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Via email

17 December 2009

Dear Sir/Madam,

SUBMISSION – TAX LAWS AMENDMENT (TRANSFER OF PROVISIONS) BILL 2009

Taxpayers Australia is pleased to provide a submission to Treasury in response to the Tax Laws Amendment (Transfer of Provisions) Bill 2009.

We welcome the Government's initiative to continue the process of rewriting the income tax law from the 1936 Act to the 1997 Act.

The appended document sets out our views in response to the issues raised.

Should you wish to discuss any aspect of this submission please contact either myself or Andy Nguyen on 1300 657 572.

Yours Faithfully,

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Taxpayers Australia Inc

Tax Laws Amendment
(Transfer of Provisions)
Bill 2009

Submission

17 December 2009

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Head of Taxation and Superannuation



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Contents

Executive Summary	1
Specific Comments	2
Concluding Comments	12

1. Executive Summary

Our submission sets out our comments in relation to the rewrite of the following provisions from the *Income Tax Assessment Act 1936* (ITAA36) to the *Income Tax Assessment Act 1997* (ITAA97) and Taxation Administration Act 1953 (TAA53):

- Part VI – collection and recovery provisions;
- Schedule 2C – forgiveness of commercial debts;
- Schedule 2E – leases of luxury cars;
- Schedule 2G – farm management deposits; and
- Schedule 2J – general insurance.

Given the nature of Taxpayers Australia’s membership base, we have not made specific comments in relation to the rewrite of Schedule 2J - general insurance

In the main, Taxpayers Australia welcomes the rewrite of the above mentioned provisions in order to provide clarity and certainty to taxpayers and to take further steps to rewrite the ITAA36 into the ITAA97.

We encourage the Government to fully complete the transfer of other provisions, with the aim of having one complete Income Tax Assessment Act which is easy to navigate and apply.

Given that the rewrite has been undertaken with no intention to change the interpretation of the law, our comments have been directed to the application of the new provisions and also its relevance.

Where required, we have requested that certain areas be clarified for the benefit of taxpayers and advisers.

To the extent that the provisions are amended as a result of subsequent feedback or in light of any recommendations provided by the forthcoming Henry Review, we welcome the opportunity to comment on any future drafts of the rewritten provisions.

2. Specific comments

2.1 Collection and recovery of income tax

Division 1 of Part IV ITAA36

Security deposits

Section 213 ITAA36 has been rewritten under subdivision 255-D of the TAA53, and requires the taxpayer to provide a security deposit for current and future tax related liabilities where that taxpayer is conducting a temporary business. As noted at para. 2.35, it now extends to all taxes and is therefore, not limited to income taxes.

We question the potential application of these provisions by the Commissioner of Taxation, as in practice, we would envisage that it would be difficult to identify such a business which would require the taxpayer to make an up-front deposit.

Further, given that most businesses would be required to register for GST, PAYG and PAYGW purposes when applying for an Australian Business Number (ABN), we expect that the Commissioner of Taxation no longer need to resort to these provisions.

On this basis, we suggest that either the provision not be replicated or modified such that the operation of the law is streamlined.

Division 8 of Part IV ITAA36

Payment plans

According to the Explanatory Memorandum at para. 2.44, the existing rules under the ITAA36 providing the Commissioner with the power to make payment arrangements for collecting estimated debts will be removed and that similar provisions under the TAA53 would be relied upon in any case.

We envisage that such a provision to include section 255-15 TAA53, which provides that the Commissioner may permit a taxpayer to pay an amount of a "tax related liability" by instalments under an arrangement between the taxpayer and the Commissioner.

A "tax related liability" is defined under section 255-1 TAA53 to be a pecuniary liability to the Commonwealth arising directly under as a taxation law (including a liability the amount of which is not yet due and payable).



Taxpayers Australia Inc
Tax Laws Amendment (Transfer of Provisions) Bill 2009

Arguably, an estimate of a tax liability by the Commissioner would fall within this meaning.

Nonetheless, to provide guidance to taxpayers, we suggest that a comment be inserted in the Explanatory Memorandum directing taxpayers to the actual provisions which may be relied upon under the TAA53 in order for taxpayers to obtain a payment plan.

2.2 Commercial debt forgiveness rules

Application date

According to the Explanatory Memorandum at para. 3.45, the provisions are intended to apply to debts forgiven in the 2010-11 income year and later income years.

The Explanatory Memorandum does not make it clear whether the application date differs where a taxpayer with a substituted accounting period (SAP) has its debt forgiven.

For example, if the taxpayer is an early balancer with a year end of 31 December 2010 (ie. 2010-11 income year) would the rewritten provisions apply for the SAP of that taxpayer. A literal reading of the provisions suggests that an early balancer is expected to apply the rewritten rules for the year ended 31 December 2010.

We suggest that guidance be provided in the Explanatory Memorandum to provide certainty to taxpayers on the timing of the application of the new provisions.

Subdivision 245-A - Debts to which operative rules apply

Treatment of trust as an entity (optional comment)

According to the Explanatory Memorandum at para. 3.13, the current commercial debt forgiveness provisions apply to trustees when the trust estate's debt is forgiven. This provision is not reproduced in the rewritten provisions – rather, as explained in the Explanatory Memorandum, the provisions apply to trusts to the extent that it satisfies the meaning of “entity” under section 960-100 ITAA97

Given that the rewritten provisions refer to the term “you”, to provide clarity to users, we suggest that the Explanatory Memorandum makes reference to the meaning of “you” under section 4-5 ITAA97, which states that the term applies to entities generally.

Accrued but unpaid interest

Under the current provisions in section 245-20 ITAA36, the meaning of “debt” includes accrued interest which has not been paid to be included as part of the original debt and not a separate debt. The rewritten provisions will not replicate this provision.

On this basis, there is no clear guidance as to how the accrued interest should be treated for the purposes of the commercial debt forgiveness provisions.

In other words, should such accrued interest be treated as a separate debt and a net forgiven amount calculated for that debt should it subsequently be forgiven, pursuant to the rewritten provision under section 245-55 ITAA97. Alternatively, are such amounts ignored for the purposes of the commercial debt forgiveness provisions?

In addition, the Explanatory Memorandum at para. 3.12, states the following:

Further, in conflating the time at which the interest accrued with the time at which the original debt was incurred, it can actually distort the value of the forgiven debt

We note that this comment is unclear and does not provide guidance on the tax treatment of accrued interest. We also fail to understand how the value of a debt is “distorted” by the accrued interest.

Taxpayers Australia suggest that a provision be drafted or a comment made in the Explanatory Memorandum stating specifically the tax treatment for unpaid accrued interest if such amounts are not included in the original debt amount and the calculation of the “net forgiven amount”.

Subdivision 245-C – Calculation of gross forgiven amount of debt

Section 245-55(3) ITAA97 – Assumption of liability rule

Section 245-55(1) ITAA97 requires that the value of the debt forgiven be valued at its market value on the assumption that at the time the debt was incurred and when it was forgiven, there is a capacity for the debt to be paid. This is referred to as the “assumption of liability” rule.

Under the current and the rewritten provisions, this rule is ignored to the extent that section 245-55(3) ITAA97 applies.



Taxpayers Australia Inc
Tax Laws Amendment (Transfer of Provisions) Bill 2009

More specifically, section 245-55(3)(a)(ii) ITAA97 requires that the forgiveness of the debt was a “CGT event” involving a “CGT asset” that was “taxable Australian property”.

The recent Full Federal Court case, *Commissioner of Taxation v Tasman Group Services Pty Ltd* [2009] FCAFC 148 considered the application of this rule in light of whether the CGT asset had a “necessary connection with Australia” (the predecessor to “taxable Australian property”).

One of the categories in which a CGT asset has such a connection is an asset which has been used in the carrying on of a business through a “permanent establishment” in Australia. The same category also applies under the meaning of “taxable Australian property” as contained in section 855-15 ITAA97.

In that case, the assumption of liability rule was held by the courts to apply on the basis that the loan provided by a foreign parent company of a wholly owned Australian subsidiary was not carrying on a business in Australia. Rather, the business was carried on by the Australian subsidiary and therefore, the funds lent were not used to carry on that subsidiary’s business in Australia.

To provide guidance in light of this case, we suggest that an example be drafted into the legislation to demonstrate circumstances where the debt, as a CGT asset would be considered to be taxable Australian property.

Subdivision 245-D – Calculation of gross forgiven amount of debt

Section 245-90 agreement

Under the current and rewritten provisions, the taxpayer is allowed to transfer some of the tax effect of the forgiveness to the creditor if both are companies with a common ownership.

Pursuant to section 245-90 under the current and rewritten provisions, this is achieved by the creditor and taxpayer entering into an agreement.

More specifically, if an agreement is made by the taxpayer and the creditor, the creditor would forgo a capital or revenue loss and the taxpayer would have their “net forgiven amount reduced”.

In practice, there is no approved form available to taxpayers so that the parties can put in place an agreement.



Taxpayers Australia Inc
Tax Laws Amendment (Transfer of Provisions) Bill 2009

To simplify the process of having a written agreement in place and the compliance costs in maintaining such records, we suggest that a choice, similar to that in section 103-25 ITAA97 in that the way the taxpayer prepares their tax return is sufficient evidence of the making of that choice.

As a result, the taxpayer will not apply the net forgiven amount in their tax return and the creditor will not recognise the capital or revenue loss in their tax return.

Subdivision 245-G - Record keeping

Strict liability offence

According to the Explanatory Memorandum at para. 3.43, the failure to keep the requisite records is a strict liability offence of 30 penalty units (refer section 245-265 ITAA97). The provisions remove the defence of a reasonable excuse.

Taxpayers Australia believes that the removal of the provisions which allow a reasonable excuse to be unfair to taxpayers where there are extenuating circumstances which may be outside the control of the taxpayer.

For example, the loss of the records by the taxpayer due to fire, flood or natural disaster may be circumstances where it may be unfair to levy a strict liability penalty.

Based on the foregoing, we suggest that the provision which allows a reasonable excuse be reinstated in the re-write of these provisions to provide fairness to taxpayers.

Other comments

Company groups

Under the re-write of the commercial debt forgiveness provisions, subdivision G of Schedule 2C is not reproduced. In broad terms, we understand that the special rules under this subdivision were introduced to enable net forgiven amount to be applied to losses in other group companies.

However, due to the advent of the tax consolidation regime (effective from 1 July 2002), such debt forgiveness within the consolidated group would be ignored for income tax purposes and therefore, there would be no need to apply subdivision G as it current stands.

In maintaining consistency with the tax consolidation provisions and the policy intent, Taxpayers Australia agrees with the exclusion of subdivision G under the rewritten provisions.

2.3 *Luxury car leases*

Application date

According to the Explanatory Memorandum at para. 4.50, the provisions are intended to apply to assessments for the 2010-11 income year and later income years.

The Explanatory Memorandum does not make it clear whether the application date differs where a taxpayer with a substituted accounting period.

For example, if the taxpayer is an early balancer with a year end of 31 December 2010 (ie. 2010-11 income year) would the rewritten provisions apply in respect of that SAP. A literal reading of the provisions suggest that an early balancer is expected to apply the rewritten rules for the year ended 31 December 2010.

We suggest that guidance be provided in the Explanatory Memorandum to provide certainty to taxpayers on the timing of the application of the new provisions.

Subdivision 242-B – Amount to be included in lessor's assessable income

Balancing charge under Division 40 ITAA97

According to the Explanatory Memorandum at para. 4.17, sections 42A-35(2) and (3) ITAA36 which provide a balancing charge for the notional sale of the luxury car, has been removed in the rewrite due to the application of Division 40 ITAA97. Taxpayer's Australia agrees with the treatment.

Currently, section 242-30 provides a note directing to the application of section 40-285 (relating to a balancing charge amount to be included assessable income).

Taxpayers Australia does not believe that such a note provides sufficient information to the user to take into consideration the possible balancing charge from the notional disposal of the luxury car to the lessee.

On this basis, in addition to the note, we suggest that section 242-30 (as a non-operative provision), outline clearly that the lessor refer to Division 40 to determine the balancing charge due to a notional sale under section 242-15 of the rewritten provisions.

Similarly, we suggest that a note also be inserted under section 242-15(1) ITAA97 (rewritten provisions) detailing the application of the balancing charge provisions.

Subdivision 242-C - Deductions allowable to lessee

Accrual amount

Section 242-50 makes reference to the term “accrual amount”, however, without having read section 242-35, the user would find it difficult to determine that this amount is required to be calculated.

On this basis, we suggest that a note be inserted at section 242-50 outlining that the accrual amount is determined in the relevant provision.

Subdivision 242-E – Extension, renewal and final ending of the lease

Lessee stops having right to use car

Section 242-90 deems there to be a notional disposal from the lessee to the lessor where the lessee stops having the right to use the car.

On this basis, the application of Division 40 ITAA97 would ordinarily apply.

The rewritten provision fails to refer to the application of Division 40 ITAA97. On this basis, to provide ease of use, Taxpayers Australia suggests that a non-operative note be inserted after section 242-90(2) outlining the application of the balancing adjustment provisions.

2.4 Farm Management Deposits

Subdivision 392 ITAA97 – Long-term averaging of primary producer’s tax liability

Meaning of taxable primary production income and non-primary production income

Pursuant to @393-10(d) under the rewritten rules, a taxpayer would not be entitled to a deduction for making a farm management deposit if their “taxable non primary production income” for the year is not more than \$65,000.

As noted in the Explanatory Memorandum at para. 5.27, subdivision 393-C of Schedule 2G has not been rewritten because similar rules appear in Subdivision 392-C of the ITAA97 for calculating the averaging adjustment for long-term averaging of primary producer’s tax liability.

However, we understand that the provisions are not identical and the difference in the meaning arises in the definition of “primary production deductions” which is used determining “taxable primary production income”.

Consequently, subsection 392-80(3) ITAA97 was rewritten to exclude apportionable deductions in determining the meaning of “primary production deductions”. Arguably, this meaning is the same as that presently contained under section 393-60(5) ITAA36.

Our concern in relation to changing the meaning of “primary production deduction” and consequently, the meaning of “taxable primary production income” is its implications for the income averaging rules for primary producers.

Para. 5.28 of the Explanatory Memorandum state that the Schedule 2G approach is generally more concessional than Division 392.

This comment appears to suggest that, in excluding “apportionable deductions”, the taxable non-primary production income would decrease (by virtue of the taxable primary production income increasing).

Whilst the change to this definition maintains the status quo, we suggest that broader consideration be given to the impact of this definition change to the income average rules for primary producers and a comment made as to that impact for taxpayers in the Explanatory Memorandum (whether favourable or unfavourable).



Taxpayers Australia Inc
Tax Laws Amendment (Transfer of Provisions) Bill 2009

In addition, we note that the current Division 392 adopts a “method statement” approach in its drafting. If this meaning is maintained, we suggest that this approach in drafting that Division be retained in section 392-80(3) ITAA97 to maintain consistency.

3. Concluding comments

Taxpayers Australia welcomes the rewrite of the provisions in the Tax Laws Amendment (transfer of Provisions) Bill 2009.

In the main, the rewrite satisfies the objectives of bringing these provisions in the ITAA97 and TAA53 (where relevant) and makes the application of these rules easier to navigate and follow.

We welcome the Government’s continual initiative to transfer these provisions with the aim of having one complete Income Tax Assessment Act.