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Recent tax changes for South Australian businesses and business families

Julie Van der Velde FCPA





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Similar Business Test
Treasury Laws Amendment (2017 Enterprise Incentives No. 1)
Bill 2017

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Similar Business Test

- Accessing tax losses
- Bad debt deductions
- Net capital losses

•Current Tests

- COT – majority ownership stays the same
- SBT - same business from immediately before COT is failed until year in which loss utilised
 - No new types of transactions
 - No new business activities

- Not a replacement but in addition to the same business test
- Focus still on maintaining identity of business

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Similar Business Test

- To apply from 1 July 2015
- New activities /transactions may pass test => evolve from / complement business before test time
- EM indicates a need for clear similarity in business identity
- Examples in EM
 - Former business continues to generate greater part of the total income – 85%
 - Additional applications of existing business technology
 - On balance the similarities outweigh the differences – fact and degree
 - Test is failed where manufacturing ends and only distribution continues

Anti avoidance rules

- Apply where activities change immediately before change of ownership

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Similar Business Test

- LCG 2017/D6 published July 2017
- How the Commissioner will apply the new test
 - extent to which same assets are being used
 - extent to which engage in same activities and operations
 - compare identity of business before and after test time
 - extent to which changes from development or commercialisation of assets/ processes/ products/ services/ marketing methods of business before test time

“The similar business test operates in a way that is comparable to the same business test, but removes the negative limbs which apply as part of that test.”

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Small Business Turnover Threshold(s)

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Announced in 2016/17 Budget
Treasury Laws Amendment (Enterprise Tax Plan) Act 2017

Small Business Turnover threshold Increase to \$10 m from 1 July 2016

- Simplified depreciation rules – instant asset write off
- Accelerated depreciation for primary producers
- Deductions for professional expenses for start ups
- Immediate deduction for prepaid expenses
- PAYG Instalment concession
- Simplified trading stock rules
- Two year amendment period
- Simpler BAS and GST rules
- Small business restructure rollover

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Announced in 2016/17 Budget
Treasury Laws Amendment (Enterprise Tax Plan) Act 2017

Small Business Turnover threshold Increase from 1 July 2016

- FBT concessions \$10 million from 1 April 2017
- Unincorporated small business tax discount is 8% limited to entities with turnover less than \$5 million
 - Current cap of \$1,000.00 per individual per year retained
- Small business CGT concessions \$2 million threshold

• Useful link: <https://www.ato.gov.au/business/small-business-entity-concessions/concessions/>

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Trust Issues

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Blenkinsop v Herbert [2017] WASC 87
Changing guardians

- This was an appeal for the removal and replacement of a guardian of a trust
- The problem was that the court found it only had authority to remove a guardian if he or she is a fiduciary
- The guardian is often the appointor
- The guardian is what the deed says it is – powers/ duties/ responsibilities all determined under the deed
- Issue here was whether the guardian was a fiduciary
 - in each case this will depend upon the wording of the deed and the facts
 - what was the intention of the settlor as determined from the deed and facts
 - in this case the court found guardians were effectively appointed to take care of their own interests – not fiduciaries

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Lewski v Commissioner of Taxation [2017] FAF 145
Validity of Trust Resolutions

- 2006 Trustee 1 resolved to distribute 100% of distributable income to Mrs Lewski
 - Also, resolved if there was a variation by the Commissioner to distribute 100% of variation to Company 1
- 2007 Trustee 2 resolved to distribute first \$3½ million to Company 2 and remainder to Mrs Lewski
 - Also, resolved if there was a variation by the Commissioner to distribute 100% of variation to Company 2
- The Commissioner varied the income of each trust in the relevant years
- Full Court of the Federal Court found:
 - the 'variation' resolutions were actually allowed under the terms of the relevant deeds
 - whether or not the 'variation' resolutions were allowed the overall effect of the two resolutions together was too uncertain to create present entitlement
 - the distributions to Mrs Lewski were contingent

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Lewski v Commissioner of Taxation [2017] FAF 145
Validity of Trust Resolutions

- Essentially a lucky error
- Mrs Lewski had tried to disclaim the distributions on December 2015
- Court found her husband acted as her tax agent with full authority and he had known of the distributions well before that date
- Disclaimer not allowed
- Other Trust Resolution issues
 - Dates
 - Definition of income
 - Permitted Beneficiaries

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PGC 2016/16 Fixed Entitlements and Fixed Trusts

Released 13 September 2017

What the Commissioner will consider in determining if a trust is fixed

- Relevant for:
 - Trust loss rules
 - Capital gains tax rollovers
 - Value shifting
- Not relevant for:
 - Franking credit holding periods
 - Non-arms length income rules for SMSFs

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PGC 2016/16 Fixed Entitlements and Fixed Trusts

Released 13 September 2017

What the Commissioner will consider in determining if a trust is fixed

- There has to be a deed
- The deed has to give fixed entitlements
- BUT interests may be defeasible if there are powers to:
 - amend the trust deed
 - to issue or redeem units
 - issue units of different classes or to reclassify units
 - classify receipts as being on income or capital account if units do not all have equal rights to income and capital
 - appoint a beneficiary's interest in the income or capital of the trust to another beneficiary
 - to settle or appoint any part of the corpus of the trust to a new trust with different beneficiaries
 - enforce the forfeiture or cancellation of partly paid units due to the non-payment of a call except where such partly paid units would be void *ab initio*

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PGC 2016/16 Fixed Entitlements and Fixed Trusts

Safe Harbour

- Most likely only the 6th safe harbor is relevant to SME and family business structures, requires:
 - trust instrument
 - all beneficial interests in income and capital are vested
 - all beneficial interests have the same rights to receive the income and capital of the trust
 - all beneficial interests can be expressed as a percentage of total income and capital
 - trust is not a discretionary trust or a trust with default income or capital beneficiaries
 - trustee has never exercised a power capable of defeating a beneficiary's interest to defeat a beneficiary's interest
 - no arrangement which would cause s 272-35 of Schedule 2F of the ITAA 36 to apply
- Rely on safe harbour or request Commissioner's discretion s 272-5(3)

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ATO approaches

Trusts Taskforce changed its name to Tax Avoidance Taskforce – Trusts from 1 July 2017

- **Priorities**
 - focused compliance activity on privately owned and wealthy groups
 - target known scheme designers and promoters
 - gather intelligence and focus on specific risks
- **Splitting Trusts**
 - ATO is developing guidance on splitting trusts
 - previously ATO Private Binding Ruling 1012921290075 December 2015 indicated one can split a trust
 - ruling now has 'note' that the ATO are reconsidering their position on this
- **Amending Deeds (TA 2016/12)**
 - to provide different definitions of income which facilitate divergence of taxable income and economic benefit

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Shareholder loans

PGC 2017/13
TD 2017/D3

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Division 7A continues to evolve

In the 2016/17 Budget the Government announced amendments to apply from 1 July 2018

Based on recommendations of the Board of Tax

- Self-correction mechanism to rectify inadvertent breaches
- Appropriate safe harbour rules to provide certainty and simplify compliance
- Simplified rules regarding 109N loans:
 - loan duration
 - minimum interest rate
- technical amendments to improve the integrity and operation of Division 7A and provide increased certainty

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Board of Tax Review

- Released by Government in June 2015
- Recommendations included:
 - No requirement for formal loan agreement => must be written/ electronic evidence by lodgement date
 - Statutory interest rate fixed for life of loan
 - Based on Reserve Bank indicator lending rate 'small business; variable; other; overdraft' prior May
 - Maximum term 10 years:
 - Pay down to 75% by end year 3
 - Pay down to 55% by end year 5
 - Pay down to 25% by end year 8
 - Fully repaid by end year 10
 - All existing 7 year loans would be extended
 - Existing 25 year loans allowed to run to term
 - All Pre 1997 loans would be 10 year loans from date new rules start

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Board of Tax Review

- Recommendations included:
 - Allow trustees to make a single irrevocable election
 - Election will exclude all loans and UPEs between that trust and a private company to be excluded
 - Election means that the trust no longer has access to CGT discount on any asset other than:
 - Business Goodwill
 - Intangible assets inherently connected with the business carried on by the trustee
 - Self correction mechanism to allow a taxpayer to reverse effect of prior deemed dividend if:
 - reasonable to infer the deemed dividend was caused unintentionally; and
 - appropriate steps to put parties where they would have been had dividend not arisen
 - Voluntary corrective action is prima facie evidence cause unintentional
- Recommended against allowing deemed dividends to be franked

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PCG 2017/13
released 19 July 2017

UPE arrangements in accordance with Option 1 PSLA 2010/4

- Valid adoption of Option - seven year sub trust arrangement due to end in 2017 or 2018 financial year
- At end the full amount of the principal must be paid by the trustee to the company
- But PCG allows:
 - Company calls on the amount (sub trust ends)
 - Amount paid to company (no need for cash)
 - Amount lent to trustee as a 109N complying loan
- Effectively the 2011 sub trusts (UPE arose between 16/12/09 and 30/6/10) are able to be outstanding over 14 years
- Applies for one year only
 - WHY? New legislation from 1 July 2018 with no exposure draft released as at end October 2017?

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TD 2017/D3
28 June 2017

s 109T and ordinary commercial transactions

- s 109T treats a payment/ loan from a private company to entity 1 as a payment/ loan to entity 2 if it is reasonable to conclude the payment/ loan was made as part of an arrangement to pay or loan to entity 2
- Commissioner will look at benefit to entity 2 rather than whether the first payment/ loan was commercial
- Commissioner considers 'even if some/ all of payment is assessable to entity 1 s 109T can still apply'
- Example 1:
 - Franked dividend from company to company and second company lends to individual
- Example 4:
 - Franked dividend to trust which used the funds to buy a property
 - Trustee distributes the property as tax free capital distribution to individual
 - Trustee recognises a loss
 - Trustee distributes income after loss to company 2

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South Australian State Budget Tax Changes

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Stamp duty surcharge for foreign purchasers of South Australian residential property

- Foreign purchasers acquiring residential property in South Australia on or after 1 January 2018
- Pay 4% of the dutiable value of the property as a surcharge + stamp duty otherwise payable
- If the property is exempt from duty also exempt from surcharge
- Foreign natural person**
 - not an Australian citizen, Australian permanent resident or New Zealand citizen who holds a special category visa
- Foreign Corporation**
 - incorporated outside Australia or at least 50% of shares held by foreign persons, companies or trusts
- Foreign Trust**
 - the trustee, a person who has the power to appoint, an identified object or a person who takes capital in default is foreign

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Other State Budget changes

Stamp Duty

- Off the plan concession extended to 30 June 2018 but not available to foreign purchasers

Land Tax

- 5 year exemption if bought eligible apartment off the plan between 22 June and 30 September

Payroll Tax

- New rate scale to replace small business rebate will be introduced for payrolls \$600,000.00 to \$1.5 million

Bank Levy

- From 1 July 2017
- Using commonwealth base
- Quarterly at 0.015% on liabilities

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Other State Budget changes

Administration changes

- From 1 July 2017
- Allow RevenueSA to collect information for the Commonwealth Government
- increase costs of a conveyance
- increased likelihood of error particularly with trustee purchasers and vendors

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Family Farm Exemption

Statutes Amendment and Repeal (Simplify No 2) Bill 2017

- Current Exemption applies to transfers from:

- natural person to natural person
- natural person to trustee
- trustee to natural person
- trustee to trustee

"family company"

- "a company is a family company if each shareholder of the company is a relative of all other shareholders of the company"

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Changes to corporate tax rate

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Treasury Laws Amendment (Enterprise Tax Plan) Act 2017

- Royal Assent on 19 May 2017
- Reduces tax rate to 25% by 2026/27 year
 - This year Turnover < \$25m tax rate 27.5%
 - 2018/19 Turnover < \$50m tax rate 27.5%
 - 2024/25 Turnover < \$50m tax rate 27%
 - 2025/26 Turnover < \$50m tax rate 26%
 - 2026/27 Turnover < \$50m tax rate 25%

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Treasury Laws Amendment (Enterprise Tax Plan) Act 2017

Franking Dividends

- A dividend can only be franked at the rate applicable to the year in which it is paid
 - Current year earnings taxed 27.5% dividend paid July 2018 franked at 27.5%
 - 2018/19 earnings taxed at 27.5% dividend paid July 2019 franked at 27%
- Shareholder receives \$100 in 2017/18
- Credit 30% is \$42.86 net cash after tax c. \$72.86
- Credit 27.5% is \$37.93 net cash after tax c. \$70.34

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Bywater Investments Limited v Commissioner of Taxation [2016] HCA 45

- High Court held CM&C of a foreign company is a question of fact and degree
 - depends on where CM&C of the company is actually situated
 - determined by considering the course of business and trading and not by constituent documents
 - no general principle /presumption CM&C located where directors reside or where meetings are held
- Esquire Nominees Ltd v Commissioner of Taxation [1973] HCA 67
 - Effectively confined to its facts no principle established

Key issues for residence

- Distinction between advice and decision making
- If CM&C in Australia a company carries on business here per se

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Bywater Investments Limited v Commissioner of Taxation [2016] HCA 45

Tax Ruling TR 2017/D2

- a company will carry on business in Australia if it is controlled in Australia
- CM&C of a business is factually part of carrying on the business

"Where a company is established and maintained to make profit for its shareholders, and invests its assets in gainful activities that have a prospect of profit, then it is likely to be carrying on business"

ATO

"the policy decision made by the government to cut the tax rate for small companies was not meant to apply to passive investment companies"
Minister O'Dwyer

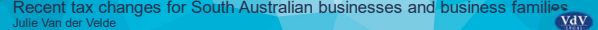
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Treasury Laws Amendment (Enterprise Tax Plan Base Rate Entities) Bill 2017

- Introduced 18 October 2017
- base rate entity passive income
 - distributions (including franking credits) from companies other than non portfolio dividends
 - non share dividends made by a company
 - interest rent and royalties
 - a gain on a qualifying security;
 - a net capital gain
 - an amount included in the assessable income of a partner or a beneficiary of a trust estate that is referable (directly or indirectly) to base rate entity passive income
- 80% maximum

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Foreign Resident CGT Withholding

Budget changes and remedial power

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Foreign Resident CGT Withholding

Applies to all Australian and foreign resident purchasers & Vendors

- Applied from 1 July 2016 at 10%
- Applies to TARP (including indirect interests and options and rights to acquire)
- Excluded transactions for less than \$2 million market value
- If Vendor does not have clearance certificate purchaser must withhold from purchase price and remit to ATO

From 1 July 2017

- Rate increased to 12½%
- Excluded transactions for less than \$750,000 market value

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Foreign Resident CGT Withholding

Who is a foreign resident?

- If you are the purchaser – anyone without a clearance certificate
- If you are the vendor
 - Individual resident?
 - Ordinary concept of reside, OR
 - Domicile in Australia unless permanent place of abode outside, OR
 - In Australia ½ year unless permanent place of abode elsewhere and do not intend to reside, OR
 - Commonwealth superannuation scheme members and dependants



Foreign Resident CGT Withholding

- Company resident?
 - if incorporate in Australia, OR
 - carries on business in Australia, AND
 - either CM&C in Australia or voting controlled by Australian residents
- Trust (other than unit trust) resident?
 - if trustee is resident, OR
 - CM&C in Australia at any time in the relevant year
- Unit Trust resident?
 - if CM&C and any trust property in Australia, OR
 - 50% + held by Australian residents and trustee carries on business in Australia



Thank you

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