TAX ALERT

PiperAlderman

Government tightens non-commercial loan rules - two new exemptions announced to benefit rural communities and small business operators

Earlier in the year, the Federal Government announced as part of its Budget that the non-commercial loan rules in Division 7A of the *Income Tax Assessment Act 1936** would be extended to cover circumstances where a shareholder (or their associate) is permitted to use a company asset, such as real estate or a car for free or at a rate that is less than market value.

While fringe benefits tax would apply to the use of such assets by employees or their associates, the same use of the assets by shareholders or their associates who are not emmployee would be tax free. The Government's measure is intended to remove this inconsistent treatment by treating the use of a company asset as a 'payment' made to a shareholder and deeming that 'payment' to be a taxable unfranked dividend.

After public consultation, the Government has added two new features to the measure:

- An "otherwise deductible rule" for certain payments - any "business use" assets (i.e. not for private use) that are provided to a shareholder under a right-to-use or a licence (but not a lease of real property) will be disregarded from the amount of any 'payment' made to shareholders as they will be deemed to be otherwise deductible.

  E.g. 'payments' made to farmer-shareholders that involve the provision of farmland that is owned by their private company for use by a related business entity to conduct their farming business would be disregarded and would therefore not attract a requirement to pay for the use.

  E.g. 'payments' made to hotel operator-shareholders that involve the provision of furniture and fittings in the hotel which are owned by their company, would be disregarded.

- A 'residence' exemption for certain payments - any residence that is an integral part of the business real property and is owned by a private company but is lived in under a right-to-use or a licence as part of the carrying on of the business is disregarded.

  E.g. a residence co-located with a hotel and owned by a private company, which is occupied by the shareholders of that private company.

Please contact a member of the tax team should you require any further explanation.

* Division 7A deems loans to shareholders, former shareholders and their associates to be unfranked dividends received by the shareholders unless the loans comply with strict rules concerning interest rates, term, minimum annual repayments and security.

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