Key tax implications of Australian budget

The 2012-13 Australian budget was announced on 8 May 2012 and includes proposals to introduce a limited loss carryback, clarify the general anti-avoidance rule, increase the Managed Investment Trust withholding tax rate and eliminate the capital gains tax discount currently available to individual nonresidents.

The various budget announcements are expected to be introduced into the Parliament on a staggered basis. Some measures will be introduced into Parliament quite quickly, while other matters will be the subject of consultation and will not become draft law for some time. The government does not control either House of Parliament, which adds some complexity to the process of getting the measures passed by Parliament. Some of the key announcements are as follows:

Corporate tax

- The government has decided not to proceed with a cut to the corporate tax rate from 30% to 29%. This is projected to save AUD 4.76 billion, and the government has stated that it will focus these savings on other measures, such as the company loss carryback measures.

- The government will allow companies to claim refunds on prior year tax payments through the carryback of losses. As from 1 July 2012, companies will be able to carry back up to AUD 1 million of losses to get a refund for tax paid in the previous year. From 1 July 2013, the AUD 1 million loss carryback will apply for tax paid up to two years earlier. There is no apparent limit on the size of the taxpayer or the economic group that can benefit from these measures. However, the mechanics of how the refund is to work were not set out in the announcement.

- The government had previously announced an amendment (expansion) of the general anti-avoidance rule (Part IVA) with effect from 2 March 2012, and it confirmed its commitment to amend the rule to ensure the provision remains effective against tax avoidance schemes. The proposed amendment is intended to clarify the circumstances in which a taxpayer obtains a “tax benefit” in connection with a scheme, and follows several recent Federal Court decisions that found that the Commissioner of Taxation had incorrectly determined that the anti-avoidance rules should apply to remove the perceived “tax benefits.” A common feature of the cases was that the taxpayers had choices about the manner in which they carried out business transactions, with the choices leading to different tax outcomes.

There is considerable uncertainty about the current operation of Part IVA because of the proposed retroactive nature of the amendment. This uncertainty will be felt most by taxpayers that undertake mergers, disposals, acquisitions and other transactions that may have different tax outcomes depending on how they are carried out. A cautious approach to the tax considerations will be necessary, and it can be expected that the Australian Taxation Office will keep a close eye on major transactions that occur in the period since the announcement was made.

- The government has proposed “more consistent tax treatment for bad debts between related parties irrespective of whether they are members of a tax consolidated group.” Where a debt as between members of a tax consolidated group is bad, the transaction is disregarded due to tax consolidations. It is proposed that where the parties are related but not in the same tax consolidated group, a deduction for bad debts written off will not be available. This could affect group financing activities outside of tax consolidated groups, such as within non-wholly owned groups, stapled groups and involving nonresident debtors. The measure also will ensure that the gain to the debtor will not be subject to tax.

- The government has announced that it will clarify that limited recourse debt includes arrangements where the creditor’s right to recover the debt is effectively limited to the financed asset or security provided. The measure will ensure that tax deductions are not available for capital expenditure on assets that have been financed by limited recourse debt to the extent the taxpayer is not effectively at risk for the expenditure and does not make an economic loss. No further details are available as yet.
• The Tax Breaks for Green Buildings Program, which was announced as part of the 2010 government election commitment, was intended to provide businesses that invest in eligible assets or capital works to improve the energy efficiency of their existing buildings with the ability to apply for a one-off bonus tax deduction of 50% of the cost of these improvements. This program was originally due to start on 1 July 2011, but was then deferred to 1 July 2012. The government has now announced that the program will no longer proceed due to the various incentives provided by the Clean Energy Future package.

Funds

• The Managed Investment Trust (MIT) withholding tax rate will be increased from 7.5% to 15% as from 1 July 2012. The two main categories of income/gain subject to MIT withholding are:
  
o Net rental income, so this will increase the tax rate for property investments into Australia via a MIT structure; and
  
o Gains on the disposal of Taxable Australian Property (TAP), including real property and 10% or greater interests in entities that are Australian land rich.

Other income, such as dividends and interest, fall outside the MIT withholding regime and remain subject to existing dividend/interest withholding tax rules. Gains on the disposal of non-TAP (e.g. shares in non-Australian land-rich entities where a capital election has been made under the MIT rules) are not subject to MIT withholding, so should not be affected by the announcement.

• The government reiterated its commitment to a comprehensive/permanent Investment Manager Regime (IMR) from 1 July 2011; this is directed at hedge funds and is not expected to be of direct benefit to private equity funds.

• Currently, individual nonresidents of Australia who earn taxable Australian capital gains (including through certain funds) are eligible for the capital gains tax (CGT) discount – effectively, half rate taxation. The CGT discount will be removed for gains accruing after 8 May 2012, but remains available for gains accruing before that date where nonresidents choose to obtain a valuation as at that date.

Not announced

• It had been expected that the thin capitalization rules would be tightened, but there was no announcement in the budget. The potential changes mooted included a reduction in the safe harbor debt ratio from 75% of relevant assets to 60% and the removal of the arm’s length debt test. There is still a prospect that the thin capitalization rules will be tightened in due course.

• The budget did not elaborate on the expected timing of the proposed controlled foreign company or foreign accumulation fund reforms. These changes are not expected to be introduced before 1 July 2013.

• Finally, although there were no major new indirect tax measures announced, the government confirmed its increased focus on Goods and Services Tax compliance activities by allocating additional funds to the Australian Taxation Office for the 2014-15 and 2015-16 years.

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