

## 2009/10 Federal Budget - the good, the bad & the ugly

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The 2009/10 Australian Federal Budget was handed down on Tuesday, 12 May 2009. It contains some tax measures that are good and ought to be applauded. It contains some measures which are bad (in the sense that they achieve little if anything) and, finally, it contains some measures that are just plain ugly. In fact, the ugly measures are uncalled for at a time when appropriate fiscal measures are not only necessary, but are absolutely essential, if Australia is to return to economic growth. Below we outline and examine the main tax measures released in this year's Budget. It should be noted, however, that not all the tax measures are considered.

### The good ...

#### Investment allowance - from 30% to 50% (ie 9% to 15% cash discount)

Current	Proposed	Start date
Small businesses with a turnover of less than \$2 million are entitled to a <b>30%</b> additional tax deduction for all capital assets acquired between 13 December 2008 and 31 December 2009	The government now proposes that small businesses obtain a <b>50%</b> tax break for assets acquired during the same period, provided they are installed before the end of 2010	Effective 13 December 2008

Previously, the small business investment allowance measure was significantly criticised on the basis that it represented only a **9% cash discount** (for a corporate taxpayer) and thus provided little, if any, incentive for business to undertake

necessary investments. Now that the measure has increased to a **15% cash discount**, it is most definitely an improved measure.

However, the measure is still not enough. Also, the measure is somewhat misconceived, in that it encourages consumption by business in order to obtain an additional tax deduction.

The main problem with Australia's economy, at present, is rising unemployment. A simple tax solution to this problem would have been to allow an accelerated tax deduction for employment related expenditure. For example, an 110% tax deduction for salary and wages paid by small businesses to employees. Or, perhaps, depending on the extent of stimulus required, an 120% tax deduction for salary and wages paid by small businesses would have been much more effective.

Such a simple and beneficial measure, would have provided an incentive for small businesses to maintain their existing workforce as well as providing a necessary tax break for those businesses. Maintaining the workforce at its current level would more likely have a stimulatory effect on the Australian economy as compared to a weak 15% cash discount on investments.

Also, calls by small business to abolish completely CGT on small business assets (as in the United States) could have been addressed in this Budget. Whilst as a tax advisor, a lot of our work relates to advising on the small business tax concessions in Division 152 of the ITAA 1997, it is perhaps about time that the provisions be abolished entirely in favour of an outright exemption from CGT for all small business CGT assets. This would not only encourage investment, but would also help reduce the growing compliance costs of small business associated with ensuring the rules in Division 152 are met.

### **Income testing of entrepreneur's tax offset to be deferred**

<b>Current</b>	<b>Proposed</b>	<b>Start date</b>
The Entrepreneur's Tax Offset is currently not subject to any income testing	Income testing for the ETO is to be introduced from 1 July 2009 (as opposed to 1 July 2008 as first proposed in the 2008/09	Effective 1 July 2009

	Budget)	
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Given the current global economic crisis, the deferral of the income testing of the entrepreneur's tax offset is to be welcomed. Introducing the measure now would only work to further dampen any chance of economic recovery in Australia.

### **Unlimited amendment periods to be abolished**

<b>Current</b>	<b>Proposed</b>	<b>Start date</b>
The Commissioner presently has unlimited time to amend certain tax assessments	The time to amend assessments will be limited	Effective from date of Royal Assent of enacting legislation

This measure is definitely worth a round of applause. The Commissioner should not be entitled to unlimited powers of amendment of assessments. The Commissioner's power to amend assessments should have long been the subject of time limitations so as to provide taxpayers with certainty of their position under tax law.

There can be nothing worse than a looming concern in the mind of taxpayers that they may one day be the subject of an amended assessment regarding their tax affairs of say 5, 10 or even 15 or more years ago. This measure should be welcomed by taxpayers and deserves greater publicity than it has been provided.

### **Other good measures**

- The Medicare levy low-income thresholds will be increased to \$17,794 for individuals and \$30,025 for individuals with families from the 2009/10 income year.
- The Government will provide a mechanism to conduct triennial review of guidelines for, and organizations on, the four deductible gift registers, commencing from the 2009/10 income year.
- Certain grants and subsidy payments relating to the Victorian bushfires and floods in Far North Queensland will be exempt from income tax.

## The bad ...

### Inflated property prices to remain - First Home Owner's Boost extended

Current	Proposed	Start date
First Home Owner's Boost was to end on 30 June 2009	The boost will now be extended as follows: <ul style="list-style-type: none"><li>▪ extension for an extra 6 months, from 1 July 2009 to 31 December 2009;</li><li>▪ from 1 July to 30 September inclusive, the scheme will remain as is; and</li><li>▪ from 1 October to 31 December 2009, the boost will be reduced by 50% - ie \$3,500 for purchasing an established home and \$7,000 for purchasing a new home.</li></ul>	Effective 1 July 2009

It appears to be common knowledge that the so-called first homeowner's boost achieves little more than inflating already high property prices. However, the Government has continued to support and extend this measure in the name of first home owners. It is unclear why the Government continues to fuel this measure despite the fact that it is well known that the measure is not really working to assist first home buyers at all, but is instead assisting vendors, real estate agents and property and construction companies. To be an honest measure, the measure could be reformed so as to **actually** assist first home owners.

As an alternative, the scope of the main residence exemption could be widened further. Or, perhaps, to assist the property industry, **if that is the actual focus of the measure**, an exemption could be provided for a first investment property. While these measures may not provide a direct cash incentive for individuals buying their first home, they are more honest and could have less of an adverse effect on prices in the property market and still work to stimulate the property industry.

## The ugly ...

### Australians overseas - watch out - section 23AG to be narrowed

Current	Proposed	Start date
Any Australian resident working overseas for a continuous period of 91 consecutive days or more is presently eligible for an exemption which means that they do not pay any Australian tax on their foreign employment income (section 23AG of the ITAA 1936).	<p>The foreign employment exemption is to be restricted to:</p> <ul style="list-style-type: none"><li>▪ an aid or charitable worker employed by a recognised non-government organisation;</li><li>▪ a government aid worker; or</li><li>▪ a specified government employee (eg defence and police force personnel deployed overseas).</li></ul> <p>Other workers will only be eligible to a tax offset for any taxes paid overseas.</p>	Effective 1 July 2009

The effect of the narrowing of the existing section 23AG exemption is to impose Australian taxation on most individuals who are Australian residents, who relocate overseas, *at the very least*, at the same rate as if they had remained in Australia. This effectively denies Australian resident individuals any tax incentive to relocate overseas. Alternatively, individuals who relocate will have to try and become residents of the countries to which they relocate to avoid Australian tax applying. Only by becoming resident overseas will they cease being taxed on their employment income in Australia (section 6-5 of the ITAA 1997).

It is not entirely clear why the Rudd Government has narrowed the scope of the exemption in section 23AG of the ITAA 1936. The narrowing is seriously distortionary. It basically results in individuals who relocate overseas, but remain Australian residents, being taxed on their employment remuneration income at a minimum at the tax rate that would have applied had they remained in Australia.

In particular, for Generation X and Y individuals, the measures will inhibit the choices available to them in selecting a work destination. With the increased mobility of labour worldwide, the narrowing of the exemption works much like a tariff and/or quota in that it modifies the allocation of labour resources globally. All nations in the world should be able to attract bright talent by reducing the tax rates which apply to individuals which come to their nations. This should provide a basis for competition between countries.

In essence, the Rudd Government has impaired this free movement of labour by Australian residents, particularly young Australians. The new measure is nothing short of ridiculous. It will probably not be revenue-raising to any great degree and it merely punishes individuals who choose to leave Australia in search of lower tax rates. At a time of high unemployment and falling opportunities within Australia, the restricted scope of the exemption should not only be criticised, but should be outright shunned. It is little wonder why there continues to be a long-term exodus of talent from Australia. Reducing further tax incentives for short-term relocation, merely encourages individuals to consider their medium to long-term relocation prospects overseas.

### **Employee share schemes - deferral opportunity & exemption abolished**

<b>Current</b>	<b>Proposed</b>	<b>Start date</b>
<p>Individuals part of employee share schemes can choose whether to be assessed in the income year of acquisition or defer the assessment to a later date.</p> <p>In addition, an exemption applies to shares or options with a value under \$1,000.</p>	<p><b>All</b> discounts on shares and options provided under either a qualifying or non-qualifying share scheme will be assessed in the income year in which they are <b>acquired</b>.</p> <p>Employees will <b>no longer</b> be able to elect to defer taxation on their discount to a later time.</p> <p>The \$1,000 tax exemption will be limited to those employees with a taxable income of less than \$60,000 per annum.</p>	<p>Effective 12 May 2009</p>

For quite some time now, there has been speculation about the proposed abolition of the deferral of the inclusion of the discount of shares and rights under employee share schemes. While considered a fair measure to many, the measure does reduce the tax incentives to issue shares and rights in companies. This could mean that companies will feel under additional strain to provide cash remuneration as an alternative to share and option schemes to compensate individuals. At a time when corporates are confronting increasing difficulty in retaining staff and providing them with adequate remuneration, it is questionable whether right now is an appropriate time to introduce this measure. Particularly, given that the commencement date for the measure is the time of announcement of the Federal Budget. Perhaps the measure could have waited, at least until such time as the Australian economy recovers or, at least, the end of this income year.

### **New quarantining for non-commercial losses**

<b>Current</b>	<b>Proposed</b>	<b>Start date</b>
All taxpayers can presently deduct losses from unprofitable business activities against their own income, provided certain tests are met. There is no quarantining of any losses against only income from the business activity itself.	<p>Taxpayers with an adjusted taxable income of <b>over \$250,000</b> annually will have excess deductions quarantined to the business activity under the non-commercial losses rules.</p> <p>The existing rules will continue to apply to taxpayers with an annual adjusted taxable income of \$250,000 or less.</p>	Effective 1 July 2009

The new non-commercial losses quarantining measure is aligned with the Rudd Government's political ideology. It is a measure consistent with the Government's attempts to increase taxes on the "rich". Therefore, the measure can neither be criticised nor applauded, except on ideological grounds.

However, the measure appears to be simply a way around increasing the tax rates applicable to higher income earners, a general measure, in favour of a narrower

measure which is unlikely to impact all of the “rich”. It may have been more honest to have introduced a new rate of tax for individuals over the \$250,000 mark. Moreover, the \$250,000 threshold appears to have been chosen arbitrarily.

## Other tax measures - the “indifferent” ...

### Closely held trusts & new TFN requirements

Current	Proposed	Start date
Closely held trusts are currently not subject to any TFN reporting requirements	The TFN requirements will apply to closely held trusts, including family trusts, from 1 July 2010. If a beneficiary does not provide a TFN to a trustee, trust distributions will be subject to withholding at the top marginal tax rate.	1 July 2010

It is important that all trustees of family trusts be aware of their new obligations under the TFN withholding provisions. No doubt the measures will catch many off-guard. Advisors, including all accountants and tax agents, should inform their clients of the new measures and their consequences. The measures are not entirely unique, however, as similar provisions exist with respect to interest bearing deposits, thus, it should be fairly straightforward for advisors to explain the measures to their clients.

### Other measures in brief

- The current R&D concessionary rules will all be replaced by a new R&D tax credit from 2010/11.
- The non-commercial loan rules will be extended to payments by way of a licence or right to use real property and chattels from 1 July 2009.
- Australia’s foreign source income attribution regimes will be reformed.

- Technical amendments will be made to the Uniform Capital Allowance Rules (including a new definition of depreciating asset).
- The Government will implement the Board of Taxation's recommendations to improve the tax treatment of off-market share buy-backs. This will commence from the date of Royal Assent of enacting legislation.
- The government will change the thin capitalisation regime for approved authorised deposit taking institutions.
- Australian managed investment trusts will be able to make an irrevocable election to apply the capital gains tax regime as the primary code for taxing certain disposals of assets, with effect from the 2008/09 income year.
- From 1 November 2008, limited CGT roll-over will be provided for assets transferred between trusts that have the same beneficiaries with the same entitlements, and no material discretionary elements.
- The Carbon Pollution Reduction Scheme will now only commence from 1 July 2011.