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THE PARLIAMENT OF THE COMMONWEALTH OF AUSTRALIA

HOUSE OF REPRESENTATIVES

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TAXATION LAWS AMENDMENT (DROUGHT RELIEF  
MEASURES) BILL 1995

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EXPLANATORY MEMORANDUM

(Circulated by authority of the Treasurer,  
the Hon Ralph Willis, MP)







## ***Table of contents***

**General outline and financial impact..... 1**

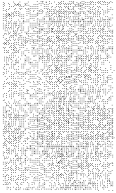
### **Chapter**

*1 Drought investment allowance..... 3*

*2 Farm management bonds..... 33*

**Index..... 37**





## ***General outline and financial impact***

### **Drought investment allowance**

Amends the income tax law to provide for a deduction of 10% of the capital expenditure incurred on fodder and water storage facilities, water conveyancing facilities and minimum tillage equipment which satisfy the criteria of the drought investment allowance.

***Date of effect:*** 24 March 1995

***Proposal announced:*** 8 December 1994 and 23 March 1995

***Financial impact:*** \$15 million for 1996-97, \$10 million for 1997-98. Financial impact for 1995-96 cannot be estimated accurately but is likely to be no greater than \$10 million.

***Compliance cost impact:*** There will be no additional compliance costs relating to the allowance to acquire fodder storage facilities or minimum tillage equipment.

In addition to their normal records, taxpayers who claim the allowance for water storage facilities and water transport equipment will need to have a water conservation plan in place. The water conservation plan will add to their costs.

Advisers should readily identify eligible expenditure and so taxpayers should not incur additional costs for return preparation. The new provisions have been written in a more explanatory drafting style using features developed by the Taxation Law Improvement Project. This should make them easier to understand.

### **Farm management bonds**

Amends the *Loans (Income Equalization Deposits) Act 1976* to make farm management bonds (FMB) more attractive investment vehicles for farmers. The 'default' investment component of FMBs is increased to 100%, the maximum amount of FMBs is increased to \$150,000 for each farmer, withholding tax on withdrawal of FMBs is eliminated, and the

treatment of FMBs where a farmer ceases to be engaged in primary production is brought into line with other repayments unrelated to serious financial difficulties.

***Date of effect:*** Royal Assent

***Proposals announced:*** 8 December 1994 and 23 March 1995

***Financial impact:*** \$6 million over the next four years.

***Compliance cost impact:*** There will be no change in the level of compliance costs imposed on primary producers making deposits in FMBs.

## **Drought investment allowance**

### **Overview**

1.1 *Schedule 1* of the Bill will make various amendments to the *Income Tax Assessment Act 1936* (the Act) to provide for an investment allowance of 10 per cent for capital expenditures of up to \$50 000 per taxpayer in each year the allowance is claimed on fodder storage, water storage for live stock, water conveyancing and minimum tillage equipment.

### **Summary of the amendments**

#### **Purpose of the amendments**

1.2 The purpose of the amendments is to encourage farmers throughout Australia to prepare for future droughts by providing incentives to invest in fodder and water storage for livestock, in water conveyancing, and in minimum tillage equipment, so as to encourage drought mitigation by sustainable farming practices. [*Subsection 625(1)*]

#### **Date of effect**

1.3 The amendments will apply to capital expenditure incurred on fodder and water storage facilities, water conveyancing facilities and minimum tillage equipment after the date of announcement. This is in accordance with the joint Prime Minister's and Minister for Primary Industries and Energy's Press Release (No. 3891) of 8 December 1994 on Additional Drought Relief, and the Treasurer's Press Release No 31 of 23 March 1995 on Drought Preparedness Taxation Incentive.

### **Background to the legislation**

1.4 These measures are part of the Government's drought assistance package which recognises that drought is a feature of Australian farming.

The current drought shows the need for measures that enable farmers to prepare better for drought, and so survive without undue hardship.

1.5 Due to the adoption of features of the improved drafting style for the taxation laws, this new investment allowance is drafted as a Part of the Act, rather than a Subdivision. The improved drafting style groups sections into larger units and uses subdivisions as the smallest grouping unit above sections.

1.6 This legislation has many policy features in common with the general investment allowance which terminated on 30 June 1994. The new provisions have been reordered so that they flow more logically.

## **Explanation of the amendments**

1.7 **Item 1 of Part 1 of Schedule 1** of the Bill will introduce *new Part XII* into the *Income Tax Assessment Act 1936*. These amendments will provide incentives to Australian primary producers through the 'drought investment allowance'. The proposed drought investment allowance will provide for a deduction of 10% of capital expenditure incurred on buying or constructing:

- fodder storage facilities;
- live stock drinking water storage facilities (including dams and tanks);
- all water transport facilities (including bore reticulation); and
- minimum tillage equipment.

## **Object, key principle and overview**

1.8 The object of these amendments is to provide a tax incentive, that is in the form of a tax deduction, to encourage primary producers and lessors of property to primary producers to invest in drought mitigation property. **[New subsection 625(1)]**

1.9 The key principle gives a broad picture of the area of law with which it deals and sets a framework from which the reader can understand and identify the detailed rules.

1.10 In relation to this new Part, the key principle summarises the effect of the Part which creates a deduction in the form of drought investment allowance provided various eligibility criteria are satisfied. **[New section 626]**

1.11 Expenditure must be at least \$3,000 on any item. The item must be drought mitigation property. The item must be for use in producing



assessable primary production income. Then drought investment allowance of 10% of the expenditure applies. The allowance is limited to a total of \$5,000 for the drought mitigation property first used or installed ready for use in the year the allowance is claimed.

1.12 An overview of the Part enables the reader to locate the Divisions containing those provisions which are of immediate relevance, and alerts the reader to any other Divisions which may also be of use.  
*[New section 627]*

## Key concepts

1.13 The new provisions refer to 'drought mitigation property'. This property is first mentioned in the object clause and is defined in *new section 650 in Division 4* which contains the key concepts for this Part.

### Drought mitigation property

1.14 Fodder storage facilities, water storage facilities, water transport facilities and minimum tillage equipment are the four kinds of drought mitigation property, to which the allowance applies. *[New section 650]*

#### *Fodder storage facilities*

1.15 Any buildings or structures, acquired by or constructed by or on behalf of the primary producer, will be drought mitigation property if those buildings or structures are for use for the storage of grain, hay or fodder. The need for this sort of storage has increased over recent years.  
*[New section 651]*

#### *Water storage facilities*

1.16 In drought, primary producers need stored water for livestock, and may need that water at several appropriate points. Facilities for use on the particular farm in storing water mainly for livestock are water storage facilities, and so drought mitigation property, provided their use is in accordance with an approved water conservation plan. These facilities are listed as including dams, earth tanks, underground tanks, or above ground tanks, or the bases, stands or covers of these tanks, or any other structures or improvements. *[New subsection 652(1)]*

1.17 Because water must be stored predominantly for livestock, a facility will not qualify as drought mitigation property if it stores water mainly for other purposes, such as domestic use or irrigation of crops. However, some use of water for other purposes is consistent with water being stored mainly for livestock.

***Water transport facility***

1.18 Water is more useful in a drought if it can be moved around the primary producer's land to the place where it is needed most. Facilities for use on the particular farm in transporting water are water transport facilities, and so drought mitigation property, provided the use is accordance with an approved water conservation plan.

1.19 Water transport facilities include bores or wells, pumps or windmills, pipes or water towers or header tanks or other structures or improvements that are used on particular land for transporting water. These facilities can help move water where it will be of most benefit, and can ensure there is as little waste as possible. The water may be for any primary production use, not just for livestock *[new subsection 652(2)]*. Capital expenditure on vehicular water tankers is not eligible for this allowance, as they are neither structures nor improvements.

***Water conservation plan***

1.20 The use of any water storage and transport facilities should be in accordance with an approved water conservation plan. Approval of this plan must be in writing and may be given by an officer of a water conservation agency or an approved farm water resource consultant. *[New subsections 653(1), (3) and (4)]*

1.21 Such a plan describes the location and nature of any water storage facilities or water transport facilities for which the allowance is to be claimed. It describes the way in which the facilities will effectively improve the drought preparedness of the land on which they are to be used and of the natural environment of which that land forms part. It describes the way in which the facilities will avoid any significant adverse effect on water quality or availability in other areas.

1.22 An approved water conservation plan would best be part of a broader process of property management planning, as would an approved land management plan for the purposes of section 75D of the Act. Water conservation that is part of such a broader process is likely to produce the greatest benefits for the primary producer, because it will be integrated with other improvements in carrying on primary production. The Government's preferred method of integration is through property management planning which integrates natural resource information with the nature conservation and production aspects of a property into a management plan. Some of the costs involved in preparing a property management plan may be deductible under section 75D (land degradation) or section 51(1) (deductions of normal business expenses including monitoring and updating). Several government-funded training programs are available to encourage the adoption of property management planning. Landholders are encouraged to incorporate their water conservation plan

into a broader property management plan; however, a water conservation plan need not be part of a larger process. *[New subsection 653(2)]*

1.23 Some ways of improving drought preparedness include the use of water storage facilities or water transport facilities to water stock closer to available pasture or hand feeding sites (to reduce land degradation), to water stock away from waterways and enable them to be excluded from waterways (to protect riverbanks, vegetation, and water quality), and to reduce wastage of surface or ground water by conveying water more efficiently (for example, in pipes rather than open channels where appropriate).

1.24 The areas beyond the land, and things on the land other than the soil, that are included in the natural environment of which the land is a part have various connections to the land. For instance, the land may be part of a common catchment area, or may draw on a common aquifer. There may be areas affected by windblown soil from the land, or other erosion. Uncultivated areas may include vegetation and animal populations; and there are other possible connections to the land.

1.25 Even if adverse effects are limited or exceeded by benefits for drought preparedness, a water conservation plan cannot be approved unless there is no significant adverse effect of the water storage facilities or water transport facilities on either the availability or the quality of water elsewhere. Adverse effects can arise, for example, where water storage or transport will substantially reduce the availability of water elsewhere (for instance, by taking too much of a river's flow or of an artesian basin's reservoir). Some forms of water transport can contribute to overland flooding or water logging, or salinity problems elsewhere by their effect on a water table, and so have a substantial adverse effect on water quality.

1.26 The process of approval of water conservation plans by appropriate people ensures that conservation plans will achieve real gains for drought preparedness, without significant cost elsewhere. Good plans will weigh up the relevant factors, seeking a proper balance between costs and benefits of particular water storage facilities and water transport facilities. Professional approval will give the opportunity for appropriately qualified and experienced people to contribute improvements to plans. It will improve the balance between benefits and costs, and will ensure that proposals that have no net benefit for drought preparedness, or that cause significant harm to water availability or quality elsewhere, are not approved. *[New subsection 653(2)]*

#### ***Water conservation agency***

1.27 A water conservation agency will be a State or Territory Government department or authority which has the responsibility for the management of water resources. This is not restricted to departments or authorities which have this as their sole or predominant responsibility. If

the responsibility is shared between agencies, there could be more than one such agency in a particular State or Territory; however, the State or Territory is likely to decide which agency is to give such approvals. **[New subsection 653(3)]**

#### ***Farm water resource consultants***

1.28 Persons may be approved as farm water resource consultants by the Secretary to the Department of Primary Industries and Energy or the Secretary's authorised delegate. The following matters must be considered before the approval is given: the qualifications, experience and knowledge of the person in relation to the management of water resources on land used for primary production, the standing of the person in the professional community, and anything else that is relevant. **[New subsections 653(5) and (6)]**

1.29 Someone whose approval as a farm water resource consultant is refused or revoked by the Secretary to the Department of Primary Industries and Energy or his authorised delegate can have that decision reviewed by a tribunal under the *Administrative Appeals Tribunal Act 1975*. The proposed provisions need not specifically state that the Secretary to the Department has the power to revoke an approval as a farm water resource consultant, as this power is available by virtue of section 33 of the *Acts Interpretation Act 1901*. **[New subsection 653(7)]**

1.30 Farm water resource consultants need the capacity to ensure that water storage and transport facilities do contribute to more effective availability and use of water, and do not make that improvement at the cost of off-farm environmental damage to water quality or availability.

#### ***Minimum tillage equipment***

1.31 Minimum tillage equipment must be for use in planting and cultivation. (Equipment for other uses is unlikely to involve any degree of tillage, and so there is unlikely to be any "minimum tillage" form of the equipment to encourage.) When it is used for planting and cultivation, it involves no tillage of the soil, or, if it does involve tillage, it does not seriously affect the soil structure, which retains a high degree of organic matter or of surface cover. **[New subsection 654(1)]**

1.32 The purpose of including capital expenditure on minimum tillage equipment in the drought investment allowance is to encourage farmers to purchase such equipment because its use will ensure that both organic matter and moisture are preserved in the soil. This can greatly reduce the need for water and the effect of drought.

1.33 Legislative examples of minimum tillage equipment to which the drought investment allowance would apply include trash tillage implements, boom sprays and markers, zero and reduced tillage planters,

trash seeders, deep ploughs and seed drills. Types of agricultural equipment excluded from being eligible for the drought investment allowance include, as examples in law, one way disk ploughs, mouldboard ploughs, offset disc ploughs, tined tillage and seeding implements with a low capacity for trash clearance, rotary hoes, tined harrows and rollers that compact the soil significantly. The general definition of minimum tillage equipment should be applied in the light of these examples, which were provided by representatives of primary producers. *[New subsections 654(2) and (3)]*

### **Eligibility criteria for drought investment allowance**

1.34 To obtain the drought investment allowance several criteria must be satisfied. These are imposed so that the provisions will actually benefit those whom the drought investment allowance is designed to assist.

1.35 There are two types of taxpayers who are eligible for this allowance, primary producer taxpayers who will own the drought mitigation property and taxpayers which are leasing companies and lease drought mitigation property to primary producers. Primary producers who own the drought mitigation property will be dealt with first.

#### **Primary producers**

1.36 Primary producers must incur capital expenditure of at least \$3,000 on a new item of drought mitigation property. If they acquire the property, they must incur the expenditure to do so after 23 March 1995 and before 1 July 2000. If they construct the property, they must start to do so after 23 March 1995 and before 1 July 2000. *[New subsections 628(1) and (3)]*

1.37 Primary producers must use this drought mitigation property only in Australia and for the purpose of producing assessable primary production income. They cannot lease it, hire out it out under a hire-purchase agreement or grant a right to use it to another person and still retain the allowance *[new subsection 628(2)]*. (This restriction is the same as that which existed in the general investment allowance which terminated on 30 June 1994 and the words here have the same meanings).

1.38 Where a primary producer uses minimum tillage equipment under the terms of a contract (for instance, a contract for services plus equipment) to produce assessable income which is not assessable primary production income then this use will not infringe these provisions *[new subsection 676(3)]*. An example of such a use is where a primary producer uses minimum tillage equipment on a neighbour's farm and is paid for this work.

1.39 Any item of drought mitigation property must be in place and used or ready for use by 30 June 2001. **[New subsection 628(4)]**

1.40 Where a primary producer incurs capital expenditure on drought mitigation property, the deduction allowable for such expenditure shall be claimed in the year of income in which the property is first used or is installed ready for use. It amounts to 10% of the capital expenditure on the property. **[New sections 629 and 630]**

***Limit on deductions***

1.41 Primary producers cannot claim more than \$5,000 of drought investment allowance in any one year of income. The total amount is the lesser of \$5,000 and 10% of capital expenditure on all the items of drought mitigation property first installed, or installed ready for use, in that year. Only items on which capital expenditure exceeds \$3,000 are relevant. Excess expenditure, or any deduction based on it, does not carry over to other years. **[New subsections 628(1) and 631(1)]**

***Proportionate allocation of limit***

1.42 Sometimes a primary producer may have incurred more than \$50,000 of capital expenditure on drought mitigation property first used, or installed ready for use, in a particular year and may need to know how much deduction is allowable on each particular item of property. Then, the taxpayer will allocate the limit of \$5,000 for that year proportionately to the qualifying expenditure on each item. **[New subsection 631(2)]**

1.43 An example of the proportionate allocation of the deduction limit:

- a primary producer incurs a total of \$150,000 of expenditure on two items of drought mitigation property
- new section 630 says that the taxpayer can claim 10% of the expenditure
- new subsection 631(1) places a ceiling of \$5,000 on that 10%
- this means that this primary producer can only claim \$5,000; that is, one third of the total deductions available
- the cost of each item of property is the basis of allocating the proportions available
- assume item 1 cost \$90,000 and item 2 cost \$60,000, the initial deductions would be \$9,000 and \$6,000 respectively

- but because of the proportion that the ceiling has to the total deductions available, only one third of each available deduction is allowable
- this means that there is a allowable deduction of \$3,000 on item 1 and \$2,000 on item 2
- this gives a total deduction of \$5,000. [*New subsection 631(3)*]

***Relationship with other deductions***

1.44 Double deductions are denied by sections 82, 122N, 123E and 124AH. The first denies double deductions in general terms, while the last three state that where a deduction has been claimed under the mining and quarrying provisions (Division 10), or under the provisions relating to the transport of minerals and quarrying materials (Division 10AAA) or under the petroleum prospecting and mining provisions (Division 10AA) respectively the same expenditure cannot be deducted under another provision of the Act. *New subsection 632(1)* overrides these four provisions and effectively allows a double deduction.

1.45 There are exceptions to this. Any expenditure incurred in having mains electricity connected (section 70A), expenditure eligible for the 150% research and development deduction (section 73B), and expenditure incurred in exploration and prospecting under the general mining (section 122J), quarrying (section 122JF) and the petroleum mining provisions (section 124AH) cannot be claimed under this allowance. [*New subsection 632(2)*]

1.46 If a deduction is allowable for depreciation purposes on an item of drought mitigation property and the annual depreciation percentage is 100%, then there will be no deduction under this part [*new subsection 632(3)*]. At present, such items are either under \$300 (and so could not have any qualifying expenditure) or have an effective life of less than 3 years.

***Loss of deduction on drought mitigation property***

***Disposal of item within 12 months***

1.47 If the primary producer disposes of the drought mitigation property within 12 months of its first use or its installation in readiness for use, the primary producer is no longer entitled to the deduction. [*New subsection 633(1)*]

1.48 Disposal includes loss or destruction of the drought mitigation property, or leasing it, hiring it under a hire-purchase agreement or granting a right to use it to another person. Entitlement to the deduction is lost if the drought mitigation property is used outside Australia or for a purpose other than producing assessable primary production income.

***[New subsections 633(2), (5) and (6)]***

1.49 Where a primary producer disposes of part of its interest in the drought mitigation property, the primary producer is not entitled to the deduction unless the Commissioner determines that an amount that is allowed. ***[New subsection 633(3) and (4)]***

*Disposal of item after 12 months*

1.50 If the primary producer disposes of the drought mitigation property 12 months or more after its first use or its installation in readiness for use and meant to do so when buying or building the property, then the primary producer is not entitled to the deduction ***[new subsection 634(1)]***. However, the Commissioner may determine that this loss of deduction should not happen. Some circumstances that might be considered by the Commissioner in making this determination would be the length of time the primary producer held the drought mitigation property, or any technological advances that had occurred in relation to similar items of property ***[new subsections 634(3)]***.

1.51 Disposal includes loss or destruction of the property, or leasing it, hiring it under a hire-purchase agreement or granting a right to use it to another person. The deduction is lost where the property is used outside Australia or for any purpose other than producing assessable primary production income. Such purposes could include private purposes, the production of exempt income, or carrying on a business other than primary production. ***[Subsection 634(1)]***

*Recoupment of expenditure*

1.52 Where a primary producer, who incurred expenditure on drought mitigation property, is recouped for any of that expenditure, then the primary producer will be deemed never to have incurred the expenditure and so cannot get the allowance. ***[New subsection 635(1)]***

1.53 Where the amount of recoupment for drought mitigation property is not separately identified when received in a lump sum along with recoupment of other expenditure, the amount of recoupment in relation to expenditure on drought mitigation property is calculated in proportion to the share the expenditure on drought mitigation property represents as a proportion of all expenditures recouped. ***[New subsection 635(2)]***



## **Leasing companies**

### ***Entitlement to deduction***

1.54 As mentioned earlier in paragraph 1.35 above, companies which lease the equipment are also eligible for the drought investment allowance provided they satisfy certain criteria specific to them. **[New subsection 636(1)]**

1.55 For the purposes of this Part, a leasing company is a corporation that carries on, in Australia, as its sole or principal business the business of banking, borrowing money, lending money with or without security, letting property on hire under a hire-purchase agreement or leasing property. **[New subsection 680(1)]**

### ***Criteria for qualifying for the deduction***

1.56 The minimum amount of capital expenditure that can be incurred by a leasing company in acquiring new drought mitigation property is \$3,000 and this expenditure must be incurred after 23 March 1995 and before 1 July 2000. Where the leasing company has the drought mitigation property constructed, construction must commence after 23 March 1995 and before 1 July 2000. The drought mitigation property must be used only in Australia by the lessee in producing assessable primary production income. **[New subsections 636(1), (2) and (4)]**

1.57 Where a primary producer uses minimum tillage equipment under the terms of a contract (for instance, a contract for services plus equipment) to produce assessable income which is not assessable primary production income then this use will not infringe these provisions **[new subsection 676(3)]**. An example of such a use is where a primary producer uses minimum tillage equipment on a neighbour's farm and is paid for this work.

1.58 The lease, which should be negotiated at arms length, and in the course of the leasing company carrying on business in Australia, must be for a term of at least 4 years. **[New subsection 636(3)]**

1.59 Where an item of drought mitigation property has been ordered or construction started by 30 June 2000 but it has not been delivered or constructed, to gain the benefit of the allowance the drought mitigation property must be in place and first used or installed ready for use by the lessee by 1 July 2001. **[New subsection 636(5)]**

### ***Timing of deduction***

1.60 Where the deduction for capital expenditure on drought mitigation property is allowable, the deduction shall be claimed in the year of income in which the property is first used, or is installed ready for use, by the lessee. The deduction amounts to 10% of the capital expenditure,

subject to comment below on **new sections 639 and 640**. [**New sections 637 and 638**]

***Prohibition on claiming allowance for expenditure required by former arrangements***

1.61 These provisions do not include a specific anti-avoidance rule denying deductions to leasing companies where they had a contract or arrangement to lease the property to the lessee (or an associate) on or before the date of announcement. In such cases the general anti-avoidance provisions of Part IVA are applicable to the lessor (see subsection 82AB(8)).

***Limitation on deduction***

1.62 Leasing companies may only claim \$5,000 worth of deduction per item. [**New section 639**]

***Limit on total deductions***

1.63 There is a limit on the total amount of deductions of drought investment allowance that may be claimed by a leasing company in any particular year of income. Such claims may neither lead to nor add to a loss for income tax purposes.

1.64 This limit is determined by reducing the leasing company's assessable income by deductions other than the drought investment allowance, development allowance, the general investment allowance or the previous years' losses. If the remaining amount is too small for the leasing company to take advantage of the whole amount of its drought investment allowance then the proportion of the amount that reduces the leasing companies assessable income to zero is the amount of deduction allowed. [**New section 640**]

***Proportionate allocation of limits***

1.65 Where a leasing company's deductions are limited in total or in relation to a particular item of drought mitigation property and the leasing company needs to know how much of any deduction is allowable on each particular item of property, the leasing company will calculate what proportion the expenditure on the item bears to the total amount of expenditure affected by the limit. The leasing company will then allocate the reduced allowance in proportion to the relevant expenditure. [**New section 641**]

***Relationship with other deductions***

1.66 Double deductions are denied by sections 82, 122N, 123E and 124AH. The first denies double deductions in general terms, while the last three state that where a deduction has been claimed under the mining and

quarrying provisions (Division 10), or under the provisions relating to the transport of minerals and quarrying materials (Division 10AAA) or under the petroleum prospecting and mining provisions (Division 10AA) the same expenditure cannot be deducted under another provision of the Act. ***New subsections 642(1)*** overrides these four provisions and effectively allows a double deduction.

1.67 There are exceptions to this. Any expenditure incurred in having mains electricity connected (section 70A), expenditure eligible for the 150% research and development deduction (section 73B), and expenditure incurred in exploration and prospecting under the general mining (section 122J), quarrying (section 122JF) and the petroleum mining provisions (section 124AH) cannot be claimed under this allowance. ***[New subsections 642(2)]***

### ***Loss of entitlement to deductions***

#### ***Contracts or arrangements before lease entered into***

1.68 If, before entering the lease with the leasing company, the lessee has entered into a contract or arrangement with another person so that the other person can use the property, the leasing company is not entitled to the deduction. ***[New section 643]***

#### ***Disposal of item within 12 months***

1.69 The leasing company will not be entitled to a deduction if, within 12 months after the drought mitigation property was first used or installed ready for use by the lessee,

- the leasing company disposes of the item to someone other than the lessee,
- the property is lost or destroyed,
- the lessee uses the property outside Australia or for a purpose other than producing assessable primary production income,
- the lessee causes the termination of the lease other than by acquiring the property,
- the lessee subleases the property or grants a right to use it,
- the lessee acquires the property and subsequently disposes of it, or
- the lessee acquires the property and leases the property or grants a right to use it. ***[New section 644]***

*Disposal etc of item after 12 months*

1.70 Similarly, if any of the above events occurs 12 months or more after the drought mitigation property was first used or installed in readiness for use by the lessee, the leasing company will not be entitled to the deduction if at the time of entering the lease the leasing company intended to dispose of the item or the lessee intended any of the other kinds of these events to occur. **[New subsections 645(1) and (2)]**

1.71 However, the Commissioner may determine that the leasing company keeps either all or part of the deduction. **[New subsection 645(3)]**

*Recoupment of expenditure*

1.72 Where a leasing company which incurred expenditure on drought mitigation property is recouped, then the leasing company will be deemed never to have incurred that expenditure and so cannot get the allowance. **[New subsection 646(1)]**

1.73 Where the amount of recoupment for drought mitigation property is not separately identified when received in a lump sum along with recoupment of other expenditure, the amount of recoupment in relation to expenditure on drought mitigation property is calculated in proportion to the share the expenditure on drought mitigation property represents as a proportion of all expenditures recouped. **[New subsection 646(2)]**

***Transfer of entitlement to deduction***

*Leasing company may transfer entitlement to lessee*

1.74 The leasing company is able to transfer its deduction for drought mitigation property to the lessee provided certain criteria are met. The lessor (the leasing company) must give the lessee a written declaration stating the amount of the deduction transferred in whole or in part to the lessee before the 8th of the month that follows the month in which the lease was executed. This declaration must describe the property, its acquisition date, or the date on which construction began, the amount of expenditure incurred, the date the lease was entered into, the name and address of the lessee and the term of the lease. **[New subsections 647(1) and (2)]**

1.75 Transferred deductions are not taken into account in determining the amount of deductions relating to drought mitigation property that a leasing company may claim. After the total level of deductions has been reduced by the amount of transferred deductions, any provisions which would operate to reduce or take away a leasing company's deductions will operate only on the remaining deductions. **[Subsection 647(3)]**

*Transferred deductions taken into account in applying \$5,000 limit*

1.76 In calculating the total allowance a lessee may claim, regard is had to any allowance the lessee claims for its own expenditure together with those deductions transferred from a leasing company. **[New section 648]**

*Loss of lessee deductions*

1.77 The lessee will lose entitlement to the deduction, if 12 months or more after the lessee first used the drought mitigation property or had it installed for use:

- the lessee uses the property outside Australia or for a purpose other than producing assessable primary production income,
- the lessee caused termination of the lease otherwise than by the lease ending, or by acquiring the equipment,
- the lessee enters into a contract or arrangement under which the lessee subleases the property or grants a right to use it,
- the lessee acquires the property and disposes of it (by sale or otherwise), or
- the lessee acquires the property and leases the property or grants a right to use the property to another person. **[New subsection 649(1)]**

Similar rules apply to deny the lesser's deduction, and so any transfer of that deduction to the lessee, within the first 12 months. See the discussion above of **new section 644**.

1.78 To lose the entitlement, the lessee must have meant to do something of one of these kinds of things when leasing the item **[new subsection 649(2)]**. The Commissioner may, nevertheless, determine that the lessee loses either none or only part of the entitlement to the deduction **[new subsection 649(3)]**.

*Anti-avoidance*

1.79 These provisions do not include a specific anti-avoidance rule denying deductions to leasing companies where they had a contract or arrangement to lease the property to the lessee (or an associate) before the date of announcement. In such cases the general anti-avoidance provisions of Part IVA are applicable to the lessor (see old subsection 82AL).

## Special provisions about primary producers

### Primary producer partnerships

#### *No primary producer deduction for partnership that leases out an item*

1.80 If a partnership leases an item of drought mitigation property to anyone, the partnership cannot claim a deduction for the expenditure it incurred in acquiring or constructing the item. *[New section 655]*

#### *Amount assessable where disposal of partner interest*

1.81 If a partnership acquires an item of drought mitigation property and the partnership has taken the drought investment allowance into account in determining the partnership's net income or partnership loss, then special provisions apply. *[New subsection 656(1)]*

1.82 If a partner disposes of the whole or part of the interest in the partnership or in the item of drought mitigation property, within 12 months of the item of drought mitigation property being first used or installed ready for use, then that partner will include in its assessable income the share of the deduction proportionate to what the partners agreed is the share of the expenditure to be borne by the partner, or if there is no agreement, the share of the deduction that is proportionate to the partner's partnership interest. *[New subsections 656(2) and (4)]*

1.83 Similarly, if a partner disposes of the whole or part of their interest in the partnership, or in the item of drought mitigation property, 12 months or more after the item was first used or installed ready for use, and the partner meant to dispose of the whole or part of their interest in the partnership when the item was acquired or constructed once the partnership became entitled to the deduction, then that partner will include in its assessable income the share of the deduction proportionate to what the partners agreed is the share of the expenditure to be borne by the partner or, if there is no agreement, the share of the deduction that is proportionate to the partner's partnership interest. *[New subsections 656(3) and (4)]*

1.84 For a particular year of income, a **partner's partnership interest**, which is the partner's interest in the partnership, is the ratio of the individual interest of the partner in the partnership's net income or partnership loss to the net income or partnership loss. *[New section 677]*

1.85 In circumstances where the partner disposed of part of their interest in the partnership, the Commissioner can determine that the partner loses none or part of the deduction. *[New subsection 656(5)]*

## Group companies of primary producers

### *Entitlement to primary producer deduction not lost for disposals in less than 12 months within company groups*

1.86 A company loses entitlement to a deduction if the company disposes of, or loses, the item of drought mitigation property or it is destroyed within 12 months of its first use or installation in readiness for use **[new subsection 633(2)]**. This restriction can result in the inefficient use of property within company groups. Therefore where a company disposes of an item of drought mitigation property to another company and they are members of the same group, then, subject to certain conditions, the restriction on disposal is overridden **[new subsection 657(1), (2) and (3)]**. Group company is defined in **new section 682(1)**.

1.87 The restrictions are that throughout the period of 12 months following the first use or installation in readiness for use, of the item:

- where the transferee was the holding company of the transferor, the property has not been owned by anyone other than the transferee or another group company of the transferee **[new paragraph 657(4)(a)]**; or
- where the transferee was a wholly-owned subsidiary of the taxpayer, the property has not been owned by anyone other than the transferee or another wholly-owned subsidiary of the taxpayer **[new paragraph 657(4)(b)]**; or
- where the transferee was a wholly-owned subsidiary of another company and the transferor is a wholly-owned subsidiary of the same company, the property has not been owned by anyone other than the company that is the parent of both subsidiaries or another of the parent's group companies **[new paragraph 657(4)(c)]**; or
- where the transferee was a wholly-owned subsidiary of other companies and the transferor is a wholly-owned subsidiary of the same companies, the item of property has not been owned by anyone other than another wholly owned subsidiary of the same companies **[new paragraph 657(4)(d)]**.

1.88 These restrictions ensure that any holder of property must remain a group company of the transferor in one of these ways throughout the period of 12 months.

1.89 **New subsection 657(5)** supplements the requirements in **new subsection 657(4)**. It requires that the holding company of the group including the transferee and transferor must be an eligible public company. Eligible public company is defined in **new subsection 682(6)** see comments later.

1.90 Within the 12 month period, the item of drought mitigation property must not be leased to another person or let on hire under a hire-purchase agreement, or be subject to a grant of a right to use. Also it must not be used outside Australia or used for a purpose other than producing assessable primary production income. *[New subsection 657(6)]*

1.91 There will be no restriction on leasing or granting a right to use the property if the company who is leased it or is granted the right to use is a group company of the company which owned the property and is an eligible public company. The relevant companies must remain group companies for the length of the lease or at the end of the initial 12 month period, whichever ever occurs first. If the earlier time occurs in an income year after the one in which the lease or rights to use was granted the group company must be an eligible public company for that later year of income too. *[New subsections 657(7) and (8)]*

1.92 If a court order made under a State or Territory law relating to companies vests all of the undertaking, property and liabilities of a holding company in a substitute company then this other company will be the relevant company for the purposes of *new subsections 657(4) and (5)* provided the persons who owned the shares in the holding company are the owners, with the same respective interests, of substituted company and the company is dissolved. *[New subsection 657(9)]*

**Deduction not lost to primary producer despite leasing etc during 12 month period**

1.93 Where a taxpayer company has leased the item of drought mitigation property or granted rights to another company to use it and the other company is a group company, the company does not lose its entitlement to the deduction if the group company remains a group company of the taxpayer company for so much of the term of the lease or period of the grant as happens within the 12 month period after the company first used the item or installed it ready for use. The group company must to use the item only in Australia and for the purpose of producing assessable primary production income other than by leasing the item or granting a right to use it to another person. *[New section 658]*

**Deduction not lost to primary producer despite leasing etc item after 12 month period**

1.94 Where the company leased the item of drought mitigation property or granted rights to use it to another company which is a group company, the company will not lose its entitlement to the deduction if while using the item the group company remains as such and the use is only in Australia and for the purpose of producing assessable primary production income other than by leasing the item or granting a right to use it to another person. *[New section 659]*



**Deduction not lost to primary producer despite taking item on lease etc despite contract etc for use of item after 12 month period**

1.95 If a taxpayer enters into a contract or arrangement with another person for the use of an item of drought mitigation property by that other person and the taxpayer acquired the item from a leasing company which has transferred the deduction to the taxpayer, then the first lessee of the property will not lose entitlement to the deduction if the other person is a group company of the taxpayer. *[New subsection 660(1)]*

1.96 The taxpayer will not lose the entitlement to the deduction if while using the item the user remains a group company of the taxpayer and the use is both in Australia and for the purpose of producing assessable primary production income other than by leasing the item or granting a right to use it to another person. *[New subsection 660(2)]*

**Special provisions about leasing companies**

**Leasing company partnerships**

1.97 There are special provisions applicable where a leasing company is a partner in a partnership. *[New Division 6, Subdivision A]*

***Partner deduction for property leased out by partnership***

1.98 Where a partnership, with a leasing company as a partner, incurs expenditure in acquiring or constructing an item of drought mitigation property which is leased, *new section 636* applies to the partner which is the leasing company. The amount of the deduction which the leasing company may claim is the part of the expenditure agreed by the partners to be borne by the leasing company or the part of the expenditure proportionate to of the leasing company's partnership interest in the expenditure. *[New subsection 661(1)]*

***Loss of partner deduction if pre-lease contract etc***

1.99 Where a lessee has entered into a contract or arrangement regarding the use of the item of drought mitigation property prior to leasing the item from the partnership, then the leasing company partner cannot claim the deduction. *[New section 662]*

***Loss of partner deduction where disposal by partner within 12 months***

1.100 Where a partner disposes of the whole or part of its interest in either the partnership or the item of drought mitigation property, that partner will not be entitled to the drought investment allowance deduction. If the disposal should occur within 12 months of the lessee first using the item or having it installed ready for use *[new section 663(1)]*. However, in circumstances where the partner has disposed of part of its interest the

Commissioner may determine that all or part of the deduction is allowable **[new section 663(2)]**.

***Loss of partner deduction where disposal by partnership etc within 12 months***

1.101 The partner will not be entitled to a deduction under **new section 661** if, before 12 months elapses after the item of drought mitigation property was first used or installed ready for use by the lessee,

- the partnership disposes of the item to someone other than its lessee,
- the item is lost or destroyed,
- the lessee uses the item outside Australia or for a purpose other than producing assessable primary production income,
- the lessee causes the termination of the lease other than by acquiring the item,
- the lessee subleases the item or grants a right to use it,
- the lessee acquires the item and subsequently disposes of it, or
- the lessee acquires the item and leases the property or grants a right to use it. **[New section 664]**

***Loss of partner deduction where disposal by partner etc after 12 months***

1.102 Similarly, if the partner disposes of either the whole or part of the partner's interest in the partnership or in the item of drought mitigation property to someone other than the lessee 12 months or more after the item of property was first used or installed in readiness for use by the lessee, the partner will not be entitled to the deduction if the partner intended to dispose of the property when the lease was entered into. **[New subsection 665(1)]**

1.103 Where the whole or part of the partner's interest has been disposed of the Commissioner may determine, nevertheless, that the partner does not lose all or part of the deduction. **[New subsection 665(2)]**

***Loss of partner deduction where disposal by partnership etc after 12 months***

1.104 Similarly, if the partnership disposes of either the whole or part of the item of drought mitigation property to someone other than the lessee 12 months or more after the property was first used or installed in readiness for use by the lessee, the partnership will not be entitled to the deduction.

1.105 The partnership is not entitled to the deduction if the lessee does any of the following:

- the lessee uses the property outside Australia or for a purpose other than producing assessable primary production income,
- the lessee causes the termination of the lease other than by acquiring the property,
- the lessee subleases the property or grants a right to use it,
- the lessee acquires the property and subsequently disposes of it, or
- the lessee acquires the property and leases the property or grants a right to use it. *[New paragraph 666(1)(a)]*

1.106 The partnership must have intended to dispose of the property, or the lessee must have meant to do the things, listed in paragraph 1.104 when the lessee took the property on lease. *[New paragraph 666(1)(b)]*

1.107 The Commissioner may determine that the partnership does not lose all or part of the deduction. *[New subsection 666(2)]*

### **Group companies**

#### ***Deduction not lost to leasing company despite lessee contract etc for use of property before start of 12 month period***

1.108 Where a lessee enters a contract or arrangement with another company who is a group company of the lessee for the use of an item of drought mitigation property by that company, the leasing company does not lose the deduction if the use of the item was to occur while the group company remained as a group company and the use was only in Australia and for the purpose of producing assessable primary production income other than by the leasing of the item or granting a right to use it. This requirement continues for the term of the contract or arrangement up to the end of the 12 month period after the lessee first used the item or installed it ready for use. *[New section 667]*

1.109 This section applies to override the effect of **new sections 643 and 662**. The former denies deductions when a lessee has entered into a contract or arrangement with another person for the use of the item and this contract was entered into before the lease.

1.110 **New section 662** denies the deduction to a partner when a lessee has entered into a contract or arrangement with another person for the use of the item and this contract was entered into before the item was leased by the partnership.

***Deduction not lost to leasing company despite lessee contract etc for use of property within 12 month period***

1.111 Where a lessee enters a contract or arrangement with another person for the use of an item of drought mitigation property by that person or where the lessee acquired the item of drought mitigation property and then entered into a contract or arrangement with another person for its use by that person and in both cases the person is a group company of the lessee, subject to some conditions the leasing company does not lose its deduction.

1.112 The use of the item by the group company must occur while the group company remain as such and the use must be both in Australia and for the purpose of producing assessable primary production income other than by the leasing of the item or granting a right to use it. This requirement continues for the term of the contract or arrangement up to the end of the 12 month period after the lessee first used the item or installed it ready for use. *[New section 668]*

1.113 This section applies to override the effect of *new paragraphs 644(d), 664(d), 644(f) and 664(f)*. The first denies deductions when while leasing the item the lessee enters into a contract or arrangement with another person for the use of the item.

1.114 *New paragraph 664(d)* denies the deduction to a partner when, while leasing the item from a partnership, a lessee has entered into a contract or arrangement with another person for the use of the item.

1.115 *New paragraphs 644(f) and 664(f)* operate on a similar basis but in circumstances where the lessee grants a right to use the item while leasing it.

***Deduction not lost to leasing company despite lessee contract etc for use of property after 12 month period***

1.116 Where a lessee enters a contract or arrangement with another person for the use of an item of drought mitigation property by that person or the lessee acquired the item of drought mitigation property and entered into a contract or arrangement with another person for the use of the item and in both cases the person is a group company of the lessee, subject to some conditions the leasing company does not lose the deduction.

1.117 The use of the item by the group company must occur while the group company remained as such and the use must only be in Australia and for the purpose of producing assessable primary production income other than by the leasing of the item or granting a right to use it. *[New section 669]*

1.118 This section applies to override the effect of *new paragraphs 645(1)(d) and 645(1)(f), and subsection 666(1)*. The paragraphs deny

deductions when while leasing the item the lessee enters into a contract or arrangement with another person for the use of the item or the lessee acquires the item and enters into a contract or arrangement with another person for the use of the item.

1.119 ***New subsections 666(1)*** denies the deduction to a partner when 12 months or more after the item is first used or installed ready for use by the lessee, who while leasing the item from a partnership, the lessee:

- the lessee uses the property outside Australia or for a purpose other than producing assessable primary production income,
- the lessee causes the termination of the lease other than by acquiring the property,
- the lessee subleases the property or grants a right to use it,
- the lessee acquires the property and subsequently disposes of it, or
- the lessee acquires the property and leases the property or grants a right to use it. ***[New paragraphs 664(b) to (f)]***

#### **Lease-back of used property**

1.120 This Subdivision applies so that the drought investment allowance is not lost when drought mitigation property is sold to, and then leased back to the seller by, the leasing company. ***[Subdivision C, Division 6, new section 670]***

1.121 In some circumstances, no formal transfer or sale of property to the leasing company occurs until the plant has been completed and operated by the lessee for a relatively short period.

1.122 There are some qualifications upon this arrangement, as the lessee must not use the property or hold it for use for more than 6 months before the sale to the leasing company and the lease back. ***[New paragraph 670(1)]***

#### **Transitional**

1.123 The purpose of the transitional provision is to cover a lease entered into after 23 March 1995 but before this legislation commences. This provision will allow a leasing company to transfer a deduction under these provisions to a lessee if a lease was made after 23 March 1995 and before Royal Assent. It allows a leasing company to give a declaration in the month after Royal Assent, as the leasing company might otherwise have to give a declaration before the provisions had become law. ***[New section 671]***

## **Definitions**

1.124 Certain words are defined for the purposes of this legislation.

### **Acquire**

1.125 Acquire means becoming the owner of the property; taking the property on hire under a hire-purchase agreement; or having the property constructed by someone else on your own premises. *[New section 672]*

### **Ownership of item of property where Crown lease**

1.126 Where a person who is a lessee of Crown land has an item of property affixed to that land, and through the operation of section 54AA the lessee is taken to own the affixed item of property, then the lessee is the owner for the purposes of these provisions. *[New section 673]*

### **Hire-purchase agreement**

1.127 A hire-purchase agreement is an agreement under which a person hires an item of property on particular items. The hirer has either an absolute or conditional right to purchase that item of property. As mentioned above under 'acquire', the hirer is considered the owner of property for the purposes of this allowance. The person from whom the item is hired is not. *[New subsection 674(1)]*

1.128 An agreement is not a hire-purchase agreement if in determining whether any amount is payable on the exercise of a right to purchase the property, no regard is had to any part of the payments before the right is exercised. *[New subsection 674(2)]*

### **Dispose and hire-purchase**

1.129 Where an item of property is subject to a hire-purchase agreement which the purchaser (hirer) breaches and the person from whom the item is hired then repossesses the item of property, the purchaser disposes of the item at the time the other person repossesses the property. *[New section 675]*

### **Assessable primary production income**

1.130 Where a taxpayer derives assessable income in the course of carrying on a business of primary production, or other assessable income as a result of carrying on that business, that income is assessable primary production income. *[New subsection 676(1)]*

1.131 If an unlisted company has an item of property which it uses for the purpose of producing assessable primary production income that item cannot be used by its directors, shareholders or employees or their relatives for private or domestic purposes. Use of the item for private or domestic purposes that are only incidental to the purpose of producing

assessable primary production income will not cause the company to lose the allowance. *[New subsection 676(2)]*

**Install ready for use**

1.132 An item is installed ready for use when it is installed ready for use and held in reserve. *[New section 678]*

**Lease**

1.133 Lease includes all forms of letting items on hire other than hire-purchase. *[New section 679]*

**New**

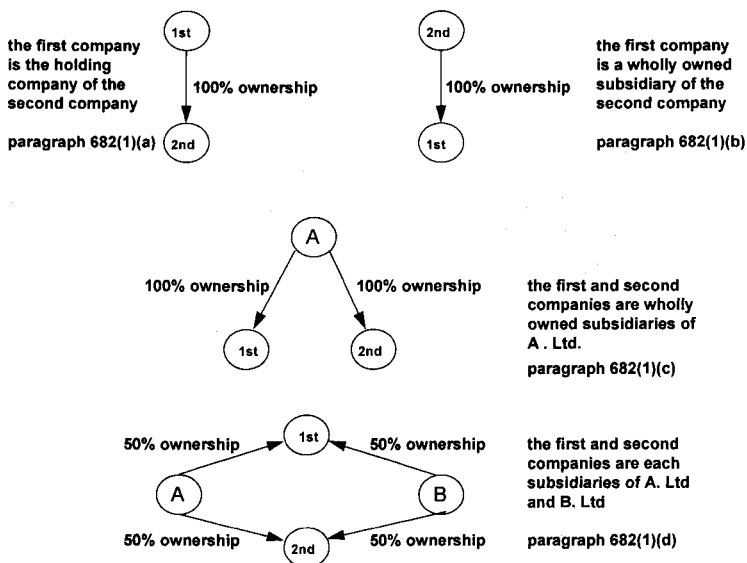
1.134 To obtain the drought investment allowance, an item of drought mitigation property must be new. New items have not been previously used by anyone, acquired by someone for use by them, or held by someone for use by them. Reconditioned or wholly or mainly reconstructed items are not new. *[New section 681]*

**Group company and associated terms**

1.135 It is necessary to have a concept of group company within these provisions because of provisions under which one company within a group can dispose of, or lease, or grant a right to use drought mitigation property to another company within that group without losing the right to the allowance.

1.136 One company within the group must be a listed public company.

1.137 There are four situations where companies can constitute a company group.



1.138 *New subsection 682(2)* specifies the conditions under which one company is to be taken to be the holding company of another at a particular time. Firstly, the holding company may be an eligible public company. Secondly, the subsidiary company may be an eligible subsidiary of a public company. [*New paragraphs 682(2)(a) and (b)*]

1.139 A further condition is that, at the particular time, all the shares in the subsidiary company are to be beneficially owned by the holding company. Beneficially is used here to cover both direct and indirect ownership.

1.140 *New sub-paragraph 682(2)(c)(i)* covers the situation where the holding company owns all the shares directly in the subsidiary.

1.141 *New sub-paragraphs 682(2)(c)(ii) and (iii)* cover situations of one or more interposed companies between the holding company and the relevant subsidiary company. All of the interposed companies must be subsidiaries of a public company.

1.142 A company will also be a holding company of another company in circumstances where a dividend paid at the particular time, and successively distributed through all companies and trustees interposed between the holding company and the relevant subsidiary, would flow through to be received in full and wholly for the benefit of the holding company. [*New paragraph 682(2)(d)*]



### **Eligible subsidiary**

1.143 A company is a subsidiary of a public company if at the end of a year of income, public companies beneficially owned all the shares of the subsidiary at all times during its year of income, and could not be prevented from exercising their voting power in the subsidiary for their own benefit or from receiving any dividends or distributions of capital that might be paid up or made by their subsidiary during the income year.

1.144 There should be no agreement in existence during the income year that could affect the voting power of the public companies in their subsidiary after the year of income or the rights of the parent company to dividends or distributions of capital that might be paid or made by their subsidiary after the income year. *[New subsection 682(5)]*

### **Eligible public company**

1.145 A company is an eligible public company if its shares are listed for quotation in the official list of stock exchange in Australia or elsewhere and were so listed on the last day of the year of income. *[New subsection 682(6)]*

### **Adjustment of excessive amounts in respect of drought mitigation property**

1.146 Where amount is said to be payable for the construction an item of drought mitigation property and this amount is greater than the market value of the item when construction is completed, then the amount that may be claimed as drought investment allowance is based on the market value at the completion date.

1.147 Where an amount is said to be payable for the acquisition of such an item and the acquisition cost is greater than the market value, then the amount that may be claimed as drought investment allowance is based on the market value at the date of the contract. *[New subsection 683(1)]*

1.148 Where an item of drought mitigation property is being constructed by someone else on another person's property, under a contract which provides that materials for construction are to be purchased for an amount which exceeds the market value of the item on its completion, then the cost of the materials is the market value of the item when its construction is complete.

1.149 In any other case of construction, if the price of the materials is greater than the market value of the materials at the date of the contract then the amount that may be claimed as drought investment allowance is the market value of the materials at the date of the contract. *[New subsection 683(2)]*

1.150 The Commissioner may determine that neither subsection 683(1) nor 683(2) apply. *[New subsection 683(3)]*

### **Index of Definitions**

1.151 *New section 684* lists the definitions in Part XII alphabetically and gives the number of the provision in which each is located.

## **Part 2 of Schedule 1**

### **Consequential Amendments**

#### ***Current year losses***

1.152 Sections 50A to 50N prevent losses incurred by a company in one part of an income year being offset against profits derived in another part of the year where there has been a disqualifying change in the degree of ownership or control of the company between the two periods. The effect of these "current year loss" measures is to deny a deduction for the relevant losses.

1.153 To calculate those losses, the year is broken into periods before and after the disqualifying change and the profit or loss for each period is calculated as if each period was a year of income. Generally, income and deductions are allocated according to the period to which they relate. Those amounts that relate to both periods, such as plant depreciation, are apportioned between the periods.

1.154 Some amounts are not attributed to a particular period and are instead taken into account in the final calculation of taxable income for the whole year. One such amount is a leasing company's entitlement to the drought investment allowance from its leasing business. As leasing companies are to be entitled to the drought investment allowance from their leasing business, the current year loss measures are to be amended to include a reference to amounts so allowable to leasing companies. *[Items 2 and 3]*

#### ***Allowance in addition to depreciation***

1.155 Income tax law contains a number of provisions to prevent double deductions in respect of the same expenditure. Subsection 56(3) prevents double deductions for expenditure on plant by reducing the depreciable cost of plant by the amount allowed as deductions under another provision.

1.156 The drought investment allowance is to be generally available in addition to depreciation deductions. Accordingly, subsection 56(3) is being amended to ensure that the depreciable cost of plant is not reduced

by any amount allowed as a drought investment allowance deduction.  
**[Item 4]**

### ***Limit on leasing companies***

1.157 Section 82AC limits the amount that leasing companies can claim for development allowance from their leasing business to the amount of net income. Where a leasing company is entitled to deductions for both the development allowance and the drought investment allowance from the leasing business, the limit is to apply in relation to the sum of deductions allowable under both provisions. **[Item 5]**

### ***Arrangements for the use of property***

1.158 Division 16D (sections 159GE to 159GO) deals with arrangements that have the effect of transferring property related deductions from tax-exempt bodies and the like, which are unable to use those deductions, to taxable entities which can use the deductions. The effect of the measure is to deny the taxable entity the relevant property deductions such as plant depreciation and the development allowance and treat the arrangement as if it were a loan. This amendment ensures that the drought investment allowance will not be available for drought mitigation property used in such arrangements. **[Items 6 and 7]**

### ***Amendment of assessments***

1.159 Section 170 imposes time limits on making amendments to assessments, generally 4 years from the date tax became due and payable under the original assessment. However, there are circumstances where it might be necessary to amend returns outside that 4 year period. Subsection 170(10) enables assessments to be amended at any time in a number of specified circumstances.

1.160 The drought investment allowance, like the development allowance and the former general investment allowance, contemplates a number of circumstances where it might be necessary to amend an assessment outside the standard 4 year period and so subsection 170(10) is being amended to include a reference to the drought investment allowance provisions. **[Item 8]**



## Farm management bonds

### Overview

2.1 This Chapter explains the amendments contained in *Schedule 2* of the Bill, which amend the *Loans (Income Equalization Deposits) Act 1976*. These measures are to make farm management bonds (FMBs) a more attractive investment vehicle for farmers. FMBs provide a greater return if they are repaid to meet certain sources of serious financial difficulties, and so help farmers to prepare for difficulties including commodity price collapse and drought.

### Summary of the amendments

#### Purpose of the amendments

2.2 The purpose of the amendments is to make FMBs more attractive to farmers so that they will be more self sufficient in times of drought and the collapse of commodity prices, and will not be so reliant on Government for help.

2.3 The measure increases the 'default' investment component of FMBs to 100%, increases the maximum amount of FMBs to \$150,000 for each farmer, eliminates withholding tax on withdrawal of FMBs, and brings the treatment of FMBs where a farmer ceases to be engaged in primary production into line with other repayments unrelated to serious financial difficulties.

### Background to the legislation

2.4 Income equalization deposits (IEDs) are made from primary producers' before-tax income. They earn interest at the short term bond rate which the primary producer may claim each year or may redeposit in the IEDs. Any amounts repaid, as interest or otherwise, are taxable.

2.5 Because IEDs are deposits of income on which tax has not been paid, they earn interest only on an investment component. Otherwise, primary producers would both defer tax and earn interest on it. For IEDs generally, the investment component is 61%, corresponding to an average tax rate of 39%. For FMBs, the investment component is 80%, corresponding to an average tax rate of 20%. Although the rate can be varied by regulation, the default rate set in the law has not been varied.

2.6 IEDs generally may be repaid in a range of circumstances. An amount of 20% is withheld from them to anticipate income tax to be paid later. Withholding tax generally helps to prevent the cash flow problem of income from an IED during a year, followed by a balance of tax outstanding later.

2.7 The National Drought Policy of 1992 introduced FMBs as a new concessionary IED. FMBs earn higher returns than IEDs because of their higher investment component if they are repaid to meet serious financial difficulties due to commodity price collapse, or due to drought, disease, flood, fire or the like. Farmers have not yet used FMBs to prepare for disaster to a great extent

2.8 FMBs are not 'locked in'. However, if primary producers seek repayment in circumstances other than the kind of serious financial difficulties for which they provide, the FMBs are repaid only as IEDs, and any overpaid interest reduces the balance date. So FMBs are likely to be repaid in years when total income is especially low, and when financial need is exceptional.

## **Explanation of the amendments**

2.9 There are three changes which make FMBs more attractive:

- that proportion of a deposit in the FMB scheme which attracts interest has been increased from 80% to 100% *[item 1]*
- the maximum amount that may be held as a FMB has been increased from \$80,000 to \$150,000 *[item 2]*
- the 20% withholding tax that was imposed on withdrawals of FMBs has been eliminated entirely *[item 3]*.

2.10 FMB deposits are not a form of superannuation. These measures ensure that they are not withdrawn as FMBs on the retirement of the primary producer. Currently, when someone stops being a primary producer and does not become a primary producer again within 120 days, all their IEDs and FMBs must be withdrawn. At present, FMBs withdrawn because of retirement from primary production are withdrawn as FMBs,

with interest on a larger component of the deposit than for IEDs (section 19 of the Loan (Income Equalization Deposits) Act 1976).

2.11 The amendment has the effect that when a taxpayer retires from primary production any deposits that person has made after these changes take effect will be treated as being IEDs and as always having been IEDs. This means that they will have earned a lower level of interest and any interest that has accrued on the FMBs will have to be recalculated and any excess interest that has been paid in the past will have to be repaid **[item 5]**. This is the same treatment that applies:

if a taxpayer requests repayment of the deposit within 12 months of making the deposit specifies that he is experiencing serious financial difficulties that do not relate to a fall in commodity prices or natural disaster and his circumstances have changed since making the deposit; and;

if a taxpayer requests repayment of the deposit, 12 months after making it, and gives no reason for withdrawal (section 15A of the *Loan (Income Equalization Deposits) Act 1976*).

## **Application**

2.12 FMBs will earn interest on 100% of their value after the Bill receives Royal Assent. **[Subitem 8(1)]**

2.13 Depositors will be able to reinvest their interest on their FMBs provided that the amount they have deposited does not exceed the maximum limit of \$150,000 after the Bill receives Royal Assent. **[Subitem 8(2)]**

2.14 Depositors will be able to invest in FMBs up to a maximum limit of \$150,000 after the Bill receives Royal Assent. **[Subitem 8(3)]**

2.15 Any requests for repayment of FMBs after the Bill receives Royal Assent need no longer include a statement of the amount of how much of the deposit that is being repaid should be included in the taxpayer's assessable income. **[Subitem 8(4)]**

2.16 Where a primary producer ceases to be one and does not resume the business within 120 days and requests repayment of FMBs that were deposited after the Bill receives Royal Assent, the person authorizing the repayment will treat the FMB deposit as always having been an IED deposit and any interest that has accrued on the FMBs will have to be recalculated and any excess interest that has been paid in the past will have to be repaid. **[Subitem 8(5)]**

2.17 Where a request for repayment of FMBs is made after the Bill receives Royal Assent, the Secretary to the Department of Primary Industries and Energy no longer has to advise the primary producer of the requirement that the primary producer may notify the Secretary of the amount to be included in the primary producer's assessable income as a result of withdrawal of the FMB or the amount of withholding tax applicable. **[Subitem 8(6)]**

2.18 Withholding tax will not be subtracted from FMBs where the request for repayment was made after the Bill receives Royal Assent. **[Subitem 8(7)]**



## Index

| Clause | Description       | Paragraph reference |
|--------|-------------------|---------------------|
| 1.     | Short title.....  | Self explanatory    |
| 2.     | Commencement..... | Self explanatory    |
| 3.     | Schedules .....   | Self explanatory    |

### *Schedule 1 - Amendments of the Income Tax Assessment Act 1936 relating to drought investment allowance*

#### *Part 1 - Addition of new part*

| Item | Description  | Paragraph reference |
|------|--|---------------------|
| 1.   | Insertion of Part XII - drought investment allowance ..... |                     |

| New section | Description                                   | Paragraph reference |
|-------------|---|---------------------|
| 625.        | Object .....                                  | 1.8                 |
| 626.        | The key principle.....                        | 1.9                 |
| 627.        | Overview of Part.....                         | 1.11-1.12           |
| 628.        | Expenditure qualifying for the deduction..... | 1.36-1.39, 1.41     |
| 629.        | Timing of deduction .....                     | 1.40                |
| 630.        | Amount of the deduction.....                  | 1.40                |
| 631.        | \$5000 limit on total deductions .....        | 1.41-1.43           |
| 632.        | Relationship with other deductions .....      | 1.44-1.46           |
| 633.        | Disposal etc. of item within 12 months .....  | 1.47-1.49, 1.86     |
| 634.        | Disposal etc. of item after 12 months .....   | 1.50-1.51           |

|      |  |                         |
|------|--|-------------------------|
| 635. | Recruitment of expenditure .....   | 1.52-1.53               |
| 636. | Expenditure qualifying for the deduction .....   | 1.54, 1.56-1.59         |
| 637. | Timing of deduction .....  | 1.60                    |
| 638. | Amount of the deduction .....  | 1.60                    |
| 639. | \$5000 limit on deduction for any one item .....   | 1.62                    |
| 640. | Limit on total deductions .....  | 1.63-1.64               |
| 641. | Proportionate allocation of limits .....   | 1.65                    |
| 642. | Relationship with other deductions .....   | 1.66-1.67               |
| 643. | Contracts or arrangements before lease entered into .....  | 1.68, 1.109             |
| 644. | Disposal etc. of item within 12 months .....   | 1.69, 1.77, 1.113-1.115 |
| 645. | Disposal etc. of item after 12 months .....  | 1.70-1.71, 1.77, 1.118  |
| 646. | Recoupment of expenditure .....  | 1.72-1.73               |
| 647. | Leasing company may transfer entitlement to lessee .....   | 1.74-1.75               |
| 648. | Transferred deduction taken into account in applying \$5000 limit<br>under section 631 .....                                     | 1.76                    |
| 649. | Loss of lessee entitlement .....   | 1.77-1.78               |
| 650. | Meaning of drought mitigation property .....   | 1.14                    |
| 651. | Meaning of fodder storage facility .....   | 1.15                    |
| 652. | Meaning of water storage facility and water transport facility .....   | 1.16-1.19               |
| 653. | Meaning of approved conservation plan and associated terms .....   | 1.12-1.30               |
| 654. | Meaning of minimum tillage equipment .....   | 1.31-1.33               |
| 655. | No primary producer deduction for partnership that leases out item .....   | 1.80                    |
| 656. | Amount assessable where disposal of partner interest .....   | 1.81-1.83, 1.85         |
| 657. | Entitlement to primary producer deduction not lost for disposals in<br>fewer than 12 months within company groups .....          | 1.86-1.92               |
| 658. | Deduction not lost to primary producer despite leasing etc. item<br>during 12 month period .....                                 | 1.93                    |
| 659. | Deduction not lost to primary producer despite leasing etc. item<br>after 12 month period .....                                  | 1.94                    |
| 660. | Deduction not lost to primary producer taking item on lease despite<br>contract etc. for use of item after 12 month period ..... | 1.95-1.96               |
| 661. | Partner deduction for property leased out by partnership .....   | 1.98                    |

|      |  |                         |
|------|--|-------------------------|
| 662. | Loss of partner deduction if pre-lease contract etc .....  | 1.99, 1.109-1.110       |
| 663. | Loss of partner deduction where disposal by partner within 12 months .....   | 1.100                   |
| 664. | Loss of partner deduction where disposal by partnership etc. within 12 months .....  | 1.101, 1.119            |
| 665. | Loss of partner deduction where disposal by partner after 12 months .....  | 1.102-1.103             |
| 666. | Loss of partner deduction where disposal by partnership etc. after 12 months .....   | 1.104-1.107, 1.119      |
| 667. | Deduction not lost to leasing company despite lessee contract etc. for use of property before start of 12 month period ..... | 1.108                   |
| 668. | Deduction not lost to leasing company despite lessee contract etc. for use of item within 12 month period .....              | 1.111-1.112             |
| 669. | Deduction not lost to leasing company despite lessee contract etc. for use of property after 12 month period .....           | 1.116-1.117             |
| 670. | Deduction for property used by lessee .....  | 1.120-1.122             |
| 671. | Modification of date in section 647 .....  | 1.123                   |
| 672. | Meaning of acquire .....   | 1.125                   |
| 673. | Ownership of item of property where Crown lease .....  | 1.126                   |
| 674. | Meaning of hire-purchase agreement .....   | 1.127-1.128             |
| 675. | Special meaning of dispose in the case of hire-purchase .....  | 1.129                   |
| 676. | Meaning of assessable primary production income .....  | 1.38, 1.57, 1.130-1.131 |
| 677. | Meaning of partner's partnership interest .....  | 1.84                    |
| 678. | Meaning of install ready for use .....   | 1.132                   |
| 679. | Meaning of lease .....   | 1.133                   |
| 680. | Meaning of leasing company .....   | 1.55                    |
| 681. | Meaning of new .....   | 1.134                   |
| 682. | Group company and associated terms .....   | 1.86, 1.89, 1.135-1.145 |
| 683. | Adjustment of excessive amounts in respect of drought mitigation property .....  | 1.146-1.150             |
| 684. | Index of definitions .....   | 1.151                   |

***Part 2 - Consequential amendments***

| <b>Item</b> | <b>Paragraph reference</b> |
|-------------|----------------------------|
| 2.          | 1.152-1.154                |
| 3.          | 1.152-1.154                |
| 4.          | 1.155-1.156                |
| 5.          | 1.157                      |
| 6.          | 1.158                      |
| 7.          | 1.158                      |
| 8.          | 1.159-1.160                |

***Schedule 2 - Amendments of the Loan (Income Equalization Deposits) Act 1976 relating to farm management bonds***

| <b>Item</b> | <b>Paragraph reference</b> |
|-------------|----------------------------|
| 1.          | 2.9                        |
| 2.          | 2.9                        |
| 3.          | 2.9                        |
| 4.          | 2.15                       |
| 5.          | 2.10-2.11, 2.16            |
| 6.          | 2.12                       |
| 7.          | 2.18                       |
| 8.          | 2.12-2.18                  |







