

# EXPOSURE DRAFT

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

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**Commencement information**

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

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## 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
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##### **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

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1 under section 820-62, to the extent that they were not applied by  
2 the joining entity under paragraph 820-57(2)(b) in respect of the  
3 income year in which the joining time occurred or any earlier  
4 income year.

## 5 **6 After paragraph 815-140(1)(a)**

6 Insert:

7 (aa) the entity:

- 8 (i) is *not* a \*general class investor in relation to the income  
9 year; and  
10 (ii) has *not* made a choice under subsection 820-85(2A) or  
11 820-185(2A) in relation to the income year; and

## 12 **7 Section 820-35**

13 Omit “Subdivision 820-B”, substitute “Subdivision 820-AA, 820-B”.

## 14 **8 Paragraph 820-37(1)(a)**

15 Repeal the paragraph, substitute:

16 (a) either:

- 17 (i) the entity is an \*outward investing financial entity  
18 (non-ADI) or an \*outward investing entity (ADI) for a  
19 period that is all or any part of that year (and is not a  
20 \*general class investor for that year); or  
21 (ii) assuming that the entity were a \*financial entity for all  
22 of that year, it would be, for all of that year, an outward  
23 investing financial entity (non-ADI) and *not* an inward  
24 investing financial entity (non-ADI); and

## 25 **9 Subsection 820-40(1)**

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

## 27 **10 Subparagraph 820-40(1)(a)(ii)**

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

## 30 **11 Subparagraph 820-40(1)(a)(iii)**

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

## 33 **12 After Subdivision 820-A**

34 Insert:

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## 1 Subdivision 820-AA—Thin capitalisation rules for general class 2 investors

### 3 Guide to Subdivision 820-AA

#### 4 820-41 What this Subdivision is about

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

#### 9 Table of sections

##### 10 Operative provisions

#### 11 Operative provisions

#### 12 820-43 Thin capitalisation rule for general class investors

##### 13 *Thin capitalisation rule*

- 14 (1) This subsection disallows all or part of an entity's \*debt deductions  
15 for an income year if, for that year:
- 16 (a) the entity is a \*general class investor (see subsection (2)); and
  - 17 (b) the entity:
    - 18 (i) has *not* made a choice under subsection (3) or (4) (fixed  
19 ratio test applies); or
    - 20 (ii) has made a choice under subsection (3) (group ratio test  
21 applies); or
    - 22 (iii) has made a choice under subsection (4) (external third  
23 party debt test applies).

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

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

28 Note 3: A consolidated group or MEC group may be a general class investor  
29 to which this Subdivision applies: see Subdivisions 820-FA and  
30 820-FB.

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*General class investor*

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- (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.

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

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

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

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

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

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

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

## 14 **820-45 Amount of debt deduction disallowed**

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

18 (a) if the entity has *not* made a choice under subsection  
19 820-43(3) or (4) in relation to the income year (fixed ratio  
20 test applies)—the amount by which the entity’s \*net debt  
21 deductions for the income year exceed the entity’s \*fixed  
22 ratio earnings limit for the income year (see section 820-47);  
23 or

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

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

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

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

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- 1 (a) first, divide the total disallowed amount by the \*debt  
2 deductions of the entity for the income year;  
3 (b) next, multiply the amount of the particular debt deduction by  
4 the result of paragraph (a).
- 5 (3) An entity's *net debt deductions* for an income year is worked out  
6 as follows:  
7 (a) first, work out the sum of the entity's \*debt deductions for the  
8 income year;  
9 (b) next, work out the sum of each amount included in the  
10 entity's assessable income for that year that is:  
11 (i) interest; or  
12 (ii) an amount in the nature of interest; or  
13 (iii) any other amount that is calculated by reference to the  
14 time value of money;  
15 (c) next, subtract the result of paragraph (b) from the result of  
16 paragraph (a).

## 17 **820-47 Meaning of *fixed ratio earnings limit* and *group ratio earnings*** 18 ***limit***

- 19 (1) An entity's *fixed ratio earnings limit* for an income year is 30% of  
20 its \*tax EBITDA for the income year.
- 21 (2) An entity's *group ratio earnings limit* for an income year is its  
22 \*group ratio for the income year multiplied by its \*tax EBITDA for  
23 the income year.

## 24 **820-49 Meaning of *tax EBITDA***

- 25 An entity's *tax EBITDA* for an income year is worked out as  
26 follows:  
27 (a) first, work out the entity's taxable income or \*tax loss for the  
28 income year (disregarding the operation of this Division and  
29 treating a tax loss as a negative amount);  
30 (b) next, add the entity's \*net debt deductions for the income  
31 year;  
32 (c) next, add the sum of the entity's deductions (if any) under  
33 Subdivision 40-B and Division 43 for the income year from  
34 its assessable income for the income year;  
35 (d) next, add the sum of each of the entity's tax losses for earlier  
36 income years, to the extent that they are deducted under

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1 Division 36 from its assessable income for the income year;  
2 and

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

## 4 **820-51 Meaning of *group ratio*, *GR group*, *GR group parent* and *GR*** 5 ***group member***

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

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

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

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

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

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

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

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

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

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

## 28 **820-53 Meaning of *GR group net third party interest expense* and** 29 ***financial statement net third party interest expense***

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

36 (a) an amount in the nature of interest;



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

## 6 **820-55 Meaning of *entity EBITDA* and *GR group EBITDA***

- 7 (1) The *entity EBITDA*, of an entity for a period, is the sum of the  
8 following for the entity for the period:  
9 (a) the entity’s net profit (disregarding tax expenses);  
10 (b) the entity’s \*adjusted net third party interest expense;  
11 (c) the entity’s depreciation and amortisation expenses.
- 12 (2) The *GR group EBITDA*, for a period, of a \*GR group for the  
13 period, is the sum of the following, as disclosed in the \*audited  
14 consolidated financial statements for the period, for the GR group:  
15 (a) the GR group’s net profit (disregarding tax expenses);  
16 (b) the GR group’s \*adjusted net third party interest expense;  
17 (c) the GR group’s depreciation and amortisation expenses.
- 18 (3) For the purposes of subsection (2), in working out the \*GR group’s  
19 \*GR group EBITDA for the period, if a \*GR group member for the  
20 period of the GR group has an \*entity EBITDA for the period of  
21 less than zero, disregard that entity EBITDA.

## 22 **820-57 Special deduction for previously FRT disallowed amounts—** 23 **fixed ratio test**

- 24 (1) An entity can deduct the amount worked out under subsection (2)  
25 from its assessable income for the income year if:  
26 (a) the entity has *not* made a choice under subsection 820-43(3)  
27 or (4) in relation to the income year (fixed ratio test applies);  
28 and  
29 (b) the entity’s \*fixed ratio earnings limit for the income year  
30 exceeds the sum of the entity’s \*net debt deductions for the  
31 income year.
- 32 (2) Work out the amount of the deduction as follows:  
33 (a) first, work out the amount of the excess mentioned in  
34 paragraph (1)(b);  
35 (b) next, apply against that excess each of the entity’s \*FRT  
36 disallowed amounts for the previous 15 income years (to the

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1 extent that they have not already been applied under this  
2 paragraph in respect of any of those previous income years).  
3 The amount of the deduction is the total amount applied under  
4 paragraph (b).

- 5 (3) For the purposes of paragraph (2)(b):  
6 (a) apply \*FRT disallowed amounts in sequence, where a FRT  
7 disallowed amount for an earlier income year is applied  
8 before a FRT disallowed amount from a later income year;  
9 and  
10 (b) apply FRT disallowed amounts up to, but not beyond, the  
11 excess mentioned in paragraph (1)(b).

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

## 14 **820-59 Meaning of *FRT disallowed amount***

- 15 (1) An entity has a *fixed ratio test disallowed amount* (or *FRT*  
16 *disallowed amount*) for an income year equal to:  
17 (a) if \*debt deductions of the entity for the income year are  
18 disallowed under subsection 820-43(1) and the amount  
19 disallowed is worked out in accordance with  
20 paragraph 820-45(1)(a) (fixed ratio test applies)—the amount  
21 disallowed; or  
22 (b) otherwise—zero.
- 23 (2) Subsection (3) applies if:  
24 (a) an entity has *not* made a choice under subsection 820-43(3)  
25 or (4) in relation to an income year; and  
26 (b) the entity makes a choice under subsection 820-43(3) or (4)  
27 in relation to a subsequent income year.
- 28 (3) Despite subsection (1), for the purpose of applying section 820-57  
29 in respect of that subsequent income year and later income years,  
30 treat the entity as having a FRT disallowed amount of zero for  
31 every income year before that subsequent income year.
- 32 (4) Subsection (6) applies for the purposes of applying a FRT  
33 disallowed amount of an entity for an income year (the  
34 *disallowance year*) under paragraph 820-57(2)(b), in order to work  
35 out the an amount of a deduction from its assessable income for  
36 another income year (the *deduction year*) under  
37 subsection 820-57(1).

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- 1 (5) However, subsection (6) applies only if the entity is a company.
- 2 (6) Despite subsection (1), treat the FRT disallowed amount for the  
3 disallowance year as being zero unless, assuming that the  
4 modifications set out in subsection (7) were made:
- 5 (a) the company would meet the conditions in section 165-12  
6 (company must maintain the same owners); and
- 7 (b) the conditions in one or more of paragraphs 165-15(1)(a), (b)  
8 and (c) (the same people must control the voting power) do  
9 not exist in relation to the company.
- 10 (7) For the purposes of subsection (6), the modifications are as  
11 follows:
- 12 (a) treat the FRT disallowed amount as the company's \*tax loss;
- 13 (b) treat the disallowance year as the \*loss year;
- 14 (c) treat the period from the start of the disallowance year to the  
15 end of the deduction year as the \*ownership test period;
- 16 (d) disregard the following provisions:
- 17 (i) subsection 165-12(1);
- 18 (ii) subsection 165-115B(3);
- 19 (iii) subsection 415-35(3).
- 20 (8) To avoid doubt, in applying subsection (6), have regard to  
21 Divisions 165, 166 and 167.

## 22 **Subdivision 820-AB—External third party debt concepts**

### 23 **Guide to Subdivision 820-AB**

#### 24 **820-60 What this Subdivision is about**

25 {to be drafted}

#### 26 **Table of sections**

27 **Operative provisions**

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## 1 Operative provisions

### 2 **820-61 Meaning of *external third party earnings limit* and *external*** 3 ***third-party debt conditions***

- 4 (1) An entity's *external third party earnings limit* for an income year  
5 is the sum of each \*debt deduction of the entity for the income year  
6 that is attributable to a \*debt interest issued by the entity that  
7 satisfies the \*external third-party debt conditions in relation to the  
8 income year.
- 9 (2) A \*debt interest issued by an entity satisfies the *external*  
10 *third-party debt conditions* in relation to an income year if the  
11 following conditions are satisfied:
- 12 (a) the entity issued the debt interest to an entity that is not an  
13 \*associate entity (see subsection (9)) of the entity; and
  - 14 (b) the debt interest is not held at any time in the income year by  
15 an entity that is an associate entity of the entity;
  - 16 (c) the holder of the debt interest has recourse for payment of the  
17 debt only to the assets of the entity;
  - 18 (d) the entity uses the proceeds of issuing the debt interest  
19 wholly to fund its investments covered by subsection (3) and  
20 its Australian operations.
- 21 (3) This subsection covers investments that relate only to:
- 22 (a) assets that are attributable to the entity's \*Australian  
23 permanent establishments; or
  - 24 (b) assets that the entity holds for the purposes of producing  
25 assessable income.
- 26 (4) If the condition in subsection (5) is met in relation to the income  
27 year, in applying subsection (2) in relation to a relevant debt  
28 interest mentioned in subsection (5):
- 29 (a) treat the conditions in paragraphs (2)(a) and (b) as being  
30 satisfied; and
  - 31 (b) treat the reference in paragraph (2)(c) to the assets of the  
32 entity as being a reference to:
    - 33 (i) the assets of the entity; and
    - 34 (ii) the assets of each other borrower mentioned in  
35 subsection (5).
- 36 (5) This subsection applies in relation to an income year (the *relevant*  
37 *year*) if:
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- 1 (a) an entity (the *conduit financier*) issued a \*debt interest (the  
2 *ultimate debt interest*) to another entity (the *ultimate lender*);  
3 and  
4 (b) one or more other entities (the *borrowers*) are \*associate  
5 entities of each other; and  
6 (c) each borrower issued a debt interest (a *relevant debt interest*)  
7 to the conduit financier; and  
8 (d) the conduit financier financed the amount loaned under each  
9 relevant debt interest only with proceeds from the ultimate  
10 debt interest; and  
11 (e) the terms of each relevant debt interest are the same as the  
12 terms of the ultimate debt interest (other than terms as to the  
13 amount of the debt); and  
14 (f) the ultimate debt interest:  
15 (i) satisfies the \*external third-party debt conditions in  
16 relation to any income year; or  
17 (ii) would satisfy the external third-party debt conditions in  
18 relation to any income year if paragraph (2)(c) were  
19 disregarded; and  
20 (g) the ultimate lender has recourse for payment of the ultimate  
21 debt interest only to:  
22 (i) the assets of each borrower; and  
23 (ii) each asset of the conduit financier that is a relevant debt  
24 interest; and  
25 (h) a choice under subsection (6) for the relevant year has been  
26 made by:  
27 (i) the conduit financier; and  
28 (ii) each borrower.
- 29 (6) An entity may make a choice under this subsection for an income  
30 year for the purposes of this section.
- 31 (7) A choice under subsection (6) must be:  
32 (a) made in the \*approved form; and  
33 (b) made on or before the earlier of the following days:  
34 (i) the day the entity lodges its \*income tax return for the  
35 income year;  
36 (ii) the day the entity is required to lodge its income tax  
37 return for the income year.
- 38 (8) A choice under subsection (6) cannot be revoked.
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- 1 (9) For the purposes of this section, in determining whether an entity is  
2 an *associate entity* of another entity, treat the reference in  
3 paragraph 820-905(1)(a) to “an \*associate interest of 50% or more”  
4 as instead being a reference to “a \*TC control interest of 10% or  
5 more”.

## 6 **13 Subsections 820-85(1) and (2)**

7 Repeal the subsections, substitute:

### 8 *Thin capitalisation rule*

9 (1A) Subsection (1) applies if:

- 10 (a) an entity is an \*outward investing financial entity (non-ADI)  
11 (see subsection (2)) for all of an income year; and  
12 (b) either:  
13 (i) the entity has made a choice under subsection (2A) in  
14 relation to the income year; or  
15 (ii) otherwise—the entity’s \*adjusted average debt (see  
16 subsection (3)) for the income year exceeds its  
17 \*maximum allowable debt (see section 820-90) for the  
18 income year.

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

22 (1) This subsection disallows:

- 23 (a) if paragraph (1A)(b)(i) applies—all or part of the entity’s  
24 \*debt deductions for the income year (to the extent that they  
25 are not attributable to an \*overseas permanent establishment  
26 of the entity); or  
27 (b) if paragraph (1A)(b)(ii) applies—all or a part of each debt  
28 deduction of the entity for the income year (to the extent that  
29 it is not attributable to an overseas permanent establishment  
30 of the entity).

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

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

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

# EXPOSURE DRAFT

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*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).

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**Outward investing financial entity (non-ADI)**

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<b>Item</b>	<b>If:</b>	<b>and:</b>	<b>then:</b>
2	the entity (the <b><i>relevant entity</i></b> ) 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 <b><i>outward investor (financial)</i></b> 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 <b><i>outward investor (financial)</i></b> 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.



# EXPOSURE DRAFT

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1 (2B) A choice under subsection (2A) must be:

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

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

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

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

8 (2C) A choice under subsection (2A) cannot be revoked.

9 **14 Subsection 820-90(1)**

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

11 **15 Paragraph 820-90(1)(b)**

12 Repeal the paragraph.

13 **16 Subsection 820-90(1) (notes 1 and 2)**

14 Repeal the notes.

15 **17 Subsection 820-90(2)**

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

17 **18 Paragraph 820-90(2)(b)**

18 Repeal the paragraph.

19 **19 Subsection 820-90(2) (notes 1 and 2)**

20 Repeal the notes.

21 **20 Section 820-95**

22 Repeal the section.

23 **21 Section 820-105**

24 Repeal the section.

25 **22 Subsection 820-110(1)**

26 Repeal the subsection.

27 **23 Subsection 820-111(1)**

28 Repeal the subsection.

# EXPOSURE DRAFT

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## 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:

# EXPOSURE DRAFT

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- 1 (i) the entity has made a choice under subsection (2A) in  
2 relation to the income year; or  
3 (ii) otherwise—the entity’s \*adjusted average debt (see  
4 subsection (3)) for the income year exceeds its  
5 \*maximum allowable debt (see section 820-190) for the  
6 income year.

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

10 (1) This subsection disallows:

- 11 (a) if paragraph (1A)(b)(i) applies—all or part of the entity’s  
12 \*debt deductions for the income year; or  
13 (b) if paragraph (1A)(b)(ii) applies—all or a part of each debt  
14 deduction of the entity for the income year.

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

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

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

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

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

27 *Inward investing financial entity (non-ADI)*

- 28 (2) The entity is an *inward investing financial entity (non-ADI)* for a  
29 period that is all or a part of an income year if, and only if, it is:  
30 (b) an \*inward investment vehicle (financial) for that period (as  
31 set out in item 2 of the following table); or  
32 (d) an \*inward investor (financial) for that period (as set out in  
33 item 4 of that table).

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# EXPOSURE DRAFT

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## Inward investing financial entity (non-ADI)

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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	<i>inward investment vehicle (financial)</i> 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	<i>inward investor (financial)</i> for that period

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

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

5 (2A) An entity that is an \*inward investing financial entity (non-ADI)  
6 for a period that is all or part of an income year may make a choice  
7 under this subsection to apply the external third party debt test in  
8 relation to that income year.

9 (2B) A choice under subsection (2A) must be:

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

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

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

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

16 (2C) A choice under subsection (2A) cannot be revoked.

17 **27 Subsection 820-185(3) (method statement, step 2,**  
18 **paragraph (a))**

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

20 **28 Subsection 820-185(3) (method statement, step 2,**  
21 **paragraph (b))**

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

23 **29 Paragraph 820-190(1)(b)**

24 Repeal the paragraph.

# EXPOSURE DRAFT

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## 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:

# EXPOSURE DRAFT

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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:

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*Inward investing financial entity (non-ADI)*

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

7 **43 At the end of Subdivision 820-FA**

8 Add:

9 **820-62 Treatment of FRT disallowed amounts—joining case**

- 10 (1) This section applies if:
- 11 (a) an entity (the *joining entity*) becomes a \*member of a  
12 \*consolidated group (the *joined group*) at a time (the *joining*  
13 *time*) in an income year (the *joining year*); and  
14 (b) the joining entity had a \*FRT disallowed amount for an  
15 income year ending before the joining time.
- 16 (2) Subject to subsection (3), the \*FRT disallowed amount is  
17 transferred at the joining time from the joining entity to the \*head  
18 company of the joined group (even if they are the same entity).
- 19 (3) To avoid doubt, the result of the transfer under subsection (2) is  
20 that the \*head company of the joined group has the \*FRT  
21 disallowed amount for the income year mentioned in  
22 paragraph (1)(b).
- 23 (4) The \*FRT disallowed amount is transferred under subsection (2)  
24 only to the extent (if any) that the FRT disallowed amount could  
25 have been applied by the joining entity under paragraph  
26 820-57(2)(b) in respect of an income year (the *trial year*)  
27 consisting of the period described in subsection (4) if:
- 28 (a) at the joining time, the joining entity had not become a  
29 \*member of the joined group (but had been a \*wholly-owned  
30 subsidiary of the \*head company if the joining entity is not  
31 the head company); and  
32 (b) the amount applied by the joining entity under paragraph  
33 820-57(2)(b) in respect of the trial year were not limited by  
34 the joining entity's excess mentioned in paragraph  
35 820-57(2)(b) in respect of the trial year.
- 36 (5) For the purposes of subsection (4), the period is the period:
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# EXPOSURE DRAFT

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- 1 (a) starting at the latest of these times:  
2 (i) the time 12 months before the joining time;  
3 (ii) the time the joining entity came into existence;  
4 (iii) the time the joining entity last ceased to be a \*subsidiary  
5 member of a \*consolidated group, if the joining entity  
6 had been a member of a consolidated group before the  
7 joining time but was not a \*member of a consolidated  
8 group just before the joining time; and  
9 (b) ending just after the joining time.
- 10 (6) If the \*FRT disallowed amount was for an income year all or part  
11 of which occurs in the trial year, the transfer of the FRT disallowed  
12 amount under subsection (2) is not prevented by the fact that the  
13 FRT disallowed amount was for that income year.
- 14 (7) For the purposes of subsection 820-59(6) and (7), to the extent that  
15 the \*FRT disallowed amount is transferred under subsection (2)  
16 from the joining entity to the \*head company of the joined group,  
17 this Act operates (except so far as the contrary intention appears)  
18 for the purposes of income years ending after the joining time as if  
19 the head company had the FRT disallowed amount for the income  
20 year in which the joining time occurs.
- 21 (8) To the extent that the \*FRT disallowed amount is not transferred  
22 under subsection (2) from the joining entity to the \*head company  
23 of the joined group, the FRT disallowed amount cannot be applied  
24 under paragraph 820-57(2)(b) by any entity in respect of an income  
25 year ending after the joining time.
- 26 (9) If, apart from this subsection, the \*head company of the joined  
27 group would have 2 or more \*FRT disallowed amounts (the  
28 *transferred FRT disallowed amounts*) for a particular income year  
29 as a result of the operation of subsection (2):  
30 (a) treat it as having only one FRT disallowed amount for the  
31 income year; and  
32 (b) treat that one FRT disallowed amount as being equal to the  
33 sum of the transferred FRT disallowed amounts.

## 820-63 Treatment of FRT disallowed amounts—leaving case

34  
35 To avoid doubt, if the \*head company of a \*consolidated group has  
36 a \*FRT disallowed amount and an entity ceases to be a \*subsidiary  
37 member of the group, the entity is not taken because of



# EXPOSURE DRAFT

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1 section 701-40 (the exit history rule) to have the FRT disallowed  
2 amount.

## 3 **44 After section 820-980**

4 Insert:

### 5 **820-985 Records about group ratio**

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

8 (2) The records must:

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

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

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

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

## 19 **45 After subsection 820-905(1)**

20 Insert:

21 (1A) Subsection (1) does not apply to a trustee of a \*complying  
22 superannuation entity (other than a \*self managed superannuation  
23 fund).

## 24 **46 Subsection 995-1(1)**

25 Insert:

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

## 28 **47 Subsection 995-1(1) (definition of *arm's length debt* 29 *amount*)**

30 Repeal the definition.

## 31 **48 Subsection 995-1(1)**

32 Insert:

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# EXPOSURE DRAFT

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

2 *external third-party debt conditions* has the meaning given by  
3 section 820-61.

4 *external third party earnings limit* has the meaning given by  
5 section 820-61.

6 **49 Subsection 995-1(1) (paragraph (a) of the definition of**  
7 ***financial entity*)**

8 Repeal the paragraph.

9 **50 Subsection 995-1(1)**

10 Insert:

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

13 *fixed ratio earnings limit* has the meaning given by section  
14 820-47.

15 *fixed ratio test disallowed amount* has the meaning given by  
16 section 820-59.

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

18 *general class investor* has the meaning given by subsection  
19 820-43(2).

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

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

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

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

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

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

27 *group ratio earnings limit* has the meaning given by section  
28 820-47.

# EXPOSURE DRAFT

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

3 Repeal the definition.

4 **52 Subsection 995-1(1) (definition of *inward investing entity***  
5 ***(non-ADI)*)**

6 Repeal the definition.

7 **53 Subsection 995-1(1)**

8 Insert:

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

11 **54 Subsection 995-1(1) (definition of *inward investor***  
12 ***(general)*)**

13 Repeal the definition.

14 **55 Subsection 995-1(1)**

15 Insert:

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

17 **56 Subsection 995-1(1) (definition of *outward investing entity***  
18 ***(non-ADI)*)**

19 Repeal the definition.

20 **57 Subsection 995-1(1)**

21 Insert:

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

24 **58 Subsection 995-1(1) (definition of *outward investor***  
25 ***(general)*)**

26 Repeal the definition.

27 **59 Subsection 995-1(1) (paragraphs (a), (c) and (e) of the**  
28 **definition of *safe harbour debt amount*)**

29 Repeal the paragraphs.

# EXPOSURE DRAFT

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1 **60 Subsection 995-1(1)**

2 Insert:

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

4 **61 Subsection 995-1(1) (paragraphs (b) and (d) of the**  
5 **definition of *worldwide gearing debt amount*)**

6 Repeal the paragraphs.

# EXPOSURE DRAFT

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1 **Part 2—Application**

2 **62 Application**

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