

1985

THE PARLIAMENT OF THE COMMONWEALTH OF AUSTRALIA
HOUSE OF REPRESENTATIVES

TAXATION LAWS AMENDMENT BILL (NO.2) 1985

INCOME TAX (INDIVIDUALS) BILL 1985

INCOME TAX (COMPANIES, CORPORATE UNIT
TRUSTS AND SUPERANNUATION FUNDS)
BILL 1985

MEDICARE LEVY BILL 1985

EXPLANATORY MEMORANDUM

PART A

(Circulated by authority of the Treasurer,
the Hon. P.J. Keating, M.P.)

FOREWORD

Part A of this memorandum contains explanations designed to provide a broad guide to the main Bill that has been introduced to give effect to a number of taxation measures foreshadowed in the 1985-86 Budget and in earlier announcements. Also included is a brief explanation of accompanying Bills that declare and impose rates of income tax and Medicare levy for 1985-86.

Part B of the memorandum, to be issued shortly, will contain a clause by clause explanation of the Bills.

GENERAL OUTLINETaxation Laws Amendment Bill (No.2) 1985

This Bill will amend -

the Income Tax Assessment Act 1936 -

- .. to effectively treat as loan arrangements certain non-leveraged finance leases (and similar arrangements) by governments and tax-exempt government authorities (proposal announced at 5:00pm Eastern Standard Time on 15 May 1984) and by residents or non-residents who are not subject to Australian tax on income derived from the use outside Australia of the leased property (proposal announced at 5:00pm Eastern Summer Time on 16 December 1984);
- .. to introduce statutory investment rules so that income tax concessions applicable to the income of, and contributions to, employer-sponsored superannuation funds will be conditional upon - under the basic rule - not more than 10% of the fund's assets (measured at cost) being invested with the employer or an associate of the employer (proposal announced on 11 March 1985);
- .. to increase from \$1,200 to \$1,500 the annual deduction limit for contributions to qualifying superannuation funds by self-employed persons and employees not covered by employer-sponsored superannuation schemes (1985-86 Budget announcement);
- .. to increase from \$50,000 to \$55,000 the maximum amount of the "post-June 1983" component of lump sum termination payments that is subject to tax at a rate of not more than 15% where made to a taxpayer aged 55 or more (1985-86 Budget announcement);
- .. to abolish, for the year of income that commenced on 1 July 1985 and subsequent years of income, the general concessional expenditure rebate (proposal announced on 17 July 1985);
- .. to provide a medical and hospital expense rebate at the standard rate of tax - presently 30 per cent - for net expenditure (which presently qualifies for the general

concessional rebate) in excess of \$1,000 incurred by taxpayers on their own or their dependants' behalf with effect from the year of income that commenced on 1 July 1985 (proposal announced on 17 July 1985);

- .. to exempt from tax the income of animal racing clubs for the 1985-86 and subsequent years of income (1985-86 Budget announcement);
- .. to allow, with effect from 1 July 1985, a deduction for expenses incurred by candidates in seeking election to local governments or the Australian Capital Territory House of Assembly, subject to an upper limit of \$1,000 per election (1985-86 Budget announcement);
- .. to increase from \$75 to \$220 for married (legally or de facto) taxpayers and from \$50 to \$170 for other taxpayers the existing rebates of tax (and the income levels above which they shade out) available for taxpayers wholly or mainly dependent on social security unemployment, sickness or special benefits (1985-86 Budget announcement);
- .. to allow income tax deductions for gifts to the Australian Academy of the Humanities and the Royal Australian and New Zealand College of Psychiatrists (1985-86 Budget announcement);
- .. to provide the method of calculating provisional tax for the 1985-86 income year.

. the Taxation Administration Act 1953 -

- .. to provide for the conduct of investigations in the Australian Capital Territory by or for State and Northern Territory revenue authorities, and to permit Commonwealth taxation information to be provided to State and Territory revenue authorities for the purposes of the administration of their revenue laws (proposal announced on 20 December 1983); and

. the Taxation Administration Act and various other Commonwealth taxation laws -

- .. to extend the operation of the secrecy provisions of taxation laws to persons who, although not appointed or employed by the Commonwealth, perform services for the Commonwealth.

Income Tax (Individuals) Bill 1985

This Bill will -

- . formally impose tax payable for the 1985-86 financial year by individuals, and by trustees generally, at the rates declared by the Income Tax (Rates) Act 1982; and
- . formally impose provisional tax for the 1985-86 year of income.

Income Tax (Companies, Corporate Unit Trusts and Superannuation Funds) Bill 1985

This Bill will declare and impose the rates of tax payable for 1985-86 by companies and registered organizations, by trustees of corporate unit trusts, superannuation funds and ineligible approved deposit funds, and by trustees in respect of trust income of non-resident company beneficiaries of trust estates.

Medicare Levy Bill 1985

This Bill will -

- . declare and impose the basic rate of levy of 1 per cent for 1985-86 and, until the Parliament otherwise provides, for 1986-87;
- . exempt from levy individuals with taxable incomes of \$7,526 or less and families and sole parents with family income of \$12,504 or less; the family or sole parent threshold to be raised by a further \$1,530 for each dependent child or student; and
- . reduce the levy otherwise payable by veterans, war widows, Defence Force personnel, holders on a non-income tested basis of pensioner health benefits cards, health benefits cards and health care cards, and other "prescribed persons" who are exempt from the levy for part of a year, or who are required to pay levy because they have dependants eligible for Medicare benefits.

FINANCIAL IMPACTTaxation Laws Amendment Bill (No.2) 1985

The potential saving to the revenue arising from the introduction of the finance leasing measures is estimated to be in excess of \$100m for 1985-86 and even larger amounts for subsequent years.

The introduction of the statutory investment rules for employer-sponsored superannuation funds should have no effect on the revenue.

The estimated cost of increasing from \$1,200 to \$1,500 the maximum deduction for superannuation contributions by self-employed persons and "unsupported" employees is nil in 1985-86, \$14m in 1986-87, and \$10m in 1987-88.

The estimated cost of increasing from \$50,000 to \$55,000 the upper limit of lump sum termination payments taxed at a maximum rate of 15% is \$0.5m in 1985-86, rising to \$8m per annum in future when payments are wholly attributable to the post-June 1983 period.

The proposed abolition of the concessional expenditure rebate will result in a revenue gain of \$15m in 1985-86 and \$80m in a full year.

Provision of a medical and hospital expense rebate will have a negligible revenue effect in 1985-86, but a full year cost of \$20m.

The estimated cost of exempting the income of animal racing clubs is nil in 1985-86 and \$1m in a full year.

The estimated cost of allowing a deduction of up to \$1000 per election for expenses incurred by taxpayers in seeking election to local government or the Australian Capital Territory House of Assembly is nil in 1985-86 and \$2m in a full year.

The estimated cost of increasing the rebate of tax available to taxpayers in receipt of social security unemployment, sickness or special benefits is nil in 1985-86 and \$9m in a full year.

The revenue cost of extending the income tax gift provisions to admit the Australian Academy of the Humanities and the Royal Australian and New Zealand College of Psychiatrists is estimated at nil for 1985-86 and less than \$200,000 for a full year.

The Commonwealth/State and Territory co-operation measures will require some commitment of Australian Taxation Office resources. However, reciprocal State and Territory co-operation has the potential to yield revenue for the Commonwealth and offset administration costs.

The proposed amendments of the taxation secrecy provisions to bring within their scope persons who are not actually appointed or employed by, but perform duties for, the Commonwealth are of an administrative nature and will have no revenue consequences.

Medicare Levy Bill 1985

The revenue gain from removing the ceiling on the Medicare levy payable by individuals and married couples is estimated at \$7m in 1985-86 and \$12m in a full year. The estimated cost of increasing the low income thresholds is \$10m in 1985-86 and \$15m in a full year.

MAIN FEATURES

The main features of the Bills are as follows:

Taxation Laws Amendment Bill (No.2) 1985Non-leveraged finance leasing and other similar arrangements (Clause 27)

By amendments proposed by this Bill, income tax deductions in respect of the cost of, or capital expenditure incurred on, property that is the subject of certain non-leveraged finance leases or similar arrangements, other than deductions for interest on moneys borrowed to fund the acquisition or capital expenditure, will not be allowable to the owner of that property. Instead, the lease (or similar arrangement) will be treated as though it were a loan by the owner to enable the lessee or user to acquire the leased property and the lease payments will be treated as repayments of loan principal and payments of interest.

Whether an arrangement is one to which the amendments apply - broadly, an arrangement under which all, or substantially all, the risks and benefits associated with the ownership of the property that is the subject of the arrangement are transferred to the lessee or user of the property - will be determined by reference to a number of specified tests. Such tests include whether the user guarantees to the owner an amount equal to the residual value of the property at the expiration of the period of the arrangement, whether the user has a right to purchase the property, whether the period of the arrangement is equal to 75% or more of the property's effective life and whether payments under the arrangement equal, or exceed, 90% of the lesser of the property's cost price or depreciated value at the commencement of the arrangement.

Except in certain specific circumstances, where an arrangement satisfying the tests (a qualifying arrangement) exists, relevant deductions will be denied if the use of the property, or the effective control of its use, is in the hands of either -

- a government or a tax-exempt government authority and the arrangement was entered into after 5:00pm on 15 May 1984 (the time at which the proposal in relation to relevant arrangements by the particular entities was announced); or

a person who uses the property outside Australia for the purpose of producing income which is exempt from tax in Australia and the arrangement was entered into after 5:00pm on 16 December 1984 (the time at which the proposal in relation to relevant arrangements by such persons was announced).

The relevant deductions to be denied under the proposed amendments are investment allowance and depreciation deductions and the special capital expenditure deductions available in relation to general and petroleum mining operations, timber operations and the transport of certain minerals, and for the cost of certain income-producing buildings.

In treating the arrangement as a loan, the payments to the owner of the property will, for the purpose of calculating the owner's taxable income, be broken into a non-assessable "principal" component and an assessable "interest" component. The interest component will be calculated, on the basis of actuarial methods, on the amount of principal outstanding at the commencement of each payment period. The loan principal at the commencement of the arrangement will be taken to be the lesser of the cost and the depreciated value of the property at that time, with the loan period being equated to the period of the arrangement. The loan principal will be reduced throughout the term of the arrangement by the amount of the non-assessable principal component of any payment. At the expiration of the arrangement period, the value of the property for income tax purposes will be the amount of the original deemed loan principal reduced by the total of the principal components of payments.

Statutory investment rules for employer-sponsored superannuation funds

(Clauses 16, 17, 19 to 26 and 34)

The Bill will give effect to the proposal announced on 11 March 1985 to introduce statutory rules to limit the level of investment (including loans) by an employer-sponsored superannuation fund with the sponsoring employer. The consequences of non-compliance with the new rules (that will first apply for the 1985-86 year of income) will be that the investment income of the fund is taxed at the rate of 30% and that employer and employee contributions are not deductible for income tax purposes.

The basic rule will require that no more than 10% of an employer-sponsored superannuation fund's assets (measured at cost) be invested with the sponsoring employer or an associate of the employer. A transitional rule, that will apply up to and including the 1994-95 income year, will require that, for funds in existence at 11 March 1985, investments with the sponsoring employer or an associate be limited to the greater of -

- (a) 10% of the fund's assets; and
- (b) the level of investment as at 11 March 1985.

For 1995-96 and subsequent income years, the basic 10% investment rule will apply to all employer-sponsored superannuation funds.

The rules will not apply in respect of life assurance policies held by superannuation funds covering employees of the life office concerned.

Safeguarding provisions will operate to prevent circumvention of the rules by methods such as the use of intermediaries, reciprocal loans by the funds of separate employers and the direct or indirect use of fund assets as security for loans from third parties. In addition, funds that as at 11 March 1985 would - because employer investments exceeded 70% of assets - have failed to satisfy the previously applicable requirement that they hold at least 30% of assets in public securities (including at least 20% in Commonwealth securities - the 30/20 rule) will not satisfy the transitional rule until the level of investment with the employer is equal to, or less than, 70% of the cost of all the fund's assets as at 11 March 1985.

Special provisions will operate to prevent retrospective application of the rules in a case where a superannuation fund's 1985-86 year of income commenced before 11 March 1985, and to ensure that the rules do not apply in certain specified circumstances where their application would be unreasonable.

Deductions for certain superannuation contributions
(Clause 17)

The Bill will give effect to the proposal announced in the 1985-86 Budget to increase the maximum deduction available for superannuation contributions by self-employed persons and employees who are not supported by an employer-sponsored superannuation scheme. That maximum will be increased from \$1200 to \$1500 per annum in respect of contributions made during the 1985-86 income year and subsequent income years.

Rebate of tax in respect of eligible termination payments
(Clause 31)

Another 1985-86 Budget proposal to which the Bill will give effect is to increase from \$50,000 to \$55,000 the upper limit on the "post-June 1983" component of lump sum superannuation and kindred payments that is taxed at a maximum rate of 15%.

At present, this concessional rate applies to the first \$50,000 of the component of a lump sum termination payment that relates to service after 30 June 1983, where the recipient is aged 55 or more. The revised maximum of \$55,000 will apply to such payments made during the 1985-86 or subsequent income years. If a taxpayer has already benefited from the concessional rate of tax in relation to payments made in earlier years, but not all of the existing \$50,000 threshold has been used up, further payments will be eligible for concessional treatment until the new \$55,000 threshold is extinguished. If the existing threshold has been used up in earlier years, subsequent payments up to \$5,000 will qualify for concessional treatment.

Abolition of the general concessional expenditure rebate and its replacement with a medical expenses rebate
(Clauses 15, 28 and 29)

The Bill will implement the proposal announced on 17 July 1985 to abolish, with effect from the year of income that commenced on 1 July 1985, the income tax general concessional expenditure rebate and to provide a medical and hospital expense rebate at the standard rate of tax - currently 30 per cent - for net expenditure in excess of \$1,000 incurred by taxpayers on their own or their dependants' behalf. The items to be treated as rebatable amounts for purposes of the new medical expense rebate are identical to those items which are currently rebatable medical expenses.

Under existing arrangements, where self-education expenditure falls within the terms of the general deduction provisions and also qualifies as a rebatable amount for purposes of the general concessional expenditure rebate, the first \$250 of such expenditure incurred by a taxpayer in an income year is absorbed by the concessional expenditure rebate provisions, leaving the general deduction provisions applicable only to the balance of such expenditure. With the proposed abolition of the concessional expenditure rebate the first \$250 of relevant self-education expenses will continue to remain outside the scope of the general deduction provisions.

Exemption of income of animal racing clubs
(Clause 11)

The Bill will, as announced in the 1985-86 Budget, exempt from tax the income derived by a society, association or club which is established for the encouragement or promotion of animal races, and which is not carried on for the purposes of profit or gain to individual members.

The proposed exemption will apply in respect of income of animal racing clubs for the 1985-86 and subsequent years of income.

Local government election expenses
(Clause 13)

The Bill will give effect to the Budget proposal to allow a deduction of up to \$1,000 per election for expenses incurred by taxpayers in seeking election to local governments or the Australian Capital Territory House of Assembly. The deduction is to be available for successful as well as unsuccessful candidates and will apply for expenses incurred in the 1985-86 and subsequent income years.

The expenditure incurred by a taxpayer in contesting an election will be allowable as a deduction in the year of income in which it is incurred, subject to the \$1,000 limit per election. Where some or all of the expenditure allowed or allowable as a deduction is reimbursed to the taxpayer, or paid on his or her behalf, the amount so reimbursed or paid will be included in the taxpayer's assessable income in the year of income in which it is reimbursed or paid.

Where expenditure in relation to a particular election is incurred over more than one income year, the \$1,000 limit will be applied in a year of income by limiting the deduction for expenditure on the election in that year to the amount (if any) by which \$1,000 exceeds the deduction or the sum of the deductions allowed or allowable to the taxpayer in the preceding year or years of income. Any reimbursement, or payment on behalf of the taxpayer, of expenditure on the election included in the taxpayer's assessable income in a preceding year of income will reduce the deduction or deductions taken to have been allowed or allowable in the preceding year or years in making the above calculation.

Also, where a taxpayer incurs election expenses some or all of which are not allowable in a year of income because of the \$1,000 limit, then any reimbursement or payment on the taxpayer's behalf of expenses in respect of that election, in that or a subsequent year of income, will only be included in the taxpayer's assessable income to the extent that the reimbursement or payment (or the sum of the amounts) exceeds the expenditure not allowable as a deduction.

Rebate in respect of certain pensions, etc.
(Clause 30)

This Bill will give effect to the Budget proposal to increase the maximum rebates of tax, and increase the income levels above which the rebates shade-out, for

taxpayers in receipt of social security unemployment, sickness or special benefits. For married (including de facto married) taxpayers the maximum rebate will be increased from \$75 to \$220 and will shade-out at the rate of 12.5 cents for each dollar of taxable income in excess of \$8,795 (\$7,989 in 1984-85). For other taxpayers the maximum rebate will increase from \$50 to \$170 and will shade-out at the rate of 12.5 cents for each dollar of taxable income in excess of \$5,275 (\$4,783 in 1984-85). No rebate will be available at taxable incomes in excess of \$10,555 for married taxpayers and \$6,635 for others. The new rebates will apply in respect of the 1985-86 and subsequent years of income.

Gifts

(Clause 14)

The Bill will give effect to a 1985-86 Budget proposal by extending those provisions of the income tax law that authorise deductions for gifts of the value of \$2 or more made to specified organisations to include the Australian Academy of the Humanities and the Royal Australian and New Zealand College of Psychiatrists. Gifts made to those organisations after 20 August 1985 will qualify for deduction.

Provisional tax for 1985-86 year of income

(Clause 35)

Provisional tax for the 1985-86 year of income is to be calculated, basically, by applying 1985-86 rates of tax and Medicare levy to 1984-85 taxable incomes as increased by 11 per cent. Apart from the exception outlined below, to the extent that rebates and credits are allowed in 1984-85 income tax assessments, they generally will be taken into account in calculating the 1985-86 provisional tax.

The concessional expenditure rebate allowed to a taxpayer in 1984-85 will not be taken into account in the calculation. This rebate is to be removed with effect from the commencement of the 1985-86 income year - see notes on clause 28.

Commonwealth/State and Territory co-operation measures

(Clauses 45 to 48)

The Bill will amend the Taxation Administration Act to allow the Commissioner of Taxation, on request, to authorise a Commonwealth, State or Northern Territory taxation officer to conduct an investigation in the Australian Capital Territory for the purposes of a State or Northern Territory taxation law. An officer so authorised is to have rights similar to those a Commonwealth officer has for Commonwealth taxation purposes - namely, the right

to reasonable access to documents and the right to obtain information and evidence. Where a State or Northern Territory taxation officer undertakes an investigation in the Australian Capital Territory, that officer will be subject to the obligation to observe secrecy in respect of any information obtained.

The Bill will also amend the Taxation Administration Act to authorise the Commissioner to provide information (including copies of documents) obtained under any Commonwealth taxation law to a State, Northern Territory or Australian Capital Territory taxation officer if such an officer is authorised by law to provide similar information to the Commissioner. This general authorisation will replace the separate authorisations (that are, as a consequence, being omitted) in the various Commonwealth taxation laws. At the same time, it will provide uniformity as to the taxation authorities to whom Commonwealth taxation information may be communicated and as to the obligation on recipients of such information not to disclose the information.

For the purposes of these co-operation measures, the Bill will provide an exception to the general rule of evidentiary law that a document is not admissible as evidence in a court unless it is the original document. This statutory exception will apply where, for the purposes of proceedings in relation to a Commonwealth taxation law, a document is obtained, or a copy is made of or an extract is taken from a document, pursuant to a taxation law of the Commonwealth, a State, the Northern Territory or the Australian Capital Territory. In these circumstances, a copy of or an extract from the original document is to be admissible as evidence as if it were the original document, provided that a Commonwealth, State or Territory taxation officer, as is appropriate, has certified the copy or extract to be a true copy of or extract from the original document. The exception will not apply in respect of proceedings for an offence against a Commonwealth taxation law if there is any doubt as to whether the copy or extract is a true copy or extract, or in respect of any other proceedings if it is proved that the copy or extract is not a true copy or extract.

Officers to observe secrecy

(Clauses 4, 6, 8, 10, 38, 40, 42, 44, 50, 52 and 54)

The various taxation laws administered by the Commissioner of Taxation contain secrecy provisions that prohibit the disclosure by officers, except in a limited number of specified circumstances, of information about the affairs of other persons that may be acquired in the course of the officers' duties. For that purpose, an officer is generally defined in the relevant provisions as a person who has been appointed or employed by the Commonwealth. As a result, other persons (such as officers from another

country) who are performing duties for the Australian Taxation Office, but who are neither employed nor appointed by the Commonwealth, are generally not bound by the taxation secrecy provisions.

The secrecy provisions of the income tax law were amended last year to remedy this defect. This Bill will similarly amend the secrecy provisions of the various other taxation laws.

Income Tax (Individuals) Bill 1985

The rates of tax payable for individuals for 1985-86 and, until the Parliament otherwise provides, for 1986-87 by individuals and trustees generally, as declared by the Income Tax (Rates) Act 1982, will be formally imposed by this Bill. It will also formally impose provisional tax for 1985-86.

Income Tax (Companies, Corporate Unit Trusts and Superannuation Funds) Bill 1985

The rates of tax payable for 1985-86 by companies, by registered organizations, by trustees of corporate unit trusts, ineligible approved deposit funds and superannuation funds, and by trustees in respect of trust income of non-resident company beneficiaries, will be declared and imposed by this Bill.

The rates are generally the same as those for 1984-85, but the Bill also imposes a rate of tax of 30 per cent on the investment income of superannuation funds to which section 121CC, which is proposed to be included in the Income Tax Assessment Act 1936 by the accompanying Taxation Laws Amendment Bill (No.2) 1985, applies.

Medicare Levy Bill 1985

The Medicare levy will, by this Bill, be payable on taxable incomes for 1985-86 and, until the Parliament otherwise provides, for 1986-87. Main features of the levy arrangements contained in the Bill are -

- . the basic rate of levy will be 1 per cent of the taxable income of the individual or trustee (clause 6);
- . no levy will be payable by -
 - .. a person whose taxable income does not exceed \$7,526 (clause 7); or
 - .. a married (including de facto) couple where the sum of the couple's taxable incomes does not exceed \$12,504 or by a sole parent where his or her taxable income does not exceed

\$12,504. For each dependent child or student maintained by a married couple or sole parent, the threshold for payment of the levy is to be increased by \$1,530 (clause 8);

relief from levy will also be provided for -

.. veterans, war widows, Defence Force personnel, holders on a non-income tested basis of pensioner health benefits cards, health benefits cards and health care cards, and other "prescribed persons" under existing provisions of Part VIIB of the Income Tax Assessment Act 1936, who are exempt from the levy for part of a year, or who are required to pay levy because they have dependants eligible for Medicare benefits (clause 9).

The Bill does not place a limit on the amount of levy payable by an individual or a married couple.

The provisions of Part VIIB of the Income Tax Assessment Act 1936 concerning, amongst other things, liability to the levy, exemptions for certain trustees and prescribed persons and the definition of prescribed persons, remain unchanged.