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Mr Stephen Dodshon
Acting Assistant Commissioner
International Risk and Projects, Public Groups
Australian Taxation Office

Email: Stephen.Dodshon@ato.gov.au

13 February 2024

Dear Mr Dodshon,

Amendments to the Thin Capitalisation rules – ATO's Public Advice and Guidance (PAG) consultation

CPA Australia is Australia's leading professional accounting body and one of the largest in the world. We represent the diverse interests of more than 173,000 members in over 100 countries and regions. We make this submission in response to the ATO's **Amendments to the Thin Capitalisation rules – ATO's Public Advice and Guidance (PAG) consultation** on behalf of our members and in the broader public interest.

In response to the ATO's request, we make the following comments in the table below for your consideration. We believe our comments would further improve the efficacy of the ATO's PAG on the amendments to the thin capitalisation rules.

Please refer to the Appendix for our detailed discussions. If you have any queries, contact Bill Leung, Tax Technical Advisor on (03) 9606 9779 or bill.leung@cpaaustralia.com.au.

Yours sincerely,

Ram Subramanian
Interim Head of Policy and Advocacy

Appendix

Detailed discussion

ITAA 1997 Provision	Issue	Priority
s815-140(1)(a)	**Interaction between thin cap and transfer pricing** In [PCG 2017/4] the ATO should seek to include safe-harbours for general class investors (e.g. simplified options for smaller taxpayers) relating to the quantum of debt borrowed to reduce compliance costs for smaller groups (e.g. consistent with simplified transfer pricing record-keeping options)	High
Division 820 Subdivision 820-EAA Part IVA ITAA 1936	**Application of Part IVA ITAA 1936** Recommend application of Part IVA to restructures in response to the new thin capitalisation rules (e.g. refinancing of pre-existing arrangements). As an example, does Part IVA (potentially) apply when taxpayers restructure or refinance, including pre-existing arrangements to not be caught by the new thin capitalisation rules, including the debt creation deduction rules?	High
s820-35	**The $2 million *de minimis* threshold** The $2 million *de minimis* threshold measures on a gross basis and it needs to change from a gross basis to a net basis given the introduction of a "net debt deduction" concept. This would prevent taxpayers from being caught where amounts are duplicated within a group and being counted twice. As an example, an amount borrowed and on-lent to a related party resulting in $1 million of interest on each leg of the back-to-back loan would result in $2 million total debt deductions in the group. Under a net debt deduction test there would more appropriately be $1 million of net debt deductions as the interest income derived by the interposed entity would reduce the $2 million gross amount to a $1 million net amount. The ATO will need to clarify how taxpayers can overcome this double counting problem.	High

ITAA 1997 Provision	Issue	Priority
s820-40(1)(a)(i)	**Guidance on meaning of "economically equivalent to interest"** There is no statutory definition or guidance regarding what constitutes an 'amount that is economically equivalent to interest'. Some examples to consider: • GIC/SIC are specific deductions under s 25-5(1)(c) covering tax-related expenses but do not arise out of financing arrangements. While the Government announced that these will be non-deductible from 1 July 2025 (which was one of the measures announced in the Mid-Year Economic and Fiscal Outlook 2023-24), there is still a requirement to consider if these are now to be debt deductions from 1 July 2023. • Short-term schemes otherwise excluded under **section 974-25** (i.e. those with a term of 100 days or less). • Vendors may offer a discount for prompt payment for goods/services. Should the customer not pay the discounted price, is the excess over the discounted price economically equivalent to interest?	High
s820-60(1)(b)	**Part year rule for general class investors** It is not clear how an entity can be a general class investor for part of an income year. Section 820-46(2) suggests that an entity will be a general class investor for an income year, and no provision is made for a part-year general class investor. Guidance should be provided explaining whether an entity needs to meet the inward or outward requirements for all of the income year or only a part of the income year, to be a general class investor. Further, guidance is required to explain what the consequence is. For example, if an entity only becomes an outward investor on the last day of the income year, are they considered a general class investor the whole income year with all debt deductions for that year subject to denial under Division 820?	High

ITAA 1997 Provision	Issue	Priority
s820-60(1)-(2)	**Effect of custodians on excess tax EBITDA rule** Many registered schemes hold their property via a custodian. This creates a further trust relationship. That custodian trust may not itself be a unit trust or managed investment trust. As a result, this may prevent a transfer of a trust excess tax EBITDA amount from subsidiary trust through to a parent trust where the custodian is regarded as a trust. We note that **section 276-115** covers this scenario for attribution managed investment trusts (AMITs). It applies if "a trust that is a custodian is a member of an AMIT in respect of an income year". In this case, subsection (3)(a) ignores the custodian and treats the underlying member as the relevant member of the AMIT. In the absence of such a provision, the ATO should confirm whether excess tax EBITDA amounts can be transferred to members of entities that hold their membership interest through a custodian. In particular, clarification should be provided as to whether such members are viewed as having a direct (rather than indirect) TC control interest in the controlled entity.	High
s820-427A(5)	**Third part debt test - development asset concession** The development asset concession has been expanded to cover not only the development of land assets (per the Bill) and certain incidental movable property (per the Exposure Draft), but also to cover certain offshore renewable energy infrastructure and offshore electricity transmission infrastructure. However, the development asset concession does not apply to certain onshore infrastructure development projects where the underlying assets are not land. For example, certain renewable energy projects do not qualify as interests in land, such that the development assets concession will not be available for the development of these projects. Is this understanding correct? If yes, the ATO will need to clarify how taxpayers can overcome this problem.	High

ITAA 1997 Provision	Issue	Priority
s820-427A(3)(c)	**Third part debt test - “minor and insignificant" assets** "Minor and insignificant" assets are to be disregarded in considering the assets to which the holder of the debt interest has recourse for payment of the debt. This is intended to address a concern that if an entity granted general security over all of its assets, and it had immaterial foreign assets, that it would automatically fail the base third party debt test. The Supplementary Explanatory Memorandum provides no clear guidance as to how "minor and insignificant" assets are to be determined, other than noting that it is intended to prevent the requirements being failed for "inadvertent and superficial reasons". To take an example, it is not clear whether disregarding minor and insignificant assets includes assets that are material in value but fleeting by reference to time – such as, for example, an asset consisting of material cash in a foreign bank account, that is then withdrawn after a short period into an Australian bank account. More generally, it is also not clear why this is not a permissible asset, given that the bank account would be expected to contribute towards the tax base of Australia (i.e., where it is interest earning). Similarly, and if the rule is intended to not result in the requirements being satisfied for "inadvertent and superficial reasons", it is not clear if long standing (but de minimis by value) assets could be considered to give rise to a failure for "inadvertent" reasons; certainly, the asset may be intended to be held for a long period (and in that sense the granting of security over it is not "inadvertent"), notwithstanding that it is not material by value.	High
s820-427(2)(e)(i) and (ii)	**Third party debt test – swaps** Clarification is required for what “directly associated” means in s427(2)(e)(ii). It is not clear how taxpayers are to show the swap is “directly associated” with hedging or managing interest rate risk in respect of a particular debt interest. As an example, if a borrower has issued two debt interests, one for $60 million, and the other for $40 million, and has also entered into an interest rate swap with a notional principal of $80 million, it is unclear how this rule applies and to show the swap is “directly associated” with hedging or managing interest rate risk in respect of that other debt interest.	High

ITAA 1997 Provision	Issue	Priority
s820-427(2)(e)(i) and (ii)	**Third party debt test – back to back swaps** The most common swaps in a conduit financing scenario are for the conduit financer to enter into a swap, and then to enter into back-to-back swap arrangements with the entities to which it is on-lending. These very common arrangements are not permissible under the third party debt test, because the back-to-back swap arrangements will result in debt deductions that are referable to amounts paid or payable to an associate entity. Accordingly, taxpayers will be required to enter into economically equivalent (but structurally different) arrangements by embedding swap-elements into the on-lending arrangements. This will likely result in income tax implications on closing out the back-to-back swap, and also has the potential to result in the conduit financer ceasing to be a pure conduit for income tax purposes (i.e., where it does not close out, at the same time, the third party swap arrangements). Given the substance of these arrangements are materially the same, it is unclear why the amendments have not facilitated the ordinary type of arrangements entered into in a conduit financing scenario.	High

ITAA 1997 Provision	Issue	Priority
s820-40	**Definition of debt deduction – interest rate derivatives** The proposed amendments remove the requirement for a nexus between the debt deduction and a debt interest issued by the entity and replaced with “calculated by reference to the time value of money” with “economically equivalent to interest.” In addition, there is a proposed amendment to subsection(3), which sets out amounts which are specifically excluded from the definition of debt deduction to remove “losses and outgoings directly associated with hedging or managing financial risk in respect of the debt interest.” Therefore, it appears that all flows under interest rate derivatives could be included in the definition of a “debt deduction” ,especially noting the comment at 2.159 of the Explanatory Memorandum. By removing the nexus between the deduction and a debt interest issued by the entity, the concern is that deductions on losses arising from circumstances entirely unrelated to a debt interest could be caught within the expanded definition of “debt deduction”. In the current form, the proposed rules do not permit a conduit financer to pass through the costs associated with managing foreign currency risk pertaining to the ultimate debt interest (the external loan) on behalf of the group. The way in which the proposed rules are currently drafted, the passing on of such costs would mean that a conduit financier would not be able to satisfy the third party debt test. There are two problems with the current drafting which lead to this result, or (in the case of the second) arguably lead to this result: 1. the cost of hedging foreign currency risk relating to a foreign currency denominated debt does not fall within the meaning of 'debt deduction', and 2. it is unclear whether the term *'hedging or managing the interest rate risk'* is a composite phrase or 'hedging' and 'managing interest rate risk' are separate exclusions. This wording creates uncertainty as to whether the hedging of foreign currency risks relating to debt would be able to be recovered by a conduit financier without breaching the conduit financier conditions. it is unclear whether the term used in the existing draft conduit financier rules *'hedging or managing the interest rate risk*’ is a composite phrase or whether each is a separate alternative – that is, whether the term is only referring to arrangements relating to interest rate risk or whether the term 'hedging' should be read as contemplating not only the hedging of interest rate risk, but also foreign currency risks.	High

ITAA 1997 Provision	Issue	Priority
s820-427(2)(e)(i) and (ii)	**Third party debt test – cross-currency swaps** Cross-currency interest rate swaps hedge interest rate fluctuations in a foreign currency. It is unclear if these debt deductions are available, as the arrangement goes beyond hedging or managing interest rate risk, that is, with the equal value principal amounts exchanged at the origin and maturity. For taxpayers who have borrowed in a foreign currency, cross-currency interest rate swaps are very common in this scenario.	High
s820-48(3)	**Cross staple arrangements and deemed TPDT choice may apply even where there is no managed investment trust (MIT)** The deemed choice for entities that have entered into cross staple arrangements may pick up private arrangements. The definitions in s 12-436, Sch 1 TAA just requires common (80%+) ownership of an asset entity and operating entity (i.e. one trading, one non-trading). While s 12-437 then makes certain income non-concessional MIT income (NCMI) of an asset entity that is a MIT, the concept of cross staple arrangement as defined does not require any of the entities to be MITs or even trusts. Therefore, this deemed choice may unintentionally capture private arrangements. For example, a family group may consist of a number of operating companies and a single unit trust that holds an investment property (that is leased to each of the operating companies). If the trust makes a TPDT election (e.g. because it is only financed by bank loan) this may result in the company also making a deemed election. We do not believe that this is outcome is intended. LCR 2020/2 (from paragraph 30) provides some guidance about the meaning of arrangement in the considering the meaning of ‘cross staple arrangement’. Guidance of this nature should cover the application of the concept to the new thin capitalisation rules and in particular to a broader variety of structures that do not involve MITs. It is noted that “the object to the measures” is stated to be one of the factors that regard should be had to, at paragraph 34 of LCR 2020/2.	High

ITAA 1997 Provision	Issue	Priority
s820-60(4)	**Attribution of excess tax EBITDA amount by loss trusts** The modification to section 351, by treating references to “greater of those percentages” to “lesser of those percentages”, can result in an unintended outcome where a trust does not have actual income for the year (i.e. a loss year). If a trust has no income for the year of income, then the share of income to which beneficiaries are entitled may be considered to be nil. This type of risk is acknowledged in section 152-78(2) for the purpose of the small business CGT concessions. This may not impact a section 351 calculation, as the provision ordinarily requires the greater of the income and corpus percentages to be calculated (thus allowing one to count the capital rights). However, where a “lesser of those percentages” is adopted, this could have the unintended outcome of attributing no excess to controlling interest holders in loss years. ATO guidance should clarify whether a controlling entity can be taken to hold a direct control interest in a trust for these purposes where the trust has no distributable income for a year.	High
s820-52 and s820-60	**Excess tax EBITDA and CGT discount** Where a trust (the underlying trust) disposes of a property and distributes a net capital gain to another Australian trust (the holding trust), the calculation of the tax EBITDA for both the underlying trust and the holding trust would be based on the discounted capital gain (and not the gross capital gain). This effectively results in the tax EBITDA being determined based on 50% of the gross capital gain realised by the underlying trust. Where the net income of the trust is ultimately assessable to foreign investors and subject to managed investment trust (MIT) withholding tax (or other taxpayers that do not qualify for the CGT discount, such as companies), an anomaly arises because the investors are liable to pay tax on the gross capital gain (excluding the CGT discount), but the debt deduction for interest is capped at 30 per cent of the discounted capital gain. This could effectively result in a taxpayer’s “fixed ratio earning limit” being reduced by up to 50 per cent of the intended amount. The above outcome for trusts is contrasted to where an underlying company disposes of a property. In this case, the excess tax EBITDA calculation would be determined based on 100 per cent of the gross capital gain. This effectively allows the company’s debt deductions to be determined based on the full capital gain and increase both the tax EBITDA and the excess tax EBITDA amount for the company (as compared to a trust). Is this understanding correct? If yes, the ATO will need to clarify how taxpayers can overcome this 50 per cent discount problem.	High

ITAA 1997 Provision	Issue	Priority
s820-427A(3)(c)	**Whether recourse requirement is tested on an actual or hypothetical basis** It is not clear whether recourse to Australian assets needs to be expressly limited in the terms and conditions of any loan agreement or whether this condition can be satisfied by the borrower (and/or obligors) by merely not holding any of the excluded assets during the relevant income year? Many taxpayers would be relying on satisfying this condition on the basis that they hold no foreign assets even though they have entered into a loan agreement that does not limit recourse to Australian assets only (i.e. if the entity were to acquire a foreign asset, then the lender would have recourse to that asset). In practice, third party lenders are unlikely to limit their rights as a creditor only to Australian assets and taxpayers would instead ensure they do not hold foreign assets in order for their borrowings to meet the third party debt conditions. The ATO should clarify whether the recourse requirement is satisfied where an entity holds no prohibited assets despite the terms of the borrowing not expressly limiting the lender's recourse in any way.	High
s820-427A(3)(c)	**Meaning of 'Australian assets'** There is no definition of "Australian assets" and this is likely to cause significant uncertainty, particularly where assets are intangible assets (e.g. financial instruments, membership interests in other entities, etc). There is an existing definition of "average Australian assets" in section 820-37(1)(a) but that definition is not one that applies for the purposes of Division 820 more broadly. ATO guidance should explain what is considered to be an Australian asset for purposes of the third party debt test. Does it require an active business to be undertaken in Australia? What about passive investments in Australia, does it satisfy 'Australian assets'?	High
Subdivision 820-EAA	**Meaning of mere restructuring** The Supplementary Explanatory Memorandum indicates that schemes involving a "mere restructuring" of an arrangement that would otherwise be caught by the debt deduction rules is permitted, provided there is no associated artificiality or contrivance. Guidance and examples are needed from when mere restructuring is permitted to when it is associated with artificial or contrivance.	High

ITAA 1997 Provision	Issue	Priority
Subdivision 820-EAA s820-427A(3)(d)	**Cash pooling - intermingling of Funds** Significant issues arise with applying these debt creation rules in practice given the test time for deductibility of interest on debt under general principles is the time at which the borrowing is entered into. The third-party debt condition (para 820-427A(3)(d)) require that the entity uses all, or ‘substantially all’ of the funds borrowed to fund its commercial activities in connection with Australia. Where a group has foreign assets, this is a significant compliance burden. Group borrowing is generally comingled, it is not always specifically possible for a business to narrowly trace the purpose of a borrowing particularly where funds are used for normal commercial transactions in the context of the day to day running of a business. For example, with one bank account being used to fund the cash-flow requirements arising from multiple ordinary business activities. Borrowings which were incurred in the course of carrying out these ordinary business activities have been intermingled within the one bank account. Under the proposed of the debt creation rules, it will be necessary to somehow track through one bank account the multiple uses of the borrowed funds (including the acquisition/holding of trading stock) and identify the debt which relates to non-deductible purposes in order to determine the debt which gives rise to non-deductible interest. There are practical difficulties with regards to tracking multiple transactions or funds through a single bank account. The ATO will need to provide clear guidance and examples as to how, practically, a business could be expected to determine their position under these rules when one bank account is used to fund many ordinary business transactions but, under the proposed rules, interest on any borrowings to fund some of these ordinary business transactions will need to be separately identified and treated as non-deductible. Given the rules are to have this retrospective effect, guidance and examples from the ATO are needed as to how a business might actually implement such a historical review. This is given the practical complexity of reviewing thousands of historical transactions going back many years to try and identify any borrowing which will now have a non-deductible purpose under the proposed debt creation rules, even if they are genuine commercial transactions.	High
Subdivision 820-EAA	**Conduit financier** As an example: If an entity borrows from a conduit financer (i.e., ultimately sourced from a third party), and makes a lease payment to an associate entity, that would arguably be similar to a payment of a royalty and is for the use of an asset As such, does the debt deduction creation rules apply? If yes, that means debt deduction is denied where there is no mischief. In the example given, the payment would be treated as assessable income and subject to tax, and the ultimate source of the funding is from a third party.	High

ITAA 1997 Provision	Issue	Priority
s820-49	**Scope of obligor group for trusts and partnerships** Trustees are personally liable such that all their assets are at risk. Normally a creditor would only have rights to be subrogated to trustee's right of indemnity such that they would only have recourse to assets forming the trust estate where there is no breach of trust. Any other trust estates with the same trustee would not have their assets exposed. However, the creditor would still have recourse to the trustee's personal assets. For a $2 corporate trustee this would include those $2. As such there would be a recourse rule unless specific clauses in the loan contract limit the recourse to assets belonging to the trusts. Does the operation of the general law of trusts that makes trustees personally liable for obligations incurred result in the trustee generally being a member of the trust's obligor group? If the trust is required to lodge an income tax return (e.g. because it acts in its own right as well as in a trustee capacity), does this therefore result in the trustee being deemed to make a TPDT choice if it is a general class investor? For partnerships the same issue arises as partners are jointly and severally liable. Even for limited partnerships (which is deemed to be a company) there should be one general partner whose own assets are at risk and such assets do not belong to the entity that is the limited partnership (or deemed company). Do these principles generally result in partners being members of the partnership's obligor group and, where the partner is a general class investors deemed to make a TPDT choice?	Medium
s820-49	**Scope of obligor group where borrowing entity has subsidiaries** Clarity is required to understand when subsidiaries would be considered to be members of the obligor group of its parent entity. Where the borrower holds membership interests in subsidiaries, the lender may take possession of its assets and therefore take control of a subsidiary and ultimately cause the subsidiary to sell its assets and distribute the proceeds to the parent (or distribute the assets to the parent in-specie). This may depend on the nature of any of security provided by the parent entity. Guidance should be provided so that groups understand if and when subsidiary entities may become part of the parent entity's obligor group even if the subsidiary does not provide any direct security for the parent's borrowings.	Medium

ITAA 1997 Provision	Issue	Priority
s820-60(3)	**Excess tax EBITDA amounts where entities have different accounting periods** The trust excess tax EBITDA does not specifically consider the situation of a controlled entity having a Substituted Accounting Period that does not align to the controlling entity's income year. For example, is a notional calculation for the controlled entity necessary in such situations? Or is it the case that the controlling entity's excess tax EBITDA amount is based on the controlled entity's tax EBITDA for the income year that ends during the controlling entity's income year (even if the two year are not aligned)? The ATO should provide guidance on how the rules operate in these circumstances.	Medium
s820-52(6B)(a)	**Effect of the same circumstances rule on members of AMITs for tax EBITDA purposes** The "same circumstances" rule in s 276-80(2)(b) has the effect of putting the member into the shoes of the trustee. Refer to paragraph 8 of LCR 2015/6. Examples 2 and 4 of the LCR make it clear that section 276-80 does not assess members of AMITs, but instead the underlying provision that would apply if the amount was derived directly does (e.g. section 6-5 for interest income and section 44 for dividend income). For example, if an entity holds less than 1% of an AMIT and the AMIT holds a 10%+ shareholding interest in a company, the effect of the same circumstances rule could be interpreted to mean that the member of the AMIT may be treated as having received a dividend from a company in which it holds a 10%+ interest. This could result in that dividend income being excluded from the member's tax EBITDA under s 820-52(3). This outcome would appear to be inconsistent with the proposed amendments. A similar outcome would arise for small investors in AMITs (i.e. less than 10%) if the AMIT holds interests of greater than 10% in partnerships or other trusts. In addition to outcomes identified above, this could also result in significant compliance costs for AMITs as they would then have to separately track and report amounts that are referable to distributions from subsidiary trusts, companies and partnerships in which they hold an interest of 10% or more. Such amounts may become 'characters' that are required to be treated differently from other amounts due to the effect that they have on the tax treatment of its members. The ATO should clarify if this is indeed how the rules operate and whether AMITs will be required to report 'characters' in respect of the determined member components that include the AMIT's income from associate entity distributions.	Medium

ITAA 1997 Provision	Issue	Priority
s820-52(9)	**When to test associate entity relationship** The concept of associate entity in section 820-905 is tested "at a particular time". However, the rules in subsections 820-52(3), (6), (6B) and (8) do not specify <u>when</u> an entity must test whether a company, trust, AMIT or partnership is an associate entity. This may lead to uncertainty where a shareholder, beneficiary or partner is not an associate entity of a company, trust or partnership for the entire income year. For example, if the test is met for one day during the income year, clarity is required as to whether the test is satisfied for the entire income year or period. We also note other provisions may require clarification as to when the associate entity relationship must be tested. These are the provisions that rely on: - Section 820-48(2) - Section 820-54(5) - Section 820-427D	Medium
s820-52(6)(b) 820-52(6B)(b)	**Further clarity on the effect of disregarding distributions** Paragraph 1.16 of the Supplementary EM states that this amendment is to ensure distributions from trusts that are associate entities are disregarded in calculating tax EBITDA in the event they are considered ordinary income under section 6-5 in the hands of the beneficiary or member. We believe a broader interpretation of these provisions could also have the effect of disregarding the CGT consequences of trust distributions (e.g. capital distributions). A distribution by a unit trust could result in CGT event E4 or E10 occurring for the member. The ATO should confirm that disregarding distributions does not exclude the effect of the distribution on the operation of Part 3-1 of the ITAA 1997 (i.e. the CGT provisions) such that distributions resulting in capital gains under CGT event or E4 or E10 are not excluded from tax EBITDA.	Medium

ITAA 1997 Provision	Issue	Priority
s820-56(1)(b)	**Clarify that negative net debt deductions increases the excess amount** It should be clarified that the excess of an amount over a negative amount results in that excess increasing. This would be a similar view to that contained in ATO ID 2002/942. For example, an entity derives $100,000 of interest income during the year and nothing more. This should result in: Tax EBITDA being nil due to $100,000 of taxable income (being the starting point under s 820-52(1)(a)) being reduced by $100,000 by adding an amount of negative $100,000 (at s 820-52(1)(b)) and The FRT limit of nil (i.e. tax EBITDA of nil x 30%) exceeding the amount of debt deductions by $100,000 for the purpose of section 820-56(1)(b) (i.e. nil exceeds negative $100,000 by $100,000). Further, if the entity also derived $100,000 of sales income, its FRT limit should be $30,000 (i.e. tax EBITDA of $100,000 x 30%) and this should exceed its debt deductions (of negative $100,000) by $130,000.	Medium

ITAA 1997 Provision	Issue	Priority
s820-52(1)(c)	**It is not clear what a deduction for "an entire amount of an expense incurred" is** This is a difficult concept to easily carve out of Division 40 given the variety of mechanisms in the Division. Division 40 provides deductions for some items based on the "decline in value" of depreciating assets via section 40-25 with some provisions deeming the decline in value to be the entire "cost" (e.g. section 40-80) or the entire amount of "capital expenditure" incurred (e.g. s 40-540, 40-548, 40-551). Note the use of "expenditure" rather than "expense". Other provisions directly provide deductions for capital expenditure (e.g. generally those in Subdivisions 40-G, 40-H, 40-I and 40-J). Within those Subdivisions, some expenditure is immediately deductible (e.g. 40-H items, some 40-G items) with others providing deductions over time (e.g. 40-I and 40-J). Arguably any "decline in value" deductions aren't deductions for an amount of "expense". Other deductions such as s 40-880 may also be considered deductions for the entire amount incurred (just spread over 5 years). There are also difficulties where some provisions have a "to the extent" test such as s 40-735. If the provision provides a deduction for 99% of an amount incurred due to a 99% nexus than it would not have provided a deduction for the "entire" expense and therefore would not be covered by this exclusion. An approach similar to that taken in respect of the "once-only deduction" concept in FBT may be appropriate. Refer to sections 19, 24, 44 and 52 of the FBTAA 1986 where it is used and section 136 for its definition. TD 93/46 provides some ATO guidance on this concept and clarifies that the term "once-only deduction" means a deduction that is wholly or partly allowable in one year for the expenditure and not in any other year, with a deduction spread over more than once year, <u>such as depreciation on equipment with a life of more than one year… would not be a once-only deduction.</u> Consistency with TD 2023/6 should also be considered as this tax determination explicitly considers what is an "expense incurred", in a different context, being the ESIC provisions, and suggests this is an accounting concept. This may mean that depreciation is never "incurred" and also suggests that if for accounting purpose that capital expenditure is not full expense then it won't be an "expense incurred". This may mean the exclusion for "entire amount of expense incurred" is extremely limited if this view is taken for the purpose of section 820-52(1)(c).	Medium

ITAA 1997 Provision	Issue	Priority
s820-52(6)	**Effect of disregarding Subdivision 115-C on tax EBITDA** Subdivision 115-C only deems an extra capital gain, rather than including amounts in assessable income. For example, if a taxpayer has a direct capital gain of $100 and an indirect capital gain (via Subdivision 115-C) of $100 and has $100 of capital losses, if the taxpayer <u>actually</u> chose to apply the capital loss against the 115-C gain under Step 1 in section 102-5, does the “disregarding” of 115-C then deem the application of the capital loss against the direct gain (i.e. because there would be no other gains to apply to the capital loss to) such that tax EBITDA is reduced by $100? Alternatively, because the actual net capital gain only consisted of the direct capital gain that remained after applying capital losses against the 115-C gain, the effect of the disregarding of Subdivision 115-C is that the $100 net capital gain remains and constitutes tax EBITDA. The effect of disregarding Subdivision 115-C should be clarified. There may need to be a product that clarifies the interaction similar to TD 2023/D1 which considered the interaction between the NALI provision and the CGT rules.	Medium
s820-60(1)(c)-(d) & (2)(c)-(d)	**Whether excluded entities can attribute excess tax EBITDA** An entity must be a general class investor and not using the GRT or TPDT in order to be either a controlling or controlled entity for the purposes of the excess attribution rule. However, it is not necessarily the case that entities to which sections the 820-35, 820-37 and 820-39 exemptions apply are not able to be controlling entities or controlled entities for these purposes. These exclusions only apply to prevent certain Subdivisions from disallowing debt deductions. They do not switch off the application of Division 820 more broadly (i.e. they may still be general class investors). The guidance should clarify the interaction between the general class investor requirement and exclusions in sections 820-35 to 820-39.	Medium
s820-60(1)(a)(i)	**Resident trust for CGT purposes for holding trusts** A resident trust for CGT purposes has to have property of the trust situated in Australia or carry on a business in Australia. A trust that is a mere holding trust may not be considered to carry on a business. Further if the trust merely holds units in subsidiary trusts or shares in companies, it is not clear whether those units or shares are “situated in Australia”, even if the subsidiaries are themselves Australian. The ATO should clarify whether such holding vehicles would be eligible to be controlling entities for the purposes of the excess tax EBITDA rule.	Low

ITAA 1997 Provision	Issue	Priority
s820-47(6)(c)(ii)	**Past year due dates for lodgement** The time limit to apply for a revocation is proposed to be the earlier of 4 years after lodgment of the income tax return and 4 years after the day the entity was required to lodge its income tax return. It is difficult for taxpayers to know when their lodgment due date was 4 years in the past (as opposed to the date they actually lodged), especially where extensions were granted and there has been a change in tax agent. The ATO systems do not allow for historical tracking of lodgment due dates. The ATO should explain how taxpayers can establish past year due dates (e.g. will screenshots from the ATO portal be sufficient?).	Low
s820-60(3) Step 1(b)	**Effect of unusable FRT disallowed amounts on excess tax EBITDA amount** The method statement requires the controlled entity to reduce its FRT earnings limit by the total of its carry forward FRT disallowed amounts. It is not clear how this applies where the trust or company's FRT disallowed amounts could not be deducted under section 820-56 because the controlled entity fails to pass the loss rules. Section 820-59(3) deems the FRT disallowed amount to be zero if s 820-59(4) or (5) applies, but only for a limited purpose, being to determine the amount that can be deducted in that later year. The FRT disallowed amount still exists until the 15-year time period expires and may be deductible in a later year. This "deemed zero" treatment may not extend to the application of section 820-60. Accordingly, Step 1(b) may be interpreted as requiring a subtraction for all prior year FRT disallowed amounts the controlled entity continues to carry forward, even where they may not be deductible. By way of contrast, section 820-58 deems those amounts to be zero for all later income years where a group ratio test or third party debt test choice is made. ATO guidance should explain whether unusable FRT disallowed amounts have the effect of reducing the excess tax EBITDA amount or whether they are deemed to be zero for this purpose.	Low
s820-60(4)-(6)	**Effect of the "entitled to acquire" rule in sections 350 and 351 and 820-865** It may be possible for the total of TC direct control interests held in a controlled entity to sum to more than 100% if members hold options to acquire interest in addition to holding membership interests. The ATO should provide guidance as to how the "entitled to acquire" rule interacts with the attribution of excess tax EBITDA amounts.	Low

ITAA 1997 Provision	Issue	Priority
s820-46(3)(a) s820-53(1)	**Meaning of "corresponding" for the purposes of the group ratio test** Unclear what it means for a period to "correspond" to an income year where the period for accounting purposes does not align to the income year. Where there is a six-month overlap (e.g. 31 December period but 30 June income year) it is not clear which period corresponds (e.g. the period where the first half falls within the income year or where the second half falls within the income year).	Low
s820-53(2) s820-55(3)	**Single entity rule and GR Group** It is not clear if a GR Group can consist of a single tax consolidated group. Para 2.35 of the EM suggests one entity cannot be a GR Group, but it is unclear if this is on the basis of the single entity rule applying (i.e. is a tax consolidated group consisting of three companies one entity or three entities for these purposes?) It is also unclear what the effect of the single entity rule is in disregarding specific entities with negative EBITDAs? Does a taxpayer have to consider each subsidiary member's EBITDA on an entity-by-entity's basis? Does it matter if the entity for which the group ratio is being determined is itself a member of the tax consolidated group or whether the entity is not a member of the group (but is part of the same GR group as members of a tax consolidated group). For example, there could be a GR group consisting of two tax consolidated groups with a common foreign parent entity. There may be different group ratios for each taxpayer if the single entity rule applies in a different way for each taxpayer.	Low
s820-54(2)	**Meaning of "third party" interest expense** It is not clear why the words "third party" are used in reference to interest expenses and interest income. The consolidated financial statements should already ignore intra-group amounts and will instead, simply disclosure interest income or interest expenses. What meaning is to be given to "third party" when applying these rules?	Low

ITAA 1997 Provision	Issue	Priority
820-54(2)	**Treatment of capitalised interest expenses for group ratio purposes** Paragraph 134 of the OECD's BEPS Action 4 report states that capitalised interest is to be specifically adjusted for in the net third party interest expense and may be recognised "in the period where the interest is incurred, or as it is amortised over the life of the related asset". It is unclear if the current modifications in s 820-54(1) are intended to specifically include capitalised interest in the year they are incurred as "amounts that are economically equivalent to interest" despite the amounts not being recognised as expenses in the year they are incurred. If amounts of capitalised interest are not included in full in the year they are incurred they would not appear to be captured in later years as they would not be disclosed as interest expenses in those years. Rather, they may be treated as amortisation expenses and instead added back to increase the group EBITDA (denominator) and this reducing the group ratio without ever being including group's net third party interest expense (the numerator). For example, $100 of capitalised interest expense in year 1 should result in $100 in the numerator and $100 added back to group EBITDA in denominator. When the $100 is amortised over its life it should NOT be added back to group EBITDA as this would unfairly reduce the ratio. Therefore, it should be clarified that net third party interest expenses should include amounts of capitalised interest incurred during the period.	Low