KJ
Accounting & Business Solutions

Federal Budget 2020-21: Key tax measures

Budget Night

Budget Night is the night 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.

However, due to the economic uncertainty 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 2020–21 budget is based on a positive outlook and is aimed at building individual and business confidence. This budget is likely to mainly benefit SMEs and individuals.

The Key Tax Measures

Personal tax cuts: The stage 2 tax cuts are being brought forward 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.

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**) 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.

KJ
Accounting & Business Solutions

Currently legislated rates and thresholds — resident tax payers

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.

Key insights

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.

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.

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.
- 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.

Key insights

It is designed to improve cash flow for qualifying businesses that purchase eligible assets and to encourage new investment to support economic recovery.

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: 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;
- thirdly, the loss-carry back ceases to operate from the end of the 2021–22 income year; and
- finally, the entity is a corporate entity.

The majority of small business are conducted outside a corporate structure, so this measure is not of benefit to all.

Example

In the 2018–19 and 2019–20 income years, XYZ 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.

Fringe benefits tax: from 1 April 2021, those businesses with an aggregated annual turnover of between $10 million and $50 million will be exempt from the 47 per cent FBT on car parking and multiple work-related portable electronic devices (such as phones or laptops) provided to employees

FBT exemption for skills training of redeployed employees: 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 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.

Capital gains tax - CGT exemption for granny flat arrangements: 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.

New wage subsidy – JobMaker: This new subsidy is to encourage the hiring of young unemployed individuals and the creation of new apprenticeships and traineeships.

Eligible employers can claim a JobMaker Hiring Credit from the ATO which will be paid quarterly in arrears.

Some points to note include:

- Employment must commence from 7 October 2020 to 6 October 2021
- Employees aged 16 to 29 — credit of $200 per week
- Employees aged 30 to 35 — credit of $100 per week
- Annual maximum — $10,400 per position
- Employees must work at least 20 hours per week
- Employees must have received JobSeeker Payment Youth Allowance (other) or Parenting Payment for at least 1 out of 2 months prior to hiring

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.

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.

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 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.

Deferment of proposed R&D changes: 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. 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.

Current and proposed R&D tax incentive rates and thresholds

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% Above 2%	8.5% 16.5%	**33.5%** **41.5%**	**38.5%** **46.5%**

Note – This report has been sourced and summarised from the Budget Measures Budget Paper No. 2 2020 – 21 and The Tax Institutes Federal Budget Summary 2020 – 2021 paper.