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Tax Laws Amendment (2008 Measures No. 6) Bill 2008

Bernard Pulle, Kali Sanyal and Leslie Nielson
Economics Section
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Morag Donaldson
Law and Bills Digest Section
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Tax Laws Amendment (2008 Measures No. 6) Bill 2008

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Links: The relevant links to the Bill, Explanatory Memorandum and second reading speech can be accessed via BillsNet, which is at http://www.aph.gov.au/bills/. When Bills have been passed they can be found at ComLaw, which is at http://www.comlaw.gov.au/.

Purpose

The main purposes of the Bill are:

- to amend the capital gains tax (CGT) and tax consolidation provisions in the *Income Tax Assessment Act 1997* (ITAA 1997) to restrict CGT scrip for scrip rollover to genuine takeovers
- to amend the 'assistance in collection' provisions of the *Taxation Administration Act 1953* (the Administration Act)
- to amend the *Superannuation Guarantee (Administration) Act 1992* (the SGAA 1992) in relation to the late payment offset, and
- to make minor amendments to other tax legislation, including the *Income Tax Assessment Act 1936* (ITAA 1936), as part of the Government's commitment to the care and maintenance of taxation laws.

Background

Schedule 1—CGT roll-overs for corporate restructures under the *Income Tax Assessment Act 1997*

Overview of the purpose of the current legislation on scrip for scrip roll-over

Subdivision 124-M of the ITAA 1997, which deals with capital gains arising from scrip for scrip roll-over, was inserted into the ITAA 1997 by the *New Business Tax System (Capital Gains Tax) Act 1999*. It applies to CGT events happening on or after the day on which that Act received Royal Assent, namely, 10 December 1999.

The Hon. Peter Costello, MP, then Treasurer, in the second reading speech on the New Business Tax System (Capital Gains Tax) Bill 1999 explained that the purpose of the scrip for scrip roll-over was to improve corporate acquisition activity in Australia as follows:

> The changes in relation to rollover relief relate to where there is a takeover and somebody sells their shares because of the takeover and takes shares in the new company. They are essentially exchanging the scrip they have for the scrip of the company making the takeover. They will be able to do that capital gains tax free. That will give enormous benefits to small shareholders throughout Australia and it will free up the market for competitive takeovers and give an improvement in the economic benefits that that will bring.[1]

Subdivision 124-M of the ITAA 1997 allows a taxpayer to choose a roll-over where shares or trust interests owned by the taxpayer and acquired on or after 20 September 1985 are replaced with other shares or trust interests. For example, where a replacement of shares in one company by shares in another company takes place such as in a company takeover, a taxpayer receiving the replacement shares will be entitled to scrip for scrip roll-over under certain circumstances.

The roll-over allows a taxpayer to disregard the capital gains from the original shares, units or other interest. The replacement shares, units or other interests are taken to have been acquired for the cost base of the original interest.

The roll-over is only available if the exchange is a consequence of an arrangement that results in the acquiring entity (or the wholly owned group of which it is a member) becoming the owner of 80 per cent or more of the original company or trust (80 per cent rule). The 80 per cent or more requirement is in subsection 124-780(2) of Subdivision 124-M.

Subsection 124-795(3) provides that the roll-over under Subdivision 124-M is not available if a roll-over is available under Division 122 of the ITAA 1997, dealing with disposal of assets to a wholly-owned subsidiary, or if a roll-over is available under Subdivision 124-G, dealing with company reorganisation.

The reader is referred to the Australian Taxation Office (ATO) fact sheet on Takeovers and mergers, scrip-for-scrip rollover for further details on the operation of the scrip for scrip rollover.[2]

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1. The Hon. Peter Costello MP, Treasurer, 'New Business Tax System (Income Tax Rates) Bill (No. 1) 1999' (and related Bills), Second reading speech, *Debates*, House of Representatives, 21 October 1999, p. 12179, http://parlinfo.aph.gov.au/parlInfo/search/display/display.w3p;query=Id%3A%22chamber%2Fhansardr%2F1999-10-21%2F0091%22, accessed on 27 January 2009.

2. See http://www.ato.gov.au/individuals/content.asp?doc=/Content/36712.htm, accessed on 27 January 2009.

2008 Budget proposal on modifications to the scrip for scrip rollover

Budget Paper No. 2, 2008-09, at page 18 indicated that the Government will modify the scrip for scrip capital gains tax roll-over provisions in relation to corporate restructures.

> The Government will modify the scrip for scrip capital gains tax roll-over provisions to ensure that, for corporate restructures, the acquiring entity's cost base of shares in the target entity reflects the tax costs of the target entity's net assets, with effect from 7.30 pm (AEST) on 13 May 2008. This cost base will also be used in determining the value of the target entity's assets in consolidation if the target entity subsequently joins the acquiring entity's consolidated group. This measure has an ongoing unquantifiable revenue impact.
>
> Under the current provisions, the acquiring entity obtains a market value cost base for the shares it acquires in the target entity. This can result in significant unintended tax benefits arising if, for example, the target entity subsequently joins the acquiring entity's consolidated group. The measure will prevent companies from obtaining unintended tax benefits if they restructure.[3]

On 13 May 2008, the Hon. Chris Bowen, MP, Assistant Treasurer and Minister for Competition Policy and Consumer Affairs, confirmed the changes announced in the Budget, adding that:

> 'This measure will replace the former Government's announced changes to the consolidation rules following certain CGT roll-overs, which caused significant disruption to the operation of Australia's capital markets.'
>
> 'The private sector has been consulted in the development of this measure. The measure will ensure that genuine commercial transactions which have been on hold since the former Government's announcement will now to able to proceed with certainty.'[4]

The former government's proposals for changes to consolidation rules following certain CGT roll-overs were made by the Hon. Peter Dutton, then Minister for Revenue and Assistant Treasurer, in Press Releases of 12 October 2007 and 16 October 2007.[5]

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3. See http://www.budget.gov.au/2008-09/content/bp2/download/bp2.pdf, accessed on 28 January 2009

4. The Hon. Chris Bowen, MP, Assistant Treasurer and Minister for Competition Policy and Consumer Affairs, *Scrip for scrip roll-over provisions and corporate restructures*, media release, 13 May 2008, http://assistant.treasurer.gov.au/DisplayDocs.aspx?doc=pressreleases/2008/033.htm&pageID=003&min=ceb&Year=2008&DocType=0, accessed on 23 January 2009.

5. The Hon. Peter Dutton, MP, then Minister for Revenue and Assistant Treasurer, *Improving the integrity of the tax consolidation regime*, media release, 12 October 2007, http://ministers.treasury.gov.au/DisplayDocs.aspx?doc=pressreleases/2007/124.htm&pageI

The tax minimisation schemes that the amendments seek to prevent

Basically, the tax minimisation practice involves entities exploiting the scrip for scrip roll-over measures and the tax consolidation regime to effectively increase the capital allowance deductions on the assets of an entity after that entity joins a consolidated group or multiple entry consolidated group (MEC group) and reduce capital gains on the disposal of assets of that entity.

The experience of the ATO of the use of such schemes for tax minimisation purposes is described in the Explanatory Memorandum as follows:

> 1.6 Companies are able to gain significant tax benefits by restructuring in a way that attracts the scrip for scrip roll-over rather than the exchange of shares roll-over. These tax benefits are compounded if the entity taken over becomes a member of the acquiring entity's consolidated group.
>
> 1.7 For example, some entities have entered into schemes that involve the insertion of a new holding company above the original entity (known as 'top hat' schemes). The schemes are designed to attract a scrip for scrip roll-over. As a result, the holding company obtains a market value cost base for the shares it acquires in the original entity under the scheme even though there is no significant change in the underlying ownership of the assets.
>
> 1.8 Where the original entity subsequently joins the holding company's consolidated group, the consolidation tax cost setting rules apply to push this market value cost base into the underlying assets of the original entity. This effectively allows the tax costs of the original entity's assets to be reset which, in turn, can lead to an increase in capital allowance deductions and a reduction in capital gains that arise on the disposal of those assets.[6]

Thus, underlying the tax minimisation schemes using the scrip for scrip roll-over measures is the fact that these measures and the consolidation measures result in giving a market value cost base for the underlying assets of the original entity when that entity joins the acquiring company's consolidated group.

Outline of proposed measures to restrict scrip for scrip roll-over to genuine takeovers

The measures proposed in Schedule 1 to the Bill are directed at preventing a market value cost base arising when shares and other interests in a target entity are acquired by an

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D=003&min=pcd&Year=&DocType=0, accessed on 23 January 2009; the Hon P. Dutton, MP, *Tax consolidation rules following CGT rollovers*, media release, 16 October 2007, http://ministers.treasury.gov.au/DisplayDocs.aspx?doc=pressreleases/2007/127.htm&pageID=003&min=pcd&Year=&DocType=0, accessed on 23 January 2009.

6. Explanatory Memorandum, p. 8.

acquiring entity following a scrip for scrip roll-over under an arrangement which is a restructure.

A summary of the proposed measures is set out below:

> 1.9 The scrip for scrip CGT roll-over provisions will be modified to prevent a market value cost base from arising for any qualifying interests acquired by the acquiring entity under an arrangement that is taken to be a restructure.
>
> 1.10 An arrangement will be taken to be a restructure if, broadly, just after the arrangement was completed (the completion time) the market value of the replacement interests issued by the acquiring entity under the arrangement in exchange for qualifying interests in the original entity is more than 80 per cent of the market value of all the shares (including options, rights and similar interests to acquire shares) issued by the replacement entity.
>
> 1.11 If an arrangement that qualifies for scrip for scrip roll-over is taken to be a restructure, then the cost base for the qualifying interests that the acquiring entity acquires in the original entity will reflect the cost bases of the underlying net assets of the original entity (rather than the market value of the original entity).
>
> 1.12 In addition, if the original entity becomes a member of a consolidated group or multiple entry consolidated group (MEC group) under the arrangement, then the head company of the group can elect to retain the tax costs of the original entity's assets.[7]

Press commentary on proposed measures

The following press commentary appears to suggest that genuine scrip takeovers are likely to re-emerge and that tax minimisation by internal restructure be prevented by the measures in **Schedule 1**.

In December 2008, the *Australian Financial Review* reported comments from Ernst & Young and PricewaterhouseCoopers on the proposed changes:

> 'Scrip takeovers are likely to re-emerge, particularly in the current environment; where obtaining debt finance for acquisitions can be very difficult,' Ernst & Young partner Don Green said.
>
> 'Existing companies, seeing an attractive target company, will be able to undertake scrip takeovers and will know the tax implications with certainty, rather than relying on government announcements without legislation.'

and:

7. ibid., pp. 8–9.

> PricewaterhouseCoopers tax partner Mike Davidson said: 'They have gone back to the underlying theme of only trying to target a certain type of transaction which is really just an internal restructure, which is quite good.'
>
> However, he said the legislation stated the change would apply to listed companies for a takeover 'completed' after May 13, but Mr Bowen had previously announced it would apply to arrangements 'entered into' after that date.
>
> 'So people could be doing deals thinking we're safe,' Mr Davidson said, 'but all of a sudden we're caught by these provisions.'[8]

The *Australian Financial Review* also published comments from KPMG following the announcement of the Budget changes in May 2008:

> KPMG mergers and acquisitions tax partner Peter Poulos said the policy was designed to stop companies restructuring specifically to limit CGT on any subsequent sale of assets.
>
> He said that the crucial aspect of the measure announced in the budget was that it did not apply in instances where there was a change in ownership.
>
> 'They have designed the law in such a way so that internal transactions don't step up but genuine scrip-for-scrip deals like Westpac and St George or BHP Billiton and Rio Tinto won't be affected,' Mr Poulos said.[9]

Financial impact

The Explanatory Memorandum states that the financial impact of the measures in **Schedule 1** is 'unquantifiable'.[10]

Schedule 2—Mutual assistance in collection provisions of the *Taxation Administration Act 1953*

The amendment of the mutual assistance in collection provisions of the Administration Act has been proposed in **Schedule 2**. The proposed changes aim to bring a degree of

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8. J. Kehoe, 'Consolidation fix favours scrip bids', *Australian Financial Review*, 8 December 2008, p. 6, http://parlinfo.aph.gov.au/parlInfo/download/media/pressclp/O2BS6/upload_binary/o2bs60.pdf, accessed on 23 January 2009.

9. M. Dunkley & J. Kehoe, 'Scrip and restructuring schemes doomed', *Australian Financial Review*¸ 15 May 2008, p. 14, http://parlinfo.aph.gov.au/parlInfo/download/media/pressclp/9SFQ6/upload_binary/9sfq62.pdf, accessed on 23 January 2009.

10. Explanatory Memorandum, p. 3.

coherence among counterparts of the Australian Taxation Office (ATO) in partner countries.

The current assistance in collection provisions were enacted by the *International Tax Agreements Amendment Act (No. 1) 2006* to enable the Commissioner to meet Australia's existing and future treaty obligations for mutual assistance in collection of tax debts. To be more precise, these provisions authorise the Commissioner to take action to collect or to conserve tax debts owed in another country where the debtor is resident in Australia or has assets in Australia.

Two issues are significant. The ***first*** one is when a foreign tax debt is deemed as 'never to have been payable' when the debt is reduced under subsection 263-35(6) of the Administration Act. The Commissioner may encounter difficulty in instituting proceedings to commence or finalise the debt when a debtor has made a part payment in a foreign country where the debt has been reduced as a consequence of an amendment to the debtor's liability. The ***second*** issue is the types of payments that the Commissioner is able to make to the foreign country. Under the current law only the principal amount, and any general interest charge (GIC) referable to that amount, has been collected by the Commissioner and paid to the foreign country. However, the amendments in **Schedule 2** address the ambiguity in this area, and will allow the Commissioner to pay to other countries any other amounts that are needed to be paid.

Financial impact

According to the Explanatory Memorandum, the financial impact of the measures in **Schedule 2** is 'nil'.[11]

Schedule 3—Late payment offset for superannuation guarantee contributions

The Superannuation Guarantee (SG) scheme, administered by the Australian Taxation Office (ATO), requires employers to provide a prescribed minimum level of superannuation support in each quarter for their employees. From 1 July 2008, this prescribed minimum level is 9 per cent of an employee's ordinary time earnings. If the employer fails to make these payments, the amount not paid is known as a 'SG shortfall'.

About SG obligations

Employer's payments of their SG obligations are required to be made within a 28 day period after the end of the relevant quarter. This day is the 'due date'.

Employers are required to self-assess their liability to the pay the shortfall and any associated penalties. Under existing section 33 of the SGAA 1992, they must also lodge an SG Statement with the ATO. Employers who fail to self assess their SG liability may

11. Explanatory Memorandum, p. 4.

be issued with a default assessment by the ATO under existing section 36. The Commissioner for Taxation may amend a previous assessment under existing section 37 of the SGAA 1992. These are the formal assessments of an employer's liabilities under the SG regime referred to in the proposed amendments to the SGAA 1992.

These assessments take effect on the later of:

- the day the statement was lodged, or
- the day the SG statement was required to be lodged for the quarter.

Under existing section 33 of the SGAA 1992, an employer who has an SG shortfall for a quarter must lodge an SG statement on or before the 28th day of the second month after the end of the quarter, that is, on or before:

- for a quarter beginning on 1 January — 28 May in the next quarter
- for a quarter beginning on 1 April — 28 August in the next quarter
- for a quarter beginning on 1 July — 28 November in the next quarter
- for a quarter beginning on 1 October — 28 February in the next quarter.

Payment of SG charge

The total of the payments to be made is known as the 'SG charge' (see below for further explanation). The employer must pay the SG charge, if any, to the Australian Taxation Office (ATO) at any point in time after the due date.

The SG charge is made up of the amount of the shortfall plus an interest and an administration component. The shortfall and interest component of the charge are distributed by the ATO for the benefit of those employees in respect of whom the charge was paid.

Offsetting SG obligations with a late payment

Under existing section 23A of the SGAA 1992, employers who make contributions to a superannuation fund *after* the due date, that is after the 28th day following the end of the relevant quarter, can offset the late payment against the components of the SG charge liability that relate to the relevant employee's entitlements. To benefit from the offsetting rule, the employer must elect to make a late contribution to employee's superannuation funds either:

- in a statement having effect under existing section 35 of the SGAA 1992 as the employer's assessment for the quarter (see above), or
- before the end of a four year period from when the employer's superannuation guarantee charge for that quarter becomes payable under existing paragraph 23A(2)(b).

The actual payment can be made at any time after the election has been made. In extreme circumstances this can lead to lengthy delays in the actual payment being made. As late payments of the employer's obligations are not tax deductible under existing section 26-95 of the ITAA 1997, there is little incentive for an employer to make these payments promptly.

The advantages of the proposed amendments to the SGAA 1992 are:

- they limit the time during which an employer may defer the payment of their SG obligations in circumstances where a late payment is made, and
- they potentially limit the amount of the interest component of the SG charge if the proposed amendments to the SGAA 1992 are complied with.

Recent legislation in this area

Changes to the SG charge regime were last dealt with in Schedule 2 of *Tax Laws Amendment (2008 Measures No. 2) Act 2008*, which received Royal Assent on 24 June 2008. It appears that the amendments made by that particular Act were not sufficiently comprehensive to achieve all the Government's aims in this area.

For further information about that amendment see the Bills Digest for Tax Laws Amendment (2008 Measures No. 2) Bill 2008.

Basis of policy commitment

The particular measure was announced by the Minister for Superannuation and Corporate Law on 20 March 2008.[12]

Financial impact

The Explanatory Memorandum notes that the proposed measure in **Schedule 3** will have a 'minimal' financial impact.[13]

Schedule 4—Minor amendments

Schedule 4 to the Bill makes a number of minor amendments to a variety of tax legislation. Many of these amendments simply update outdated terminology or references to legislation, or correct minor grammatical errors (such as replacing references to singular

12. Senator the Hon. Nick Sherry, Minister for Superannuation and Corporate Law, '*Reducing the super red tape burden on business*', Media Release, No. 014, Canberra, 20 March 2008.

13. Explanatory Memorandum, p. 4.

verbs with references to plural ones).[14] There are, however, some substantive amendments in Schedule 4 which are explained in the Main Provisions section below.

Financial impact

The Explanatory Memorandum makes the following comment in relation to the financial impact of the minor amendments in Schedule 4 to the Bill:

> The revenue impact of extending capital allowance roll over relief for depreciating assets to the case where a fixed trust is converted to a company, is unquantifiable, but is expected to involve a minimal to small cost to revenue. Each of the other amendments will have a nil to minimal revenue impact.[15]

Main provisions

Schedule 1—CGT roll-overs for corporate restructures under the *Income Tax Assessment Act 1997*

Item 1 of Schedule 1 inserts a **new item 2A** in the table appearing after section 112–53 of the ITAA 1997. Section 112–53 sets out a table of relevant provisions in a scrip for scrip roll-over. A 'scrip for scrip roll-over' is a roll-over that occurs under Subdivision 124–M of the ITAA 1997 (being sections 124.775 to 124.810 of the ITAA 1997). **Item 1** inserts reference to the situation where an interest is 'acquired by an entity where there is a roll-over under Subdivision 124M and the arrangement is taken to be a restructure', where the first element of the entity's cost base and the reduced cost base is affected. The applicable provision of the ITAA 1997 in this situation is **proposed section 124–784B** (see below).

Section 124–780 of the ITAA 1997 (found in Subdivision 124–M) deals with the replacement of shares, where under a single arrangement an entity swaps a share (the entity's original interest) in a company (the original entity) for a share (the holder's replacement interest) in another company, or if the entity swaps an option in the original entity for an option in the other company. The exchange of a share (or option) in the original company for an option (or a share) in the other company does not constitute a scrip for scrip roll-over. The acquiring entity (either alone or as part of a group) must end up holding at least 80 per cent of the voting rights in the original company: subsection 124–780(4). The term '***arrangement***' is defined in subsection 995–1(1) as 'any arrangement, agreement, understanding, promise or undertaking, whether express or implied, and whether or not enforceable (or intended to be enforceable) by legal proceedings'.

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14. See, for example, items 1, 6–8, 10–13, 15, 19–24, 28–34, and 37–38 of Schedule 4.

15. Explanatory Memorandum, p. 5. **Items 16–17** of **Schedule 4** deal specifically with extending capital allowance roll over relief for depreciating assets to the case where a fixed trust is converted to a company.

When is an 'arrangement' a restructure?

Item 2 inserts **proposed sections 124–784A, 124–784B and 124–784C** into the ITAA 1997.

Proposed section 124–784A provides that an '***arrangement***' is a restructure if the replacement entity for the arrangement knows, or could reasonably be expected to know, that a roll-over under section 124–780 has been, or will be, obtained in relation to the arrangement, and that there is a 'common stakeholder' for the arrangement, <u>and</u> if the result of applying the formula in step 2 of the method statement in **proposed subsection 124–784A(2)** is more than 80 per cent of the result obtained by applying the formula in step 3 of that subsection.

Under **proposed subsection 124–784A(3)**, if interests in an entity are listed for quotation in a list of an '***approved stock exchange***' at the time the arrangement is completed ('the completion time'), the replacement entity may choose for the market value of the interest in the original entity to be assessed at the 'officially quoted price' of the interest at that time, rather than applying the formula in **proposed subsection 124–784A(2)**. The term '***approved stock exchange***' is defined in subsection 995–1(1) of the ITAA 1997 by reference to the 'meaning given by section 470' of the ITAA 1936, being:

(a) a stock exchange named in regulations made for the purposes of this definition; or

(b) until regulations are so made--a stock exchange named in Schedule 3. [16]

The term '***officially quoted price***' is defined in **proposed subsection 124–784A(6)** as the weighted average of the price at which the interest on the stock exchange was traded at least once in the week when the interest needs to be valued. Where the interest is quoted on two or more approved stock exchanges on a relevant day, the entity can choose which of the officially quoted prices to use: **proposed subsection 124–784A(7)**.

Calculating the cost base and reduced cost base of an acquiring entity

Proposed subsection 124–784B sets out the method of calculating the 'cost base' and 'reduced cost base' of the acquiring entity.[17] It applies to each qualifying interest in the

16. Schedule 12 to the Income Tax Regulations 1936 sets out a list of approved stock exchanges in Argentina, Australia, Austria, Belgium, Bermuda, Brazil, Canada, Chile, China, Colombia, Denmark, Finland, France, Germany, Greece, Hong Kong, Hungary, India, Indonesia, Ireland, Israel, Italy, Jamaica, Japan, Republic of Korea, Luxembourg, Malaysia, Mexico, Netherlands, New Zealand, Nigeria, Norway, Pakistan, Peru, Philippines, Poland, Portugal, Singapore, Slovakia, Slovenia, South Africa, Spain, Sri Lanka, Sweden, Switzerland, Taiwan, Thailand, Trinidad and Tobago, Turkey, United Kingdom, United States, Uruguay, Venezuela, Federal Republic of Yugoslavia and Zimbabwe. The approved stock exchanges in Australia are the Australian Stock Exchange Limited, the Bendigo Stock Exchange Limited and the National Stock Exchange of Australia Limited.

original entity that is acquired under an arrangement to which **proposed section 124–784A** applies, but where the first element of the cost base of the acquiring entity is not worked out under section 124–782.[18]

The formula for working out the first element of the cost base of the acquiring entity is set out in the method statement contained in **proposed subsection 124–784B(2)**. It is calculated by reference to the market value and the cost bases of the original entity's pre-CGT assets and post-CGT assets (except trading stock) at the 'completion time'. Where the original entity's CGT assets (except trading stock) had no cost base, the relevant amount for inclusion in the formula is the 'maximum amount of consideration' the original entity would need to receive if it were to dispose of the asset at the completion time without incurring an amount by way of assessable income or deduction. The formula also provides for the assessment of the original entity's trading stock.

Proposed subsection 124–784B(3) provides that where the qualifying interest is acquired under the arrangement partly in exchange for one or more replacement interests and partly in exchange for something else, the formula in **proposed subsection 124–784B(2)** applies only for working out 'the first element of that part of the cost base of the qualifying interest that is attributable to the replacement interests'.[19]

Proposed subsections 124–784B(4) and (5) deal with the treatment of liabilities in step 4 of the formula in **proposed subsection 124–784B(2)**.

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17. The term 'cost base' of a CGT asset is defined in subsection 995–1(1) of the ITAA 1997 by reference to Subdivision 110–A of that Act. The cost base of a CGT asset generally has five elements, which can be summarised as the costs of purchasing the asset; costs that are incidental to the purchase; costs of owning the asset; capital expenditure in preserving, moving or installing the asset; and capital expenditure in establishing, preserving or defending one's title to, or right over, the asset: section 110–25. The term 'reduced cost base' is defined in subsection 995–1(1) of the ITAA 1997 by reference to Subdivision 110–B of that Act. Section 110–55 sets out the five elements to the reduced cost base of a CGT asset. They are the same as the elements of the cost base of a CGT asset in section 110–25, except for the third element. In the case of a reduced cost base, the assessment of the third element depends on how the asset is treated under Division 58, which deals with capital allowances for depreciating assets previously owned by an exempt entity.

18. Section 124–782 deals with the transfer or allocation of the cost base of shares acquired by the acquiring entity. It may not apply, for example, where the dual requirements of the section cannot be satisfied: (a) that the original interest holder obtains a roll-over; and (b) that the original interest holder is a significant stakeholder or a common stakeholder for the arrangement.

19. For example, where part of the first element of the cost base and reduced cost base of the qualifying interest is attributable to cash, it is worked out using the general rules about cost base. See section 110–25 of the ITAA 1997.

Proposed subsection 124–784B(6) states that the reduced cost base of the acquiring entity for the qualifying interest in the original entity is worked out 'similarly'. While it is not entirely clear, it seems that this means that the reduced cost base is worked out according to the formula in proposed subsection 124–784B(2) for calculating the first element of the cost base of the acquiring entity. However, to avoid doubt, it would be prudent to make specific reference to the appropriate subsection.

Proposed subsection 124–784B(7) states that for the purposes of step 5 of the formula in **proposed subsection 124–784(2)** (which deals with the situation of classes of membership interests in the original entity), an option, right, or similar interest (including a contingent option, right or interest) to acquire a membership interest in the original entity is treated 'as if it were a membership interest in the original entity'.

Allocating an appropriate cost base to equity issues or new debt

Proposed section 124–784C deals with the allocation of an appropriate cost base to equity issues or new debt owed by an acquiring entity under the arrangement to the '***ultimate holding company***' of a '***wholly owned group***', where the cost base is worked out under **proposed section 124–784B**.

The term '***ultimate holding company***' (of a wholly owned group) is defined in subsection 995–1(1) of the ITAA 1997 by reference to the meaning of that term in section 124–780 (see above, at the beginning of the Main Provisions section). Particularly, subsection 124–780(7) states: 'A company is the ultimate holding company of a wholly-owned group if it is not a 100% subsidiary of another company in the group'.

The term '***wholly owned group***' is defined in subsection 995–1(1) of the ITAA 1997 by reference to the meaning of the term in section 975–500 of that Act. Section 975–500 states:

> Two companies are members of the same wholly-owned group if:
>
> (a) one of the companies is a 100% subsidiary of the other company; or
>
> (b) each of the companies is a 100% subsidiary of the same third company.

Proposed subsection 124–784C(2) provides that the first element of the cost base of the equity or debt is that part of the cost base of the qualifying interest worked out under **proposed subsection 124–784B** as 'may be reasonably allocated to the equity or debt' and 'is not more than the market value of the equity of debt at the completion time'. The term '***market value***' is usually defined according to the plain and ordinary meaning of the term:

section 960–400 of the ITAA 1997. However, subsection 995–1(1) of the ITAA 1997 provides that the term's ordinary meaning is 'affected by Subdivision 960–S'.[20]

Proposed subsection 124–784C(3) provides that any capital gain of the ultimate holding company from the repayment of new debt owed by an acquiring entity under the arrangement is 'disregarded to the extent that it relates to the difference between the part of the cost base worked out under [proposed] section 124–784B and the market value of the debt at the completion time'. As stated in the note to the proposed subsection, there may be a capital gain if the debt is assigned or exchanged.

Another exception to the scrip for scrip roll-over provisions

Item 3 of Schedule 1 to the Bill inserts **proposed subsection 124–795(4)** into the ITAA 1997. Section 124–795 deals with the exceptions to the scrip for scrip roll-over provisions in Subdivision 124–M. The proposed insertion makes it clear that a taxpayer obtains a scrip for scrip roll-over in relation to the exchange of a qualifying interest if the replacement entity makes a choice to that effect under **proposed subsection 124–795(4)** and either the replacement entity or the original entity notifies the taxpayer in writing of the choice before the exchange.

Effect on arrangements where CGT roll-overs are obtained

Item 4 of Schedule 1 inserts **proposed Subdivision 715–W** at the end of Division 715, which deals with interactions between Part 3–90 of the ITAA 1997 (which deals with consolidated groups) and other areas of the income tax law. **Proposed Subdivision 715–W** deals with the effect on arrangements where CGT roll-overs are obtained. There are four proposed sections in the proposed Subdivision: **proposed sections 715–910, 715–915, 715–920 and 715–925**.

Proposed section 715–910 applies if, as the result of an arrangement to which proposed section 124–784A (see above) applies, an 'original entity' becomes a 'subsidiary member of a consolidated group', <u>and</u> **proposed section 715–920** does not apply.[21] The term 'subsidiary member of a consolidated group' is defined in subsection 995–1(1) of the ITAA by reference to the definition in section 703–15 of that Act.[22]

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20. Subdivision 960–S comprises sections 960–400 (see immediately above), 960–405 (which deals with the effect of the GST on the market value of an asset) and 960–410 (which deals with the market value of non-cash benefits).

21. **Proposed section 715–920** applies if the original entity was the head company of another consolidated group before the arrangement was completed.

22. The requirements of a 'subsidiary member' of a consolidated group are set out in item 2 of the table in section 703–15, including that the entity must be a company, trust or partnership (but not one covered by section 703–20); and if the entity is a company—all or some of its taxable income (if any) must be taxable apart from Part 3–90 at a rate that is or equals the

Proposed subsection 715–910(2) states that for the purposes of proposed section 124–784B, the 'completion time' for the arrangement is the time the original entity becomes a member of the group. It also states that Division 701 (Core rules) is to be disregarded in relation to the original entity becoming a member of the group. **Proposed subsection 715–910(3)** states that the head company may choose that section 701–10 (dealing with the cost to a head company of the assets of another entity which becomes a subsidiary member of the group) and subsection 701–35(4) (dealing with setting a value of trading stock at a tax-neutral amount) do not apply to the original entity's assets in respect of the original entity becoming a subsidiary member of the group.

Proposed section 715–915 deals with the effect on restructures where the original entity is a head company. It provides that <u>if</u> proposed section 124–784A applies in relation to an arrangement, and the original entity (within the meaning of that section) for the arrangement is the 'head company of a consolidated group' just before the arrangement was completed, and proposed section 715–920 does not apply (because the original entity was not the head company of another consolidated group before the arrangement was completed), then for the purposes of section 124–784B, the rules in subsections 701–1(1) and 701–5 apply in respect of the group.

Subsection 701–1(1) is known as the 'single entity rule' and provides:

> (1) If an entity is a subsidiary member of a consolidated group for any period, it and any other subsidiary member of the group are taken for the purposes covered by subsections (2) and (3) to be parts of the head company of the group, rather than separate entities, during that period.[23]

Section 701–5 is known as the 'entry history rule' and provides:

> For the head company core purposes [detailed in subsection 701–1(2)] in relation to the period after the entity becomes a subsidiary member of the group, everything that happened in relation to it before it became a subsidiary member is taken to have happened in relation to the head company.

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corporate tax rate; and the entity must not be a non-profit company (as defined in the *Income Tax Rates Act 1986*). The entity must be an Australian resident (but not a prescribed dual resident), if it is a company; and must be a wholly-owned subsidiary of the head company of the group and, if there are interposed between them any entities, the set of requirements in section 703–45, section 701C–10 of the *Income Tax (Transitional Provisions) Act 1997* or section 701C–15 of that Act must be met.

23. The core purposes contained in subsections 701–1(2) and (3) are: working out the amount of the head company's liability (if any) for income tax calculated by reference to any income year in which any of the period occurs or any later income year; working out the amount of the head company's loss (if any) of a particular sort for any such income year; working out the amount of the entity's liability (if any) for income tax calculated by reference to any income year in which any of the period occurs or any later income year; and working out the amount of the entity's loss (if any) of a particular sort for any such income year.

The term 'head company of a consolidated group' is defined is subsection 995–1(1) as having the meaning given by section 703–15 of the ITAA 1997, which provides that an entity is the 'head company' of a consolidated group if the requirements in item 1 of the table in the section are met. The requirements are that (i) the entity must be a company (but not one covered by section 703–20) that has all or some of its taxable income (if any) taxed at a rate that is or equals the corporate tax rate; (ii) the entity must be an Australian resident (but not a prescribed dual resident); and (iii) the entity must not be a wholly-owned subsidiary of another entity that meets the requirements in (i) or (ii) or, if it is, it must not be a subsidiary member of a consolidatable group or consolidated group.

Proposed section 715–920 deals with the effect on restructures where the original entity is a head company that becomes a subsidiary member of another group. **Proposed section 715–920** applies if proposed section 124–784A applies in relation to an arrangement; the original entity for the arrangement is the head company of a consolidated group (the 'acquired group') just before the arrangement was completed; and as a result of the arrangement both the original entity and the subsidiary members of the acquired group (just before the arrangement was completed) become subsidiary members of another group at the completion of the arrangement.

Proposed subsection 715–920(2) provides that for the purposes of proposed section 124–784B, the 'original entity' is taken to be the head company of the acquired group at the completion time for the arrangement. Further, the operation of Part 3–90 of the ITAA 1997 for the 'head company core purposes' (mentioned in subsection 701–1(2)) in relation to the original entity and the entities that were subsidiary members of the acquired group just before the arrangement was completed (see above) continues to have effect at the completion time for the arrangement: **proposed paragraphs 715–920(2)(a) and (b)**. **Proposed subsection 715–920(2)** also states that the 'completion time' is the time when the original entity becomes a member of the other group (**proposed paragraph 715–920(2)(c)**), and that Division 701 (Core rules) is to be disregarded in relation to the original entity becoming a member of the group. Finally, **proposed subsection 715–920(3)** is in similar terms to **proposed subsection 715–910(3)** and applies to the acquiring group**.**

Proposed section 715–925 deals with the effect on restructures where the original entity ceases to be a subsidiary member. It states that if, as the result of an arrangement to which proposed section 124–784A applies, an original entity ceases to be a subsidiary member of a consolidated group after the completion time, and does not become a member of another consolidated group, then (for the purposes of proposed section 124–784B) the completion time for the arrangement is the time when the original entity ceases to be a subsidiary member.

Application of the amendments in Schedule 1

Item 6 provides that the amendments in Schedule 1 apply to:

- an arrangement that is or relates to a takeover bid (as defined in the *Corporations Act 2001*) if the relevant step specified in sections 633 and 635 of that Act (for an off-market bid or a market bid, as the case may be) is completed after 7.30pm (legal Australian Capital Territory Time) on 13 May 2008
- an arrangement if a court makes an order (under subsection 411(1) of the *Corporations Act 2001*) for a meeting or meetings of a company's members (or one or more classes of a company's members) about the arrangement, and the application for the order was made after 7.30pm (legal Australian Capital Territory Time) on 13 May 2008, and
- in relation to an arrangement which does not fall within the first two dot-points: a decision to enter into the arrangement was not made before 7.30pm (legal Australian Capital Territory Time) on 13 May 2008.

Notably, the amendments operate retrospectively, which may cause concern or a practical difficulty for those entities to whom the amendments apply, if the entity is not otherwise already aware of the Government's intention to revise the law. However, on 13 May 2008, the Treasurer announced the planned modification of the scrip for scrip roll-over provisions for corporate restructures as part of the 2008–09 Budget—with the associated financial statements being available to the public from that time.[24]

Schedule 2—Mutual assistance in collection provisions of the *Taxation Administration Act 1953*

Division 263 of the Administration Act deals with mutual assistance in collection of foreign tax debts, where there is an agreement in force between Australia and a foreign country or territory 'that contains an article relating to assistance in collection of foreign tax debts'.[25] As noted in the Assistant Treasurer's Second Reading Speech when introducing the Bill on 3 December 2008, the mutual assistance provisions 'enable the Commissioner of Taxation to take action to collect or conserve tax debts owed in another country where the debtor is resident in Australia or has assets in Australia'.[26]

Item 1 of **Schedule 2** to the Bill inserts **proposed subsection 263–30(1A)** into existing Schedule 1 to the Administration Act to make clear that the amount owed by the debtor may not be the same as the amount of a 'foreign revenue claim' entered in the Foreign

24. See, for example, Budget Paper No. 2, Part 1: Revenue Measures, http://www.budget.gov.au/2008-09/content/bp2/html/revenue-01.htm, accessed on 13 January 2009.

25. Section 263–5 of the Taxation Administration Act 1953.

26. The Hon. Chris Bowen MP, Assistant Treasurer, 'Second Reading Speech: Tax Laws Amendment (2008 Measures No. 6) Bill 2008', House of Representatives, *Debates*, 3 December 2008, p. 15, http://www.aph.gov.au/hansard/reps/dailys/dr031208.pdf, accessed on 13 January 2009.

Revenue Claims Register (the Register) kept by the Commissioner of Taxation under section 263–20 of the Administration Act.[27]

Items 2 and 3 of **Schedule 2** clarify the wording of existing subsection 263–30(2) and the heading to existing section 263–35 (being 'Amending the Register'). The heading needs to be amended as a consequence of the proposed amendments to section 263–35 contained in **items 4–7** of **Schedule 2**.

Item 4 of **Schedule 2** inserts **proposed subsection 263–35(2A)** to make clear that the Commissioner may reduce an amount to be recovered from a debtor under existing paragraph 263–35(2)(b) without amending the Register.[28]

Item 5 of **Schedule 2** replaces existing subsection 263–35(5) with a new provision. The amendment removes the reference to the debtor being 'taken never to have been liable to pay an amount (including any general interest charge)' where the Commissioner removes particulars of a foreign revenue claim from the Register, and replaces it with a reference to the debtor being 'entitled to a credit for the purposes of Part IIB'.[29] **Item 6** makes a similar amendment to the wording of existing subsection 263–35(6), and **item 7** inserts a note at the end of existing subsection 263–35(6) to direct attention to the fact that how the credit is applied is set out in Part IIB of the Administration Act.

Item 8 inserts **proposed subsection 263–40(3)** into Schedule 1 to the Administration Act. Section 263–40 deals with payment by the Commissioner to the competent authority (or a nominee) of all or part of an amount recovered from a debtor under a registered foreign revenue claim. The proposed subsection gives the Commissioner a discretion to pay to the competent authority all or part of judgment interest and/or costs recovered in the course of legal proceedings, where the costs 'represent an amount that has previously been paid by the competent authority to the Commonwealth in relation to the recovery of the claim'. The proposed amendment includes no guidance on the exercise of the discretion—although, at least in relation to the costs of legal proceedings, the payment to the competent authority would seem to be in the nature of reimbursement of an amount already paid by the competent authority to the Commonwealth to recover the foreign debt.

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27. Existing section 263–30 deals with when the amount owed by the debtor becomes a pecuniary liability owed by the debtor to the Commonwealth, and when that liability becomes due and payable. Existing section 263–20 requires the Commissioner of Taxation to keep a register of foreign revenue claims.

28. Existing paragraph 263–35(2)(b) provides that the Commissioner may, with the agreement of the relevant competent authority, 'reduce an amount to be recovered from a debtor under the claim'.

29. Part IIB of the Administration Act deals with 'running balance accounts', application of payments and credits, and related matters. See particularly Division 3 of Part IIB, which deals with the treatment of payments, credits and 'running balance account' surpluses.

Item 9 provides that the amendments made by Schedule 2 to the Bill apply to foreign revenue claims already contained in the Register at the commencement of Schedule 2 (being Royal Assent) and to claims that are entered in the Register after that date.

Schedule 3—Late payment offset for superannuation guarantee contributions

Schedule 3 amends the *Superannuation Guarantee (Administration) Act 1992* in relation to the late payment offset for superannuation guarantee contributions. Under existing section 23A of the SGAA 1992, where an employer makes a late superannuation guarantee contribution for an employee, the employer may offset that contribution against any superannuation guarantee charge liability.

Item 1 of **Schedule 3** to the Bill amends existing paragraph 23A(1)(a) by including a requirement for the contribution to be made 'before the employer's original assessment of that quarter is made'. As noted above, the employer's own assessment of their SG obligations where a late payment is to be made for the quarter must be submitted on or before the 28th day of the second month after the end of the quarter.

The effect of this amendment is to set a time limit for making a late SG payment on the behalf of an employee of:

- on or before the 28th day of the second month after the end of the quarter (the date by which an employer must submit their self assessment of their SG charge liability, or

- the date on which the ATO issues a default assessment

if the employer is to take advantage of the SG charge offset provisions in existing section 23A of the SGAA 1992.

Item 2 of **Schedule 3** replaces the requirement in existing paragraph 23A(1)(b) that the election (by the employer to have the contribution offset) must be made 'within 4 years after the employer's superannuation guarantee charge for the quarter became payable' with the requirement that the election be made 'within 4 years after the employer's original assessment for the quarter is made'. This amendment requires that the employer to elect to make use of the existing offset provisions in section 23A of the SGAA 1992 by the above dates.

Item 3 amends existing subsection 23A(3) by making it clear that the contribution is offset 'at the time the employer's original assessment for the quarter is made'. A benefit of this particular proposed amendment is to limit the amount of interest component that accrues as part of the SG charge to interest that accumulates between the due date and the date on which the original assessment for the quarter is made.

Item 4 replaces existing subsection 49(3A) of the SGAA 1992 with a revised subsection. Section 49 deals with an unpaid superannuation guarantee charge, and appears in Part 6 of the Act, which deals with the collection and recovery of the charge. The proposed revision is much clearer and simpler than the existing provision, and makes it plain that an election under section 23A 'has effect from the time the employer's original assessment for the quarter is made'.

Item 5 states that the amendments in Schedule 3 to the Bill apply to elections under section 23A of the SGAA 1992 made on or after the commencement of Schedule (that is, on or after Royal Assent).

Schedule 4—Minor amendments

Fringe Benefits Tax Assessment Act 1986

Item 2 of **Schedule 4** amends steps 3 and 4 of the method statement in subsection 5C(3) of the *Fringe Benefits Tax Assessment Act 1986*, and also inserts proposed step 5 of the method statement. Section 5C sets out how to work out an employer's 'aggregate fringe benefits amount'.

Subsection 5C(3) contains the method statement for working out an employer's 'type 1' aggregate fringe benefits amount for a year of tax. The proposed amendment simplifies step 3 of the method, and also makes clear that the 'excluded fringe benefits' must also be 'GST-creditable benefits'. Note 1 to revised step 3 comments that existing subsection 5E(3) explains what is an 'excluded fringe benefit',[30] and Note 2 to revised step 4 notes that section 149A explains what is a 'GST-creditable benefit'.[31]

Item 3 of **Schedule 4** to the Bill amends steps 3 and 4 of the method statement in existing subsection 5C(4), which deals with the calculation of an employer's 'type 2' aggregate fringe benefits amount for a year of tax.

Item 4 provides that the amendments made by **items 2 and 3** apply to the year of tax starting on 1 April 2000 and later years of tax. Again, this means that the proposed

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30. Subsection 5E(3) defines 'excluded fringe benefit' (among numerous things) as a fringe benefit such as the provision of meal entertainment (as defined in section 37AD), car parking fringe benefit (see subsection 136(1)); or a fringe benefit that is reduced under section 60 (about remote area housing) or is provided to address a security concern relating to the personal safety of an employee, or an associate of an employee and that arises in respect of the employee's employment.

31. For the text of section 149A, see http://www.austlii.edu.au/au/legis/cth/consol_act/fbtaa1986312/s149a.html, accessed on 13 January 2008. A GST-creditable benefit is basically the provision of a thing or service (or a licence to use a thing) to an employee, where the provider of the benefit (or a person who is or was a member of the same GST group as the provider) is entitled to a tax input credit under the *A New Tax System (Goods and Services Tax) Act 1999* because of the provision (acquisition, or importation) of the benefit/thing.

amendments will operate retrospectively, which may or may not infringe a taxpayer's rights. However, the amendments seem unlikely to affect taxpayers unduly, given that they seem to do little more than simplify existing procedures.

Income Tax Assessment Act 1936

Item 9 amends subsection 82KZMGA(1) of the ITAA 1936. Section 82KZMGA deals with deductions for certain forestry expenditure, and currently provides:

> (1) A taxpayer cannot deduct expenditure in relation to which the requirements in section 82KZMG [which also deals with deductions for certain forestry expenditure] are met if:
>
> > (a) the taxpayer holds the taxpayer's interest in the agreement mentioned in section 82KZMG as an initial participant in the agreement; and
> >
> > (b) a CGT event happens in relation to that interest within 4 years after the end of the year of income in which the taxpayer first incurred expenditure under the agreement.
>
> (2) Despite section 170, the Commissioner may amend the taxpayer's assessment at any time within 2 years after the end of the year of income in which the CGT event happens, for the purpose of giving effect to this section.[32]

Item 9 replaces existing subsection 82KZMGA(1) with a revised provision that makes it clear that the requirements in paragraph 82KZMG(2)(a) do not need to be met. It also inserts the requirement that the expenditure must be 'incurred on or before 30 June 2008', which is also the end date for expenditure under paragraph 82KZMG(2)(a)—the difference between that paragraph and **proposed paragraph 82KZMGA(1)(c)** being that existing paragraph 82KZMG(2)(a) requires that the expenditure 'must be incurred on or after 2 October 2001 and on or before 30 June 2008 under an agreement'. According to the Explanatory Memorandum for the Bill, **item 9** removes 'a discrepancy in the law that may inhibit the trading of pre-2 October 2001 interests in forestry managed investment schemes' and 'reflects the original policy intent of the *Tax Laws Amendment (2007 Measures No. 3) Act 2007*'.[33]

Income Tax Assessment Act 1997

Item 26 revises the example in subsection 122–50(1). Section 122–50 of the ITAA 1997 deals with the disposal or creation of assets by an individual or trustee to a wholly-owned company, where all the assets are acquired on or after 20 September 1985. In addition to the things mentioned in the existing example, the revised example also refers to the market value of the taxpayer's plant and equipment, and office furniture at the time of disposal.

32. Section 170 of the ITAA 1936 sets out when the Commissioner may amend an assessment.

33. Explanatory Memorandum, Table 4.3, p. 48.

According to the Explanatory Memorandum, the example was correct when it was first introduced, but has not been updated to reflect changes in the law since that time.[34]

Taxation (Interest on Overpayments and Early Payments) Act 1983

Item 45 inserts paragraph (a) into the definition of 'income tax crediting amount' into subsection 3(1) of the *Taxation (Interest on Overpayments and Early Payments) Act 1983.* The whole of that paragraph was inadvertently repealed by the *Tax Laws Amendment (2007 Measures No. 4) Act 2007.*[35] **Item 45** reinstates the part of the paragraph which 'allowed interest to be paid to taxpayers when a credit entitlement arose that was not related to foreign tax credits'.[36]

Part 2—Asterisking amendments of the *Income Tax Assessment Act 1997*

Part 2 of **Schedule 4** to the Bill corrects the 'asterisking' of words in the ITAA 1997. Where an asterisk appears immediately before a term in the ITAA 1997, the asterisk indicates to the reader that the term is defined in the Act: section 2.10 of the ITAA 1997. The purpose of **item 52** is twofold: some items in the table in **item 52** insert an asterisk before some terms which are actually defined in the ITAA 1997 but which are not currently asterisked, and some items in the table in **item 52** remove an asterisk before a term where the asterisk is not required (such as where the asterisked term has already been asterisked in the relevant subsection).

Part 3—Repeal of the *Pay-roll Tax Act 1941*

Item 53 of **Schedule 4** to the Bill repeals the whole of the *Pay-roll Tax Act 1941*.

As noted in the Explanatory Memorandum, 'Commonwealth payroll tax ceased to apply to wages paid after 1 September 1971, which is the date the Commonwealth transferred responsibility for payroll tax to the States'.[37]

While the *Pay-roll Tax Assessment Act 1941* was repealed by the *Tax Laws Amendment (Repeal of Inoperative Provisions) Act 2006*, the *Pay-roll Tax Act 1941* has remained on the statute books, even though it has not been operative for nearly 40 years.

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34. ibid., Table 4.4, p. 50.

35. ibid., Table 4.7, p. 52.

36. The proposed paragraph itself refers to 'any amount of a credit that does not arise under Division 770 of the *Income Tax Assessment Act 1997* or under the *International Tax Agreements Act 1953*'. Division 770 of the ITAA 1997 deals with foreign income tax offsets. The *International Tax Agreements Act 1953* is an 'Act to give the force of Law to certain Conventions and Agreements with respect to Taxes on Income and Fringe Benefits, and for purposes incidental thereto': see long title to that Act.

37. Explanatory Memorandum, Table 4.9, p. 53.

Members, Senators and Parliamentary staff can obtain further information from the Parliamentary Library on (02) 6277 2795 (Morag Donaldson) or (02) 6277 2469 (Bernard Pulle).