



## Tax Laws Amendment (2005 Measures No. 6) Bill 2005

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## Glossary

The Bill	Tax Laws Amendment (2005 Measures No. 6) Bill 2005
The Welfare to Work Act	<i>Family and Community Services Legislation Amendment (Welfare to Work) Act 2005</i>
CCB	Child Care Benefit
<i>Coleambally</i>	<i>Coleambally Irrigation Mutual Co-Operative Ltd v Commissioner of Taxation</i> [2004] FCAFC 250 (7 September 2004)
Commissioner	Commissioner of Taxation
DGR	deductible gift recipient
ITAA 1936	<i>Income Tax Assessment Act 1936</i>
ITAA 1997	<i>Income Tax Assessment Act 1997</i>
MEO	medical expenses offset
TAA 1953	<i>Taxation Administration Act 1953</i>
the Federal Court	Federal Court of Australia

## Tax Laws Amendment (2005 Measures No. 6) Bill 2005

**Date Introduced:** 7 December 2005

**House:** House of Representatives

**Portfolio:** Treasury

**Commencement:** Sections 1-3 as well as Schedules 1, 2, 4 and 5 will commence upon the Tax Laws Amendment (2005 Measures No. 6) Bill 2005 ('Bill') receiving Royal Assent. Schedule 3 of the Bill will commence the later of the following days: the start of the day on which this Act receives the Royal Assent or immediately after the commencement of the Family and Community Services Legislation Amendment (Welfare to Work) Act 2005 ('Welfare to Work Act'). Should the Welfare to Work Act not be enacted, then the provisions in Schedule 3 will not commence.

### Purpose

The Bill implements a range of changes to the taxation legislation. The respective Schedules have different purposes which are discussed under their individual headings.

### Background

Each Schedule of the Bill has a different background which, so far as necessary, will be discussed under each individual heading below.

### Main Provisions

#### Schedule 1 – Consolidation: available fraction for loss utilisation purposes

Loss utilisation can occur in several ways, for example, where an entity joins a group and brings with it losses which can be used by the head company of the group. Australian tax law restricts the way in which such losses may be utilised. There are various ways in which this can be done, one of which is called the 'available fraction' method.

The 'available fraction' is:

... the proportion that the joining entity's market value (at the time of the joining) bears to the value of the whole group (including the joining entity) at that time.<sup>1</sup>

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**Item 1, Schedule 1** repeals subsection 707-320(4) and substitutes a **new subsection 707-320(4)** of the *Income Tax Assessment Act 1997* (ITAA 1997). **New subsection 707-320(4)** provides that:

- (4) For a bundle of losses:
- (a) subject to paragraph (b)-the **available fraction** is worked out to 3 decimal places, rounding up if the fourth decimal place is 5 or more; or
  - (b) if the available fraction worked out under paragraph (a) is 0.0000 and, if it worked out to more decimal places, it would include one or more non-zero digits-the **available fraction** is worked out to the number of decimal places that includes the first or only such digit, rounding up if the next decimal place is 5 or more.

Examples: For 0.000328, the available fraction is 0.0003. For 0.000086, the available fraction is 0.00009.

This amendment will apply from 1 July 2002. This amendment removes an unintended consequence and is beneficial legislation.

## **Schedule 2 – Extension of mutuality principle**

The amendments in Schedule 2 of the Bill are designed to remedy the impact of the *Coleambally Irrigation Mutual Co-operative Ltd v Commissioner of Taxation* [2004] FCAFC 250 (7 September 2004) (*Coleambally*) on certain ‘not-for-profit’ entities. The aim of the amendments is to restore the pre-*Coleambally* situation for affected not-for-profit entities.

In *Coleambally*, the Full Federal Court held that the ‘mutuality principle’ could not be relied upon by non-profit organisations to reduce their assessable income. ‘Not-for-profit’ entities include clubs, professional associations and some friendly societies.<sup>2</sup>

The mutuality principle recognises that:

Amounts are not ‘derived’ for income tax purposes unless they are received from an external source.

The principle is that where a number of people agree to contribute sums to a fund for a common purpose that is created and controlled for their mutual benefit, as in the case of certain insurance funds and clubs and societies, any repayments from that fund to the contributing members are not income as such...<sup>3</sup>

State and Territory legislation governs the definition of a ‘not-for-profit’ entity.<sup>4</sup> In order to be classified as ‘not-for-profit’ an entity’s constitution must prohibit the distribution of surplus funds to members either on a winding up or whilst the entity is operating.<sup>5</sup>

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**Schedule 2, item 3, new section 59-35** provides that income is not assessable or exempt income to an entity if the amount would be a mutual receipt, but for the 'entity's constituent document preventing the entity from making any distribution, whether in money, property or otherwise, to its members.'

**Schedule 2, item 4** provides that the amendments made by the Bill apply to income years commencing on or after 1 July 2000. This is beneficial legislation designed to ensure that the taxation status of not-for-profit entities is not affected by the Federal Court's decision in *Coleambally*.

### **Schedule 3 – Child care tax offset**

**Schedule 3** of the Bill amends subdivision 61-IA of the ITAA 1997 to ensure that eligibility for the Child Care Tax Rebate (CCTR) is preserved, notwithstanding changes to the work/training/study requirements for access to Child Care Benefit (CCB) with the passage of the Family and Community Services Legislation Amendment (Welfare to Work) Bill 2005.<sup>6</sup> The CCTR was announced during the 2004 Election campaign and can be claimed from the 2005-06 tax year onwards.<sup>7</sup>

The passage of that Bill means that from 1 July 2006, a 15 hour per week activity requirement (or 30 hours over 2 weeks) will be required to be met to access more than 25 hours a week CCB.<sup>8</sup>

Under the current tax legislation, eligibility for the CCTR for out-of-pocket child care expenses can only be met where the person otherwise qualifies for CCB for more than 20 hours a week (up to 50 hours a week of CCB). However, the passage of the Family and Community Services Legislation Amendment (Welfare to Work) Bill will change the CCB access rules from 1 July 2006. From 1 July 2006, to access more than 24 hours a week CCB (and up to 50 hours a week) a person will need to be working for 15 hours a week or more. So for child CCTR, there will be persons who met the old CCB rules but not the new CCB rules. So that these persons continue to be able to access the CCTR, this Schedule proposes to amend the tax legislation to allow continued access to the CCTR to those who would have met the old CCB rules.

#### **CCB access rules before the passage of the Family and Community Services Legislation Amendment (Welfare to Work) Bill 2005**

CCB for more than 20 hours a week and up to 50 hours per week is payable to the taxpayer and their partner if they met either of the following conditions:

- the CCB work/training/study test at some time in the week (no minimum hours required)
- had an exemption from meeting the test; or
- subject to a provision where there was no requirement to meet the test.

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Where one of these requirements are met, more than 20 hours of CCB is payable; that is from 21 hours up to 50 hours a week.

### **New test to be eligible for more than 24 hours a week CCB**

The new CCB test to satisfy the child care work/training/study requirement is contained in the Family and Community Services Legislation Amendment (Welfare to Work) Bill 2005. The new test applies in the first week commencing after 1 July 2006.

The new test **requires that for more than 25 hours of CCB (up from 20 hours a week) to be payable and up to 50 hours a week the person will:**

- need to be engaged in a work activity for at least 15 hours a week or more, or
- where there are two parents, both parents each will need to be engaging in work activity for 15 hours a week or more.

### **Comment**

This is beneficial legislation. Notwithstanding the CCB rules are to change from 1 July 2006, in regards to access to more than 24 hours a week CCB and up to 50 hours a week, access to the CCTR will be preserved for those who would have met the old CCB rules.

### **Schedule 4 – Medical expenses offset**

Section 159P of the *Income Tax Assessment Act 1936* (ITAA 1936) provides a tax offset for any net medical expenses incurred over \$1,500 in an income year. The rate of offset is 20 per cent on expenses over the \$1,500 threshold.

Prior to the amendment taxpayers could claim in respect of medical procedures that were cosmetic.

The effect of the amendment is to exclude cosmetic procedures from being eligible for the medical expenses offset. Expense which are cosmetic in nature *and* do not attract a Medicare benefit are classed as ‘ineligible medical expenses.’<sup>9</sup>

**Item 2, Schedule 4** of the Bill inserts **new subsection 159P(4)** into the ITAA 1936:

***ineligible medical expenses*** means payments:

- (a) to a legally qualified medical practitioner, nurse or chemist, or a public or private hospital, in respect of a cosmetic operation that is not a professional service for which a medicare benefit is payable under Part II of the *Health Insurance Act 1973*; or
- (b) to a legally qualified dentist for:

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- (i) dental services; or
- (ii) treatment;

that is solely cosmetic.

**Item 9, Schedule 4** provides that the amendments will apply to assessments for the 2005-06 and later years of income.

Procedures which are not solely cosmetic will be unaffected by the amendment.

### **Schedule 5 – Specific gift recipient**

**Items 1, 3-10, Schedule 5** of the Bill amend ITAA 1997 to update the lists of deductible gift recipients (DGRs) and extend the period for which deductions are allowed for gifts to certain fund that have time-limited DGR status.<sup>10</sup>

The ITAA 1997 is amended to allow make deductible gifts to be made to the following bodies:

- International Specialised Skills Institute Incorporated
- Yachad Accelerated Learning Project Limited
- C E W Bean Foundation
- The Vietnam War Memorial of Victoria Incorporated
- Australian Red Cross Society-US 2005 Hurricane Relief Appeal
- The Salvation Army Hurricane Katrina Relief Appeal; and
- Xanana Vocational Education Trust.

**Item 2, Schedule 5** of the Bill **amends subsection 30-50(2)** of the ITAA 1997 and extends the DGR listing of the City of Onkaparinga Memorial Gardens Association Incorporated to 30 June 2005.

## **Concluding Comments**

The Schedule 1 amendments address an unintended consequence and are beneficial.

The Schedule 2 amendments in respect of restoring the pre-*Coleambally* situation for situation for affected not-for-profit entities are beneficial.

The Schedule 3 amendments in respect of the child care benefit rules are beneficial legislation. Despite the CCB rules changing from 1 July 2006, access to the child care tax rebate will be preserved for those who would have met the old CCB rules.

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The Schedule 4 amendments exclude eligibility to the medical expenses offset for solely cosmetic procedures.

The Schedule 5 amendments update the lists of deductible gift recipients. This is beneficial legislation.

## Endnotes

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- 1 CCH *Australian Master Tax Guide*, CCH Australia Limited, Sydney, 2005, p. 739.
- 2 Explanatory Memorandum, Tax Laws Amendment (2005 Measures No. 6) Bill 2005, para 2.2, p. 11.
- 3 R L Deutsch, M L Friezer, I G Fullerton, M M Gibson, P J Hanley, and T J Snape, *Australian Tax Handbook 2004*, Thomson Legal & Regulatory Limited, 2004 at para 10350, p. 272.
- 4 For example, *Associations Incorporations Act 1981* (VIC).
- 5 *ibid.*, pp.273–4.
- 6 Dale Daniels and Katrina Gunn, Family and Community Services Legislation Amendment (Welfare to Work) Bill 2005, *Bills Digest*, No. 75 2005-06, Parliamentary Library, Canberra, 20 December 2005. <http://www.aph.gov.au/library/pubs/bd/2005-06/06bd075.pdf>
- 7 Greg McIntosh, ‘The New Child Care Tax Rebate’, *Research Note No. 3 2005-06*, Parliamentary Library, Canberra, 5 August 2005. <http://www.aph.gov.au/library/pubs/rn/2005-06/06rn03.pdf>
- 8 Explanatory Memorandum, para 3.2, p. 15.
- 9 Explanatory Memorandum, para 4.17, p. 21.
- 10 Explanatory Memorandum, para 5.1, p. 25.

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