

Deloitte.

Federal Budget Brief 2008

Safe and sound



A deft balancing act

The Rudd Government's debut budget is a deft balancing act, perched on a platform of global economic uncertainty.

The Government has demonstrated it is a prudent economic manager while launching major nation-building initiatives and measures to assist working families.

Business will welcome the strong economic discipline.

The numbers look impressive: A \$21.7 billion surplus, well-exceeding the promised 1.5% of GDP.

The budget is built on realistic macroeconomic forecasts – a modest 2.75% growth for 2008-09, inflation at 3.25% by the end of the financial year, and unemployment rising from 4.2 to 4.75% in the same period.

A fiscally conservative budget for uncertain times.

The razor gang's sweep through public expenditure sends a loud and clear message of conservative economic management. Cuts of \$7.3 billion eclipse new expenditure of \$5.3 billion, again exceeding market expectations.

There is a convergence of views held by the Government and the Reserve Bank. This budget does as much as possible to give business the confidence to plan in an environment of global uncertainty.

The budget reflects a down payment on the Government's productivity agenda.

We have to remember that there are a number of major reviews in the wings on collection and use of public monies. Future funds have been stashed away to address business's major objectives of infrastructure, skills and education, and health. The Rudd Government now needs to show that it can deliver.



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A comprehensive review of the tax system

One of the areas that will test whether the Government can deliver is the proposed comprehensive review of Australia's tax system. The review follows the recent 2020 Summit, which suggested a comprehensive review of state and Federal taxes to consider measures to harmonise and simplify taxes, reduce inefficient taxes, ensure a progressive system and address the negative interaction with the welfare system.

The review will examine and make recommendations to create a tax structure that will position Australia to deal with the demographic, social, economic and environmental challenges of the 21st century and enhance Australia's economic and social outcomes. This tax review is a priority for corporate Australia because of the increase in tax paid by business at all levels of government.

The review will encompass Australian commonwealth and state taxes, except GST, and interactions with the transfer system, and will consider:

- the balance between taxation of the returns from work, investment and savings, consumption and the role for environmental taxes
- further improvements to the tax and transfer system facing individuals, families and retirees
- the taxation of consumption and property and other taxes
- simplifying the tax system, including the interactions between Federal, state and local government taxes
- interrelationships between the elements of the tax system, as well as the proposed emission trading system.

The review will be conducted in several stages with an initial discussion paper to be released by the end of July 2008 and a final report provided to Treasury by the end of 2009.

Although there have been numerous tax reform initiatives in the past, this is the first time that Federal, state and local taxes have been part of a single comprehensive review. We hope that the interaction issues, some of which result in additional compliance costs, are addressed and resolved as part of this review.



Personal income tax cuts

Tax cuts announced during the 2007 election campaign have been delivered - but top marginal rate cut deferred until 2010-11

From 1 July 2008, the 30% threshold will increase from \$30,001 to \$34,001, the 40% threshold from \$75,001 to \$80,001 with the biggest jump in the 45% threshold, from \$150,001 to \$180,001. From 1 July 2009, there will be further increases in the 30% threshold – to \$35,001 – the 40% marginal tax rate will be reduced to 38%. There will also be additional increases in the 30% threshold and the 38% marginal tax rate will be reduced further from 1 July 2010. The previously budgeted reductions in the top marginal rate for taxpayers with incomes over \$180,000 have been deferred until after 2010-11, with a resulting saving of \$5.3 billion over the forward estimates period. The changes are detailed in the table below:

Current tax threshold income range (\$)	Tax rate %	New thresholds from 1 July 2008 income range (\$)	Tax rate %	New thresholds from 1 July 2009 income range (\$)	Tax rate %	New thresholds from 1 July 2010 income range (\$)	Tax rate %
0 – 6,000	0	0 – 6,000	0	0 – 6,000	0	0 – 6,000	0
6,001 – 30,000	15	6,001 – 34,000	15	6,001 – 35,000	15	6,001 – 37,000	15
30,001 – 75,000	30	34,001 – 80,000	30	35,001 – 80,000	30	37,001 – 80,000	30
75,001 – 150,000	40	80,001 – 180,000	40	80,001 – 180,000	38	80,001 – 180,000	37
150,000+	45	180,000+	45	180,000+	45	180,000+	45

The Government has also set an 'aspirational' tax goal over six years for a personal income tax system with a reduced number of rates - from four to three – set at 15%, 30% and 40%.

Low-income tax offset

From 1 July 2008, the low-income tax offset will be increased to \$1,200 (currently \$750) and will begin to phase out from \$30,000. Taxpayers eligible for the full low income tax offset will not pay tax until their annual income exceeds \$14,000 (up from the current \$11,000). From 1 July 2009, there will be a further increase of the low-income tax offset to \$1,350 (increasing the effective tax-free threshold to \$15,000), and from 1 July 2010, the offset will again increase to \$1,500 (increasing the effective tax free threshold to \$16,000).

Medicare levy

Significant changes to the Medicare levy surcharge were also confirmed. From 1 July 2008, the threshold after which the levy is applied will be doubled to \$100,000 for singles and increased to \$150,000 for families (previously \$100,000).

From 1 July 2007, the Medicare levy low-income threshold will be increased to \$17,309 (currently \$16,740) for individuals, and \$29,207 (currently \$28,247) for families, with the additional amount of threshold for each dependent child or student increasing to \$2,682 (currently \$2,594). These changes reflect the movements in CPI for the year.



Changes to means testing

Changes have been announced to the means testing of government support payments, including support payments for the pension, family assistance, superannuation co-contributions and financial and retirement savings assistance. The definition of income that is used for the purpose of means-testing will be expanded to include non-wage remuneration and losses from discretionary activities. Specifically, salary sacrifice contributions to superannuation, reportable fringe benefits, net financial investment losses, and net rental property losses will be included. Essentially, the increase in items considered as income will reduce the number of individuals who will qualify for the payments.

Employee share scheme changes

The Government has proposed two legislative changes to the taxation treatment of shares or rights acquired under an employee share scheme to improve the integrity of the tax law.

The first change is to the election requirements for taxpayers who wish to pay tax on the market value at grant of qualifying rights and shares granted under employee share plans.

Employers will see reduced administration costs associated with employee share trusts

The law currently requires taxpayers who elect to pay tax at grant to include the market value of the right or share in their tax return for that year. However, the law currently provides discretion for the Commissioner to allow late elections that, if approved, allow taxpayers to change their choice in a later year after they have observed the market conditions. The benefit to taxpayers in making an election to be taxed on the value of the right or share at grant is that any further growth in value is taxed under the capital gains tax provisions and, where the share or right is held for at least 12 months prior to disposal, only half of any further gain is subject to tax.

The Government proposes to change the election procedures so that a taxpayer who wishes to elect to be taxed at grant must include the value of the discount at grant in the tax return for that year (where it exceeds the \$1,000 exemption available for certain qualifying exemption plans). Taxpayers who do not include an amount in their income tax returns in the year the share or right is granted will be taken to have chosen to be taxed under the deferred option (whereby the discount is typically taxed at exercise of an option or lifting of restrictions on shares, although it may be at an earlier time such as at termination of employment). A taxpayer will therefore need to decide, before filing their tax return for the year of grant, whether they want to be taxed upfront or defer the tax until a later date. They will not be able to go back and amend a prior filed return to get the benefit of the capital gains tax concession.

The second change is in connection with a potential double taxation issue on delivery of shares through employee share trusts.

Until last night, it was possible for the individual employee and the trustee of the employee share trust both to have a tax event on the individual becoming entitled to a share under their employer's equity incentive plans. The double taxation arose as a result of an exemption not applying where an individual receives a share from the employee share trust that was received through exercising a right to acquire the share previously granted by their employer.

We anticipate the proposed amendment should provide certainty about the tax treatment of trustees of employee share trusts when administering the delivery of shares to participants who were previously granted rights. This will be a relief to current employers who provide performance-based reward in the form of equity and who purchase shares on market to avoid diluting shareholder interest.

This amendment to employee share trusts along with other changes made in recent years should now make these vehicles more attractive for employers in Australia.

Scrip for scrip arrangements

The budget announcement on scrip transactions will provide the market with greater certainty about the scrip-for-scrip rules. The previous Government made a number of announcements in October 2007 that created uncertainty about these transactions. In summary, the announcements meant that all scrip arrangements would be denied a market-value cost base uplift. This failed to take into account the reason for providing a market-value uplift for legitimate scrip transactions. Essentially, the market-value uplift ensured that double taxation did not occur on the same economic gain by both the acquiring entity and the shareholders of the takeover entity.

Measures will now only apply to arrangements after last night's budget

The Rudd Government has moved to calm the market by providing a more targeted integrity measure. Deloitte has been critically involved in a number of very detailed submissions to the Government and Treasury, and is working with Treasury on refining the proposed measures. It is pleasing that the majority of these submissions have been taken into account in the announcement made by the Government.

The proposed changes will now only apply where the scrip transaction is more in the nature of a 'restructure' than a genuine 'takeover'. The Government has sought to make this distinction by proposing a new 20% market-value test. Under the test, an arrangement will be taken to be a restructure if the market value of the net assets of the acquiring entity immediately before the arrangement is less than 20% of the market value of its net assets immediately after the arrangement is completed. For example, if Aco has \$20 of assets, and acquires Bco, which has \$80 of assets, the 20% market-value test would be satisfied as the net assets before the takeover (\$20) would be at least 20% of the net assets of Aco after the takeover (\$100). Where the arrangement is taken to be a takeover, market-value cost bases will not be denied (as long as the existing integrity rules are satisfied).

Where the arrangement is taken to be a restructure, the cost base of the shares in the target entity will be worked out with regard to the total cost base of the target entity's assets less its liabilities, rather than the market value of its shares. In the case of a partial rollover that is a restructure, (i.e. where the consideration for the acquisition of the target entity's shares is partly cash), the Government will allow a market-value cost base for the shares to the extent of the cash consideration.

Acquiring entities will have the choice of whether to access the cost base step-up instead of providing the target entity's shareholders with scrip-for-scrip rollover. This might be attractive for a company that is acquiring a target company with a shareholder base that cannot readily take advantage of the benefits of scrip-for-scrip rollover, such as those with a large non-resident shareholder base. As a simplification measure, the Government has indicated that the acquiring entity will be able to make this election without having first to determine whether the transaction satisfies the criteria to be classified as a restructure.

We note that some issues still need to be ironed out. For example, the announcement is silent about the means by which the market value of a company will be determined. We are pleased to see that the Government is adopting a pragmatic approach to this issue by indicating that they would consider accepting proxies for market value, such as the quoted price of shares on a stock exchange.

There is also a technical issue about the timing of when the acquiring entity needs to be valued for the purpose of the 20% market-value test. The announcement refers to valuations that need to be performed before and after an arrangement. Depending on the definition of 'arrangement', this may or may not take into account certain events that occur before the completion of the arrangement. For example, if Aco announces a takeover of Bco, but completes the transaction over a six-month period, there may be issues about when Aco needs to be valued both before and after the arrangement, which may affect the 20% calculation.

The announcement is also silent on whether the Government will allow an acquiring entity the flexibility to adopt the 'stick method', (i.e. the retention of the target entity's tax cost for its assets) rather than being required to conduct a full blown tax consolidation calculation. The use of the stick method would not only provide taxpayers with a reduction in compliance costs, but would ensure that goodwill would not unduly affect the tax cost setting process under the tax consolidation provisions.

A welcome change in position is the Government's announcement that these measures will now only apply to arrangements either announced to the Australian Stock Exchange, in the case of a listed company, or to shareholders, in the case of an unlisted company, after 7:30pm EST on 13 May 2008 rather than the date of the original announcement late last year. Uncertainty may also arise for certain transactions where there are delays in introducing these measures. Accordingly, it will be important for the Government to commit to introducing this into Parliament as soon as possible.

Managed funds

Distributions from managed investment trusts to non-resident investors

The withholding tax rate on distributions from Australian-managed investment trusts (MIT) to non-resident investors will be reduced from the current non-final rate of 30% to a final rate of 7.5% over three years.

The new withholding tax regime will apply to fund payments made by Australian MITs to foreign residents. Fund payments will generally be calculated as the net income of the MIT, disregarding dividends, interest, royalties, foreign-sourced income and capital gains or losses from CGT assets that are not taxable Australian property. It will cover fund payments made directly by MITs as well as distributions through intermediaries (including custodians).

As an integrity measure, the reduced withholding provisions will only apply to foreign investors who are resident in a country with which Australia has effective exchange of information (EOI) arrangements that cover tax matters. The EOI jurisdictions will be specified in regulations and may include countries with which Australia has double tax agreements and certain other countries with which Australia has concluded tax information exchange arrangements (TIEAs), although we will need to wait for the regulations to confirm this.

The rate reduction will be phased in over three years:

- a 22.5% non-final withholding tax for fund payments for the first income year after the enabling legislation receives Royal Assent (2008/09 income year)
- a 15% final withholding tax for fund payments in the second income year (2009/10 income year)
- a 7.5% final withholding tax for fund payments of the third and later years (2010/11 and following income years).

Withholding tax on taxable distributions from listed property trusts and other managed investment schemes reduced from 30% to 7.5% over the next three years.

As a transitional measure for the first year, investors resident in EOI jurisdictions will be eligible to claim deductions for expenses relating to fund payments. Investors resident in non-EOI jurisdictions will be subject to a 30% final withholding tax, effective for fund payments for the first income year in which the enabling legislation receives Royal Assent.

As the withholding will become a final tax (with the exception of the first year), foreign investors will not be required to lodge an Australian tax return for distributions received from the MIT from the 2009 year onwards. Foreign investors in non-MIT funds will continue to be subject to the existing provisions of Division 6 of the 1936 Income Tax Assessment Act.

The new provisions are likely to be modelled on the existing withholding tax provisions for MITs, and it will be interesting to see whether an issue will arise in relation to fund payments which is currently an issue with Australian-sourced discount capital gains - whether the withholding tax applies to the actual gain or the discount gain.

The reduction in withholding tax on taxable distributions from listed property trusts and other managed investment schemes from 30% to 7.5% over the next three years is very welcome. It shows the Federal Government has followed through on one of its promises to the property industry last year. The cut will make the level of tax on income from investment into Australian property through a listed or wholesale trust by a non-resident investor very competitive compared with other major economies such as US and UK. It will also lift the burden of filing Australian tax returns from many non-resident investors.

The change will be a mixed blessing for more sophisticated investors. By making the withholding a final tax (15% in 2009-2010 and 7.5% from 2010-2011 onwards) with no ability to claim a refund, some investors who utilise leveraged holding entities to make their property investments may find their effective tax rate has in fact increased even though the headline rate has reduced. The Treasurer has softened the blow by allowing such investors time to restructure to prevent this change from affecting their net return.

Australia as a regional financial hub

The Government's commitment to establishing Australia as a regional financial hub is welcome.

While the proposed 7.5% tax rate for foreign residents investing in Australian property trusts will be good for the commercial and rural property sectors, the Government should consider other measures to enhance Australia's position as a regional financial hub. These measures could include tax incentives for fund managers and their employees, clarity on the taxation of sovereign wealth investment, measures to facilitate the IPO of foreign companies in Australia, and special economic zones for true international fund management activities or offshore banking type concessions for such activities.

The ultimate measure of success will be if fund managers move to Australia from established centres like Singapore and Hong Kong as a result of these measures.

Changes to the eligible investment rules

Eligible investment rules modified to reduce compliance costs and uncertainty about the operation of Division 6C for managed funds, particularly property trusts

The Government has stated that they will modify the eligible investment rules to reduce compliance costs and uncertainty about the operation of Division 6C for managed funds, particularly property trusts.

The purpose of Division 6C is to tax trusts as companies when they behave in the same way as a trading company, but the current rules are based on a narrow set of criteria that has not kept up with the pace of change. Given the devastating result of a trust failing the current tests, we are pleased that Treasury appears to be offering more latitude to managed funds by updating the current regime. There is an opportunity for Australia to lead the world in providing a flexible set of rules to promote innovation, and we look forward to amendments to the tax system that allow Australia's REIT industry to realise its full potential.



In the Budget, the Government reiterated their previous comments that they will clarify the scope and meaning of investment in land for the purposes of deriving rent, as well as introduce a 25% allowance for non-rental income from investments in land (excluding capital gains). They also intend to expand the range of financial instruments that managed funds may invest in or trade.

Deloitte has previously lodged submissions that raise concerns about the redefinition of 'rent', in particular that it may narrow rather than widen its scope and so reduce the number of trusts eligible for the exclusion where their activities are limited to investments in land primarily for rent.

The Government intends these measures to have effect from the date of Royal Assent of the amending legislation. The application date is therefore uncertain.

Finance-related items

The Government intends to reintroduce the Taxation of Financial Arrangements Stages 3 and 4 measures, with mandatory effect for income years commencing on or after 1 July 2009. The elective start date of 1 July 2008 contained in the Tax Laws Amendment (Taxation of Financial Arrangements) Bill 2007 will no longer apply.

Deloitte welcomes the confirmation of this initiative and the extension of time to allow taxpayers to consider and implement appropriate systems and procedures to cater for the complex rules.

The legislation is expected to be introduced in spring 2008. Deloitte anticipates that taxpayers will take some time to absorb the changes, given the already voluminous state of the previous Bill and the extensive issues that have been raised by industry.

Re-introduction of the TOFA measures with effect on or after 1 July 2009

We note that the previously-introduced Bill did not contain important interaction rules such as the tax consolidation interactions. We hope that such measures will be included when the Bill is reintroduced.

The Government has also indicated that it will introduce measures to facilitate the characterisation of Upper Tier 2 and similar capital instruments issued by certain institutions, such as authorised deposit-taking institutions (ADIs) that are banks, as debt under the debt/equity rules. Current debt/equity transitional arrangements will be extended to 1 July 2008 to ensure that the law preceding the debt/equity tax rules continues to apply for Upper Tier 2 instruments.

The Government has not decided, however, whether or not to proceed with the previous Government's announcement of new regulations to ensure that 'solvency clauses' do not preclude certain term subordinated notes from being debt for tax purposes. These clauses allow the issuer to defer payment if the payment would cause insolvency, and are commonly found in Lower Tier 2 term subordinated notes issued by ADIs.

Tax measures announced but not enacted

Numerous measures were announced by the previous Government but were not enacted prior to the election of the Rudd Government in November last year. The Government has, therefore, sought to eliminate uncertainty about the status of these tax measures by indicating which measures will or will not be introduced, and the expected timeframes for their introduction and application.

Of the 57 measures that were announced but not enacted, the Government has decided to proceed with 34 and not to proceed with three, but is undecided about the remaining 20. The Government has undertaken to state its position on these remaining 20 measures as soon as possible.

Consolidation

A number of modifications that were intended to clarify the operation of the consolidation rules and improve interactions with other parts of the law were previously announced. The Government has indicated that it will proceed on the basis of the prior Government's announcements.

A critical issue that has been highlighted to the previous and current Governments has been the different application dates proposed for different measures. For certain measures, this may have a detrimental effect on taxpayers that have either:

- applied the law appropriately based on the current provisions and who may be adversely affected by a retrospective legislative change
- applied the law in a manner consistent with what was perceived to be the policy intent and who may be affected by a prospective legislative change.

The Government has recognised this issue and proposed an ongoing consultation process during the development of the legislation, which we hope will address the application dates and the need for appropriate transitional rules and possibly also include a review of some of the proposed measures. It is expected that legislation implementing these measures will be introduced in the winter or spring sittings 2008.

Foreign currency amendments

The Government will proceed with amendments to the foreign currency provisions designed to extend compliance cost-saving measures and ensure that the provisions operate as intended. These amendments were announced by the previous Government on 4 August 2004, and the proposed application date of 1 July 2003 has been retained. Legislation implementing these amendments is expected to be introduced in spring 2008. We note that the ATO has released guidance allowing taxpayers to rely on these proposed measures despite the fact that they have not been enacted.

Private rulings requiring valuations

A number of provisions in the income tax laws, such as the consolidation and thin capitalisation rules, may require valuations to be made. The Government has, therefore, agreed to consult on draft regulations for valuations obtained for a private ruling. These regulations will assist the Commissioner in accessing valuation services for taxpayers who have requested a private ruling involving the value of any thing affecting their tax obligations.

Draft regulations and explanatory materials released by the Government indicate that the regulations will give effect to a legislative power of the Commissioner to charge the applicant of a private ruling an amount in accordance with the regulations for the valuer making or reviewing the valuation. These regulations are expected to be introduced in the second half of 2008.

Simplified imputation system

The Government will finalise the implementation of the simplified imputation system, which commenced on 1 July 2002. The main outstanding amendment is the redrafting of the franking credit trading rules (the 45/90 day holding period and related payment rules). The Government's press release does not specify a commencement date for the franking credit trading rules, but legislation is not expected to be introduced before 2009.

Company loss recoupment rules

Three changes to improve the operation of the company loss recoupment rules will be implemented. The first change is ensuring that companies do not fail the continuity of ownership test because they have multiple classes of shares on issue, or have special dividend or capital return distribution arrangements. Clarification of the meaning of 'voting power' in the context of the continuity of ownership test where a company's shares have different voting rights in relation to different matters is the second proposed change. The third change will ensure that the entry history rule in the consolidation regime is disregarded when applying the same business test. These changes will apply from 1 July 2002, except for the second change, which will apply from 1 July 2007. It is not expected that legislation will be introduced before 2009.

Thin capitalisation rules and AIFRS

Changes to the thin capitalisation rules to address some of the adverse affects of the adoption of Australian equivalents to International Financial Reporting Standards (AIFRS) were announced by the previous Minister for Revenue and Assistant Treasurer on 12 September 2007. In recognition of this, the previous Government put in place a transitional period during which entities may elect to use either AIFRS or AGAAP to make thin capitalisation calculations. The transitional period expires on 31 December 2008.

The Treasurer and the Assistant Treasurer announced on 13 May 2008 that the Rudd Government has decided to proceed with this measure and adjust the recognition and valuation of assets, liabilities and equity capital under the thin capitalisation rules following the adoption of AIFRS. Legislation is expected to be introduced in winter 2008.

Sovereign immunity

The previous Government announced in November 2005 that legislation would be introduced to clarify the current practice of exempting foreign governments and their investment bodies from interest and dividend withholding taxes. This is one of the measures on which the Government has yet to make a decision.

Corporate residency

In response to the recommendations of the Review of International Tax Arrangements, the previous Government announced in May 2003 that the company residence rules will be amended so that companies that are residents under domestic income tax law, but are non-residents for the purposes of a tax treaty, are treated as non-resident for all purposes of the income tax law. This is another measure on which the Government has yet to make a decision.

Tax treaties

Legislation to give force of law to the revised treaties with Japan and South Africa is expected to be introduced in winter 2008 and spring 2008 respectively.

Small to medium-sized enterprises

Family trusts

The family trust election measures were put in place in 1995-96. Essentially the measures allow discretionary trusts to access revenue losses where a family trust election was made. The election meant that the discretionary trust could only distribute amounts of income and capital to members of the family group of a nominated test individual. Most family trusts operating in Australia have lodged family trust elections limiting the beneficiaries to whom they can distribute. Distributions outside the family group are subject to family trust distributions tax.

In 2007, the previous Government extended the family group of all family trusts that have made family trust elections to include lineal descendants of a nephew, niece or child of the nominated individual or the individual's spouse. These amendments were made due to the unintended outcomes that occurred where distributions were made to family members who were not included in the definition.

The Rudd Government intends to reverse this amendment with effect from 1 July 2008. As a result, trusts that have lodged a family trust election will only be able to distribute to the children and grandchildren of the nominated individual and the children of the individual's siblings. This limitation will have a number of consequences. Firstly, it makes the choice of the nominated individual a critical one, which is likely to cause great distress to families trying to nominate one sibling over another. Secondly, income from assets accumulated in old family trusts cannot pass through to great-grandchildren without the additional tax impost of family trust distributions tax. Finally, the limitation to grandchildren may shorten the life of the trust and family groups may choose to wind up the trust and pay the tax if they wish to pass on benefits beyond the restricted family group.



The Government will also prevent family trusts from making a one-off variation to the nominated individual specified in the family trust election, other than for marriage breakdowns. This change will also have effect from 1 July 2008.

Small business CGT concessions

Some technical corrections will be made to the small business CGT concessions. Under current law, taxpayers relying on the \$2 million turnover test cannot access the small business CGT concessions where the relevant asset was owned by one entity but was used by a related entity that carried on a business. For partnerships, the small business entity test requires the taxpayer making the capital gain to be a partner of the partnership, and for the asset to be an asset of the partnership. From a policy perspective it was difficult to reconcile why the rules should apply differently depending on whether a taxpayer qualified for the concessions under the \$6 million net asset value test or the \$2 million turnover test.

The Government has announced it will extend the CGT small business concessions to small business entities where a taxpayer owns an asset used by a related entity carrying on a business, and for partners owning a CGT asset used in the partnership business. This proposal was foreshadowed by the previous Government and is proposed to have effect from the 2007/08 income year.

Fringe benefits tax

Rules about salary-packaged items tightened



The Budget included a number of measures to tighten the rules about items offered as part of salary packages:

- eligible work-related items such as laptop computers, electronic diaries, computer software, PDAs and protective clothing will only be exempt from FBT if they are provided for work purposes. Amendments to the legislation are likely to introduce additional substantiation requirements to document that the items are being used for business purposes. The exemption will also be limited to one item of each type per employee per year. The list of exempt work-related items will be clarified to deal with advances in technology
- the exemption for property consumed on an employer's business premises will be amended to specifically exclude items obtained through salary sacrifice meal card type arrangements. Existing balances on meal cards will remain eligible for exemption provided that they are used by 31 March 2009.

The otherwise deductible rule will be amended where a benefit is provided to an employee and an associate in relation to a jointly-held investment asset. The rule will no longer apply to reduce the taxable value of the employee's associate's share of expenses related to the jointly-held asset. The measure will apply to new arrangements from 7.30pm EST on 13 May 2008 and to existing arrangements from 31 March 2009.

Other budget measures

Green initiatives

The Government has delivered \$2.3 billion in funding to tackle climate change through a range of initiatives spread over four years:

- \$260 million to Australian businesses to reduce their impact on the environment
- \$1.7 billion to improve energy efficiency and develop clean energy options including renewable energy and clean coal technology
- \$300 million over five years to subsidise the provision of low-interest loans for the installation of green technologies to improve water and energy efficiency for households.

The Government has allocated funding to work on the development on the emissions trading scheme, however the tax implications of the scheme are still to be determined.

\$2.3 billion to tackle climate change

Cancellation of interests in widely-held entities

Under the current law, when shares or units in widely-held entities, (i.e. public companies) are cancelled, surrendered or brought to an end, a taxpayer is required to calculate any capital gains tax liability using the asset's market value rather than the amount they actually receive. The change will mean that any capital gains tax liability is calculated based on the amount the taxpayer receives rather than the share or unit's market value at the time of cancellation. Importantly, the change will have retrospective effect from the start of the 2006-07 income year.

Capital gains tax relief for policy holders on demutualisation of their health insurer

The Government will provide relief from capital gains tax to policy holders of health insurers who receive shares when their insurer demutualises, from 1 July 2007.

Increase to luxury car tax

The Government has announced that the luxury car tax rate will increase from 25% to 33% from 1 July 2008. As a result, a car worth \$100,000 (inclusive of GST and luxury car tax) will be subject to an additional \$2,541 in luxury car tax. There will not be a change to the luxury car tax threshold of \$57,123.

Depreciation period for computer software increased

The depreciation period for expenditure on 'in-house computer software' is to increase from two and a half years to four years on a straight-line basis with effect from 13 May 2008. This expenditure includes the acquisition and development of computer software. The four-year depreciation period is the same period as the Commissioner's effective life used for computer hardware.

Political donations – no longer deductible

From 1 July 2008 donations and gifts to political parties from individuals and businesses will no longer be tax deductible.

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