidated group or MEC group by an entity that used to be a member of the group .....	Subdivisions 709-D and 719-I

**17 Subsection 25-35(5) (table item 6)**

Repeal the item, substitute:

6	An entity that used to be a member of a consolidated group or MEC group can deduct a bad debt that used to be owed to a member of the group only if certain conditions are met	Subdivisions 709-D and 719-I
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**18 Subsection 165-120(1) (note 3)**

Repeal the note, substitute:

Note 3: Subdivisions 709-D and 719-I modify how this Subdivision operates in relation to a company that used to be a member of a consolidated group or MEC group and that writes off as bad a debt that used to be owed to a member of the group.

**19 Subparagraph 709-215(2)(c)(ii)**

Repeal the subparagraph, substitute:

- (ii) section 63G of the *Income Tax Assessment Act 1936*;
- (iii) section 267-65 in Schedule 2F to that Act.

***Income Tax (Transitional Provisions) Act 1997***

**20 At the end of Division 719**

Add:

**Subdivision 719-I—Bad debts**

**Table of sections**

719-450 Application of Subdivision 719-I of the *Income Tax Assessment Act 1997*

**719-450 Application of Subdivision 719-I of the *Income Tax Assessment Act 1997***

Subdivision 719-I of the *Income Tax Assessment Act 1997* applies on and after 1 July 2002.

## **Part 2—Making and revoking certain choices**

### *Income Tax (Transitional Provisions) Act 1997*

**21 Paragraph 701-5(2)(b)**

Omit “2004”, substitute “2005”.

**22 Paragraph 701-5(4)(a)**

Omit “2004”, substitute “2005”.

**23 Paragraph 707-145(a)**

Omit “2005”, substitute “2006”.

**24 Paragraph 707-325(5)(b)**

Omit “2004”, substitute “2005”.

**25 Subsection 707-325(6)**

Omit “2004”, substitute “2005”.

**26 Subparagraph 707-327(5)(a)(ii)**

Omit “2004”, substitute “2005”.

**27 Paragraph 707-327(5)(b)**

Omit “2004”, substitute “2005”.

**28 Subparagraph 707-328A(4)(a)(ii)**

Omit “2004”, substitute “2005”.

**29 Paragraph 707-328A(4)(b)**

Omit “2004”, substitute “2005”.

**30 Paragraph 707-350(5)(b)**

Omit “2004”, substitute “2005”.

**31 Subsection 707-350(6)**

Omit “2004”, substitute “2005”.

**32 Section 719-310**

Omit “2005”, substitute “2006”.

## **Part 3—Application**

### **33 Application**

The amendments made by this Schedule apply on and after 1 July 2002.

## Schedule 4—Thin capitalisation

### *Income Tax (Transitional Provisions) Act 1997*

#### 1 At the end of Division 820

Add:

#### **820-45 Transitional provision—accounting standards and prudential standards**

- (1) This section applies to 3 consecutive income years of an entity beginning on or after 1 January 2005.
- (2) Subject to subsection (3), the entity may choose, for any or all of those income years, to use the accounting standards in force under the *Corporations Act 2001* immediately before 1 January 2005 (rather than the current accounting standards) for the purpose of calculating amounts applicable to the entity under Division 820 of the *Income Tax Assessment Act 1997*.

Note 1: Making the choice for an income year does not require the entity to maintain a full set of accounts based on those old accounting standards.

Note 2: The choice is only for the purposes of calculating amounts for the purposes of the thin capitalisation regime.

- (3) If the entity makes a choice under subsection (2) for an income year but an associate entity of that entity does not, the entity may, in working out its associate entity excess amount so far as it relates to that associate entity at a time in that year, use either the accounting standards in force under the *Corporations Act 2001* immediately before 1 January 2005 or the current accounting standards.
- (4) If an ADI makes a choice under subsection (2) for an income year, the ADI must also choose to use for that year the prudential standards in force under the *Banking Act 1959* immediately before 1 January 2005 (rather than the current prudential standards) for the purpose of calculating amounts applicable to the ADI under Division 820 of the *Income Tax Assessment Act 1997*.

Note 1: Making the choice for an income year does not require the entity to maintain capital adequacy calculations based on those old prudential standards.

Note 2: The choice is only for the purposes of calculating amounts for the purposes of the thin capitalisation regime.

- (5) For an income year for which an entity does not make a choice under subsection (2), the current accounting standards will be used for the purpose of calculating amounts applicable to the entity under Division 820 of the *Income Tax Assessment Act 1997*.
- (6) For an income year for which an ADI does not make a choice under subsection (2), the current prudential standards will be used for the purpose of calculating amounts applicable to the ADI under Division 820 of the *Income Tax Assessment Act 1997*.

## **Schedule 5—Forestry managed investments**

### ***Income Tax Assessment Act 1936***

#### **1 Paragraph 82KZMG(2)(a)**

Omit “30 June 2006”, substitute “30 June 2008”.

## **Schedule 6—Debt and equity interests**

### **Part 1—Related party at call etc. loans**

#### *Income Tax Assessment Act 1997*

##### **1 At the end of subsection 164-10(1)**

Add:

- ; or (c) a \*debt interest in the company changes at a particular time (the *change time*) to an \*equity interest in the company because of subsection 974-110(1) or (2); or
- (d) the following conditions are satisfied in relation to an interest in the company:
  - (i) immediately before subsection 974-75(4) ceases to have effect, the interest is taken to be a debt interest in the company because of that subsection;
  - (ii) the interest is an equity interest in the company at the time (the *change time*) that is immediately after that cessation;
  - (iii) subsection 974-75(6) does not apply to the interest in relation to the income year that includes the change time; or
- (e) the following conditions are satisfied in relation to an interest in the company:
  - (i) subsection 974-75(6) applies to the interest in relation to a particular income year;
  - (ii) that subsection does not apply to the interest in relation to the next income year;
  - (iii) the interest is an equity interest in the company at the time (the *change time*) that is the start of that next income year.

##### **2 Subsection 164-15(2)**

Repeal the subsection, substitute:

- (2) If paragraph 164-10(1)(c), (d) or (e) applies in relation to a particular interest in the company, there is a credit to the

\*non-share capital account at the change time referred to in that paragraph of an amount equal to:

$$\text{Amount received} - \frac{\text{Share capital}}{\text{account credit}} - \text{Amount returned}$$

where:

**amount received** is the market value, when it was provided, of the consideration the company received for the issue of the interest.

**amount returned** is so much of the amount received as has been returned to a holder of the interest before the change time.

**share capital account credit** is the amount of any credit made to the company's share capital account in respect of the issue of the interest.

### **3 At the end of section 164-15**

Add:

(5) To avoid doubt, if:

- (a) it appears that a credit to the company's \*non-share capital account has arisen under this section because an interest in the company appears to be, or have become, an \*equity interest at a time in a particular income year; and
- (b) because subsection 974-75(6) or 974-110(1A) is subsequently found to apply in relation to the interest and that income year, the interest was not in fact, or did not in fact become, an equity interest at that time;

the credit referred to in paragraph (a) is taken never to have arisen.

### **4 Subsection 164-20(3)**

Repeal the subsection, substitute:

(3) If:

- (a) an \*equity interest in the company changes at a particular time (the **change time**) to a \*debt interest in the company because of subsection 974-110(1) or (2); or
- (b) an equity interest in the company changes to a debt interest in the company, with effect from a time (the **change time**) that is the start of a particular income year, because of subsection 974-110(1A); or

(c) the following conditions are satisfied in relation to an interest in the company:

- (i) subsection 974-75(6) does not apply to the interest in relation to a particular income year;
- (ii) the interest is an equity interest in the company at the end of that income year;
- (iii) subsection 974-75(6) applies to the interest from the time (the *change time*) that is the start of the next income year;

there is, or is taken to have been, a debit to the \*non-share capital account at the change time equal to:

Credits in relation to the interest    –    Debits in relation to the interest

where:

*credits in relation to the interest* is the sum of all the credits that have been made to the \*non-share capital account in relation to the interest before the change time.

*debits in relation to the interest* is the sum of all the debits that have been made to the \*non-share capital account in relation to the interest before the change time.

## **5 At the end of section 164-20**

Add:

(4) To avoid doubt, if:

- (a) it appears that a debit to the company's \*non-share capital account has arisen because an interest in the company appears to be, or have become, a \*debt interest at a time in a particular income year; and
- (b) because subsection 974-75(6) or 974-110(1A) is subsequently found not to apply in relation to the interest and that income year, the interest was not in fact, or did not in fact become, a debt interest at that time;

the debit referred to in paragraph (a) is taken never to have arisen.

## **6 Paragraph 974-75(4)(c)**

Repeal the paragraph, substitute:

- (c) either:

- (i) the loan is repayable on demand made by the connected entity, and repayment is required immediately on the making of the demand, or is required at the end of a particular period after the demand is made (being a period that is not longer than is reasonably necessary to arrange repayment); or
- (ii) the loan is repayable on the death of the connected entity (if the connected entity is an individual); and

#### 7 At the end of subsection 974-75(4)

Add:

Note: If this subsection ceases to have effect in relation to an interest that is, according to the other provisions of this Division, an equity interest immediately after the cessation, an adjustment to the company's non-share capital account will occur at that time (see subsection 164-15(2)).

#### 8 At the end of section 974-75

Add:

*Further exception for certain related party at call loans*

- (6) In applying this Division in relation to a particular \*scheme and a particular income year (which may be the income year in which the scheme is entered into or a later income year), the scheme is taken not to give rise to an **equity interest** in a company, and instead to give rise to a **debt interest** in the company, if:
  - (a) the scheme takes the form of a loan to the company that satisfies paragraphs (4)(a), (b) and (c); and
  - (b) the company's annual turnover (worked out at the end of the income year) is less than \$20,000,000.

Note: If this subsection does not apply in relation to the previous income year or the next income year, and the scheme gives rise to an equity interest according to the other provisions of this Division, an adjustment to the company's non-share capital account will occur at the end of the previous income year or the start of the next income year (see subsections 164-15(2) and 164-20(3)).

- (7) For the purpose of paragraph (6)(b), the question whether a company's annual turnover (worked out at the end of an income year) is less than \$20,000,000 is to be determined in accordance with subsection 188-10(2) of the \*GST Act, as if that amount of

\$20,000,000 were a turnover threshold for the purposes of that subsection of the GST Act.

## **9 Subsection 974-110(1) (heading)**

Repeal the heading, substitute:

*Change to existing scheme—general rule*

## **10 After paragraph 974-110(1)(c)**

Insert:

and (d) subsection (1A) does not apply to the change;

## **11 After subsection 974-110(1)**

Insert:

*Change to existing scheme—special rule for changing a related party at call etc. loan to a private company from equity to debt*

(1A) If:

- (a) a \*scheme takes the form of a loan that satisfies paragraphs 974-75(4)(a), (b) and (c); and
- (b) the scheme gives rise to an \*equity interest (disregarding the effect this subsection has on the characterisation of the interest because of the change referred to in paragraph (c) of this subsection); and
- (c) the scheme is subsequently changed; and
- (d) the change occurs in the period starting immediately after the end of a particular income year (the *year of effect*) and ending at the end of the earlier of the following days:
  - (i) the due date for lodgment of the company's return of income for the year of effect;
  - (ii) the date of lodgment of the company's return of income for the year of effect; and
- (e) the scheme, as it exists immediately after the change, would give rise to a \*debt interest in the company if the interest came into existence when the change occurred; and
- (f) the company is a \*private company in relation to the year of effect; and
- (g) subsection 974-75(6) does not apply in relation to the loan and the year of effect; and

(h) the company elects that this subsection is to apply to the change;

this Division applies as if the scheme, as it exists immediately after the change, had come into existence at the start of the year of effect, and as if no other change of a kind referred to in subsection (1) had occurred in relation to the interest in the period commencing at the start of the year of effect and ending when the first-mentioned change was made.

Note 1: This will mean that:

- (a) the characterisation of the interest will change, with effect back to the start of the year of effect; and
- (b) that characterisation will not be affected by other changes that occurred after the start of the year of effect and before the change to which this subsection applies.

Note 2: This section can apply to an interest a number of times so that, for example, an interest that is an equity interest when issued may change to debt because of one subsequent change and then back to equity because of a later change.

Note 3: An adjustment to the company's non-share capital account will be taken to have occurred at the start of the year of effect (see subsection 164-20(3)).

(1B) An election for the purposes of paragraph (1A)(h):

- (a) must be in writing; and
- (b) can only be made in the period referred to in paragraph (1A)(d); and
- (c) cannot be revoked.

## **12 Subsection 974-110(3)**

Omit "and (2)(c)", substitute ", (1A)(e) and (2)(c)".

## **13 Application of amendments**

- (1) The amendments made by the items in this Part, other than item 6, apply to:
  - (a) schemes entered into on or after 1 July 2005; and
  - (b) schemes entered into before 1 July 2005, in so far as they continue to exist on and after 1 July 2005.
- (2) The amendment made by item 6 applies in accordance with item 118 of Schedule 1 to the *New Business Tax System (Debt and Equity) Act*

2001, as though the amendment were one of the *debt and equity test amendments* within the meaning of item 118 of that Schedule.

## **Part 2—Technical amendments taken to have commenced on 1 July 2001**

### ***Income Tax Assessment Act 1936***

#### **14 Subsection 160AOA(2)**

Omit “paragraphs (aaa) and (da)”, substitute “paragraph (aaa)”.

#### **15 Subsection 160APAAAB(6)**

Omit “paragraph (c)”, substitute “paragraph (d)”.

### ***Income Tax Assessment Act 1997***

#### **16 Paragraph 104-35(5)(c)**

After “\*equity interests”, insert “or non-equity shares (within the meaning of the *Income Tax Assessment Act 1936*)”.

#### **17 Paragraph 104-35(5)(e)**

After “equity interests”, insert “, non-equity shares (within the meaning of the *Income Tax Assessment Act 1936*)”.

#### **18 Paragraph 104-155(5)(c)**

After “\*equity interests”, insert “or non-equity shares (within the meaning of the *Income Tax Assessment Act 1936*)”.

#### **19 Paragraph 104-155(5)(e)**

After “equity interests”, insert “, non-equity shares (within the meaning of the *Income Tax Assessment Act 1936*)”.

#### **20 Section 109-10 (table item 2, column headed “In these circumstances:”)**

After “\*equity interests”, insert “or non-equity shares (within the meaning of the *Income Tax Assessment Act 1936*)”.

#### **21 Section 109-10 (table item 2, column headed “You acquire the asset at this time:”)**

After “equity interests”, insert “or non-equity shares”.

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## **22 At the end of section 974-75**

Add:

- (5) If, while subsection (4) applies to a \*financing arrangement, a circumstance occurs that would otherwise have attracted the operation of subsection 974-110(1) or (2) in relation to the arrangement:
- (a) that subsection of section 974-110 does not apply to change the result that subsection (4) of this section produces in relation to the arrangement; but
  - (b) for the purpose of applying this Division in relation to the arrangement after subsection (4) of this section has ceased to have effect, that subsection of section 974-110 is taken to have produced the result that it would have produced if subsection (4) of this section had not applied to the arrangement.

## **23 Subsection 974-105(1) (example)**

Omit “section 974-20”, substitute “section 974-70”.

## **24 Subsections 974-110(1) and (2) (note 3)**

Omit “164-20(4)”, substitute “164-20(3)”.

## **25 Application of amendments made by items 14 to 24**

The amendments made by items 14 to 24 apply in accordance with item 118 of Schedule 1 to the *New Business Tax System (Debt and Equity) Act 2001*, as though those amendments were *debt and equity test amendments* within the meaning of item 118 of that Schedule.

## ***New Business Tax System (Debt and Equity) Act 2001***

### **26 Subitem 118(2) of Schedule 1**

Omit “any election made under”.

### **27 Subitem 118(9) of Schedule 1**

Repeal the subitem, substitute:

- (9) If paragraph (6)(a) applies to an interest:
- (a) paragraph 164-10(1)(b) of the *Income Tax Assessment Act 1997* applies to the interest as if the second reference in that

**Schedule 6** Debt and equity interests

**Part 2** Technical amendments taken to have commenced on 1 July 2001

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paragraph to “1 July 2001” were instead a reference to “1 July 2004”; and

- (b) section 164-15 of the *Income Tax Assessment Act 1997* applies to the interest as if the following references were instead references to “1 July 2004”:
- (i) the first reference in subsection 164-15(3) to “1 July 2001”;
  - (ii) the reference in subsection 164-15(3) to “that day”;
  - (iii) the references in paragraph 164-15(3)(b) and subsection 164-15(4) to “1 July 2001”.

## **Part 3—Other technical amendments**

### ***Income Tax Assessment Act 1997***

#### **28 Paragraph 104-35(5)(c)**

Omit “non-equity shares (within the meaning of the *Income Tax Assessment Act 1936*)”, substitute “\*non-equity shares”.

#### **29 Paragraph 104-35(5)(e)**

Omit “(within the meaning of the *Income Tax Assessment Act 1936*)”.

#### **30 Paragraph 104-155(5)(c)**

Omit “non-equity shares (within the meaning of the *Income Tax Assessment Act 1936*)”, substitute “\*non-equity shares”.

#### **31 Paragraph 104-155(5)(e)**

Omit “(within the meaning of the *Income Tax Assessment Act 1936*)”.

#### **32 Section 109-10 (table item 2, column headed “In these circumstances:”)**

Omit “non-equity shares (within the meaning of the *Income Tax Assessment Act 1936*)”, substitute “\*non-equity shares”.

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*[Minister's second reading speech made in—  
House of Representatives on 18 August 2005  
Senate on 7 September 2005]*

(138/05)