



**PRACTICE
STATEMENT No. 20
2nd release**

SUBJECT	REVENUE COLLECTION DIVISION: THE INCOME TAX GENERAL ANTI-AVOIDANCE PROVISION
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CONFIDENTIALITY STATUS	May be released to the public
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PRACTICE CO-ORDINATOR	Chief Auditor Risk & Compliance Division

INDEX

Introduction	2
Legislative basis	3
Explanation of section	3
Application of section to tax avoidance schemes	4
Examples of schemes to which section applies	5
Attachment A: Text of new section 108	6

INTRODUCTION

1. This statement sets out the practice of the Revenue Collection Division in relation to the general anti-avoidance provision found in section 108 of the *Income Tax Act*. It is issued with the authority of the Chief Executive Officer of the Fiji Islands Revenue and Customs Authority, who is also Commissioner of Inland Revenue.

LEGISLATIVE BASIS

2. The *Income Tax (Budget Amendment) Act 2004*, passed by Parliament in March 2004, repealed the existing section 108 and replaced it with new provisions (see Attachment A for text of new section 108).
3. The purpose of replacing the wording of section 108 was to provide for a more effective mechanism for dealing with tax avoidance schemes. The former section 108 is identical word-for-word with the former Australian section 260, which operated from 1936 to 1981, and was itself based on other overseas legislation dating back to 1878. Australian section 260 was tested in the Australian courts in the 1970s and 1980s in numerous cases, and was at most times thrown out by those courts as being ineffective.
4. The *Income Tax Act's* new section 108 is modelled on the Australian tax law's Part IVA, which has been held by the courts there as being effective against artificial, blatant, contrived tax avoidance schemes with no commercial value. By closely following the wording of the Australian legislation, Fiji courts will have access to the vast body of case law on the interpretation of Part IVA.
5. The new legislation has no application to establish commercial practices such as those operated through the use of tax incentives. It is also not applicable where a taxpayer has reduced their tax through a mechanism provided for under the law, such as choice of trading stock valuation method or depreciation method.
6. A related amendment was also made to the act at the same time. In section 103 it was clarified that the expression "overseas tax" also refers to "foreign tax credit" for the purpose of the new section 108.

EXPLANATION OF SECTION

7. The new section 108 applies to schemes entered into for the sole or dominant purpose of obtaining a tax benefit. It will not apply to arrangements of a normal business or commercial nature (such as negative gearing of a rental property). It is designed to operate against blatant, artificial or contrived arrangements.

8. The new section applies after the Commissioner has considered 3 points:

- is there a scheme?
- was a tax benefit obtained?
- was the sole or dominant purpose to obtain a tax benefit?

If the answer to all 3 questions is “yes” then the Commissioner may determine that all or part of the tax benefit is cancelled, and amend the taxpayer’s assessments accordingly.

9. The following is an analysis of new Section 108 by subsection:

Subsection	Effect
(1)	Provides some definitions of the terms used in the new section, such as “scheme” and “carrying out”.
(2)	Provides the scope of the sections’ operation. The operation of the new section is not limited by other sections of the Act or the tax treaties Fiji has with other countries.
(3)	Defines a “tax benefit” in relation to income, deductions and foreign tax credits. It specifically excludes benefits, which arise from a taxpayer exercising their rights under the Act (such as choosing a particular method of depreciating assets or valuing trading stock, or electing to split allowances between a husband and wife).
(4)	Extends the operation of the new section to schemes, which seek to avoid withholding tax (such as the withholding tax payable on royalty payments made to overseas companies).
(5)	The central operative provision of the new section. The section only applies to schemes entered into or carried out after 31 December 2003. This start date ensures that the section does not unfairly apply to arrangements in a retrospective manner. The taxpayer must have obtained a tax benefit in relation to the scheme. The Commissioner must have regard to 8 factors before concluding whether or not the scheme was entered into for the purpose of enabling the taxpayer to obtain a tax benefit.
(6)	This subsection specifically applies the new section to schemes aimed at stripping company profits. Under this type of scheme, directors or their associates “strip” or remove all the assets out of a company,

leaving behind an empty shell with a large tax debt that cannot be collected. They then start business under the name of a newly incorporated company, which has purchased the former business and its assets.

The subsection is worded to catch schemes which are variations on the usual arrangement e.g. where an irrecoverable loan (a “non-share dividend”) is made to the purchasing company; or the arrangement is with associates of the new company’s shareholders (“non-share equity shareholders”) rather than to the shareholders themselves.

- (7) This subsection is another operative provision which gives effect in situations where subsections (5) or (6) apply.

It gives the Commissioner power to make determinations which reverse the effect of the scheme. Notice in writing of the determination must be sent to the taxpayer, and the taxpayer can object to the determination.

The Commissioner can subsequently amend assessments to give effect to the determination. The taxpayer may object to these assessments in the usual manner, which gives them recourse to the legal system if not satisfied.

APPLICATION OF SECTION TO TAX AVOIDANCE SCHEMES

10. The decision to invoke section 108 will usually be initiated in the Risk & Compliance Division of FIRCA. The nature of the schemes, which the section seeks to attack, requires a thorough investigation to obtain all the documentation and evidence required to substantiate the use of section 108 against an appeal by the taxpayer.
11. A suspected scheme detected in other parts of FIRCA, such as in the Assessing area, should be referred for a full audit prior to making a decision on whether to invoke section 108. A submission from an auditor as to whether section 108 is to be used should be considered by the senior management and the Legal Unit of FIRCA. The submission must show consideration of the factors (aa) to (hh) listed in subsection 5(a)(i) of section 108.
12. Where the tax avoidance scheme can be attacked using a specific anti-avoidance provision under the act, the specific provision should be used rather than section 108. Examples of specific anti-avoidance provisions can be found in section 15 and subsection 20(1). In such cases section 108 should only be used where the specific anti-avoidance provision appears to be inadequate in attacking the scheme.

13. In the course of considering whether section 108 is to be applied in a particular case, reference should be made to overseas case law by searching the various on-line tax law databases and services. Particular reference should be made to the case law on Part IVA in Australia, which has many concepts relevant to those in section 108.

EXAMPLES OF SCHEMES TO WHICH SECTION APPLIES

14. The overseas experience in combating tax avoidance schemes shows that there is no limit to the creativity of tax advisers in devising innovative schemes. This statement cannot therefore give an exhaustive list of the types of schemes which section 108 will be applied to, but the following examples involving international transactions give some idea of the intended use of the new provisions:

Transfer pricing

The taxpayer may be a large multi-national enterprise, which imports goods or commodities into Fiji from a related entity overseas. It may inflate the prices of the imports so that profits and therefore taxes are minimized in Fiji, and the profits are shifted to an overseas tax jurisdiction with lower or no taxes. Alternatively, head office costs such as management fees may be inflated. Recent trends have been seen in the case of educational institutions, the overseas parent companies of which charge the Fiji company an unrealistically high cost for learning materials, and no royalty is payable by the Fiji company from which withholding tax would have been payable.

Thin capitalization

A foreign company funds its Fiji subsidiary through a high percentage of debt as opposed to equity funding which does not reflect the commercial reality of such loans. The Fiji company then has large interest payments which it sends to the overseas parent tax free, when it would otherwise have been making dividend payments on equity funding.

Withholding tax avoidance

A Fiji company wished to repatriate accumulated profits to an offshore parent in a country such as Australia where it would have to deduct 20% withholding tax. The shareholders set up a new company in a tax haven to acquire the shares of the Fiji company. The profits are sent to the tax haven free of withholding tax. This scheme has been noticed in the garment industry.

Treaty shopping

A company, which is based in Australia, conducts business in Fiji through a local company. The assets and business of the Fiji company are sold to a British company (ultimately owned by the Australian company) so that the more favourable definition of the term “royalty” in the Fiji-UK tax treaty will apply rather than the definition in the Fiji-Australia treaty.

15. The new section 108 will not only be applied where international transactions are involved, but also domestic transactions. The previous section 108 was tested in the Fiji courts only twice, with one win and one loss to the Commissioner. Both cases involved domestic transactions. The facts of each case are summarised below as further examples of arrangements which would be attacked under the new section 108 if similar arrangements were to occur today.¹

Deo Narayan Sahay v CIR 21 FLR 171, 26/11/75

A husband and wife started a family company and leased the company a house they owned, with the company to act as trustee for the benefit of their children. The company paid them rent of \$50 per annum and subleased the property for \$3000 per annum. The court held that the purpose of the transaction was the avoidance of tax.

“The appellant was able and intended by the arrangements made to siphon off the income from the house property into a trust fund and thereby decrease his taxable income.” (Spring JA)

Jethalal Naranji v CIR Unreported, Ct Rev, No 2 of 1968, 12/11/68

Two brothers involved in land development established a partnership in which their wives were the partners. It was purported that the wives were carrying on the business of land development, with the taxpayer engaged to manage the business. The Commissioner claimed that the profits of the wife should be assessed to the husband, but the court held that the arrangement was not motivated by tax avoidance, even though it provided tax benefits.

¹ These two cases are described in more detail in *Fiji Income Tax Law* by Peter Fulcher, Institute of Justice & Applied Legal Studies, University of the South Pacific, 1999, at pp.274-277.

TEXT OF NEW SECTION 108

“Schemes to reduce income tax

Interpretation

108-(1) In this Section, unless the contrary intention appears:

“foreign tax credit” means a credit within the meaning of Section 103.

“scheme” means:

- (i) any agreement, arrangement, understanding, promise or undertaking, whether express or implied and whether or not enforceable, or intended to be enforceable, by legal proceedings; and
- (ii) any scheme, plan, proposal, action, course of action or course of conduct;

“taxpayer” includes a taxpayer in the capacity of a trustee.

The definition of **“taxpayer”** in subsection (1) shall not be taken to affect in any way the interpretation of that expression where it is used in this Act other than this subsection.

The reference in the definition of **“scheme”** in subsection (1) to a scheme, plan, proposal, action, course of action or course of conduct shall be read as including a reference to a unilateral scheme, plan, proposal, action, course of action or course of conduct, as the case may be.

A reference in this subsection to the **“carrying out”** of a scheme by a person shall be read as including a reference to the carrying out of a scheme by a person together with another person or other persons.

A reference in this Section to a scheme or a part of a scheme being entered into or carried out by a person for a particular purpose shall be read as including a reference to the scheme or the section of the scheme being entered into or carried out by the person for 2 or more purposes of which that particular purpose is the dominant purpose.

Operation of this subsection

(2) (a) Nothing in the provisions of this Act other than this Section shall be taken to limit the operation of this Section.

(b) Where a provision of this Act other than this subsection is expressed to have effect where a deduction would be allowable to a taxpayer but for or apart from a provision or provisions of this Act, the reference to that provision or to those provisions, as the case may be, shall be read as including a reference to subsection (7)(a).

(c) Where a provision of this Act other than this subsection is expressed to have effect

where a deduction would otherwise be allowable to a taxpayer, that provision shall be deemed to be expressed to have effect where a deduction would, but for subsection (7)(a), be otherwise allowable to the taxpayer.

Tax benefits

(3) (a) Subject to this subsection, a reference in this Section to the obtaining by a taxpayer of a tax benefit in connection with a scheme shall be read as a reference to:

- (i) an amount not being included in the total income of the taxpayer of a year of income where that amount would have been included, or might reasonably be expected to have been included, in the total income of the taxpayer of that year of income if the scheme had not been entered into or carried out; or
- (ii) a deduction being allowable to the taxpayer in relation to a year of income where the whole or a part of that deduction would not have been allowable, or might reasonably be expected not to have been allowable, to the taxpayer in relation to that year of income if the scheme had not been entered into or carried out; or
- (iii) a foreign tax credit being allowable to the taxpayer where the whole or a part of that foreign tax credit would not have been allowable, or might reasonably be expected not to have been allowable, to the taxpayer if the scheme had not been entered into or carried out; and, for the purposes of this Section, the amount of the tax benefit shall be taken to be:
 - (iv) in a case to which subparagraph (i) applies - the amount referred to in that subparagraph; and
 - (v) in a case to which subparagraph (ii) applies - the amount of the whole of the deduction or of the part of the deduction, as the case may be, referred to in that subparagraph; and
 - (vi) in a case where subparagraph (iii) applies - the amount of the whole of the foreign tax credit or of the part of the foreign tax credit, as the case may be, referred to in that subparagraph.

(b) A reference in this Section to the obtaining by a taxpayer of a tax benefit in connection with a scheme shall be read as not including a reference to:

- (i) the total income of the taxpayer of a year of income not including an amount that would have been included, or might reasonably be expected to have been included, in the total income of the taxpayer of that year of income if the scheme had not been entered into or carried out where:
 - (aa) the non-inclusion of the amount in the total income of the taxpayer is attributable to the making of an agreement, choice, declaration, election or selection, the giving of a notice or the exercise of an option expressly provided for by this Act; and
 - (bb) the scheme was not entered into or carried out by any person for the purpose of creating any circumstance or state of affairs the existence of which is necessary to enable the declaration, agreement, election, selection, choice, notice or option to be made, given or exercised, as the case may be; or
- (ii) a deduction being allowable to the taxpayer in relation to a year of income the whole or a part of which would not have been, or might reasonably be expected not to have been, allowable to the taxpayer in relation to that year of income if the scheme had not been entered into or carried out where:

(aa) the allowance of the deduction to the taxpayer is attributable to the making of a declaration, agreement, election, selection or choice, the giving of a notice or the exercise of an option by any person, being a declaration, agreement, election, selection, choice, notice or option expressly provided for by this Act; and

(bb) the scheme was not entered into or carried out by any person for the purpose of creating any circumstance or state of affairs the existence of which is necessary to enable the declaration, agreement, election, selection, choice, notice or option to be made, given or exercised, as the case may be; or

(iii) a foreign tax credit being allowable to the taxpayer the whole or a part of which would not have been, or might reasonably be expected not to have been, allowable to the taxpayer if the scheme had not been entered into or carried out, where:

(aa) the allowance of the foreign tax credit to the taxpayer is attributable to the making of a declaration, agreement, election, selection or choice, the giving of a notice or the exercise of an option by any person, being a declaration, agreement, election, selection, choice, notice or option expressly provided for by this Act; and

(bb) the scheme was not entered into or carried out by any person for the purpose of creating any circumstance or state of affairs the existence of which is necessary to enable the declaration, agreement, election, selection, choice, notice or option to be made, given or exercised, as the case may be.

(c) A reference in this Section to the obtaining by a taxpayer of a tax benefit in connection with a scheme is to be read as not including a reference to the total income of the taxpayer of a year of income not including an amount that would have been included, or might reasonably be expected to have been included, in the total income of the taxpayer of that year of income if the scheme had not been entered into or carried out where the scheme consisted solely of the making of the agreement or election.

(d) For the purposes of subparagraph (b)(i)(aa), (b)(ii)(aa) and (b)(iii)(aa);

(i) the non-inclusion of an amount in the total income of a taxpayer; or

(ii) the allowance of a deduction to a taxpayer; or

(iii) the allowance of a foreign tax credit to a taxpayer; is taken to be attributable to the making of a declaration, election, agreement or selection, the giving of a notice or the exercise of an option where, if the declaration, election, agreement, selection, notice or option had not been made, given or exercised, as the case may be:

(iv) the amount would have been included in that total income; or

(v) the deduction would not have been allowable; or

(vii) the foreign tax credit would not have been allowable.

Withholding tax avoidance

(4) (a) This subsection applies in relation to a particular amount if a taxpayer is not liable to pay withholding tax on an amount where that taxpayer would have, or could reasonably be expected to have, been liable to pay withholding tax on the amount if a scheme had not been entered into or carried out.

(b) For the purposes of this Section, if this subsection applies in relation to an amount, the taxpayer is taken to have obtained a tax benefit in connection with the scheme of an amount equal to the amount mentioned in subsection (4)(a).

Schemes to which section applies

(5) (a) This Section applies to any scheme that has been or is entered into after 31 December 2003, and to any scheme that has been or is carried out or commenced to be carried out after that date (other than a scheme that was entered into on or before that date), whether the scheme has been or is entered into or carried out in Fiji or outside Fiji or partly in Fiji and partly outside Fiji, where-

(i) a taxpayer (in this section referred to as the “relevant taxpayer”) has obtained, or would but for subsection (7) obtain, a tax benefit in connection with the scheme; and

(ii) having regard to-

(aa) the manner in which the scheme was entered into or carried out;

(bb) the form and substance of the scheme;

(cc) the time at which the scheme was entered into and the length of the period during which the scheme was carried out;

(dd) the result in relation to the operation of this Act that, but for this Section, would be achieved by the scheme;

(ee) any change in the financial position of the relevant taxpayer that has resulted, will result, or may reasonably be expected to result, from the scheme;

(ff) any change in the financial position of any person who has, or has had, any connection (whether of a business, family or other nature) with the relevant taxpayer, being a change that has resulted, will result or may reasonably be expected to result, from the scheme;

(gg) any other consequence for the relevant taxpayer, or for any person referred to in sub-subparagraph (ff), of the scheme having been entered into or carried out; and

(hh) the nature of any connection (whether of a business, family or other nature) between the relevant taxpayer and any person referred to in sub-subparagraph (ff),

it would be concluded that the person, or one of the persons, who entered into or carried out the scheme or any part of the scheme did so for the purpose of enabling the relevant taxpayer to obtain a tax benefit in connection with the scheme or of enabling the relevant taxpayer and another taxpayer or other taxpayers each to obtain a tax benefit in connection with the scheme (whether or not that person who entered into or carried out the scheme or any part of the scheme is the relevant taxpayer or is the other taxpayer or one of the other taxpayers).

Stripping of company profits

(6) (a) Where-

(i) as a result of a scheme that is, in relation to a company-

(aa) a scheme by way of or in the nature of dividend stripping; or

(bb) a scheme having substantially the effect of a scheme by way of or in the nature of a dividend stripping,

any property of the company is disposed of;

(ii) in the opinion of the Commissioner, the disposal of that property represents, in whole or in part, a distribution (whether to a shareholder or another person) of profits of the company (whether of the accounting period in which the disposal occurred or of any

earlier or later accounting period);

(iii) if, immediately before the scheme was entered into, the company had paid a dividend out of profits of an amount equal to the amount determined by the Commissioner to be the amount of profits the distribution of which is, in his opinion, represented by the disposal of the property referred to in sub-subparagraph (i), an amount (in this subsection referred to as the “notional amount”) would have been included, or might reasonably be expected to have been included, by reason of the payment of that dividend, in the total income of a taxpayer of a year of income; and

(iv) the scheme has been or is entered into after 31 December 2003, whether in Fiji or outside Fiji, the following provisions have effect:

(v) the scheme shall be taken to be a scheme to which this Section applies;

(vi) for the purposes of subsection (7), the taxpayer shall be taken to have obtained a tax benefit in connection with the scheme that is referable to the notional amount not being included in the total income of the taxpayer of the year of income; and

(vii) the amount of that tax benefit shall be taken to be the notional amount.

(b) Without limiting the generality of subsection (6)(a), a reference in that subsection to the disposal of property of a company shall be read as including a reference to-

(i) the payment of a dividend by the company;

(ii) the making of a loan by the company (whether or not it is intended or likely that the loan will be repaid);

(iii) a bailment of property by the company; and

(iv) any transaction having the effect, directly or indirectly, of diminishing the value of any property of the company.

(c) This subsection:

(i) applies to a non-share equity interest in the same way as it applies to a share; and

(ii) applies to an equity holder in the same way as it applies to a shareholder; and

(iii) applies to a non-share dividend in the same way as it applies to a dividend.

(d) In this subsection, “property” includes a chose in action and also includes any estate, interest, right or power, whether at law or in equity, in or over property.

Cancellation of tax benefits etc.

(7) (a) Where a tax benefit has been obtained, or would but for this subsection be obtained, by a taxpayer in connection with a scheme to which this Section applies, the Commissioner may-

(i) in the case of a tax benefit that is referable to an amount not being included in the total income of the taxpayer of a year of income - determine that the whole or a part of that amount shall be included in the total income of the taxpayer of that year of income; or

(ii) in the case of a tax benefit that is referable to a deduction or a part of a deduction being allowable to the taxpayer in relation to a year of income - determine that the whole or a part of the deduction or of the part of the deduction, as the case may be, shall not be allowable to the taxpayer in relation to that year of income; or

(iii) in the case of a tax benefit that is referable to a foreign tax credit, or a part of a foreign tax credit, being allowable to the taxpayer - determine that the whole or a part of

the foreign tax credit, or the part of the foreign tax credit, as the case may be, is not to be allowable to the taxpayer;
and, where the Commissioner makes such a determination, he shall take such action, as he considers necessary to give effect to that determination.

(b) Where the Commissioner determines under subsection (7)(a) that an amount is to be included in the total income of a taxpayer of a year of income, that amount shall be deemed to be included in that total income by virtue of such provision of this Act as the Commissioner determines.

(c) Where a tax benefit has been obtained, or would but for this subsection be obtained, by a taxpayer in connection with a scheme to which this Section applies:

(i) the Commissioner may determine that the taxpayer is subject to withholding tax under this Act on the whole or part of that amount; and

(ii) if the Commissioner makes such a determination, he or she must take such action as he or she considers necessary to give effect to that determination.

(d) A determination under subsection (7)(a) or (7)(c) must be in writing.

(e) Notice of the determination must be given to the taxpayer and, in the case of a determination under subsection (7)(c), to the person who paid the amount.

(f) More than one determination may be included in the same notice.

(g) A failure to comply with subsection (7)(e) does not affect the validity of a determination.

(h) If the Commissioner makes a determination under subsection (7)(c), the amount that the Commissioner determines is taken to be subject to withholding tax is taken to have been subject to withholding tax at all times by virtue of such provision under this Act as the Commissioner determines.

(i) If the taxpayer is dissatisfied with a determination under subsection (7)(c), the taxpayer may object against it in the manner set out in this Act.

(j) Where the Commissioner has made a determination under subsection (7)(a) or (7)(c) in respect of a taxpayer in relation to a scheme to which this Section applies, the Commissioner may, in relation to any taxpayer (in this paragraph referred to as the **“relevant taxpayer”**)-

(i) if, in the opinion of the Commissioner-

(aa) there has been included, or would but for this paragraph be included, in the total income of the relevant taxpayer of a year of income an amount that would not have been included or would not be included, as the case may be, in the total income of the relevant taxpayer of that year of income if the scheme had not been entered into or carried out; and

(bb) it is fair and reasonable that that amount or a part of that amount should not be included in the total income of the relevant taxpayer of that year of income, determine that that amount or that part of that amount, as the case may be, should not have been included or shall not be included, as the case may be, in the total income of the relevant taxpayer of that year of income; or

(ii) if, in the opinion of the Commissioner-

(aa) an amount would have been allowed or would be allowable to the relevant taxpayer as a deduction in relation to a year of income if the scheme had not been entered into or carried out, being an amount that was not allowed or would not, but for this paragraph, be allowable, as the case may be, as a deduction to the relevant taxpayer in relation to that year of income; and

(bb) it is fair and reasonable that that amount or a part of that amount should be allowable as a deduction to the relevant taxpayer in relation to that year of income, determine that that amount or that part, as the case may be, should have been allowed or shall be allowable, as the case may be, as a deduction to the relevant taxpayer in relation to that year of income; or

(iii) if, in the opinion of the Commissioner:

(i) an amount would have been allowed, or would be allowable, to the relevant taxpayer as a foreign tax credit if the scheme had not been entered into or carried out, being an amount that was not allowed or would not, apart from this paragraph, be allowable, as the case may be, as a foreign tax credit to the relevant taxpayer; and

(ii) it is fair and reasonable that the amount, or a part of the amount, should be allowable as a foreign tax credit to the relevant taxpayer;

determine that that amount or that part, as the case may be, should have been allowed or is allowable, as the case may be, as a foreign tax credit to the relevant taxpayer; and the Commissioner shall take such action, as he considers necessary to give effect to any such determination.

(k) Where the Commissioner makes a determination under paragraph (j) by virtue of which an amount is allowed as a deduction to a taxpayer in relation to a year of income, that amount shall be deemed to be so allowed as a deduction by virtue of such provision of this Act as the Commissioner determines.

(l) Where, at any time, a taxpayer considers that the Commissioner ought to make a determination under paragraph (j) in relation to the taxpayer in relation to a year of income, the taxpayer may post to or lodge with the Commissioner a request in writing for the making by the Commissioner of a determination under that paragraph.

(m) The Commissioner shall consider the request and serve on the taxpayer, by post or otherwise, a written notice of his decision on the request.

(n) If the taxpayer is dissatisfied with the Commissioner's decision on the request, the taxpayer may object against it in the manner set out in this Act.

(o) Nothing in this Act prevents the amendment of an assessment at any time before the expiration of 6 years after the date on which tax became due and payable under the assessment if the amendment is for the purposes of giving effect to subsection (7)(a).

(p) Nothing in this Act prevents the amendment of an assessment at any time if the amendment is for the purpose of giving effect to subsection (7)(j).

*****End of Practice Statement*****