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SUBJECT: Treasury Laws (Enterprise Tax Plan Base Rate Entities) Bill 2017

CPA Australia represents the diverse interests of more than 160,000 members in 118 countries. Our vision is to make CPA Australia the global accountancy designation for strategic business leaders. Against this background, and in the public interest, our organisation provides the following comments

Overall the exposure draft materials well reflect the necessary legislative changes required to give effect to the government's policy intent in this area. Also, the 80 per cent assessable test is unobjectionable.

However, there are a number of issues that require consideration and clarification either in the draft provisions, the draft explanatory memorandum or by way of ATO guidance.

The issues identified as requiring clarification (in no particular order) are as follows:

- We note that 'business' is defined in s995(1)(1) of the *Income Tax Assessment Act 1997*.[1] However, 'carrying on a business' is still awaiting definition. Case law and footnote 3 from TR2017/D2 provides no more than guidance. However, we acknowledge that the ATO is working on providing market guidance on this key issue in the near future.
- 'Active' vs 'passive' are not defined in principle. Passive is 'base rate passive income' as specific items listed in section 23AB. However, there are situations where such a prescriptive approach could lead to an unreasonable outcome. For example, an IT company may be receiving income which is technically a royalty, but in a business sense it is active income - especially if ongoing services are linked.
- The requirement to trace through partnerships and trusts is a technical necessity. But it is too vague to be workable, relying on 'attribution' in section 23AB(f). The experience of 1985-1986 on negative gearing quarantining demonstrated that the necessary 'look through' provisions were impractical, too costly to enforce and ineffectively constructed.
- Also regarding the tracing through partnerships, trusts and companies – in the most vanilla structures this should be possible – however, in a self-assessment system what is the mechanism to ensure all companies, partnerships and trusts actually do the tracing? This needs to be fleshed out.
- How will the proposed provisions apply to investment businesses? Consider a business that actively trades put and call options, and/ or cum/ ex dividend share trading? In this type of business there is a likelihood that there will be significant dividend and interest income. Is it all active income, or a mix of active and passive income? To be able to determine the split is essential.
- The need for a Commissioner's discretion rule – there will be situations arising where a taxpayer who is running a business that would normally pass the 80 per cent test may fail due to an extraordinary event.

One example is a primary production business - where due to seasonal conditions such as drought the entity has nil active income in any given year. However, the entity may still receive passive income – such as interest on a farm management deposit, or other passive income. These business entities

[1] ***"business"*** includes any profession, trade, employment, vocation or calling, but does not include occupation as an employee.

may, for circumstances largely outside their control, fall under or over the 80 per cent threshold from year to year.

A second example where an active business that would normally pass the 80 per cent test may fail due to an extraordinary event- for example receiving an extraordinary dividend, or even making a capital gain from a share buyback.

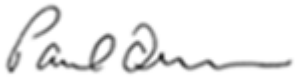
A third example where an active business that would normally pass the 80 per cent test may fail due to an extraordinary event is a business impacted by a disaster or personal circumstances such as illness or death of the small business owner. Such companies may for a short period of time stop receiving active income because they cannot trade, however they could still be receiving passive income such as rent or dividends.

There are many other similar examples where a windfall gain could lead to an anomalous outcome in any given year.

Given these scenarios and on equity grounds we encourage the government to consider including an appropriate Commissioner's discretion in these draft provisions as a mechanism to address these and other anomalous outcomes where a company may temporarily breach the 80 per cent test.

Should you have any questions regarding this submission, please do not hesitate to contact me on (03) 9606 9701 or at paul.drum@cpaaustralia.com.au.

Yours sincerely



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