Chapter 8

Using the benefits of the mining boom to assist small businesses

8.1 This chapter discusses the aspects of the Minerals Resource Rent Tax (MRRT) legislative package which relate to the taxation treatment of small businesses. Schedules 1, 2 and 3 to the Tax Laws Amendment (Stronger, Fairer, Simpler and Other Measures) Bill 2011 (Stronger, Fairer, Simpler Bill) seek to amend the *Income Tax Assessment Act 1997* (ITAA 1997) and related legislation to:

- abolish the entrepreneurs' tax offset (ETO);
- increase the small business instant asset write-off threshold from $1,000 to $6,500 and allow for simplified depreciation of assets which cost more than $6,500; and
- allow small businesses to claim an accelerated initial deduction for motor vehicle purchases.

8.2 Overall, the proposed changes are designed to improve incentives, simplify existing arrangements and give added support to small businesses. The Minister's second reading speech links the removal of the ETO and the new measures outlined elsewhere in the bill, arguing that the removal of the ETO 'makes way for better targeted small business assistance'.[1]

8.3 Although not included in these bills, it is also worth noting that businesses will be supported by other measures in the *Stronger, Fairer, Simpler* package of reforms announced by the government in May 2010. These reforms are linked to the MRRT (which is also part of the *Stronger, Fairer, Simpler* reforms), and include important measures such as the cut in the company tax rate from 30 to 29 per cent from 2013–14.

Abolishing the entrepreneurs' tax offset

8.4 Schedule 1 seeks to abolish the ETO by repealing subdivision 61-J of the ITAA 1997.

8.5 The ETO was announced by the Howard Government as part of its 2004 re-election campaign[2] and was subsequently introduced in early 2005. The ETO is a

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1 The Hon. Bill Shorten MP, Minister for Financial Services and Superannuation, Second Reading Speech, Tax Laws Amendment (Stronger, Fairer, Simpler and Other Measures) Bill 2011, *House of Representatives Hansard*, 2 November 2011, p. 12417.

2 The Hon. John Howard MP, Prime Minister, 'Promoting an Enterprise Culture', *Media release*, 26 September 2004.

tax offset equal to 25 per cent of the income tax payable by certain small businesses (those with an aggregated turnover of $50,000 or less). The tax offset is phased-out when the annual turnover is greater than $50,000 but less than $75,000. Amendments passed in 2010 introduced a new income test which restricted access to the ETO for businesses with high alternative sources of household income (adjusted annual income of $70,000 for singles and $120,000 for families).

8.6 The Regulation Impact Statement associated with the introduction of the ETO noted that the objectives of the measure were to:

> … provide encouragement for enterprising Australians in the early days of a small business, in particular to provide a greater benefit to businesses with greater productivity, and to provide incentive for the growth of small business especially the very small, micro and home-based businesses which are in the STS [simplified tax system].[3]

8.7 When analysing the ETO, the Australia's Future Tax System Review (AFTS Review, also known as the Henry Review) observed that around 73 per cent of ETO recipients receive a benefit of less than $600.[4] The AFTS Review concluded:

> Removing the ETO would reduce compliance and administration costs and provide a more equitable and neutral treatment between self-employment and employment income. The ETO is very complex to administer and provides problematic incentives related to business structure.[5]

8.8 Illustrating the AFTS Review's concerns regarding complexity and administration costs relative to the benefits realised by those eligible, the example below, published by the Australian Taxation Office (ATO) to assist an individual or a business in calculating their ETO, results in an offset of only $135 being realised:

> During 2009–10, Jenny ran a physiotherapy practice from her home. The net income from her practice is $18,000 (that is, $30,000 turnover less $12,000 business expenses). This is Jenny's net small business income. In addition she had a part-time job from which she received wages of $27,000. She is married to Geoff who earned $96,000 in 2009–10. Geoff has no other income.[6]

8.9 The proposed amendments in schedule 1 are intended to commence from the date of the Royal Assent. The amendments are expected to result in a revenue gain of

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3 Tax Laws Amendment (2004 Measures No. 7) Bill 2004, *Explanatory Memorandum*, p. 30.

4 Australia's Future Tax System Review, *Report to the Treasurer*, part 2: detailed analysis, vol. 1, December 2009, p. 89.

5 Australia's Future Tax System Review, *Report to the Treasurer*, part 2: detailed analysis, vol. 1, December 2009, p. 89.

6 Australian Taxation Office, 'Entrepreneurs tax offset' www.ato.gov.au/businesses/content.aspx?menuid=0&doc=/content/00149627.htm&page=14&H14 (accessed 30 January 2012).

$365 million over the forward estimates ($180 million in 2013–14 and $185 million in 2014–15).[7]

Increasing the small business instant asset write-off threshold and simplified asset depreciation

8.10 Currently, subdivision 328-D of the ITAA 1997 provides that small businesses may choose to deduct amounts for most of their depreciating assets on a diminishing value basis using a pool[8] that is treated as a single depreciating asset. The pool rate is 30 per cent for most depreciating assets (general small business pool), and five per cent for depreciating assets that have an effective life of 25 years or more (long life small business pool). Depreciating assets with a value of less than $1,000 may be immediately deducted.

8.11 Schedule 2 to the Stronger, Fairer, Simpler Bill seeks to:

- increase the small business instant asset write-off threshold from $1,000 to $6,500; and
- consolidate the general small business pool and the long-life small business pool and into a single general small business pool which will be written off at one rate (15 per cent in the year of allocation and 30 per cent in other years).

8.12 The Minister's second reading speech provides a useful illustration of the types of benefits small businesses could expect from the amendments:

> This increase from a threshold of $1,000 will allow small businesses to claim a deduction for more expensive assets—those costing less than $6,500 instead of less than $1,000—providing a cash flow benefit. Small business will benefit from this initiative when they purchase assets such as a computer, photocopier and printer.
>
> The government will also simplify the depreciation regime for depreciating assets costing $6,500 or more. Instead of having to allocate assets to one of two depreciation pools, each with a different depreciation rate (five per cent and 30 per cent), small business will now be able to allocate assets to a single depreciation pool with a single rate of 30 per cent (and 15 per cent in the first year). Simplicity is what a person in their own business wants and needs, and we will give them less complexity and a system that is easier to understand.[9]

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7 Tax Laws Amendment (Stronger, Fairer, Simpler and Other Measures) Bill 2011, *Revised Explanatory Memorandum*, p. 3.

8 The ITAA 1997 explains that 'broadly a pool is made up of the costs of the depreciating assets that are allocated to it or, in some cases, a proportion of those costs'. *Income Tax Assessment Act 1997*, s. 328-170.

9 The Hon. Bill Shorten MP, Minister for Financial Services and Superannuation, Second Reading Speech, Tax Laws Amendment (Stronger, Fairer, Simpler and Other Measures) Bill 2011, *House of Representatives Hansard*, 2 November 2011, p. 12417.

8.13 The proposed amendments are broadly consistent with the AFTS Review, which recommended that small businesses be allowed to write off depreciating assets costing less than $10,000, as well as a single pool for remaining depreciating assets.[10]

8.14 The measures are expected to cost $2.3 billion over the forward estimates ($1.16 billion in 2013–14 and $1.14 billion in 2014–15).[11]

Accelerated initial deductions for motor vehicles

8.15 Schedule 3 seeks to amend the ITAA 1997 to allow small businesses to claim an accelerated initial deduction for motor vehicles acquired from 2012–13 onwards. Small businesses purchasing a motor vehicle will be able to write-off up to $5,000 of its value immediately and, following the amendments made by schedule 2, will then be able to depreciate any remaining value at 15 per cent for the first year and 30 per cent in other years.

8.16 The measures are expected to cost $350 million over the forward estimates ($200 million in 2013–14 and $150 million in 2014–15).[12]

Submitters' views

8.17 Few submissions commented on the amendments contained in schedules 1, 2 and 3 to the Stronger, Fairer, Simpler Bill. The National Farmers' Federation (NFF) submitted:

> While most farm capital expense items will cost well in excess of the designated threshold, the NFF is positive about the proposal to allow small farm businesses to access improved depreciation write-downs of assets such as fencing, sheds and other capital works worth less than $6,500. We acknowledge that cars are an exception and the first $5,000 can be written off in depreciation, regardless of whether the asset is valued at a higher amount … The NFF also welcomes the administrative benefits of allowing for the write-off all other assets (except for buildings) in a single depreciation pool at a rate of 30 per cent (15 per cent in the first year).[13]

Committee view

8.18 While the mining boom can have benefits for the entire economy, it has also helped facilitate challenging operating environments for many other businesses within the two-speed economy.

10 Australia's Future Tax System Review, *Report to the Treasurer*, part 2: detailed analysis, vol. 1, December 2009, p. 173.

11 Tax Laws Amendment (Stronger, Fairer, Simpler and Other Measures) Bill 2011, *Revised Explanatory Memorandum*, p. 4.

12 Tax Laws Amendment (Stronger, Fairer, Simpler and Other Measures) Bill 2011, *Revised Explanatory Memorandum*, p. 5.

13 National Farmers' Federation, *Submission 19*, p. 3.

8.19 Revenue from the MRRT will allow some of the benefits of the mining boom to be invested in the broader economy by improving conditions for businesses operating in other sectors. Increasing the small business instant asset write-off threshold and allowing for simplified asset depreciation will assist many small businesses throughout the country. The removal of the entrepreneurs' tax offset, which acts as a disincentive for small businesses to grow, is a sensible proposal that will also be of overall benefit to small businesses.

8.20 The committee believes these measures to help small businesses should be supported by the Senate.

Senator Mark Bishop
Chair