To eliminate 'negative gearing' for rental properties, introduce a depreciation allowance for newly constructed rented residential accommodation, to ensure that sums received from the sale of future income rights are treated as income, to establish an airline profits tax agreement with the People's Republic of China, to allow greater self-assessment of tax liability and to close a loophole in the ACT payroll tax laws.

The measures to be introduced by this Bill have been announced at various times since July 1985. The decision to remove negative gearing - that is where the interest on a rented property exceeds the income from the property and the excess is deducted from other income - from rented domestic premises was announced on 17 July 1985 and will apply to investments made after that day. On the same day, it was announced that a 4% depreciation allowance would be introduced for residential buildings constructed after 17 July 1985. In the Second Reading Speech for this Bill, the Minister Assisting the Treasurer estimated that the elimination of negative gearing for rented domestic premises will raise $55 million in 1986-87 and $100 million in 1987-88. It was also estimated that the extension of the depreciation allowance to rented residential premises would cost $2 million in 1986-87 and $7 million in 1987-88.[1]

The decision to legislate on the sale of future income rights follows the decision of the Federal Court in FCT v Myer Emporium Ltd (85 ATC 4601). In this case the
court decided that the sum received for the sale of a right to future income was capital and, as such, not taxable under the Income Tax Assessment Act 1936. The intention to legislate to overcome this decision was announced on 9 October 1985.

An agreement to avoid the double taxation of profits made by QANTAS and the Chinese national airline CAAC, was signed in Beijing on 22 November 1985. In a Press Release dated 24 November 1985 the Treasurer announced that legislation would be introduced to give effect to the agreement.

As the ACT payroll tax laws currently stand it is possible for employers to split their operations so that each separate entity can take advantage of the payroll exemptions which phase out at $325,000. In a Press Release by the Treasurer dated 26 July 1985 it was announced that the legislation would be amended to close this loophole. In the Press Release it was estimated that such practices were costing $7 million per annum.

Main Provisions

For a detailed analysis of the clauses of the Bill refer to the Explanatory Memorandum.

Income Tax Assessment Act 1936

This Act will be amended by Part II of the Bill (clauses 3 to 26).

Clause 11 will insert a new Sub-division G into Division 3 of Part III of the Act to remove negative gearing for rented residential property.

Proposed section 82KZC defines a number of terms used in the Sub-division and defines the commencement date as 17 July 1985.

A deduction for rental property loan interest incurred after the commencement date will only be allowed where the income from that property exceeds the eligible deductions in the year of income. Where this is the case, deductions will be limited to the amount of the excess (proposed section 82KZD).

Where the amount of interest paid exceeds the excess, the amount that cannot be claimed as a deduction in
that year will be carried forward and may be deducted from the rental property income in future years (proposed section 82KZE).

Proposed section 82KZF will allow the interest that cannot be deducted to be transferred between resident companies that form part of a group as defined in section 80G of the Act. The amount that may be transferred will be limited to the amount that will balance the transferee companies rental property account (i.e., transferred interest will only be able to be deducted from rental property income).

Property will be deemed to have been acquired, and so the interest obligation incurred, when there is a change in the majority underlying interests in the property between 26 September 1985 and the end of the year of income. Majority underlying interest is defined to mean more than 50% of the beneficial right to the property or the income. Subject to this rule, where property is acquired between 17 June and 26 September 1985 by reason of the death of another, the property will be deemed to have been acquired when the deceased acquired it (proposed section 82KZL).

Clauses 12 to 15 deal with the transfer of rights to receive future income. The current rules which treat income from a transferred right to receive income as income in the transferor's hands where the right to the income was transferred for less than seven years and the interest in the property was not transferred, will be amended. As a result of the amendments, this rule will only apply to transfers between associates for a sum less than would be received in an arms length transaction (clause 14 which will amend section 102B of the Principal Act).

Where a right to receive income arising from the ownership of an interest in property is transferred for consideration, and the property is not also transferred, that consideration will be included in the income of the transferor (clause 15 which will insert a new section 102CA into the Act). These amendments will apply to transfers made after 9 October 1985 other than transfers pursuant to a contract made on or before 9 October 1985 (sub-clause 25(5)).

Clauses 16 to 18 will extend the depreciation allowance to recently constructed accommodation. Clause 17 contains a number of interpretation provisions that define such matters as when a building will be taken to be used for
rented residential accommodation. New sub-sections 124ZG(2A) and 124ZG(2B) will be inserted into the Act by clause 18. Under the new provisions capital spent after 17 July 1985 on building, altering, extending or improving accommodation that is to be used to produce income will be subject to the normal building depreciation provisions (i.e., generally at 4% p.a. over 25 years). If only part of the building is used to produce income, only the expenditure relating to that part will be depreciable.

Clauses 19 to 24 will facilitate the introduction of greater self-assessment. A new section 169A will be inserted into the Act to allow the Commissioner to rely solely on the information supplied in a return when making an assessment (clause 19). Section 170 of the Act, which deals with the circumstances when the Commissioner may amend an assessment, will be amended to allow the Commissioner to alter returns to correct errors of law (clause 20). Where an amended assessment increases the amount of tax payable and the taxpayer is not subject to penalty tax, the taxpayer will be liable to pay interest at the rate specified in the Taxation (Interest on Overpayments) Act 1983. The Commissioner will have power to remit all or part of the interest payable (clause 21).

Income Tax (International Agreements) Act 1953

This Act will be amended by clauses 28 and 29 to incorporate the agreement with the People's Republic of China to avoid double taxation of airline profits. The agreement appears as a Schedule to this Bill.

Pay-roll Tax (Territories) Assessment Act 1971

Part IV of this Bill (clauses 31 to 41) will amend this Act to introduce grouping provisions for certain employers.

Clause 37 will insert a new Part IVA, titled Grouping Provisions, into the Act. The major features of the proposed Part are:

- the formula for calculating the 'deductible amount' is contained in proposed section 21A and is based on, amongst other items, the total wages paid by the group, the annual exemption level and the number of days in the relevant financial year;
companies will be considered part of a group if they constitute a group for the purposes of the Companies Act 1981 (proposed section 21B); where employees are shared (proposed section 21C) or where there is common control (proposed section 21D);

the Commissioner will have a discretion to exclude people from groups, though this discretion cannot be exercised where companies are considered to be part of a group by virtue of the Companies Act 1981 (proposed section 21F);

groups will be able to designate one employer as the designated group employer (proposed section 21G); and

the formula for calculating the amount that may be deducted by the nominated group employer and is based on the annual exemption level (proposed section 21H).

**Taxation (Interest on Overpayments) Act 1983**

This Act will be amended to allow interest to be paid by the Commissioner where the Commissioner decides to reduce the tax payable other than at the taxpayers request or as a result of another amended assessment where the amendment was at the taxpayers request (clause 45).

The amendments will apply to assessments for the 1985/86 and subsequent tax years (clause 47) and form part of the self-assessment provisions.

For further information, if required, contact the Economics and Commerce Group.
Reference