Tax Laws Amendment (2006 Measures No. 4) Act 2006

No. 168, 2006

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

Note: An electronic version of this Act is available in ComLaw (http://www.comlaw.gov.au/)

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Tax Laws Amendment (2006 Measures No. 4) Act 2006

No. 168, 2006

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

[*Assented to 12 December 2006*]

The Parliament of Australia enacts:

1 Short title

This Act may be cited as the *Tax Laws Amendment (2006 Measures No. 4) Act 2006*.

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.

Commencement information		
Column 1	**Column 2**	**Column 3**
Provision(s)	**Commencement**	**Date/Details**
1. Sections 1 to 4 and anything in this Act not elsewhere covered by this table	The day on which this Act receives the Royal Assent.	12 December 2006
2. Schedules 1 and 2	The day on which this Act receives the Royal Assent.	12 December 2006
3. Schedule 3, items 1 and 2	The day on which this Act receives the Royal Assent.	12 December 2006
4. Schedule 3, items 3 to 5	13 December 2005.	13 December 2005
5. Schedule 4	The day on which this Act receives the Royal Assent.	12 December 2006

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Each Act that is specified in a Schedule to this Act is amended or repealed as set out in the applicable items in the Schedule concerned, and any other item in a Schedule to this Act has effect according to its terms.

4 Amendment of assessments

Section 170 of the *Income Tax Assessment Act 1936* does not prevent the amendment of an assessment if:

(a) the assessment was made before the commencement of this section; and

(b) the amendment is made within 4 years after that commencement; and

(c) the amendment is made for the purpose of giving effect to Schedule 2.

Schedule 1—Marriage breakdown roll-over

Income Tax Assessment Act 1997

1 At the end of Subdivision 118-A

Add:

118-75 Marriage breakdown settlements

(1) A *capital gain or *capital loss you make as a result of *CGT event C2 happening is disregarded if:

(a) you make the gain or loss in relation to a right that directly relates to the breakdown of a marriage or de facto marriage; and

(b) at the time of the CGT event:

(i) you and your *spouse or former spouse are separated; and

(ii) there is no reasonable likelihood of cohabitation being resumed.

Example: Maude receives an amount from Claude by way of a settlement directly related to the breakdown of their marriage. CGT event C2 would happen to Maude on satisfaction of her legally enforceable right to the amount. Any capital gain or loss that Maude makes in these circumstances is disregarded.

(2) For the purposes of this section, the question whether *spouses or former spouses have separated is to be determined in the same way as it is for the purposes of section 48 of the *Family Law Act 1975* (as affected by sections 49 and 50 of that Act).

2 Before section 118-180

Insert:

Roll-overs under Subdivision 126-A

118-178 Previous roll-over under Subdivision 126-A

(1) This section applies to you if:

(a) you *acquired an *ownership interest in a *dwelling from another person (your ***former partner***) as a result of a *CGT event (the ***earlier event***); and

(b) your former partner acquired the ownership interest on or after 20 September 1985; and

(c) there was a roll-over under Subdivision 126-A (marriage breakdown roll-over) for the earlier event; and

(d) a CGT event (the ***later event***) happens in relation to the ownership interest.

(2) This Subdivision applies to the later event in the way that it would if:

(a) your *ownership interest had commenced when your former partner's ownership interest commenced (the ***acquisition time***); and

(b) from the acquisition time until the time your former partner's ownership interest ended:

(i) you had used the *dwelling in the same way that your former partner used it; and

(ii) the dwelling had been your main residence for the same number of days as it was your former partner's main residence.

Example 1: Peter (the transferor spouse) is the 100% owner of a dwelling that he uses only as a main residence before transferring it to Susan (the transferee spouse). Susan uses the dwelling only as a rental property.

Susan will be eligible for a partial main residence exemption having regard to how both Peter and Susan used the dwelling.

Example 2: Caroline (the transferor spouse) is the 100% owner of a dwelling that she uses only as a rental property before transferring it to David (the transferee spouse). David uses the dwelling only as a main residence.

David will be eligible for only a partial main residence exemption having regard to how both Caroline and David used the dwelling.

3 At the end of subsection 126-5(1)

Add:

; or (d) something done under:

(i) a financial agreement made under Part VIIIA of the *Family Law Act 1975* that is binding because of section 90G of that Act; or

(ii) a corresponding written agreement that is binding because of a corresponding foreign law; or

(e) something done under:

(i) an award made in an arbitration referred to in section 13H of the *Family Law Act 1975*; or

(ii) a corresponding award made in an arbitration under a corresponding State law, Territory law or foreign law; or

(f) something done under a written agreement:

(i) that is binding because of a State law, Territory law or foreign law relating to de facto marriage breakdowns; and

(ii) that, because of such a law, cannot be overridden by an order of a court (except to avoid injustice).

4 After subsection 126-5(3)

Insert:

(3A) There is no roll-over because of paragraph (1)(d) or (f) unless the conditions set out in section 126-25 are met.

5 Subsection 126-5(5) (note)

Omit "Note", substitute "Note 1".

6 At the end of subsection 126-5(5)

Add:

Note 2: A roll-over under this Subdivision may have an effect on the transferee's main residence exemption: see sections 118-178 and 118-180.

7 At the end of subsection 126-15(1)

Add:

; or (d) something done under:

(i) a financial agreement made under Part VIIIA of the *Family Law Act 1975* that is binding because of section 90G of that Act; or

(ii) a corresponding written agreement that is binding because of a corresponding foreign law; or

(e) something done under:

(i) an award made in an arbitration referred to in section 13H of the *Family Law Act 1975*; or

(ii) a corresponding award made in an arbitration under a corresponding State law, Territory law or foreign law; or

(f) something done under a written agreement:

(i) that is binding because of a State law, Territory law or foreign law relating to de facto marriage breakdowns; and

(ii) that, because of such a law, cannot be overridden by an order of a court (except to avoid injustice).

8 At the end of section 126-15

Add:

(5) There is no roll-over because of paragraph (1)(d) or (f) unless the conditions set out in section 126-25 are met.

9 At the end of Subdivision 126-A

Add:

126-25 Conditions for the purposes of subsections 126-5(3A) and 126-15(5)

(1) The conditions referred to in subsections 126-5(3A) and 126-15(5) are that:

(a) at the time of the trigger event:

(i) the *spouses, or former spouses, involved are separated; and

(ii) there is no reasonable likelihood of cohabitation being resumed; and

(b) the trigger event happened because of reasons directly connected with the breakdown of the marriage or de facto marriage.

(2) For the purposes of this section, the question whether *spouses or former spouses have separated is to be determined in the same way as it is for the purposes of section 48 of the *Family Law Act 1975* (as affected by sections 49 and 50 of that Act).

10 Application

(1) The amendment made by item 1 of this Schedule applies to CGT events that happen after the day on which this Act receives the Royal Assent.

(2) The amendments made by items 2 to 9 of this Schedule apply to CGT events that:

(a) are trigger events for the purposes of Subdivision 126-A of the *Income Tax Assessment Act 1997*; and

(b) happen after the day on which this Act receives the Royal Assent.

11 Transitional

The reference in paragraph 126-5(1)(e) or 126-15(1)(e) of the *Income Tax Assessment Act 1997* to section 13H of the *Family Law Act 1975* includes a reference to section 19D or 19E of that Act as in force immediately before the commencement of item 36 of Schedule 4 to the *Family Law Amendment (Shared Parental Responsibility) Act 2006*.

Schedule 2—Consolidation

Income Tax (Transitional Provisions) Act 1997

1 Section 701-35 (heading)

Repeal the heading, substitute:

701-35 Act, transaction or event giving rise to CGT event for pre-formation roll-over after 16 May 2002 to be disregarded if cost base etc. would be different

2 Paragraph 701-35(1)(a)

After "in relation to an asset", insert "(the ***roll-over asset***)".

3 Paragraph 701-35(1)(b)

Omit "that asset", substitute "the roll-over asset".

4 Paragraph 701-35(1)(b)

Omit "the roll-over had not occurred or there had been no such roll-over relief", substitute "the act, transaction or event that gave rise to the CGT event had not occurred in relation to the roll-over asset".

5 Subsection 701-35(1)

Omit "CGT event had not happened", substitute "act, transaction or event had not occurred in relation to the roll-over asset".

6 After subsection 701-35(2)

Insert:

(2A) Subsection (1) does not apply if:

(a) the act, transaction or event mentioned in subsection (1) happened before a demerger and in connection with the demerger; and

(b) before the transitional group came into existence, at least one of the following entities ceased to be a member of the demerger group because of the demerger:

(i) the originating company in relation to the roll-over, or the transferor in relation to the roll-over relief;

(ii) the recipient company, or the transferee in relation to the roll-over relief; and

(c) when the transitional group came into existence, at least one of those entities was *not* a member of that group.

7 Paragraph 701-35(3)(a)

Omit "the asset mentioned in subsection (1)", substitute "the roll-over asset".

8 Application

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

Schedule 3—Simplified imputation system: imputation for NZ resident companies

Part 1—Main amendments

Income Tax Assessment Act 1997

1 After section 220-300

Insert:

Effect of NZ franking company making distribution that is non-assessable and non-exempt

220-350 Providing for a franking credit to arise

(1) This section has effect if:

(a) an *NZ franking company makes a *franked distribution to a company (the ***receiving company***); and

(b) the distribution does not *flow indirectly through the receiving company to another entity; and

(c) because of section 23AI, 23AJ or 23AK of the *Income Tax Assessment Act 1936*:

(i) all of the distribution is *exempt income, or is *non-assessable non-exempt income, in the hands of the receiving company; or

(ii) part of the distribution is exempt income, or is non-assessable non-exempt income, in the hands of the receiving company.

(2) A *franking credit arises in the receiving company's *franking account on the day on which the distribution is made.

Note: If only part of the distribution is exempt income or non-assessable non-exempt income:

(a) a franking credit in relation to the distribution will arise under this section in relation to the part of the distribution that is exempt income, or that is non-assessable non-exempt income; and

(b) another franking credit in relation to the distribution will arise under item 3 of the table in subsection 205-15(1) in relation to

the part of the distribution that is not exempt income, or that is not non-assessable non-exempt income (see also subsection 207-90(2)).

(3) The amount of the *franking credit that so arises is:

(a) if subparagraph (1)(c)(i) applies—the amount of the franking credit on the distribution made by the *NZ franking company; or

(b) if subparagraph (1)(c)(ii) applies—so much of the franking credit on the distribution made by the NZ franking company as is attributable to the part of the distribution referred to in that subparagraph.

(4) The table in subsection 205-15(1) has effect subject to this section.

2 Application of amendment made by item 1

The amendment made by item 1 applies to distributions made on or after 1 April 2003.

Part 2—Consequential amendments

Income Tax Assessment Act 1936

3 At the end of subsection 128TB(1)

Add:

; or (e) the following subparagraphs are satisfied in relation to a dividend paid to the company:

(i) an FDA credit arises for the company under section 128TA in relation to the dividend;

(ii) a franking credit arises in the company's franking account because of the application of section 220-350 of the *Income Tax Assessment Act 1997* in relation to the dividend.

4 At the end of subsection 128TB(3)

Add:

; or (e) in a paragraph (1)(e) case—the amount of the franked part of the dividend.

5 Application of amendments made by items 3 and 4

The amendments made by items 3 and 4 apply to dividends paid on or after 1 April 2003.

Schedule 4—CGT and foreign residents

Part 1—Main amendments

Income Tax Assessment Act 1997

1 Division 136

Repeal the Division.

2 At the end of Part 4-5

Add:

Division 855—Capital gains and foreign residents

Table of Subdivisions

Guide to Division 855
855-A Disregarding a capital gain or loss by foreign residents
855-B Becoming an Australian resident

Guide to Division 855

855-1 What this Division is about

A foreign resident can disregard a capital gain or loss unless the relevant CGT asset is a direct or indirect interest in Australian real property, or relates to a business carried on by the foreign resident through a permanent establishment in Australia.

Special rules apply for individuals who were Australian residents but have become foreign residents (see also Subdivision 104-I) and for foreign resident beneficiaries of fixed trusts.

There are also rules dealing with what happens when a foreign resident becomes an Australian resident.

Subdivision 855-A—Disregarding a capital gain or loss by foreign residents

Table of sections

855-5 Objects of this Subdivision
855-10 Disregarding a capital gain or loss from CGT events
855-15 When an asset is taxable Australian property
855-20 Taxable Australian real property
855-25 Indirect Australian real property interests
855-30 Principal asset test
855-35 Reducing a capital gain or loss from a business asset—Australian permanent establishments
855-40 Capital gains and losses of foreign residents through fixed trusts

855-5 Objects of this Subdivision

(1) The objects of this Subdivision are to improve:
  (a) Australia's status as an attractive place for business and investment; and
  (b) the integrity of Australia's capital gains tax base.

(2) This is achieved by:
  (a) aligning Australia's tax laws with international practice; and
  (b) ensuring interests in an entity remain subject to Australia's capital gains tax laws if the entity's underlying value is principally derived from Australian real property.

855-10 Disregarding a capital gain or loss from CGT events

(1) Disregard a *capital gain or *capital loss from a *CGT event if:
  (a) you are a foreign resident, or the trustee of a *foreign trust for CGT purposes, just before the CGT event happens; and
  (b) the CGT event happens in relation to a *CGT asset that is not *taxable Australian property.

Note: A capital gain or capital loss from a CGT asset you have used at any time in carrying on a business through a permanent establishment in Australia may be reduced under section 855-35.

(2) The *CGT asset in relation to which a *CGT event happens includes the following:

(a) for CGT event D1 (about creating contractual or other rights)—the CGT asset that is the subject of the creation of the contractual or other rights;

Example: You grant an easement over land in Australia. The land is the subject of the creation of the rights in the easement. Therefore, the CGT event happens in relation to the land.

(b) for CGT event D2 (about granting an option)—the CGT asset that is the subject of the option;

(c) for CGT event F1 (about granting a lease)—the CGT asset that is the subject of the lease;

(d) for CGT event J1 (about a company ceasing to be a member of wholly-owned group after roll-over)—the roll-over asset.

855-15 When an asset is taxable Australian property

There are 5 categories of *CGT assets that are ***taxable Australian property***. They are set out in this table.

CGT assets that are taxable Australian property

Item	Description
1	*Taxable Australian real property (see section 855-20)
2	A *CGT asset that: (a) is an *indirect Australian real property interest (see section 855-25); and (b) is not covered by item 5 of this table
3	A *CGT asset that: (a) you have used at any time in carrying on a *business through a permanent establishment (within the meaning of section 23AH of the *Income Tax Assessment Act 1936*) in Australia; and (b) is not covered by item 1, 2 or 5 of this table
4	An option or right to *acquire a *CGT asset covered by item 1, 2 or 3 of this table
5	A *CGT asset that is covered by subsection 104-165(3) (choosing to disregard a gain or loss on ceasing to be an Australian resident)

Note: An asset is also taxable Australian property if it was acquired by a company after 28 January 1988 and before 26 May 1988 from a foreign resident as a result of a disposal for which there was a roll-over under section 160ZZN or 160ZZO of the *Income Tax Assessment Act 1936*: see section 136-25 of the *Income Tax (Transitional Provisions) Act 1997*.

855-20 Taxable Australian real property

A *CGT asset is ***taxable Australian real property*** if it is:

(a) real property situated in Australia; or

(b) a *mining, quarrying or prospecting right (to the extent that the right is not real property), if the minerals, *petroleum or quarry materials are situated in Australia.

855-25 Indirect Australian real property interests

(1) A *membership interest held by an entity (the ***holding entity***) in another entity (the ***test entity***) at a time is an ***indirect Australian real property interest*** at that time if:

(a) the interest passes the *non-portfolio interest test (see section 960-195):

(i) at that time; or

(ii) throughout a 12 month period that began no earlier than 24 months before that time and ended no later than that time; and

(b) the interest passes the principal asset test in section 855-30 at that time.

(2) For the purposes of subsection (1), in working out whether the interest passes the *non-portfolio interest test and the principal asset test in section 855-30:

(a) apply section 350 of the *Income Tax Assessment Act 1936* as if the words “, or is entitled to acquire,” (wherever occurring) were omitted; and

(b) apply section 351 of that Act as if:

(i) the words “, or that the beneficiary is entitled to acquire” (wherever occurring) were omitted; and

(ii) the words “, or that the entity is entitled to acquire” in paragraph 351(2)(d) were omitted.

(3) The first element of the *cost base and *reduced cost base of a *CGT asset on 10 May 2005 is the *market value of the asset on that day if, on that day:

(a) the CGT asset was a *membership interest you held in another entity; and

(b) you were a foreign resident, or the trustee of a trust that was not a *resident trust for CGT purposes; and

(c) the CGT asset was a *post-CGT asset; and

(d) the CGT asset did not have the necessary connection with Australia (within the meaning of this Act as in force on that day) disregarding the operation of paragraph (b) of item 5 and paragraph (b) of item 6 of the table in section 136-25 (as in force on that day).

(4) Also, Parts 3-1 and 3-3 apply to the asset as if you had *acquired it on that day.

855-30 Principal asset test

(1) The purpose of this section is to define when an entity's underlying value is principally derived from Australian real property (see paragraph 855-5(2)(b)).

(2) A *membership interest held by an entity (the ***holding entity***) in another entity (the ***test entity***) passes the principal asset test if the sum of the *market values of the test entity's assets that are *taxable Australian real property exceeds the sum of the *market values of its assets that are *not* taxable Australian real property.

(3) For the purposes of subsection (2), treat an asset of an entity (the ***first entity***) that is a *membership interest in another entity (the ***other entity***) as if it were instead the following 2 assets:

(a) an asset that is *taxable Australian real property (the ***TARP asset***);

(b) an asset that is not taxable Australian real property (the ***non-TARP asset***).

(4) For the purposes of subsection (2), treat the *market value of the TARP asset and the non-TARP asset according to the following table.

Market value of the TARP asset and the non-TARP asset			
Item	**If:**	**the market value of the TARP asset is:**	**the market value of the non-TARP asset is:**
1	(a) the first entity's *direct participation interest in the other entity is less than 10%; or (b) the holding entity's *total participation interest in the other entity is less than 10%	zero	the *market value of the *membership interest mentioned in subsection (3)
2	item 1 does not apply	the product of: (a) the sum of the *market values of all the assets of the other entity that are *taxable Australian real property; and (b) the first entity's *direct participation interest in the other entity	the product of: (a) the sum of the market values of all the assets of the other entity that are *not* taxable Australian real property; and (b) the first entity's direct participation interest in the other entity

Note: For the purposes of item 2 of the table, it is necessary to work out the market value of any TARP assets and non-TARP assets in relation to any membership interests held by the other entity before working out the value of the TARP asset and non-TARP asset held by the first entity.

(5) For the purposes of this section, disregard the *market value of any asset acquired by the test entity, or by any other entity, if the *acquisition was done for a purpose (other than an incidental purpose) that included ensuring that a *membership interest in any entity would not pass the principal asset test in this section.

855-35 Reducing a capital gain or loss from a business asset—Australian permanent establishments

(1) This section applies to a *CGT asset that is *taxable Australian property under item 3 of the table in section 855-15 because you have used it at any time in carrying on a *business through a permanent establishment (within the meaning of section 23AH of the *Income Tax Assessment Act 1936*) in Australia.

(2) The *capital gain or *capital loss you make from a *CGT event in relation to the asset is reduced if you used it in this way for only part of the period from when you *acquired it to when the CGT event happened.

(3) The gain or loss is reduced by this fraction:

$$\frac{\text{Number of days the asset was not used in the way described in subsection (1)}}{\text{Number of days in that period}}$$

855-40 Capital gains and losses of foreign residents through fixed trusts

(1) The purpose of this section is to provide comparable taxation treatment as between direct ownership, and indirect ownership through a *fixed trust, by foreign residents of *CGT assets that are not *taxable Australian property.

(2) A *capital gain you make in respect of your interest in a *fixed trust is disregarded if:

(a) you are a foreign resident when you make the gain; and

(b) the gain is attributable to a *CGT event happening to a *CGT asset of a trust (the ***CGT event trust***) that is:

(i) the fixed trust; or

(ii) another fixed trust in which that trust has an interest (directly, or indirectly through a *chain of fixed trusts); and

(c) either:

(i) the asset is not *taxable Australian property for the CGT event trust at the time of the CGT event; or

(ii) the asset is an interest in a fixed trust and the conditions in subsections (5), (6), (7) and (8) are satisfied.

Note: Section 115-215 treats a portion of a trust's capital gain as a capital gain made by a beneficiary, and applies the CGT discount to that portion as if the gain were made directly by the beneficiary.

(3) You are not liable to pay tax as a trustee of a *fixed trust in respect of an amount to the extent that:

(a) the amount gives rise to a *capital gain that is disregarded for a beneficiary under subsection (2); or

(b) the amount gives rise to a deduction for a beneficiary under subsection (9).

(4) To avoid doubt, subsection (3) does not affect the operation of subsection 98A(1) of the *Income Tax Assessment Act 1936* (about taxing beneficiaries who are foreign residents at the end of an income year).

Conditions

(5) The conditions in subsections (6), (7) and (8) must be satisfied if the relevant *CGT event happens to an interest in a *fixed trust (the ***first trust***) and the interest is *taxable Australian property at the time of the CGT event.

(6) At least 90% (by *market value) of the *CGT assets of:

(a) the first trust; or

(b) a *fixed trust in which the first trust has an interest (directly, or indirectly through a *chain of fixed trusts);

must not be *taxable Australian property at the time of the relevant *CGT event.

(7) If the condition in subsection (6) is not satisfied for the first trust (but is satisfied for a trust covered by paragraph (6)(b)), the condition in subsection (8) must be satisfied for the first trust, and for each other trust in the *chain of trusts between the first trust and the trust that satisfied the condition in subsection (6).

(8) The condition is that, assuming any interest in a *fixed trust in that *chain not to be *taxable Australian property, at least 90% (by *market value) of the *CGT assets of the trust must not be taxable Australian property.

Foreign resident companies

(9) If a company's assessable income for an income year includes an amount under subsection 98A(1) of the *Income Tax Assessment Act 1936* because it is a beneficiary described in subsection 98(3) of that Act, the company can deduct for the income year the amount of a *capital gain that would be disregarded for it under this section for that year had section 115-215 of this Act applied to it for that year.

Note 1: Section 98A of the *Income Tax Assessment Act 1936* deals with taxing beneficiaries who are foreign residents at the end of an income year.

Note 2: Subsection 98(3) of that Act makes the trustee liable for tax on the share of the income of the trust to which a foreign resident company is presently entitled.

Note 3: Section 115-215 treats a portion of a trust's capital gain as a capital gain made by a beneficiary, and applies the CGT discount to that portion as if the gain were made directly by the beneficiary.

Subdivision 855-B—Becoming an Australian resident

Table of sections

855-45 Individual or company becomes an Australian resident
855-50 Trust becomes a resident trust
855-55 CFC becomes an Australian resident

855-45 Individual or company becomes an Australian resident

(1) If you become an Australian resident, there are rules relevant to each *CGT asset that you owned just before you became an Australian resident, except an asset:

(a) that is *taxable Australian property; or

(b) that you *acquired before 20 September 1985.

Note: This section has effect subject to section 768-950 (individuals who become Australian residents and are temporary residents immediately after they become Australian residents).

(2) The first element of the *cost base and *reduced cost base of the asset (at the time you become an Australian resident) is its *market value at that time.

(3) Also, Parts 3-1 and 3-3 apply to the asset as if you had *acquired it at the time you became an Australian resident.

(4) This section does not apply to a *share or right if:
  (a) it is a *qualifying share or a *qualifying right; and
  (b) you have not made an election under section 139E of the *Income Tax Assessment Act 1936* covering the share or right; and
  (c) the *cessation time for the share or right has not occurred.

855-50 Trust becomes a resident trust

(1) If a trust becomes a *resident trust for CGT purposes, there are rules relevant to each *CGT asset that the trustee owned just before the trust became a resident trust for CGT purposes, except one:
  (a) that is *taxable Australian property; or
  (b) that the trustee *acquired before 20 September 1985.

(2) The first element of the *cost base and *reduced cost base of the asset (at the time the trust becomes a *resident trust for CGT purposes) is its *market value at that time.

(3) Also, Parts 3-1 and 3-3 apply to the asset as if the trustee had *acquired it at the time the trust became a *resident trust for CGT purposes.

Exception

(4) This section does not apply to a trust if, just before it became a *resident trust for CGT purposes, it was a *CFT because of paragraph 342(a) of the *Income Tax Assessment Act 1936*.

Note: This section is disregarded in calculating the attributable income of a trust: see section 102AAZB of the *Income Tax Assessment Act 1936*.

855-55 CFC becomes an Australian resident

(1) This section applies to a *CFC that stops at a time (the ***residence change time***) being a resident of a *listed country or an *unlisted country and becomes an Australian resident.

(2) Section 855-45 does not apply to the *CFC.

(3) The modifications of Parts 3-1 and 3-3 of this Act in sections 411 to 414 of the *Income Tax Assessment Act 1936* have the effect they would have, in relation to each *commencing day asset owned by

the *CFC at the residence change time, if those modifications were used to work out the taxable income of the CFC rather than its *attributable income.

(4) However, if a *capital gain on a *commencing day asset of the *CFC (for a period before the residence change time) was subject to tax (within the meaning of Part X of the *Income Tax Assessment Act 1936*) in a *listed country, the modifications of Parts 3-1 and 3-3 of this Act in sections 411 to 414 of the *Income Tax Assessment Act 1936* have the effect they would have in relation to the asset if:

(a) those modifications were used to work out the taxable income of the CFC rather than its *attributable income; and

(b) the *commencing day of the CFC were the residence change time.

Note: This section is disregarded in calculating the attributable income of a CFC: see section 410 of the *Income Tax Assessment Act 1936.*

Part 2—Other amendments

Income Tax Assessment Act 1997

3 Subsection 104-160(3)

Omit all the words after "except one", substitute:

that is *taxable Australian property:

(a) covered by item 1 or 3 of the table in section 855-15; or

(b) covered by item 4 of that table because it is an option or right to *acquire a *CGT asset covered by item 1 or 3 of that table.

4 After subsection 104-160(4)

Insert:

(4A) If the asset is an *indirect Australian real property interest, or an option or right to acquire such an interest, this Part and Part 3-3 apply to the asset as if the first element of the *cost base and *reduced cost base of the asset (just after the time of the event) were its *market value at the time of the event.

(4B) Subsection (4A) does not apply if the *capital gain or *capital loss you make is disregarded under subsection (5) or (6), or subsection 104-165(2).

5 Subsection 104-160(6) (note 2)

After "in relation to the asset", insert "where he or she ceases to own the asset".

6 Subsection 104-165(3)

Omit "have the *necessary connection with Australia", substitute "be *taxable Australian property".

7 Paragraph 104-165(3)(a)

After "asset", insert ", if the CGT event involves you ceasing to own the asset".

8 At the end of section 104-165

Add:

Note: If you are an individual who was in Australia on 6 April 2006, and you remain an Australian resident from that day until you stop being one, and you were an Australian resident for less than 5 years during the 10 years before you stopped being one, see section 104-166 of the *Income Tax (Transitional Provisions) Act 1997*.

9 Section 104-166

Repeal the section.

10 Subsection 104-170(3)

Omit all the words after "time of the event", substitute:

except one that is *taxable Australian property:

(a) covered by item 1 or 3 of the table in section 855-15; or

(b) covered by item 4 of that table because it is an option or right to *acquire a *CGT asset covered by item 1 or 3 of that table.

11 After subsection 104-170(4)

Insert:

(4A) If the asset is an *indirect Australian real property interest, or an option or right to acquire such an interest, this Part and Part 3-3 apply to the asset as if the first element of the *cost base and *reduced cost base of the asset (just after the time of the event) were its *market value at the time of the event.

(4B) Subsection (4A) does not apply if the *capital gain or *capital loss the trustee makes is disregarded under subsection (5).

12 After Subdivision 960-G

Insert:

Subdivision 960-GP—Participation interests in entities

Table of sections

960-180 Total participation interest
960-185 Indirect participation interest
960-190 Direct participation interest
960-195 Non-portfolio interest test

960-180 Total participation interest

An entity's ***total participation interest*** at a particular time in another entity is the sum of:

(a) the entity's *direct participation interest in the other entity at that time; and

(b) the entity's *indirect participation interest in the other entity at that time.

960-185 Indirect participation interest

(1) Work out the ***indirect participation interest*** that an entity (the ***holding entity***) holds at a particular time in another entity (the ***test entity***) by multiplying:

(a) the holding entity's *direct participation interest (if any) in another entity (the ***intermediate entity***) at that time;

by:

(b) the sum of:

(i) the intermediate entity's direct participation interest (if any) in the test entity at that time; and

(ii) the intermediate entity's indirect participation interest (if any) in the test entity at that time (as worked out under one or more other applications of this section).

(2) If there is more than one intermediate entity to which paragraph (1)(a) applies at that time, the holding entity's ***indirect participation interest*** is the sum of the percentages worked out under subsection (1) in relation to each of those intermediate entities.

960-190 Direct participation interest

(1) Use the following table to work out the ***direct participation interest*** that one entity holds in another entity.

Direct participation interest	
If the other entity is this kind of entity:	**the direct participation interest that the first entity holds in the other entity is:**

Direct participation interest		
	If the other entity is this kind of entity:	**the direct participation interest that the first entity holds in the other entity is:**
1	A company (within the meaning of Part X of the *Income Tax Assessment Act 1936*)	the direct control interest (within the meaning of section 350 of the *Income Tax Assessment Act 1936*) that the first entity holds in the other entity
2	A trust (within the meaning of Part X of the *Income Tax Assessment Act 1936*)	the direct control interest (within the meaning of section 351 of the *Income Tax Assessment Act 1936*) that the first entity holds in the other entity
3	A *partnership	the direct control interest (within the meaning of section 350 of the *Income Tax Assessment Act 1936*) that the first entity would hold in the other entity, if the assumptions in subsection (3) of this section were made

(2) For the purposes of subsection (1):

(a) apply sections 350 and 351 of the *Income Tax Assessment Act 1936* as if those sections apply for the purposes of this Division rather than only for the purposes of Part X of that Act; and

(b) do not apply subsections 350(6) and (7) and 351(3) and (4) of that Act.

(3) For the purposes of item 3 of the table in subsection (1), assume that:

(a) the *partnership is a company; and

(b) the partners in the partnership are shareholders in the company; and

(c) the total amount of assets or capital contributed to the partnership is the total paid-up share capital of the company; and

(d) a partner's right of distribution of capital, assets or profits on the dissolution of the partnership is a shareholder's right to distribution of capital or profits of the company on winding-up; and

(e) a partner's right of distribution of capital, assets or profits otherwise than on the dissolution of the partnership is a shareholder's right to distribution of capital or profits of the company otherwise than on winding-up.

960-195 Non-portfolio interest test

An interest held by an entity (the ***holding entity***) in another entity (the ***test entity***) passes the non-portfolio interest test at a time if the sum of the *direct participation interests held by the holding entity and its *associates in the test entity at that time is 10% or more.

Part 3—Consequential amendments

Financial Corporations (Transfer of Assets and Liabilities) Act 1993

13 Section 19

Omit "had, while it is an asset of the receiving corporation, the necessary connection with Australia", substitute "is, while it is an asset of the receiving corporation, taxable Australian property".

Note: The heading to section 19 is altered by omitting "**has necessary connection with Australia**" and substituting "**is taxable Australian property**".

Income Tax Assessment Act 1936

14 Subsection 6(1) (definition of *necessary connection with Australia*)

Repeal the definition.

15 Subsection 6(1)

Insert:

> ***taxable Australian property*** has the same meaning as in the *Income Tax Assessment Act 1997*.

16 Paragraph 23AH(3)(c)

Omit "does not have the necessary connection with Australia", substitute "is not taxable Australian property".

17 Paragraph 102AAZB(a)

Omit "136-45", substitute "855-50".

18 Paragraph 396(2)(b)

Omit "has the necessary connection with Australia (within the meaning of the *Income Tax Assessment Act 1997*)", substitute "is taxable Australian property".

19 Subsection 396(3)

Omit "and in deciding whether a CGT asset has the necessary connection with Australia, disregard the residency assumption in applying category 8 or 9 of the table in section 136-25 of the *Income Tax Assessment Act 1997*".

20 Paragraph 399(1)(c)

Omit "136-45", substitute "855-50".

21 Subsection 406(2)

Omit "having the necessary connection with Australia", substitute "that is taxable Australian property".

22 Subsection 406(3)

Repeal the subsection, substitute:

(3) In determining whether a CGT asset is taxable Australian property, disregard the residency assumption.

23 Section 408

Omit "because of Subdivision 136-A", substitute "that is not disregarded under Subdivision 855-A".

24 Paragraph 410(d)

Omit "136-40", substitute "855-45".

25 Paragraph 410(e)

Omit "136-50", substitute "855-55".

26 Subsection 438(4)

Omit "does not have the necessary connection with Australia within the meaning of the *Income Tax Assessment Act 1997*", substitute "is not taxable Australian property".

27 Subparagraph 245-55(4)(a)(ii) in Schedule 2C

Omit "having the necessary connection with Australia", substitute "that was taxable Australian property".

28 Paragraph 245-65(2A)(b) in Schedule 2C

Omit "having the necessary connection with Australia", substitute "that was taxable Australian property".

Income Tax Assessment Act 1997

29 Section 12-5 (table item headed "foreign residents")

Omit "section 768-615", substitute "subsection 855-40(9)".

30 Paragraph 104-215(2)(b)

Omit "does not have the *necessary connection with Australia", substitute "is not *taxable Australian property".

31 Paragraph 104-230(7)(c)

Omit "does not have the *necessary connection with Australia", substitute "is not *taxable Australian property".

32 Section 109-55 (table item 15, column 2)

Omit "did not have the necessary connection with Australia", substitute "was not *taxable Australian property".

33 Section 109-55 (table item 15, column 4)

Omit "section 136-40", substitute "section 855-45".

34 Section 109-55 (table item 15A, column 2)

Omit "did not have the necessary connection with Australia", substitute "was not *taxable Australian property".

35 Section 109-55 (table item 16, column 2)

Omit "did not have the necessary connection with Australia", substitute "was not *taxable Australian property".

36 Section 109-55 (table item 16, column 4)

Omit "section 136-45", substitute "section 855-50".

37 Section 112-87 (table item 1, column 4)

Omit "section 136-40", substitute "section 855-45".

38 Section 112-87 (table item 2, column 4)

Omit "section 136-45", substitute "section 855-50".

38A Section 112-97 (at the end of the table)

Add:

28	On 10 May 2005, a foreign resident holds certain membership interests	first element of *cost base and *reduced cost base	subsection 855-25(3)

39 Paragraph 116-95(1)(c)

Omit "has the *necessary connection with Australia", substitute "is *taxable Australian property".

40 Subsection 121-30(2)

Omit "Subdivision 768-H", substitute "section 855-40".

41 Subsection 122-25(6)

Repeal the subsection, substitute:

(6) If you are an individual at the time of the trigger event, either:
- (a) you and the company must both be Australian residents at that time; or
- (b) both of the following requirements must be satisfied:
  - (i) each asset must be *taxable Australian property at that time;
  - (ii) the shares in the company mentioned in subsection 122-20(1) must be taxable Australian property just after that time.

42 Subsection 122-25(7)

Repeal the subsection, substitute:

(7) If you are a trustee of a trust at the time of the trigger event, either:
- (a) at that time, the trust must be a *resident trust for CGT purposes and the company must be an Australian resident; or
- (b) both of the following requirements must be satisfied:
  - (i) each *CGT asset must be a CGT asset of the trust that is *taxable Australian property at that time; and
  - (ii) the shares in the company mentioned in subsection 122-20(1) must be taxable Australian property just after that time.

43 Subsection 122-135(6)

Repeal the subsection, substitute:

(6) For a partner who is not a trustee of a trust at the time of the trigger event, either:
  (a) the partner and the company must both be Australian residents at that time; or
  (b) both of the following requirements must be satisfied:
    (i) each asset must be *taxable Australian property at that time; and
    (ii) the shares in the company mentioned in subsection 122-130(1) must be taxable Australian property just after that time.

44 Subsection 122-135(7)

Repeal the subsection, substitute:

(7) For a partner who is a trustee of a trust at the time of the trigger event, either:
  (a) at that time, the trust must be a *resident trust for CGT purposes and the company must be an Australian resident; or
  (b) both of the following requirements must be satisfied:
    (i) each *CGT asset must be a CGT asset of the trust that is *taxable Australian property at that time; and
    (ii) the shares in the company mentioned in subsection 122-130(1) must be taxable Australian property just after that time.

45 Paragraph 124-70(3)(b)

Omit “not a *resident trust for CGT purposes”, substitute “a *foreign trust for CGT purposes”.

46 Subsection 124-70(4)

Omit “have the *necessary connection with Australia just before”, substitute “be *taxable Australian property just before”.

47 Subsection 124-70(4)

Omit “have the *necessary connection with Australia just after”, substitute “be taxable Australian property just after”.

48 Subparagraph 124-240(f)(ii)

Omit "have the *necessary connection with Australia", substitute "were *taxable Australian property just before that time and the new shares are taxable Australian property when they are issued".

49 Subparagraph 124-245(e)(ii)

Omit "have the *necessary connection with Australia", substitute "were *taxable Australian property just before that time and the new units are taxable Australian property when they are issued".

50 Paragraph 124-295(7)(b)

Repeal the paragraph, substitute:

(b) if you are a foreign resident at that time:

(i) the original rights or original option were *taxable Australian property just before that time; and

(ii) the new rights or new option are taxable Australian property when they are issued.

51 Paragraph 124-300(7)(b)

Repeal the paragraph, substitute:

(b) if you are a foreign resident at that time:

(i) the original rights or original option were *taxable Australian property just before that time; and

(ii) the new rights or new option are taxable Australian property when they are issued.

52 Paragraph 124-365(4)(b)

Repeal the paragraph, substitute:

(b) if you are a foreign resident at that time:

(i) your shares in the original company were *taxable Australian property just before that time; and

(ii) your shares in the interposed company are taxable Australian property just after the completion time.

53 Paragraph 124-375(4)(b)

Repeal the paragraph, substitute:

(b) if you are a foreign resident at that time:

(i) your shares in the original company were *taxable Australian property just before that time; and

(ii) your shares in the interposed company are taxable Australian property just after the completion time.

54 Subsection 124-380(4)

Repeal the subsection.

55 Paragraph 124-450(4)(b)

Repeal the paragraph, substitute:

(b) if you are a foreign resident at that time:

(i) your units were *taxable Australian property just before that time; and

(ii) your *shares in the company are taxable Australian property just after the completion time.

56 Paragraph 124-460(4)(b)

Repeal the paragraph, substitute:

(b) if you are a foreign resident at that time:

(i) your units were *taxable Australian property just before that time; and

(ii) your *shares in the company are taxable Australian property just after the completion time.

57 Subsection 124-465(4)

Repeal the subsection.

58 Subparagraph 124-520(1)(e)(ii)

Omit "has the *necessary connection with Australia", substitute "was *taxable Australian property just before that time and the *shares are taxable Australian property when they are issued".

59 Subsection 124-795(1)

Omit "the replacement entity is an Australian resident or a *resident trust for CGT purposes", substitute "the replacement interest is *taxable Australian property".

60 Subsection 124-795(1) (note)

Repeal the note.

61 Subsections 124-795(4) and (5)

Repeal the subsections.

62 Subsection 124-860(8)

Repeal the subsection.

63 Subsection 124-870(3)

Omit "have the *necessary connection with Australia", substitute "are *taxable Australian property".

64 At the end of section 124-875

Add:

Exception: asset must be taxable Australian property for foreign resident transferee

(6) For a transferee that is a foreign resident, this section only applies to a *CGT asset that is *taxable Australian property just after the transferee *acquires it under the trust restructure.

65 Paragraph 125-55(2)(b)

Omit "does not have the *necessary connection with Australia", substitute "is not *taxable Australian property".

66 Subsection 125-55(2) (note)

Repeal the note, substitute:

Note: For ***taxable Australian property***, see section 855-15.

67 Paragraph 125-70(1)(f)

Repeal the paragraph.

68 Paragraph 126-20(1)(c)

Omit "did not have the *necessary connection with Australia", substitute "was not *taxable Australian property".

69 Subsection 126-50(5) (table, heading to column 4)

Omit "**have the necessary connection with Australia**", substitute "**be taxable Australian property**".

70 Paragraph 126-75(1)(c)

Omit “did not have the *necessary connection with Australia”, substitute “was not *taxable Australian property for the originating company”.

71 Subsection 128-15(4) (table item 1, column 2)

Omit “item 2 or 3”, substitute “ item 2, 3 or 3A”.

72 Subsection 128-15(4) (after table item 3)

Insert:

3A	If you were a foreign resident just before you died—an asset that was not *taxable Australian property just before you died, except one covered by item 2	the *market value of the asset on the day you died	the market value of the asset on the day you died

73 Subsection 128-25(2) (note 2)

Omit “Subdivision 136-B”, substitute “Subdivision 855-B”.

74 Paragraph 130-80(4)(c)

Omit “does not have the *necessary connection with Australia”, substitute “is not *taxable Australian property”.

75 Subsection 130-80(4) (note 1)

Repeal the note, substitute:

Note: Sections 768-955 and 855-45 deal with shares or rights that are not taxable Australian property.

76 Paragraph 130-83(4)(c)

Omit “does not have the *necessary connection with Australia”, substitute “is not *taxable Australian property”.

77 Subsection 130-83(4) (note 1)

Repeal the note, substitute:

Note 1: Sections 768-955 and 855-45 deal with shares or rights that are not taxable Australian property.

78 Paragraph 130-85(4)(c)

Omit "does not have the *necessary connection with Australia", substitute "is not *taxable Australian property".

79 Subsection 130-85(4) (note 1)

Repeal the note, substitute:

Note 1: Sections 768-955 and 855-45 deal with shares or rights that are not taxable Australian property.

80 Subparagraph 170-255(1)(d)(ii)

Omit "one of the items in the table in subsection 136-15(1) is satisfied", substitute "the *CGT asset that is the subject of the creation of the contractual or other rights is *taxable Australian property".

81 Subparagraph 170-255(1)(d)(iii)

Omit "had the *necessary connection with Australia", substitute "was *taxable Australian property".

82 Subparagraph 170-255(1)(d)(iv)

Omit "had the *necessary connection with Australia", substitute "was taxable Australian property".

83 Subdivision 768-G (heading)

Repeal the heading, substitute:

Subdivision 768-G—Reduction in capital gains and losses arising from CGT events in relation to certain voting interests in active foreign companies

84 Section 768-505 (heading)

Repeal the heading, substitute:

768-505 Reducing a capital gain or loss from certain CGT events in relation to certain voting interests

85 Subsection 768-505(1)

After "(the ***holding company***)", insert "that is an Australian resident".

86 Paragraph 768-540(1)(c)

Repeal the paragraph, substitute:

(c) the asset is *not* any of the following:

(i) *taxable Australian property;

(ii) a *membership interest in a company that is an Australian resident;

(iii) a membership interest in a *resident trust for CGT purposes;

(iv) an option or right to acquire a membership interest mentioned in subparagraph (ii) or (iii); and

87 Subdivision 768-H

Repeal the Subdivision.

88 Paragraph 768-915(b)

After "from the CGT event", insert ", or the capital gain or loss from the CGT event would have been disregarded under Division 855,".

89 Section 768-915 (note)

Repeal the note.

90 Paragraph 768-920(1)(c)

Omit "does not have the *necessary connection with Australia", substitute "is not *taxable Australian property".

91 Paragraph 768-920(2)(d)

Omit "does not have the *necessary connection with Australia", substitute "is not *taxable Australian property".

92 Subsection 768-920(4) (note)

Omit "Division 136 nor section 768-915", substitute "section 768-915 nor Division 855".

93 Subsection 768-920(5)

Omit "Division 136 and section 768-915", substitute "section 768-915 and Division 855".

94 Subsection 768-920(8)

Omit "subsections 136-40(3) and 768-955(3)", substitute "subsections 768-955(3) and 855-45(3)".

95 Section 768-950

Omit “Section 136-40”, substitute “Section 855-45”.

96 Paragraph 768-955(1)(b)

Repeal the paragraph, substitute:

(b) is not *taxable Australian property; and

97 After section 960-60

Insert:

960-61 Functional currency for calculating capital gains and losses on indirect Australian real property interests

(1) Subsection (2) applies if:

(a) you are a foreign resident; and

(b) a *CGT event happens in relation to a *CGT asset that is an *indirect Australian real property interest for you; and

(c) the sole or predominant currency in which you keep your accounts at the time of the CGT event is a currency other than Australian currency.

(2) You must use the *applicable functional currency to work out the amount of your *capital gain or *capital loss (if any).

98 After subsection 960-70(3)

Insert:

Calculating capital gains and losses on indirect Australian real property interests

(3A) If subsection 960-61(2) applies, your ***applicable functional currency*** for the purposes of that subsection is the sole or predominant currency in which you keep your accounts at the time of the *CGT event.

99 Subsection 960-80(1) (at the end of the table)

Add:

6	(a) you are a *foreign resident who makes a *capital gain or *capital loss from a *CGT event in relation to an asset that is an *indirect Australian real property interest; and (b) you are required by subsection 960-61(2) to work out the amount of your capital gain or capital loss in the *applicable functional currency	(a) first, for the purpose of working out, for the income year, the amount of your capital gain or capital loss from the CGT event, an amount that is not in the applicable functional currency is to be translated into the applicable functional currency; and (b) second, the amount of the capital gain or capital loss is to be translated into Australian currency.

100 Subsection 995-1(1)

Insert:

> ***direct participation interest*** has the meaning given by section 960-190.

101 Subsection 995-1(1)

Insert:

> ***foreign trust for CGT purposes*** means a trust that is not a *resident trust for CGT purposes.

102 Subsection 995-1(1)

Insert:

> ***indirect Australian real property interest*** has the meaning given by section 855-25.

103 Subsection 995-1(1)

Insert:

> ***indirect participation interest*** has the meaning given by section 960-185.

104 Subsection 995-1(1) (definition of *necessary connection with Australia*)

Repeal the definition.

105 Subsection 995-1(1)

Insert:

non-portfolio interest test: an interest held by an entity in another entity passes the ***non-portfolio interest test*** in the circumstances set out in section 960-195.

106 Subsection 995-1(1)

Insert:

taxable Australian property has the meaning given by section 855-15.

107 Subsection 995-1(1)

Insert:

taxable Australian real property has the meaning given by section 855-20.

108 Subsection 995-1(1)

Insert:

total participation interest has the meaning given by section 960-180.

Part 4—Application and transitional

Income Tax (Transitional Provisions) Act 1997

109 After Subdivision 104-G

Insert:

Subdivision 104-I—Australian residency ends

104-165 Choices made under subsection 104-165(2) of the *Income Tax Assessment Act 1997*

(1) This section applies if:

(a) a choice was made under subsection 104-165(2) of the *Income Tax Assessment Act 1997*; and

(b) because of the choice, an asset is taken to have the necessary connection with Australia under subsection 104-165(3) of the *Income Tax Assessment Act 1997* just before the commencement of Schedule 4 of the *Tax Laws Amendment (2006 Measures No. 4) Act 2006*.

(2) To avoid doubt, the choice has effect for the purposes of subsection 104-165(3) of the *Income Tax Assessment Act 1997* as in force on and after that commencement.

Note: This means that the asset will be taxable Australian property under the *Income Tax Assessment Act 1997* as in force on and after that commencement.

104-166 Subsection 104-165(1) still applies if you continue to be a short term Australian resident

Subsection 104-165(1) of the *Income Tax Assessment Act 1997* continues to apply, despite its repeal by item 20 of Schedule 1 to the *Tax Laws Amendment (2006 Measures No. 1) Act 2006*, to an individual:

(a) who is in Australia on the day on which that item receives the Royal Assent; and

(b) who remains an Australian resident from that day until the time subsection 104-165(1) is applied in respect of him or her.

110 Section 136-25 (heading)

Repeal the heading, substitute:

136-25 When an asset is taxable Australian property

111 Section 136-25

Omit "has the necessary connection with Australia", substitute "is taxable Australian property".

112 Application of this Schedule

The amendments made by this Schedule apply to CGT events that happen on or after the commencement of this item.

[*Minister's second reading speech made in—*
House of Representatives on 22 June 2006
Senate on 16 October 2006]

(100/06)