

5 October 2022

The Honourable Dr Jim Chalmers MP Treasurer

Parliament House Canberra ACT 2600

Dear Treasurer,

2022-23 pre-budget submission

Income tax matters

1.0 Introduction

- 1.1 Tax & Super Australia (TSA) is a not-for-profit member organisation that has assisted tax and superannuation professionals for over 100 years. With a membership and subscriber base of more than 15,000 practitioners, TSA is at the forefront of educating and advocating on behalf of independent tax, superannuation and financial services professionals.
- 1.2 Our members have an ongoing interest in the effective functioning of Australia's tax system and this pre-budget submission is made by TSA on behalf of those interests.
- 1.3 While there are a number of longer-term macro-economic measures that will require a considered policy response in due course (such as broadening the GST base, streamlining the FBT system and simplifying/harmonising the employee/contractor distinction), we have compiled a list of specific income tax issues that we believe require response within the short to medium term.

2.0 Trust distributions and uncertainty around s 100A

- 2.1 The draft guidance material released by the ATO in February 2022 has the potential to disturb distribution practices followed by many thousands of Australian family businesses for decades.
- 2.2 While s 100A may, on its face, apply to circumstances where unclaimed present entitlements are accumulated in a family trust, we consider such an outcome is inconsistent with the mischief the provision was designed to prevent (the insertion of low tax or tax-free beneficiaries). We note these provisions were introduced at the height of the tax avoidance era and before the introduction of Part IVA in 1981.
- 2.3 The decision of Logan J in the *Guardian case* that the ordinary family dealing exception applies unless the arrangement includes features of artificiality is under appeal to the Full Federal Court, with a decision pending.

2.4 Subject to the outcome of the *Guardian* appeal, we submit the government should consider the following options:

1. Repeal s 100A on the basis that Part IVA makes it redundant.
2. Amend s 100A to deem distributions made to members of a family group as defined in s 272-90, Subdiv 272-D, Schedule 2F of the ITAA 1936 as falling within the ordinary family dealing exemption.
3. Ensure that the ATO's updated view of the operation of s 100A is not applied retrospectively.

3.0 Taxation of Trusts

3.1 Aside from the specific s 100A issue highlighted above, the taxation of trusts in accordance with respective provisions contained at Division 6 and Division 6E of the Income Tax Assessment Act 1936 and Section 115C of the Income Tax Assessment Act 1997, has been a particularly difficult and challenging part of the taxation regime for tax professionals, the Australian Taxation Office (ATO) and for taxpayers.

3.2 We consider that these difficulties and challenges in administering the taxation of trusts arises, in general, due to the complexity of interpreting the 'flow through' concepts inherent in the legislative framework (e.g. the concept of present entitlement, the differences in understanding trust law concepts and tax concepts, the economic differences that arise where distributable income does not flow to a beneficiary in receipt of the taxation distribution).

3.3 In light of the foregoing, we recommend that the government re-consider the proposal as raised by Treasury and as provided in its reform paper: *Modernising the Taxation of Trust Income – Options for reform November 2011*.

3.4 In that Paper Treasury proposed three alternative models for reform as follows:

- The Patch Model
- The Proportionate within class model, and
- The Trustee Tax and Deduction Model.

3.5 Whilst each of the foregoing have their merits in respect of the reform of taxation policy, we consider that the proposal contained at Section 8.3 in respect of a 'Trustee Tax and Deduction' model, if adopted, could overcome the many difficulties for tax professionals and taxpayers in administering their compliance obligations under the trust taxation regime.

3.6 We note that the advantages provided by Treasury in respect of the ‘Trustee Tax and Deduction’ model, as proposed, were as follows:

A TAD model has a number of potential benefits as it:

- reduces complexity and compliance costs by avoiding the need to apply detailed trust concepts such as ‘income of the trust estate’ and ‘present entitlement’ in order to determine the tax liabilities of the beneficiaries and trustees of the trust;
- reduces the reliance on individual trust deeds. Currently, the ‘income of a trust estate’ can be as varied as trust deeds themselves;
- defines key concepts and reduces the need to apply trust concepts; and
- reduces the scope for beneficiaries to be taxed on amounts that they are not entitled to under trust law.

3.7 The TAD model was renamed the ‘economic benefits model’ (EBM) and subject to further analysis in Treasury’s *Policy Options paper*, released in October 2012. Since that time there appears to have been little or no progress on the issue.

3.8 We recommend that the government consider the foregoing in relation to the taxation of trusts to improve the taxation and economic outcomes for taxpayers and the improved administrative efficiency of tax professionals.

4.0 Division 7A

4.1 Tax practitioners and their private company clients continue to await progress on simplification reforms to Division 7A *ITAA 1936* first announced by the previous government more than five years ago.

4.2 Changes announced in the 2016-17 budget drew on a number of recommendations from the Board of Taxation’s Post Implementation Review of Division 7A, and included:

- a self-correction mechanism to assist taxpayers to rectify inadvertent breaches of Division 7A promptly.
- appropriate safe harbour rules to provide certainty and simplify compliance for taxpayers.

- simplified rules regarding complying Division 7A loans, including in relation to loan duration and the minimum interest rate.
- a number of technical amendments to improve the integrity and operation of Division 7A and provide increased certainty for taxpayers.

4.3 In the 2018-19 budget, the former government announced two further changes:

- for all unpaid present entitlements to come within the scope of Division 7A.
- a deferral of the start date of the 2016–17 announcements.

4.4 The ongoing delays in the simplification of Division 7A result in increased complexity, compliance costs and uncertainty for tax practitioners and their small to medium business clients. We urge the government to clarify its position, specifically whether, when and how the previously announced changes will proceed.

5.0 Residence rules for individuals

5.1 As part of the May 2021 federal budget, the then government announced that it would adopt the recommendations of the Board of Taxation ('the Board') contained in their December 2019 report '[Reforming Individual Tax Residency Rules – a model for modernisation](#)'. The Board put forward a two-step framework that relies primarily on a 183-day bright line test. For the vast majority of individuals, this test will likely negate the difficulty in interpreting the current application of the residency question.

5.2 The Board of Taxation's proposals represent a significant improvement over the current position, and we therefore encourage the new Government to review the position and enact legislation within the shortest practicable timeframe.

6.0 CGT roll-overs

6.1 The Board of Taxation was requested to identify and evaluate opportunities to rationalise the existing CGT rollovers and associated provisions into a simplified set of rules that have a substantially similar practical effect but are easier to use and interpret. We understand the Board has provided interim written advice to the previous government on 25 March 2021.

6.2 We request the government to release the Board's report and engage with the tax profession about the next steps in this area.

6.3 The question of roll-overs should also facilitate a function in which the entity transferring assets to a transferee entity is not subject to the onerous requirement of also transferring the legal interest and ownership of those assets.

6.4 That is, the roll-over should enable the transferor entity to choose an option under which the legal ownership of assets remains in the existing entity.

- 6.5 The current requirement in which on rollover, the transferor entity transfers the legal title in property held by it, including motor vehicles, lease agreements, employee contracts, etc, can be onerous. In particular, small and medium sized businesses under which a rollover may be contemplated can find the administration of such and the transfer of asset holdings to a new entity costly, and overwhelming, particularly in terms of the time commitment to undertake such a task.
- 6.6 Consistent with other legislation (example Division 6C of the income Tax Assessment Act 1936) under which a public trading trust is required to lodge a company income tax return for the trust, (whilst the assets of the PTT remain held in the name of the PTT for the purposes of legal ownership), the requirement to not transfer the legal title of the asset when a CGT rollover choice is made by a taxpayer, should be an option that may be chosen by that entity.
- 6.7 The outcome of this option, for example, is that a trustee chooses a section 122 A rollover to that of a company entity. The ‘business’ and assets are taxed under the corporate tax regime. The legal title of the assets remain under the trustee’s name.

7.0 Luxury car tax

- 7.1 With the local manufacture of motor vehicles coming to an end some years ago, it is difficult to justify the continued application of the luxury car tax (LCT).
- 7.2 The LCT is, in our submission, a clumsy and arbitrary proxy for luxury which fails to promote vertical or horizontal equity. We do not impose a luxury tax on diamonds, fur coats or yachts, so why tax moderately expensive cars?
- 7.3 Australia’s robust progressive income tax system, coupled with its largely means-tested transfer system, is a much more effective and comprehensive way of redistributing income.
- 7.4 Short of its abolition (or phasing out), the LCT threshold should be significantly increased. The LCT today applies to far more vehicles than it did when it was first introduced. Increasing the threshold to around \$100,000 would mean that it applies to cars that most fair-minded people would regard as luxury vehicles.

8.0 Car depreciation limit

- 8.1 As is the case with the LCT, the car depreciation limit has not kept up with automotive industry changes and today applies to far more vehicles than it did on its introduction. While TSA has no objection in principle to having some sort of cap on business depreciation for cars, we consider the threshold should be raised to somewhere around \$100,000 and more appropriately indexed thereafter.

9.0 GST registration threshold for not for profits

- 9.1 The GST registration threshold for not for profits has been set at \$150,000 for a number of years now. While this is double the registration threshold for ordinary businesses, \$150,000 is a relatively low threshold. Singapore, for example, has a threshold of S\$1 million (AUD 1,070,000).
- 9.2 To avoid NFPs incurring compliance costs by exceeding the current low threshold, it may be time to review the settings and significantly raise the threshold – we would suggest doubling it to \$300,000. This would help charities and other NFPs focus more on pursuing their core mission rather than chasing down relatively trivial GST debits and credits.

10.0 Announced but unenacted measures

- 10.1 The professional bodies have made a number of submissions with regard to announced but unenacted taxation measures. This seems to be a perennial problem in the tax arena and creates uncertainty for practitioners and the ATO alike.
- 10.2 We would urge the government to ensure that sufficient resources are available to Treasury to enable the laws to keep pace with the various announcements made (including drafting resources).

TSA would be happy to constructively engage on any of the issues listed above.

Please feel free to contact the undersigned on 0400 819 698 should you require any further information.

Yours faithfully,



Phillip London | Head of Tax