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| **EXPOSURE DRAFT** |

Inserts for

Treasury Laws Amendment (Measures for Future Bills) Bill 2023: Thin capitalisation interest limitation

| Commencement information | | |
| --- | --- | --- |
| Column 1 | Column 2 | Column 3 |
| Provisions | Commencement | Date/Details |
| 1. | The first 1 January, 1 April, 1 July or 1 October to occur after the day this Act receives the Royal Assent. |  |
|  |  |  |

Schedule X—Thin capitalisation and other amendments

Part 1—Main amendments

Income Tax Assessment Act 1997

1 Paragraph 25‑90(b)

Omit “section 768‑5, or”.

2 Paragraph 230‑15(3)(c)

Omit “section 768‑5, or”.

3 Section 705‑60 (after table item 6)

Insert:

|  |  |  |
| --- | --- | --- |
| 6A | Subtract from the result of step 6 the step 6A amount worked out under section 705‑112, which is about \*FRT disallowed amounts that the joining entity transferred to the \*head company under section 820‑62 | To stop the joined group getting benefits both through higher \*tax cost setting amounts for the joining entity’s assets and through FRT disallowed amounts transferred to the head company |

4 Section 705‑60 (cell at table item 7, column headed “What the step requires”)

Omit “step 6”, substitute “step 6A”.

5 After section 705‑110

Insert:

705‑112 If joining entity transfers a FRT disallowed amount to the head company—step 6A in working out allocable cost amount

(1) For the purposes of step 6A in the table in section 705‑60, the step 6A amount is worked out by multiplying the sum of the \*FRT disallowed amounts mentioned in subsection (2) by the \*corporate tax rate.

(2) The \*FRT disallowed amounts are the joining entity’s FRT disallowed amounts that are transferred to the \*head company under section 820‑62, to the extent that they were not applied by the joining entity under paragraph 820‑57(2)(b) in respect of the income year in which the joining time occurred or any earlier income year.

6 After paragraph 815‑140(1)(a)

Insert:

(aa) the entity:

(i) is *not* a \*general class investor in relation to the income year; and

(ii) has *not* made a choice under subsection 820‑85(2A) or 820‑185(2A) in relation to the income year; and

7 Section 820‑35

Omit “Subdivision 820‑B”, substitute “Subdivision 820‑AA, 820‑B”.

8 Paragraph 820‑37(1)(a)

Repeal the paragraph, substitute:

(a) either:

(i) the entity is an \*outward investing financial entity (non‑ADI) or an \*outward investing entity (ADI) for a period that is all or any part of that year (and is not a \*general class investor for that year); or

(ii) assuming that the entity were a \*financial entity for all of that year, it would be, for all of that year, an outward investing financial entity (non‑ADI) and *not* an inward investing financial entity (non‑ADI); and

9 Subsection 820‑40(1)

Omit “in relation to a \*debt interest issued by the entity,”.

10 Subparagraph 820‑40(1)(a)(ii)

Omit “under the \*scheme giving rise to the debt interest”, substitute “under a \*scheme giving rise to a \*debt interest”.

11 Subparagraph 820‑40(1)(a)(iii)

Omit “under the scheme giving rise to the debt interest”, substitute “under a scheme giving rise to a debt interest”.

12 After Subdivision 820‑A

Insert:

Subdivision 820‑AA—Thin capitalisation rules for general class investors

Guide to Subdivision 820‑AA

820‑41 What this Subdivision is about

This Subdivision sets out the thin capitalisation rules that apply to general class investors (that is, entities that are not dealt with in rules set out in Subdivisions 820B, 820‑C, 820‑D or 820‑E). These rules deal with the following matters {to be drafted}.

Table of sections

Operative provisions

Operative provisions

820‑43 Thin capitalisation rule for general class investors

Thin capitalisation rule

(1) This subsection disallows all or part of an entity’s \*debt deductions for an income year if, for that year:

(a) the entity is a \*general class investor (see subsection (2)); and

(b) the entity:

(i) has *not* made a choice under subsection (3) or (4) (fixed ratio test applies); or

(ii) has made a choice under subsection (3) (group ratio test applies); or

(iii) has made a choice under subsection (4) (external third party debt test applies).

Note 1: This Subdivision does not apply if the total debt deductions of that entity and all its associate entities for that year are $2 million or less, see section 820‑35.

Note 2: To work out the amount to be disallowed, see section 820‑45.

Note 3: A consolidated group or MEC group may be a general class investor to which this Subdivision applies: see Subdivisions 820‑FA and 820‑FB.

General class investor

(2) The entity is a ***general class investor*** for an income year if, and only if:

(a) the entity is *not* any of the following for all of the income year:

(i) an \*outward investing financial entity (non‑ADI);

(ii) an \*inward investing financial entity (non‑ADI);

(iii) an \*outward investing entity (ADI);

(iv) an \*inward investing entity (ADI); and

(b) assuming that the entity were a \*financial entity for all of the income year, it would be, for the income year, any of the following:

(i) an outward investing financial entity (non‑ADI);

(ii) an inward investing financial entity (non‑ADI).

(3) If:

(a) an entity is a \*general class investor for an income year; and

(b) the entity is a \*GR group member for the period corresponding to the income year of a \*GR group for the period; and

(c) the \*GR group EBITDA for the period of the GR group is not less than zero;

the entity may make a choice under this subsection to apply the group ratio test in relation to that income year.

(4) An entity that is a \*general class investor for an income year may make a choice under this subsection to apply the external third party debt test in relation to that income year.

(5) However, an entity cannot make a choice under subsection (4) in relation to an income year if:

(a) the entity has one or more \*associate entities in respect of which the following conditions are satisfied:

(i) the associate entity is a \*general class investor for the income year;

(ii) this Subdivision does not apply to disallow \*debt deductions of the associate entity for the income year, because of section 820‑35, 820‑37 or 820‑39; and

(b) at least one of those associate entities does not make a choice under subsection (4) in relation to the income year.

(6) For the purposes of subsection (5), in determining whether an entity is an ***associate entity*** of another entity, treat the reference in paragraph 820‑905(1)(a) to “an \*associate interest of 50% or more” as instead being a reference to “a \*TC control interest of 10% or more”.

(7) A choice under subsection (3) or (4) must be made:

(a) in the \*approved form; and

(b) on or before the earlier of the following days:

(i) the day the entity lodges its \*income tax return for the income year;

(ii) the day the entity is required to lodge its income tax return for the income year.

(8) A choice under subsection (3) or (4) cannot be revoked.

820‑45 Amount of debt deduction disallowed

(1) The amount (the ***total disallowed amount***) disallowed under subsection 820‑43(1) of the \*debt deductions of an entity for an income year is:

(a) if the entity has *not* made a choice under subsection 820‑43(3) or (4) in relation to the income year (fixed ratio test applies)—the amount by which the entity’s \*net debt deductions for the income year exceed the entity’s \*fixed ratio earnings limit for the income year (see section 820‑47); or

(b) if the entity has made a choice under subsection 820‑43(3) in relation to the income year (group ratio test applies)—the amount by which the entity’s net debt deductions for the income year exceed the entity’s \*group ratio earnings limit for the income year (see section 820‑47); or

(c) if the entity has made a choice under subsection 820‑43(4) in relation to the income year (external third party debt test applies)—the amount by which the entity’s debt deductions for the income year exceed the entity’s \*external third party earnings limit for the income year (see section 820‑61).

Note: The disallowed amount also does not form part of the cost base of a CGT asset. See section 110‑54.

(2) The amount by which a particular \*debt deduction is disallowed as a result of subsection (1) is worked out as follows:

(a) first, divide the total disallowed amount by the \*debt deductions of the entity for the income year;

(b) next, multiply the amount of the particular debt deduction by the result of paragraph (a).

(3) An entity’s ***net debt deductions*** for an income year is worked out as follows:

(a) first, work out the sum of the entity’s \*debt deductions for the income year;

(b) next, work out the sum of each amount included in the entity’s assessable income for that year that is:

(i) interest; or

(ii) an amount in the nature of interest; or

(iii) any other amount that is calculated by reference to the time value of money;

(c) next, subtract the result of paragraph (b) from the result of paragraph (a).

820‑47 Meaning of *fixed ratio earnings limit* and *group ratio earnings limit*

(1) An entity’s ***fixed ratio earnings limit*** for an income year is 30% of its \*tax EBITDA for the income year.

(2) An entity’s ***group ratio earnings limit*** for an income year is its \*group ratio for the income year multiplied by its \*tax EBITDA for the income year.

820‑49 Meaning of *tax EBITDA*

An entity’s ***tax EBITDA*** for an income year is worked out as follows:

(a) first, work out the entity’s taxable income or \*tax loss for the income year (disregarding the operation of this Division and treating a tax loss as a negative amount);

(b) next, add the entity’s \*net debt deductions for the income year;

(c) next, add the sum of the entity’s deductions (if any) under Subdivision 40‑B and Division 43 for the income year from its assessable income for the income year;

(d) next, add the sum of each of the entity’s tax losses for earlier income years, to the extent that they are deducted under Division 36 from its assessable income for the income year; and

If the result of paragraph (d) is less than zero, treat it as being zero.

820‑51 Meaning of *group ratio*, *GR group*, *GR group parent* and *GR group member*

(1) If an entity is a \*GR group member for a period of a \*GR group for the period, the entity’s ***group ratio*** for the income year corresponding to the period is worked out as follows:

(a) first, work out the \*GR group net third party interest expense, for that period, of the GR group;

(b) next, work out the \*GR group EBITDA for that period of the GR group;

(c) next, divide the result of paragraph (a) by the result of paragraph (b).

If the result of paragraph (b) is zero or less, the entity’s ***group ratio*** for the income year is zero.

(2) A ***GR group***, for a period, is the group comprised of the following:

(a) a worldwide parent entity (as described in subsection 820‑935(6) whose financial statements mentioned in that subsection are \*audited consolidated financial statements for the worldwide parent entity for the period;

(b) each other entity that is fully consolidated on a line‑by‑line basis in those audited consolidated financial statements.

(3) The worldwide parent entity mentioned in paragraph (2)(a) is the ***GR group parent*** for the period of the \*GR group.

(4) Each of the entities mentioned in paragraphs (2)(a) and (b) is a ***GR group member*** for the period of the \*GR group.

820‑53 Meaning of *GR group net third party interest expense* and *financial statement net third party interest expense*

(1) The ***GR group net third party interest expense***, for a period, of a \*GR group for the period, is the amount that would be the group’s \*financial statement net third party interest expense for the period if the \*audited consolidated financial statements for the period for the \*GR group parent, for the period, for the group, were prepared on the basis that the following were treated as interest:

(a) an amount in the nature of interest;

(b) any other amount that is calculated by reference to the time value of money.

(2) The ***financial statement net third party interest expense***, for a period, of a \*GR group for the period, is:

(a) if the \*audited consolidated financial statements for the GR group parent for the period for the group disclose the amount of the group’s net third party interest expense for the period—that amount, reduced by the amount of each payment (if any) covered by subsection (3); or

(b) otherwise:

(i) the amount of the group’s third party interest expenses for the period disclosed in those audited consolidated financial statements, reduced by the amount of each payment (if any) covered by subsection (3);

reduced by:

(ii) the amount of the group’s third party interest income for the period disclosed in those audited consolidated financial statements, reduced by the amount of each payment (if any) covered by subsection (3).

(3) For the purposes of subsection (2), this subsection covers a payment if:

(a) the payment is made by an entity to an \*associate entity of the entity; and

(b) either

(i) the entity is a \*GR group member for the period of the \*GR group and the associate entity is *not* such a GR group member; or

(ii) the entity is not a GR group member for the period of the GR group and the associate entity is such a GR group member.

(4) The ***adjusted net third party interest expense***, for a period, of an entity for a period, is the amount that would be the entity’s net interest expense for the period if the following payments were disregarded:

(a) a payment is made by the entity to an \*associate entity of the entity;

(b) a payment is made by an associate entity of the entity to the entity.

(5) For the purposes of subsections (3) and (4), in determining whether an entity is an ***associate entity*** of another entity, treat the reference in paragraph 820‑905(1)(a) to “an \*associate interest of 50% or more” as instead being a reference to “a \*TC control interest of 10% or more”.

820‑55 Meaning of *entity EBITDA* and *GR group EBITDA*

(1) The ***entity EBITDA***, of an entity for a period, is the sum of the following for the entity for the period:

(a) the entity’s net profit (disregarding tax expenses);

(b) the entity’s \*adjusted net third party interest expense;

(c) the entity’s depreciation and amortisation expenses.

(2) The ***GR group EBITDA***, for a period, of a \*GR group for the period, is the sum of the following, as disclosed in the \*audited consolidated financial statements for the period, for the GR group:

(a) the GR group’s net profit (disregarding tax expenses);

(b) the GR group’s \*adjusted net third party interest expense;

(c) the GR group’s depreciation and amortisation expenses.

(3) For the purposes of subsection (2), in working out the \*GR group’s \*GR group EBITDA for the period, if a \*GR group member for the period of the GR group has an \*entity EBITDA for the period of less than zero, disregard that entity EBITDA.

820‑57 Special deduction for previously FRT disallowed amounts—fixed ratio test

(1) An entity can deduct the amount worked out under subsection (2) from its assessable income for the income year if:

(a) the entity has *not* made a choice under subsection 820‑43(3) or (4) in relation to the income year (fixed ratio test applies); and

(b) the entity’s \*fixed ratio earnings limit for the income year exceeds the sum of the entity’s \*net debt deductions for the income year.

(2) Work out the amount of the deduction as follows:

(a) first, work out the amount of the excess mentioned in paragraph (1)(b);

(b) next, apply against that excess each of the entity’s \*FRT disallowed amounts for the previous 15 income years (to the extent that they have not already been applied under this paragraph in respect of any of those previous income years).

The amount of the deduction is the total amount applied under paragraph (b).

(3) For the purposes of paragraph (2)(b):

(a) apply \*FRT disallowed amounts in sequence, where a FRT disallowed amount for an earlier income year is applied before a FRT disallowed amount from a later income year; and

(b) apply FRT disallowed amounts up to, but not beyond, the excess mentioned in paragraph (1)(b).

Note: As a result of paragraph (b), part of a FRT disallowed amount may be applied against the excess mentioned in paragraph (1)(b).

820‑59 Meaning of *FRT disallowed amount*

(1) An entity has a ***fixed ratio test disallowed amount*** (or ***FRT disallowed amount***) for an income year equal to:

(a) if \*debt deductions of the entity for the income year are disallowed under subsection 820‑43(1) and the amount disallowed is worked out in accordance with paragraph 820‑45(1)(a) (fixed ratio test applies)—the amount disallowed; or

(b) otherwise—zero.

(2) Subsection (3) applies if:

(a) an entity has *not* made a choice under subsection 820‑43(3) or (4) in relation to an income year; and

(b) the entity makes a choice under subsection 820‑43(3) or (4) in relation to a subsequent income year.

(3) Despite subsection (1), for the purpose of applying section 820‑57 in respect of that subsequent income year and later income years, treat the entity as having a FRT disallowed amount of zero for every income year before that subsequent income year.

(4) Subsection (6) applies for the purposes of applying a FRT disallowed amount of an entity for an income year (the ***disallowance year***) under paragraph 820‑57(2)(b), in order to work out the an amount of a deduction from its assessable income for another income year (the ***deduction year***) under subsection 820‑57(1).

(5) However, subsection (6) applies only if the entity is a company.

(6) Despite subsection (1), treat the FRT disallowed amount for the disallowance year as being zero unless, assuming that the modifications set out in subsection (7) were made:

(a) the company would meet the conditions in section 165‑12 (company must maintain the same owners); and

(b) the conditions in one or more of paragraphs 165‑15(1)(a), (b) and (c) (the same people must control the voting power) do not exist in relation to the company.

(7) For the purposes of subsection (6), the modifications are as follows:

(a) treat the FRT disallowed amount as the company’s \*tax loss;

(b) treat the disallowance year as the \*loss year;

(c) treat the period from the start of the disallowance year to the end of the deduction year as the \*ownership test period;

(d) disregard the following provisions:

(i) subsection 165‑12(1);

(ii) subsection 165‑115B(3);

(iii) subsection 415‑35(3).

(8) To avoid doubt, in applying subsection (6), have regard to Divisions 165, 166 and 167.

Subdivision 820‑AB—External third party debt concepts

Guide to Subdivision 820‑AB

820‑60 What this Subdivision is about

{to be drafted}

Table of sections

Operative provisions

Operative provisions

820‑61 Meaning of *external third party earnings limit* and *external third‑party debt conditions*

(1) An entity’s ***external third party earnings limit*** for an income year is the sum of each \*debt deduction of the entity for the income year that is attributable to a \*debt interestissued by the entity that satisfies the \*external third‑party debt conditions in relation to the income year.

(2) A \*debt interest issued by an entity satisfies the ***external third‑party debt conditions*** in relation to an income yearif the following conditions are satisfied:

(a) the entity issued the debt interest to an entity that is not an \*associate entity (see subsection (9)) of the entity; and

(b) the debt interest is not held at any time in the income year by an entity that is an associate entity of the entity;

(c) the holder of the debt interest has recourse for payment of the debt only to the assets of the entity;

(d) the entity uses the proceeds of issuing the debt interest wholly to fund its investments covered by subsection (3) and its Australian operations.

(3) This subsection covers investments that relate only to:

(a) assets that are attributable to the entity’s \*Australian permanent establishments; or

(b) assets that the entity holds for the purposes of producing assessable income.

(4) If the condition in subsection (5) is met in relation to the income year, in applying subsection (2) in relation to a relevant debt interest mentioned in subsection (5):

(a) treat the conditions in paragraphs (2)(a) and (b) as being satisfied; and

(b) treat the reference in paragraph (2)(c) to the assets of the entity as being a reference to:

(i) the assets of the entity; and

(ii) the assets of each other borrower mentioned in subsection (5).

(5) This subsection applies in relation to an income year (the ***relevant year***) if:

(a) an entity (the ***conduit financer***) issued a \*debt interest (the ***ultimate debt interest***) to another entity (the ***ultimate lender***); and

(b) one or more other entities (the ***borrowers***) are \*associate entities of each other; and

(c) each borrower issued a debt interest (a ***relevant debt interest***) to the conduit financer; and

(d) the conduit financer financed the amount loaned under each relevant debt interest only with proceeds from the ultimate debt interest; and

(e) the terms of each relevant debt interest are the same as the terms of the ultimate debt interest (other than terms as to the amount of the debt); and

(f) the ultimate debt interest:

(i) satisfies the \*external third‑party debt conditions in relation to any income year; or

(ii) would satisfy the external third‑party debt conditions in relation to any income year if paragraph (2)(c) were disregarded; and

(g) the ultimate lender has recourse for payment of the ultimate debt interest only to:

(i) the assets of each borrower; and

(ii) each asset of the conduit financer that is a relevant debt interest; and

(h) a choice under subsection (6) for the relevant year has been made by:

(i) the conduit financer; and

(ii) each borrower.

(6) An entity may make a choice under this subsection for an income year for the purposes of this section.

(7) A choice under subsection (6) must be:

(a) made in the \*approved form; and

(b) made on or before the earlier of the following days:

(i) the day the entity lodges its \*income tax return for the income year;

(ii) the day the entity is required to lodge its income tax return for the income year.

(8) A choice under subsection (6) cannot be revoked.

(9) For the purposes of this section, in determining whether an entity is an ***associate entity*** of another entity, treat the reference in paragraph 820‑905(1)(a) to “an \*associate interest of 50% or more” as instead being a reference to “a \*TC control interest of 10% or more”.

13 Subsections 820‑85(1) and (2)

Repeal the subsections, substitute:

Thin capitalisation rule

(1A) Subsection (1) applies if:

(a) an entity is an \*outward investing financial entity (non‑ADI) (see subsection (2)) for all of an income year; and

(b) either:

(i) the entity has made a choice under subsection (2A) in relation to the income year; or

(ii) otherwise—the entity’s \*adjusted average debt (see subsection (3)) for the income year exceeds its \*maximum allowable debt (see section 820‑90) for the income year.

Note: This Subdivision does not apply if the total debt deductions of that entity and all its associate entities for that year are $2 million or less, see section 820‑35.

(1) This subsection disallows:

(a) if paragraph (1A)(b)(i) applies—all or part of the entity’s \*debt deductions for the income year (to the extent that they are not attributable to an \*overseas permanent establishment of the entity); or

(b) if paragraph (1A)(b)(ii) applies—all or a part of each debt deduction of the entity for the income year (to the extent that it is not attributable to an overseas permanent establishment of the entity).

Note 1: To work out the amount to be disallowed, see section 820‑115.

Note 2: For the rules that apply to an entity that is an outward investing financial entity (non‑ADI) for only a part of an income year, see section 820‑120 in conjunction with subsection (2) of this section.

Note 3: A consolidated group or MEC group may be an outward investing financial entity (non‑ADI) to which this Subdivision applies: see Subdivisions 820‑FA and 820‑FB.

Outward investing financial entity (non‑ADI)

(2) The entity is an ***outward investing financial entity (non‑ADI)*** for a period that is all or a part of an income year if, and only if, it is an \*outward investor (financial) for that period (as set out in items 2 and 4 of the following table).

| **Outward investing financial entity (non‑ADI)** | | | |
| --- | --- | --- | --- |
| **Item** | **If:** | **and:** | **then:** |
| 2 | the entity (the***relevant entity***) is one or both of the following throughout a period that is all or a part of an income year:  (a) an \*Australian controller of at least one \*Australian controlled foreign entity (not necessarily the same Australian controlled foreign entity throughout that period);  (b) an Australian entity that carries on a \*business at or through at least one \*overseas permanent establishment (not necessarily the same permanent establishment throughout that period) | the relevant entity is a \*financial entity throughout that period | the relevant entity is an ***outward investor (financial)*** for that period |
| 4 | (a) the entity (the relevant entity) is an \*Australian entity throughout a period that is all or a part of an income year; and  (b) throughout that period, the relevant entity is an \*associate entity of another Australian entity; and  (c) that other Australian entity is an \*outward investing financial entity (non‑ADI) or an \*outward investing entity (ADI) for that period | the relevant entity is a \*financial entity throughout that period | the relevant entity is an ***outward investor (financial)*** for that period |

Note: To determine whether an entity is an Australian controller of an Australian controlled foreign entity, see Subdivision 820‑H.

(2A) An entity that is an \*outward investing financial entity (non‑ADI) for a period that is all or part of an income year may make a choice under this subsection to apply the external third party debt test in relation to that income year.

(2B) A choice under subsection (2A) must be:

(a) made in the \*approved form; and

(b) made on or before the earlier of the following days:

(i) the day the entity lodges its \*income tax return for the income year;

(ii) the day the entity is required to lodge its income tax return for the income year.

(2C) A choice under subsection (2A) cannot be revoked.

14 Subsection 820‑90(1)

Omit “an \*inward investment vehicle (general) or”.

15 Paragraph 820‑90(1)(b)

Repeal the paragraph.

16 Subsection 820‑90(1) (notes 1 and 2)

Repeal the notes.

17 Subsection 820‑90(2)

Omit “an \*inward investment vehicle (general) or”.

18 Paragraph 820‑90(2)(b)

Repeal the paragraph.

19 Subsection 820‑90(2) (notes 1 and 2)

Repeal the notes.

20 Section 820‑95

Repeal the section.

21 Section 820‑105

Repeal the section.

22 Subsection 820‑110(1)

Repeal the subsection.

23 Subsection 820‑111(1)

Repeal the subsection.

24 Section 820‑115

Insert:

(1) If subparagraph 820‑85(1A)(b)(i) applies, the amount (the ***total disallowed amount***) disallowed under subsection 820‑85(1) of the \*debt deductions of an entity for an income year is the amount by which those debt deductions (to the extent that they are not attributable to an \*overseas permanent establishment of the entity) exceed the entity’s \*external third party earnings limit for the income year (see section 820‑61).

Note: The disallowed amount also does not form part of the cost base of a CGT asset. See section 110‑54.

(2) The amount by which a particular \*debt deduction is disallowed as a result of subsection (1) is worked out as follows:

(a) first, divide the total disallowed amount by the \*debt deductions of the entity for the income year;

(b) next, multiply the amount of the particular debt deduction by the result of paragraph (a).

25 Section 820‑115

Omit:

The amount of \*debt deduction disallowed under subsection 820‑85(1) is worked out using the following formula:

Substitute:

(3) If subparagraph 820‑85(1A)(b)(ii) applies, the amount of a \*debt deduction of an entity for an income year disallowed under subsection 820‑85(1) is worked out using the following formula:

26 Subsections 820‑185(1) and (2)

Repeal the subsections, substitute:

Thin capitalisation rule

(1A) Subsection (1) applies if:

(a) an entity is an \*inward investing financial entity (non‑ADI) (see subsection (2)) for all of an income year, but is not also an \*outward investing financial entity (non‑ADI) (see section 820‑85) for all or any part of that year; and

(b) either:

(i) the entity has made a choice under subsection (2A) in relation to the income year; or

(ii) otherwise—the entity’s \*adjusted average debt (see subsection (3)) for the income year exceeds its \*maximum allowable debt (see section 820‑190) for the income year.

Note: This Subdivision does not apply if the total debt deductions of that entity and all its associate entities for that year are $2 million or less, see section 820‑35.

(1) This subsection disallows:

(a) if paragraph (1A)(b)(i) applies—all or part of the entity’s \*debt deductions for the income year; or

(b) if paragraph (1A)(b)(ii) applies—all or a part of each debt deduction of the entity for the income year.

Note 1: To work out the amount to be disallowed, see section 820‑220.

Note 2: For the rules that apply to an entity that is an outward investing financial entity (non‑ADI) as well as an inward investing financial entity (non‑ADI), see Subdivision 820‑B.

Note 3: For the rules that apply to an entity that is an inward investing financial entity (non‑ADI) for only a part of an income year, see section 820‑225 in conjunction with subsection (2) of this section.

Note 4: To calculate an average value for the purposes of this Division, see Subdivision 820‑G.

Note 5: A consolidated group or MEC group may be an inward investing financial entity (non‑ADI) to which this Subdivision applies: see Subdivisions 820‑FA and 820‑FB.

Inward investing financial entity (non‑ADI)

(2) The entity is an ***inward investing financial entity (non‑ADI)*** for a period that is all or a part of an income year if, and only if, it is:

(b) an \*inward investment vehicle (financial) for that period (as set out in item 2 of the following table); or

(d) an \*inward investor (financial) for that period (as set out in item 4 of that table).

| **Inward investing financial entity (non‑ADI)** | | | |
| --- | --- | --- | --- |
| **Item** | **If the entity is a:** | **and the entity:** | **the entity is an:** |
| 2 | \*foreign controlled Australian entity throughout a period that is all or a part of an income year | is a \*financial entity throughout that period | ***inward investment vehicle (financial)*** for that period |
| 4 | \*foreign entity throughout a period that is all or a part of an income year | is a \*financial entity throughout that period | ***inward investor (financial)*** for that period |

Note 1: To determine whether an entity is a foreign controlled Australian entity, see Subdivision 820‑H.

Note 2: An entity covered by item 4 of the table may be required to keep certain records, see Subdivision 820‑L.

(2A) An entity that is an \*inward investing financial entity (non‑ADI) for a period that is all or part of an income year may make a choice under this subsection to apply the external third party debt test in relation to that income year.

(2B) A choice under subsection (2A) must be:

(a) made in the \*approved form; and

(b) made on or before the earlier of the following days:

(i) the day the entity lodges its \*income tax return for the income year;

(ii) the day the entity is required to lodge its income tax return for the income year.

(2C) A choice under subsection (2A) cannot be revoked.

27 Subsection 820‑185(3) (method statement, step 2, paragraph (a))

Omit “an \*inward investment vehicle (general) or”.

28 Subsection 820‑185(3) (method statement, step 2, paragraph (b))

Omit “an \*inward investor (general) or”.

29 Paragraph 820‑190(1)(b)

Repeal the paragraph.

30 Subsection 820‑190(1) (notes 1 and 2)

Repeal the notes.

31 Section 820‑195

Repeal the section.

32 Section 820‑205

Repeal the section.

33 Section 820‑215

Repeal the section.

34 Section 820‑216

Repeal the section.

35 Section 820‑218

Repeal the section.

36 Section 820‑220

Insert:

(1) If subparagraph 820‑185(1A)(b)(i) applies, the amount (the ***total disallowed amount***) disallowed under subsection 820‑185(1) of the \*debt deductions of an entity for an income year is the amount by which those debt deductions exceed the entity’s \*external third party earnings limit for the income year (see section 820‑61).

Note: The disallowed amount also does not form part of the cost base of a CGT asset. See section 110‑54.

(2) The amount by which a particular \*debt deduction is disallowed as a result of subsection (1) is worked out as follows:

(a) first, divide the total disallowed amount by the \*debt deductions of the entity for the income year;

(b) next, multiply the amount of the particular debt deduction by the result of paragraph (a).

37 Section 820‑220

Omit:

The amount of \*debt deduction disallowed under subsection 820‑185(1) is worked out using the following formula:

Substitute:

(3) If subparagraph 820‑185(1A)(b)(ii) applies, the amount of a \*debt deduction of an entity for an income year disallowed under subsection 820‑185(1) is worked out using the following formula:

38 Subsection 820‑225(2) (method statement, step 2, paragraph (a))

Omit “an \*inward investment vehicle (general) or”.

39 Subsection 820‑225(2) (method statement, step 2, paragraph (b))

Omit “an \*inward investor (general) or”.

40 Subsections 820‑583(1) and (2)

Repeal the subsections, substitute:

General class investor

(1) The \*head company of a \*consolidated group or of a \*MEC group is a ***general class investor*** for a period that is all or part of an income year if:

(a) for that period, the head company satisfies the requirement in subsection 820‑43(2); and

(b) no \*member of the group is a \*financial entity or \*ADI at any time during that period.

Outward investing financial entity (non‑ADI)

(2) The \*head company of a \*consolidated group or of a \*MEC group is an ***outward investing financial entity (non‑ADI)*** for a period that is all or part of an income year if, and only if, it is an \*outward investor (financial) for that period (because of subsection (3)).

41 Paragraph 820‑583(3)(a)

Omit “item 1 or 3”, substitute “item 2 or 4”.

42 Subsections 820‑583(4) and (5)

Repeal the subsections, substitute:

Inward investing financial entity (non‑ADI)

(4) The \*head company of a \*consolidated group or of a \*MEC group is an inward investing financial entity (non‑ADI) for a period that is all or part of an income year if, and only if, it is an \*inward investment vehicle (financial) for that period (because of subsection (6)).

43 At the end of Subdivision 820‑FA

Add:

820‑62 Treatment of FRT disallowed amounts—joining case

(1) This section applies if:

(a) an entity (the ***joining entity***) becomes a \*member of a \*consolidated group (the ***joined group***) at a time (the ***joining time***) in an income year (the ***joining year***); and

(b) the joining entity had a \*FRT disallowed amount for an income year ending before the joining time.

(2) Subject to subsection (3), the \*FRT disallowed amount is transferred at the joining time from the joining entity to the \*head company of the joined group (even if they are the same entity).

(3) To avoid doubt, the result of the transfer under subsection (2) is that the \*head company of the joined group has the \*FRT disallowed amount for the income year mentioned in paragraph (1)(b).

(4) The \*FRT disallowed amount is transferred under subsection (2) only to the extent (if any) that the FRT disallowed amount could have been applied by the joining entity under paragraph 820‑57(2)(b) in respect of an income year (the ***trial year***) consisting of the period described in subsection (4) if:

(a) at the joining time, the joining entity had not become a \*member of the joined group (but had been a \*wholly‑owned subsidiary of the \*head company if the joining entity is not the head company); and

(b) the amount applied by the joining entity under paragraph 820‑57(2)(b) in respect of the trial year were not limited by the joining entity’s excess mentioned in paragraph 820‑57(2)(b) in respect of the trial year.

(5) For the purposes of subsection (4), the period is the period:

(a) starting at the latest of these times:

(i) the time 12 months before the joining time;

(ii) the time the joining entity came into existence;

(iii) the time the joining entity last ceased to be a \*subsidiary member of a \*consolidated group, if the joining entity had been a member of a consolidated group before the joining time but was not a \*member of a consolidated group just before the joining time; and

(b) ending just after the joining time.

(6) If the \*FRT disallowed amount was for an income year all or part of which occurs in the trial year, the transfer of the FRT disallowed amount under subsection (2) is not prevented by the fact that the FRT disallowed amount was for that income year.

(7) For the purposes of subsection 820‑59(6) and (7), to the extent that the \*FRT disallowed amount is transferred under subsection (2) from the joining entity to the \*head company of the joined group, this Act operates (except so far as the contrary intention appears) for the purposes of income years ending after the joining time as if the head company had the FRT disallowed amount for the income year in which the joining time occurs.

(8) To the extent that the \*FRT disallowed amount is not transferred under subsection (2) from the joining entity to the \*head company of the joined group, the FRT disallowed amount cannot be applied under paragraph 820‑57(2)(b) by any entity in respect of an income year ending after the joining time.

(9) If, apart from this subsection, the \*head company of the joined group would have 2 or more \*FRT disallowed amounts (the ***transferred FRT disallowed amounts***) for a particular income year as a result of the operation of subsection (2):

(a) treat it as having only one FRT disallowed amount for the income year; and

(b) treat that one FRT disallowed amount as being equal to the sum of the transferred FRT disallowed amounts.

820‑63 Treatment of FRT disallowed amounts—leaving case

To avoid doubt, if the \*head company of a \*consolidated group has a \*FRT disallowed amount and an entity ceases to be a \*subsidiary member of the group, the entity is not taken because of section 701‑40 (the exit history rule) to have the FRT disallowed amount.

44 After section 820‑980

Insert:

820‑985 Records about group ratio

(1) An entity must keep records under this section for a \*group ratio that the entity worked out for the purposes of this Division.

(2) The records must:

(a) contain particulars that have been taken into account in working out the \*group ratio; and

(b) be sufficient for a reasonable person to understand how the group ratio has been worked out.

(3) The entity must prepare the records before the time by which the entity must lodge its \*income tax return for the income year in relation to all or a part of which the amount is worked out.

Note: A person must comply with the requirements in section 262A of the *Income Tax Assessment Act 1936* about the keeping of these records (see subsections (2AA) and (3) of that section).

45 After subsection 820‑905(1)

Insert:

(1A) Subsection (1) does not apply to a trustee of a \*complying superannuation entity (other than a \*self managed superannuation fund).

46 Subsection 995‑1(1)

Insert:

***adjusted net third party interest expense*** has the meaning given by section 820‑53.

47 Subsection 995‑1(1) (definition of *arm’s length debt amount*)

Repeal the definition.

48 Subsection 995‑1(1)

Insert:

***entity EBITDA*** has the meaning given by section 820‑55.

***external third‑party debt conditions*** has the meaning given by section 820‑61.

***external third party earnings limit*** has the meaning given by section 820‑61.

49 Subsection 995‑1(1) (paragraph (a) of the definition of *financial entity*)

Repeal the paragraph.

50 Subsection 995‑1(1)

Insert:

***financial statement net third party interest expense*** has the meaning given by section 820‑53.

***fixed ratio earnings limit*** has the meaning given by section 820‑47.

***fixed ratio test disallowed amount*** has the meaning given by section 820‑59.

***FRT disallowed amount***: see ***fixed ratio test disallowed amount .***

***general class investor*** has the meaning given by subsection 820‑43(2).

***GR group*** has the meaning given by section 820‑51.

***GR group member*** has the meaning given by section 820‑51.

***GR group net third party interest expense*** has the meaning given by section 820‑53.

***GR group parent*** has the meaning given by section 820‑51.

***group EBITDA*** has the meaning given by section 820‑55.

***group ratio*** has the meaning given by section 820‑51.

***group ratio earnings limit*** has the meaning given by section 820‑47.

51 Subsection 995‑1(1) (definition of *inward investment vehicle (general)*)

Repeal the definition.

52 Subsection 995‑1(1) (definition of *inward investing entity (non‑ADI)*)

Repeal the definition.

53 Subsection 995‑1(1)

Insert:

***inward investing financial entity (non‑ADI)*** has the meaning given by section 820‑185

54 Subsection 995‑1(1) (definition of *inward investor (general)*)

Repeal the definition.

55 Subsection 995‑1(1)

Insert:

***net debt deductions*** has the meaning given by section 820‑45.

56 Subsection 995‑1(1) (definition of *outward investing entity (non‑ADI)*)

Repeal the definition.

57 Subsection 995‑1(1)

Insert:

***outward investing financial entity (non‑ADI)*** has the meaning given by section 820‑85

58 Subsection 995‑1(1) (definition of *outward investor (general)*)

Repeal the definition.

59 Subsection 995‑1(1) (paragraphs (a), (c) and (e) of the definition of *safe harbour debt amount*)

Repeal the paragraphs.

60 Subsection 995‑1(1)

Insert:

***tax EBITDA*** has the meaning given by section 820‑49.

61 Subsection 995‑1(1) (paragraphs (b) and (d) of the definition of *worldwide gearing debt amount*)

Repeal the paragraphs.

Part 2—Application

62 Application

The amendments made by Part 1 of this Schedule apply in relation to assessments for income years starting on or after 1 July 2023.