Proposed tax changes to Division 7A

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Small to medium businesses are to be affected by proposed tax changes to the Shareholder Loan rules in Division 7A. The changes are expected to apply on 1 July 2019.

Perhaps the most notable proposed change is the introduction of the 10-year loan model to replace the existing 7-year and 25-year loan models. The current rule, first introduced in December 1997, is that if a private company provides a benefit to a shareholder or their associate, the recipient would be taxed as if they were dividends. This is applicable when the loans are funded from profits taxed at the company tax rate.

But there are a number of exceptions to the rule. One is when the value of the benefit is converted to a loan which is considered a complying loan (according to the requirements in Division 7A), and interest charges and principal repayments are made over a 7-year period (for an unsecured loan).

Loans entered before December 1997 are also currently exempted from the general rule but the proposed changes are to see that these previously exempted loans are not only to be subject to division 7A, but also require a 10-year fixed term for repayments. Experts say businesses who have had loan agreements for decades will now be forced to find the money to pay them off faster.

The new loan model will have a variable interest rate and payments of both principal and interest in each income year. The Treasury is still reviewing the policy.

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