Growing the Business of Farming | NSW Farmers Association

Farm Tax Implications – Proposed Changes to Non-Commercial Loan Legislation

Issue

In the 2009-10 Federal Budget, the Australian Government announced its intention to introduce new legislation to prevent shareholders and their associates avoiding tax on the use of company assets such as land, cars, boats and houses.

If enacted, farmland that is owned by a private company will be unintentionally caught by the legislation. This may have financial and administrative consequences for the farming sector, with a deemed market rental paid on the company asset, which is taxable in the hands of the company.

Background

Many family farms use corporate structures to hold assets, with a separate entity, often comprising the same family members as the company shareholders, operating the farm trading enterprise. These arrangements have often functioned with no formal lease agreement or payment between the asset owning company and the trading entity. Implicit in this arrangement, however, is a “license” to use the land asset. If the proposed legislation is passed in its current form “licenses” will, for tax purposes, be treated as a lease.

On 12 May 2009, the Federal Treasurer, the Hon Wayne Swan MP, issued a media release outlining initiatives aimed at ‘improving fairness and integrity in the tax system’. One initiative announced is an extension to the non-commercial loan rules in Division 7A of the Income Tax Assessment Act 1936, whereby shareholders (or their associates) will no longer be permitted to use a company asset such as land or a car for free or at a discounted rate.

According to the ATO, granting a lease to a shareholder to use company property has always been caught by Division 7A Part III of the *Income Tax Assessment Act 1936* while licenses have not. The proposed legislation will extend the Division 7A provisions to cover licenses. As such, licenses to use company assets will be considered leases and charged at a deemed market rate. Licenses in the hands of the company will, therefore, be treated as taxable income.

Concerns with the Proposed Changes

The Association is extremely concerned that the proposed legislation will inadvertently capture bona-fide primary production business assets, when clearly the legislation is aimed at closing a loophole that enables shareholders or associates to utilise luxury company assets tax-free.

The Treasury Department will shortly release a discussion paper on the proposed amendments to Division 7A. The Association will be making a submission to strongly voice its concerns and contacting Members on both sides of Parliament to highlight the unintended consequences of the proposed legislation. The Government has advised the Association that it won’t be enacting the proposed legislation without consulting with industry first.

The Association, in consultation with legal counsel, proposes an amendment to the foreshadowed legislation, “carving out” an exclusion clause for legitimate business assets.

The amendment, which will be the cornerstone of the submission to Treasury, is as follows:

"The proposed changes to Division 7A of Part III ITAA 1936 should not apply to business assets owned by a private company that are used exclusively in a business operated by a shareholder in the private company or an associate of such a shareholder".