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AUSTRALIAN FEDERAL BUDGET 2018-19

Introduction

As expected for a pre-election Budget, the Government has sought to balance benefits to the household and business sectors with significant tax relief and infrastructure spends, against the need to minimise the deficit. This has been achieved in part by better revenue numbers driven by stronger local and global economic conditions, another year of growth and the ending of tax losses generated out of the GFC.

Among the more significant reforms, the Government has undertaken:

- Staged personal income tax concessions and reforms – Low income tax offsets & increase in thresholds
- Aged Care Concessions – widening of the pension loan scheme and pension work bonus
- Significant infrastructure spending of over $24 billion
- Extensive changes to address the Black Economy and cash payments more generally
- Small business changes including extending the $20k write-off for another 12 months
- Superannuation changes including banning exit fees when changing funds, rules relating to high-income employees who breach the concessional cap and the capping of fees for small accounts
- Confining of R&D tax incentive
- MITs and AMITs – changing the tax treatment of stapled securities and removing the CGT % discount at the trust level
- Extending the multinational tax integrity rules

All Budget 2018-19 documents are available to download from the Treasury's Budget 2018 website.

For an in-depth analysis, please select an area of reform below:

- **Corporate Tax**
  The Government will seek to press ahead with its broader agenda of corporate tax cuts but has introduced significant anti-avoidance measures to seek to capture lost revenue.

- **International**
  Over several years the Government has introduced a significant suite of integrity measures targeted at multinational taxpayers, including the multinational anti-avoidance law (**MAAL**) and the diverted profits tax (**DPT**). This year's Budget broadens the scope of entities to which the MAAL and DPT will apply.

- **Open Banking & Technology**
  The Budget reflects the Government's intention to move forward with its Open Banking Regime and Consumer Data Right, providing approximately $45 million of funding over the next four years. It also announced a range of measures in relation to technology and the digital economy, including a number of interesting new scientific initiatives.

- **Project, Infrastructure & Environment**
  The Budget reflects the Government's continued investment in significant regional, urban and water projects across the nation, spending over $24 billion on infrastructure funding and financing in 2018-19 to 2024-25. In addition, infrastructure specific funds for critical land transport infrastructure projects, and to alleviate congestion, increase traffic safety and improve network efficiency were announced.

- **Tax Compliance**
  There has been a significant focus on compliance with the release of the Black Economy Package to combat tax evasion. The Government will implement the recommendations of its Black Economy Taskforce, targeting sectors where there is a higher risk of underreporting income.

- **Small Business**
  In addition to extending the 20K instant asset write-off initiative for a further 12 months, the Budget also reflects a renewed focus on integrity changes for small businesses.

- **Personal Tax & Superannuation**
  One of the platform measures in the Budget is the announcement of a seven-year Personal Income Tax Plan, with three key steps, and a range of changes have been announced to the superannuation regime.

- **Goods & Services Tax (GST) & Foreign Imports**
  There were no major GST reforms in the Budget, with the most significant change to extend GST to offshore sellers of hotel accommodation in an effort to level the playing field for local sellers. Craft brewers and distillers also benefited from additional support, whilst significant measures were announced to combat illicit tobacco trade.

- **Funds**
  The Budget is consistent with the Government's planned overhaul of the taxation of stapled structures announced in March, which will tighten Australia's thin capitalisation rules. The reforms limit access to beneficial rates of withholding tax on distributions from stapled entities.

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1. Corporate Tax

The Government will seek to press ahead with its broader agenda of corporate tax cuts but has introduced significant anti-avoidance measures to seek to capture lost revenue.

Corporate Tax Cuts

The Government has recommitted to the broader 'enterprise tax plan' beyond those already legislated for small and medium enterprises. This seeks to reduce the corporate tax rate and simplify the tax system for corporate entities.

Wind back of Research & Development

The Government has announced its intention to amend the research and development (R&D) tax incentive to better target the program and improve its integrity and fiscal affordability. The announcement has been made in response to the recommendations of the 2016 Review of the R&D Tax Incentive. The changes will apply for income years starting on or after 1 July 2018 and include the following:

Companies with aggregated annual turnover of $20 million or more

For companies with aggregated annual turnover of $20 million or more, the Government will introduce an R&D premium that ties the rates of the non-refundable R&D tax offset to the incremental intensity of R&D expenditure as a proportion of total expenditure for the year. The marginal R&D premium will be the claimant's company tax rate plus:

- 4 percentage points for R&D expenditure between 0% and up to 2% R&D intensity;
- 6.5 percentage points for R&D expenditure above 2% and up to 5% R&D intensity;
- 9 percentage points for R&D expenditure above 5% and up to 10% R&D intensity; and
- 12.5 percentage points for R&D expenditure above 10% R&D intensity.

The maximum amount of R&D expenditure eligible for concessional R&D tax offsets will be increased from $100 million to $150 million per annum.

The 2016 report recommended that an "intensity threshold" be introduced, so that only companies directing a certain percentage of their total expenses to R&D would receive the non-refundable tax offset. However, the Government has opted to use a "scaling" method, with the incentive increasing with the intensity of the expenditure. A link to the intensity of the expenditure is a response to research stating that spillovers (i.e. R&D that benefits others) are more likely to flow from R&D in large companies with higher R&D intensities.

Companies with aggregated annual turnover below $20 million

For companies with aggregated annual turnover below $20 million, the Government is proposing to introduce:

- a refundable R&D offset which will be at a premium of 13.5% above a claimant's company tax rate;
- a cap on cash refunds from refundable R&D tax offset. The cap will initially be set at $4 million per year (refundable R&D tax offsets from R&D expenditure on clinical trials will not count towards the cap); and
- R&D tax offsets not refunded will be carried forward as non-refundable tax offsets to future income years.

Compliance

The Government will implement stronger compliance and administrative measures to further improve the integrity of the R&D program. These improvements include:

- increased resourcing for the Australian Taxation Office and Department of Industry, Innovation and Science, which will be used to undertake greater enforcement activity and provide improved program guidance to participants; and

- improving the transparency of the program by enabling the ATO to publicly disclose claimant details and the R&D expenditure they have claimed and limiting time extensions to complete R&D registrations and amendments to technical provisions (such as the feedstock and clawback rules and the general anti avoidance rules).

Confirmation of consolidation changes

This change simplifies two previously announced tax consolidation integrity measures. These measures, which are as follows, have now been enacted:

- Announced in the 2013-14 Budget, the *Protecting the corporate tax base from erosion and loopholes — closing loopholes in the consolidation regime* measure contained integrity rules which prevented non-residents from 'churning' assets between consolidated groups to generate double deductions. That measure applied from 14 May 2013. The Government has deferred the start date of one aspect of the measure, which requires grouping of associates when considering whether the integrity rules apply. These grouping rules now apply from the date of introduction of the enabling legislation.
- Announced in the 2016-17 Budget, the *Tax Integrity Package — deferred tax liabilities* measure removed adjustments relating to deferred tax liabilities from the consolidation entry and exit tax cost-setting rules. The measure contained complex transitional rules which required taxpayers to determine if any deferred tax liabilities were included in entry tax cost setting calculations — if so, the measure would not apply. Following consultation, those complex transitional rules have now been removed from the final legislation.

Deferral of TOFA Rules

The Government has deferred the start date of changes to the taxation of financial arrangements (TOFA) rules announced in the 2016-17 Budget. The *Ten Year Enterprise Tax Plan — business simplification — taxation of financial arrangements — regulation reform* measure will reduce the scope of the TOFA rules, thereby decreasing compliance costs. The measure was announced originally to apply to income years commencing on or after 1 January 2018, but will now apply to income years commencing on or after the date of Royal Assent of the enabling legislation.

This measure has been deferred to allow additional time to design the simplified rules, to prevent unintended outcomes and to ensure compliance cost savings are realised.

Illegal phoenix activity

The Government will reform the corporations and tax laws and provide regulators with additional tools to help them deter and disrupt illegal phoenix activity. Illegal phoenixing involves the deliberate misuse of the corporate form, including – for example - scamming customers by not sending them goods or providing services paid for, or lost wages and superannuation entitlements. The package includes reforms to:

- introduce new phoenix offences to target those who conduct or facilitate illegal phoenixing;
- limit the ability of directors to resign when this would leave the company with no directors;
- restrict the ability of related creditors to vote on the appointment, removal or replacement of an external administrator; and
- expand the ATO's power to retain refunds where there are outstanding tax lodgements.

2. International

Over several years the Government has introduced a significant suite of integrity measures targeted at multinational taxpayers, including the multinational anti-avoidance law (**MAAL**) and the diverted profits tax (**DPT**). This year's Budget broadens the scope of entities to which the MAAL and DPT will apply. The Budget will also remove the ability of taxpayers to value assets for thin capitalisation purposes in a way that does not align with the valuation of those assets on the taxpayer's financial statements.

Significant global entity definition

The Government has announced its intention to broaden the definition of "significant global entity" (**SGE**) under the tax rules. This definition is used for a range of tax purposes to identify entities:

- which are required to prepare Country by Country reports
- to which the MAAL applies;
- to which the DPT applies; and
- which may be subject to increased scheme shortfall penalties.

The current definition applies to an entity which is a member of a group that is consolidated for accounting purposes and which is headed by a public company or a private company required to provide consolidated financial statements, with annual global revenue of at least $1 billion. The definition will be broadened to include members of large multinational groups headed by private companies, trusts and partnerships. It will also include members of groups headed by investment entities.

The changes to the definition will also make amendments to the Commissioner's power to determine that an entity is a global parent entity of an SGE, to ensure that power operates as intended.

The measure will apply to income years commencing on or after 1 July 2018.

Thin capitalisation assets valuations to be aligned with financial statements

The Government will restrict the ability of entities to make "thin capitalisation only revaluations" by requiring entities to align the value of their assets for thin capitalisation purposes with the value included in their financial statements.

Under the current thin capitalisation rules, taxpayers may in certain circumstances revalue assets for thin capitalisation purposes only, without also revaluing the assets for accounting purposes. Additionally, taxpayers may rely on concessions in the thin capitalisation rules, which allow for the recognition and revaluation of certain intangible assets not otherwise recognisable according to accounting standards. The ATO has previously expressed concerns about taxpayers using the existing rules to increase their maximum allowable debt.

Applying to income years commencing on or after 1 July 2019, all entities must rely on the asset values contained in their financial statements for thin capitalisation purposes. Valuations that were made prior to 7.30PM (AEST) on 8 May 2018 may be relied on until the beginning of an entity's first income year commencing on or after 1 July 2019.

Thin capitalisation treatment of entities that are both outward and inward investing entities

The Government will ensure that foreign controlled Australian consolidated entities and multiple entry consolidated groups that control a foreign entity are treated as both outward and inward investment vehicles for thin capitalisation purposes. This will apply for income years commencing on or after 1 July 2019. This change will ensure that inbound investors cannot access tests that were only intended for outward investors.

Film industry location incentive

The Government has confirmed that it will provide a location incentive of $140 million to attract foreign investment in the Australian film industry. Specifically, the Government will provide $140 million over four years from 2019-20 to attract international investment to sustain Australian jobs in the film production and related industries through a competitive incentive program. This funding will complement the Government's existing 'Location Offset' component of the Australian Screen Production Incentive tax rebate.

This additional funding was announced earlier this month by the Minister for Foreign Affairs. The proposed incentive effectively increases the existing Location Offset rebate from 16.5% to 30% for eligible large budget international productions that film

3. Open Banking & Technology

Open Banking

The Treasurer announced that the Government was moving forward with its Open Banking Regime and Consumer Data Right, providing approximately $45 million over the next four years to fund the work of the Australian Competition and Consumer Commission, the Office of the Australian Information Commissioner and CSIRO's Data 61. The Consumer Data Right is to commence with Australia's banking industry (through Open Banking) be extended to other industries, such as the energy and telecommunications industries, and eventually apply economy-wide. The consumer data right is to give "*Australians the ability to take control of their personal data and share it safely with trusted and accredited service providers*".

Whilst these announcements, and the other mentions of the Consumer Data Right in the papers, are consistent with the recommendations made in the Government's Review into Open Banking, detail on implementation is yet to come.

Technology

The Government announced a range of measures in relation to technology and the digital economy, including a number of interesting new scientific initiatives under the "Australian Technology and Science Growth Plan".

Taxing Digital Businesses

The Treasurer announced a discussion paper to be released in several weeks which will explore options for taxing digital businesses in Australia. The budget speech noted that this arises out of the work done by the Government with other members of the G20 over the last year. It likely that this will pick up on concepts and tax issues discussed in the OECD/G20 Interim Report 2018, "Tax Challenges Arising from Digitalisation", published in March 2018 and arising out of Action 1 of the BEPS Project.

Measures under the "Australian Technology and Science Growth Plan"

Satellite navigation improvements

The Government is allocating $224.9 million between two separate items over four years from 2018-19 to improve the accuracy, integrity of satellite navigation, covering the entirety of Australia (including areas without mobile phone coverage) and its maritime zones. The measure is intended to deliver positioning, navigation and timing (PNT) data to increase accuracy through the creation of a Satellite-Based Augmentation System (SBAS). This budget measure builds on the $12 million provided in the 2016-17 MYEFO measure for a two-year test of the safety, reliability and efficiency of SBAS, conducted via the "SBAS testbed project" in collaboration with New Zealand and private enterprise. *Other measures:*

The Government has also committed to funding:

- a review of existing domestic and international measures of innovation ($1.0 million over 2 years from 2018-19 to the Department of Industry, Innovation and Science). The review will inform the development of new metrics to ensure that innovation is more accurately measured in Australia;
- measures to strengthen Australia's capability in Artificial Intelligence (**AI**) and Machine Learning (**ML**) ($29.9 million over four years from 2018-19). The Government will support business innovation in sectors such as digital health, digital agriculture, energy, mining and cybersecurity through:
  - funding projects from AI and ML capabilities;
  - funding AI and ML-focused PhD scholarships and school-related learning to address skill gaps; and
  - the development of a roadmap and frameworks to identify global opportunities and guide future investments;
- the replacement and upgrade of Australia's computing and data capability at the Pawsey Supercomputing Centre, which is a critical component of the national research and innovation system ($70.0 million in 2017-18);
- measures to encourage more women into science, technology, engineering and mathematics education and careers ($4.5 million over four years from 2018-19);
- measures to grow the Australian space industry, including by establishing a National Space Agency ($41 million over four years from 2018-19). The cash injection is part of a longer-term plan to boost local space capability and build international representation in the increasingly lucrative sector, following on from announcements in September 2017;
- the development of a detailed business case to modernise IP Australia's patents management system and streamline access to its services via digital channels. This measure will support Australian businesses to protect their intellectual property and in doing so, support and strengthen innovation in the Australian economy;
- establishing the Asian Innovation Strategy ($20.0 million over four years from 2018-19) and the Small and Medium Enterprises Export Hubs program ($20.0 million over four years from 2018-19). These initiatives will help Australian businesses and researchers take full advantage of new growth opportunities overseas, especially in Asia; and

- measures to provide governments, businesses, researchers and individuals with access — through the Digital Earth Australia program — to reliable standardised satellite data ($36.9 million over three years from 2019-20 (and $12.8 million ongoing). This data can be used to:
    - build new digital products and services for commercial purposes,
    - interpret and analyse changes to Australia's physical landscape, enabling better understanding of environmental changes;
    - assist farmers to monitor patterns and increase the efficiency and utilisation of their land;
    - assist governments in improving disaster planning.

4. Projects, Infrastructure & Environment

Infrastructure spending is a significant part of the 2018-19 Budget with extensive spending and the creation of various new funds.

Significant projects

The Government will continue its previously announced $75 billion 10-year infrastructure plan, spending approximately $25 billion on infrastructure funding and financing in 2018-19 to 2024-25 on significant regional, urban and water projects across the nation. Major projects include:

- $3.5 billion to establish the Roads of Strategic Importance initiative to support the upgrade of key regional road corridors in Australia;
- in Victoria, up to $5 billion for the Melbourne Airport Rail Link and $1.75 billion for the North East Link;
- in Queensland, $3.3 billion for additional Bruce Highway upgrades;
- in South Australia, $1.4 billion for Adelaide North-South Corridor future priorities;
- in Western Australia, an additional $1.1 billion for Metronet projects;
- in NSW, $971 million for the Coffs Harbour Bypass on the Pacific Highway;
- in Tasmania, $461 million for the Bridgewater Bridge Replacement; and
- $518.9 million from uncommitted funding in the Infrastructure, Regional Development and Cities portfolio towards other policy priorities, including round three of the Building Better Regions Fund and round four of the Stronger Communities Programme.

New Funds

The Government announced its proposal to establish infrastructure specific funds, including:

- $250 million to establish a Major Project Business Case Fund to assist with the development of business cases for future critical land transport infrastructure projects; and
- $1 billion to establish the Urban Congestion Fund to support projects to alleviate congestion, increase traffic safety and improve network efficiency for commuter and freight movements in urban areas.

Environment – Great Barrier Reef

The Government will allocate $535.8 million over five years from 2017-18 to protect the Great Barrier Reef from climate change and pollution.

5. Tax Compliance

There has been a significant focus on compliance with the release of the Black Economy Package to combat tax evasion. The Government will implement the recommendations of its Black Economy Taskforce, targeting sectors where there is a higher risk of underreporting income. These measures include outlawing certain large cash payments greater than $10,000.

The measures are designed to disincentivise black economy behaviours and ensure greater compliance with tax obligations. These measures are expected to bring in $5.3 billion over the next four years.

Taxable Payments Reporting System (TPRS)

Under the TPRS, businesses are required to report payments to contractors to the ATO. The Government will further expand the TPRS to these industries:

- security providers and investigation services;
- road freight transport; and
- computer system design and related services.

The expansion is in response to the Black Economy Taskforce findings which identified a higher risk of non-compliance by contractors in these industries. Businesses will need to ensure they collect information from 1 July 2019, with the first annual report required in August 2020.

Economy Wide Cash Payments Limit

A $10,000 limit for cash payments made to businesses for goods and services will be introduced from 1 July 2019. Currently, large undocumented cash payments can be used to avoid tax or to launder money from criminal activity. Transactions over the limit will have to be made through an electronic payment system or by cheque. However, transactions with financial institutions and consumer to consumer non-business transactions will not be affected.

Removing tax deductibility of non-compliant payments

From 1 July 2019, businesses will no longer be able to claim deductions for payments to:

- employees if the business has not withheld any amount of PAYG (where they were required to do so); and
- contractors if the contractor does not provide an ABN and the business has not withheld any amount of PAYG (where they were required to do so).

Strengthened ATO Powers

The Government will provide $318.5 million over four years to the ATO to implement new strategies to combat the black economy, including a Black Economy Hotline (to allow the community to report black economy and illegal phoenix activities), improved government data analytics and educational activities.

Other measures

Other measures include:

- consulting on reforms to the Australian Business Number (**ABN**) system, such as the development of rigorous new identification systems for company directors; and
- providing additional funding to the Tax Practitioners Board to take action against tax agents that facilitate black economy activities.

6. Small Business

Although the 2018 Budget allows small businesses to continue enjoying the $20K instant asset write-off initiative of recent years, there has been a renewed focus on integrity changes.

In addition to the general tax compliance and integrity changes of the 2018 Budget, specific measures likely to impact on small businesses include:

- disallowing tax deductions for costs of holding onto vacant land and for concessional loans between tax exempt entities in certain circumstances;
- restricting access to small business CGT concessions in relation to partnerships; and
- introducing specific anti-avoidance measures concerning unpaid present entitlements made to private companies and circular distributions involving family trusts.

Extension of the $20K instant asset write-off measure

The Government will extend the accelerated depreciation initiative for small businesses, with aggregated annual turnover less than $10 million, by a further 12 months to 30 June 2019.

The immediate deduction applies to purchases of eligible assets costing less than $20,000 first used or installed ready for use by 30 June 2019. The immediate deductibility threshold and the balance at which the pool can be immediately deducted are normally set at $1,000.

A small business simplified depreciation pool can also be immediately deducted if the balance is less than $20,000. Current 'lock out' laws for the simplified depreciation rules (preventing small businesses from re-entering the simplified depreciation regime for five years if they opt out) will continue to be suspended until 30 June 2019.

Specific anti-avoidance measure for circular distributions involving family trusts

Circular or 'round robin' distributions made between family trusts enable a distribution to be ultimately returned to the original trustee in a way that avoids any tax being paid on that amount.
From 1 July 2019, a specific anti-avoidance measure will apply to impose tax on such distributions at a rate equal to the top personal tax rate (plus the Medicare levy). This measure is already in place for other closely held trusts that engage in circular trust distributions.

Restricting access to small business CGT concessions in relation to partnerships

From 7:30PM (AEST) on 8 May 2018, partners that alienate their income by creating, assigning or otherwise dealing in rights to the future income of a partnership will no longer be able to access the small business capital gains tax (CGT) concessions in relation to these rights.

There are no changes to the small business CGT concessions themselves, but the means by which these concessions may be accessed are now tightened. The concessions continue to be targeted at eligible small businesses with an aggregated annual turnover of less than $2 million or net assets less than $6 million.

Clarifying the operation of the Division 7A integrity rule to UPEs

From 1 July 2019, where a related private company is made entitled to a share of trust income as a beneficiary, but has not been paid that amount, that "unpaid present entitlement" will come within Division 7A of the *Income Tax Assessment Act 1936* (Cth).

Division 7A operates as an integrity rule – benefits provided by private companies to related taxpayers will be taxed as dividends unless they are structured as Division 7A complying loans or another exception applies. Accordingly, an unpaid present entitlement will either be required to be repaid to the private company over time as a complying loan or subject to tax as a dividend.

The Division 7A amendments announced in the 2016-17 Budget will now also commence on 1 July 2019 and not 1 July 2018. This will enable all Division 7A amendments to take effect as a consolidated package.

Disallowing tax deductions for costs of holding onto vacant land

From 1 July 2019, expenses associated with holding vacant land, either for residential or commercial purposes, will no longer be deductible where the land is not genuinely held for the purpose of earning assessable income (such as the practice of land banking in denying the use of land for housing or other development).

The measure will not apply to expenses associated with holding land that are incurred after:

- property has been constructed on the land and is approved to be occupied and available for rent; or
- if the land is being used by the owner to carry on a business, such as primary production.

Denied deductions will not be able to be carried forward for use in later income years. However, expenses for which deductions will be denied, but would ordinarily be a cost base element (such as borrowing expenses), may still be included in the cost base of the asset for capital gains tax (CGT) purposes when sold.

Disallowing tax deductions for concessional loans between tax exempt entities

Under this measure, concessional loans that are entered into by tax exempt entities, which become taxable after 8 May 2018, will be required to be valued as if they were originally entered into on commercial terms. Tax deductions that arise on the repayment of the principal of a concessional loan will be disallowed.

This measure is to counter the unforeseen consequence between taxation of financial arrangement rules and the rules dealing with deemed market values for tax exempt entities that become taxable.

7. Personal Tax & Superannuation

One of the platform measures in the Budget is the announcement of a seven-year Personal Income Tax Plan. The plan has three key steps. The **first step** will provide permanent tax relief to low and middle income earners. The **second step** will provide relief from bracket creep by increasing the threshold of the 32.5% personal income tax bracket. The **third step** will remove the 37% personal income tax bracket. These measures build on similar announcements in the 2016-17 budget measure and seek to provide tax relief to encourage working Australians to remain in the workforce.

Low Income Tax Offset (step 1)

For the income years of 2018-2019 to 2021-2022, the Government will provide a non-refundable tax offset of up to $530 per annum to Australian resident low and middle income taxpayers. It will be received on assessment as a lump sum, after an individual lodges their tax return.

The Low and Middle Income Tax Offset will provide the following benefits, and is in addition to the Low Income Tax Offset:

- for taxpayers with taxable income of $37,000 or less – up to $200 per annum;
- for taxpayers with taxable income between $37,000 and $48,000 – up to $530 per annum (increasing at a rate of three cents per dollar);
- for taxpayers with taxable income between $48,000 and $90,000 – all eligible for the maximum benefit of $530 per annum; and
- for taxpayers with taxable income between $90,001 and $125,333, the offset will phase out at a rate of 1.5 cents per dollar.

Bracket creep (step 2)

From 1 July 2018, the Government will increase the top threshold of the 32.5% personal income tax bracket from $87,000 to $90,000.

From 1 July 2022, the Government will:

- increase the Low Income Tax Offset from $445 to $645;
- extend the 19% personal tax bracket from $37,000 to $41,000 to lock in the benefits of step 1;
- withdraw the increased Low Income Tax Offset at:
  - a rate of 6.5 cents per dollar between incomes of $37,000 and $41,000;
  - a rate of 1.5 cents per dollar between incomes of $41,000 and $66,667; and
- further increase the top threshold of the 32.5% personal income tax bracket from $90,000 to $120,000.

Simplification (step 3)

In the third step, the Government will simplify and flatten the personal tax system by removing the 37% tax bracket entirely.

From 1 July 2024, the Government will extend the top threshold of the 32.5% personal income tax bracket from $120,000 to $200,000. This means that:

- taxpayers with taxable income exceeding $200,000 will pay the top marginal tax rate of 45%; and
- taxpayers with taxable income between $41,0001 and $200,000 will pay the marginal tax rate of 32.5%.

This measure builds on the 2016-17 Budget measure *Ten Year Enterprise Tax Plan — targeted personal income tax relief*, which extended the 32.5% personal income tax bracket from $80,000 to $87,000 from 1 July 2016. It also reflects inflation and wage growth impacts.

Superannuation

A range of changes have been announced to the superannuation regime. The key changes include:
Caps and Limits
A 3% annual cap on passive fees charged by superannuation funds on small accounts with balances below $6,000 will be introduced. Exit fees on all superannuation accounts will be banned.

The Government has announced an intention to also strengthen the ATO led consolidation regime by requiring the transfer of all inactive superannuation accounts where the balances are below $6,000 to the ATO. The ATO will expand its data matching processes to proactively reunite these inactive superannuation accounts with the member's active account, where possible. This measure will also include the proactive payment of funds currently held by the ATO.

These changes will take effect from 1 July 2019.

Changes to insurance

Insurance arrangements for certain cohorts of superannuation members will be changed. Insurance within superannuation will move from being a default framework to being offered on an opt-in basis for:

- members with low balances of less than $6,000;
- members under the age of 25 years; and
- members whose accounts have not received a contribution in 13 months and are inactive.

The changes will take effect on 1 July 2019 and affected superannuants will have a period of 14 months to decide whether they will opt in to their existing cover or allow it to switch off.

Allowable members in self-managed superannuation funds

The Government will increase the maximum number of allowable members in new and existing self-managed superannuation funds and small APRA funds from four to six, from 1 July 2019. This will provide greater flexibility for larger families to implement intergenerational solutions for managing long-term, capital intensive investments.

Preventing inadvertent concessional cap breaches by certain employees

Individuals whose income exceeds $263,157 and have multiple employers will be able to nominate that their wages from certain employers are not subject to the superannuation guarantee (SG) from 1 July 2018. This measure is intended to allow eligible individuals to avoid unintentionally breaching the $25,000 annual concessional contributions cap as a result of multiple compulsory SG contributions. Breaching the cap otherwise results in these individuals being liable to pay excess contributions tax, as well as a shortfall interest charge. Employees who use this measure could negotiate to receive additional income, which is taxed at marginal tax rates.

Three-yearly audit cycle for some self-managed superannuation funds

The annual audit requirement for self-managed superannuation funds (SMSFs) with a history of good record-keeping and compliance will be changed to a three-yearly requirement. This measure will reduce red tape for SMSF trustees that have a history of three consecutive years of clear audit reports and have lodged the fund's annual returns in a timely manner. This measure will start on 1 July 2019 and, to ensure smooth implementation, the Government will consult with stakeholders.

Pension Loans Scheme

The Pension Loans Scheme will be expanded to give all Age Pension-aged Australians the option to boost their standard of living. Full rate pensioners will be able to boost their income by up to $11,799 (singles) or $17,800 (couples) per year.

Pensioner Work Bonus

The pension work bonus will be increased to allow age pensioners to earn an extra $50 a fortnight without reducing their pension. For the first time, the bonus will be extended to self-employed individuals who can now earn up to $7,800 a year.

Testamentary Trust

From 1 July 2019, the concessional tax rates for minors receiving income from testamentary trusts will not be available for trust assets unrelated to the deceased estate. This measure will clarify that minors will be taxed at adult marginal tax rates only in respect of income a testamentary trust generates from assets of the deceased estate (or the proceeds of the disposal or investment of these assets).

Medicare Levy

Increasing the Medicare levy low-income threshold

The Medicare levy low-income thresholds for singles, families, and seniors and pensioners will be increased from the 2017-18 income year. The increases take account of recent movements in the CPI so that low-income taxpayers generally continue to be exempted from paying the Medicare levy.

The thresholds will be increased as follows:

- singles – from $21,655 to $21,980;
- family – from $36,541 to $37,089;
- single seniors and pensioners – from $34,244 to $34,758;
- family threshold for seniors and pensioners - from $47,670 to $48,385; and
- for each dependent child or student, the family income thresholds increase by a further $3,406, instead of the previous amount of $3,356.

Retaining the Medicare levy rate at 2%

The Medicare Levy increase of 0.5% as proposed in the 2017-2018 Budget to fund the NDIS will not proceed. The Medicare Levy will accordingly remain at 2.0%. Other consequential changes to related tax rates, such as the fringe benefits tax rate and withholding tax rates, will also not proceed.

8. GST & Foreign Imports

Unsurprisingly, there were no major GST reforms in the Budget. The key change was to extend GST to offshore sellers of hotel accommodation in an effort to level the playing field for local sellers. The Government also introduced 2 excise measures aimed at providing additional support to craft brewers and distillers. In addition, minor changes have been announced to the luxury car tax, as well as significant measures to combat illicit tobacco trade.

Online hotel bookings

From 1 July 2018, the purchaser of newly constructed residential premises will be required to pay GST directly to the ATO instead of the vendor.

The Government will extend the GST by ensuring that offshore sellers of hotel accommodation in Australia calculate their GST turnover in the same way as local sellers from 1 July 2019.
Currently, unlike GST registered businesses in Australia, offshore sellers of Australian hotel accommodation are exempt from including sales of hotel accommodation in their GST turnover. This means that offshore sellers of Australian hotel accommodation are often not required to register for and charge GST on their mark up over the wholesale price of the accommodation. The exemption was introduced in 2005, when most offshore sales of Australian hotel rooms were to foreigners booking through offshore tour operators, and the online booking market was relatively small.

Both Australian and foreign consumers are increasingly booking Australian hotel rooms through online services based offshore, which are taking advantage of the exemption designed for offshore tour operators. Removing the exemption will level the playing field for local sellers by ensuring the same tax treatment of Australian hotel accommodation, whether booked through a domestic or offshore company.

The measure will apply to sales made on or after 1 July 2019. Sales that occur before 1 July 2019 will not be subject to the measure even if the stay at the hotel occurs after this date.

This measure follows the Government’s decision to extend the GST to digital products (e.g. streaming or downloading of movies) and other services from 1 July 2017 and to low value imported goods from 1 July 2018. The measure will require the unanimous agreement of the States and Territories prior to the enactment of legislation.

Alcohol excise changes – craft brewers and distillers

The Government will increase the alcohol excise refund scheme cap to $100,000 per financial year, as well as extending the current concessional draught beer excise rates to 8 litre or greater kegs, from 1 July 2019.

Currently, the alcohol excise refund scheme provides eligible domestic alcohol producers with a refund of excise paid on certain alcoholic beverages (such as beer, spirits or other fermented beverages) up to a cap of $30,000 per financial year. The Government will increase this cap to $100,000 per financial year. The measure will provide additional support to domestic brewers, distillers and producers of other fermented beverages.

The Government will also extend the concessional draught beer excise rates, which currently apply to individual containers of beer exceeding 48 litres, to 8 litre or greater kegs. This will benefit craft brewers who typically use smaller sized kegs, and level the playing field with large breweries who typically use 50 litre kegs and therefore are currently taxed at lower rates.

Luxury Car Tax

The Government has announced a measure to remove Luxury Car Tax (**LCT**) on cars re-imported into Australia following a refurbishment overseas.

The LCT is a tax on cars with a GST-inclusive value above a certain threshold (for the 2018-18 financial year the threshold was $75,526 for fuel-efficient vehicles and $65,094 for all other vehicles). The current rate is 33%.

Under current law, cars that are refurbished in Australia (and subsequently exceed the relevant LCT threshold) are not subject to LCT. However, the LCT applies to cars exported from Australia for refurbishment and subsequently reimported into Australia, at a time when its value exceeds the relevant LCT threshold.

The change will ensure the same tax treatment applies, regardless of where the car is refurbished.

Illicit Tobacco

The Government has also announced a significant crackdown in the illicit tobacco trade with the introduction of five new components:

Collecting tobacco duties and taxes <u>at the border</u>

Under Australia's current system, tobacco products can be imported into Australia and stored in licensed warehouses prior to tax and duties being paid on those imports. The delayed taxing point creates an incentive for illegal tobacco market operators to source tobacco for distribution on the black market.

Under the Government's announced measure, from 1 July 2019 importers of tobacco products will be required to pay all duty and tax liabilities upon *importation*. The Government has flagged that transitional measures will apply for tobacco products that are held in licensed warehouses at the commencement of the measure on 1 July 2019, allowing eligible affected entities to pay the liability on the warehoused stock within 12 months.

The taxing point for any future domestic manufacture of tobacco will also be changed to be consistent with the new taxing point for tobacco imports (this is less relevant due to the fact that there is currently no licensed commercial tobacco production in Australia).

Current weekly settlement arrangements (which require importers to lodge excise returns detailing the deliveries made during the settlement period (usually weekly), and pay duty on those goods) will no longer apply to imported tobacco.

Creation of the Illicit Tobacco Task Force

From 1 July 2018, a multi-agency Illicit Tobacco Task Force will be formed, comprising members from a number of law enforcement and border security agencies, to increase the resources and capabilities dedicated to combatting illicit tobacco smuggling. The new Task Force will have additional powers and capabilities to enhance intelligence gathering and proactively target, disrupt and prosecute serious and organised crime groups at the centre of the illicit tobacco trade.

Additional resources to combat domestic tobacco crops

From 1 July 2018, the ATO will be provided ongoing funding to bolster its capabilities to detect and destroy domestically grown illicit tobacco crops.

Introducing a prohibited import control for tobacco

From 1 July 2019, permits will be required for all tobacco imports (except for tobacco imported by travellers within duty free limits). This will make it easier for the Australian Border Force to take enforcement action and seize tobacco where no duty has been paid, increasing the deterrent against illicit tobacco smuggling.

ATO excise systems upgrade

The ATO will upgrade and modernise its excise and excise equivalent goods payment systems beginning 2020-21 to replace the outdated paper lodgement system.

9. Funds

The Government will proceed with its planned overhaul of the taxation of stapled structures announced in March 2018.

Consistent with the previously announced measures, the reforms limit access to beneficial rates of withholding tax on distributions from stapled entities, and also limit the tax concessions for foreign pension funds and foreign governments. The measures also tighten Australia's thin capitalisation rules.

Management Investment Trusts (MITs) and Attribution MITs (AMITs) will see additional changes, with the 50% CGT discount for payments at a trust level set to be abolished.

Stapled Securities

The Government will proceed with previously announced measures regarding the taxation of stapled structures and similar arrangements.

The measures are:

- a withholding tax rate of 30% (instead of the current 15%) will be applied on distributions which are derived from trading income but have been converted to passive income through a MIT. This does not include rent received from third parties. Certain nationally significant infrastructure staples which are approved by the Government will be eligible for a 15-year exemption from this measure;
- the associate entity threshold for the thin capitalisation rules will be lowered from 50% cent to 10%. This aims to limit foreign investors using multiple layers of flow-through entities to convert trading income into interest income (so-called "double gearing" arrangements). These changes will take effect from 1 July 2018;
- the foreign pension fund withholding tax exemption for interest and dividends will be limited to portfolio investments;
- the Government will introduce a legislative framework for the current administrative practice relating to tax exemptions for foreign governments. Importantly, the Government will limit this exemption to portfolio investments; and
- the 15% concessional MIT withholding tax rate for investments in agricultural land will be removed. This does not go as far as the previously announced measure, which provided that agricultural land would not qualify as eligible investment business income of a MIT.

The above changes, except for those regarding thin capitalisation, will take effect from 1 July 2019, and will involve a transitional period of at least 7 years.

See our previous alert here for a more detailed analysis of these changes.

Updating the list of information exchange countries for MITs

The Government will update the list of countries whose residents are eligible to access a reduced withholding tax rate of 15 per cent, instead of the default rate of 30 per cent, on certain distributions from Australian MITs. Listed countries are those which have established international agreements enabling them to share taxpayer information with Australia. The update will add the 56 jurisdictions that have entered into information sharing agreements since 2012. The updated list will be effective from 1 January 2019.

This measure supports the operation of the MIT withholding tax system by providing the reduced withholding tax rate only to residents of countries that enter into effective information sharing agreements with Australia. The information sharing agreements form a part of the Government's broader commitment to safeguard against offshore tax avoidance and evasion

Removal of the 50% CGT discount at the MIT and AMIT level

From 1 July 2019, MITs and AMITs will not be able to apply the 50% CGT discount to payments at the trust level.

This measure aims to promote the flow-through nature of MITs and AMITs such that income is taxed as though investors had invested directly.

This measure aims to prevent beneficiaries who are not otherwise entitled to the CGT discount from benefiting from the application of the discount at a trust level.

It still allows MITs and AMITs that derive a capital gain to distribute the income as a capital gain that the beneficiary is then able to discount.

Impact on the proposed CCIV regime

On 21 December 2017, the Federal Government released draft legislation for the tax treatment of Corporate Collective Investment Vehicles (**CCIVs**). See our previous alert here.

The tax treatment of CCIVs is broadly based on the model for AMITs and seeks to provide flow through tax treatment together with deemed capital gains tax treatment.

The removal of the capital gains discount at the trust level for MITs and AMITs is consistent with the treatment currently proposed for CCIVs. CCIVs are not entitled to discount capital gains, however a member who is entitled to discount capital gains may apply the discount to an amount that flows through the CCIV.

It remains to be seen how the other changes will be picked up in the next draft of the CCIV tax legislation.

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