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AUSTRALIA

R&D TAX INCENTIVE UPDATE

Australia's primary innovation support mechanism, the R&D Tax Incentive, provides eligible companies with the opportunity to access cash refunds of up to 43.5% of eligible R&D expenditure.

In its recent budget the Australian government has strengthened its commitment to supporting companies to invest in research and development. The government will encourage companies of all sizes to invest in conducting R&D activity, through increased funding in a range of amendments. This represents a step in the right direction for the Australian innovation and manufacturing community.

Under the newly updated R&D tax incentive, which applies to income years commencing on or after 1 July 2021:

- The R&D expenditure threshold at which the higher R&D offset rate applies is increased from AUD100 million to AUD150 million.
- A refundable R&D tax offset of 18.5 percentage points above the company tax rate will apply to entities with aggregated turnover of less than AUD 20 million.
- The non-refundable R&D tax offset will be based on R&D intensity for entities with aggregated turnover of AUD20 million or more as follows:
  - ✓ 8.5 percentage points above the company tax rate for eligible R&D expenditure up to 2 percent R&D intensity, and
  - ✓ 16.5 percentage points above the company tax rate for eligible R&D expenditure of more than 2 per cent R&D intensity.

Who is eligible?

If your business conducts eligible Research & Development activities and is an Australian company or a foreign owned company with Australian tax residency, then you will be eligible to apply.

Documentation and record-keeping

Detailed evidence is required to prove that a company's activity was conducted in accordance with the eligibility criteria, If insufficient documentation is kept the claims will be rejected. This step is often the reason a company will fail a R&D audit. Many claimants carry on activities but fail to fully document their assessment to an appropriate standard.

R&D activities claimed without sufficient supporting evidence will be found to be unsubstantiated and deemed ineligible.

Tax Planning

For many the new rules will increase the value of the offset. There will however be a small category of claimants that will see the net benefit of their claims reduced. As such companies that currently spend or plan to spend money on R&D activities may want to start planning for the impacts from these changes before they take effect on 1 July 2021.

Expanding overseas

This continued improvement of the initiative has, over the years, made Australia one of the top ten locations for R&D investment in the world. The continuation of an attractive R&D tax incentive scheme further strengthens the raft of benefits afforded to Australian resident companies for both Australian owners and foreign owners looking to expand in Australia.

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INDIA

INDIA GOVERNMENT ABOLISHES DIVIDEND DISTRIBUTION TAX (DDT) & INDIA HAS EXTENDED EQUALISATION LEVY HORIZON TO COVER ECOMMERCE SUPPLY AND SERVICES

1. Government abolishes Dividend Distribution Tax (DDT)

What was DDT?

Dividend Distribution Tax (DDT) is a tax levied on dividends that a company pays to its shareholders out of its profits, DDT is a tax at source, and is deducted at the time the company distributes dividends.

Earlier companies were required to pay DDT at 15 percent grossed up, though including surcharge and cess the effective rate was 20.56 percent.

When and why was it abolished?

The government eliminated the dividend distribution tax that is levied on dividends issued by companies. Dividend income will now be taxed only in the hands of investors as per the tax rate applicable to their income, Finance Minister Nirmala Sitharaman announced in her Union Budget 2020 speech.

It has been argued that the system of levying DDT results in an increased tax burden for investors, especially those who are liable to pay tax at a rate less than the rate of DDT if the dividend income were to be included in their income.

Further, non-availability of credit of DDT to most foreign investors in their home country resulted in a reduced rate of return on equity capital for them.

In order to increase the attractiveness of the Indian Equity Market and to provide relief to a large class of investors, it was proposed to remove the DDT and adopt the classical system of dividend taxation under which the companies would not be required to pay DDT. The dividend is to be taxed only in the hands of the recipients at their applicable rate.

Further, in order to remove the cascading effect, Companies are now allowed deduction for the dividend received by holding company from its subsidiary. The removal of DDT will lead to estimated annual revenue forgone of Rs 25,000 Crore (USD 3.39 Billion).

This move will make India an attractive destination for investment.

Impact of Abolition of DDT

The provisions relating to the abolition of DDT are effective from April 1, 2020.

As per amendments to the Income Tax Act:

Section 115-O of the Income Tax Act, 1961 which talks about the Tax on Distributed profits on domestic companies has been amended vide Finance Act 2020 to abolished the DDT regime for any dividends declared, distributed or paid on or after 1 April 2020 (irrespective of the fact when the profit was generated) and revert to the classical system of taxing dividends at the

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level of shareholders, which was applied before DDT was introduced in 1997. ***Consequently, dividends will be subject to tax in the hands of the shareholders at applicable tax rates for resident shareholders.***

Section 115A of the Income Tax Act, 1961 which talks about the Tax on dividends of foreign companies has also been amended and the words "other than dividends referred to in section 115-O" have been OMITTED and therefore ***dividends will now be taxed at the rate of 20 percent (plus applicable surcharge and cess) in the hands of non- resident shareholders as per this section.*** This rate could be lower if the benefit under the tax treaty is available to such shareholder.

2. India has extended Equalisation Levy horizon to cover Ecommerce supply and services

Background

Equalisation Levy was introduced in India in 2016, with the intention of taxing digital transactions i.e. the income accruing to foreign e-commerce companies from India. It is aimed at taxing business to business(B2B) transactions.

In the past several years, Information Technology has gone through an exponential expansion phase in India and globally. This has led to an increase in the supply and procurement of digital services. Consequently, this has given rise to various new business models, where there is a heavy reliance on digital and telecommunication networks.

As a result, the new business models have come with a set of new tax challenges in terms of nexus, characterization and valuation of data and user contribution. The combination of inadequacy of physical presence based nexus rules in the existing tax treaties and the possibility of taxing such payments as royalty or fee for technical services creates a fertile ground for tax disputes.

To bring in clarity in this regard, the government introduced vide Budget 2016, the Equalisation Levy to give effect to one of the recommendations of the BEPS (Base Erosion and Profit Shifting) Action Plan.

Equilisation Levy Horizon Expansion

The scope of Equalisation Levy has been expanded vide Finance Act 2020 to include Non-Resident E-Commerce operator involved in:

- Online sale of goods owned by the e commerce operator
- Online provision of services provided by the e commerce operator
- Online sale of goods or provision of services facilitated by the e commerce operator;
- Any combination of the above activities

The levy is @ 2%.This levy came into force from April 1, 2020 and shall be applicable on services rendered to

- a person resident in India
- non-resident in specified circumstances and,
- a person who buys goods or services using an IP address located in India

Turnover threshold for non-resident E-commerce operators is Rs 2 crores (USD 271,590) and this 2% equalization levy needs to be deposited by the non-resident E-commerce operators themselves.

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NEW ZEALAND

IT WAS A SEA OF RED!

New Zealand presently holds its general Election every three years (there is a proposal to increase the term to four years), with the 2020 Election held on the 17th October (deferred from its original planned September date due to Covid).

Arguably the result was of no surprise to most New Zealander's, although perhaps not expected was the size of the sea of red for the Labour party, the New Zealand public in essence giving Jacinda and her team a clear mandate to govern alone.

On the taxation front, Labour had, in its pre-Election releases, signaled that they would increase the top marginal personal tax rate to 39% (presently 33% on personal incomes in excess of $70,000), but that no other new taxes or increases to existing tax rates would occur during their next three year term.

To live up to this pre-Election promise, a taxation Bill was introduced under urgency to Parliament on 1st December, and was given the Royal sign-off less than a week later, on the 7th December. As a consequence, those individuals with annual incomes in excess of $180,000, will pay 39% income tax on the excess, from April 1st 2021 (New Zealand has a 31 March income year end).

Accompanying the increase in the top marginal personal tax rate, was increased disclosure obligations for New Zealand complying trusts (foreign trusts have their own specific disclosure regimes). Unlike most jurisdictions, New Zealand classifies trusts on the basis of the tax residence of the settlor. Consequently, if the trust (between the date it was settled and the date of the distribution presently being considered by the trustees) has not had a New Zealand resident settlor at any time, then the trust will be classified as being a foreign trust. A foreign trust is only subject to New Zealand taxation on income that is deemed to be sourced from New Zealand, provided the trust has satisfied the requisite registration and disclosure obligations which now apply (post the release of the Panama papers) to foreign trusts.

An increased disclosure regime was required for New Zealand complying trusts (and non-complying trusts for that matter – those trusts deemed to be neither complying, nor foreign trusts), to enable Inland Revenue (New Zealand's taxing authority) to monitor and ensure that income that may otherwise have been subject to the new 39% rate, was not been sheltered within the trust.

This potential for income sheltering exists, because of the way complying trusts are taxed in New Zealand. Income derived by the trustees in respect of any income year, can be subject to taxation in one of two ways. The trustees (within certain timeframes) can decide to allocate the income, in whole or in part, to beneficiaries of the trust as beneficiary income. Income which is characterized as beneficiary income, is then subject to income tax at the rate that applies to the particular beneficiary (noting that a beneficiary could be an individual, a company or another trust).

Alternatively, any income not allocated by the trustees to the beneficiaries as beneficiary income, is taxed as trustee income, at a flat rate of 33%. The trustee income then forms part of the accumulated funds of the trust, and subsequent distributions of these accumulated funds to New Zealand tax resident beneficiaries, is not subject to further taxation in the beneficiaries hands. Naturally therefore, a potential tax planning opportunity exists, for New Zealand taxpayers to mitigate their personal exposure to the new top tax rate, via the use of their family trust structures.

The new disclosure rules for trusts apply from

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the 2021-22 and later income years (so 31st March 2022 income tax returns for most standard balance date trusts), so I suggest it will be some time yet before we as advisers for our clients will be able to gauge Inland Revenue's approach to the new regime.

The pre-Election promise by Labour, that under a "Jacinda-led Government", no new taxes would be introduced, either means that Jacinda is planning to leave politics in the short-term (perhaps a sibling for Neve is in the pipeline), or that we will in fact have no new taxes introduced for three more years. If this is to be believed (we are dealing with politician promises after all!), then New Zealand will remain absent of having a capital gains tax for a further three years.

In brief, this means that presently you can:

1. Acquire land in New Zealand, and depending on how the acquisition is structured and what you do with the land, potentially dispose of that land at a later time, with no income taxes payable on any gain that you make – although note that there is now a quasi-capital gains tax, whereby residential land sold within five years will be subject to tax on sale unless the land was your main home (the bright-line rules);

2. Acquires shares in both private and public companies, and provided you are not seen to have acquired the shares with any resale intention or purpose, dispose of those shares subsequently, with no income tax payable on any gain you realize; or,

3. Sell your business and not pay income tax on any non-revenue components of the sale price (goodwill, IP assets (except patents) etc).

If you would like to discuss further any of the content of this article, please do not hesitate to reach out to me.

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