

**1990-91-92**

**THE PARLIAMENT OF THE COMMONWEALTH  
OF AUSTRALIA**

**SENATE**

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**TAXATION LAWS AMENDMENT BILL 1992**

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**SUPPLEMENTARY EXPLANATORY  
MEMORANDUM**

(Amendments to be moved on behalf of the Government)

(Circulated by the authority of the Treasurer,  
the Hon J. Dawkins M.P.)

## **General Outline and Financial Impact of the Amendments**

The amendments will amend Taxation Laws Amendment Bill 1992 [originally introduced into Parliament on 19 December 1991 as Taxation Laws Amendment Bill (No.4) 1991]:

### **Depreciation**

- to correct a technical deficiency in the proposed new definition of effective life for depreciable plant in relation to second-hand plant; and
- to provide an option for taxpayers to adopt the Commissioner's published depreciation rates in lieu of those based on the proposed new effective life rules.

### **Dividend rebate for company beneficiaries**

- to allow the intercorporate dividend rebate to a company that receives income attributable to dividends either directly from a trust or partnership, or indirectly through one or more interposed trusts or partnerships;
- to change the date on which the amendments relating to private company dividends received by corporate unit trusts and public unit trusts that are taxed as companies apply to the date on which the Bill receives Royal Assent; and

### **Widely distributed finance shares**

- to make a technical correction to ensure that all paragraphs of the public company test for widely distributed finance shares under the foreign source income measures are consistent; ie.75% or more.

**Deferral of deductions for trading stock purchases involving prepayments**

- to ensure that there is not an unintended mismatch of expenditure on stock intended to be used as trading stock and income derived in relation to the disposal of the stock before the stock becomes trading stock on hand.

**Financial Impact**

These amendments to the depreciation measures make it certain that the law will be consistent with the Government's announced intentions and will have no impact on the revenue.

These amendments to the following measures will have no impact on the revenue:

- dividend rebate for company beneficiaries;
- widely distributed finance shares; and
- deferral of deductions for trading stock purchases involving prepayments.

## **Summary of proposed amendments**

Amendments to the Bill are to be moved on behalf of the Government relating to

- the calculation of the effective life of second-hand plant for depreciation purposes
- an option for taxpayers to adopt depreciation rates published by the Commissioner of Taxation
- to allow the intercorporate dividend rebate to a company that is the beneficial owner of shares that are registered in the name of a trustee
- to the widely distributed finance share measures; and
- to the deferral of deductions for trading stock purchases involving prepayments measures.

### **Depreciation**

#### ***Second-hand depreciable plant***

The proposed change will ensure that the effective life of plant is always calculated as if the plant were new. While the life of second-hand plant is usually calculated on this basis, the amendment corrects an anomaly under which some second-hand plant would have an effective life calculated differently.

#### ***Commissioner's published depreciation rates***

Under this amendment, taxpayers will be permitted to adopt rates of depreciation published by the Commissioner of Taxation in lieu of self-assessed rates, even where those rates are more generous than self-assessed rates.

### **Dividend rebate for company beneficiaries**

The effect of the amendments to the intercorporate dividend rebate provisions are that a company will be entitled to a rebate

*6 Summary of Proposed Amendments*

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under sections 46 and 46A of the Principal Act on distributions of income attributable to dividends from a trust or partnership.

**Widely distributed finance shares**

This amendment is to correct a technical deficiency in the Bill.

<b>Notes on the proposed amendments</b>
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## **Depreciation**

### ***Second-hand depreciable plant***

Chapter 1 of the Explanatory Memorandum to the Bill explains the proposed new depreciation arrangements.

Clause 16 of the Bill inserts new section 54A containing the definition of effective life [refer paragraphs 1.19 - 1.39 of the Explanatory Memorandum]. Under that definition, taxpayers estimate the effective life of their depreciable plant on the basis of certain assumptions. Subparagraph 54A(1)(a)(i) makes it clear that second-hand plant is to be treated as if new in estimating effective life.

By comparison, paragraph 54A(1)(b) - dealing with circumstances where a taxpayer reasonably expects to scrap or abandon plant at a later time - is silent about the treatment of second-hand plant for effective life purposes; that is, there is no requirement to treat second-hand plant as if new in estimating effective life. This is unintended and would permit taxpayers in those circumstances to obtain greater depreciation deductions than other owners of second-hand plant.

### ***The amendment***

Accordingly, the definition of effective life is to be amended to require owners of second-hand plant who expect to scrap or abandon that plant at a later time to assume that it is new in estimating effective life [***Clause 9 - paragraph 54A(1)(c); clauses 6 to 8 deal with minor consequential amendments***]

### ***Commissioner's published depreciation rates***

Under the present law, the Commissioner of Taxation is required to estimate the effective life of each unit of depreciable plant at the time it is first used for income producing purposes.

As a practical measure, it has been a longstanding practice of the Commissioner of Taxation to publish depreciation rates he considers appropriate for particular classes of depreciable plant. Taxpayers have been able to rely on those published rates but could seek to have the Commissioner vary the rate in respect of specific items in their use.

Under the Bill presently before the Parliament, taxpayers may "self-assess" effective life, and therefore depreciation rates, on the basis of their own particular usage of plant [subsection 54A(1)]. In expectation that many taxpayers would not wish to do this but would prefer to rely on the Commissioner's published rates, it has been made clear that, instead of making their own estimates of effective life, taxpayers could continue to adopt the Commissioner's rates, even where they were more generous than a self assessed rate would be.

### ***The amendment***

The depreciation self-assessment measures presently before the Parliament contain no legislative authority for taxpayers to adopt the Commissioner's published depreciation rates. The amendment to the Bill will require the Commissioner of taxation to determine and publish effective lives for depreciable plant which taxpayers may adopt, in lieu of their own estimate, for the purposes of calculating depreciation rates. [***Clause 5 - paragraph 54A(1)(aa) and clause 10 - subsections 54A(1A) to (1J) and (1L)***]

### ***Commissioner's determination of effective life***

The determination will reflect the Commissioner's estimate of the effective life of each class of depreciable property. In some instances, a number of different periods may be determined in respect of a class of property, reflecting different circumstances of use by separate categories of taxpayers, eg. to distinguish the use of passenger motor vehicles as taxis. The determination is to be made and published within 28 days of these amendments becoming law.

If there is a particular class of property not included in the determination, the Commissioner may be requested to

determine a period. A determination must be made within 60 days of the request or, where further information is sought by the Commissioner, within 60 days of the receipt of that information.

***Elections to adopt Commissioner's determination***

Taxpayers wishing to adopt the Commissioner's periods will generally need to make an irrevocable election within 6 months of the end of the year of income to which the election relates [*Clause 10 - subsection 54A(1K)*]

***Record keeping***

Elections are to be retained for 5 years after the year in which the property is disposed of, lost or destroyed [*Clause 11 - subsection 262A(4AE)*]

***Application dates***

Both of the depreciation changes will apply from the commencement of the new effective life rules, ie. from 1 July 1991 in respect of depreciable plant acquired on or after 13 March 1991.



## **Dividend rebate for company beneficiaries**

Amendments (1), (2), (3), (4) and (15) relate to this measure.

Clause 10 of the Bill proposes the insertion of new section 45Z into the Principal Act to modify the application of sections 46 to 46F of the Principal Act where the shares on which a dividend is paid:

- are beneficially owned by a company but the registered holder of the shares is a trustee; or
- are held by a partnership in which a company is a partner.

The first amendment will amend proposed subsection 45Z(1) of the Bill so that a company that is absolutely entitled as against the trustee to the shares on which the dividend is paid will not be entitled to the intercorporate dividend rebate on those dividends if it is acting as a trustee. [**Clause 10 - new paragraph 45Z(1)(aa)**]

The second amendment will amend new section 45Z so that a rebate will be allowable under section 46 or 46A to a company that derives income from a trust or partnership, whether directly or indirectly through a series of trusts or partnerships, that is attributable to a dividend, and the company is not absolutely entitled to the shares on which the dividend is paid. The rebate will not be available if the company is deriving the share of trust or partnership income as a trustee. [**Clause 10 - new subsection 45Z(1A)**]

This provision will modify the application of sections 46 to 46F where a company that is a unitholder in a unit trust, a joint holder of units in a unit trust or a beneficiary in a trust, including a discretionary trust, receives income that is attributable to a dividend, whether received directly by the trust or partnership, or indirectly through a series of interposed trusts or partnerships.

The third amendment will amend proposed subsection 45Z(2) of the Bill so that the rebate will not be available to a company that is acting as a trustee in relation to dividends received as a

partner in a partnership. ***[Clause 10 - new paragraph 45Z(2)(aa)]***

The fourth amendment will insert two new subsections into new section 45Z.

Under new subsection (3) a rebate will be allowable under section 46 or 46A to a company that derives income from a partnership, whether directly or indirectly through a series of trusts or partnerships, that is attributable to a dividend and the company is not a partner in the partnership that is the holder of the shares on which the dividend is paid. The rebate will not be available if the company is deriving the share of trust or partnership income as a trustee. ***[Clause 10 - new subsection 45Z(3)]***

This provision will modify the application of sections 46 to 46F when a company that receives income attributable to a dividend that is paid on shares held by a partnership in which a trustee (but not the company) is a partner, will be entitled to the rebate. For example, if a partnership holds units in a unit trust and one of the partners is the trustee of a trust in which a company is a beneficiary, the company will be entitled to the intercorporate dividend rebate on income attributable to dividends received by the partnership.

Proposed subsections 45Z(1), (1A), (2) and (3) will deny the intercorporate dividend rebate to a company that receives dividends or income attributable to a dividend in a trustee capacity. (See earlier notes.) However, they will not apply to the trustees of corporate unit trusts and public trading trusts that are taxed as companies (Divisions 6B and 6C). ***[Clause 10 - new subsection 45Z(4)]***

### ***Corporate unit trusts and public trading trusts***

Sections 102L and 102T of the Principal Act provide that dividends received by corporate unit trusts and public trading trusts that are taxed as companies (Divisions 6B and 6C) are entitled to the rebate on the same basis as other companies. Subclauses 31(1) and 31(2) of the Bill contain minor amendments to sections 102L and 102T of the Principal Act to overcome a deficiency in the present law. The effect of

subclause 63(11) of the Bill is that these amendments would apply retrospectively.

The thirteenth amendment will ensure that the application of the amendments to subsections 102L and 102T will be wholly prospective and apply from the date on which the Bill receives Royal Assent. ***[Subclause 63(11)]***

***Entitlement of company beneficiaries to rebate***

The effect of new subsections 45Z(1A) and (3) will be that a rebate will be allowable under section 46 or 46A on a company's share of trust or partnership income that is attributable to a dividend as if:

- the company was the registered shareholder in the company paying the dividend. Thus, for the purposes of sections 46 to 46F inclusive, the company is the shareholder; ***[New paragraphs 45Z(1A)(d) and 45Z(3)(d)]***
- the income attributable to the dividend was paid directly to the company and not to the trustee or partnership; ***[New paragraphs 45Z(1A)(e) and 45Z(3)(e)]***
- the amount of the dividend paid to company was equal to the amount of the company's share of the net income of the trust or partnership that is attributable to the dividend actually paid to the first trust or partnership in a chain; ***[New paragraphs 45Z(1A)(f) and 45Z(3)(f)]***
- if the company has an interest in the shares on which the dividend was paid, the company's interest in the share was the share on which the dividend was paid. The effect of deeming this to be the case is that in determining when and whether the share was acquired or disposed of by the company for the purposes of sections 46 to 46F, the matter will be determined by reference to when the company acquired or disposed of its interest in the share; ***[New paragraphs 45Z(1A)(g) and 45Z(3)(g)]***

- if the company does not have an interest in the shares on which the dividends were paid, for example the company is a beneficiary in a discretionary trust, the company will be deemed to have an interest in the share on which the dividend was paid. The company will be deemed to have acquired its deemed interest in the share when the share was acquired by the trustee; ***[New paragraphs 45Z(1A)(h) and 45Z(3)(h)]***
- the year of income in which the income attributable to dividends is included in the assessable income of the company, was the year of income in which the dividend was (indirectly) "paid" to the company. The effect of these paragraphs is that a rebate will be allowable under subsection 46(2) or 46A(5) to the company in its assessment for the year of income in which the trust or partnership distribution containing the income attributable to the dividend is included in the company's assessable income; ***[New paragraphs 45Z(1A)(i) and 45Z(3)(i)]***
- the date on which the dividend was paid to the company was the date on which the dividend was paid to the trustee or partnership, or if applicable, to the first trustee or partnership in the chain. Where the rebate depends on the dividend having been paid after a particular time, the relevant particular time will be the day the dividend was actually paid to the first trustee or partnership, or if applicable, to the first trustee or partnership in the chain; ***[New paragraphs 45Z(1A)(j) and 45Z(3)(j)]***
- the share was issued to the company at the time it was issued to the trustee or partnership. For example, in determining whether an issue of shares is one to which section 46C or 46D applies, the day the shares were issued is the day they were actually issued to the trustee or partnership, or if applicable, to the first trustee or partnership in the chain; ***[New paragraphs 45Z(1A)(k) and 45Z(3)(k)]***

- where entitlement to the rebate depends on shares having been issued to another person, as in subparagraph 46D(2)(b)(i), the relevant time was the time the shares were actually issued to the other person; ***[New paragraphs 45Z(1A)(l) and 45Z(3)(l)]***
- factors relating to the payment of a dividend that are taken into account in determining whether the dividend is a debt dividend (for the application of section 46C or 46D), were those that relate to the dividend that was actually paid to the trustee or partnership, or if applicable, to the first trustee or partnership in the chain; ***[New paragraphs 45Z(1A)(m) and 45Z(3)(m)]***
- in determining the extent to which a dividend is paid from particular profits, the dividend to be examined is the dividend actually paid to the trustee or partnership, or if applicable, to the first trustee or partnership in the chain; ***[New paragraphs 45Z(1A)(n) and 45Z(3)(n)]***
- where it is necessary to determine whether the dividend is franked, the dividend was the actual dividend that was paid to the trustee or partnership, or if applicable, to the first trustee or partnership in the chain. These provisions will apply where a private company receives an unfranked dividend from another private company that is not part of the same wholly owned group of companies; ***[New paragraphs 45Z(1A)(o) and 45Z(3)(o)]*** and
- where the date on which the dividend was declared is relevant for entitlement to the rebate, the dividend was declared on the date the dividend that was actually paid to the trustee or partnership, or if applicable, to the first trustee or partnership in the chain, was declared. ***[New paragraphs 45Z(1A)(p) and 45Z(3)(p)]***

New subsections 45Z(1A) and (3) will extend entitlement to the rebate to dividends paid after 17 August 1976. The rebate will

not be denied in any assessment that issues on or after the day on which this Bill is introduced into Parliament. Also, a company will not be able to object against an assessment in which the rebate was denied, or obtain an amendment to that assessment, that issued before the day the Bill was introduced.  
*[Clause 66]*

### **Widely distributed finance shares**

The fourteenth amendment will make a technical correction to the widely distributed finance share measures contained in the Bill. The amendment will add the words "or more" after "75%" in subparagraph 327A(2)(b)(ii) of the public company test. This will ensure that all paragraphs of the test are consistent.

#### ***[Subparagraph 327A(2)(b)(ii)]***

It is clear from the other provisions of paragraph (b) and from the Explanatory Memorandum that the words in the provision should read as "75% or more". As with the widely distributed finance share provisions, this amendment will apply from the date the foreign source income measures commenced - generally 1 July 1990.

### **Deferral of deductions for trading stock purchases involving prepayments**

Clause 14 of the Bill will insert new subsection 51(2A) to defer deductions under section 51 for expenditure incurred by a person on stock that will become the person's trading stock, until the year of income in which the stock first becomes trading stock on hand of the person. The amendment only applies to stock that will become trading stock.

The amendment will overcome a weakness in the law that allowed for a mismatch of expenditure on trading stock and income from selling the trading stock. The mismatch occurred if, in a year of income, a person paid for stock intended to become trading stock, but that stock did not come on hand as trading stock until a later year of income. The person was able to get a tax deduction under section 51 for the cost of the stock in the year the expenditure was incurred. A compensating adjustment to account for unsold trading stock at the end of the year (which would have effectively deferred the deduction) could not be made in a case like this because the stock was not trading stock on hand at the end of the year. The ability to achieve a mismatch like this allowed people to obtain a tax advantage by bringing forward a tax deduction for trading stock that would not be sold until a later year.

Although the amendment proposed by clause 14 overcomes this deficiency, it could disadvantage a person who disposes of the stock before the year of income in which the stock becomes trading stock on hand. This could happen, for instance, where a person has incurred expenditure in respect of goods on order from a manufacturer and agrees to sell the goods before they are manufactured. The relevant goods become the trading stock on hand of the person when the person has the power to dispose of the actual goods. Under proposed section 51(2A), a deduction for the expenditure on those goods will be deferred until the year of income in which that happens. If the person has derived assessable income in relation to the disposal of the goods in an earlier year of income, there will be a mismatch which is the opposite of the mismatch that the amendment in clause 14 of the Bill sought to rectify.



To ensure that people are not disadvantaged, an amendment is proposed to new subsection 51(2A). The subsection will not apply to expenditure incurred on stock that will become trading stock unless some part of the stock has not become trading stock on hand by the end of the year of income in which the expenditure was incurred. Where the subsection does apply, a deduction is to be allowable in respect of each part of the stock, equal to the expenditure attributable to the relevant part, in the year in which :

- the relevant part of the stock first becomes trading stock on hand; or
- an amount of assessable income is derived in respect of the disposal of the relevant part of the stock;

whichever happens first. This means that a deduction for prepaid stock will not be deferred past the time when a person derives assessable income in respect of the disposal of that stock.