
# Federal Budget 2020–21 Report

6 October 2020

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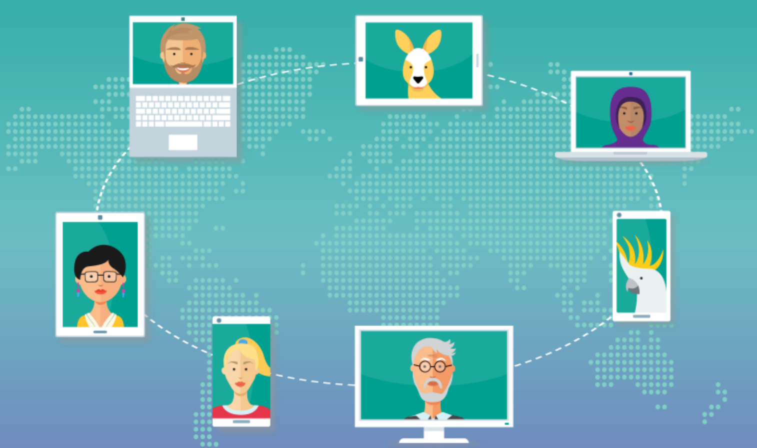

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# Contents

**Introduction** .......... **1**
What happens on Budget Night? .......... 1
The Budget Papers and related materials .......... 1
What happens next? .......... 2
Other Budget-related reports .......... 2
**Preamble** .......... **3**
A great start — more holistic reform needed! .......... 3
Major economic parameters .......... 5
**Measures | Start dates at a glance** .......... **6**
**Personal Tax & Transfer** .......... **8**
Individuals .......... 8
Stage 2 of personal income tax cuts brought forward by two years and LMITO retained for one more year .......... 8
**Business Taxation** .......... **12**
Small business .......... 12
Expanded access to small business tax concessions .......... 12
Business tax relief .......... 13
Further extension to instant asset write-off .......... 13
Loss carry-back .......... 15
State and Territory business support grants .......... 17
Victorian COVID-19 business support grants treated as NANE income .......... 17
Corporate taxation .......... 18
Corporate residency test .......... 18
Business incentives .......... 21
Government deferring proposed R&D changes .......... 21
International tax .......... 24
Various international tax measures .......... 24
Fringe benefits tax .......... 25
FBT exemption for skills training of redeployed employees .......... 25
Reducing the compliance burden of record keeping .......... 26
**Retirement and Wealth** .......... **27**

Capital gains tax ..... 27
CGT exemption for granny flat arrangements ..... 27
Superannuation ..... 29
Your Future, Your Super ..... 29
**Indirect Taxation ..... 30**
GST ..... 30
Expanded access to simplified accounting method ..... 30
**Administration ..... 31**
ATO funding ..... 31
Additional funding to address serious and organised crime in the tax and superannuation system ..... 31
**Abbreviations | Glossary ..... 32**
Legislative references ..... 34
**Contact ..... 35**

# Introduction

## What happens on Budget Night?

Budget Night is when the Treasurer tables the annual Appropriation Bills for the forthcoming year in the House of Representatives and delivers the second reading speech on those Bills. Since 1994, the Appropriation Bills have generally been tabled on the second Tuesday in May.[1]

The Budget Speech is usually delivered at 7.30pm, by legal time in the Australian Capital Territory. The Appropriation Bills are introduced into the House of Representatives, and the Treasurer tables other Budget related materials.

However, due to the uncertainty of the full economic impacts of the COVID-19 pandemic which made it difficult for the Government to formulate reliable economic and fiscal estimates in the first half of calendar 2020, the Government announced on 6 March 2020 that it had decided to defer the 2020–21 Budget until 6 October 2020.

### The Budget Papers and related materials

The main budget materials are the four key Budget Papers[1]:

| | | |
|---|---|---|
| ■ | Budget Paper No. 1: Budget Strategy and Outlook | Provides high level information on the overall economic outlook internationally and for Australia, and the Commonwealth's fiscal position. |
| ■ | Budget Paper No. 2: Budget Measures | Contains information about measures the Government intends to take to implement its policy decisions. Each measure is classified according to the revenue, expense or capital effect on the Commonwealth's finances.<br><br>Each measure has a 'costing' attached to it. This is the expected effect of the measure on the Commonwealth's finances over the forward estimates period[2]. |
| ■ | Budget Paper No. 3: Federal Financial Relations | Contains information about payments the Commonwealth makes to the States and Territories. |
| ■ | Budget Paper No. 4: Agency Resourcing | Deals mostly with appropriations and provides information on the individual amounts appropriated to each Commonwealth entity.<br><br>Also contains information amounts of money earmarked for specific activities or purposes. |

The key tax and superannuation measures of interest to the tax profession are typically contained in **Budget Paper No. 2**, under the revenue and expense headings for the Treasury portfolio.

1 Source: Parliament of Australia, The Budget: a quick guide.

2 See Glossary on **page 32**.

Along with the Budget Papers, the Government also publishes:

(a) the Budget Speech; and

(b) a Budget Overview.

The Budget Papers and related materials are made available on the internet at [budget.gov.au](budget.gov.au) when (or shortly after) the Treasurer commences the Budget Speech.

A series of media releases setting out the key tax and superannuation measures contained in the Budget are also made available on Budget Night by either:

- the Treasurer, The Hon Josh Frydenberg MP, on his media release webpage; or
- the Assistant Treasurer, The Hon Michael Sukkar MP, on his media release webpage.

### What happens next?

On the Thursday evening, immediately following Budget Night, the Leader of the Opposition, The Hon Anthony Albanese MP, will deliver the Opposition's Budget Reply Speech.

This year, both houses of Parliament sit from 6–8 October. The House of Representatives only sits from 19–29 October; both houses sit from 9–12 November then the final Parliamentary sitting for 2020 is 30 November–10 December. The 2021 sitting dates have not been announced yet, but Parliament typically resumes in early February.

This means that there are limited sitting days for the Government to pass its legislative program. It could be many weeks, months or even years, before taxpayers have certainty on all of the measures announced on Budget Night. There is a long list of measures which remain announced and unenacted from previous Budgets.

## Other Budget-related reports

Under the Charter of Budget Honesty, additional budget reports must be publicly released and tabled in Parliament through the year:

- **Mid-Year Economic and Fiscal Outlook** (**MYEFO**) — the Treasurer must release the MYEFO report within six months of the Budget, or by the end of January in a given year, whichever is later. The MYEFO report must update any information that has changed from the Budget during the year.

  Given the deferral of the Budget from 12 May to 6 October this year, it is uncertain whether a MYEFO report will be released in December 2020 as would have been the case had the Budget been released in May.
- **Final Budget Outcome** (**FBO**) — the Treasurer must also produce a FBO within three months of the end of each financial year. The FBO must contain the fiscal outcomes for the Commonwealth for the relevant year.[3] The Final Budget Outcome for 2020–21 is expected in September 2021.

The 2020–21 Budget figures will be updated when the 2021–22 Budget is announced, expected on 11 May 2021.[4]

3 Source: Parliament of Australia, The Budget: a quick guide.

4 This date is yet to be confirmed by the Government.

# Preamble


## Bob Deutsch, CTA

Senior Tax Counsel

## and Andrew Mills, CTA (Life)

Director of Tax Policy & Technical


6 October 2020

## A great start — more holistic reform needed!

In the usual fashion, many of the announcements in the 2020–21 Budget were foreshadowed by either government announcements or well-placed leaks.

While the pre-Budget submissions were many and varied, The Tax Institute was not alone in calling for announcements in the Budget presaging long-term structural change to our tax system. Many of the announcements in the Budget are welcome, however real and significant Tax Reform is desperately needed.

As mentioned in last weeks' TaxVine Preamble, the settings for the current Budget are unlike those seen in decades. For many, it will only be the tales related by parents and grandparents that could echo what the economy is currently facing. Recently, the Government confirmed the second quarter of negative growth on 2 September 2020 — -7% for the June quarter 2020 following the negative 0.3% growth in the March quarter 2020.

The Final Budget Outcome for 2019–20 revealed a significant deficit — $85.3 billion in underlying cash terms and a net operating deficit of $92.3 billion. While it is true to say that Australia has fared better than many countries, that does not detract from the significant challenge ahead. The immediate Budget challenge was foreshadowed to give rise to a significant deficit – even greater than the 2019–20 outcome – and this was confirmed with a forecast Budget deficit for 2020–21 of $213.7 billion.

We had been told that the Government will not be focusing on measures that would seek to return the budget to surplus until the rate of unemployment falls below 6%. Of course, some of the measures in this year's Budget are focused on achieving that goal. Given that the outcome of falling unemployment is lower social security outlays and greater tax collections, it is logical that this would be the Government's focus.

The key tax measures in the 2020–21 Budget are likely to mainly benefit SMEs and individuals. While there are some 18 tax related measures, the key items can be summarised as follows:

- **Personal tax cuts:** The stage 2 tax cuts are being advanced with the start date moving from 1 July 2022 to 1 July 2020. The effect of back-dating the change is that money will flow into the pockets of affected taxpayers as soon as the legislation receives Royal Assent. The Stage 3 tax cuts retain their original legislated start date of 1 July 2024 and no changes have been made as part of the current package. That of course leaves them with a significant degree of uncertainty as to whether they will ever be implemented despite being law.

- **Instant asset write-off:** The immediate write-off of new business investments made after 7:30 pm on 6 October 2020 and before 1 July 2022 will provide a strong incentive for all but the very largest businesses (i.e. those with turnover in excess of $5 billion) to invest in their future. It is perhaps surprising that a cap on the size of the investment was not imposed — this provides a welcome short term opportunity for large scale business asset investment. Businesses with an aggregated annual turnover of less than $50 million will also be allowed to write off second hands assets.
- **Loss carry-back:** The temporary loss carry-back provisions will provide a significant leg-up for struggling businesses making current year losses but profits in previous years. In such cases, any tax paid in respect of a previous year will be refunded to the taxpayer which will assist the business in funding its on-going operations. There is no monetary cap on the relief but there are constraints:
  - first, the furthest the loss carry-forward can be carried back is to the 2018–19 income year;
  - secondly, the carry-back must not generate a franking account deficit; and
  - thirdly, the loss-carry back ceases to operate from the end of the 2021–22 income year.

  The majority of small business are conducted outside a corporate structure, so this measure offers these taxpayers little in the way of refunds of previous tax paid.

All three measures are to be welcomed. However, the immediate write-off and the loss carry-back measures should be permanent features of a robust tax system, with some cap on the size of the investment in the case of the investment write-off.

Other measures in the Budget cover corporate residency, fringe benefits tax (**FBT**) reform and Research and Development (**R&D**) incentive refinements.

Regrettably, the opportunity was not taken to include in the Budget any announcements relating to:

- long overdue finalisation of reform to Division 7A;
- improvements to the superannuation guarantee regime;
- the $10,000 cash payment limit which was proposed to commence on 1 January 2020;
- the 3-year audit cycle which was due to start on 1 July 2019;
- a bundle of early release of superannuation measures for crime victims and domestic violence victims;
- ABN reforms announced in last year's Budget, including reconfirming details on the Australian Business Register (**ABR**) which was due to start on 1 July 2022; and
- measures regarding the licensing of an individual's fame or image which was proposed to commence from 1 July 2019.

Nonetheless, The Tax Institute is very supportive of a Budget which provides good positive incentives for struggling businesses to bat on, employ people and get back on the road to a post-COVID-19 recovery, as well as put cash into the pockets of lower to middle bracket wage earners through welcome tax relief.

It is a great start but is merely a first step towards what ultimately must to be holistic tax reform.

Kind regards,

**Andrew Mills and Bob Deutsch**

# Major economic parameters[5]

| | Outcomes | | Forecasts | | Projections | |
|---|---|---|---|---|---|---|
| | 2018–19 | 2019–20 | **2020–21** | 2021–22 | 2022–23 | 2023–24 |
| **Underlying cash balance**<br>Per cent of GDP | **($4.2b)**<br>(0.5%) | **($85.3b)**<br>(4.3%) | **($213.7b)**<br>**(11.0%)** | **($112.0b)**<br>(5.6%) | **($87.9b)**<br>(4.2%) | **($66.9b)**<br>(3.0%) |
| Nominal GDP[6] | 5% | 1.7% | **(1.75%)** | 3.25% | 4.5% | 5.0% |
| Real GDP[7] | 2.25% | (0.2%) | **(1.5%)** | 4.75% | 2.75% | 3.0% |
| Unemployment rate | 5% | 7% | **7.25%** | 6.5% | 6% | 5.5% |
| CPI | 1.6% | (0.3%) | **1.75%** | 1.5% | 1.75% | 2.0% |
| Gross debt<br>Per cent of GDP | $542.0b<br>27.8% | $684.3b<br>34.5% | **$872.0b**<br>44.8% | $1,016.0b<br>50.5% | $1,083.0b<br>51.6% | $1,138.0b<br>51.6% |
| Net debt<br>Per cent of GDP | $373.5b[8]<br>19.2% | $491.2b[8]<br>24.8% | **$703.2b**[8]<br>36.1% | $812.1b<br>40.4% | $899.8b<br>42.8% | $966.2b<br>43.8% |

5 Source: Budget Paper No. 1. The ‘Budget year’ is 2020–21, while 2021–22, 2022–23 and 2023–24 are referred to as the ‘forward years’.

6 Nominal GDP is unadjusted for inflation.

7 Real GDP is adjusted for inflation.

8 Estimate only.

# Measures | Start dates at a glance

| Budget measure | Start date |
|---|---|
| **Personal Tax & Transfer** | |
| Stage 2 of personal income tax cuts brought forward by two years and LMITO retained for one more year | 1 July 2020 |
| **Business Taxation** | |
| Expanded access to small business tax concessions | Various |
| Further extension to instant asset write-off | Eligible depreciable assets acquired from 7:30pm (AEDT) on 6 October 2020 and first used or installed by 30 June 2022 |
| Loss carry-back | Losses made in the 2019–20, 2020–21 and 2021–22 income years only |
| Victorian COVID-19 business support grants treated as NANE income | Grants announced on or after 13 September 2020<br>Payments made between 13 September 2020 and 30 June 2021 |
| Corporate residency test | First income year after Royal Assent but option to apply the new law from 15 March 2017 |
| Government deferring proposed R&D changes | Deferred from 1 July 2019 to income years starting on or after 1 July 2021 |
| Various international tax measures | Various |
| FBT exemption for skills training of redeployed employees | 2 October 2020 |
| Reducing the compliance burden of record keeping | 1 April of the FBT year after the date of Royal Assent of the enabling legislation |
| **Retirement and Wealth** | |
| CGT exemption for granny flat arrangements | 1 July following the date of Royal Assent of enabling legislation |
| Your Future, Your Super | 1 July 2021 |

| Budget measure | Start date |
| --- | --- |
| **Indirect Taxation** | |
| Expanded access to simplified accounting method | 1 July 2021 |
| **Administration** | |
| Additional funding to address serious and organised crime in the tax and superannuation system | Extension of current funding arrangement to 30 June 2023 |

# Personal Tax & Transfer

## Individuals

### Stage 2 of personal income tax cuts brought forward by two years and LMITO retained for one more year

**START DATE**

From the 2020–21 income year

The Government announced that it will bring forward Stage 2 of the Personal Income Tax Plan from the 2019–20 Budget by two years, from 1 July 2022 to 1 July 2020.

Under the revised plan:

- the upper income threshold of the 19% personal income tax bracket will increase from $37,000 to $45,000; and
- the upper income threshold of the 32.5% personal income tax bracket will increase from $90,000 to $120,000.

The low and middle income tax offset (**LMITO**) (see **Table 3** on **page 10**) which is worth up to $1,080, will be retained until 1 July 2021.

The bring forward of the Stage 2 personal tax cuts by two years means people who earn:

- between $45,000 and $90,000 will have an additional $1,080 of post-tax income in 2020–21;
- more than $120,000 will have an additional $2,565 of post-tax income in 2020–21.

Stage 3 of the Personal Income Tax Plan remains unchanged and commences from 2024–25 as legislated.

*Source: Budget Paper No. 2 page 18*

*Media Release, 6 October 2020, Treasurer*

#### Background

##### 2018 amendments

Amendments made by the *Treasury Laws Amendment (Personal Income Tax Plan) Act 2018*[9] (2018 Act) gave effect to the announcements made on 8 May 2018 as part of the 2018–19 Budget.

The 2018 Act made the following changes:

- introduced the LMITO to reduce the tax payable by low and middle income earners in the 2018–19 to 2021–22 income years;
- from 2022–23 — merges the LMITO and the low income tax offset (**LITO**) into a more generous new low income tax offset; and
- progressively increases the income tax rate thresholds in 2018–19, 2022–23 and 2024–25.

[9] Enacted on 21 June 2018 as Act No. 47 of 2018.

### 2019 amendments

Further amendments to the Personal Income Tax Plan were made by the *Treasury Laws Amendment (Tax Relief So Working Australians Keep More Of Their Money) Act 2019*[10] (**2019 Act**), which gave effect to the announcements made on 2 April 2019 as part of the 2019–20 Budget.

The 2019 Act made the following changes:

- increased the base and maximum amounts of the LMITO for the 2018–19 to 2021–22 income years to $255 (from $200) and $1,080 (from $530);
- increases the amount of the LITO from 2022–23, ensuring all taxpayers remain better off following the cessation of the LMITO in 2022–23;
- reduces the tax payable by individuals from 2022–23 by increasing the upper threshold of the first personal rate of income tax of 19% from $41,000 to **$45,000**; and
- reduces the tax payable by individuals from 2024–25 by lowering the second personal rate of income tax from 32.5% to **30%**.

## Currently legislated rates and thresholds

The rates and thresholds, as currently legislated, may be summarised as follows:

### Residents

**TABLE 1:** Summary of individual income tax rates — residents

| **To 30 June 2018** | | STAGE 1 **From 1 July 2018** | | STAGE 2 **From 1 July 2022*** | | STAGE 3 **From 1 July 2024** | |
|---|---|---|---|---|---|---|---|
| Income threshold | Tax rate | Income threshold | Tax rate | Income threshold | Tax rate | Income threshold | Tax rate |
| $18,200 | 19% | $18,200 | 19% | $18,200 | 19% | $18,200 | 19% |
| $37,000 | 32.5% | $37,000 | 32.5% | $45,000 | 32.5% | $45,000 | 30% |
| $87,000 | 37% | $90,000 | 37% | $120,000 | 37% | $200,000 | 45% |
| $180,000 | 45% | $180,000 | 45% | $180,000 | 45% | | |

* Under the 2020–21 Budget measure, this will become 1 July 2020.

[10] Enacted on 5 July 2019 as Act No. 52 of 2019.

**TABLE 2:** Individual income tax rates: **2019–20 and 2020–21** — residents

| Taxable income | Marginal rate | Tax on this income |
|---|---|---|
| $0–$18,200 | Nil | Nil |
| $18,201–$37,000 | 19% | 19 cents for each $1 over $18,200 |
| $37,001–$90,000 | 32.5% | $3,572 plus 32.5 cents for each $1 over $37,000 |
| $90,001–$180,000 | 37% | $20,797 plus 37 cents for each $1 over $90,000 |
| $180,001 and over | 45% | $54,097 plus 45 cents for each $1 over $180,000 |

**TABLE 3:** Income tax offsets

<table>
<tr><th>Offset</th><th colspan="2">STAGE 1 — From 1 July 2018</th><th colspan="2">STAGE 2 — From 1 July 2022</th></tr>
<tr><th></th><th>Taxable income</th><th>Rate</th><th>Taxable income</th><th>Rate</th></tr>
<tr><td rowspan="4">LITO</td><td>$0–$37,000</td><td>$445</td><td>$0–$37,500</td><td>$700</td></tr>
<tr><td rowspan="2">$37,000–$66,666</td><td rowspan="2">$445 less 1.5 cents for every $1 by which the taxable income exceeds $37,000</td><td>$37,501–$45,000</td><td>$700 less 5 cents for every $1 by which the taxable income exceeds $37,500</td></tr>
<tr><td>$45,001–$66,666</td><td>$700 less 1.5 cents for every $1 by which the taxable income exceeds $45,000</td></tr>
<tr><td>$66,667 and over</td><td>Nil</td><td>$66,667 and over</td><td>Nil</td></tr>
<tr><td rowspan="5">LMITO</td><td>$0–$37,000</td><td>$255</td><td colspan="2" rowspan="5">LMITO available only until 1 July 2021</td></tr>
<tr><td>$37,001–$48,000</td><td>$255 plus 7.5% of the amount of the income that exceeds $37,000</td></tr>
<tr><td>$48,001–$90,000</td><td>$1,080</td></tr>
<tr><td>$90,001–$126,000</td><td>$1,080 less 3% of the amount of the income that exceeds $90,000</td></tr>
<tr><td>$126,001 and over</td><td>Nil</td></tr>
</table>

### Non-residents and working holiday makers

**TABLE 4:** Individual income tax rates: **2019–20 and 2020–21** — non-residents

| Taxable income | Marginal rate | Tax on this income |
|---|---|---|
| $0–$90,000 | 32.5% | 32.5 cents for each $1 |
| $90,001–$180,000 | 37% | $29,250 plus 37 cents for each $1 over $90,000 |
| $180,001 and over | 45% | $62,550 plus 45 cents for each $1 over $180,000 |

**TABLE 5:** Individual income tax rates: **2019–20 and 2020–21** — working holiday makers

| Taxable income | Marginal rate | Tax on this income |
|---|---|---|
| $0–$37,000 | 15% | 15 cents for each $1 |
| $37,001–$90,000 | 32.5% | $5,550 plus 32.5 cents for each $1 over $37,000 |
| $90,001–$180,000 | 37% | $22,775 plus 37 cents for each $1 over $90,000 |
| $180,001 and over | 45% | $56,075 plus 45 cents for each $1 over $180,000 |

#### Key insights

From 1 July 2020, the Government proposes to:

- bring forward Stage 2 of the Personal Income Tax Plan by two years; and
- retain the LMITO for the 2020–21 income year.

This will provide significant tax relief to individual taxpayers. In particular, low and middle income earners will receive tax relief of up to $2,475 for singles, and up to $5,490 for dual income families, compared with the 2017–18 settings.

This measure is designed to help put more money into the pockets of taxpayers in the expectation they will spend much of it. In turn, this will keep businesses operating and ensures employers are retaining and hiring staff.

# Business Taxation

## Small business

### Expanded access to small business tax concessions

**START DATE**

Various — see below

The Government announced that it will expand access to a range of small business tax concessions currently available only to small business entities[11].

Under the measures, businesses with an aggregated annual turnover of $10 million or more and less than $50 million will have access to the 10 small business concessions set out in the table below.

**TABLE 6**: Expanded small business tax concessions

| Concession | Legislative reference | Start date |
|---|---|---|
| Immediate deduction for certain start-up expenses | s 40-880(2A) of the ITAA 1997 | 1 July 2020 |
| Immediate deduction for certain prepaid expenditure | s 82KZM of the ITAA 1936 | 1 July 2020 |
| FBT exemption for car parking benefits | s 59GA of the FBTA 1986 | 1 April 2021 |
| FBT exemption for multiple work-related portable electronic devices | s 58X(2)(a) and s 58X(4) of the FBTA 1986 | 1 April 2021 |
| Simplified trading stock rules | Subdiv 328-E of the ITAA 1997 | 1 July 2021 |
| Remit PAYG instalments based on GDP-adjusted notional tax | s 45-130(1)(d) of Schedule 1 to the TAA 1953 | 1 July 2021 |
| Settle excise duty monthly on eligible goods[12] | s 61C of the Excise Act 1901 | 1 July 2021 |
| Settle excise-equivalent customs duty monthly on eligible goods[12] | | 1 July 2021 |
| Two-year amendment period | Item 2 of the table in s 170(1) of the ITAA 1936 | 1 July 2021 |
| Simplified accounting method determination for GST purposes | s 123-5 of the GSTA 1999 | 1 July 2021 |

11 Defined in s 328-110 of the ITAA 1997 as an entity that, broadly, carries on a business and has an aggregated annual turnover of less than $10 million.

12 Eligible small businesses can currently apply to defer settlement of excise duty and excise-equivalent customs duty from a weekly to a monthly reporting cycle. See ATO web guidance.

*Source: Budget Paper No. 2 page 16–17*

*Joint Media Release, 2 October 2020, Treasurer and Assistant Treasurer and Minister for Housing*

### Key insights

This range of 10 small business tax concessions, currently only available to small business entities, will be available to medium-sized businesses with an aggregated annual turnover of less than $50 million. This higher threshold is consistent with the threshold that applies to:

- the COVID-19 stimulus measure, the temporary cash flow boost; and
- the $30,000 instant asset write off as it applied to entities between 2 April 2019 and 12 March 2020.

# Business tax relief

## Further extension to instant asset write-off

**START DATE**

Eligible depreciable assets acquired from 7:30pm (AEDT) on 6 October 2020 and first used or installed by 30 June 2022

The Government has announced that it will support businesses with an aggregated annual turnover of less than $5 billion by enabling them to deduct the full cost of eligible depreciable assets acquired from 7:30pm (AEDT) on 6 October 2020 and first used or installed by 30 June 2022.

Full expensing the cost in the year of first use will apply to new depreciable assets and the cost of improvements to existing eligible assets. For small and medium-sized businesses, full expensing also applies to second-hand assets.

Other considerations:

- Larger business entities can still deduct the full cost of eligible second-hand assets costing less than $150,000 that are purchased by 31 December 2020 under the enhanced instant asset write-off (**IAWO**).
- Businesses that acquired eligible assets for the pre-existing enhanced $150,000 IAWO will have an extra six months, until 30 June 2021, to first use or install those assets.
- Small businesses can deduct the balance of their simplified depreciation pool at the end of the income year while full expensing applies. The five-year limitation period where a small business entity opts out of this regime continues to remain suspended.

*Source: Budget Paper No. 2 page 20*

*Media Release, 6 October 2020, Treasurer*

**TABLE 7:** Eligibility for further extended instant asset write off

| | Small business entities | Medium business entities | Larger business entities |
|---|---|---|---|
| Meaning of entity size – legislative reference | s 328-110 | s 40-82(4) | s 40-82(4A) |
| Claim for IAWO | s 328-180 | s 40-82 | s 40-82 |
| Aggregated annual turnover threshold | < $10 million | ≥ $10 million to < $50 million | ≥ $50 million to < $500 million |
| Asset acquired | From 7:30pm (AEDT) on 6 October 2020 | From 7:30pm (AEDT) on 6 October 2020 | From 7:30pm (AEDT) on 6 October 2020 |
| First used or installed | By 30 June 2022 | | |
| Application to second-hand assets | Yes | Yes | No |
| Existing $150,000 IAWO | Acquired from 7:30pm (AEST) on 12 May 2015 to 31 December 2020, and first used or installed by 30 June 2021 | Acquired from 7:30pm (AEST) on 2 April 2019 to 31 December 2020, and first used or installed by 30 June 2021 | |

(Legislative references in this table are to the ITAA 1997)

## Key insights

- For eligible depreciable assets acquired from 7:30pm (AEDT) on 6 October 2020 and first used or installed by 30 June 2022, over 99% of businesses will be able to write off the full value of any eligible asset they purchase for their business. This will be available for small, medium and larger businesses with a turnover of less than $5 billion until 30 June 2022.
- It is designed to improve cash flow for qualifying businesses that purchase eligible assets and to encourage new investment to support the economic recovery.
- Relevant consideration: whether businesses will be confident to spend to acquire depreciable assets given the present and future uncertainty as a result of the COVID-19 pandemic, and during the period from the date of announcement to the date the measures become law.
- The decision to acquire assets should be driven by commercial business considerations and not for reasons to acquire an immediate tax benefit.

## Loss carry-back

**START DATE**

Losses made in the 2019–20, 2020–21 and 2021–22 income years only

The Government has announced that it will re-introduce a 'loss carry-back' mechanism which will allow corporate tax entities (**CTEs**) that have paid tax in the past, but are now in a tax loss position, to carry their loss back to those past years to obtain a refund of some of the tax they previously paid.

This measure will enable many distressed businesses to claim back the taxes they paid on their pre-COVID-19 profits against losses they are incurring during the current recession.

Under the measure, CTEs with an aggregated annual turnover of less than $5 billion will be allowed to carry-back losses from the 2019–20, 2020–21 and 2021–22 income years against taxable incomes from the 2018–19, 2019–20 or 2020–21 income years.

The loss that is carried back against a taxed profit from a previous income year will generate a refundable tax offset in the year in which the loss is made. Eligible CTEs can elect to claim the tax refund when they lodge their 2020–21 and 2021–22 tax returns.

The resulting tax refund is limited in two ways:

- the amount carried back must not be more than the earlier taxed profits; and
- the carry-back must not generate a franking account deficit.

Under the current law, companies are required to carry losses forward to offset profits in future years. CTEs that do not elect to carry-back their losses under this measure can still carry the losses forward under the normal rules.

*Source: Budget Paper No. 2 page 21*

*Media Release, 6 October 2020, Treasurer*

### Example

In the 2018–19 and 2019–20 income years, Zipline Adventures Pty Ltd paid tax of $3 million on $10 million of taxable income (i.e. the company made an annual taxable profit of $5 million, which attracted tax of $1.5 million each year).

In 2020–21, the company made a tax loss of $4 million.

Under the current law, the company can carry the loss forward to offset against assessable income in a future income year.

Under loss carry-back, the company can choose to carry-back the $4 million loss against the taxes paid in the 2018–19 and 2019–20 income years. It claims a refundable tax offset of $1.2 million in its 2020–21 income tax return.

**Variation to facts**

Assume the above facts, but the company also paid a franked dividend of $4.67 million in September 2019. This gave rise to a franking debit of $2 million. Assume the credit to the franking account was $3 million (arising from the tax payments), so the balance in the franking account in 2020–21 is $1 million, after allowing for the franking debit attributable to the dividend paid in 2019–20.

Under loss carry-back, the company can choose to carry-back only $3.33 million of the $4 million loss against the taxes paid in the 2018–19 and 2019–20 income years. It claims a refundable tax offset of $1 million in its 2020–21 income tax return. The balance of the loss, i.e. $666,667 can be carried forward under the normal rules.

## Legislative background

### Measure introduced in 2013

The loss carry-back measure was originally introduced by the Gillard Government.[13] The measure was designed to help businesses facing pressures in a 'patchwork economy' and encourage them to invest and grow.

The measure was contained in Schedules 5 and 6 to the *Tax and Superannuation Laws Amendment (2013 Measures No. 1) Act 2013*.[14] Under the measure, a corporate tax entity that paid tax in the past, but was later in a tax loss position, was allowed to carry its loss back to those past years to obtain a refund of some of the tax previously paid. This was done through the mechanism of a refundable tax offset, which avoided the need to amend any prior year tax returns.

The amount of the tax offset that the entity could receive was the lowest of:

- the tax value of the amount of the loss the entity chooses to carry-back;
- the tax payable on $1 million of taxable income ($300,000 at the then single corporate tax rate of 30%);
- the entity's franking account balance at the end of the current year; or
- the tax liability for the year(s) the entity carries the loss back to.

The measure had the following features:

- It was available only to corporate tax entities.
- It was limited to revenue losses and was not available for capital losses.
- A loss could be carried back for a maximum of two years (a transitional one year carry-back period applied for 2012–13).

The measure applied to assessments for the 2012–13 and later income years.

13 The measure was announced by then Treasurer, Wayne Swan, and then Assistant Treasurer, David Bradbury, in Joint Media Release No. 022 on 6 May 2012.

14 Enacted on 28 June 2013 as Act. 88 of 2013.

### Measure repealed in 2014

The measure was repealed[15] in 2014 by then Prime Minister, Tony Abbott. It was repealed because he wanted to remove any measures that were funded by the abandoned minerals resource rent tax.

#### Key insights

The former loss carry-back allowed companies to effectively use current losses against past taxes paid. This is a scheme that is common in many OECD countries. In fact, the absence of it probably leaves Australia a bit behind the rest of the world.

The amount of tax that could previously be claimed back was capped at $300,000 — this meant losses of up to $1 million could be set off against past taxes. This was of most benefit to small and medium sized businesses.

Under the new loss carry-back, the measure is capped in the following ways:

- the CTE must have an aggregated annual turnover of less than $5 billion;
- the amount carried back must not be more than the earlier taxed profits; and
- the carry-back must not generate a franking account deficit.

Given that the majority of small businesses are conducted outside a corporate structure (i.e. they conduct their businesses as sole traders or through a partnership or trust structure), this measure offers these taxpayers little in the way of refunds of previous tax paid.

We await the legislative provisions, but it is assumed that the measure will also be confined to revenue losses and will not be available for capital losses.

Loss carry-back is a welcome measure, but it would be preferable if this were a permanent fixture of the law.

# State and Territory business support grants

## Victorian COVID-19 business support grants treated as NANE income

The Government has announced that the Victorian Government's business support grants for small and medium business will be treated as non-assessable, non-exempt (**NANE**) income for tax purposes. The Victorian grants were originally announced by the Victorian Premier, Daniel Andrews, on 13 September 2020 in response to the economic impact of the COVID-19 pandemic.

**START DATE**

Grants announced on or after 13 September 2020

Payments made between 13 September 2020 and 30 June 2021

15 The loss carry-back measure was repealed by Schedule 2 to the *Minerals Resource Rent Tax Repeal and Other Measures Act 2014*, which was enacted on 5 September 2014 as Act No. 96 of 2014.

This arrangement has potential to be extended to all States and Territories on an application basis. Eligibility would be restricted to future grants program announcements for small and medium businesses facing similar circumstances to Victorian businesses affected by the Stage 4 restrictions.

Furthermore, a new power will be introduced in the income tax laws to make regulations to ensure that specified State and Territory COVID-19 business support grant payments are NANE income.

Eligibility for this treatment will be limited to grants announced on or after 13 September 2020 and for payments made between 13 September 2020 and 30 June 2021.

*Source: Budget Paper No. 2 page 14*

### Key insights

The Government's decision to assist Victorian business support grants and all future grants from other States and Territories, on an application basis, is a very welcome response.

This measure means that the grant from the State or Territory government is of full value to businesses rather than a portion being effectively transferred to the Commonwealth via the tax system.

The ultimate tax outcome of such a grant will depend on the type of entity that receives the grant. If the grant is received by:

- a sole trader — the tax-free nature of the grant will be retained;
- a discretionary trust — the tax-free nature of the grant will be retained when it is distributed to the beneficiaries;
- a unit trust — the tax-free nature of the grant will be retained when it is distributed to the beneficiaries due to the exception to CGT event E4 in s 104-71 of the ITAA 1997;
- a company — the tax-free nature of the grant will be lost when it is distributed to shareholders, as it will give rise to an unfranked dividend.

# Corporate taxation

## Corporate residency test

The Government announced that it will make technical amendments to clarify the corporate residency test.

The Government will amend the law to provide that a company that is incorporated offshore will be treated as an Australian resident for tax purposes if it has a 'significant economic connection to Australia'.

This test will be satisfied where the company's:

- core commercial activities are undertaken in Australia; and
- central management and control (**CMAC**) is in Australia.

**START DATE**

First income year after Royal Assent but option to apply the new law from 15 March 2017

This measure is stated to have effect from the first income year after the date of Royal Assent of the enabling legislation. Accordingly, it is expected that the law will be drafted to commence from the first income year following the enactment of enabling legislation.

However, the Government has indicated that taxpayers will have the option of applying the new law from 15 March 2017, being the date on which the ATO withdrew Taxation Ruling, 'TR 2004/15: Income tax: residence of companies not incorporated in Australia – carrying on a business in Australia and central management and control' (TR 2004/15), in light of the decision in the *Bywater Investments Ltd v Federal Commissioner of Taxation* [2016] HCA 45 (***Bywater***) case.

Separately, the Government has announced that it intends to undertake public consultation on potential amendments to the corporations law with the objective of providing businesses greater flexibility in the way in which they comply with corporations law regulations. Among other things, this measure would allow businesses to utilise technology to hold virtual AGMs.

*Source: Budget Paper No. 2 page 13*

## Background

### Tax issue

Australia operates a residence-based approach to determine the tax liability of a taxpayer. Accordingly, for corporate tax entities, clarity around the corporate residency rules is critical to determine the scope of Australia's taxing rights over profits derived by such entities.

To determine residency for a company that is not incorporated in Australia, the law requires an assessment of whether the company carries on business in Australia and either that the company's CMAC or voting power be controlled in Australia.

After a review by the Board of Taxation (**the Board**) in 2003[16] the ATO expressed its view in TR 2004/15 that the carrying on of business in Australia is a separate requirement to the CMAC test and must be established independently of the exercise of CMAC in Australia. The ATO maintained the position set out in TR 2004/15 until the High Court's decision in *Bywater* in 2016.

Thereafter, the ATO's interpretation of the corporate residency rules departed from its long held position. This gave rise to a great deal of uncertainty among corporate taxpayers as to whether they fell within the scope of the rules, and therefore within the Australian corporate tax net.

On 15 March 2017, the ATO withdrew TR 2004/15 and replaced it with Taxation Ruling 'TR 2018/5 Income tax: central management and control test of residency' (**TR 2018/5**) in which the ATO took the view that a company that carries on business and has its CMAC in Australia will carry on business in Australia within the meaning of the CMAC test.

This view was founded on the basis that the CMAC of a business is factually part of the carrying on of that business. In addition, the ATO subsequently released 'Practical Compliance Guideline PCG 2018/9 Central Management and control test of residency: identifying where a company's central management and control is located' to assist foreign incorporated companies in applying the principles outlined in TR 2018/5.

16 See pages 106-109 *International Taxation, A report to the Treasurer Volume 1 The Board of Taxation's Recommendations*, 28 February 2003.

### The Board's 2019 review

In August 2019, the Government requested the Board to undertake a review of the operation of Australia's corporate tax residency rules, including the definition of 'a corporate resident'. The objective of the review was to assess whether the rules operate appropriately in light of contemporary, commercial board practices and international tax integrity rules.

In particular, the Treasurer requested that the Board consider whether the corporate tax residency rules:

- minimise commercial uncertainty and ambiguity;
- are consistent with and aligned with modern day corporate board practices;
- protect the tax system against multinational profit shifting; and
- otherwise support Australia's tax integrity rules as they apply to multinational corporations.

In its Reform Options paper of December 2019, one of the reform options canvassed by the Board was retention of the CMAC test but with legislative modification. Specifically, the Board recommended that the CMAC test be modified to ensure that it is applied in two steps (consistent with the view taken in former TR 2004/15).

In light of responses to public consultation, the Board also recommended clarification of the meaning of the criteria in relation to 'carrying on business in Australia' and 'CMAC'.

### Key insights

This measure is consistent with the recommendation made by the Board in its 2020 report titled 'Review of Corporate Tax Residency' and is designed to reflect the position prior to the decision in the *Bywater* case. This is a welcome announcement that will provide long awaited certainty for corporate taxpayers, and it substantially reinstates the position in the withdrawn TR 2004/15.

This measure is expected to have effect from the first income year after the date of Royal Assent of the enabling legislation, although the Government has indicated that taxpayers will have the option of applying the new law from 15 March 2017, being the date on which the ATO withdrew TR 2004/15, in light of the decision in the *Bywater* case. It will be interesting to see how the start date election is drafted in the legislation and in particular, whether it will only be able to be retrospectively applied from 15 March 2017 or if it may be applied from any date thereafter (for example, by companies incorporated after 15 March 2017).

The Government has separately announced a non-tax measure which aims to provide businesses greater flexibility in the way in which they comply with regulations. Among other things, this measure allows businesses to utilise technology to hold virtual AGMs. It is intended to reduce regulatory costs and reduce the cost of compliance. It will be interesting to see whether the ATO issues guidance on the tax implications of virtual AGMs, in light of the corporate residency measure.

# Business incentives

## Government deferring proposed R&D changes

**START DATE**

Deferred from 1 July 2019 to income years starting on or after 1 July 2021

The Government has announced that it will make additional enhancements to the proposed changes to the R&D tax incentive, which are currently before the Senate. The aim of this measure is to encourage R&D investment in Australia and to assist businesses to navigate the economic impacts of the COVID-19 pandemic.

Small R&D entities (with an aggregated annual turnover of less than $20 million) will be able to access the refundable R&D tax offset at a premium of 18.5 percentage points above their corporate tax rate. The Government has stated that it will not proceed with the $4 million cap on annual cash refunds for small R&D entities.

The intensity tiers for larger R&D entities (with an aggregated annual turnover of $20 million or more) will be reduced from three tiers to two[17]. This is designed to provide greater certainty for R&D investment while still incentivising entities for which R&D forms a greater proportion of their business expenditure. The R&D premium ties the rate of the non-refundable R&D tax offset to an entity's incremental R&D intensity, being R&D expenditure as a proportion of total expenses for a given year.

For larger R&D entities, the marginal R&D premium will be the claimant entity's tax rate plus:

- a premium of 8.5 percentage points above the entity's tax rate for R&D expenditure between 0%–2% R&D intensity; or
- a premium of 16.5 percentage points above the entity's tax rate for R&D expenditure above 2% R&D intensity.

The Government has decided to defer the start date of this measure so that all changes to the R&D tax incentive program apply to the income years starting on or after **1 July 2021**.

The Government has indicated that all other aspects of the 2019–20 MYEFO measure, such as the increase to the R&D expenditure threshold from $100 million to $150 million per annum, will remain unchanged.

[17] The original bill containing the proposed changes detailed four tiers. This was reduced to three tiers when the measures were reintroduced into Parliament on 5 December 2019.

**TABLE 8**: Current and proposed R&D tax incentive rates and thresholds[18]

| Aggregated annual turnover[19] of the R&D entity | Rate of R&D tax offset | R&D spend as % of total expenditure | Proposed premium | Proposed R&D tax offset rate | |
|---|---|---|---|---|---|
| | | | | **Corporate tax rate: 25%** | **Corporate tax rate: 30%** |
| Less than $20 million | Refundable **43.5%** tax offset | Not applicable | 18.5% | **43.5%** | **48.5%** |
| $20 million or more, or controlled by exempt entities | Non-refundable **38.5%** tax offset | Initial 2%<br>Above 2% | 8.5%<br>16.5% | **33.5%**<br>**41.5%** | **38.5%**<br>**46.5%** |

*Source: Budget Paper No. 2 page 19–20*

## Background

### Legislative background

On 8 May 2018, the Government announced as part of the 2018–19 Budget that it would amend the R&D tax incentive to better target the program, and improve its integrity and fiscal affordability. This was in response to the recommendations of the April 2016 Review of the R&D Tax Incentive which concluded the program falls short of meeting its stated objectives of encouraging industry to conduct R&D activities that might otherwise not be conducted and which benefit the wider Australian economy. The review also found that the cost of the program had exceeded initial estimates. The changes to the R&D tax incentive were proposed to apply from **1 July 2018**.

Schedules 1 to 3 of the *Treasury Laws Amendment (Making Sure Multinationals Pay Their Fair Share of Tax in Australia and Other Measures) Bill 2018* (**the 2018 Bill**), which was introduced into Parliament on 20 September 2018, were proposed to give effect to the Budget measures. The Senate Economics Legislation Committee considered the 2018 Bill and reported on 11 February 2019. In its report, the Committee concluded:

> The committee recognises the need for the Government to maintain public confidence in the integrity and financial sustainability of the R&D tax incentive. This confidence promotes business innovation across the economy and allows the scheme to meet its stated objectives of additionality and spillovers. Further, the committee recognises that, while the R&D tax incentive in its current form is falling short of these aims and objectives, there is a need to reform the R&D tax incentive. On the weight of evidence presented, the committee considers that the bill should not proceed until there is further consideration of the R&D tax incentive measures.

The 2018 Bill lapsed on 11 April 2019 with the calling of the 2019 Federal election.

The measures were then resurrected in the *Treasury Laws Amendment (Research and Development Tax Incentive) Bill 2019* (**the 2019 Bill**) which was introduced into Parliament on 5 December 2019. The 2019 Bill proposed that the measures commence on **1 July 2019** instead of 1 July 2018, given the delay since the original announcement.

[18] See s 355-100 of the ITAA 1997.

[19] As defined in s 328-115 of the ITAA 1997. Includes the annual turnovers of affiliates of the R&D entity and entities connected with the R&D entity.

On 6 February 2020, the Senate referred the provisions of the Bill to the Economics Legislation Committee for inquiry and report by 30 April 2020. The reporting date for the inquiry was subsequently extended to 7 August 2020, and later to 24 August 2020. On 21 August 2020, the reporting date was extended from 24 August 2020 to 12 October 2020.

The Bill remains before the Senate.[20]

### The previous proposed changes to the R&D tax incentive

Broadly, the Bill proposed to make the following changes:

- increase the R&D expenditure threshold from $100 million to $150 million and make the threshold a permanent feature of the law;
- instead of a flat 43.5% rate for all R&D entities, link the R&D tax offset for small R&D entities (i.e. those with an aggregated annual turnover of less than $20 million) to their corporate tax rate, plus a premium of 13.5 percentage points. For 2019–20, the offset rate was proposed to be **41%** (i.e. 13.5% + 27.5%) if the company were a base rate entity, or **43.5%** (i.e. 13.5% + 30%) if the company were not a base rate entity.[21] In 2020–21, the offset rate for a company that was a base rate entity would have been **39.5%** (i.e. 13.5% + 26%);
- cap the refundability of the R&D tax offset at $4 million per annum. This would have equated to spending of $9.756 million for base rate entities (assuming a corporate tax rate of 27.5%) and $9.195 million for other R&D entities; and
- increase the targeting of the incentive to larger R&D entities (i.e. those with an aggregated annual turnover of $20 million or more) with high levels of R&D intensity, which would have reduced the benefits provided to certain entities and increased the benefit to others. The percentage point premium was proposed to range from 4.5% to 12.5%. This would have resulted in an R&D tax offset ranging from 32% to 42.5% depending on the entity's corporate tax rate and its level of R&D intensity — that is, the amount of R&D expenditure expressed as a proportion of the R&D entity's total expenses.

#### Key insights

The Government's decision to defer the proposed changes to reform the R&D tax incentive means that the existing rules will continue to apply until the end of the 2020–21 income year.

The decision accords with the Joint Professional Bodies' submission to the Government in June 2020 asking for certainty in relation to the R&D incentive. In particular, the submission sought a delay in the start date from 1 July 2019 to **1 July 2021**.The deferral is intended to provide businesses with certainty as they manage the economic effects of the COVID-19 pandemic.

[20] The Bill was introduced into the Senate on 10 February 2020.

[21] A company may not be a base rate entity because its aggregated annual turnover is $50 million or more, in which case it would not be a small R&D entity for the purposes of the R&D tax offset. It may also not be a base rate entity because its *base rate entity passive income* is more than 80% of its assessable income. This would not be common, but it would have resulted in a company that is eligible for the R&D tax offset being able to claim the offset at the rate of 43.5% for 2019–20.

Other countries have also introduced incentives to encourage innovation including concessional tax rates, accelerated deductions and 'patent box' arrangements. This may have been an opportunity to take a broader look at the settings for encouraging R&D and innovation more broadly. Nonetheless, the more generous uplifts for the offset will be most welcome by business.

# International tax

## Various international tax measures

The Government announced a number of measures in the international tax area.

### Modernising and expanding Australia's tax treaty network

The main focus will be on what the Government describes as 'refurbishing' Australia's treaties with key strategic partners. This is likely to mean that the Government will seek to update those treaties in line with the Multilateral Instrument.

*Budget fact sheet: Lower Taxes: Supporting households, driving investment and creating jobs, page 13*

### Updating the list of exchange of information jurisdictions

**START DATE**

1 July 2021

The Government announced that the list of exchange of information countries for managed investment trust (**MIT**) withholding tax purposes will be expanded with effect from 1 July 2021 — most notably including Hong Kong in that list, among others.

*Source: Budget Paper No. 2 page 17*

### Income tax exemptions available to individuals engaged by the IMF and the World Bank

**START DATE**

1 July 2017

The Government announced that it will clarify that workers engaged by the International Monetary Fund (**IMF**) and the World Bank will be entitled to an income tax exemption.

This brings the tax law into line with Australia's obligations under international arrangements.

*Source: Budget Paper No. 2 page 22*

### Strengthening Australia's foreign investment framework

**START DATE**

Funding over 4 years

The Government announced that it will spend $86.3 million over four years to improve the Foreign Investment Review Board (**FIRB**) systems.

This follows on from the announcement in the *July 2020 Economic and Fiscal Update* that the Government would spend $54.1 million over four years to extend the powers of the FIRB to check a greater range of proposed foreign investments.

*Source: Budget Paper No. 2 page 23*

### Key insights

While there are few international announcements in the current Budget, Australia remains part of ongoing talks at the Organisation for Economic Cooperation and Development (**OECD**) to address the taxation of the digital economy. The Government has previously indicated that it is unlikely to enact unilateral measures as some countries have done but rather will work with the international community in developing a multilateral solution.

# Fringe benefits tax

## FBT exemption for skills training of redeployed employees

**START DATE**

2 October 2020

The Government announced that it will provide an exemption from fringe benefits tax (**FBT**) for employer provided retraining and reskilling benefits provided to redundant, or soon to be redundant employees (described as redeployed in the Media Release) where the benefit is not related to their current role.

Currently, FBT is payable[22] if an employer provides training to its employees that is not sufficiently connected to their current employment. By removing FBT, employers will be encouraged to help workers transition to new employment opportunities within or outside their business.

The exemption will not be available for:

- retraining acquired by way of a salary packaging arrangement; or
- training provided through Commonwealth supported places at universities or extend to repayments towards student loans.

The Government will also consult on potential changes to the current arrangements for workers who undertake training at their own expense. The current tax law limits deductions to training related to current employment. This may act as a disincentive for Australian workers to retrain and reskill to support their future employment needs. The Government will also consult on potential changes to the current arrangements to determine whether it should be extended to future employment and skills needs.

*Source: Budget Paper No. 2 page 15*

*Joint Media Release, 2 October 2020, Treasurer and Assistant Treasurer and Minister for Housing*

22 There is currently no exemption for the provision of such training, and the costs if borne by the employee would generally not be deductible.

### Key insights

From 2 October 2020, the Government is exempting employer-provided retraining activities from FBT. This measure is designed to encourage businesses to retrain and redeploy their workers to new roles within the business.

## Reducing the compliance burden of record keeping

**START DATE**

1 April of the FBT year after the date of Royal Assent of the enabling legislation

The Government will provide the Commissioner with the power to allow employers to rely on existing corporate records, rather than employee declarations and other prescribed records, to finalise their fringe benefits tax (**FBT**) returns.

Currently, the FBT legislation prescribes the form for certain records which practically forces employers, and in some cases employees, to create additional records in order to comply with their FBT obligations.

*Source: Budget Paper No. 2 page 15–16*

*Budget fact sheet: Lower Taxes: Supporting households, driving investment and creating jobs, page 14*

### Key insights

The Government is cutting red tape by giving the Commissioner power to allow employers to use existing corporate records, rather than prescribed records, to complete their FBT return.

This measure is designed to reduce the time employers and employees spend on record keeping.

# Retirement and Wealth

## Capital gains tax

### CGT exemption for granny flat arrangements

**START DATE**

1 July following the date of Royal Assent of enabling legislation

The Government has announced that it will provide a targeted capital gains tax (**CGT**) exemption for granny flats where there is a formal agreement in place.

Under the measure, CGT will not apply to the creation, variation or termination of a formal written granny flat arrangement. This will remove the adverse tax consequences for the property owner while providing protection for older parents or people with disabilities.

The CGT exemption will be available only in respect of a granny flat interest within the meaning of s 12A of the Social Security Act 1991. The exemption will not be available for a property that is not the principal home (as defined in s 11A of the Social Security Act 1991) of the taxpayer (for example, a rental property that happens to contain a granny flat).

*Source: Budget Paper No. 2 page 23*

*Joint Media Release, 5 October 2020, Treasurer and Assistant Treasurer and Minister for Housing*

#### Background

##### Tax issue

Under current tax laws, a homeowner may have to pay CGT where there is a formal agreement for a family member to reside in their home — for example, when an older parent lives with their child either in the same dwelling or a separately constructed dwelling.

Interests in granny flats can affect social security entitlements, and those entering into granny flat arrangements are encouraged to document them in writing. In some cases, the tax consequences have been a deterrent to families establishing a formal and legally enforceable family agreement, which leaves no protection of the rights of the older person if there is a breakdown in the agreement. This has led to elder abuse in some cases.

If the older person pays the homeowner rent, this is assessable income for the homeowner, but it also results in a partial loss of the CGT main residence exemption (**MRE**) under s 118-190 of the ITAA 1997.

If the older person pays the homeowner a lump sum (for example, $400,000 to build the granny flat on the understanding that the older person or their estate will receive the funds back when the property is later sold), this results in CGT event D1 happening to the homeowner. This results in a taxable capital gain of $400,000, and the gain cannot be discounted because the rights created under the contractual arrangement have not been held by the homeowner for at least 12 months when the CGT event happened.

The homeowner is at risk of:

- losing part of their CGT MRE when they later sell their home where the older person pays regular rent-type payments under the arrangement;
- being assessed on a capital gain under CGT event D1 where a lump sum is paid to create contractual rights.

### Board of Taxation review

On 29 November 2018, then Assistant Treasurer, Stuart Robert, requested the Board of Taxation (**the Board**) undertake a review of the tax treatment of granny flat arrangements and recommend any potential changes. This review was in response to the Australian Law Reform Commission's 2017 report: Elder Abuse – a National Legal Response, which identified the development of formal and legally enforceable family agreements as a measure to prevent elder abuse.

The Board of Taxation completed its review and provided its report to the Government in November 2019.

The Board found that:

- 'informal' granny flat arrangements, based on concepts of trust and 'natural love and affection' present real risks[23] to the older person residing in the granny flat;
- people contemplating these arrangements should be encouraged to formalise them, by entering into a written and legally enforceable agreement setting out the parties' rights and obligations;
- CGT is a significant obstacle in the way of detailed, considered written agreements.

### Key insights

This is a welcome announcement in a complex area which has caused concerns for the regulator (the ATO) and taxpayers for many years.

The Government advises that, 'the measure will commence as early as 1 July 2021 subject to the passing of legislation'. Accordingly, it is expected that the law will be drafted to commence from 1 July following the enactment enabling legislation. It is a shame that the changes will not be given immediate effect from the date of announcement, as this would provide peace of mind to older Australians and those living with a disability. It would also relieve the homeowner of adverse tax consequences. As a result, this change is likely to encourage these arrangements to be formally documented, which would be expected to help address elder abuse.

The Joint Media Release indicates that CGT will not apply to the creation, variation or termination of a formal written granny flat arrangement, but this would seem to address only one of the two CGT issues. It will be interesting to see whether the law is drafted to also preserve the MRE for the homeowner where they receive regular rent-type payments under the arrangement.

[23] The older person may transfer substantial money or property in return for a mere promise or expectation but there is nothing to show for the transferred assets. If the relationship breaks down, or other unforeseen circumstances arise, the older person can, in the worst case, be left homeless.

One hopes the exemption will be broad enough to cover all of the various arrangements that apply to granny flats because not all are straight forward. Some are paid up front; some are paid over time; and some are paid later once the older parent receives funds such as an inheritance.

This issue has arisen because of CGT event D1. Would giving money to an adult child to improve their main residence to accommodate the elderly parent ordinarily be considered a taxable capital gain in the absence of such specific rules? Most would regard this as a private arrangement. This is another example of overly complex law that leads to unexpected tax outcomes.

# Superannuation

## Your Future, Your Super

**START DATE**

1 July 2021

The Government announced a *Your Future, Your Super* package under which it will make changes to the superannuation system with a view to reducing costs and saving Australians $17.9 billion over 10 years.

Australians are currently paying $30 billion per year in superannuation fees which is expected to grow to around $45 billion by 2034.

The measures:

- prevent the creation of unintended multiple superannuation accounts when employees change jobs;
- give members access to a new interactive online Your Super comparison tool which will encourage funds to compete harder for members' savings;
- impose a requirement that superannuation products meet an annual objective performance test. Those that fail will be required to inform members. Persistently underperforming products will be prevented from taking on new members;
- increase trustee accountability by strengthening their obligations to ensure trustees only act in the best financial interests of members. The Government will also require superannuation funds to provide better information regarding how they manage and spend members' money in advance of Annual Members' Meetings.

*Source: Budget Paper No. 1 page 30*

*Joint Media Release, 6 October 2020, Treasurer and Assistant Minister for Superannuation*

### Key insights

The *Your Future, Your Super* proposals continue the government's non-tax superannuation changes that are designed to improve the super system efficiency, make funds more accountable and super more visible to members

# Indirect Taxation

## GST

### Expanded access to simplified accounting method

The Government announced that it will expand the Commissioner's power to create a simplified accounting method determination for GST purposes to business that have an aggregated annual turnover of $10 million or more and less than $50 million.

**START DATE**

1 July 2021

*Source: Budget Paper No. 2 page 16*

*Joint Media Release, 2 October 2020, Treasurer and Assistant Treasurer and Minister for Housing*

#### Background

Under s 123-5 of the GSTA 1999, the Commissioner may determine to provide certain eligible entities with the choice to use a simplified accounting method (**SAM**) to help work out their net GST amount by estimating the proportion of their sales and purchases of trading stock that are GST-free.

The entity must be either:

- a small business entity[24] — that is, the entity carries on a business and its aggregated annual turnover is less than $10 million; or
- an entity that does not carry on a business and its GST turnover does not exceed the small enterprise turnover threshold of $2 million.

#### Key insights

Currently this choice tends to be utilised by small retailers whereas it would appear that this measure will allow a greater number of entities to use the simplified accounting method in calculating their net GST amount.

[24] Other than because of s 328-110(4) of the ITAA 1997 which concerns entities that determine their aggregated annual turnover for an income year is less than $10 million only at the end of that year.

# Administration

## ATO funding

### Additional funding to address serious and organised crime in the tax and superannuation system

The Government announced that it will provide $15.1 million to the ATO to counteract serious and organised crime in the tax and superannuation systems. This tax integrity measure extends the original announcement made in the 2017–18 Budget by an additional two years to 30 June 2023.

**START DATE**

Extension of current funding arrangement to 30 June 2023

*Source: Budget Paper No. 2 page 13*

#### Background

In the 2017–18 Federal Budget, then Treasurer, Scott Morrison, announced that the Government would provide $28.2 million to the ATO to target serious and organised crime in the tax system. The 2017–18 Budget announcement extended a pre-existing measure, under which the ATO's compliance activities in this area were funded until 30 June 2017, by four years to 30 June 2021.

The announcement in the 2020–21 Budget further extends the measure to 30 June 2023. The funding provided under this measure is intended to enable the ATO to continue its compliance activities targeting serious and organised crime.

#### Key insights

The Government proposes to provide additional funding of $15.1 million to the ATO to counteract serious and organised crime in the tax and superannuation systems.

This announcement extends the measure originally announced in the 2017–18 Budget by two years to 30 June 2023. The funding provided under this measure is intended to enable the ATO to continue its compliance activities targeting serious and organised crime.

# Abbreviations | Glossary

| Term | Explanation |
|---|---|
| 2020–21 Budget | Federal Budget for the 2020–21 income year (or whichever year is referred to) |
| AEDT | Australian Eastern Daylight Time |
| Appropriations[25] | All monies received by the Commonwealth must be paid into the Consolidated Revenue Fund which is established by the Constitution. Funds may not be withdrawn from the Consolidated Revenue Fund without an 'appropriation' by the Parliament. An 'appropriation' is the legal authorisation by the Parliament for the release of monies from the Consolidated Revenue Fund.<br>An appropriation is required before any monies may be spent by the Government.<br>A request by the Government for the release of monies is made by the introduction of a series of Appropriation Bills into the House of Representatives. These Bills are introduced on Budget Night. |
| ATO | Australian Taxation Office |
| Commissioner | Commissioner of Taxation |
| CPI | The Consumer Price Index is a commonly used statistic in the calculation of inflation.<br>The CPI is a fixed weighted price index that relates to household expenditure on retail goods and services and other items such as housing, government charges and consumer credit charges.<br>The CPI measures price movements from a reference base period (currently 1989–90) which is assigned the value 100.0.[26] |
| FBO | Final Budget Outcome (see explanation below) |
| FBT | Fringe benefits tax |
| Forward estimates period | This period is the Budget year (i.e. 2020–21) plus the three following financial years (2021–22 to 2023–24). |

25 Source: Parliament of Australia, The Budget: a quick guide.

26 Source: Parliament of Australia, consumer price index.

| Term | Explanation |
|---|---|
| GDP | Gross domestic product of Australia is the total market value of all goods and services produced within Australia in a given period of time.<br><br>**Real GDP** is adjusted for inflation while **nominal GDP** is unadjusted for inflation.<br><br>The percentage change in real GDP is called economic growth. Economic growth is generally considered to be good when it is positive, i.e. the economy is growing, and bad when it is negative, i.e. the economy is contracting.<br><br>As the average living standard per head of population can only be rising if economic growth exceeds population growth, economists and commentators generally want to see economic growth exceed about 2% per annum.[27] |
| GST | Goods and services tax |
| Joint Bodies | Joint professional bodies |
| MYEFO | Mid-Year Economic and Fiscal Outlook (see explanation below) |
| NANE income | Non-assessable non-exempt income |
| PAYG | Pay As You Go |
| R&D | Research and development |
| Recession | A contracting economy is defined to be in 'recession' if it contracts for two or more consecutive quarters.<br><br>There have been five recessions since 1960: in 1961, 1974–75, 1982–83, 1990–91 and 2020.[27]<br><br>The economy contracted 7% for the June 2020 quarter following the negative 0.3% growth in the March 2020 quarter. |
| Underlying cash balance | The underlying cash balance refers to the surplus or deficit for the financial year, determined on a cash basis. |
| Unemployment rate | The unemployment rate is the percentage of the labour force that is measured as unemployed. The labour force is a measure of the economically active population, i.e. employed people plus unemployed people.<br><br>The Australian Bureau of Statistics (**ABS**) defines a person who is unemployed as one who, during a specified reference period, is not employed for one hour or more, is actively seeking work, and is currently available for work.[28] |

27 Source: Parliament of Australia, gross domestic product.

28 Source: Parliament of Australia, unemployment.

# Legislative references

| Abbreviation | Description |
|---|---|
| FBTA 1986 | *Fringe Benefits Tax Assessment Act 1986* |
| GSTA 1999 | *A New Tax System (Good and Services) Act 1999* |
| ITAA 1936 | *Income Tax Assessment Act 1936* |
| ITAA 1997 | *Income Tax Assessment Act 1997* |
| TAA 1953 | *Taxation Administration Act 1953* |

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