

Chapter 8

Schedule 7 – Partial capital gains tax roll-over for statutory licences

Overview

8.1 Schedule 7 of the bill proposes to amend the *Income Tax Assessment Act 1997* to extend the existing statutory licence capital gains tax (CGT) roll-over (under Subdivision 124-C) to provide for roll-over where one or more new licences are issued in consequence of the ending of one or more licences and to provide for a partial roll over. A partial roll-over would apply where one or more statutory licences end and are replaced by one or more new licences and the licensee also received non licence capital proceeds such as money.

Background and summary

8.2 The Minister for Revenue and Assistant Treasurer announced this measure on 8 June 2007. At that time, he explained that the amendments would have particular application to the Achieving Sustainable Groundwater Entitlements (ASGE) program. The ASGE program is a joint NSW and Australian Government initiative to ensure the six major groundwater systems in NSW are sustainable in the long term.¹ The program aims to address groundwater over-allocation and over-extraction through a number of measures, including replacing existing groundwater licences. The program also includes a financial assistance package for affected licence holders of up to \$100 million. However, payments under the ASGE have apparently been delayed for some time pending a range of matters, including clarification of their taxation status.² Indeed, the committee was told that to date, no cash payments have been made under the ASGE, even though many old groundwater licences have been replaced with new licences, often with lower entitlements.³

1 EM, p. 156; see also NSW Government, *Achieving sustainable groundwater entitlements program*, http://www.waterwise.nsw.gov.au/water/groundwater_entitlements.shtml (accessed 22 August 2007).

2 Mr Michael Murray, Gwydir Valley Irrigators Association (GVIA)/NSW Irrigators' Council (NSWIC), *Proof Committee Hansard*, 28 August 2007, p. 11; see also Sophie Morris, 'Compo to flow for irrigators', *Australian Financial Review*, 13 June 2007, p. 14; NSWIC, 'Taxation of Groundwater Payments The Prime Minister Must Act', Press Release, 20 June 2007, available at: http://www.nswirrigators.org.au/pdf/press_release/25%20million%20tax%207%20June.pdf (accessed 21 August 2007).

3 Mr Murray, GVIA/NSWIC, *Proof Committee Hansard*, 28 August 2007, pp 10-11; also GVIA and NSWIC, *Submission 13*, p. [2].

Intended benefits of changes

8.3 The amendments proposed by Schedule 7 would ensure that licence holders who are also offered a cash payment under the ASGE program will obtain a partial CGT roll-over where the access licence (and any other new licences) replaces the original bore licence or licences.⁴

8.4 Although the amendments have particular application to the ASGE, they also have broader application. For example, media reports have suggested that they may also be relevant to the buy back of water licences under the \$10 billion National Plan for Water Security.⁵

Issues

8.5 The committee received one submission on schedule 7 of the Bill. The NSW Irrigators' Council (NSWIC) and the Gwydir Valley Irrigators Association (GVIA) generally welcomed the amendments in Schedule 7, telling the committee that they would 'rectify an anomaly' in the CGT treatment of payments under the ASGE.⁶

8.6 The GVIA and NSWIC were satisfied that the amendments 'will result in an equitable taxation treatment of licences and ex-gratia payments made under the ASGE program'. They explained that, without these amendments, in some cases individual CGT liability would exceed any ex-gratia payment received under the ASGE.⁷

8.7 However, the GVIA and NSWIC raised a concern about the timing of the CGT event C2.⁸ They told the committee that their advice — including informal discussions with Treasury and the ATO — suggested that the CGT event C2 occurred on the day the old licences were extinguished and the new licences were issued. They pointed out that, in the case of the ASGE, the extinguishment of licences has occurred on different dates in different groundwater systems:

...five of the six valleys had their licences extinguished in the last financial year but the licences for the Lachlan Valley have not yet been extinguished

4 The Hon. Peter Dutton MP, Minister for Revenue and the Assistant Treasurer, 'Continuing to Improve Australia's Tax System', Press Release No. 100, 16 August 2007; 'Capital Gains Tax (CGT) roll-over on the ending of a statutory licence', Press Release No. 069, 8 June 2007.

5 Fleur Anderson and Sophie Morris, 'Tax deal aids water buy-back', *Australian Financial Review*, 9 June 2007, p. 4; Sophie Morris, 'Compo to flow for irrigators', *Australian Financial Review*, 13 June 2007, p. 14. See also EM, pp 148-154 for other examples.

6 Mr Murray, *Proof Committee Hansard*, 28 August 2007, p. 11; GVIA and NSWIC *Submission 13*, p. [2]; also NSWIC, '\$25 Million Tax Top-Up, Press Release', 20 June 2007, available at: [http://www.nswirrigators.org.au/pdf/press_release/\\$25%20Million%20Tax%20Top-Up%20_2_.pdf](http://www.nswirrigators.org.au/pdf/press_release/$25%20Million%20Tax%20Top-Up%20_2_.pdf) (accessed 21 August 2007).

7 GVIA and NSWIC, *Submission 13*, p. [2]; Mr Michael Murray, *Proof Committee Hansard*, 28 August 2007, p. 10.

8 See further section 104.25 of the ITAA for a description of CGT event C2.

and, again, they are probably either weeks or months away from being extinguished and the new ones issued.⁹

8.8 The GVIA and NSWIC explained that this meant that licence holders in the Lachlan Valley would qualify for enhanced CGT Small Business Concessions, which commenced on 1 July 2007.¹⁰

8.9 The GVIA and NSWIC therefore suggested that Schedule 7 be amended to deem that the CGT event C2 occurs at the time the licence holder receives and accepts the letter of offer from the NSW Government (rather than the day the old licences were extinguished and the new licences issued).¹¹ They argued that:

Without this you will see an inequity in the ASGE programme with entitlement holders in the Lower Lachlan being able to avail themselves of the enhanced CGT Small Business Concessions, while entitlement holders in the other groundwater sources will be denied this opportunity, yet both groups will become entitled to the payments in the same financial year.¹²

8.10 In response, Treasury explained that the taxing point for CGT is when there is a change of ownership of the particular CGT asset. In the case of the groundwater licences at issue, this meant the time that old groundwater licences were extinguished and new licences issued. Treasury acknowledged that this would mean that:

Irrigators in the lower Lachlan may be able to access the enhanced CGT small business concessions, which apply from the 2007-08 income year... that difference in treatment arises from the timing of the ending of their bore licences... The fact that they were offered their cash payment in the same year as those whose licences ended in late 2006 does not change the timing of the CGT event that led to the cash payment.¹³

8.11 Treasury told the committee that:

If the legislation were amended in accordance with the wishes of the irrigators council, it would create a precedent for taxpayers in similar circumstances to seek a change in the timing of the CGT event so that they too could benefit where more generous tax arrangements were not available at the time that the event occurred. More generally, amending the legislation would not only represent a change in the timing of the CGT event C2 but also bring into question the timing of CGT events more

9 Mr Murray, *Proof Committee Hansard*, 28 August 2007, p. 11; GVIA and NSWIC, *Submission 13*, p. [3].

10 Mr Murray, *Proof Committee Hansard*, 28 August 2007, p. 11.

11 GVIA and NSWIC, *Submission 13*, p. [3].

12 GVIA and NSWIC, *Submission 13*, p. [3].

13 Mr Paul McMahon, Manager, Capital Gains Tax Unit, Department of the Treasury, *Proof Committee Hansard*, 28 August 2007, p. 12.

generally. A more general change in the timing of the CGT events would be complex to legislate and difficult to comply with and administer...¹⁴

Committee view

8.12 The committee welcomes the amendments proposed by Schedule 7 and hopes that their passage will mean payments under the ASGE program can be made without further delay. The committee notes the issue and suggested amendment raised by the GVIA and NSWIC in relation to the timing of the CGT event. However, the committee acknowledges Treasury's response that to amend Schedule 7 as suggested would create a problematic precedent.

14 Mr McMahon, *Proof Committee Hansard*, 28 August 2007, p. 12.