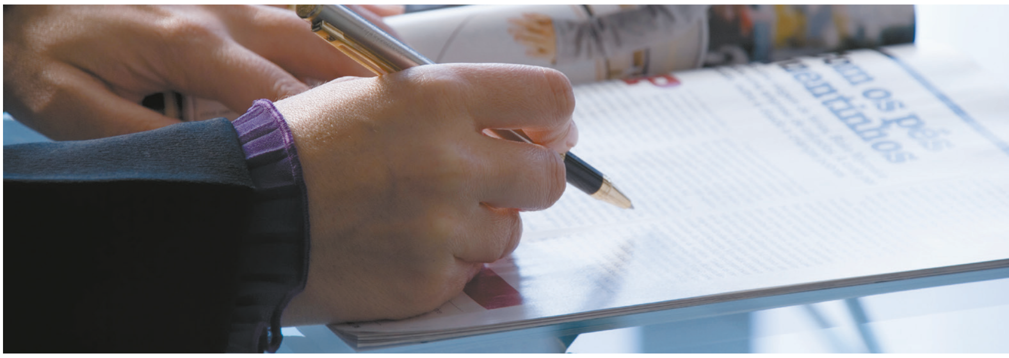

TECHNICAL UPDATE

MYEFO 2014/15 – FEDERAL BUDGET DEFICIT BLOWS OUT FROM $29B TO $40B

THE OVERALL OUTLOOK IS FOR A REVISED BUDGET DEFICIT FOR THE 2014-15 YEAR FROM $29.8 BILLION TO $40.4 BILLION. THE INCREASED DEFICIT IS THE PRODUCT OF FALLING FEDERAL REVENUES, FALLING COMMODITY PRICES AND THE FAILURE OF THE SENATE TO PASS EXPENDITURE CUTS ANNOUNCED IN THE MAY BUDGET.

There are a number of expenditure announcements in the Statement, most notably, a reduction of $3.7 billion from the Foreign Aid Budget over the next three years. In addition, 175 government bodies will be dissolved or amalgamated to take advantage of synergies and to reduce administration costs.

There are a small number of revenue measures that have been announced either through the statement or announced by the Government since the May Federal Budget.

They key revenue announcements include:

- An extension to the statutory effective life of in-house software
- A deferral of the commencement date for the removal of the R&D tax incentive for companies with annual aggregated assessable income of $20 billion or more
- A decision to not proceed with proposed amendments to the interest deductibility rules for multi nationals in relation to provisions that were to be targeted to address conduit arrangements
- Tax concessions for employee share option schemes.

There was also a decision to freeze the level of Family Tax Benefit payments and certain Government benefits at current levels for an additional year.

In-house software depreciation

The Government announced an increase in the statutory effective life for in-house computer software.

In-house computer software is computer software that has been acquired by or developed for use by a taxpayer, including situations where taxpayers acquire the right to use computer software. The software must be acquired or developed for the exclusive use of the taxpayer within their business, and not for resale.

SECTOR

Tax

CONTACT

MARCUS LEONARD
National Leader, Tax
Tel: +61 2 9240 9771
marcus.leonard@bdo.com.au

LISA PRITCHARD
Partner, Adelaide
Tel: +61 8 7421 1418
lisa.pritchard@bdo.com.au

MARK MOLESWORTH
Partner, Brisbane
Tel: +61 7 3237 5999
mark.molesworth@bdo.com.au

ERIC OLUFSON
Partner, Cairns
Tel: +61 7 4046 0000
eric.olufson@bdo.com.au

MAL SCIACCA
Partner, Darwin
Tel: +61 8 8981 7066
mal.sciacca@bdo.com.au

BRETT SKIRVING
Partner, Hobart
Tel: +61 3 6234 2499
brett.skirving@bdo.com.au

DAVID BLAKE
Partner, Melbourne
Tel: +61 3 9603 1709
david.blake@bdo.com.au

JAMES MASSIE-TAYLOR
Partner, Perth
Tel: +61 8 6382 4600
james.massie-taylor@bdo.com.au

Currently, the statutory life for in-house computer software is four years, resulting in a prime cost depreciation rate of 25%. Under the Government announcement, any in-house software acquired or developed (eligible for depreciation) on or after 1 July 2015 will have a statutory effective life of five years, resulting in a prime cost depreciation rate of 20%.

Adjustments will also be made where the costs of in-house computer software have been allocated to software development pools on or after 1 July 2015.

Removal of Research and Development (R&D) tax incentive from large companies to be delayed 12 months

The R&D tax incentive provides tax offsets to companies that incur certain R&D expenditure. For companies with an aggregated turnover of $20 million or more, this is in the form of a 38.5% non-refundable tax offset (reduced from a 40% rate for income years commencing on or after 1 July 2014).

As part of the 2013-14 Federal Budget, the former Federal Government announced the removal of the incentive for companies with annual aggregated assessable income of $20 billion or more. This was to start from 1 July 2013.

As part of the 2014-15 MYEFO the start date for such removal has been extended to 1 July 2014. This represents an estimated extra cost for the budget of $300 million.

Targeted anti avoidance arrangements for interest expense deductions for multi nationals will not proceed

In the 2013-14 Federal Budget the previous Government announced various changes to the deductibility of interest expenses for multi national enterprises including the repeal of section 25-90, which allows Australian companies to claim tax deductions for interest expenses on borrowings to acquire non-portfolio shares in foreign companies that pay non taxable dividends.

While section 25-90 appears to be incongruous by allowing tax deductions for expenses incurred in gaining non-taxable income, it was introduced as part of the expansion of the Thin Capitalisation measures in 2001 that meant Australian entities became subject to the thin capitalisation rules that had the potential of limiting their tax deductions for interest expenses. Section 25-90 was introduced as a trade off against this expansion of the Thin Capitalisation rules.

The current Government announced in November 2013 that it would not be progressing with the repeal of section 25-90 but instead would consult with industry on the possible introduction of a targeted anti-avoidance measure to deal with perceived manipulation of section 25-90. Following this consultation the Government has now decided this targeted anti-avoidance measure is not required because there is sufficient flexibility in the existing Thin Capitalisation safe harbour limits to cover this issue. The Government considers there will be no cost or revenue from abandoning this measure.

Employee Share Schemes

The Government has confirmed its previous announcement that the taxing point for employee share options issued at a discount will be the date the options are exercised (when shares are acquired). In addition, for start up companies, options issued at a small discount (15% or less) the tax will not be paid until the shares are sold and will be taxed under CGT rather than as income. These new rules will apply from 1 July 2015

Rates of Family Tax Benefit

In the 2014-15 Federal Budget, the Government announced that the payment rates for Family Tax Benefit A and B would be frozen until 1 July 2016. This is because there would be a pause on indexation for those rates for two years from 1 July 2014.

In the 2014-15 MYEFO the Government has announced that the current maximum and base rates of Family Tax Benefit will be maintained for an additional year from 1 July 2016 to 1 July 2017.

Eligibility Thresholds for Australian Government Benefit Payments

In the 2014-15 Federal Budget, the Government announced that the current eligibility thresholds for various Government benefit payments would be frozen until 1 July 2017. This is because there would be a pause on indexation for income thresholds for 3 years from 1 July 2014.

In the 2014-15 MYEFO the Government has announced that the current eligibility thresholds will be maintained for an additional year from 1 July 2017 to 1 July 2018.

Affected payments include Family Tax Benefit, Newstart Allowance and Parenting Payments.

Eligibility thresholds for pension and pension related payments, and the Child Care Benefit and Child Care Rebate will not be affected by this measure.

BDO Comment

The 2014/15 MYEFO is surprisingly low on tax changes. Given the dramatic increase in the budget deficit from $29.8 billion to $40.4 billion, it could have been expected the Government would be looking to fill the hole with additional taxation. We are pleased to see the Government has not taken this approach and has accepted that we may need budget deficits for a few more years yet to assist the recovery of the Australian economy.

Given the weakening of commodity prices and the reduction in China's growth rate, Australia needs to take care in relation to the economy. We encourage all sides of the Australian politics to see the long-term needs for the economy and introduce and pass rational measures to support the health of the Australian economy, society and environment.

National expertise

The BDO Tax team is one of the largest and most dynamic tax practices in Australia, with 27 partners and more than 150 specialists located in each major city across the country.

MORE INFORMATION

1300 138 991

www.bdo.com.au

NEW SOUTH WALES
NORTHERN TERRITORY
QUEENSLAND
SOUTH AUSTRALIA
TASMANIA
VICTORIA
WESTERN AUSTRALIA