



Taxation Laws Amendment Act (No. 8) 2003

No. 107, 2003

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

Note: An electronic version of this Act is available in SCALEplus
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No. 107, 2003

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

[Assented to 21 October 2003]

The Parliament of Australia enacts:

1 Short title

This Act may be cited as the *Taxation Laws Amendment Act (No. 8) 2003*.

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.	21 October 2003
2. Schedules 1 to 5	The day on which this Act receives the Royal Assent.	21 October 2003
3. Schedule 6	1 July 2003.	1 July 2003
4. Schedule 7, items 1 to 5	The day on which this Act receives the Royal Assent.	21 October 2003
5. Schedule 7, items 6 to 8	Immediately after the commencement of Schedule 7 to the <i>Taxation Laws Amendment Act (No. 7) 2003</i> .	
6. Schedule 7, items 9 to 14	The day on which this Act receives the Royal Assent.	21 October 2003
7. Schedule 7, item 15	Immediately after the commencement of item 11 of Schedule 8 to the <i>Taxation Laws Amendment Act (No. 5) 2003</i> .	
8. Schedule 7, items 16 to 22	The day on which this Act receives the Royal Assent.	21 October 2003

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Each Act that is specified in a Schedule to this Act is amended or repealed as set out in the applicable items in the Schedule concerned, and any other item in a Schedule to this Act has effect according to its terms.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 made before the commencement of this section for the purposes of giving effect to this Act.

Schedule 1—Franking of non-share dividends

Part 1—Amendment of the Income Tax Assessment Act 1997

1 Subsection 215-25(1)

Omit all the words after paragraph (d), substitute:

; and (e) it is reasonable to expect that, having regard to the available profits mentioned in paragraph (d), the amount of the entity's *adjusted available frankable profits immediately after each of the committed distributions is paid will be greater than nil.

The *available frankable profits* immediately before the entity pays the non-share dividend is then the smallest of the amounts of the adjusted available frankable profits mentioned in paragraph (e).

2 Subsection 215-25(2)

Repeal the subsection, substitute:

(2) The entity's *adjusted available frankable profits* immediately after a committed distribution is paid is the amount that would be its *available frankable profits at that time if all committed distributions to be paid after that time, and the *non-share dividend, were ignored.

3 Subparagraph 215-25(3)(b)(i)

Omit “when”, substitute “immediately after”.

4 Subsection 995-1(1)

Insert:

adjusted available frankable profits has the meaning given by subsection 215-25(2).

Part 2—Amendment of the Income Tax Assessment Act 1936

5 Subsection 160APAAAB(6)

Omit all the words after paragraph (d), substitute:

; and (e) it is reasonable to expect that, having regard to the profits mentioned in paragraph (d), the amount of the company's adjusted available frankable profits (see subsection (12A)) immediately after each of the committed share dividends is paid will be greater than nil.

The available frankable profits immediately before the company pays the non-share dividend is then the smallest of the amounts of the adjusted available frankable profits mentioned in paragraph (e).

6 Subsection 160APAAAB(7)

Repeal the subsection.

7 Subparagraph 160APAAAB(8)(b)(i)

Omit "when", substitute "immediately after".

8 After subsection 160APAAAB(12)

Insert:

(12A) A company's *adjusted available frankable profits* immediately after a committed share dividend is paid is the amount that would be its available frankable profits at that time if all committed share dividends to be paid after that time, and the non-share dividend, were ignored.

Part 3—Application

9 Application

- (1) The amendments made by Part 1 of this Schedule apply to non-share dividends paid after 30 June 2002.
- (2) The amendments made by Part 2 of this Schedule apply to non-share dividends paid after 30 June 2001 and before 1 July 2002.

Schedule 2—Various amendments relating to consolidated groups

Part 1—Tax cost setting for certain depreciating assets

Income Tax Assessment Act 1997

1 Paragraph 701-55(2)(d)

Omit “section 40-95 (other than subsections (2) and (5))”, substitute “subsections 40-95(1) and (3)”.

Part 2—Cost base and reduced cost base of pre-CGT assets

Income Tax Assessment Act 1997

2 Subsection 126-60(3) (note)

Omit “Note”, substitute “Note 1”.

3 At the end of subsection 126-60(3)

Add:

Note 2: Under section 716-855, where there have been certain roll-overs, the cost base and reduced cost base of pre-CGT assets for the purposes of Part 3-90 (Consolidated groups) are worked out by applying subsection (2), rather than subsection (3), of this section.

4 At the end of subsection 705-65(1)

Add:

Note: Under section 716-855, if membership interests are pre-CGT assets that have been subject to certain roll-overs, the cost base and reduced cost base are worked out in the same way as if they were post-CGT assets.

5 After section 716-850

Insert:

716-855 Working out the cost base or reduced cost base of a pre-CGT asset after certain roll-overs

If:

- (a) it is necessary for the purposes of this Part to work out the *cost base or *reduced cost base of a *pre-CGT asset owned at a particular time; and
- (b) before that time:
 - (i) the owner was the recipient company involved in a roll-over under Subdivision 126-B in relation to a *CGT event that happened in relation to the CGT asset; or

- (ii) the owner was the transferee in relation to a disposal of the CGT asset to which section 160ZZO of the *Income Tax Assessment Act 1936* applied;

the cost base or reduced cost base is worked out as if, in applying Subdivision 126-B or section 160ZZO in relation to the CGT event or the disposal, the provisions of that Subdivision or section applying to CGT assets *acquired on or after 20 September 1985 replaced those that applied to CGT assets acquired on or before that date.

Note: The effect is that the owner's cost base or reduced cost base will be the same as that of the originating company or transferor, as is the case with post-CGT assets.

Income Tax (Transitional Provisions) Act 1997

6 After section 701-5

Insert:

701-7 Working out the cost base or reduced cost base of a pre-CGT asset after certain roll-overs

Section 716-855 applies for the purposes of this Division in the same way as that section applies for the purposes of Part 3-90 of the *Income Tax Assessment Act 1997*.

Part 3—CGT event in respect of reduction in tax cost setting amounts for reset cost base assets

Income Tax Assessment Act 1997

7 Section 104-5 (at the end of the table)

Add:

L8 Reduction in tax cost setting amount for reset cost base assets on joining cannot be allocated	Just after entity becomes subsidiary member	<i>no capital gain</i>	amount of reduction that cannot be allocated
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[See section 104-535]

8 At the end of Subdivision 104-L

Add:

104-535 Where reduction in tax cost setting amounts for reset cost base assets cannot be allocated: CGT event L8

- (1) **CGT event L8** happens if:
 - (a) an entity becomes a *subsidiary member of a *consolidated group or a *MEC group; and
 - (b) the *tax cost setting amount for a reset cost base asset of the entity is reduced under subsection 705-40(1) (including in its application in accordance with Subdivisions 705-B to 705-D); and
 - (c) some or all (the **unallocated amount**) of the reduction cannot be allocated as mentioned in subsection 705-40(2).
- (2) The time of the event is just after the entity becomes a *subsidiary member of the group.
- (3) For the head company core purposes mentioned in subsection 701-1(2), the *head company makes a **capital loss** equal to the unallocated amount.

9 Section 110-10 (at the end of the table)

Add:

L8 Reduction in tax cost setting amount for reset cost 104-535
 base assets on joining cannot be allocated

10 Subsection 705-40(2) (at the end of the note)

Add “: see CGT event L8”.

Part 4—Replacement of continuity of ownership test for retention of accelerated depreciation

Income Tax Assessment Act 1997

11 Subsection 701-80(3)

Repeal the subsection, substitute:

Section applies to certain depreciating assets

(3) This section applies if:

- (a) a *depreciating asset to which Division 40 applies becomes that of the *head company because subsection 701-1(1) (the single entity rule) applies when the entity becomes a *subsidiary member of the group; and
- (b) just before the entity became a subsidiary member, subsection 40-10(3) or 40-12(3) of the *Income Tax (Transitional Provisions) Act 1997* applied for the purpose of the entity working out the asset's decline in value under Division 40; and

Note: The effect of those subsections was to preserve an entitlement to accelerated depreciation.

- (c) the *tax cost setting amount that applies in relation to the asset for the purposes of section 701-10 when it becomes an asset of the head company is not more than the entity's *terminating value for the asset.

12 Paragraph 705-45(a)

Repeal the paragraph, substitute:

- (a) an asset of the joining entity is a *depreciating asset to which Division 40 applies; and
- (aa) just before the entity became a subsidiary member, subsection 40-10(3) or 40-12(3) of the *Income Tax (Transitional Provisions) Act 1997* applied for the purposes of the joining entity working out the asset's decline in value under Division 40; and

Note: The effect of those subsections was to preserve an entitlement to accelerated depreciation.

Part 5—Transitional adjustment to over-depreciation provisions where no unfranked or partly franked dividends

Income Tax (Transitional Provisions) Act 1997

13 Subsection 701-30(3)

Repeal the subsection, substitute:

Creation of, or increase in, tax deferral amount

- (3) For the purposes of applying section 705-50 (reduction in tax cost setting amount for over-depreciated assets) of the *Income Tax Assessment Act 1997* in relation to an asset of the transitional entity that becomes that of the head company under subsection 701-1(1) of that Act when the transitional group comes into existence:
- (a) if, before the transitional group came into existence, the transitional entity paid any dividends to which paragraph 705-50(2)(b) of that Act applies—the tax deferral amount in relation to the dividends under subsection 705-50(3) of that Act is increased by the amount worked out under subsection (4) of this section; and
 - (b) if paragraph (a) does not apply—the transitional entity is taken to have paid dividends to which paragraph 705-50(2)(b) of that Act applies and there is taken to be a tax deferral amount in relation to the dividends under subsection 705-50(3) of that Act whose amount is worked out under subsection (4) of this section.

14 Subsection 701-30(4)

Omit “The increase”, substitute “The amount for the purposes of paragraphs (3)(a) and (b)”.

Note: The heading to subsection 701-30(4) is replaced by the heading “*Amount for purposes of paragraphs (3)(a) and (b)*”.

Part 6—Adjustments for errors etc.

Taxation Administration Act 1953

15 Subsection 8W(1C)

Omit “, so far as they were made in a statement made as mentioned in subsection 705-230(2) of that Act”, substitute “that were made in a statement that was made before the Commissioner became aware of the errors”.

16 Subsection 8W(1C) (formula)

Repeal the formula, substitute:

$$\text{Tax on capital gain} \times \left[1 - \frac{\text{Adjusted reset cost base asset setting amount}}{\text{Original reset cost base asset setting amount}} \right]$$

17 Subsection 8W(1C) (definition of *capital gain*)

Repeal the definition.

18 Subsection 8W(1C)

Insert:

tax on capital gain means the product of:

- (a) the *capital gain that the *head company makes as a result of *CGT event L6 happening as mentioned in section 104-525 of the *Income Tax Assessment Act 1997*; and
- (b) the *corporate tax rate in respect of taxable income for the income year in which that CGT event happens.

19 Paragraph 284-80(2)(b) in Schedule 1

Omit “the income tax return mentioned in subsection 705-230(2) of that Act”, substitute “it and it was made before the Commissioner became aware of the errors”.

20 Subsection 284-80(2) in Schedule 1 (formula)

Repeal the formula, substitute:

$$\text{Tax on capital gain} \times \left[1 - \frac{\text{Adjusted reset cost base asset setting amount}}{\text{Original reset cost base asset setting amount}} \right]$$

21 Subsection 284-80(2) in Schedule 1 (definition of *capital gain*)

Repeal the definition.

22 Subsection 284-80(2) in Schedule 1

Insert:

tax on capital gain means the product of:

- (a) the *capital gain that the *head company makes as a result of *CGT event L6 happening as mentioned in section 104-525 of the *Income Tax Assessment Act 1997*; and
- (b) the *corporate tax rate in respect of taxable income for the income year in which that CGT event happens.

23 Subsection 284-150(3) in Schedule 1

Omit “in an income tax return as mentioned in subsection 705-230(2) of the *Income Tax Assessment Act 1997*”, substitute “mentioned in section 705-315 of the *Income Tax Assessment Act 1997* that were made in a statement that was made before the Commissioner became aware of the errors”.

24 Subsection 284-150(3) in Schedule 1 (formula)

Repeal the formula, substitute:

$$\text{Tax on capital gain} \times \left[1 - \frac{\text{Adjusted reset cost base asset setting amount}}{\text{Original reset cost base asset setting amount}} \right]$$

25 Subsection 284-150(3) in Schedule 1 (definition of *capital gain*)

Repeal the definition.

26 Subsection 284-150(3) in Schedule 1

Insert:

tax on capital gain means the product of:

- (a) the *capital gain that the *head company makes as a result of *CGT event L6 happening as mentioned in section 104-525 of the *Income Tax Assessment Act 1997*; and
- (b) the *corporate tax rate in respect of taxable income for the income year in which that CGT event happens.

Part 7—Extension of certain consolidation provisions to cover MEC groups

Income Tax Assessment Act 1997

27 Section 102-30 (table item 7A)

After “consolidated group” (twice occurring), insert “or a MEC group”.

28 Section 104-5 (table row relating to event number L1)

After “consolidated group”, insert “or MEC group”.

29 Subdivision 104-L (heading)

Repeal the heading, substitute:

Subdivision 104-L—Consolidated groups and MEC groups

30 Subsection 104-500(1)

After “*consolidated group”, insert “or a *MEC group”.

31 Paragraphs 104-505(1)(a), 104-510(1)(a), 104-515(1)(a), 104-520(1)(a) and 104-525(1)(a)

After “*consolidated group”, insert “or a *MEC group”.

32 Subsection 104-525(6) (definition of *current asset setting amount*)

After “*consolidated group”, insert “or the *MEC group”.

33 Subsection 104-530(1)

After “*consolidated group”, insert “or a *MEC group”.

34 Section 110-10 (table rows relating to event numbers L1 and L6)

After “consolidated group”, insert “or MEC group”.

Income Tax (Transitional Provisions) Act 1997

Schedule 2 Various amendments relating to consolidated groups

Part 7 Extension of certain consolidation provisions to cover MEC groups

35 Paragraph 701B-1(1)(b)

After “consolidated group”, insert “or the MEC group”.

36 Subsection 719-2(1)

After “than”, insert “Division 701B,”.

37 Subsection 719-160(2)

After “Divisions 701”, insert “, 701A”.

Part 8—Excess franking deficit tax offsets

Income Tax Assessment Act 1997

38 At the end of section 701-30

Add:

Excess franking deficit tax offset for the income year

- (10) For the purposes of applying section 205-70 in relation to an income year after the income year (the *current income year*) to which this section applies, the entity has an excess mentioned in paragraph 205-70(1)(c) (about excess franking deficit tax offsets) for the current income year only if it has such an excess for the non-membership period (if any) ending at the end of the current income year. The amount of the excess for the current income year is the amount of the excess for the non-membership period.

39 At the end of Division 709

Add:

Subdivision 709-C—Treatment of excess franking deficit tax offsets when entity becomes a subsidiary member of a consolidated group

Guide to Subdivision 709-C

709-180 What this Subdivision is about

This Subdivision provides that any excess in the tax offset arising from a franking deficit tax liability of an entity that becomes a subsidiary member of a consolidated group is transferred to the head company of the group.

Table of sections

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709-190 Exit history rule not to treat leaving entity as having a franking deficit tax offset excess

709-185 Joining entity's excess franking deficit tax offsets transferred to head company

- (1) This section operates if:
- (a) an entity (the *joining entity*) becomes a *subsidiary member of a *consolidated group at a time (the *joining time*); and
 - (b) the joining entity is entitled to a *tax offset under section 205-70 for the income year that ends or, if subsection 701-30(3) applies, that is taken by subsection (3) of that section to end, at the joining time; and
 - (c) the offset exceeds (the excess being the *joining entity's excess*) the amount that would have been the joining entity's income tax liability for that income year if it did not have that offset (but had all its other tax offsets).

Transfer of excess to head company

- (2) For the purpose of applying subsection 205-70(1) to the *head company of the *consolidated group for the income year in which the joining time occurs:
- (a) if the head company does not, after taking into account any application of this section to any other entity that became a *subsidiary member of the group before the joining time, have an excess mentioned in paragraph 205-70(1)(c) for the previous income year—the head company is taken to have an excess mentioned in that paragraph for the previous income year equal to the joining entity's excess; and
 - (b) if the head company does have such an excess—that excess is taken to be increased by the amount of the joining entity's excess.

Joining entity prevented from utilising excess in later income years

- (3) For the purpose of applying subsection 205-70(1) to the joining entity for any income year after that in which the joining time occurs, the joining entity's excess is disregarded.

709-190 Exit history rule not to treat leaving entity as having a franking deficit tax offset excess

To avoid doubt, if:

- (a) the *head company of a *consolidated group is entitled to a *tax offset under section 205-70 for an income year; and
- (b) the offset exceeds the amount that would have been the head company's income tax liability for that income year if it did not have that offset (but had all its other tax offsets); and
- (c) an entity ceases to be a *subsidiary member of the group in the income year;

the entity is *not* taken because of section 701-40 (the exit history rule):

- (d) to have the excess mentioned in paragraph (b); or
- (e) to have another excess of that kind because of the circumstances that caused the head company to have the excess.

Part 9—Application

40 Application

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

Schedule 3—Conservation covenants

Income Tax Assessment Act 1997

1 Paragraph 31-5(2)(e)

Repeal the paragraph, substitute:

- (e) the covenant must have been entered into with:
 - (i) a fund, authority or institution that meets the requirements of section 31-10; or
 - (ii) the Commonwealth, a State, a Territory or a *local governing body; or
 - (iii) an authority of the Commonwealth, a State or a Territory.

2 Application

The amendment made by this Schedule applies to conservation covenants entered into on or after 1 July 2002.

Schedule 4—Depreciation of cars for FBT

Fringe Benefits Tax Assessment Act 1986

1 Subsection 11(1) (definition of *B*)

Repeal the definition, substitute:

B is the amount worked out for the person and the car using the formula in subsection (1AA).

2 After subsection 11(1)

Insert:

(1AA) The formula for working out the amount of *B* for the person and the car for subsection (1) is:

$$\frac{150\%}{\text{Effective life of the car}}$$

where:

effective life of the car is the number of years in the period specified as the effective life of the car in a determination made by the Commissioner under section 40-100 of the *Income Tax Assessment Act 1997* and in effect at the most recent time (before the end of the year of tax) the person became the owner of the car.

3 Application

The amendments of the *Fringe Benefits Tax Assessment Act 1986* made by this Schedule apply in relation to a person and a car if the person becomes the owner of the car after 30 June 2002 (whether or not anyone else owned the car before the person becomes the owner of it).

Schedule 5—Endorsement of perpetual bodies as deductible gift recipients

Income Tax Assessment Act 1997

1 Paragraph 30-125(1)(c)

Repeal the paragraph, substitute:

(c) meets the requirements of:

- (i) if the entity is established by an Act and the Act (or another Act) does not provide for the winding up or termination of the entity—subsections (4) and (5); and
- (ii) in any other case—subsections (4), (5) and (6).

2 Paragraph 30-125(2)(d)

Repeal the paragraph, substitute:

(d) the entity meets the requirements of:

- (i) if the entity is established by an Act and the Act (or another Act) does not provide for the winding up or termination of the entity—subsections (4) and (5); and
- (ii) in any other case—subsections (4), (5) and (6).

3 Application of amendments

The amendments made by items 1 and 2 apply in relation to gifts made on or after 1 July 2003.

Schedule 6—Farm management deposits

Income Tax Assessment Act 1936

1 Section 393-25 of Schedule 2G

Insert:

entity has the same meaning as in the *Income Tax Assessment Act 1997*.

2 Section 393-25 of Schedule 2G (definition of *financial institution*)

Repeal the definition, substitute:

financial institution means an entity that:

- (a) is an ADI (authorised deposit-taking institution) for the purposes of the *Banking Act 1959*; or
- (b) carries on in Australia the business of banking, so long as a State or a Territory guarantees the repayment of any deposit taken in the course of that business; or
- (c) carries on in Australia a business that consists of or includes taking money on deposit, so long as a State or a Territory guarantees the repayment of any deposit taken in the course of that business.

Note: An entity can also be a *financial institution* for the purposes of this Subdivision in the limited circumstances described in section 393-52.

3 Application

The amendment of the *Income Tax Assessment Act 1936* made by item 2 of this Schedule applies to deposits and transfers made on or after 1 July 2003.

4 At the end of Subdivision 393-B of Schedule 2G

Add:

393-52 Certain entities taken to be financial institutions for pre-1 July 2003 deposits and transfers*Scope*

- (1) This section applies if the condition in subsection (2) or (3) is satisfied.
- (2) The condition in this subsection is satisfied if:
 - (a) a deposit (the *eligible deposit*) of money was made before 1 July 2003 with an entity (the *non-complying entity*) that was not a financial institution; and
 - (b) if the deposit was made after 17 June 2003:
 - (i) the deposit was made in accordance with an agreement of a particular kind; and
 - (ii) on 17 June 2003, the non-complying entity was offering to enter into agreements of that kind; and
 - (iii) the agreements mentioned in subparagraph (ii) described such a deposit as a farm management deposit; and
 - (c) the deposit was made in good faith.
- (3) The condition in this subsection is satisfied if:
 - (a) the depositor of a farm management deposit made a written request before 1 July 2003 to the financial institution with which the deposit was made to transfer the deposit to an entity (the *non-complying entity*); and
 - (b) the financial institution transferred the deposit to the non-complying entity within a reasonable period after the request; and
 - (c) the non-complying entity was not a financial institution when the deposit was transferred; and
 - (d) the condition in subsection (2) is not satisfied in relation to the deposit (the *eligible deposit*) arising from the transfer to the non-complying entity; and
 - (e) if the request was made after 17 June 2003:
 - (i) the eligible deposit was made in accordance with an agreement of a particular kind; and
 - (ii) on 17 June 2003, the non-complying entity was offering to enter into agreements of that kind; and

- (iii) the agreements mentioned in subparagraph (ii) described such a deposit as a farm management deposit; and
- (f) the request was made in good faith.

Non-complying entity taken to be financial institution

- (4) This Subdivision (other than this section) applies in relation to the eligible deposit as if the non-complying entity were a **financial institution** throughout the period:
 - (a) beginning:
 - (i) if the condition in subsection (2) is satisfied—when the eligible deposit was made; or
 - (ii) if the condition in subsection (3) is satisfied—when the eligible deposit was transferred as mentioned in paragraph (3)(b); and
 - (b) ending:
 - (i) if the depositor makes, before the deadline mentioned in subsection (6), a written request to the non-complying entity to transfer the eligible deposit to a financial institution, and that transfer is made within a reasonable period after the request—at the time the transfer is made; or
 - (ii) if subparagraph (i) does not apply and the eligible deposit was repaid in full before that deadline—at the time the eligible deposit was repaid; or
 - (iii) in any other case—immediately before that deadline.

Deposit taken to be repaid in certain circumstances

- (5) If:
 - (a) the depositor fails, before the deadline mentioned in subsection (6), to make a written request to the non-complying entity to transfer the eligible deposit to a financial institution; or
 - (b) if such a request is made—the non-complying entity fails to transfer the eligible deposit to that financial institution within a reasonable period after the request;the eligible deposit is taken for the purposes of section 393-15 to have been repaid immediately before that deadline (to the extent that it was not actually repaid before that deadline).

Note: This will mean that it is assessable under section 393-15 (as that section applies because of subsection (4)) in the year of income when the eligible deposit is taken to be repaid, rather than in any later year in which it might be actually repaid.

Deadline

- (6) The deadline is:
- (a) if the term of the eligible deposit:
 - (i) is longer than 12 months; and
 - (ii) ends after 1 July 2004;the earlier of:
 - (iii) the day on which the term of the eligible deposit ends;
 - or
 - (iv) 1 July 2007; or
 - (b) in any other case—1 July 2004.

Deposit with non-complying entity and other deposit with a financial institution

- (7) Ignore subsection (4) in deciding, for the purposes of subsection 393-45(1), whether the requirement in subsection 393-35(7) has been contravened.

Schedule 7—Tax offset arising from franking deficit tax liability

Part 1—Amendment of the Income Tax Assessment Act 1997

1 Division 205 (heading)

Repeal the heading, substitute:

Division 205—Franking accounts, franking deficit tax liabilities and the related tax offset

2 Section 205-1

Omit:

- creates a liability to pay franking deficit tax if the account is in deficit at certain times.

substitute:

- creates a liability to pay franking deficit tax if the account is in deficit at certain times; and
- creates a tax offset for that liability.

3 Section 205-5 (heading)

Repeal the heading, substitute:

205-5 Franking accounts, franking deficit tax liabilities and the related tax offset

4 At the end of section 205-5 (before the note)

Add:

- (6) A tax offset is available to an entity that has incurred a liability to pay franking deficit tax.

5 At the end of Division 205

Add:

205-70 Tax offset arising from franking deficit tax liabilities

When does the tax offset arise?

- (1) A *corporate tax entity is entitled to a *tax offset for an income year for which it satisfies the *residency requirement (the **relevant year**) if at least one of the following applies:
 - (a) the entity has incurred a liability to pay *franking deficit tax in the relevant year;
 - (b) the entity incurred such a liability in a previous income year for which it did not satisfy the residency requirement, and that liability has not been taken into account in working out a tax offset under this section;
 - (c) when the entity was last entitled to a tax offset under this section for a previous income year, that offset exceeded the amount that would have been its income tax liability for that year if it did not have that offset (but had all its other tax offsets).

The amount of the tax offset

- (2) Work out the amount of the *tax offset for the relevant year as follows:

Method statement

Step 1. Work out the total amount of *franking deficit tax that is covered by paragraph (1)(a).

Then reduce it by 30% if it exceeds 10% of the total amount of *franking credits that arose in the entity's *franking account in the relevant year.

Step 2. Work out the total amount of *franking deficit tax that is covered by paragraph (1)(b) for a previous income year.

Then reduce it by 30% if it exceeds 10% of the total amount of *franking credits that arose in the entity's *franking account in that previous income year.

- Step 3.* Add up the results of step 2 for all the previous income years covered by paragraph (1)(b).
- Step 4.* Work out the excess that is covered by paragraph (1)(c).
- Step 5.* Add up the results of steps 1, 3 and 4. The result is the *tax offset to which the entity is entitled under this section for the relevant year.

Note: This method statement is modified for certain late balancing entities: see section 205-70 of the *Income Tax (Transitional Provisions) Act 1997*.

Priority of the tax offset

- (3) Apply the *tax offset by subtracting the tax offset from the amount that would have been the entity's income tax liability for the relevant year if it did not have the tax offset (but had all its other tax offsets).

Note: If the tax offset exceeds that amount, the excess will be included in a tax offset for the next income year for which the entity satisfies the residency requirement: see paragraph (1)(c) and step 4 of the method statement.

Example: The following apply to a corporate tax entity that satisfies the residency requirement for an income year:

- the entity's income tax liability for that year would be \$100,000 if its tax offsets were disregarded;
- for that year, the entity has a tax offset of \$60,000 under this section (the **franking deficit offset**) and a tax offset of \$80,000 in respect of overseas tax paid by the entity (the **foreign tax credit**).

Under subsection (3), the foreign tax credit must be applied before the franking deficit offset is applied. As a result, that credit and \$20,000 of the franking deficit offset combine to reduce the entity's income tax liability to nil. The remaining \$40,000 of the franking deficit offset will be included in a franking deficit offset for the next income year for which the entity satisfies the residency requirement.

Residency requirement

- (4) To determine whether the entity satisfies the *residency requirement for the relevant year, section 205-25 has effect as if each of the following were an event specified in a relevant table for the purposes of that section:
- (a) the entity incurring a liability to pay *franking deficit tax in the relevant year;
 - (b) the assessment of the entity's income tax liability for the relevant year that is made on the *assessment day for that year.

6 At the end of subsection 219-50(1)

Add:

Note: The operation of this section is affected by section 219-75 if a tax offset under section 205-70 is applied to work out the company's income tax liability.

7 At the end of subsection 219-55(1)

Add:

Note: The operation of this section is affected by section 219-75 if a tax offset under section 205-70 is, or has been, applied to work out the company's income tax liability.

8 At the end of Division 219

Add:

219-70 Tax offset under section 205-70

- (1) In applying section 205-70 to a *life insurance company, that section has effect as if:
- (a) the reference in paragraph 205-70(1)(c) to the amount that would have been an entity's income tax liability for a previous income year were a reference to the part of such an amount in respect of the company that is attributable to its shareholders; and
 - (b) the reference in subsection 205-70(3) to the amount that would have been an entity's income tax liability for the relevant year were a reference to the part of such an amount in respect of the company that is attributable to its shareholders.

- (2) In working out the part of an amount that is attributable to the company's shareholders for the purposes of this section, regard is to be had to the accounting records of the company.

Example: The following apply to a life insurance company that satisfies the residency requirement for an income year:

- the company has a tax offset of \$60,000 under section 205-70 (the *franking deficit offset*) for that year;
- the company's income tax liability for that year would be \$100,000 if the franking deficit offset were disregarded;
- 20% of the \$100,000 is attributable to the company's shareholders (the *shareholders' part*).

As a result of applying \$20,000 of the franking deficit offset to reduce the shareholders' part to nil, the company's income tax liability becomes \$80,000. The remaining \$40,000 of the offset will be included in a franking deficit tax offset for the next income year for which the company satisfies the residency requirement.

219-75 Working out franking credits and franking debits where a tax offset under section 205-70 is applied

Revised shareholders' ratio—modification of section 219-50

- (1) Subsection (2) applies to a *life insurance company if a *tax offset under section 205-70 is applied to work out the company's income tax liability for an income year.

Note: This means subsection (2) applies if the tax offset is applied to reduce the part of the amount mentioned in paragraph 219-70(1)(b) in relation to the income year.

- (2) For the purposes of working out the amount of a *franking credit or *franking debit for the company in relation to the income year (other than a franking credit covered by item 1 of the table in section 219-15), section 219-50 has effect as if:
- (a) steps 1 and 2 of the method statement in section 219-50 were omitted; and
 - (b) the reference in step 3 of that method statement to the *shareholders' ratio were a reference to the *revised shareholders' ratio* worked out as follows:

<i>Method statement</i>

Step 1. Work out the remainder (if any) of the part of the amount mentioned in paragraph 219-70(1)(b) after the *tax offset is applied to reduce that part.

Note: The part mentioned in paragraph 219-70(1)(b) is the part of an amount of the company's income tax liability for the income year that is attributable to its shareholders.

Step 2. Divide the step 1 result by the company's total income tax liability for the income year (after applying the *tax offset).

The result (which can be nil) is the company's **revised shareholders' ratio** for the income year.

Example: For the 2002-2003 income year X Co (which is a life insurance company) has a tax offset of \$68,000 under section 205-70. Its income tax liability for that year would have been \$400,000 on the assessment day (1 February 2004) if the tax offset were disregarded. Of that liability, \$80,000 is attributable to the shareholders. The step 1 result is therefore \$12,000 (\$80,000 minus \$68,000).

X Co's income tax liability after applying the tax offset is \$332,000 (\$400,000 minus \$68,000). The revised shareholders' ratio is therefore 3/83 (\$12,000 divided by \$332,000).

For that income year, the company paid \$249,000 of PAYG instalments before the assessment day and \$83,000 of income tax one month after that day.

On the assessment day, a franking credit of \$9,000 arises under item 2 of the table in section 219-15 (\$249,000 multiplied by 3/83). On the day the additional amount of tax is paid, another franking credit of \$3,000 arises under item 4 of that table (\$83,000 multiplied by 3/83).

Adjustment resulting from amended assessment—modification of section 219-55

- (3) Subsection (4) applies to a *life insurance company if:
- (a) the assessment of the company's income tax liability for an income year (the **previous assessment**) is amended; and
 - (b) at least one of the following applies:
 - (i) a *tax offset under section 205-70 is applied in making that amended assessment;
 - (ii) a tax offset under section 205-70 was applied in making the previous assessment.
- (4) Section 219-55 has effect in relation to the company as if:

- (a) if subparagraph (3)(b)(i) of this section applies—a reference in that section to the new ratio were a reference to the revised shareholders' ratio that is based on the amended assessment; and
- (b) if subparagraph (3)(b)(ii) of this section applies—the reference in paragraph (1)(b) of that section to the *shareholders' ratio used previously were a reference to the revised shareholders' ratio that is based on the previous assessment.

Example: Continuing the example in subsection (2), the assessment of X Co for the 2002-2003 income year is amended on 31 March 2004. Under the amended assessment, X Co's income tax liability would be \$300,000 if the tax offset were disregarded.

Of that liability, \$60,000 is attributable to the shareholders. That amount is reduced by the tax offset of \$68,000 to nil.

X Co's liability to pay income tax is therefore reduced to \$240,000 (\$300,000 minus \$60,000) and it will receive a refund of \$92,000 (\$332,000 minus \$240,000). As the revised shareholders' ratio has become nil, no franking debit arises from the refund.

The franking credits that previously arose from the payments of PAYG instalments and income tax would not have arisen if the new revised shareholders' ratio had been used. Section 219-55 (as applied by subsection (4) of this section) therefore operates to create an adjustment to cancel those franking credits. The adjustment is a franking debit of \$12,000 that arises on the day of the amendment of the assessment.

9 Application

Subject to the rules on the application of Part 3-6 of the *Income Tax Assessment Act 1997* set out in the *Income Tax (Transitional Provisions) Act 1997*, the amendments made by items 1 to 8 apply to events that occur on or after 1 July 2002.

Part 2—Amendment of the Income Tax (Transitional Provisions) Act 1997

10 At the end of Division 205

Add:

[The next section is section 205-70.]

205-70 Tax offset arising from franking deficit tax liabilities

General application rule

- (1) Section 205-70 of the *Income Tax Assessment Act 1997* has effect in relation to a corporate tax entity's assessments for the 2002-2003 income year and later income years, except as provided in the following subsections.

Late balancing entities—2001-2002 income year

- (2) If a corporate tax entity's 2001-2002 income year ends after 30 June 2002, section 205-70 of the *Income Tax Assessment Act 1997* has effect in relation to the entity's assessment for that income year as if the following method statement had replaced the method statement in that section.

Method statement

Step 1. Work out the total amount of *franking deficit tax that is covered by paragraph (1)(a).

Step 2. Add to the step 1 result the excess that is covered by paragraph (1)(c).

The result is the *tax offset to which the entity is entitled under this section for the relevant year.

Late balancing entities—2002-2003 income year

- (3) If:

- (a) a corporate tax entity's 2002-2003 income year ends after 30 June 2003; and
- (b) the entity makes a valid election under section 205-20 in that income year;

section 205-70 of the *Income Tax Assessment Act 1997* has effect in relation to the entity's assessment for that income year as if the following method statement had replaced the method statement in that section.

Method statement

Step 1. Work out the total amount of *franking deficit tax that is covered by paragraph (1)(a) and was incurred before 30 June 2003.

Step 2. Work out the total amount of *franking deficit tax that is covered by paragraph (1)(a) and was incurred on 30 June 2003.

Then reduce it by 30% if it exceeds 10% of the total amount of *franking credits that arose in the entity's *franking account during the period of 12 months immediately preceding that date.

Step 3. Work out the total amount of *franking deficit tax that is covered by paragraph (1)(a) and was incurred after 30 June 2003.

Then reduce it by 30% if it exceeds 10% of the total amount of *franking credits that arose in the entity's *franking account after that date and before the end of the last day on which the entity incurred a franking deficit tax liability in the relevant year.

Step 4. Work out the total amount of *franking deficit tax that is covered by paragraph (1)(b) and was incurred in the 2001-2002 income year.

Step 5. Work out the excess that is covered by paragraph (1)(c).

Step 6. Add up the results of steps 1, 2, 3, 4 and 5. The result is the *tax offset to which the entity is entitled under this section for the relevant year.

Late balancing entities—later income years

- (4) If:
- (a) an income year of a corporate tax entity ends after 30 June 2004; and
 - (b) the entity makes a valid election under section 205-20 in that income year;

section 205-70 of the *Income Tax Assessment Act 1997* has effect in relation to the entity's assessment for that income year as if the following method statement had replaced the method statement in that section.

Method statement

Step 1. Work out the total amount of *franking deficit tax that is covered by paragraph (1)(a) and was incurred on or before the 30 June in the relevant year.

Then reduce it by 30% if it exceeds 10% of the total amount of *franking credits that arose in the entity's *franking account during the period of 12 months immediately preceding that 30 June.

Step 2. Work out the total amount of *franking deficit tax that is covered by paragraph (1)(a) and was incurred after the 30 June in the relevant year.

Then reduce it by 30% if it exceeds 10% of the total amount of *franking credits that arose in the entity's *franking account after that date and before the end of the last day on which the entity incurred a franking deficit tax liability in the relevant year.

Step 3. Work out the total amount of *franking deficit tax that is covered by paragraph (1)(b) in relation to a previous income year and was incurred on or before the 30 June in that income year.

Then reduce it by 30% if it exceeds 10% of the total amount of *franking credits that arose in the entity's *franking account during the period of 12 months immediately preceding that 30 June.

Step 4. Work out the total amount of *franking deficit tax that is covered by paragraph (1)(b) in relation to a previous income year and was incurred after the 30 June in that income year.

Then reduce it by 30% if it exceeds 10% of the total amount of *franking credits that arose in the entity's *franking account after that date and before the end of the last day on which the entity incurred a franking deficit tax liability in that income year.

Step 5. Add up the results of steps 3 and 4 for all the previous income years covered by paragraph (1)(b).

Step 6. Work out the excess that is covered by paragraph (1)(c).

Step 7. Add up the results of steps 1, 2, 5 and 6. The result is the *tax offset to which the entity is entitled under this section for the relevant year.

Application of the 30% reduction rule

- (5) If a franking credit has been taken into account previously in reducing an amount worked out under a step in the method statement in:
- (a) subsection (3) or (4); or
 - (b) section 205-70 of the *Income Tax Assessment Act 1997*;
- that credit is not to be taken into account again in reducing another amount worked out under a step in such a method statement.

205-75 Working out the tax offset for the first income year

First income year and relevant liabilities

- (1) This section applies to a corporate tax entity in relation to:
- (a) this income year of the entity (the ***first income year***):

- (i) the 2001-2002 income year if subsection 205-70(2) applies to the entity; or
- (ii) the 2002-2003 income year if subsection 205-70(2) does not apply to the entity; and
- (b) amounts of liabilities incurred by the entity (the **relevant liabilities**) that:
 - (i) are covered by paragraph (1)(a) of section 160AQK or of 160AQKAA (as appropriate) of the *Income Tax Assessment Act 1936*; and
 - (ii) have not been applied under that Act to reduce the entity's income tax liabilities for an earlier income year.

Relevant liabilities carried forward to the first income year

- (2) Section 205-70 of the *Income Tax Assessment Act 1997* has effect in relation to the entity as if:
 - (a) so much of the relevant liabilities as were incurred by the entity during the first income year were liabilities to pay franking deficit tax under that Act; and
 - (b) so much of the relevant liabilities as were incurred by the entity before the start of the first income year were the excess mentioned in paragraph (1)(c) of that section.
- (3) Subsection (2) has effect only for the purposes of working out:
 - (a) whether or not the entity is entitled to a tax offset under section 205-70 of the *Income Tax Assessment Act 1997* for the first income year or a later income year; and
 - (b) the amount of that tax offset.

205-80 Application of Subdivision C of Division 5 of the *Income Tax Assessment Act 1936*

- (1) This section applies if Subdivision C of Division 5 of the *Income Tax Assessment Act 1936* would, apart from section 160AOAA of that Act, apply in relation to an entity's assessment for a year of income that ends before 1 July 2002.
- (2) Section 160AOAA of that Act does not prevent:
 - (a) the making of a determination under that Subdivision on or after that date for an offset to reduce the entity's income tax liability for that year of income; and

Schedule 7 Tax offset arising from franking deficit tax liability

Part 2 Amendment of the Income Tax (Transitional Provisions) Act 1997

- (b) the operation of any provision in that Subdivision in relation to that determination.
- (3) However, in working out the amount of that offset, any liabilities to pay franking deficit tax or deficit deferral tax that have been taken into account in working out a tax offset under section 205-70 of the *Income Tax Assessment Act 1997* must be disregarded.

Part 3—Consequential amendments

Income Tax Assessment Act 1936

11 Subsection 160AO(2)

Omit all the words from and including “the amount of Australian tax”, substitute:

the amount of Australian tax that:

(a) before the allowance of that credit or those credits (as the case may be); and

(b) before the application of any tax offset under section 205-70 of the *Income Tax Assessment Act 1997*;

is payable by the person in respect of the person’s taxable income of that year of income.

12 Application

The amendment made by item 11 applies in relation to an entity’s assessments for the first income year (within the meaning of section 205-75 of the *Income Tax (Transitional Provisions) Act 1997*) and later income years.

Income Tax Assessment Act 1997

13 Section 13-1 (after table item headed “foreign tax”)

Insert:

franking deficit tax

liabilities to pay 205-70

14 Section 13-1 (table item headed “imputation”)

Omit “see *dividends*”, substitute “see *dividends* and *franking deficit tax*”.

15 After subparagraph 36-55(1)(b)(ii)

Insert:

and (iii) it did not have any tax offset under section 205-70;

16 Section 67-30

After “got those offsets”, insert “and any tax offset under section 205-70”.

17 Subsection 995-1(1) (paragraph (b) of the definition of residency requirement)

Omit “section 220-205”, substitute “section 205-70 or 220-205”.

18 Application

The amendments made by items 13 to 17 apply in relation to an entity’s assessments for the first income year (within the meaning of section 205-75 of the *Income Tax (Transitional Provisions) Act 1997*) and later income years.

Taxation Administration Act 1953

19 Section 45-340 in Schedule 1 (after paragraph (a) of step 1 of the method statement)

Insert:

(aa) section 205-70 of the <i>Income Tax Assessment Act 1997</i> (for liabilities to pay *franking deficit tax); or

20 Application

The amendment made by item 19 applies in relation to the calculation of an entity’s adjusted tax:

- (a) for a base year that is the first income year (within the meaning of section 205-75 of the *Income Tax (Transitional Provisions) Act 1997*) or a later income year; and
- (b) only for the purposes of a PAYG instalment period that includes, or starts after, the day on which this Act receives the Royal Assent.

21 Section 45-375 in Schedule 1 (after paragraph (a) of step 1 of the method statement)

Insert:

(aa) section 205-70 of the *Income Tax Assessment Act 1997* (for liabilities to pay *franking deficit tax); or

22 Application

The amendment made by item 21 applies in relation to the calculation of an entity's benchmark instalment rate, or benchmark tax, for an income year that is the first income year (within the meaning of section 205-75 of the *Income Tax (Transitional Provisions) Act 1997*) or a later income year.

[*Minister's second reading speech made in—
House of Representatives on 11 September 2003
Senate on 18 September 2003*]

(138/03)
