



**CORPORATE TAX
ASSOCIATION**
of Australia Incorporated

Small Business and General Business Tax Break Submission

Corporate Tax Association of Australia Inc.

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EXECUTIVE SUMMARY

In this submission on the Government's Small Business and General Business Tax Break, the Corporate Tax Association (CTA) would like to comment on certain aspects of the exposure draft and explanatory memorandum.

In announcing that it would fund an investment break for all Australian businesses, the Government indicated that "*this temporary tax break will help Australian businesses boost business investment, bolster economic activity and support Australian jobs*" and added that the Business Tax Break was a key element of the \$42 billion Nation Building and Jobs Plan to support Australian jobs.

The Treasurer's Media Release (No.012) of 3rd February 2009 indicated that incentive is through the provision of a temporary 30 per cent investment allowance to small businesses for eligible capital investments of \$1000 or over, and for other businesses for capital investments of \$10,000 or more. The incentive applies where investment decisions are made before 30 June 2009 and the asset is installed before 30 June 2010.

The Media Release added that a reduced investment allowance of a 10 per cent investment allowance applies to eligible assets acquired from 1 July 2009 to 31 December 2009 where they are installed by 31 December 2010.

In the Media Release relating to the exposure draft and explanatory memorandum (No.018), the Treasurer advised that the Government was "*delivering the Tax Break because it will give businesses a vital incentive to invest in the future with confidence. This, in turn, will stimulate economic activity and support Australian jobs.*"

With the policy objectives of stimulating economic growth and job creation, spending on areas that achieve these objectives is essential. Below are the CTA's comments relating to the draft legislation that we believe will enhance the achievement of the stated objectives through the inclusion of additional assets and a technical correction to the incentive's application to taxpayers with substituted accounting periods. Addressing some concerns around leased assets, extending the period for the 30 percent investment allowance, more clearly defining what constitutes an asset for the purposes of the investment allowance, the adoption of a project basis for certain types of expenditure and addressing concerns about joint venture arrangements are other areas covered in the submission.

The draft legislation does not completely cover all those assets that could be included to maximise the impact of these allowances on economic growth and jobs. In order to maximise the impact of the incentive, all expenditure that satisfies certain basic requirements should, in our submission, be eligible. Primarily, this includes expenditure on assets subject to the provisions of division 43 of the Income Tax Assessment Act 1997 (ITAA97), software and primary production and landcare assets.

Also it is unclear whether expenditure on multiple purchases of the same asset is intended to be included where the cost of each asset is below the threshold limit but, due to multiple purchases, the overall single order exceeds the threshold limit. The incentive should apply to cases where the threshold is reached through multiple purchases of the same asset.

Certain taxpayers with balancing dates other than 30 June may be disadvantaged due to earlier cut off dates. The legislation should be redrafted to reflect hard close dates and should not be based on the year of income concept.

Taxpayers leasing assets may in some circumstances fail to fully benefit from the incentive. The legislation should be amended to allow leasing companies the option of passing the benefit to lessees.

Given delays due to long lead times in acquiring some assets, the dates relating to the 30 percent investment allowance should, in our view, be further extended. Otherwise the incentive will be of limited practical benefit to large companies considering major projects.

To avoid uncertainty, the definition of an asset should be clarified for the purposes of eligibility for the investment allowance.

Some taxpayers may not benefit from the incentive when investing large amounts on items such as fit-outs. The adoption of a project basis for the determining the eligibility of certain expenditure for the investment allowance would ensure that these types of investment will also be eligible for the incentive.

The application of the threshold test to joint venture arrangements also requires clarification.



INTRODUCTION

The CTA was formed in 1989 to represent the taxation interests of Australia's largest companies. The Association's current membership is about 125 companies across all sectors of the economy.

Over the years the CTA's focus has been on both the development and administration of Australia's tax laws. Our aim is to help bring about a fair and efficient business tax system that promotes economic growth and job creation.

Our member companies support taxation laws that are effective in achieving their underlying policy objectives without creating unintended consequences, laws that are certain in their application and do not involve unnecessary compliance costs.

The CTA participates across a wide range of consultative bodies, involving both Treasury and the Australian Taxation Office.

COMMENTS ON THE SMALL BUSINESS AND GENERAL BUSINESS TAX BREAK

EXTENSION OF TIME FOR 30 PERCENT INVESTMENT ALLOWANCE

Given that it is the 30% investment allowance that is of real commercial benefit, we believe the timeframes governing eligibility for the 30% investment allowance as outlined in the draft legislation will not allow sufficient time for business to action most major investment decisions and thus benefit from the uplifted investment allowance percentage. By the time investment decisions can be run through the approval process, contracts are negotiated and entered into and projects can be built or major assets delivered, too much time will have passed to meet the 30 June 2010 deadline.

We note that the proposed term of this incarnation of the investment allowance is rather briefer than that of its predecessors. That seems counterintuitive, given the evident severity of the current crisis.

We consider that a lengthier investment allowance period is warranted, particularly having regard to the long lead-times for major projects. Accordingly, we propose that the 30% investment allowance be extended by at least a further twelve months and probably longer if the economic crisis does not pass soon.

ASSETS THAT SHOULD BE ELIGIBLE FOR THE INVESTMENT ALLOWANCE

In order to maximise the impact of the incentive, eligibility should not be restricted just to expenditure on assets that entitle a taxpayer to a deduction under section 40-25 of ITAA97. Encouragement should likewise be given to spending on other assets as part of the clear policy to quickly stimulate the economy and create jobs.

Specifically, expenditure on capital works, software, primary production and landcare assets and bulk purchases of the same asset should also be eligible for the incentive. Expenditure in these areas clearly is intended to develop businesses, which can be expected to stimulate economic growth.

CAPITAL WORKS

Expenditure on capital works that is subject to the provisions of division 43 of ITAA97 should also be eligible for the incentive. Encouragement to make investment decisions on infrastructure and other capital projects can be expected to result in increased business investment on such projects. Expenditure on capital projects, in addition to promoting business growth, leads to significant job creation in Australia, thereby contributing strongly towards achieving the desired objectives of the incentive.

SOFTWARE

Software and development of software plays an integral part in the improvement and efficiency of large businesses in particular. Encouraging expenditure on software and software development will stimulate the productivity of business.

DIVISION 40F AND 40G ASSETS

While business expenditure incurred in respect of depreciating assets employed in primary production and landcare operations enjoy certain tax timing benefits, they are not eligible for the incentive as the draft provisions are currently framed. These important sectors are also impacted by the economic downturn and would be equally likely to respond to a permanent tax incentive such as the investment allowance as any other sector of the economy.

WHAT CONSTITUTES AN ASSET

The draft legislation uses the term asset but this may not provide sufficient detail for taxpayers to assess whether or not acquisitions are eligible for the investment allowance.

The draft legislation relies on taxpayers to identify the assets that are eligible using tests established for defining depreciating assets.

In cases where the asset is made up of different parts and components, a functionality test is used to identify the depreciating asset. The use of this test often involves taxpayers having to exercise judgement. This may raise issues in assessing eligibility as against the threshold for investment allowance purposes.

For example, a major item of expenditure in many retail and logistics businesses is the cost of shelving and racking. The cost of shelving and racking for a business may be substantially more than the \$10,000 threshold, but the cost of each unit of shelving that could arguably function on its own may not exceed the threshold.

The legislation should allow for these costs to be based on the total expenditure required for a business (or part of a business) to function in determining the eligibility for the investment allowance as well as the quantum of the investment allowance available. The functionality of the shelving “asset” in the above example is only achieved through viewing the shelves for a particular store or warehouse as one single asset.

FIT-OUTS

In many businesses, significant expenditure is incurred on refurbishment of premises and fit-outs of new premises. In many cases, some of the costs associated with the individual components of the refurbishment or fit-out will not exceed the investment

threshold, even though the overall cost of the project will be well in excess of the threshold amount.

An extension of the eligibility tests to include these types of expenditure would, in our submission, be consistent with the Government's aim of providing an incentive for significant investment by business.

A provision in the draft legislation to include expenditure on eligible projects such as the above would cater for this type of expenditure.

BULK PURCHASES

As a related matter, many businesses typically place orders for the bulk purchase of identical assets that have an individual cost that is below the threshold, but where the total amount spent is well in excess of \$10,000. For those businesses the order represents a single investment and, in our submission, should be treated as such for investment allowance purposes.

UMBRELLA AGREEMENTS

It is common in some industries for companies to enter into umbrella agreements, which set out the terms and conditions for subsequent asset acquisitions. Such agreements specify technical specifications, prices, documentation and delivery details, but do not in themselves commit the company to purchase any of the items described in the agreement. The contractual rights or obligations do not arise until the company actually places an order.

Umbrella agreements are convenient because they enable companies to place repeat orders over an extended period without each time having to negotiate terms and conditions. For the sake of clarity we consider it would be helpful if at least the Explanatory Memorandum clarified (perhaps by way of an example) that the investment time would be regarded as the date on which the company become legally and commercially committed to acquire the relevant asset by taking the final step of placing a purchase order.

Importantly, such agreements would work in the same way when the investment allowance comes to an end, so that post investment allowance asset acquisitions could not be "grandfathered" in this fashion.

SUBSTITUTED ACCOUNTING PERIODS

The Treasurer advised that a 30 per cent investment allowance is to apply where investment decisions are made before 30 June 2009 and the asset is installed before 30 June 2010.

If the 30 per cent investment allowance does not apply, a 10 per cent investment allowance applies in cases where the decision is made before 31 December 2009 and the asset is installed by 31 December 2010.

Currently the draft legislation correctly provides that the incentive applies where the investment decision is made before 30 June 2009 for the 30 per cent investment allowance or before 31 December 2009 for the 10 per cent investment allowance.

However, the draft legislation refers to income years for the termination of the incentive rather than hard dates. Although 30 June is the balance date for most Australian taxpayers, many large corporates have substituted accounting periods and have closing balance dates other than 30 June. For example an early balancer may have a balance date of 31 December 2009 in lieu of 30 June 2010. These taxpayers would be disadvantaged if the incentive provisions terminate based on the closure of years of income. In this example, any incentive that terminates in the 2009-10 income year will terminate on 31 December 2009 for an early balancing taxpayer and 30 June 2010 for a June balancing taxpayer.

OPTION TO PASS BENEFITS TO LESSEES

Depending on the type of lease arrangement in place, the investment allowance will be available to either the lessor or the lessee. Most HP or similar arrangements, where the lessee can reasonably be expected to assume ownership of the asset upon the expiry of the lease, would result in the lessee being entitled to claim the incentive. On the other hand, finance and operating leases would generally result in the lessor being entitled to the investment allowance.

While it is expected that the entitlement to the investment allowance would generally be reflected in the lease charge, there may be cases where the lessor cannot utilise the benefit, at least not for some time – for example, where the lessor is in a tax loss position.

To overcome this, and to ensure the incentive has its intended effect, it is suggested that the provisions should allow the lessor to have the option of passing the benefit on to the lessee. This could be achieved through an agreement between the lessor and lessee as to which party is entitled to claim the investment allowance.

JOINT VENTURES

The draft legislation states that the “new investment threshold” in relation to an asset acquired will be \$10,000 (where the entity involved is not regarded as a small business). The draft legislation and explanatory materials do not, however, make reference to the application of this threshold in circumstances where the assets are acquired by an unincorporated joint venture (JV) that is not regarded as a partnership for tax purposes.

An example is where a JV acquires an asset valued at \$30,000. The JV has three participants who held a 60%, 30% and 10% interest, meaning that the participants have an \$18,000, \$9,000 and \$3,000 interest in the asset respectively, i.e. only the first participant has an asset with a value exceeding \$10,000.

As the cost of the entire asset exceeds the threshold, we contend that all participants should be entitled to the investment allowance, based on their interest in that asset.

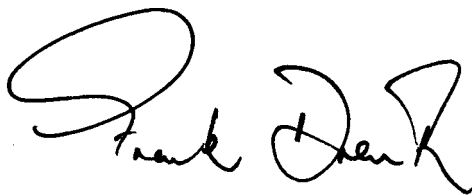
The draft legislation should therefore include a provision allowing each JV participant to claim the investment allowance where the overall cost of the asset exceeds the threshold but the interest held by a JV participant in the asset is less than the threshold.

CONCLUSION

We very much appreciate this opportunity to comment on the draft legislation prior to its introduction into the Parliament. We hope our comments will assist in improving the final Bill so that it helps achieves the Government's broader aims of stimulating the Australian economy.

If you would like to clarify any of the issues raised in this submission please do not hesitate to contact the undersigned.

Yours Faithfully,



(Frank Drenth)

Executive Director