PwC Private Clients is a national team of 50 Partners and more than 600 staff who are committed to working with private businesses of all sizes, family businesses, entrepreneurs and high net wealth individuals. We provide support including succession planning, assurance, advisory, taxation and emerging company services to private businesses across all industries and sectors. We work with many of Australia's leading family businesses as well as many of this nation's fast growing companies.

We have prepared the following submission for consideration by the Parliamentary Joint Committee on Corporations and Financial Services inquiry into family businesses in Australia. The submission focuses on the findings of the Spring 2012 PwC Private Clients Family Business survey and the following terms of reference:

4. Structural, cultural, organisational, technological, geographical and governance challenges facing family businesses.

5. The role of family trusts in facilitating family business.

PwC PRIVATE CLIENTS FAMILY BUSINESS SURVEY

During July and August 2012, PwC surveyed close to 2,000 family businesses from around the world, including 50 Australian family businesses. The PwC Private Clients Family Business Survey focuses on key areas including performance, internationalisation, and the unique qualities that set family businesses apart from listed or public companies, with the intention of increasing the availability and reliability of information and statistics about family business in Australia.

The survey supports the positions being put forward in this submission by providing a valuable insight into the current structures, strategies and views of family businesses both within Australia and globally, and the results can be recommended as a timely and accurate snapshot of family businesses in Australia.

Key findings:

- Family businesses' sales have grown less in Australia than the global average over the past financial year, but businesses are bullish about future growth.
- Fifty six per cent have grown over the previous 12 months - compared to 65 per cent globally - and 16 per cent are aiming to grow quickly and aggressively over the next five years.
- The key challenges to growth over the next five years cited are the general economic situation, competition (pricing and the number of competitors), the need to innovate, and attracting the right skills and talent.
- Family businesses believe they hold some key advantages over non-family businesses, including motivation and values within the company, agility and speed of decision making, freedom from bureaucracy, continuity, and the ability to take a longer term view.
- Some disadvantages over non-family businesses are also recognised, including reduced access to capital, family politics, difficulty in attracting non-family people into the business, and challenges around succession.
- Australian family businesses believe they play a vital role in our country's economy; including job creation and adding stability to a balanced economy.
- They generally believe that Government does not recognise the importance of family businesses, and feel more should be done to help, for example, improved access to finance and creating a level playing field for access to some of the advantages enjoyed by (public) corporations.

- Some believe that family businesses will need to float, merge, or adopt more corporate behaviour in order to survive and thrive in the years ahead.
- Almost 40 per cent intend to pass down the business and management to the next generation. The remainder are twice as likely to sell or float than to pass down but employ non-family management.

<See Appendix A: PwC Private Clients Family Business Survey>

All legislative references are to the Income Tax Assessment Act 1997 or the Income Tax Assessment Act 1936 unless otherwise noted.

4. Structural, cultural, organisational, technological, geographical and governance challenges facing family businesses

The rule against perpetuities

Abolishing the rule against perpetuity or introducing a rollover for trusts would prevent the succession issues we encounter with families holding assets in a trust reaching its 80 year limit.

Streaming of private business profits

As a result of a number of integrity rules introduced over the last decade (principally Subdivision 115-C and Subdivision 207-B), the tax rules currently allow trusts to stream income whilst companies are prevented from doing so.

We believe private company shareholders should be afforded the ability to stream franked and unfranked dividends to selected shareholders, provided the streaming of private companies is limited to members of the shareholder's family.

Rollover of assets to discretionary trusts

Currently the tax laws levy income or capital gains tax where an individual transfers an asset to their family trust, as no rollover is available.

We recommend introducing a specific roll-over to disregard any capital gains arising from such transfers provided a valid Family Trust election is in place. The Family Trust election is an integrity measure that penalises those trusts that provide benefits to non family members.

Tax consolidation

The mandatory resetting of a company's cost base in its assets (Division 705) - which occurs when undertaking most corporate restructure - can penalise family groups.

We recommend that the rules be amended to allow family groups to retain their existing cost base.

Further, family groups should have the ability to retrospectively choose to tax consolidate provided this decision is made with the ordinary amendment period of four years currently afforded to such taxpayers.

Management incentives

Many families recognise the need to attract talent from outside the family group. However, Australia's laws can double tax the issue of equity to employees of private companies; that is, the existing shareholders as well as management can suffer income tax.

We recommend that the value shifting laws (Subdivision 104-K) be amended such that they apply in the same manner as they currently apply to large companies.

5. The role of family trusts in facilitating family business

The rule against perpetuities

Trusts are well established vehicles for families to hold assets - which may have been acquired or developed by earlier generations - for the benefit of the family as a whole rather than particular individuals. Trusts can support the financial needs of family members and protect assets should an individual family member face financial difficulties; assets which if lost may threaten the viability of a family's business. Trusts are also a safer, more predictable option for passing assets – including businesses such as farms - down through generations.

With the exception of South Australia, all states impose an 80 year limit on the period during which a trust can exist; legislation which we believe has outlived any current relevance. South Australia removed the automatic imposition of the 80 year limitation on the life of trusts in 2006, while making it possible for beneficiaries to apply for a trust to be terminated if that trust has existed for longer than 80 years.

The termination of a trust can have a serious impact on families and family businesses. When a trust is dissolved, assets must be transferred to a different owner. If the value of the asset is greater than their cost, it precipitates a Capital Gains Tax (CGT) event for the beneficiaries, who may be forced to find up to 46.5 per cent of the assets' value without a liquidity event. This forced taxing point can threaten the viability of the family business.

The 80 year limit on trusts can also impact business decisions and structures before the trust is terminated. If a family is to acquire a major asset and their trust is already 50 years old, it would be unwise of them to place that asset in the existing trust – a vehicle with just 30 years remaining. This will prompt the creation of a new structure to hold the asset, further complicating the family's financial structure and increasing the cost of managing their assets.

For many older existing trusts, abolition of the 80 year rule would remove the need to consider whether changes to deed are a resettlement. We suggest a more appropriate alternative for family businesses would be to abolish the 80 year rule, and permit trusts that include a Family Trust Election to make any deed amendments necessary in order to accommodate the changing and evolving needs of their family.

We believe that to protect the future of Australia's family businesses, Government should consider abolishing the termination date of trusts, thus removing any artificial taxing points. We acknowledge that some changes will require state legislation, but believe this shouldn't preclude the rule against perpetuities from policy discussion.

Trust law rewrite

In a sophisticated economy it is difficult to avoid complexity in tax law. The laws around the calculation of taxable income of trusts (mainly Division 6 and related tax cases, including Bamford's case) are particularly complex - and in some respects antiquated - and we understand that Government is considering rewriting these laws. We agree that this is necessary, but are concerned that the rewrite may be viewed by Treasury as an opportunity to introduce laws that increase the already extensive obligations of trustees.

Division 7A rewrite

Division 7A operates to penalise families who, amongst other things, obtain loans from private businesses whose terms, whilst often commercial, do not comply with other strict requirements of the division - including regular repayment of capital within seven or ten years. In many cases families are forced to borrow from third parties as they usually offer less onerous servicing demands.

This leads to additional costs being born by families and inefficient capital markets within Australia's economy.

We recommend Division 7A be amended so that the rules don't penalise private business borrowing arrangements where either:

1. the borrowing entity is entitled to claim an income tax deduction for servicing such debt - an "otherwise deductible rule"; or

2. the terms relating to such loans are arms' length in nature.

We would also recommend removing the strict requirements that documentation be prepared within certain time frames.

PwC Private Clients is deeply committed to the family business sector. We believe family businesses make a significant contribution to our economy, and see our role as helping owners maximise opportunities today that will enable them to flourish in the future. We would value the opportunity to provide further consultation with our specialist advisors to the family business sector.

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