Div 293 tax (changes 15% tax rate on first $25K to 30%)

Taxable contributions

- The tax is imposed on the individual's taxable contributions at the rate of 15% (s 4 SSSCCIA)
    - Practical effect: a high-income earner's concessional contributions are effectively taxed at an overall rate of 30% rather than merely the contributions tax rate of 15%
- Taxable contributions:
    - Taxable income (assessable income – deductions) + SF contributions
    - Div 293 tax payable where sum of TP's 'low tax contributions' and 'income for surcharge purposes' for the year exceeds $250,000 (s 293-20)
- Division 293 tax is not deductible (s 26-98 ITAA97)
- If person's concessional contributions are less than threshold, but income exceeds threshold, Div 293 tax only applies to the part of contribution that exceeds threshold

Example: Covering concessional, non-concessional and Div 293 tax
MF made a $500,000 contribution to fund. $100,000 was given with notice to SF of concession. $400,000 is therefore non-concessional.

Concessional: $25,000 is tax-free. Individual is assessable on excess $75,000, taxed at marginal rate.
They will receive a tax offset (s 219-15) of 15% x $75,000, and assessable tax rate on $75,000.
In addition, if MF earned over $250,000, also needs to pay Div 293 tax of 15% on the $25,000.

Non-concessional: assuming no previous non-concessional carry forwards. Excess non-concessional is $100,000. If MF does not withdraw with excess they will pay 47% tax on $100,000 contribution, and fund will pay 15% tax. If MF does withdraw then MF gets full $100,000 back and also 85% of associated earnings back which will be taxed at taxpayer's marginal rate. This will be in addition to a tax offset of $15% on earnings; to reverse tax paid by SF, 292-30

Taxation of Super Funds

Tax rates:

- Low tax component: 15%
- Non-arms length component: 47%
- No-TFN contributions income: 34% (i.e. 15% + 34% = 49%)
    - I.e. if TP doesn't provide TFN, taxed at a higher rate
- Non-complying super entities: 47%

Contributions tax: SFs pay tax on assessable contributions; which are included in assessable income

Taxable income: taxable income includes assessable contributions

Imputation system (Part 3-6 ITAA97 (Div 200 to 220)

- Applies to all 'corporate tax entities'
    - Defined as a 'company', a 'corporate limited partnership', or a 'public trading trust' (s 960-115 ITAA97)
- Franking credits generally:
    - Included in resident shareholder's assessable income (s 207-20(1))
    - Give rise to tax offsets for resident shareholders (s 207-20(2))
        - This will always be the same amount as s 207-20(1)

Residency requirement

- [Company] satisfies the 'residency requirement' (s 205-25(a)) at the time it made a distribution as it was an Australian resident at the time (s 202-20)

Main franking entries

Franking credits

- The circumstances in which corporate tax entities generate franking credits in their franking accounts are set out in the table in s 205-15
- Main situations in which franking credits arise:
    - Payment of tax or PAYG instalment
    - Receipt of franked distribution
    - Liability to franking deficit tax

Franking debits

- The circumstances in which corporate tax entities generate franking credits in their franking accounts are set out in the table in s 205-30
- Main situations in which franking debits arise (s 205-30):
    - Payment of franked distribution
    - Receipt of tax refund
    - Underfranking of distribution
    - Anti-avoidance provisions apply

Dividend must be a 'frankable distribution' (s 202-40)

- A 'frankable distribution' is a distribution that is not 'unfrankable' (s 202-40)

Unfrankable distributions

- A distribution is 'unfrankable' if it falls within s 202-45, for example:
    - (e) Distributions from share capital account
    - (g) Deemed dividends under s 109 or Div 7A
    - (i) 'Demerger dividends'
    - (d) Distributions in respect of 'non-equity' shares

Fully franked dividend

- Cannot exceed the 'maximum franking credit' for the distribution (s 202-60, s 202-65)
- The maximum franking credit for a distribution is calculated according to the formula in s 202-60(2):
    - Maximum franking credit = amount of the frankable distribution (dividend) x gross up rate

Franking credit calculation (used to calculate **step 2**) – s 202-60(2)

For most companies:

$$= \frac{\text{corporate tax rate } (0.3)}{1 - \text{corporate tax rate } (0.3) = 0.7}$$

- Applicable gross-up rate is 0.3 / 0.7 which is 0.42857

For base rate entities:

$$= \frac{\text{BRE tax rate } (0.275)}{1 - \text{BRE tax rate}(0.275)}$$

- Applicable gross-up rate is 0.275 / 0.725 which is 0.3793

Partially franked distribution

- The 'unfranked part' of a distribution is the distribution less the 'franked part'
- The 'franked part' of the distributions is currently calculated as follows:

$$\text{Partially franked credits} = \% \text{ franked (e.g. } 70\% \text{ x } \mathbf{2} *)$$

* Step two, see below

Distribution statement

- Generally, this must be provided by a corporate tax entity to its members on or before the day it pays dividends (s 202-75)

Benchmark rule

- All distributions within the franking period must be franked to the same extent (s 203-25)
- This rule is designed to prevent companies from streaming franking credits to SHs who can benefit most from them (i.e. an avoidance provision)

Preconditions

- Failure to meet these means cannot include franking credit in assessable income or get tax offset

Residency requirement

- SubDiv 207-C provides that the gross-up and credit mechanism does not apply to individual or company unless entity satisfies the 'residency requirement' (207-70)
- This will be satisfied where individual or company is a resident at time distribution is made 207-75(1), or for a non-resident at the time distribution is made the entity carries out business in Australia (207-75(2))

Exempt entity rules

- Gross up and credit rules do not apply to franked distributions that are exempt income NANE income of an entity (207-90, 95)
- This operates subject to SubDiv 207-E which allows a 'exempt institution that is eligible for a refund' to benefit from franking credits 207-110 (e.g. Monash, charity)

Anti-avoidance rules

- SubDiv 207-F provides that the gross up and credit rules do not apply where imputation system has been manipulated
- Example: entity is not a 'qualified person' in relation to distribution (i.e. where the entity has not held the shares for at least 45 days) (207-145(1)(a))
- Holding period rule:
    - To satisfy this rule, entity must hold shares for a minimum period of 45 days (not including day of purchase and day of disposal, so 47 days total)
    - Preference share holders have a period of 90 days

Example

X Co pays a dividend of $700 to each of the following three resident taxpayers. A is an individual subject to tax at 47%. B is a company subject to tax at 30%. C is a complying SF subject to tax at 15%. See table below for 'gross up' and 'credit' mechanism.

	Resident Individual (47%)	**Resident Company (30%*)**	**Complying Super Fund (15%)**
1. Dividend (s 44(1))	$700	$700	$700
2. Franking credit (s 207-20(1)) (1 x 0.42857) - *if fully franked – otherwise see green below*)	$300	$300	$300
3. Taxable income (1 + 2)****	$1,000	$1,000	$1,000
4. Tax (before tax offset) (3 x PTR**) - *don't do this in exam as apply tax rate at the end*	$470	$300	$150
5. Franking tax offset (s 207-20(2)) (2 = 5)	$300	$300	$300
6. Net Tax (or Refund) (4 - 5)	$170	Nil	($150)
7. Net amount received (1 – 6)	$530	N/A***	$850

Nb for **6**: shareholder entitled to a refund if tax offset > tax payable for the income year (s 67-25), as has occurred for complying SF in this example.

Nb for **7**: only do if question asks net amount of dividend received

* Could be 27.5% if BRE

** PTR = personal tax rate

*** As company doesn't receive a dividend

**** Take away any tax losses if relevant

Partially franked credits = % franked (e.g. 70%) x step **2**

Topic fifteen: capital gains tax

Overview

- Capital gains and capital losses can only arise as a result of a 'CGT event' (s 102-20)
- If assessable income is more than CGT gain then CGT gain is reduced to zero (s 118-20(1))

CGT event A1

- Arises where taxpayer 'disposes' of a 'CGT asset' (s 104-10(1))

CGT event will occur when

- Taxpayer disposes of a CGT asset (s 104-10)
  - Occurs where there is a change of beneficial ownership (s 104-10(2))
- Time of event (s 104-10(3) is when –
  - (a) A contract for disposal is entered into, or
  - (b) If no contract, when change of ownership occurs
- Applies to:
  - Assets acquired on or after 20 September 1985 (s 104-10(5))

Sara Lee Household & Body Care (2000) HC

- An American company entered into a 'purchase and sale agreement' in May 1991 to dispose of pharmaceutical businesses operated by its subsidiaries. 'Amendment agreement' entered into in August 1991 increased the sale price of the assets owned by its Australian subsidiary.
- The time of disposal of the Australian subsidiary's assets was in May 1991 as the purchase and sale agreement was the source of the obligation to affect the disposal. It was clear from the terms of the amendment agreement that the parties did not intend to rescind the earlier contract.

When a gain / loss occurs

- A taxpayer makes a capital gain where the 'capital proceeds' from the disposal exceed the asset's 'cost base' (s 104-10(4))
- A taxpayer makes a capital loss where the 'capital proceeds' from the disposal are less than the asset's 'reduced cost base' (s 104-10(4))

CGT event C2

- Arises if ownership of an intangible asset ends by expiry, cancellation or forfeiture etc. (s 104-25(1))
- Examples: a share being redeemed, a debt being discharged, a contract expiring
- Time:
  - When taxpayer enters into the contract that results in the asset ending or, if there is no contract, when the asset ends (s 104-25(2))
  - A lease is taken to have expired even if it is extended or renewed (s 104-25(4))

When a gain / loss occurs

- Capital gain:
  - If capital proceeds are more than the asset's cost base (s 104-25(3))
- Capital loss:
  - If capital proceeds are less than the asset's reduced cost base (s 104-25(3))
- Applies to:
  - Assets acquired on or after 20 September 1985 (s 104-25)

- For leases:
  - A capital loss flowing from the expiry, surrender, forfeiture or assignment of a lease (other than a lease granted for 99 years or more) is disregarded if the lease was not used solely or mainly to produce assessable income (s 118-40)
- Capital gains and capital losses are also generally disregarded where:
  - Rights to acquire shares or units are exercised (s 130-40)
  - Shares or units are acquired by converting a convertible interest (s 130-60)
  - Where an option is exercised (s 134-1)

CGT event G1

- Arises if a company makes a payment to a shareholder in respect of a share (except where CGT event A1 or C2 happens) and some or all of payment is not a dividend under s 47*ITAA36* (s 104-135(1)) and payment not included in SH's assessable income (s 104-135(10)
  - I.e. when a company reduces its share capital account
- Time:
  - When the company makes the payment (s 104-135(1))
- Applies to:
  - Assets acquired on or after 20 September 1985 share (s 104-135(5))

When a gain / loss occurs

- Where non-assessable amount is more than share's cost base, the excess is a capital gain and share's cost base/reduced cost base is reduced to nil (s 104-135(3))
- Where non-assessable amount is not more than share's cost base, the share's cost base / reduced cost base is reduced by such amount (s 104-135(4))

CGT assets - definition (s 108-5(1)

- (a) Defined broadly as 'any kind of property'; or
- (b) 'A legal or equitable right that is not property'
- Property is includes both 'tangible' items and 'intangible' items (Gummow in *Hepples*)

Examples (contained in s 108-5(1)

- Land and buildings; shares in a company and units in a unit trust; options; debts owed to you; a right to enforce a contractual obligation; goodwill; Foreign currency and digital currency (e.g. Bitcoin) (TD 2014/26)

Non-property rights:

- Can be a CGT asset if the right is legal or equitable in nature
- Examples:
  - Amount of money in a bank account as it is a 'chose in action' (*Excellar*)
  - Causes of action or negligence and breach of contract (*Coshott*)
  - Licences or contractual rights
  - C.f. 'know-how' - the ATO considers that mere 'know-how' (i.e. knowledge or information) is not a CT asset as it is neither a form of property nor a legal or equitable right (TD 2000/33)

Not a CGT asset

- Australian currency, when used as a legal tender, is not treated as a CGT asset as it merely serves as a medium of exchange to facilitate a transaction (TD 2002/25)