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Bills Digest
No. 151 2003–04

Tax Laws Amendment (2004 Measures No. 2) Bill 2004

DEPARTMENT OF PARLIAMENTARY SERVICES

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No. 151 2003–04

Tax Laws Amendment (2004 Measures No. 2) Bill 2004

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Economics, Commerce and Industrial Relations Section
7 June 2004

Contents

The following abbreviations and acronyms are used throughout this Bills Digest.

Abbreviation	Definition
ATO	Australian Taxation Office
CGT	capital gains tax
Commissioner	Commissioner of Taxation
COT	continuity of ownership test
CTP	Compulsory Third Party
CUT	Corporate Unit Trust
DGR	deductible gift recipient
ETP	eligible termination payment
FBAAT 1986	*Fringe Benefit Tax Assessment Act 1986*
FBT	fringe benefits tax
FDA	foreign dividend account
FIF	foreign investment fund
GIC	general interest charge
GST	goods and services tax
GST Act	*A New Tax System (Goods and Services Tax) Act 1999*
ITAA 1936	*Income Tax Assessment Act 1936*
ITAA 1997	*Income Tax Assessment Act 1997*
MEC	multiple entry consolidation
NZ	New Zealand
PAYG	pay as you go
PSB	personal services business
PSI	personal services income
SIS	simplified imputation system
TAA 1953	*Taxation Administration Act 1953*
UMP	United Medical Protection Limited

Tax Laws Amendment (2004 Measures No. 2) Bill 2004

Date Introduced: 1 April 2004

House: House of Representatives

Portfolio: Treasury

Commencement: Formal provisions of the Bill commence on Royal Assent. The various measures contained in the Bill have various application dates, which are indicated in the Main Provisions section of this Bills Digest.

Purpose

There are 12 Schedules to the Bill and the main purpose of each schedule is set out below.

- **Schedule 1** to this Bill modifies the operation of the income tax law affecting life insurance companies. In particular, the amendments affect:
  - the basis of working out the ordinary class and complying superannuation class of taxable income or tax losses,
  - the taxation treatment of risk business,
  - the taxation treatment of ordinary investment business,
  - the operation of the virtual pooled superannuation trust, and
  - the operation of the segregated exempt assets.

  There are also a range of technical amendments.

- **Schedule 2** to the Bill provides greater flexibility to and clarifies certain aspects of the consolidation regime and ensures that the regime interacts appropriately with other aspects of the income tax law.

- **Schedule 3** to this Bill amends the ITAA 1997 and the ITAA 1936 to ensure that a limited partnership, formed with a legal personality separate from its partners and taxed as an ordinary partnership under the venture capital regime, is a 'partnership' for income tax purposes.

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- **Schedule 4** to this Bill amends the FBTAA 1986 to allow for continuity of FBT treatment for non-remote housing benefits where administration and payment of FBT is devolved by State or Territory governments to a departmental level.

- **Schedule 5** to this Bill amends the ITAA 1997 to ensure that capital gains tax event K6 is not inadvertently triggered by the disposal of new interests in demerged entities.

- **Schedule 6** to this Bill amends the ITAA 1997 to ensure that all individuals who make UMP support payments will be entitled to an income tax deduction for the amount of their contributions in that income year.

- **Schedule 7** to this Bill amends the GST Act to ensure that the goods and services insurance provisions apply as intended to transactions undertaken by operators of compulsory third party schemes.

- **Schedule 8** to this Bill amends the FBTAA 1986 to provide public ambulance services with the same FBT treatment as is provided to public hospitals. Public ambulance services will be able to access an FBT exemption of up to $17 000 of grossed-up taxable value per employee, and will also be able to access the remote area housing FBT exemption under the same criteria as applies to public hospitals. In addition, the ITAA 1997 will be amended to allow public ambulance services to be endorsed to receive tax deductible gifts.

- **Schedule 9** to this Bill amends the ITAA 1936 to alter the taxation treatment that applies when payments are made from overseas superannuation funds. The amendments give effect to the Government's response to the report by the Senate Select Committee on Superannuation on Taxation of Transfers from Overseas Superannuation Funds.

  The key change will enable a taxpayer who is having their overseas superannuation paid directly to an Australian complying superannuation fund to elect to have part of the payment treated as a taxable contribution in the Australian fund. By doing so the fund, rather than the individual, will pay relevant tax arising on the payment and tax will be paid at the concessional superannuation fund rate rather than at the individual's marginal rate.

- **Schedule 10** to this Bill amends, as part of the implementation of the SIS, Division 207 of the ITAA 1997. This Division deals with the tax effect of receiving a franked distribution. The amendments will include adjustment rules to provide the calculation to adjust an entity's assessable income where a franked distribution flows indirectly to the entity through a trust or partnership and the entity has no entitlement to a tax offset. This Bill will also amend the rules in the trans-Tasman imputation measures that adjust the assessable income of an Australian shareholder in receipt of a supplementary dividend paid by a New Zealand company.

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- **Schedule 11** to this Bill changes the provisions dealing with the carry-forward of excess foreign tax credits to ensure those provisions refer to the correct paragraphs in the general foreign tax credit provisions.

- **Schedule 12** to this Bill amends the alienation of PSI provisions contained in Part 2-42 of the ITAA 1997 to clarify when the Commissioner can make a PSB determination as is consistent with the policy intent.

Background

As there is no central theme to the Bill, the background to the various measures will be discussed under the Main Provisions section.

Main Provisions

Schedule 1 – Life insurance companies – amendments to improve the practical operation of the taxation regime for life insurance companies

The Review of Business Taxation made recommendations for the reform of the taxation treatment of life insurance companies.[1] Legislation to implement these reforms was enacted by the *New Business Tax System (Miscellaneous) Act (No. 2) 2000* which inserted Division 320 to the ITAA 1997.[2] Division 15 of Part III if the ITAA 1936 continues to deal with insurance with non-residents and section 148 deals with reinsurance with non-residents.

The Minister for Revenue and Assistant Treasurer, Senator The Hon. Helen Coonan, on 11 September 2002 announced amendments to the income tax law affecting life insurance companies to overcome technical problems that the industry had raised following the practical application of the new legislation. Senator Coonan said the proposed amendments will take effect from 1 July 2000.[3]

The income of life insurance companies for income tax purposes under Division 320 of the ITAA 1997 falls into three main categories:

- the ordinary class of taxable income that is taxed at the company tax rate, currently 30% - income derived in relation to risk business and ordinary investment business is included in this class,

- the complying superannuation class of taxable income that is taxed at a rate of 15% - income derived in relation to complying superannuation business is included in this class, and

- non-assessable non-exempt income derived in relation to immediate annuity business.

The significant amendments to improve the operation of the taxation regime for insurance companies include the following:

New provisions for working out the income tax, taxable income and tax loss of life insurance companies

Item 33 of **Schedule 1** repeals Subdivisions 320-D and 320-E of the ITAA 1997 and substitutes **proposed new Subdivision 320-D** which sets out the basis and methodology for working out the income tax of a life insurance company. It enables a life insurance company to have taxable incomes and tax losses of the following classes:

- the complying superannuation class, and
- the ordinary class.

Under the **proposed subsection 320-134(1)**, the basic income tax liability for a life insurance company will be the sum of:

- the taxable income relating to the complying superannuation class which is taxed at a rate of 15%, and
- the taxable income relating to the ordinary class which is taxed at the company tax rate.

To enable a life insurance company to calculate its basic income tax liability and the amount of income tax that it has to pay, new Subdivision 320-D:

- allows the company to have taxable income or tax losses for each of these classes (**Schedule 1, Item 33, sections 320-130** and **320-131**), and
- ensures that the taxable income of the complying superannuation class and the ordinary class are worked out separately; and tax losses of one class can only be applied to reduce future income of the same class. (**Schedule 1, Items 33** and **66, section 320-133** and the definition of **'class' in subsection 995-1(1)**)

Reinsurance with non-residents

Section 148 of Division 15 of Part III of the ITAA 1936 deals with reinsurance with non-residents. Prior to the introduction of Division 320, section 148 applied only to the accident and disability business of life insurance companies. The Division 320 provisions unintentionally broadened the scope of section 148.

Item 1 of **Schedule 1** amends section 148 by inserting **proposed subsection 148(10)** to ensure that section 148 applies only to the whole or part of a risk that is covered by a disability policy and relates to a disability benefit.

Reinsurance commissions

Amounts received or recovered by a life insurance company that are a refund, or in the nature of a refund, of a life insurance premium paid under a contract of reinsurance (other than amounts that relate to a risk to which subsection 148(1) of the ITAA 1936 applies) are included in assessable income under paragraph 320-15(1)(c). The Explanatory Memorandum states that reinsurance commissions are intended to be specifically included in assessable income under this paragraph.[4]

However, they could be included in assessable income under section 6-5 as income according to ordinary concepts. To remove this doubt, **Item 116** of **Schedule 1** inserts **proposed paragraph 320-15(ca)**, specifically including all reinsurance commissions (other than reinsurance commissions that relate to a risk to which subsection 148(1) applies) in a life insurance company's assessable income.

Ordinary investment business – amendment to clarify scope of section 320-75 of the ITAA 1997

At present, section 320-75 of the ITAA 1997 allows a deduction for basically the capital component of premiums received in respect of ordinary investment policies. Generally, the deduction is the sum of premiums received in respect of ordinary investment policies reduced by the amount of those premiums that an actuary determines to be attributable to fees and charges. The actuary's determination must have regard to changes in the net current termination value of relevant policies over the income year. The net current termination value of a policy at a particular time is, broadly, the amount that the company would pay to the policyholder if the policy was terminated at that time.

Item 24 of **Schedule 1** repeals section 320-75 and substitutes **proposed new section 320-75.** To clarify that **proposed new section 320-75** can only apply to ordinary investment policies (including funeral policies), **Item 73** of **Schedule 1** inserts a definition of 'ordinary investment policy' into subsection 995-1(1) of the ITAA 1997. According to this proposal, an ordinary investment policy, as defined, is a life insurance policy that is not:

- a virtual pooled superannuation trust life insurance policy,
- an exempt life insurance policy,
- a policy that provides for participating or discretionary benefits, or

- a policy (other than a funeral policy) under which benefits are paid only on the death or disability of a person.

Comparisons of key features of new law and current law[5]

New Law	Current Law
Tax losses of the complying superannuation class can be applied only to reduce future complying superannuation class income. Tax losses of the ordinary class can be applied only to reduce future ordinary class income.	Tax losses of the complying superannuation class can be applied only to reduce future complying superannuation class income. Tax losses of the ordinary class must be applied to reduce both future ordinary class income and future complying superannuation class income.
In relation to risk business: • the provisions in the ITAA 1936 relating to reinsurance with non-residents apply only to accident and disability risk covered by the relevant reinsurance contracts entered into by life insurance companies, • reinsurance commissions are specifically included in assessable income, and • the basis for determining the amount of the decrease in the value of policy liabilities that is included in assessable income is the same as the basis for determining the amount of the increase in the value of policy liabilities that is deductible.	In relation to risk business: • the provisions in the ITAA 1936 relating to reinsurance with non-residents apply to the whole of the risk covered by the relevant reinsurance contracts entered into by life insurance companies, • reinsurance commissions may not be included in assessable income, and • the basis for determining the amount of the decrease in the value of policy liabilities that is included in assessable income may be different to the basis for determining the amount of the increase in the value of policy liabilities that is deductible.

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<table>
<tr><th>New Law</th><th>Current Law</th></tr>
<tr><td>In relation to ordinary investment business:
the deduction for the capital component of ordinary investment policies does not apply to other types of policies,
funeral policies issued by friendly societies are taxed as ordinary investment policies;
the amount of the reduction in exit fees over the term of a life insurance policy is deductible, and
risk rider premiums are included in assessable income.</td><td>In relation to ordinary investment business:
the deduction for the capital component of ordinary investment policies may apply to other types of policies,
funeral policies issued by friendly societies may be taxed as risk policies,
the amount of the reduction in exit fees over the term of a life insurance policy may not be deductible, and
risk rider premiums may not be included in assessable income.</td></tr>
<tr><td>In relation to complying superannuation business:
the deduction for the capital component of premiums received in respect of virtual pooled superannuation trust policies is not reduced by the risk component of participating policies,
liabilities relating to virtual pooled superannuation trust policies and all relevant provisions for income tax can be supported by virtual pooled superannuation trust assets,
life insurance companies must transfer excess assets out of the virtual pooled superannuation trust within 30 days of the later of:
the time that the transfer value of virtual pooled superannuation trust assets is determined, and
the time that the value of the virtual pooled superannuation trust policy liabilities is determined, and
administrative penalties will be</td><td>In relation to complying superannuation business:
the deduction for the capital component of premiums received in respect of virtual pooled superannuation trust policies is reduced by the risk component of participating policies,
liabilities relating to virtual pooled superannuation trust policies and relevant provision for tax in respect of unrealised gains and for unpaid pay as you go instalments can be supported by virtual pooled superannuation trust assets,
life insurance companies must transfer excess assets out of virtual pooled superannuation trust within 30 days of the time that the transfer value of virtual pooled superannuation trust assets is determined, and
no administrative penalties are imposed if a life insurance company does not undertake the required valuations of assets and liabilities, or transfer excess</td></tr>
</table>

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New Law	Current Law
imposed if a life insurance company does not undertake the required valuations of assets and liabilities, or transfer excess assets out of the virtual pooled superannuation trust, within the specified time periods.	assets out of the virtual pooled superannuation trust, within the specified time periods.
In relation to immediate annuity business: • exempt life insurance policies include, among other things: ◦ immediate annuity policies that satisfy certain conditions, and ◦ part of a policy held by a complying superannuation fund or pooled superannuation trust where the relevant part satisfies certain conditions, • liabilities relating to exempt life insurance policies can be supported by segregated exempt assets, • life insurance companies must transfer excess assets out of the segregated exempt assets within 30 days of the later of: ◦ the time that the transfer value of segregated exempt assets is determined, and ◦ the time that the value of the exempt life insurance policy liabilities is determined, and • administrative penalties will be imposed if a life insurance company does not undertake the required valuations of assets and liabilities, or transfer excess assets out of the segregated exempt assets, within the specified time periods.	In relation to immediate annuity business: • exempt life insurance policies include, among other things: ◦ all immediate annuity policies, and ◦ policies held by a complying superannuation fund or pooled superannuation trust only where the whole of the policy satisfies certain conditions, • liabilities relating to exempt life insurance policies and relevant provisions for tax in respect of unrealised gains can be supported by segregated exempt assets, • life insurance companies must transfer excess assets out of the segregated exempt assets within 30 days of the time that the transfer value of segregated exempt assets is determined, and • no administrative penalties are imposed if a life insurance company (does not undertake the required valuations of assets and liabilities, or transfer excess assets out of the segregated exempt assets, within the specified time periods.

Application

The amendments are intended to clarify the operation of the tax regime for life insurance companies as reformed by the implementation of Division 320. Accordingly, most of the amendments apply under Item 126 of Schedule 1 from 1 July 2000, the commencement day for Division 320.[6]

Schedule 2 – Consolidation regime: providing greater flexibility

The measures in **Schedule 2** are intended to:

- provide greater flexibility to the consolidation regime,
- clarify certain aspects of the regime, and
- ensure that the regime interacts appropriately with other aspects of income tax law.

The more significant measures are considered below.

Certain corporate unit trusts and public trading trusts can be treated as head companies of consolidated groups

Certain corporate unit trusts (CUTs) and public trading trusts (PTTs) may make an election to be treated like a head company of a consolidated group under **proposed Subdivision 713-C** to be inserted into the ITAA 1997 by **Item 2** of **Schedule 2**. This will result in the CUT or PTT being treated like a company for income tax and related purposes. It will have consequential effects on other entities including:

(a) the trustees, and

(b) members of the trusts, and

(c) entities the trustees hold membership interests in.

This measure was announced by Senator The Hon. Helen Coonan, the Minister for Revenue and Assistant Treasurer in her Press Release of 27 March 2003.[7]

Summary of other measures to clarify and provide flexibility to the consolidation regime

Schedule 2 to this Bill contains the following other modifications to the consolidation regime:

- multiple entry consolidated (MEC) groups, and interposed head companies,

- cost setting for assets that the head company does not hold under the single entity rule,
- leaving rules for partners and partnerships,
- deferred acquisition payments,
- application of transitional cost setting provisions to MEC groups,
- continuity of ownership test (COT) concession for foreign losses,
- interactions with international tax rules,
- consolidation liability rules,
- calculation of capital gains tax (CGT) cost base assumed CGT event,
- interaction with the Financial Corporations (Transfer of Assets and Liabilities) Act 1993, and
- privatised assets.

Application

Generally, the amendments made by **Schedule 2** apply on or after 1 July 2002.

Schedule 3 – Venture capital partnerships

The law enacting the venture capital regime contained in the *Taxation Laws (Venture Capital) Act 2002* and the *Venture Capital Act 2002* established three new limited partnerships. These are:

- a venture capital limited partnership,
- an Australian venture capital fund of funds, and
- a venture capital management partnership.

A key feature of the regime is that these limited partnerships are regarded as partnerships for income tax purposes, making them eligible for certain venture capital concessions.[8]

However, a limited partnership that is a separate legal entity registered under State, Territory or other law may be treated as a company, and not as a partnership, under the income tax law.

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A new definition of 'partnership' is inserted into the ITAA 1997 by **Item 5** of **Schedule 3,** extending the current definition to include 'limited partnerships'. In turn, **Item 4** of **Schedule 3** inserts a new definition of 'limited partnership' into the ITAA 1997. Pursuant to this definition, 'limited partnerships' include partnerships formed as a separate legal entity solely for the purpose of becoming a venture capital limited partnership, an Australian venture capital fund of funds or a venture capital management partnership and to carry on activities as a body of that kind.

It is envisaged that these amendments will ensure that limited partnerships are eligible to access the venture capital concession.

Application

Item 6 of **Schedule 3** provides that the amendments apply to things done on or after 2 December 2003, the date when the Minister for Revenue and assistant Treasurer announced this measure in Press Release No. C112/03.

Schedule 4 – Fringe benefits tax housing benefits

A State or Territory may devolve the administration and payment of FBT to eligible State or Territory bodies. Where this happens, each nominated State or Territory body is treated as the employer of the relevant employees for the purposes of the FBTAA 1986. At the time when FBT responsibilities are devolved, a requirement could be triggered to reassess the valuation and the character of fringe benefits provided to employees. Section 135X of the FBTAA 1986 allows for continuity of FBT treatment of certain benefits, to avoid the need for reassessment where there has been no material change in the provision of the benefit.

Item 1 of **Schedule 4** to this Bill amends subsection 135X(3) of the FBTAA 1986 to allow for continuity of FBT treatment for non-remote housing benefits where administration and payment of FBT is devolved by State or Territory governments to a departmental level.

Application

Item 2 of **Schedule 4** provides that the amendments made by Schedule 4 apply in respect of the FBT year beginning on 1 April 2001 and in respect of all later FBT years.

Schedule 5 – Capital gains tax event K6 and demergers

The CGT relief for demergers in Division 125 of the ITAA 1997 ensures that the pre-CGT status of membership interests is preserved. That is, the pre-CGT status of any original membership interests in the head entity carries over to new membership interests in the demerged entity. Under a demerger, members of the head entity of a corporate group (a

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'demerger group') acquire new direct ownership interests in one or more subsidiary members of the group (the 'demerged entities').

CGT event K6 can give rise to a capital gain where a pre-CGT interest shields post-CGT assets owned by an entity. However, pursuant to paragraph 104-230(9)(a) of the ITAA 1997, CGT event K6 does not apply to entities that have been continuously listed on a stock exchange for at least five years.

Membership interests in a demerged entity are usually listed on a stock exchange only after the demerger. Those membership interests do not qualify for the exclusion from CGT event K6 until the demerged entity has been listed on a stock exchange for at least five years. That is, even when the original membership interests in the head entity have been continuously listed on a stock exchange for at least five years, CGT event K6 may apply. As a result, the pre-CGT status of membership interests in the demerged entity is not preserved.

Item 1 of **Schedule 5** to the Bill inserts **proposed subsections 104-230 (9A)** and **(9B)** to the ITAA 1997 to ensure that CGT event K6 is not inadvertently triggered by the disposal of new interests in demerged entities. The exclusion from CGT event K6 will apply to membership interests in a demerged entity where the combined period that the head entity and the demerged entity have been listed on a stock exchange is five years or more. This measure was announced by the Minister for Revenue and Assistant Treasurer in Press Release No. C097/03 of 16 October 2003.

Application

Item 2 of **Schedule 5** provides that the amendment applies to shares or units acquired under a demerger on or after 1 July 2002

Schedule 6 – Deductions for United Medical Protection support payments

The *Medical Indemnity Act 2002* introduced a scheme to address the unfunded Incurred But Not Reported (IBNR) liabilities of medical defence organisations.[9] The Medical Indemnity *(IBNR Indemnity) Contribution Act 2002* introduced a contribution scheme which imposes a liability on doctors to fund the scheme.[10] The IBNR contribution scheme is one of several components of the Australian Government's medical indemnity package, announced on 23 October 2002.

The *Medical Indemnity Amendment Act 2004* and the *Medical Indemnity (IBNR Indemnity) Contribution Amendment Act 2004* put in place three key changes to the Federal Government's medical indemnity arrangements announced on 17 December 2003.[11] These Acts:

- changed the IBNR levy payment arrangements,

- introduced a single Billing arrangement for doctors, and
- put in place revised arrangements for the Premium Support Scheme.

In particular these Acts changed:

- the name of 'IBNR levy' to 'UMP support payments',
- the method of calculating the amount of the UMP support payments, and
- the method of payment and collection and put in place new exemptions.

Item 2 of **Schedule 6** inserts **proposed section 25-105** to allow a specific deduction to individuals who are required to pay UMP support payments. This deduction will only apply to those taxpayers who are not otherwise entitled to a deduction for their contribution.

Application

Item 4 of **Schedule 6** provides that the amendments apply to amounts paid on or after 1 July 2003.

Schedule 7 – Compulsory third party insurance

Operators of compulsory third party schemes have adjustments under Division 79 of the GST Act which enable the net GST on the schemes to reflect correctly their margins after settlements of claims and other payments. In addition, supplies under the schemes are taken into account.

The normal application of Division 78 to some insurance policy payments and supplies under the schemes is modified under Subdivision 79-A. That Division is also extended so that it applies in a modified form to payments and supplies connected with, but not under, insurance policies under Subdivision 79-B.

For other settlements and payments, provisions similar to Division 78, Subdivision 79-C will apply. Certain adjustments are worked out using an 'applicable average input tax credit fraction' under Subdivision 79-D.

Division 80 deals with use of settlement sharing arrangements by the operators of compulsory third party schemes.

However, it has been found that some of the new and modified provisions do not operate as intended and in consequence some operators of Compulsory Third Party (CTP) schemes have been unable to apply the law to some transactions.

Schedule 7 of the Bill will amend several GST insurance provisions to ensure that they apply as intended to transactions undertaken by operators of CTP schemes.

The following table sets out the comparison between the proposed law and the current law.

Comparisons of key features of new law and current law[12]

New law	Current law
A contributing operator's payment received by a managing operator pursuant to a *settlement sharing arrangement*, is not treated as a recovery made by the managing operator under the general insurance provisions.	A contributing operator's payment received by a managing operator pursuant to a *settlement sharing arrangement* may also be treated as a recovery made by the managing operator under the general insurance provisions, resulting in more than one increasing adjustment for the operator.
Where an operator satisfies the *premium selection test*, and claims a decreasing adjustment on settlement of a claim under the insurance policy on the basis that the entity that acquired the policy was not entitled to an input tax credit for the premium, the operator has an increasing adjustment if it later *became or becomes* aware that the entity has such an entitlement.	Where an operator satisfies the *premium selection test*, and claims a decreasing adjustment on settlement of a claim under the insurance policy on the basis that the entity that acquired the policy was not entitled to an input tax credit for the premium, the operator has an increasing adjustment if it later *becomes* aware that the entity has such an entitlement.
An operator that makes a *sole operator election* will make a single election to apply the *average input tax credit fraction* in the calculation of all of its decreasing adjustments arising from settlements of claims under insurance policies.	An operator that makes a *sole operator election* may need to make a separate election to apply the *average input tax credit fraction* in the calculation of decreasing adjustments for each settlement it makes of a claim under an insurance policy.
A payment or supply made by an operator in connection with, but not under, a CTP insurance policy that commenced before 1 July 2003, can be treated as a *CTP hybrid payment or supply* made under the relevant CTP insurance policy.	A payment or supply made by an operator in connection with, but not under a CTP insurance policy that commenced before 1 July 2003, may in some circumstances, be treated as a compensation payment or supply.

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New law	**Current law**
An operator that charges a CTP premium, that is not consideration for a taxable supply made by the operator, is not entitled to a decreasing adjustment for any *CTP compensation or ancillary payment or supply* it makes under the CTP scheme.	An operator that charges a CTP premium, that is not consideration for a taxable supply made by the operator, may be entitled to a decreasing adjustment for any *CTP compensation or ancillary payment or supply* it makes under the scheme.
A payment or supply an operator receives in settlement of a claim it makes as an insured under an insurance policy it holds in respect of a *CTP compensation or ancillary payment or supply* is not treated as a general recovery under the CTP scheme.	A payment or supply an operator receives in settlement of a claim it makes as an insured under an insurance policy it holds in respect of a *CTP compensation or ancillary payment or supply* is treated as a general recovery under the CTP scheme.
Where an operator is exercising its rights to recover from another entity in respect of a *CTP compensation or ancillary payment or supply* it has made, and it receives a payment or supply made in compliance with a judgement or order of a court, the payment or supply is treated as made in settlement of the operator's claim.	Where an operator is exercising its rights to recover from another entity in respect of a *CTP compensation or ancillary payment or supply* it has made, and it receives a payment or supply made in compliance with a judgement or order of a court, the payment or supply is not treated as settlement of the operator's claim.
An operator that has made an election to apply the *average input tax credit fraction*, in the calculation of any decreasing adjustment arising from payments or supplies it has made in settlement of claims made under CTP insurance policies, will use the fraction relevant to the financial year in which the incident occurred.	An operator that has made an election to apply the *average input tax credit fraction*, in the calculation of any decreasing adjustments arising from payments or supplies it has made in settlement of claims made under CTP insurance policies, cannot determine the relevant fraction that applies in the calculation.
Under any *settlement sharing arrangement*, the operators are parties to the arrangement because the *person(s)* involved in the incident was, or was not, covered by an insurance policy.	Under various *settlement sharing arrangements*, the operators are parties to the arrangement depending upon whether the *driver*, or in other cases the *owner or driver*, involved in the incident was, or was not, covered by an insurance policy.

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Application

Item 14 of **Schedule 7** provides that the amendments apply, and are taken to have applied, in relation to net amounts for tax periods starting on or after 1 July 2000, the date of commencement of the GST.

Schedule 8 – FBT tax concessions for public ambulance services

On 20 January 2004, the Treasurer announced that the Government will amend the FBTAA 1986 to ensure that employees of public ambulance services are afforded the same fringe benefits tax exemption as employees of public hospitals.[13]

In the past, some public ambulance services had been accessing an FBT exemption for public benevolent institutions. Fringe benefits provided to an employee of a public benevolent institution are exempt from FBT, subject to a $30 000 cap.

Public benevolent institutions can also be endorsed to receive tax deductible gifts. However, a decision handed down by the Full Federal Court in 2003 indicates that public ambulance services controlled by State or Territory governments are not public benevolent institutions.[14] As such, these bodies cannot access the FBT exemption available to public benevolent institutions or be endorsed to receive tax deductible gifts as a public benevolent institution.

In light of this, the Treasurer announced that the Government will legislate to allow employees of public ambulance services to access a $17 000 capped fringe benefits tax exemption, consistent with that available to employees of public hospitals. As public hospitals are also given deductible gift recipient status, the Government will also legislate to provide this to public ambulance services.

$17 000 capped fringe benefits tax exemption

Section 57A of the FBTAA 1986 allows certain types of employers to access an FBT exemption. Section 5B of the FBTAA 1986 sets out the method for calculating the fringe benefits taxable amount, including the exempt amount which is capped at:

- $17 000 grossed-up taxable value per employee for public hospitals, and
- $30 000 grossed-up taxable value per employee for public benevolent institutions (that are not public hospitals).

The amendments proposed by **Items 1** to **5** of **Schedule 8** will provide that where:

- the employer provides public ambulance services or services that support those services, and

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- the employee is predominantly involved in connection with the provision of those services,

fringe benefits provided to an employee are FBT exempt, subject to a cap of $17 000 grossed-up taxable value per employee.

Exemption for remote area housing fringe benefits

Housing fringe benefits are FBT exempt where provided in a remote area under section 58ZC of the FBTAA 1986. A remote area (which is not an eligible urban area as defined in section 140 of the FBTAA 1986) is generally defined as one that is

- at least 100 kilometres from a population centre of 130 000, or more, and
- at least 40 kilometres from a population centre of 14 000, or more.

However, in relation to public hospitals a remote area is defined as one that is

- at least 100 kilometres from a population centre of 130,000 or more.

This definition also applies in certain other circumstances, such as where the employer is a charitable institution.

The amendments in **Items 6** and **7** of **Schedule 8** extend the FBT remote area housing fringe benefit exemption where:

- the employer provides public ambulance services or services that support those services,
- the employee is predominantly involved in connection with the provision of those services, and
- a remote area for this purpose will be one that is at least 100 kilometres from a population centre of 130,000.

Deductible gift recipient status

Division 30 of the ITAA 1997 allows taxpayers to claim income tax deductions for certain gifts to deductible gift recipients (DGRs). To be a DGR, a fund, authority or institution must fall within a category of organisations set out in Division 30 (or be mentioned by name under that Division). Section 30-17 includes a requirement for a fund, authority or institution to be endorsed by the Commissioner of Taxation in order to obtain DGR status.

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The amendments proposed by **Items 9** and **10** of **Schedule 8** establish a new category of fund, authority or institution in Division 30, namely:

- public ambulance service, or
- public fund established and maintained for the purpose of providing money for the provision of public ambulance services.

Application

- The amendments to the FBTAA 1986 apply in respect of the FBT year beginning on 1 April 2004 and in respect of all later FBT years (**Item 8** of **Schedule 8**),
- the amendments to the ITAA 1997 apply to gifts made on or after 1 April 2004 (**Item 11** of **Schedule 8**).

Schedule 9 – Tax concessions for overseas superannuation payments

Under current tax law, Australian residents are taxed on their worldwide earnings. Accordingly, where a superannuation benefit is paid from an overseas fund, a tax liability may arise in respect of an amount which reflects the earnings on the overseas superannuation while the individual was an Australian resident.

If the payment is made within six months of the individual becoming an Australian resident the payment is tax free (by virtue of being considered an exempt non-resident foreign termination payment).

If the payment is made outside the six month period, then the assessable amount is determined in accordance with a formula specified in section 27CAA of the ITAA 1936. Under this formula the assessable amount generally reflects the investment earnings on the overseas superannuation benefit between the time the individual became an Australian resident and the time the payment took place.

The assessable amount under current law has been included in the assessable income of the individual taxpayer in the year the payment took place and has been taxed at the taxpayer's marginal rate. Since any amount paid directly to an Australian fund is subject to the normal preservation requirements of Australian law (i.e. it will not normally be accessible until retirement after age 55), these amounts have not been available to the taxpayer to pay the related taxation liability. This has caused hardship to a number of taxpayers.

The Senate Select Committee on Superannuation reported on this issue in a report titled Taxation of Transfers from Superannuation Funds.[15] The main recommendation (Recommendation 2) in this report was that the growth in an entitlement that is transferred to an Australian complying superannuation fund should be treated as a taxable contribution. That is, the increase in the value of the entitlement, while an individual has been a resident, is to be taxed at a rate of 15%. This would ensure that the amount is taxed the same as if the accumulated entitlement had been transferred into the Australian fund when the individual became a resident, and the subsequent growth was taxed as income of the fund.

The Minister for Revenue and Assistant Treasurer, Senator The Hon. Helen Coonan, announced on 30 September 2003 changes to the taxation of payments from overseas superannuation funds as the Government's response.[16] The measures in **Schedule 9** of the Bill amend the ITAA 1936 to give effect to the following key changes:

- **Item 2** of **Schedule 9** will repeal existing section 27CAA and replace it with **proposed new section 27CAA**,
- An individual who is having overseas superannuation paid directly to an Australian complying superannuation fund may elect to have part of the payment treated as a taxable contribution by the complying superannuation fund under **proposed subsection 27CAA(3)**,
- If an individual makes such an election, then the amount that would otherwise be included in their assessable income and taxed at their marginal tax rate will be reduced under **proposed subsection 27AAC(4)** by the amount covered by the election under **proposed subsection 27AAC(3)**,
- **Item 4** of **Schedule 9** inserts paragraph 274(10(d) to the ITAA 1936 to make so much of the amount as is specified in an election under **proposed subsection 27CAA(3)** as a taxable contribution of the complying superannuation fund. By doing so the fund, rather than the individual, will pay relevant tax on the payment and tax will be paid at the concessional superannuation fund rate of 15% rather than at the individual's marginal rate. This will overcome the difficulties experienced by individuals faced with a tax liability without recourse to funds to pay the liability due to the benefits being required to be preserved in the Australian fund until retirement,
- The Foreign Investment Fund (FIF) rules will also be amended to prevent double taxation where an amount that has been taxed under the FIF rules is also treated as a taxable contribution in an Australian fund (when the amount is paid to the Australian fund) under amendments proposed by **items 5** and **6** of **Schedule 9**.

Application

Item 7 of **Schedule 9** provides that the amendments made by this Schedule apply to payments made on or after 1 July 2004.

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Schedule 10 – Franked distributions received through certain partnerships and trustees

The simplified imputation system (SIS) arose out of a recommendation of the Review of Business Taxation.[17] In the Treasurer's Press Release No. 58 of 21 September 1999, the Government announced its proposal to implement the SIS which aims to reduce compliance costs incurred by business by providing simpler processes and increased flexibility.[18] Division 207 of Part 3-6 of the ITAA 1997 is part of the core SIS rules introduced in the *New Business Tax System (Imputation) Act 2002*.[19]

Schedule 10 to the Bill amends Division 207 of the ITAA 1997, as part of the implementation of the SIS, which deals with the tax effect of receiving a franked distribution. The amendments will:

- include adjustment rules to provide the calculation to adjust an entity's assessable income where a franked distribution flows indirectly to the entity through a trust or partnership and the entity has no entitlement to a tax offset,
- rectify two technical defects that have been identified in Division 207,
- make consequential amendments to other parts of Division 207 and other parts of the SIS,
- update Division 207 so that it takes into account legislation that has been enacted since Division 207 came into operation, and
- improve the readability of the provisions.

The trans-Tasman imputation measures in Division 220 of Part 3-6 of the ITAA 1997 that deal with the effects of receiving a supplementary dividend will also be amended to implement a minor policy change and ensure consistency with Division 207.

The Explanatory Memorandum states at paragraph 10.3 that the anti-avoidance provisions in Division 7AA of Part IIIAA of the ITAA 1936, which are to be included in Division 207, will now be included in a later Bill. These provisions apply to exempt institutions that are entitled to a refund of franking credits under the refundable tax offset rules in Division 67 of the ITAA 1997.

Application

Under **Item 43(2)** of **Schedule 10,** the amendments to Division 207 will generally apply to events that occur on or after 1 July 2002, when the SIS rules commenced.

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Although the changes to Division 207 generally apply retrospectively, taxpayers will not be adversely affected as the changes clarify the operation of Division 207 but they do not change the way the law is currently applied.

Schedule 11 – Technical corrections

Schedule 11 to the Bill contains certain minor amendments to section 160AFE of the ITAA 1936 to ensure that provisions for the carry-forward of excess foreign tax credits operate properly following changes to the foreign tax credit provisions that were made as a result of the Timor Sea Treaty.

Application

Item 5 of **Schedule 5** provides that the amendments to section 160AFE will apply from the date of application of section 160AFE to taxpayers.

Schedule 12 – Personal service business determinations

The personal services income (PSI) provisions in Part 2-42 of the ITAA 1997, which have applied from 1 July 2000, implemented the recommendations of the Ralph Review of Business Taxation. The PSI provisions prevent individuals from reducing their tax by alienating income from their personal services to an associated entity (such as a company, trust or partnership) or claiming inappropriate 'business' deductions that would otherwise not be available if the individual were directly employed. Unless certain key tests contained in the PSI provisions are satisfied, the PSI derived through the entity will be treated as income of the individual, and taxed accordingly. The PSI legislation sets out four objective tests to allow individuals, and individuals operating through interposed entities, to self-assess whether they are carrying on a genuine personal service business (PSB). If taxpayers satisfy this test, they are considered to be carrying on a PSB and the PSI provisions do not apply.

The primary test is the 'results test' which considers whether the income earned is for producing a result, or whether the service provider has to supply the tools of trade or has to rectify any defects. If taxpayers fail the results test, then they can self-assess to be carrying on a PSB provided:

- less than 80% of an individual's PSI comes from the one source (the 80% rule),
- and at least one of the following tests is passed:
  - the employment test,
  - the separate business premises test, or

– the unrelated clients test.

Notwithstanding the above, taxpayers can apply to the Commissioner for a PSB determination under section 87-60 of the ITAA 1997. The effect of the Commissioner granting a PSB determination is that the PSI provisions do not apply to the taxpayer.

The Commissioner may only make a PSB determination where:

- in the absence of any unusual circumstances – the Commissioner is satisfied that the taxpayer could reasonably be expected to meet, or has met, either the results test, employment test, or separate business premises test (the unrelated clients test is not included as it is considered not rigorous enough in normal circumstances), or

- where there are unusual circumstances – the Commissioner is satisfied that, but for those unusual circumstances, the taxpayer would have passed at least one of the four PSB tests.

Schedule 12 to the Bill amends the PSI provisions to clarify when the Commissioner can make a PSB determination as is consistent with the policy intent.

According to the Explanatory Memorandum, the amendments will ensure that:

- the Commissioner may provide a PSB determination in cases where a taxpayer satisfies the unrelated clients test and, but for unusual circumstances, less than 80% of the individual's PSI would come from one source; and

- the Commissioner may not provide a PSB determination to those taxpayers who, but for unusual circumstances, would satisfy the unrelated clients test, but did not satisfy or would not have satisfied, the rule requiring that less than 80% of the individual's PSI is derived from one source.[20]

Application

The amendments in **Part 1** of **Schedule 12** apply from the 2000-01 income year as provided in **item 9**. These amendments will benefit taxpayers.

The amendments in **Part 2** of **Schedule 12** apply to assessments for the income year following the year in which the Bill receives Royal Assent as provided in **item 16.**

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Financial impact of measures in the Bill

The table below sets out the comments in the Explanatory Memorandum to the Bill of the financial impact of the measures.[21]

Financial impact of measure in:	2003-04	2004-05	2005-06	2006-07
Schedule 1- Life insurance companies	Negligible	Negligible	Negligible	Negligible
Schedule 2- Consolidation regime	Revenue cost less than $2 million per annum from 1 July 2002	Revenue cost less than $2 million per annum from 1 July 2002	Revenue cost less than $2 million per annum from 1 July 2002	Revenue cost less than $2 million per annum from 1 July 2002
Schedule 3- Venture capital	Nil	Nil	Nil	Nil
Schedule 4- FBT housing benefits	Nil	Nil	Nil	Nil
Schedule 5- CGT event K6 and demergers	Nil	Nil	Nil	Nil
Schedule 6- Deductions for UMP support payments	Not applicable	$0.8m cost to revenue	$1.6m cost to revenue	$1.5m cost to revenue
Schedule 7- Compulsory Third Party insurance	Nil	Nil	Nil	Nil
Schedule 8- Public ambulance services	$1m cost to revenue	$3.5 cost to revenue	$5m cost to revenue	$5m cost to revenue
Schedule 9-	Not applicable	First year	Negligible long	Negligible long

Financial impact of measure in:	**2003-04**	**2004-05**	**2005-06**	**2006-07**
Overseas superannuation payments		revenue gain of $1.1 million	term impact	term impact
Schedule 10- Simplified imputation system	Note A below	Note A below	Note A below	Note A below
Schedule 11- Technical corrections	Nil	Nil	Nil	Nil
Schedule 12- Personal services business determinations	The revenue impact of the measure is unquantifiable, but is expected to be insignificant.	The revenue impact of the measure is unquantifiable, but is expected to be insignificant	The revenue impact of the measure is unquantifiable, but is expected to be insignificant	The revenue impact of the measure is unquantifiable, but is expected to be insignificant

Note A

- Amendments to Division 207 will have no impact on revenue,
- A reliable estimate of the cost to revenue of the exempting entity rules cannot be made,
- The amendments to the trans-Tasman imputation measures are expected to have a small, positive but unquantifiable impact on revenue.

Endnotes

1 *A Tax System Redesigned* (July 1999); Section 14; pages 489 to 513.

2 Bills Digest 192, 1999-2000 on the New Business Tax System (Miscellaneous) Bill (No. 2) 2000.

3 Senator The Hon. Helen Coonan, Minister for Revenue and Assistant Treasurer, *Taxation of life insurance companies*, press release, 11 September 2002.

4 Explanatory Memorandum to the Bill, paragraph 1.54, p. 33.

5 Explanatory Memorandum to the Bill, after paragraph 1.11, pp. 17 to 19.

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6 Note, however, that several amendments will apply prospectively as they have a potentially adverse impact upon the life insurance companies. Explanatory Memorandum to the Bill, paragraph 1.148, p. 58.

7 Senator The Hon. Helen Coonan, Minister for Revenue and Assistant Treasurer, *Consolidation – Corporate Unit Trusts and Public Trading Trusts*, press release, 27 March 2003.

8 Bills Digest 77, 2002-03 on the Venture Capital Bill 2002.

9 Bills Digest 71, 2002-03 on the Medical Indemnity Bill 2002.

10 Bills Digest 72, 2002-03 on the Medical Indemnity (IBNR) Contribution Bill 2002.

11 Bills Digest 99-100, 2003-04 on the Medical Indemnity Amendment Bill 2004 and the Medical Indemnity (IBNR Indemnity) Contribution Amendment Bill 2004.

12 Explanatory Memorandum to the Bill, after paragraph 7.4, pp. 160 to 161.

13 The Hon. P Costello MP, Treasurer, Fringe benefits tax concessions for public ambulance services, press release, No. 2 of 20 January 2004.

14 *Ambulance Services of New South Wales v Deputy Commissioner of Taxation for the Commonwealth of Australia* [2003] FCAFC 161.

15 Report of the Senate Select Committee on Superannuation titled *Taxation of Transfers from Overseas Superannuation Funds* (July 2002).

16 Senator The Hon. Helen Coonan, Minister for Finance and Assistant Treasurer, *Government announces tax changes for overseas super*, press release, 30 September 2003.

17 *A Tax System Redesigned* (July 1999) – Report of the Review of Business Taxation with Mr John Ralph as Chairman (also referred to as the Ralph Review).

18 The Hon. P Costello MP, Treasurer, *The New Business Tax System*, media release, Canberra, 21 December 1999.

19 Bills Digest 165, 2001-02 on the New Business Tax System Imputation Bill 2002.

20 Explanatory Memorandum to the Bill, paragraph 12.11, p. 215.

21 Explanatory Memorandum to the Bill, 'General outline and financial impact', pp. 3 to 11.

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