



## New International Tax Arrangements (Foreign-owned Branches and Other Measures) Bill 2005

Thomas John  
Law and Bills Digest Section

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## Glossary

CFC	Controlled foreign companies
CGT	Capital Gains Tax
ESS	Employee share scheme
ITAA 1936	<i>Income Tax Assessment Act 1936</i>
ITAA 1997	<i>Income Tax Assessment Act 1997</i>
NITA Act 2004	<i>New International Tax Arrangements (Participation Exemption and Other Measures) Act 2004</i>
RIS	Regulatory Impact Statement
RITA	Review of International Tax Arrangements

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## **New International Tax Arrangements (Foreign-owned Branches and Other Measures) Bill 2005**

**Date Introduced:** 17 March 2005

**House:** House of Representatives

**Portfolio:** Treasury

**Commencement:** Schedule 1 to 4 of the Bill will commence on Royal Assent. Schedule 5 will commence immediately after item 140 of Schedule 2 of the *New International Tax Arrangements (Participation Exemption and Other Measures) Act 2004* commences.

### **Purpose**

The New International Tax Arrangements (Foreign-owned Branches and Other Measures) Bill 2005 (Bill) will implement a further reform package with respect to Australia's international tax arrangements. In particular, the Bill will make changes to the law relating to:

- dividends received by foreign-owned branches
- controlled foreign companies rules
- Australian branches of foreign entities, and
- cross-border employee shares or rights.

In addition, the Bill will make several technical amendments to the application rule.

### **Background**

On 13 May 2003, the Australian Government announced that it will reform Australia's international tax arrangements. This announcement was the result of an election promise made during the 2001 election campaign and a subsequent extensive review of Australia's international tax law through the Board of Taxation.<sup>1</sup> The Treasurer pointed out that the reforms aim at maintaining:

Australia's status as an attractive place for business and investment, [requiring] the tax system [...] continually to adapt to the increasingly integrated global business environment.<sup>2</sup>

The reform process is comprised of two stages—the review of the international tax arrangements and the implementation stage. The details of both stages have been set out in

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previous digests, but for the convenience of the reader, a summary prepared for [Bills Digest No. 43](#), 'New International Tax Arrangements (Managed Funds and Other Measures) Bill 2004' follows.<sup>3</sup> At pp. 2-4, this Digest stated:

### **Review of International Tax Arrangements**

In [Bills Digest No. 133 of 2003-2004](#), the review of international tax arrangements ('RITA') has been summarised as follows:

- On 2 May 2002, the Treasurer announced details of a RITA, concentrating on at least four principal areas:
  - the dividend imputation system's treatment of foreign source income
  - the foreign source income rules
  - the overall treatment of 'conduit income' and
  - high level aspects of Double Tax Agreement (DTA) policy and processes.
- A consultation paper titled [Review of International Tax Arrangements – Consultation Paper](#) was released by Treasury on 19 September 2002. This paper explored a range of international tax issues that may affect the attractiveness of Australia as a place for business and investment and identified options for consultation to be conducted by the Board of Taxation.
- After extensive public consultation, the Board of Taxation reported to the Treasurer on 28 February 2003. This report was titled [Review of International Tax Arrangements: A Report to the Treasurer](#).
- On 13 May 2003, the Treasurer released the report of the Board of Taxation and announced the [Government's response](#). To enable public consultation to be undertaken on the design of legislation, including addressing integrity issues, the Treasurer announced that the majority of reforms would not commence until 1 July 2004 or later. It was also announced that the reform package would be introduced in tranches.

### **Implementation of changes to the international tax arrangements in stages**

- The [New International Tax Arrangements Act 2004](#), which received Royal Assent on 23 June 2004, was the first tranche of the reform package. The measures in this Act effected changes to:
  - the foreign investment fund rules to reduce compliance costs for affected taxpayers (principally the superannuation and managed fund sectors)

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- the interest withholding tax ('IWT') rules to reduce the cost of obtaining offshore finance for certain unit trusts operating in Australia, and
- controlled foreign company rules to reduce the cost of complying with these rules.

For further details of individual measures included in the New International Tax Arrangements Bill 2003, readers are referred to the [Bills Digest No. 79 of 2003-04](#).

- The [New International Tax Arrangements \(Participation Exemption and Other Measures\) Act 2004](#), which received Royal Assent on 29 June 2004, had the following purposes:
  - Amend the income tax law to ignore capital gains and losses arising from capital gains tax ('CGT') events happening to shares in foreign companies which are held either by Australian companies or by controlled foreign companies in certain, specified circumstances. Broadly, the gains or losses will be disregarded to the extent that the foreign company has an underlying active business.
  - Extend the existing exemptions for branch profits earned in, and non-portfolio dividends paid from, certain listed countries to all countries. It also changes the existing classification of countries as broad-exemption listed countries, limited-exemption listed countries or unlisted countries to either listed or unlisted countries.
  - Amend sections 448 and 450 of the *Income Tax Assessment Act 1936* to reduce the scope of tainted services income. Tainted services income will, in general, no longer include income from services provided by a company to a non-resident associate, or the overseas permanent establishment of an Australian resident.

For further details of individual measures included in the New International Tax Arrangements (Participation Exemption and Other Measures) Bill 2004, readers are referred to the [Bills Digest No. 133 of 2003-04](#). (Footnotes omitted, hyperlinks active)

## Position of significant interest groups

The Australian business community reacted positively to the reform of the international tax arrangements. For example, the Australian Chamber of Commerce and Industry noted that:

The present focus on international taxation arrangements is important because of the inefficient international tax system Australia now maintains. Ways need to be identified through which changes to Australia's treatment of international income flows can mature the Australian economy and increase real incomes. It is also about

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making Australian industry competitive with the rest of the world in attracting foreign capital and skilled migrants.<sup>4</sup>

Similarly, the Chief Executive of the Business Council of Australia, Katie Lahey, was quoted stating that:

To compete effectively and secure future growth, Australia needs tax arrangements that facilitate the flow of global investment to Australia and assists Australian business to expand into international markets.<sup>5</sup>

## Main Provisions

### Schedule 1—Dividends received by foreign-owned branches

Schedule 1 of the Bill proposes to make various amendments to the *Income Tax Assessment Act 1936* (ITAA 1936) and the *Income Tax Assessment Act 1997* (ITAA 1997) with a view to harmonise Australia's international tax law with its tax treaty obligations and to improve tax neutrality between Australian branches and subsidiaries of non-resident entities.<sup>6</sup>

#### Current law

Under section 128 of the ITAA 1936, unfranked dividends paid by an Australian entity to a non-resident recipient are subject to dividend withholding tax and the expenses the recipient incurred in deriving the dividends are not deductible. This applies regardless of whether or not the dividend is attributable to a permanent establishment or branch in Australia. Franked dividends are excluded from such dividend withholding taxes under paragraph 128B(3)(ga) of the ITAA 1936, but are considered non-assessable non-exempt income of the non-resident.

#### Proposed law

Under the proposed law, franked and unfranked dividends will become assessable income of the non-resident if the dividends can be attributed to the non-resident's permanent establishment in Australia.

#### Assessable income

**Item 1** will insert proposed **new paragraph 44(1)(c)** into the ITAA 1936. This new paragraph will have the effect that dividends which are paid to Australian permanent establishments of non-resident entities, which are exempt from withholding tax, are included in the assessable income of the permanent establishment.

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## Withholding tax

**Items 5 and 6** of the Bill will make the necessary changes to section 128B of the ITAA 1936 so that dividends will cease to attract dividend withholding tax. As a result of this amendment, they will also cease to be regarded as non-assessable non-exempt income.

Proposed **new subsection 128B(3E)** will introduce three prerequisites which stipulate that the dividend in question:

- must be paid to a non-resident person who carries on business in Australia at or through a permanent establishment of the person in Australia (proposed **new paragraph 128B(3E)(a)**)
- must be attributable to the permanent establishment (proposed **new paragraph 128B(3E)(b)**), and
- is not paid to the person in the person's capacity as trustee (proposed **new paragraph 128B(3E)(c)**).

Under the second requirement, the payment of the dividend must be attributable to a permanent establishment which must be located in Australia.

## Attributable payments

Whether a payment is attributable to a permanent establishment located in Australia will be a question of fact to be ascertained on a case-by-case basis. The [Explanatory Memorandum](#) notes that '[i]t is intended that the term 'attributable to' will adopt its ordinary meaning.'<sup>7</sup>

## Permanent establishments located in Australia

The proposed amendments will also introduce a new definition for the term 'permanent establishment', stipulating that:

- if the term is defined in a double tax treaty agreed upon between the country in which the foreign company resides and Australia—the term 'permanent establishment' has the same meaning as defined in the treaty, or
- should there be no relevant tax treaty in place—the Australian domestic law definition as set out in section 6(1) of the ITAA 1936 will apply.

To fully implement this definition, further necessary amendments will be made by **items 2 and 6 of Schedule 1** (amending the ITAA 1936—proposed **new subsections 44(7) and 128B(3E)**), and, virtue of **items 8 and 10 of Schedule 1** (amending the ITAA 1997—proposed **new paragraphs 115-280(1)(b) and (ba) and 207-75(2)(c)**).

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## Tax offsets for franked dividends

The payment of franked dividends will have two consequences:

- the assessable income of the dividend paying entity's member contains an amount equal to the franking credit on the distribution, and
- the dividend paying entity's member is entitled to an offset equal to the amount of franking credit on the distribution.<sup>8</sup>

However, apart from fulfilling other conditions and requirements, to claim this offset, the member must be a resident at the time of the distribution.

The proposed changes to the ITAA 1997 will have two results:

First, under **item 10**, proposed **new subsection 207-75(2)** of the ITAA 1997, a non-resident entity will be treated as a resident for the purposes of franked dividends if the paid dividends are attributable to the entity's permanent establishment in Australia. As the result of this change, franking tax offsets are available to these non-resident entities.

Second, under **item 9**, proposed **new subsection 67-25(1DA)** of the ITAA 1997, the rules allowing so called 'excess franking tax offsets' to be converted into tax losses will not be applicable to non-resident entities which, after the introduction of proposed new subsection 207-75(2), would be eligible to claim franking tax offsets as explained above.

'Excess franking tax offsets' may occur, according to subsection 36-55(1) of the ITAA 1997, where corporate tax entities sustain current year losses. As indicated above, under certain circumstances specified in subsection 36-55(2) of the ITAA 1997, these excess franking tax offsets can be converted into an equivalent amount of tax losses. Once made, these tax losses can be carried forward for deduction in a later year of income.<sup>9</sup> This conversion will not be available to non-resident entities.

## Schedule 2—Controlled foreign companies rules

The changes proposed in the Bill will make changes to:

- the 'commencing day' with respect to certain capital gains tax events
- the provisions effecting the calculation of attributable income, and
- the definition of 'adjusted distributable profits'.

### Changes to the 'commencing day' with respect to certain capital gains tax events

For *controlled foreign companies* (CFC), the ITAA 1936 considers as 'commencing day' with respect to certain capital gains tax events the latter of the following days:

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- 30 June 1990, or
- the company became a CFC.<sup>10</sup>

The ITAA 1936 contains several modifications to the Capital Gains Tax (CGT) Rules. Those relating to CFC's are to exclude certain capital gains events which have occurred prior to the commencement date. Under the current regime, CFC's are deemed to have acquired assets owned on the commencement date at the market value on that day. Further, capital losses are not able to be carried forward.

However, the current regime can lead to two problems which may occur where an Australian resident obtains interests in a CFC after the commencement day:

- first, where the CFC makes a capital gain or loss, the cost base for the assessment of the gain or loss is the point in time in which the foreign entity became a CFC, and
- second, where an Australian resident acquires an interest in a foreign company which has been, but ceased to be, a CFC, (note: with the acquisition, the foreign entity becomes a CFC again), taxation of capital gains which accrued during the period in which the entity was not a CFC may occur. The [Explanatory Memorandum](#) notes that this may lead to an onerous due diligence process for the Australian resident acquiring the interests.<sup>11</sup>

The proposed amendment, contained in **item 5 of Schedule 2**, will substitute the current subsection against **proposed new subsection 406(1)** of the ITAA 1936 to overcome these problems by changing the meaning of commencement day with respect to these circumstances. After the changes become effective, the above problems will be rectified because:

- the cost base for the assessment of capital gains or losses will be the time at which the Australian resident obtained the interest in the foreign entity and not the commencing day, and
- any period of foreign control prior to this most recent acquisition of interest will be disregarded. In other words, the effect of the amendment will be that the commencement day is always the most recent acquisition of a controlling interest in the foreign company by an Australian resident.

The changes to provisions effecting the calculation of attributable income

The amendments will also make changes to the rules of attribution of income derived from CFCs to resident attributable taxpayers.

Under the current regime, section 457 of the ITAA 1936 provides that attribution of income to a resident attributable taxpayer will occur where a CFC changes its residency from an unlisted to a listed country.<sup>12</sup> However, where an unlisted country becomes a listed country, then, under subsection 457(3), no amount will be included in the attributable taxpayer's assessable income if the CFC was a resident of that unlisted

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country for three years or more. If the CFC was a resident in the unlisted country for less than three years, s 457 ITAA 1936 will apply, but only to tax gains on the disposal of assets held at the time the CFC's residence changed.<sup>13</sup>

The attributable income for tax-purposes consists of certain forms of income, including, for example, dividends, interest or royalties.<sup>14</sup> However, it was intended that unrealised gains on tainted assets were to be excluded from the operation of section 457 ITAA 1936. Rather, according to the [Explanatory Memorandum](#), this kind of income was to be taxed under sections 384 and 385 of the ITAA 1936.<sup>15</sup> The changes to the listed country regime were implemented as part of the *New International Tax Arrangements (Participation Exemption and Other Measures) Act 2004* (NITA Act 2004). They reduced the number of categories of countries from three to two countries and had a profound effect on the applicability and operation of paragraphs 384(2)(e) and 385(2)(e) ITAA 1936 respectively. After the NITA Act 2004 changes were implemented:

- the applicability of paragraph 384(2)(e) of the ITAA 1936 was significantly limited and the remaining application is now considered to be unjustified, and
- the outcome of the operation of paragraph 385(2)(e) of the ITAA 1936 is that attribution will occur even in situations in which it is now considered to be

**Items 1 to 4** and **9** of the Bill will provide that the exemption available under section 457 of the ITAA 1936 will become available to a CFC resident in a country which became a listed country irrespective of the three year residency requirement. Specifically, **items 2** and **4** of the Bill will repeal paragraphs 384(2)(e) and 385(2)(e) respectively to exclude attribution of this income.

### Changes to the definition of 'adjusted distributable profits'

Currently, Australian taxpayers are required under section 456 of the ITAA 1936 'to include into their assessable income, on an "accruals basis" in the current year, a share of the' attributable income earned by the CFC.<sup>16</sup> The CFC's 'attributable income' is calculated pursuant to the rules set out in sections 382 to 385 of the ITAA 1936 and depends upon, amongst other factors, whether the country in which the CFC is located is a listed or unlisted country. In addition to section 456 of the ITAA 1936, section 457 of the ITAA 1936 ensures attribution of income to the Australian taxpayer where a CFC changes from an unlisted to a listed country or where a country became listed. It has been noted that section 457 of the ITAA 1936 is 'to protect the integrity of the accruals regime', as a 'second-tier provision to preclude the switching of profits from unlisted to listed countries.'<sup>17</sup>

Pursuant to subsection 457(2) of the ITAA 1936, the amount to be included into the taxpayer's assessable income for the income is calculated on the basis of adjusted distributable profits. This provision contains also a definition of this term which was modified as a result of the NITA Act 2004 coming into force.

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However, according to the [Explanatory Memorandum](#), the current definition has the potential to provide that certain income, which has been attributed to the taxpayer by operation of section 456 of the ITAA 1936, is again attributable under section 457 of the ITAA 1936. This issue arose because the definition introduced by the NITA Act 2004 did not contemplate previous statutory accounting periods.

**Items 6 to 8 and 10** of the Bill aim to address this issue by amending the relevant provisions in the ITAA 1936, especially section 457, and the ITAA 1997 respectively.

### Schedule 3—Australian branches of foreign entities

The Australian Government proposes to introduce specific tax concessions to render Australia attractive to multinational operations. Under the current law, tax concessions are available to foreign banks: pursuant to Part IIIB of the ITAA 1936, the Australian tax regime treats Australian branches of foreign banks as separate legal entities.<sup>18</sup> As a result, ‘loans and derivative and foreign exchange transactions are treated as if made between separate companies, that is, as if they were real transactions for tax purposes.’<sup>19</sup> However, branches of foreign financial institutions other than foreign banks and their parent companies are still considered to be one legal person with the effect that the transactions between the companies are not tax effective.<sup>20</sup>

The amendments proposed in Chapter 3 of the Bill will extend the availability of limited separate entity treatment to the branches of foreign financial entities. Changes will be made to three areas:

- Applicability of Part IIIB of the ITAA 1936 to foreign financial entities

**Items 1 and 2 of Schedule 3** of the Bill will make the required modification to Part IIIB of the ITAA 1936. The changes will expand the scope of this Part to encompass foreign financial entities, bringing these entities onto the same level as foreign banks and their branches.

- Applicability of the transfer of loss provisions

Unlike Australian branches of foreign banks, foreign financial entities are unable to transfer losses incurred by unprofitable group members to profitable group members. **Items 7 to 10 of Schedule 3** of the Bill propose amendments to Division 170 of the ITAA 1997 which will permit the tax and net capital loss transfer between the Australian branches of foreign financial entities.

- Modifications to the thin capitalisation rules

Thin capitalisation rules limit the interest deductions available to an Australian entity which is foreign controlled and which has an overseas debt to equity ratio in excess of that allowed. As pointed out in [Bills Digest No. 16 of 2001-2002](#), a ‘major function of the thin capitalisation rules is to prevent multi-national corporations from organising

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their debt to equity ratios for the purpose of claiming the maximum interest deduction in Australia, where interest on borrowings is generally fully deductible.’ The key issue is that without the thin capitalisation rules, multi-national companies would be able to ‘use thin capitalisation to minimise their income taxes in Australia’ by deducting their interest expenses.<sup>21</sup> Accordingly, where the thin capitalisation rules are triggered, that is, where the Australian entity has a high level of debt funding, debt deductions are limited.<sup>22</sup>

Under the current law, Australian branches of foreign banks can elect to be either part of the parent company or may decide to remain part of a ‘single resident company’ for the purpose of determining whether the thin capitalisation rules are triggered. This choice is currently not available to the Australian branches of foreign financial institutions (which are not classified as banks).<sup>23</sup>

The amendments in this Bill will extend the thin capitalisation rules applicable to Australian branches of banks within wholly owned groups to the Australian branches of financial institutions. According to the [Explanatory Memorandum](#), this will:

allow Australian branches of foreign banks, and foreign financial entities, to be grouped with wholly-owned Australian subsidiaries of the foreign parent in determining the thin capitalisation positions of both the branches and the subsidiaries.<sup>24</sup>

The [Explanatory Memorandum](#) contains an explained diagram with further information.<sup>25</sup>

**Item 17 of Schedule 3** will provide the necessary changes to **sections 820-597 and 820-599** ITAA 1997. Section 820-597 will allow head companies of consolidated and Multiple Entry Consolidated groups to choose treating its Australian branches as itself for the purpose of the thin capitalisation rules. Under section 820-599, single entities (that is subsidiaries which cannot consolidate) may make, under certain circumstances, a similar choice. For further details on the choices which can be made by the single entity, the reader may refer to Example 3.1 in the [Explanatory Memorandum](#).<sup>26</sup>

**Items 18 to 26** contain modifications to **section 820-601 to 820-617** ITAA 1997 which are necessary as a result of the changes to choice provisions section 820-597 and 820-599 ITAA 1997.

**Item 27** proposes to repeal current section 820-609 and to substitute it with proposed **new section 820-609**. New section 820-609 will specify the situations and circumstances in which head or single companies are classified as inward or outward investing entity for the purposes of the thin capitalisation rules.

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**Item 30** proposes changes to the means with which head or single companies will calculate its adjusted average equity capital. Proposed **new subsection 820-613(3)** will provide a new method with which to calculate the amount used to increase the average value used to adjust the average equity capital. Proposed **new subsection 820-613(4)** makes modifications to the way assets are risk-weighted.

## Schedule 4—Cross-border employee shares or rights

### Background

Employee Share Schemes (ESS) are based on the idea that employees receive discounted shares or rights in return for their services. The benefit to the employee arises from receiving discounted shares is, under certain circumstances, taxable (with the benefit being the discount which is considered to be part of the employee's assessable income).<sup>27</sup>

Inequitable tax treatment, such as double or nil taxation, can arise where income from ESS is derived by employees in Australia and offshore. The Board of Taxation noted in its Report to the Treasurer that:

The international treatment of such [ESS] is currently uncoordinated. As a result, the plans may become virtually unworkable internationally because of double taxation and compliance problems; or they may become the vehicles of tax planning to reduce tax beyond what is possible purely in the domestic environment.<sup>28</sup>

In addition, the Report of the Board of Taxation noted that these problems have a detrimental impact on Australian business in recruiting skilled workers from overseas.<sup>29</sup>

According to the [Explanatory Memorandum](#), the proposed amendments aim to address the concerns raised by the Board of Taxation. In particular, they aim to:

- reduce the potential for double or nil taxation
- create a more internationally consistent tax treatment of shares acquired under ESSs, and
- assist Australian business to attract more skilled workers.<sup>30</sup>

### Proposed amendments

To avoid double taxation of offshore income derived from ESS, **Schedule 4, items 2 to 4** propose to exempt such income under the currently existing exemptions for offshore employment (sections 23AF and AG of the ITAA 1936). The proposed amendments will expand the relevant definitions specifying which offshore income is exempt to include offshore income derived from ESS. The exemption will be available where all conditions specified in sections 23 AF or AG ITAA 1936 are fulfilled.

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Where these conditions cannot be fulfilled, the taxpayer may still be able to avoid double taxation: **item 24 of Schedule 4** will modify **paragraph 160AEA(1)(q)** ITAA 1936 to ensure that offshore income from ESS is not considered as ‘passive income’ (attracting tax liability) but qualifies as income which allows the taxpayer to claim foreign income tax credits.

Where offshore employees earn offshore income under ESS, but subsequently become Australian employees providing services in Australia, parts of their offshore income relates to services provided in Australia. Still, even though the income was earned in relation to services provided in Australia, under the current rules the income may escape taxation altogether (nil taxation).

The proposed new law will provide that the ESS provisions to employees at the point in which they become Australian employees (**items 5 to 7, 14 to 16**). As a result, the offshore income which is attributable to service provided in Australia will become taxable. Further, where the shares received under the ESS qualify as so-called ‘qualifying shares’, changes to **sections 139B and E (items 7 and 8, 18 and 19)** will allow the Australian taxpayer to elect the possibly more beneficial tax treatment which such shares attract.

Because it may be difficult to ascertain prospectively how much income is earned as Australian taxpayer, the proposed amendments will provide that the taxpayer may make, under certain circumstance, changes to tax assessments for a period of four years beginning at the end of income year in which the relevant period of employment ended (**item 17**). For an example to which this proposed amendment is applied, the reader may refer to Example 4.2 in the [Explanatory Memorandum](#).<sup>31</sup>

**Item 20** proposes the relevant changes to the definitions of employee and employer within the meaning of section 139GA ITAA 1936.

**Item 22** will provides a new definition for the phrase ‘foreign service’, which will a service in a foreign country as the holder of an office or in the capacity of an employee (proposed **new section 139GBA**).

**Items 28 and 29** propose amendments to section 104-160 of the ITAA 1997 with the aim to prevent double taxation of outbound residents which could occur as the result of the interaction between the CGT rules and the ESS. The amendment proposes to disregard CGT event I1 under certain circumstances.

**Items 30, 31 and 33, 34 and 36** propose to clarify which CGT cost base rules apply where ESS shares or rights lack the necessary connection to Australia.<sup>32</sup>

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## Schedule 5—Technical corrections

The amendments proposed in Schedule 5 of the Bill aim at ensuring that Parts 2 and 3 of Schedule 2 of the NITA Act 2004 operate as intended. The reader is referred to the [Bills Digest](#) prepared in relation to this Act.<sup>33</sup>

According to the [Explanatory Memorandum](#), the corrections will rectify a drafting problem in the NITA Act 2004. It states that the ‘original application rule resulted in an ambiguity and did not clearly express the Government’s policy’.<sup>34</sup>

**Item 1 of Schedule 5** proposes to amend sub item 140(2) of Schedule 2 of the NITA Act 2004, substituting the current application rules with the new provision according to which the amendments made by:

- Parts 2 and 3 of Schedule 2 of the NITA Act 2004 will apply to things that happened after 30 June 2004, and
- Items 7, 58 and 59 of Schedule 2 of the NITA Act 2004 will apply to statutory accounting periods starting after 1 July 2004.

## Concluding Comments

The Bill is the next instalment of the Government’s reform package responding to the recommendation made by the Board of Taxation in relation to Australia’s international taxation arrangements.<sup>35</sup>

The Regulatory Impact Statement (RIS), which is attached to the [Explanatory Memorandum](#) to the Bill, notes that at the current stage, the Government is unable to provide data specifying the costs (in form of lost revenue and compliance costs for taxpayers) the tax measures in this Bill may generate.<sup>36</sup>

## Endnotes

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- 1 The Board of Taxation, [Review of International Taxation Arrangements, A Report to the Treasurer](#), Volumes 1 and 2, Canberra, 23 February 2003.
  - 2 P Costello, Treasurer, *Review of International Taxation Arrangements*, [media release](#), 13 May 2003.
  - 3 B Pulle and T John, ‘New International Tax Arrangements (Managed Funds and Other Measures) Bill 2004’, [Bills Digest](#), no. 43, Department of Parliamentary Services, Canberra, 2004-5, pp. 2–4.

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- 4 Australian Chamber of Commerce and Industry, 'Fixing International Taxation is just the start', *ACCI Review No. 94*, Canberra, December 2002.
- 5 K Lahey, cited in Business Council of Australia, *Progress on Tax Competitiveness*, [media release](#), Melbourne, 16 June 2004.
- 6 [Explanatory Memorandum](#) to the Bill, pp. 9–10.
- 7 *ibid.*, p. 13.
- 8 [Explanatory Memorandum](#), p. 15. For a general discussion of franked dividends and examples see R. L. Deutsch, M. L. Friezer, I. G. Fullerton, M. M. Gibson, P. J. Hanley, T. J. Snape, *Australian Tax Handbook*, Thomson ATP, Sydney, 2005, p. 972-3.
- 9 Deutsch, *ibid.*, p. 1028. See also [Explanatory Memorandum](#), *ibid.*, p. 16.
10. Under section 340 of the ITAA 1936, a company is considered to a CFC if it fulfils three sequential tests: first, five or less Australian residents (each with less than 1 percent control interest) have at least 50 percent inclusive control interest (or are entitled to acquire that much); second a single Australian entity has at least 40 percent control interest in the foreign company; third, five or less Australian residents have actual control of the company. See for more detail CCH Australia (eds.), 'Australian Master Tax Guide 2005', CCH Australia, Sydney, 2005, p. 1128-9.
- 11 [Explanatory Memorandum](#), p. 24.
12. Listed countries are those countries which are considered to have a tax system which is similar or closely comparable when compared to the Australian system. Listed countries are specified under section 320 ITAA 1936 and the relevant regulations. They include: Canada, France, Germany, Japan, New Zealand, United Kingdom and the US.
- 13 CCH Australia (eds.), *Australian Master Tax Guide 2005*, CCH Australia, Sydney, 2005, p. 1135.
- 14 For more detailed information see Deutsch, *op. cit.*, p. 1411–12.
- 15 [Explanatory Memorandum](#), p. 25.
- 16 Deutsch, *op. cit.*, p. 1405.
- 17 *ibid.*, p. 1411. See generally also CCH, *Tax Master Guide*, *op. cit.*, p. 1132.
18. This is a modification of the single entity rule.
- 19 Deutsch, *op. cit.*, p. 1423.
20. This is the effect of the single entity rule.
- 21 G. S. Cooper, R. E. Krever, R. J. Vann, C. Rider, *Income Taxation – Commentary and Materials*, Thompson ATP, Pyrmont, 2005, p. 821-2.
- 22 Deutsch, *op. cit.*, p. 1505.
- 23 See generally CCH Australia, *op. cit.*, p. 1242.
- 24 [Explanatory Memorandum](#), p. 35

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- 25 *ibid.*
- 26 *ibid.*
- 27 CCH Australia, *op. cit.*, p. 404. Under some circumstances, the taxpayer can invoke certain concessions in relation to so-called qualifying shares or rights.
- 28 The Board of Taxation, *op. cit.*, Vol. 1, p. 138.
- 29 The Board of Taxation, *op. cit.*, Vol. 1, p. 48.
- 30 [Explanatory Memorandum](#), p. 41.
- 31 *ibid.*, p. 52.
- 32 *ibid.*, pp. 52-3.
- 33 B Pulle, *New International Tax Arrangements (Participation Exemption and Other Measures) Bill 2004*, [Bills Digest](#), No. 133, Department of Parliamentary Services, Canberra, 2004.
- 34 *ibid.*, p. 57.
- 35 Previous instalments included the *New International Tax Arrangements Act 2004*, *New International Tax Arrangements (Participation Exemption and Other Measures) Act 2004* and the *New International Tax Arrangements (Managed Funds and Other Measures) Bill 2004*.
- 36 [Explanatory Memorandum](#), pp. 65–6.

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