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Mr Matthew Flavel  
Small Business and General Business Tax Break – Consultation  
Business Tax Division  
The Treasury  
Langton Crescent  
PARKES ACT 2600

Dear Mr Flavel,

### **Small Business and General Business Tax Break-Draft Legislation**

As you know, the Australian Equipment Lessors Association (AELA) is the association of equipment financiers and lessors in Australia. Membership includes the major and regional banks, international banks, general financiers, manufacturer financiers and rental companies (list attached). We appreciate the opportunity to comment on the draft legislation, and also the assistance received from Treasury throughout this process; many of the issues raised in our consultations with Treasury have been addressed in the draft legislation and accompanying documents. In general the draft legislation provides a simple and effective framework to stimulate business activity in Australia. However it suffers from a major drawback.

#### **Inability of Lessor to Transfer Entitlement**

The good intention of the tax break will be very significantly undermined by the inability of the lessor to transfer some or all of its allowance entitlement to the lessee. This flexibility could be easily included within the allowance framework, and would not expand the scope of the policy measure. It has been a feature of past investment allowances in Australia.

Under the draft legislation it is generally the lessor who claims the allowance, and the Explanatory Memorandum notes the intention that this would be factored into lease rentals. But if the lessor has insufficient taxable income it will not be able to currently utilise the allowance, and to that extent businesses will not get the incentive of the tax break. Particularly with the increase in the quantum of the tax break from 10% to 30%, the current challenging business environment means that many lessors are currently or potentially in this position. The availability of the allowance to business when utilising lease finance will be substantially impaired by this inability on the part of many lessors.

To some extent this can be mitigated by equipment financiers providing hire purchase and chattel mortgage as an alternative to leasing, where the customer will claim the allowance. However, some financiers provide only leasing, and these and their customers will be at a distinct disadvantage in being unable to utilise financing alternatives. The fleet leasing industry in Australia, which funds around 100,000 new cars annually, is one example in this regard.

The framework for the allowance needs to be designed to cater for the fact that it is a significant permanent tax difference. Many lessors, particularly those with little revenue outside their leasing activities, will struggle to find sufficient taxable income to claim the allowance, and accordingly will be unable to factor it into reduced rentals for their customers. Such outcome has consequences not only for competitive neutrality, but also the availability of finance across the risk spectrum in a market where access to funding is already critically constrained by the global financial crisis.

Lessors unable to utilise the allowance will have no choice but to tell their customers they will not receive the benefit of the tax break, because unlike past investment allowances there is no option for the lessor to transfer the entitlement to the lessee.

In addition, the benefit for small business of the tax break will also be undermined if the lessor is not given this discretion. Small businesses will be denied the allowance for assets between \$1,000 and \$10,000 which they fund by way of lease, as the lessor is not eligible to claim the allowance for assets under \$10,000. Providing discretion to the lessor would overcome this impairment of the measure.

As noted, this discretion has been available for past investment allowance measures. We appreciate that the current allowance is based on Division 40 of the ITAA97, which had not been enacted at the time of previous allowances; we support the approach of building on the Division 40 framework, but suggest there is nothing in this framework which is inconsistent with providing the option for the lessor to transfer some or all of its entitlement. On past occasions the lessor was required to give a statement to the lessee, specifying the amount that was transferred, and the lessee was required to keep this statement for five years. This would not be an onerous burden for lessors or lessees, particularly when contrasted to the alternative of foregoing the allowance and negating the stimulus effect.

### **Timely Announcement Critical**

As a consequence of these issues the leasing market is in a state of hiatus and confusion, aggravated by the fact that the final parameters of the allowance will not be known until the legislation receives Royal Assent. With the 30% allowance applying only from 13 December to 30 June, the dominant period of this window will have elapsed by the time of Royal Assent; this could be as late as May, leaving less than two months for the 30% allowance. Even to the extent that lessors have sufficient taxable income, it is difficult for them to confidently factor the allowance into lease rentals until the legislation passes the Parliament. These issues outlined above could be immediately resolved if the Government announced that lessors will have the discretion to transfer some or all of their entitlement to the lessee; such an outcome would be entirely consistent with the objectives of the allowance in encouraging businesses to invest now in new assets. Ideally such announcement would be made by the Government as soon as possible, and does not need to be accompanied by

legislation; lessors and lessees could then immediately enter into leasing arrangements in the knowledge that the lessee could utilise the benefit of the tax break.

### **Installed Ready for Use**

To qualify for the tax break eligible assets must be installed and ready for use by 30 June 2010 and 31 December 2010 respectively. Our members have noted that lead times for large capital investment projects can take a longer time, and the relatively short timeframes could discourage larger investment projects. We suggest that the 'first use time' (at 41-120)c)(ii)) be extended by 12 months to 'no later than 31 December 2011.

### **Asset to be Used in Australia**

The current wording of Section 41-120 would deny the investment allowance on expenditure made by Australian taxpayers on assets which are used in an Australian business to derive assessable income from the use of depreciable assets wholly or partly outside of Australia. For instance, expenditure on a transport vehicle (for example, a ship) which is manufactured, trialled and commissioned overseas and used in an Australian business partly overseas (for instance voyages to and from Australia) would give rise to assessable income but not be eligible for the investment allowance. Where the expenditure is incurred by an Australian taxpayer and the asset is used in carrying on an Australian business and generates income that is taxable in Australia, there seems no policy basis to disallow the allowance merely because the asset may be used wholly or partly outside of Australia. This is because, whether the asset is used in Australia or wholly/partly offshore, the effect in both instances is to stimulate business activity in Australia. Therefore, we suggest that the measures be amended along the following lines:

#### 41-120 Recognised new investment amount

1. An amount is a *recognised new investment amount* for the income year in relation to the asset if:

(d) at the first use time for the amount:

(i) if the amount is included in the first element of the asset's cost—you start to use the asset in Australia, or have it \*installed ready for use in Australia, or you start to use the asset to derive assessable income for the principal purpose of \*carrying on a \*business;

(ii) if the amount is included in the second element of the asset's cost—you use the asset in Australia, or have had it installed ready for use in Australia or you start to use the asset to derive assessable income, for the principal purpose of carrying on a business; and

### **Pre Contract Deliveries**

Under some commercial arrangements the assets are delivered shortly before the financing arrangements are executed. For instance, a customer may purchase a new motor vehicle to take advantage of a competitive offer available for a very limited time (e.g. 24 hours). Subsequently the customer may seek to arrange finance for the purchase.

We recommend that the following sub-section is inserted in Section 41-120

(2) For the purposes of paragraph (1)(e), disregard any previous use of the asset that was merely for the purposes of reasonable testing or trialling; or use of the asset that took place within 14 days of the \*first use time.

An alternative would be an exemption in respect of any use within 14 days prior to finalisation of financing.

### **Asset Grouping**

Businesses will often incur significant expenditure on separate assets which form part of a single purchase or agreement. The expenditure on the individual assets may be less than the thresholds currently prescribed in Section 41-135 but the total cost is significantly greater. Accordingly we recommend such purchases be considered eligible for the investment allowance, and we recommend new investment threshold Section 41-135 be amended to include:

(c) Acquisitions of multiple functionally similar assets under a single agreement are to be considered a single asset for the purposes of subsection (a) and (b).

#### **Example**

New Technology Pty Ltd operates an IT business. Some of the company's computers are no longer effective in meeting the needs of the business. Accordingly, the company decides to replace these computers and enters into an agreement on 25 June 2009 to buy 30 desktop computers each costing \$900.

The computers are delivered in batches of 5 to the company's offices.

The first delivery arrives 21 July 2009 and the computers are installed ready for use by 28 July 2009. The final delivery arrives 21 January 2010 and the computers are installed ready for use on 28 January 2010. Payment is made 7 days prior to each delivery date. All the computers are eligible for the 30% deduction.

### **Threshold Amounts**

The small business *new investment threshold* is \$1,000. However, where a small business requires finance by way of lease the threshold is effectively \$10,000 as the threshold test is applied to the financier. We suggest that the following minor amendment is made to the draft legislation.

#### 41-135 New investment threshold

The *new investment threshold* for an income year (the *relevant income year*) in relation to an asset means:

(a) \$1000 if you are a \*small business entity (or you are a lessor and the lessee is a \*small business entity) during any of the following income years:

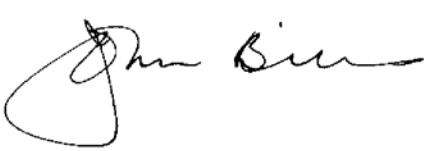
- (i) the income year in which occurs the \*investment time for any \*recognised investment amount for the asset in relation to the relevant income year;
- (ii) the income year in which occurs the \*first use time for any such amount;
- (iii) the relevant income year; or

(b) otherwise—\$10,000.

In order to ensure the lessee is a small business, the lessor will obtain appropriate confirmation from the lessee.

Thank you again for the opportunity to comment on the draft legislation, and please contact me if further input is required.

Yours sincerely

A handwritten signature in black ink, appearing to read "John Bills", is written over a thin red horizontal line.

JOHN BILLS  
**Director**