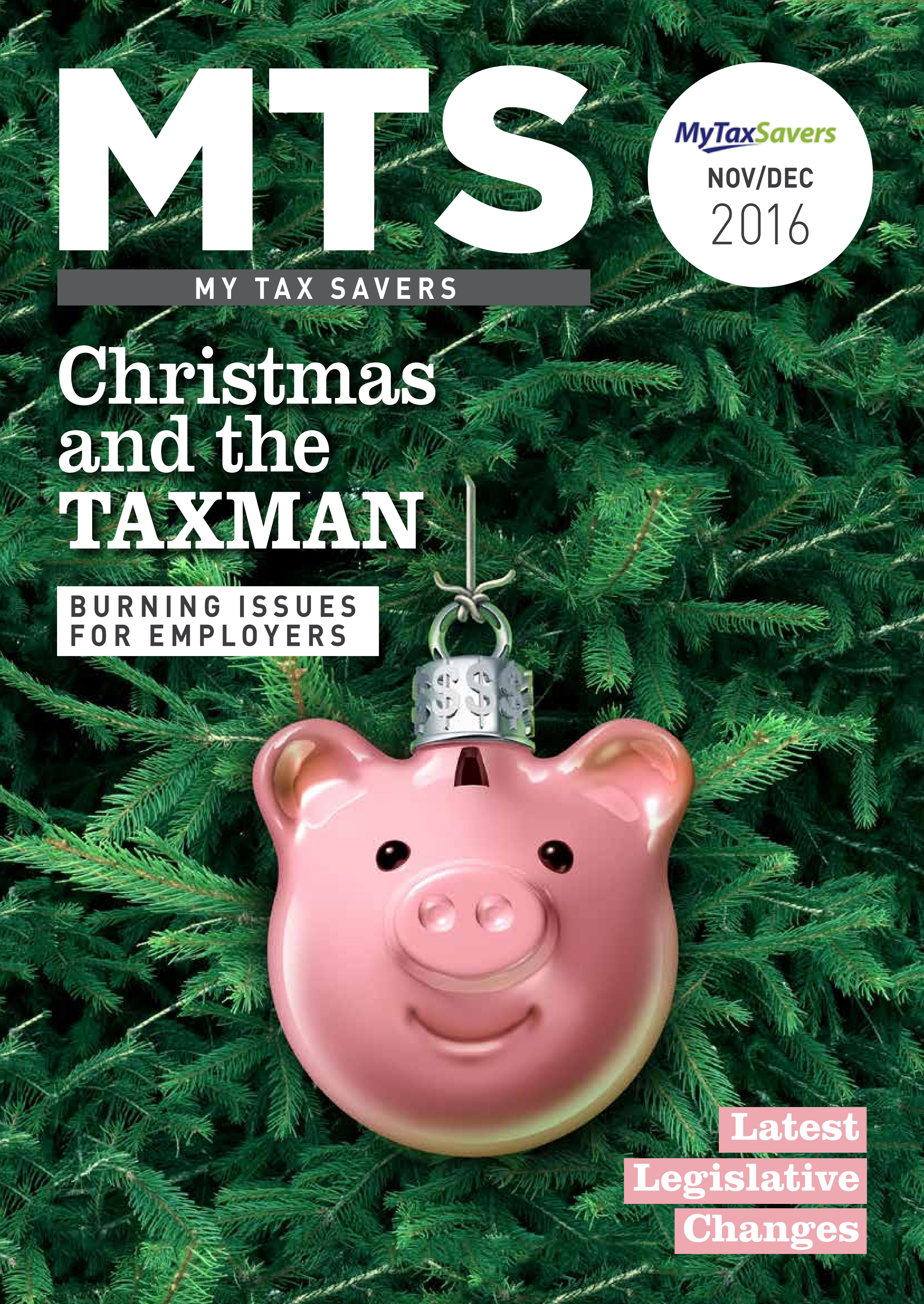
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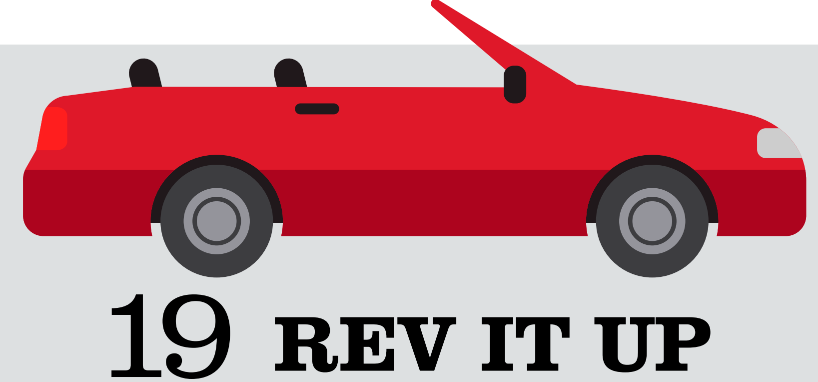

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BURNING ISSUES FOR EMPLOYERS

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Many key dates are looming for business including those relating to Activity Statements, GST, superannuation, income tax returns, and more.

NOVEMBER 2016

11 NOVEMBER
July-September quarterly Activity Statements – due for lodgement and payment (if lodging electronically)

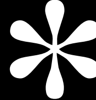
21 NOVEMBER
October monthly Activity Statements – due for lodgement and payment

28 NOVEMBER
Superannuation Guarantee Charge (SGC) Statement – due for lodgement and payment if insufficient contributions or late contributions were made for the July-September quarter by the due date

DECEMBER 2016

1 DECEMBER
Due date for income tax payment for companies that were required to lodge by 31 October

21 DECEMBER
November monthly Activity Statements – due for lodgement and payment



Where the due date falls on a weekend or public holiday, it is deferred until the next business day.

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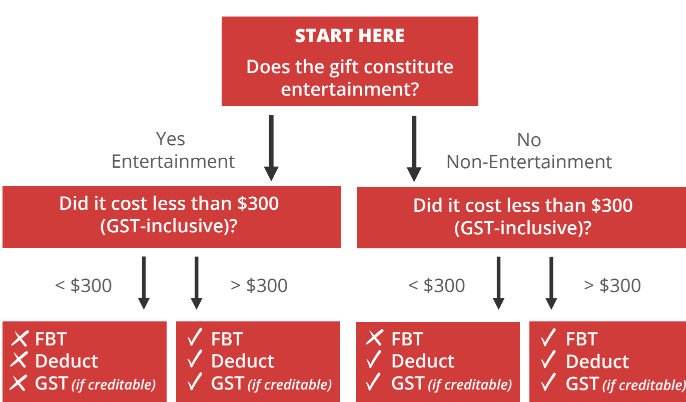
Christmas & THE TAXMAN

Christmas is traditionally a time of giving – including employers showing gratitude towards staff and clients/suppliers for their loyalty throughout the year. With the right approach, it's possible to enjoy some tax benefits out of your generosity, and also avoid Fringe Benefits Tax (FBT). But as always with tax, the landscape is layered with complexity. The following is a general summary of the tax treatment of Christmas giving.

Gifts to Employees and Associates (Spouses)

Before examining the technicalities in this area, the following flowchart provides an overview of the rules. Return to this user-friendly flowchart as and when you need to:

THIS FLOWCHART ALLOWS YOU TO ASSESS THE TAX TREATMENT OF GIFTS PROVIDED TO EMPLOYEES/ ASSOCIATES



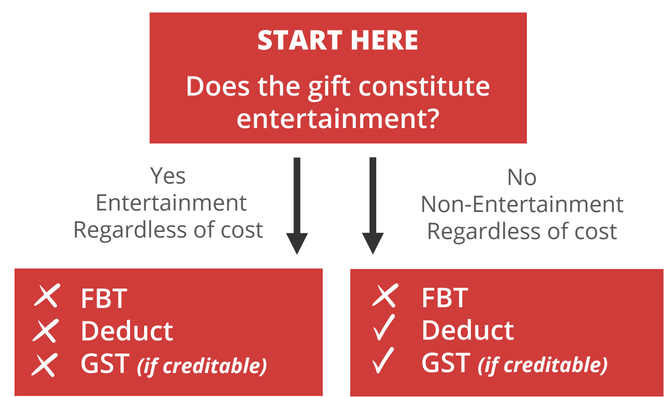
Non-entertainment gifts to staff and associates (such as Christmas hampers, bottles of alcohol, gift vouchers, pen sets etc.), are tax deductible and you can claim GST credits, irrespective of cost. Note however that you can generally avoid paying FBT if you keep the gift under $300. If this threshold is exceeded, FBT will apply. Therefore, be conscious of this threshold when providing such gifts to staff this Christmas.

On the other hand, entertainment gifts to staff and associates (such as tickets to movies/theatre/amusement park/sporting events, holiday airline tickets etc.) which are under $300 will not attract FBT, are not income tax deductible, and you can not claim GST credits. If over $300, FBT will apply, but a tax deduction and GST credits can be claimed. With the FBT rate now at a record high of 49%, the tax deduction and GST credits available is unlikely to provide a better tax outcome than avoiding FBT by keeping the gift under $300.

Gifts to Clients/Contractors/Suppliers/ Customers

Again, before examining the technicalities in this area, the following flowchart provides an overview of the rules.

THIS FLOWCHART ALLOWS YOU TO ASSESS THE TAX TREATMENT OF GIFTS PROVIDED TO CLIENTS/CUSTOMERS



No FBT is payable, irrespective of the type of gift and irrespective of cost. However, where a gift constitutes entertainment, no GST or tax deduction can be claimed. Thus, at least from a tax standpoint, it's better to provide non-entertainment gifts to clients (Christmas hampers, bottles of alcohol, gift vouchers, pen sets) and, in doing so, enjoy a tax deduction and GST credits.

Christmas Parties

Instead of gifts, it's quite common for employers to host a Christmas Party for their staff (often including spouses) at a restaurant.

Where this is the case, the total cost will generally be exempt from FBT provided the per-head cost (dinner and drinks) is kept to under $300 per person. This is known as the Minor Benefits Exemption. To enjoy this exemption the employer must use the Actual Method for valuing FBT meal entertainment. The Actual Method is the default method for valuing meal entertainment, and no formal ATO election is required to use this method. Under the Actual Method, an employer pays FBT (in the absence of an exemption) on all taxable meal entertainment provided to employees and their associates such as spouses (entertainment provided to other parties such as clients, contractors, or suppliers is exempt from FBT). The down-side of using the Minor Benefit Exemption is that the meal entertainment is not tax deductible, and nor can you claim a GST credit.

This Minor Benefit Exemption is not available if you elect to value your meal entertainment under the alternative 50/50 Method. Under this method, you pay FBT on only 50% of all taxable meal entertainment provided to employees, spouses AND third-parties such as clients/contractors/customers etc. irrespective of the cost. Likewise, you can only claim a 50% income tax deduction and 50% GST credits on such meal entertainment. However, as stated earlier, with the FBT rate now at 49%, the 50% tax deduction and 50% GST credits available under the 50/50 Method is unlikely to provide a better after-tax result than the Actual Method where no FBT is payable.

The "take-home message" is that if like many employers the only social functions you host for employees during the year are a Christmas Party (and perhaps the Melbourne Cup), be conscious of keeping the per-head cost under $300. By doing so, you may be able to exempt the entire cost.

Divorce

RELATIONSHIP rollover

According to official statistics, 1 in 3 Australian marriages will end in divorce. Aside from the emotional toll, there can be significant tax consequences unless there is careful management when assets are transferred between the two separating parties following the breakdown of a relationship. This article examines the tax relief that is available for such transfers.

INTRODUCTION

Whether it's acrimonious or cordial, the breakdown of a relationship will usually involve some asset division which may require the legal transfer of assets between the two parties or between related entities and the parties (e.g. from Family Trust to spouse). Without special rules in place, these transfers would likely have capital gains tax (CGT) consequences where the ownership of the asset changes hands. While the most common CGT asset involved is the family home, other CGT assets that could be in play in a relationship breakdown include rental properties, shares, vacant land, commercial property such as buildings/ factories/offices etc. and a variety of other business assets including in some cases the goodwill of a business.

To mitigate what would otherwise be a harsh tax outcome, *Section 126-5* of the Tax Act provides rollover relief from CGT where a CGT asset is transferred to a spouse or former spouse as the result of the breakdown of a relationship. No rollover relief is available where the CGT asset is transferred to an entity e.g. company, trust, deceased estate etc. (Sometimes, for asset protection reasons, parties wish to transfer assets to these entities rather than individuals. Where this is done following a relationship breakdown, no rollover relief is available. This potential capital gain and resulting tax cost needs to be factored in by the parties when negotiations are taking place as to the distribution of assets.).

With the transfer of CGT assets potentially creating large capital gains (or capital losses), it is important to understand and observe the requirements of *Section 126-5* which we now examine.

COURT ORDER OR AGREEMENT

The first important point to note is that rollover relief is only available if the change of ownership happens involving an individual/company/trust (as transferor) transferring an asset to his or her spouse or former spouse (the transferee/recipient) "because of" a relevant court order or specific agreement listed in *Section 126-5* of the Tax Act (including a court order, a maintenance agreement, or a financial agreement made or approved under the relevant provisions of the Family Law Act). The key point is that unless one of these types of formal agreements is struck, then the rollover relief will not be available and thus a capital gain or loss may arise upon transfer. Therefore, it is not sufficient to come to an informal, mutual agreement with your spouse or former spouse if you wish to avail yourself of CGT rollover relief. In order to strike a formal agreement which provides CGT relief, you may need the assistance of your Accountant as well as legal input.

TAX TIP – CAPITAL LOSS

Where the *Section 126-5* conditions are met (including having a formal agreement or court order) the rollover provisions apply automatically to ignore any capital gain or loss at transfer. If you therefore wish to make a capital loss on the transfer of an asset (perhaps to negate or reduce a capital gain that you have made earlier in the financial year) you may wish to transfer that asset without a formal agreement in place in relation to it.

EXAMPLE

Duncan and his wife Rhonda have divorced. As part of the settlement it is agreed that Rhonda (who for asset protection reasons held all of the couple's assets in her name) will transfer one of the couple's rental properties and a small parcel of shares to Duncan. The shares are currently harbouring a $3,000 capital loss.

Earlier in the year, Rhonda had sold some shares and made a capital gain of $5,000.

In order to avail herself of the rollover exemption and therefore avoid a capital gain on the transfer of the rental property to Duncan, Rhonda transfers the property under a formal agreement (listed in *Section 126-5* – see earlier).

However, as she wishes to realise her capital loss on her shares (which will ultimately offset the earlier capital gain) Rhonda does not include the shares as an asset under the formal agreement. She transfers these shares separately.

Note that where a CGT asset is transferred by an informal agreement between spouses and later a court sanctions the transfer, the CGT rollover relief is not available as the transfer is made "because of" the private agreement – not because of a Court order at first instance.

SPOUSE

To enjoy rollover relief, the transfer must be to a "spouse" or "former spouse". Therefore, transfers to deceased estates or other related entities such as companies do not qualify for the rollover. 'Spouse' of an individual includes de facto spouses of the same sex or of different sexes.

CONSEQUENCES OF THE ROLLOVER – TRANSFEROR

The effect of the rollover is that any capital gain or loss that would otherwise arise for the transferor of a CGT asset is disregarded (as distinct from deferred). Because the rollover relief is automatic, no election is required to be made by the transferor – be they either an individual, company or trust.

CONSEQUENCES OF THE ROLLOVER – TRANSFEREE/ RECIPIENT

This will depend on whether the CGT asset being transferred is pre-CGT or post-CGT as follows:

PRE-CGT ASSET

Where the asset was originally acquired before 20 September 1985, the recipient spouse is also taken to have acquired it before that time. Thus, if at some future point the recipient spouse disposes of that asset, there will be no CGT consequences as the asset has retained its pre-CGT exempt status.

POST-CGT ASSET

On the other hand, where the asset being transferred was acquired after 19 September 1985, the recipient spouse will be treated as having acquired that asset for the transferor's "cost base".

EXAMPLE

Assume your spouse transfers post-CGT vacant land to you which was originally purchased for $30,000 but is now worth $100,000.

In simple terms, you will be taken to have inherited the land for $30,000 plus the actual costs of transfer (e.g. conveyancing fees, stamp duty etc.).

TAX TIP

In addition to the purchase price, "cost base" of a CGT asset includes the following elements:

- Incidental Costs of acquiring the asset (consisting of broker/agent/advisor fees, stamp duty etc.)
- Ownership Costs (consisting of costs for maintaining, repairing and insuring the asset, including rates, land tax etc.)
- Enhancement Costs (consisting of capital expenditure to increase or preserve the value of the asset e.g. costs you incurred in successfully applying for zoning changes, capital costs of installing or moving an asset)
- Title Costs (consisting of costs incurred to defend, preserve or establish your rights to the asset).

TRANSFERS OF MAIN RESIDENCES

A partial CGT liability will arise where a transferred dwelling did not qualify as the main residence of both the transferor and the recipient spouse for any part of the ownership period, pre or post transfer.

Prior to this rule being introduced on 12 December 2006, the recipient spouse could avoid any CGT liability when they later disposed of a transferred dwelling, even though the dwelling had not been used prior to the transfer as the transferor's main residence. Now under this relatively new law, the recipient will be taken to have inherited the dwelling at the same time the transferor acquired it, and will be taken to have also inherited their usage of the dwelling. Consequently, upon disposal by the recipient, the usage of the dwelling by both them and their former spouse as transferor will be taken into account when applying the main residence exemption as per the following example:

EXAMPLE

(from the Explanatory Memorandum to the Tax Laws Amendment (2006 Measures No 4) Act)

George and Natalie are each 50% owners of a dwelling that they used as a rental property for 2 years before George transferred his 50% interest to Natalie. The transfer qualifies for the relationship breakdown rollover as it was made under an approved agreement pursuant to the Family Law Act.

Natalie uses the dwelling as her main residence for 4 years from the date of transfer until she sells it.

Natalie is entitled to a 66% main residence exemption on the 50% that she originally owned (representing 4 out 6 years that she occupied the dwelling). She is also entitled to a 66% main residence exemption on the 50% interest owned by George and transferred to her, having regard to how George used the dwelling.

This relatively new rule needs to be taken into account at the property division stage. If a dwelling such as a rental property is being transferred to you and it was not the main residence of your former spouse during their ownership period, then it will have an embedded tax cost by way of a CGT liability when it comes time to sell it. Therefore, when negotiations are taking place as to the distribution of assets you may need to take into account that dwellings such as this may be of lesser real value to you than at first glance.

The good news about inheriting the original acquisition date of the property from the transferor spouse is that should you wish to dispose of the dwelling immediately and turn it into cash, the 50% CGT discount will apply to the whole property, provided your former spouse owned their share for 12 months or more prior to the transfer. There will be no need to defer the sale for 12 months after the transfer.

TRANSFERS OF MAIN RESIDENCE FROM AN ENTITY TO A SPOUSE

The same CGT rollover relief that applies for transfers between spouses also applies for the transfer of assets from a company or trust to a spouse under a formal *Section 126-5* agreement.

In relation to the transfer of a dwelling however, the recipient spouse will be denied a full main residence exemption – even in the case where they lived in the house when it was owned by the company or trust before the transfer. Entities are not entitled to the main residence exemption. A partial main residence exemption will apply if the recipient treats the dwelling as their main residence post-transfer.

IN-SPECIE CONTRIBUTIONS

ASIDE FROM CASH CONTRIBUTIONS, THE OTHER WAY YOU CAN CONTRIBUTE TO SUPERANNUATION IS VIA AN IN-SPECIE CONTRIBUTION OF REAL PROPERTY OR SHARES. THIS ARTICLE EXAMINES THIS TYPE OF CONTRIBUTION, INCLUDING POSSIBLE TAX CONSEQUENCES.

BACKGROUND

Chiefly because of the concessional tax treatment and the desire to provide for retirement, voluntarily contributing to superannuation (over and above the compulsory 9.5% Superannuation Guarantee paid by employers) is still highly popular. From a taxation perspective, earnings on assets (such as dividends and rent) and earnings on cash contributions (i.e. interest) are afforded concessional tax treatment compared to earnings outside of superannuation as illustrated in the following table:

**The Government has proposed to increase this to 15% for earnings on accounts that exceed $1.6 million*

	TAX RATE	
	Inside Superannuation	Outside Superannuation
Investment earnings	15% if account is in accumulation mode 0% if account is in pension mode*	Marginal tax rate**
Capital gains	-15% if account is in accumulation mode (10% if asset is held for more than 12 months) -0% if asset is used to support a pension	Marginal tax rate**

**The marginal tax rate referred to in the above table is your individual marginal tax rate which for 2016/2017 is as follows:

Taxable Income $	2016/2017 Tax Rate (not including Medicare Levy)
0 – 18,200	Nil
18,201 – 37,000	19 cents
37,001 – 87,000	32.5 cents
87,001 – 180,000	37 cents
180,000+	47 cents

As we can see from the tables, unless you earn below $18,200, your marginal tax rate will always be higher than the highest superannuation tax rate of 15%. Therefore the tax imposed on your investment earnings inside superannuation will always be less than that imposed on these earnings outside superannuation (provided you earn more than $18,200).

PROPOSED CHANGES – THEIR IMPACT

In the 2016 Federal Budget which the Government is seeking to pass into law, proposals were announced to increase the earnings tax from tax-free to 15% on:

- Earnings in respect of Transition to Retirement Pensions and
- Earnings in respect of Account-Based Pensions, where the capital in the account exceeds $1.6 million.

Even if these proposals become law, the proposed 15% tax rate on earnings in respect of these pensions is still in most cases less than what you would pay if these earnings were made on money invested outside of superannuation.

QUARANTINING

Aside from the concessional tax rate and providing for your retirement, superannuation assets and savings are protected in the event that you become bankrupt (although Bankruptcy laws in Australia provide trustees with the ability in most cases to claw-back transactions for a period of up to five years where contributions are made with the intent of avoiding creditors). Furthermore, superannuation is not included in the income tests for Centrelink and family payments until you reach Age Pension age, while savings outside of superannuation generally are included.

Because many people lack the spare cash to make a contribution, a popular alternative is to make an in-specie contribution.

WHAT ARE THEY?

In-specie contributions are contributions to superannuation in the form of an asset other than money. The opportunity to make this style of contribution is generally only available if you have an SMSF (provided your SMSF deed permits such a contribution). Most large superannuation funds and commercial funds do not accept in-specie contributions.

In-specie contributions are restricted to two classes of asset - listed securities, and business real property:

LISTED SECURITIES

This includes shares, units, bonds, debentures, options, interests in managed investment schemes or other securities that are listed on an approved stock exchange in the tax regulations including:

- Domestic exchanges (Australian Stock Exchange, the Bendigo Stock Exchange and the National Stock Exchange of Australia)
- Foreign exchanges (those listed in the tax regulations including the New York Stock Exchange, the NASDAQ Stock Exchange, the London Stock Exchange, the Shanghai Stock Exchange, the Singapore Stock Exchange etc.).

Note that shares issued to an SMSF through an Employee Share Scheme (ESS) arrangement for an employee who is a member of the SMSF are considered a personal in-specie contribution (and not an employer contribution). Thus, unless those shares are listed on an approved stock exchange, such transactions are not permissible.

BUSINESS REAL PROPERTY

This means:

- Any freehold or leasehold interest in real property
- Any interest in Crown land, other than a leasehold interest, being an interest that is capable of alignment or transfer, or
- Any class of real property prescribed by the superannuation regulations.

Examples of 'business real property' include land or buildings used wholly or exclusively in a business (e.g. factory, shop, office, farming property, or the land on which they are based). Importantly, as with other SMSF assets, there cannot be a loan or covenant (charge) over the property unless it was acquired under a limited recourse borrowing arrangement.

The second limb of this test - business use - requires that the real property be 'wholly and exclusively' used in one or more businesses. However, the legislation does accommodate scenarios where:

- Most of the property is used for business purposes, while some of it is not used at all
- There is a minor, insignificant non-business use of the property.

What constitutes 'minor or insignificant non-business use' very much depends on the circumstances. In *SMSF* Ruling *SMSFR 2009/1*, the ATO provides an example of a commercial property used as a business office. In an empty room of that office, equipment and miscellaneous personal items of the member are sometimes stored. In that example, the ATO deems the storage to be a "minor and trifling matter". Yet, in a later example in the Ruling, where a member is using 10% of the property for personal storage, the property is not "wholly and exclusively" used in a business – hence it does not qualify as 'business real property'.

In the legislation, relief is provided for primary producers. Real property used in one or more primary production businesses does not cease to be used 'wholly and exclusively' in that business because a portion of the property (not exceeding two hectares) contains a residence which is used for private and domestic purposes i.e. the family home.

Importantly it should be noted that the mere renting out of a property is not considered to be carrying on a business, and thus such property cannot be contributed in-specie to your SMSF.

TAXATION

There are a number of taxation issues around in-specie contributions.

CONCESSIONAL TAX ON EARNINGS AND CGT

Having a property or shares within superannuation is advantageous in two respects. Firstly, any earnings on the assets such as rent or dividends are taxed at 15% (see earlier table) or tax-free if your account is in pension mode. Secondly, any capital gain made on the asset while it is in your SMSF is taxed at just 15% (or effectively 10% if held for more then 12months) or tax-free if your account is in pension mode.

TRANSFER

In-specie contributions to your SMSF ultimately involve a change of ownership of the property or shares – from your name to the name of the SMSF. This disposal may trigger a capital gain in your name; being broadly the difference between what you acquired the asset for, and its market value at the time of transfer into your SMSF. If the asset was held for more than 12 months, any capital gain may be reduced by 50%.

TAX TIP

To further offset any capital gain made on the in-specie transfer, you may wish to consider the transfer into the SMSF of shares or business real property on which a capital loss has been made, or the outright sale of these assets which you hold personally. In deciding whether to sell at a capital loss, you would need to weigh various factors such as the potential future growth of the asset, against your need to reduce any current year capital gain.

Stamp duty charges on transfer should also be considered.

CAPS

For the majority of taxpayers, an in-specie contribution of shares or business real property will count towards your non-concessional contributions cap. For 2016/2017 this cap is set at $180,000 per year or $540,000 over three years. This three-year cap allows you to bring forward three years' worth of contributions into a single year – enabling you to make large non-concessional contributions which can come in handy when making an in-specie contribution of business real property, for example.

EXAMPLE

Conrad co-owns a hardware store and land with his business partner Greg; the market value of which is $950,000. Conrad is employed by the business which pays him Superannuation Guarantee. Keen to provide for his retirement and secure asset protection for his business, in 2016/2017 Conrad transfers the title of his 50% share of the property to his SMSF.

The business real property exception will apply as the store and land are being used in a business, and the property is used exclusively for that purpose. For contribution purposes, the three-year cap will be triggered as the contribution of $475,000 (50% of $950,000) exceeds the $180,000 annual cap. Conrad will be prevented from making any further non-concessional contributions in 2016/2017 and 2017/2018. In 2018/2019, he will have a reduced cap of $65,000 ($540,000 - $475,000).

PROPOSAL

As announced on 15 September 2016, the Government is proposing to reduce the non-concessional contributions cap to $100,000 per year (or $300,000 over 3 years) from 1 July 2017. The $500,000 lifetime non-concessional contributions cap that was to be backdated to include contributions from 1 July 2017 has been scrapped. If the reduction of the cap down to $100,000 is passed into law, taxpayers will have less capacity to make large non-concessional contributions including in-specie contributions.

The Government has also announced that from 1 July 2017, individuals with a superannuation account balance of $1.6 billion will no longer be able to make non-concessional contributions to superannuation. Again, this will limit the capacity of individuals to make non-concessional contributions (including in-specie contributions) as there is currently no lifetime cap.

On the other hand, for some taxpayers, in-specie contributions will count towards your concessional contributions cap. Concessional contributions are contributions made into your SMSF that are included in the SMSF's assessable income. These contributions are taxed in your SMSF at a 'concessional' rate of 15%, which is often referred to as 'contributions tax'. The most common types of concessional contributions are employer contributions, such as Super Guarantee and salary sacrifice contributions. Concessional contributions also include personal contributions made by individuals for which the individual claims an income tax deduction. A deduction can be claimed for your personal in-specie or cash contribution where you meet the "10% Test" – that is, where less than 10% of your assessable income, your reportable fringe benefits and your reportable employer superannuation contributions (e.g. salary sacrifice contributions) for the year are from being an employee. This is otherwise referred to as the '10% Test'. Whilst most salary and wage earners are ineligible for this deduction, you may be eligible if:

- You run your own business, but were not an employee of the business (e.g. you are a Sole Trader or a Partner in a Partnership)
- You are under the age of 65 (that is, you are eligible to contribute to superannuation) and receiving pension or investment income only
- You are a contractor who is not eligible for Superannuation Guarantee from the organisations that you contract to
- You only received workers' compensation payments during the year
- You are a full-time investor
- You are a non-working spouse/individual
- You are an employee for only a small part of the year .

Returning to the earlier example, if Conrad was a sole trader for the whole year, then he would be eligible to claim his superannuation contributions (including any in-specie contributions) as a tax deduction as 0% of his income comes from being an employee. However, his deductions would be limited to a maximum contribution of $30,000 as any excess concessional contributions above the $30,000 cap must be refunded (a $35,000 cap applies to those who were 49 years or over on 30 June 2014). Conrad could instead contribute any excess above $30,000 as a non-concessional contribution and not claim a deduction on the excess. We note that the Government is proposing to reduce this concessional cap to $20,000 for all taxpayers from 1 July 2017.

BUDGET

The Government is currently seeking to legislate its 2016 Budget announcement that from 1 July 2017, all individuals eligible to contribute to superannuation will be allowed a deduction for their personal contributions (including presumably in-specie contributions) up to the concessional contributions cap – not just those individuals listed in the above categories. We will keep you apprised on when and if this proposal becomes law.

TAX TIP

Any concessional contribution deduction arising from your in-specie contribution can offset (or partially offset) any capital gain that may arise upon transfer of the shares or business real property.

HOW?

SHARES

You can transfer ASX Listed Shares held in your personal name to your SMSF simply by completing an Off-Market Transfer Form. The former Government had proposed to ban off-market transfers, but the Coalition Government has abandoned this plan, thus there is no need to sell the shares, and then have your SMSF repurchase them. On the Off-Market Transfer Form, you will name your SMSF as the purchaser of the shares. The off-market transfer must then be lodged with the ASX.

If the shares are held on the company's register this is known as an issuer-sponsored holding and you will be able to use the Australian Standard Transfer Form. You can obtain a copy of this form from the ASX website (www.asx.com.au) or from your fund's administrator (if you have one).

If your shareholdings are CHESS-sponsored then you will need to go through your broker.

REAL PROPERTY

To transfer business real property from your name to the SMSF, you will need to execute a Contract of Sale. Your lawyer will need to prepare the required documentation including lodging the transfer documents with the State Revenue Office in the relevant jurisdiction. The purchaser of the property will be the SMSF.

REMINDER

In-specie transfers must be transferred at Market Value. The Market Value must be clearly detailed in the Off Market Transfer Form prepared for the transfer of ASX Listed Securities or Managed Funds or in the event of Commercial Property in the Transfer Documentation.

CONCLUSION

In-specie contributions provide a great alternative for the many people who wish to provide for their retirement by contributing to superannuation but lack the spare cash to do so. Once inside the superannuation environment, a range of tax concessions can be enjoyed. In contemplating whether to make an in-specie contribution, you should consult with your advisor.

WHAT THE TAXMAN IS THINKING

In this edition, we flag the latest tax schemes to be wary of including those specifically aimed at individuals nearing retirement, detail a range of new legislative developments relating to employer superannuation and withholding obligations, and also list which suburbs have the most 'lost and unclaimed' superannuation and how you can chase this up.

PRE-RETIREES AND 'TOO GOOD TO BE TRUE' TAX SCHEMES

The ATO has launched "Super Scheme Smart" – a project aimed at educating people around potential pitfalls of retirement planning schemes. ATO Deputy Commissioner, Michael Cranston, said that the purpose of this initiative is to keep Australians safe from risking their retirement nest-egg through tax avoidance schemes:

> *Tax avoidance schemes have long been a target for the ATO and we have been hugely successful in identifying and shutting these down. We have recently seen an increase in the number of schemes that are designed specifically to target those approaching retirement. After working hard to build a nest-egg to fund your retirement, the last thing you want is to inadvertently risk it all by getting involved in a risky scheme. That's why the ATO is working to help individuals understand what a retirement planning scheme looks like.*

According to the ATO, individuals most at risk are those approaching retirement, typically anybody aged 50 or over looking to inject significant amounts of money into retirement – particularly SMSF members, small business owners, self-funded retirees, company directors and individuals involved in property investment. Although schemes may vary, most have the following common features. Namely, they:

- Are artificially contrived and complex, usually connected with an SMSF
- Involve a lot of paper shuffling
- Are designed to leave you the taxpayer with minimal or zero tax, or even a refund, and
- Aim to give a present day tax benefit by entering into the arrangement.

Individuals who use these illegal schemes identified by the ATO may be liable to severe tax penalties, including loss of their retirement nest-egg and also their rights to operate an SMSF. Mr. Cranston goes on to say:

> *Retirement planning makes good sense provided it is carried out within the tax and superannuation laws. Make sure you are receiving ethical professional advice when undertaking retirement planning and, if in doubt, seek a second opinion from an independent, trusted and reputable expert. While the schemes we are targeting under "Super Scheme Smart" may be complex, our message is not – if it looks too good to be true, it probably is.*

The ATO is encouraging individuals to report tax avoidance schemes. You can do so confidentially by phoning **1800 177 006** or via email to **reporttaxschemes@ato.gov.au**

WARNING

Often with these schemes, the promoter of the scheme will provide the name of a Lawyer or Accountant who they claim has given the scheme (or 'similar schemes') their professional approval. Despite this, it is recommended that you seek your own independent advice.

"DODGY" DEDUCTIONS

More than 8 million Australians claim work-related expenses each year. ATO Assistant Commissioner Graham Whyte is reminding taxpayers to ensure they get things right when lodging 2015/2016 returns over the coming months. In 2014/2015 alone, the ATO conducted over 450,000 reviews and audits of individual taxpayers, resulting in revenue adjustments of more than $1 billion. Mr. Whyte says:

> *Every tax return is scrutinised using increasingly sophisticated tools and data analytics. Consequently, we can identify and review income tax returns that may omit information or contain unreasonable deductions. When a 'red flag' is raised, our staff will investigate. If your claims seem unusual, we will check them with your employer.*

The following Real Life Case Studies provide an insight into the ATO's methods:

CASE STUDY 1 – CAR EXPENSES

A railway guard claimed $3,700 in work-related car expenses for travel between his home and workplace. He indicated that this expense related to carrying bulky tools – including large instruction manuals and safety equipment. The employer advised that the equipment could be securely stored on their premises. The taxpayer's car expense claims were therefore disallowed because the equipment could be stored at work and carrying them was his personal choice, not a requirement of his employer.

CASE STUDY 2 – TRAVEL EXPENSES

A wine expert, working at a high-end restaurant, took annual leave and went to Europe for a holiday. He claimed thousands of dollars in airfares, car expenses, accommodation, and various tour expenses, based on the fact that he'd visited some wineries. He also claimed over $9,000 for cases of wine. All his deductions were disallowed when the employer confirmed the claims were private in nature and not related to earning his income.

CASE STUDY 3 – SELF-EDUCATION

A taxpayer claimed self-education expenses for the cost of leasing a residential property, which was not his main residence. The taxpayer claimed he had to incur the expense of renting the property as he 'required peace and quiet for uninterrupted study which he could not have in his own home'. This was not deductible.

In addition to the rental expenses, the cost of a storage facility was claimed as 'the taxpayer needed to store his books and study materials'. He claimed he needed this because of the huge amount of books and study material associated with his course and that he had no space in his private or rented residence where these could be housed. This was not deductible.

The cost of renting the property was around $57,000, with additional expense of $7,500 for the storage facility. The actual cost of the study program he attended that year was only $1,200.

CASE STUDY 4 – TRAVEL EXPENSES

A medical professional made a claim for attending a conference in America and provided an invoice for the expense. When the ATO checked, they found that the taxpayer was still in Australia at the time of the conference. The claims were disallowed and the taxpayer received a substantial penalty.

ACCC TAX SCAM WARNING

In recent editions of this publication, we've mentioned that the ATO has been warning taxpayers to beware of tax scammers. Now the Australian Competition and Consumer Commission (ACCC) have issued their own general warning in relation to new scams. Acting ACCC chairperson Delia Rickard warns:

> *Scammers will go to great lengths to slip under your radar, including impersonating ATO representatives on the phone, sending out fraudulent emails and even creating bogus websites. These fraudsters contact you out of the blue, claiming you have overpaid your tax and are now entitled to a refund. To obtain the refund, they may ask you to first pay an 'administration' or 'transfer' fee. They may also ask you for your financial details so they can transfer your 'refund' to you.*
>
> *If you hand your money to these scammers, chances are you won't see it again. If you incidentally give your personal details to a scammer, your bank account and identity could be at risk of fraud. $300,000 has been reported lost to all reclaim scams to the ACCC this year, and we have received 6,000 complaints. Of these, 270 people reported the tax reclaim scam to the ACCC with over $10,000 lost.*

The ACCC provides the following advice on how to protect yourself and your business:

- Never put your Tax File Number (TFN) on your resume. Provide it to your employer only after you have started your job.
- Never share personal information, such as your TFN, ***myGov.*** or bank account details on social media.
- Change any passwords you may have shared with family or friends.
- Always keep your computer security up-to-date with anti-virus and anti-spyware software and a good firewall (and only buy software from a reputable source).
- Don't open any attachments or click on any links or reply to suspicious emails, as they may take you to a bogus website or contain a harmful virus.
- If you use a tax agent, ensure they are registered by visiting www.tpb.gov.au/onlineregister
- If you receive an email or phone call 'out of the blue' from the ATO claiming that you are entitled to a refund or asking you to confirm, update or disclose confidential details such as your TFN, press delete or just hang up.
- If you are not certain whether a call or email is a scam, verify who the other party is by using official contact details to call them directly. Never use contact details provided by the caller or sender of an email. Find them through an independent source such as a phone book or online search.
- If you think you may have provided your account details to a scammer, contact your bank or financial institution immediately.

POSTCODES WITH MOST LOST SUPER

The ATO has recently released its latest statistics on lost and unclaimed superannuation, which reveal an astonishing $11.7 billion currently sitting in lost super accounts. Deputy ATO Commissioner James O'Halloran said that the postcode with the highest amount of lost super (totaling $49 million) is 4740 in Queensland – which covers Mackay and surrounding suburbs. He goes onto say:

> *A lot of people who worked casually while they were studying or worked part-time jobs find super they had completely forgotten about. Members often lose contact with their super funds when they change jobs, move house, or forget to update their details. All small lost member accounts with balances of $4,000 or less are transferred to the ATO and become what is called 'unclaimed super'. Just like lost super, unclaimed and other ATO-held super can be claimed at any time. The top ten locations with the most lost super are in MacKay, Cairns, Toowoomba, Liverpool, Werribee, Sydney CBD, Surry Hills, Gladstone, Bondi and Campbelltown.*

Finding out whether you have any lost superannuation is now easier than ever. Simply create a ***myGov*** account by going to www.my.gov.au Once your account is established, link it to ATO online services. From there you will be able to view all your super account details, including any that has been lost or forgotten about.

TAXPAYER ALERTS

The ATO has issued two recent Taxpayer Alerts. Taxpayer Alerts are issued by the ATO to flag arrangements/schemes that they are concerned about from a tax avoidance standpoint. To view the Alerts in full, visit the legal database section of the ATO website www.ato.gov.au

TAXPAYER ALERT TA 2016/10 – CROSS BORDER, ROUND-ROBIN FINANCING ARRANGEMENTS

This Alert outlines the ATO's concerns about certain cross-border round-robin type arrangements. These arrangements involve funding of an overseas entity or operations by an Australian entity, where the funds are subsequently provided back to the Australian entity or its Australian associate in a manner which purportedly generates Australian tax deductions while not generating corresponding Australian assessable income.

While the exact mechanism varies from arrangement-to-arrangement, typically an Australian company claims interest deductions on a loan from an overseas related party which is funded by the Australian company "investing" in the overseas related party. The end result is deductions are claimed but income arising from this round-robin investment is subject to little or no tax.

TAXPAYER ALERT TA 2016/11 – RESTRUCTURES IN RESPONSE TO THE MULTI-NATIONAL ANTI-AVOIDANCE LAW INVOLVING FOREIGN PARTERSHIPS

This Alert outlines the ATO's concerns about a new scheme that attempts to avoid the Multinational Anti-Avoidance Law (MAAL). The MAAL applies to multinational groups that avoid a taxable presence in Australia by operating in Australia but booking their profits offshore.

LEGISLATIVE UPDATE

A number of key legislative developments have taken place recently that may impact you or your business either now or into the future:

NEW PAYG WITHHOLDING SCHEDULES

A range of PAYG withholding schedules have been updated from 1 October 2016.

As you may recall, in the 2016 Federal Budget the Government announced that it would provide tax relief to individuals by increasing the dollar threshold at which the 32.5% tax rate applies from $80,000 to $87,000 from 1 July 2016. As the Federal Election was held in close proximity to the Federal Budget, Parliament was unable to pass legislation to implement this change. It has now done so. From 1 October 2016 the following PAYG tables have been updated:

ATO NAT No.	Title
1004	**Schedule 1** - Statement of formulas for calculating amounts to be withheld
1023	**Schedule 3** - Tax table for actors, variety artists and other entertainers
3348	**Schedule 5** - Tax table for back payments, commissions, bonuses and similar payments
3350	**Scheudule 6** - Tax table for annuities
3351	**Schedule 7** - Tax table for unused leave payments on termination of employment
3539	**Schedule 8** - Statement of formulas for calculating HELP, SSL, TSL and SFSS components
4466	**Schedule 9** - Tax table for seniors and pensioners
70982	**Schedule 13** - Tax table for superannuation income streams
1005	Weekly tax table
1006	Fortnightly tax table
1007	Monthly tax table
1008	Weekly tax table with no and half Medicare levy
74288	Fortnightly tax table with no and half Medicare levy
1010	Medicare levy adjustment weekly tax table
1011	Medicare levy adjustment fortnightly tax table
1012	Medicare levy adjustment monthly tax table
1024	Tax table for daily and casual workers

Employers should ensure that they are using the updated tables (including having the latest software updates) when withholding from these payments.

SUPERANNUATION

Since the Federal Budget on 3 May 2016, many superannuation strategies have carried a significant element of uncertainty. As you may have heard, the Government has announced some significant changes to the superannuation proposals previously announced on Budget night. It's important to be aware that at the time of writing we still don't have any legislation passed in respect of these measures, which is essential in determining how the new law will truly operate. The Government has however indicated that legislation is expected to be introduced into Parliament before the end of 2016.

The following important changes were announced on 15 September 2016:

- The proposed lifetime cap of $500,000 per person for non-concessional contributions will not go ahead.
- From 1 July 2017, only those with a superannuation account balance below $1.6 million will be able to make non concessional contributions.
- If you are eligible to make non-concessional contributions from 1 July 2017, you will be limited to $100,000 per annum (or $300,000 over three years using existing bring-forward rules).
- The Government will retain the existing requirement that you must meet a work test to be able to contribute to super between ages 65 and 74 (they had originally proposed to remove this requirement).

There are no changes to the proposals around concessional contributions (including lowering the limit to $25,000) other than delaying the "catch-up" opportunity for those with less than $500,000 in super by 12 months to a 1 July 2018 commencement. The Government also intends to make no changes to other measures announced in the Budget including:

- Allowing all individuals eligible to contribute to superannuation a deduction for their personal contributions up to the concessional contributions cap (from 1 July 2017).
- Taxing the earnings in respect of Transition to Retirement Income Streams at 15% (up from 0%) from 1 July 2017 – irrespective of when the Income Stream commenced.
- Reducing the income threshold at which taxpayers are charged an extra 15% on their concessional contributions from $300,000 to $250,000 from 1 July 2017.

Some of these changes may result in the opportunity to make additional contributions to super, particularly before the new proposals take effect on 1 July 2017. However, in the absence of legislation to give effect to these measures, we recommend you seek advice before acting.

SMALL BUSINESS MEASURES

At the time of writing (mid-October) the legislation containing the following small business changes (to commence from 1 July 2016) was held up at a Senate Economics Legislation Committee:

- Increasing the aggregated turnover threshold for Small Business Entities from $2 million to $10 million (thus allowing many more businesses to access a range of Small Business tax concessions, but not the Small Business CGT Concessions).
- Lower the Small Business company tax rate from 28.5% to 27.5%.
- Increase the Small Business Income Tax Offset for unincorporated businesses from 5% to 8% and increase eligibility for the offset from $2 million to $5 million turnover.

With the start-date for these measures backdated to 1 July 2016, we will keep you posted as to when or if they make it through Parliament.

HELP REPAYMENTS

The so-called "Omnibus Bill" passed through Parliament in September and is now law. Among the measures contained in this Act is an extension of the High Education Loan Program (HELP) repayment regime. If you have a Higher Education Loan Program (HELP, formerly known as HECS) debt, you will soon need to start repaying it earlier.

Currently, you must commence repaying your debt through the tax system once your once your income for HELP repayment purposes reaches $54,868. The initial repayment rate is 4% of your income. From the start of the 2018/2019 year, this minimum repayment threshold will be reduced to $51,956, with a repayment rate of 2% until your income reaches $57,730 at which point the repayment rate will increase to 4%. Your HELP repayment income includes your taxable income plus any total net investment losses (which includes net rental losses from negative gearing), total reportable fringe benefit amounts, reportable super contributions (such as salary sacrificed contributions), and exempt foreign employment income.

R&D

The R&D Tax Incentive has been made less generous.

The R&D Tax Incentive is the Government's primary mechanism to encourage companies to undertake research and development in Australia. Broadly, the Incentive provides:

- 45% refundable tax offset for the first $100 million of eligible expenditure for eligible entities with a turnover of less than $20 million (which are not controlled by income tax exempt entities) for their expenditure on eligible R&D activities in Australia
- 40% non-refundable tax offset for the first $100 million of all other eligible entities for their expenditure on eligible R&D activities in Australia.

Under the changes, the higher refundable tax offset rate will be reduced from 45% to 43.5%, and the lower non-refundable rate will be reduced from 40% to 38.5%. These reductions apply from 1 July 2016.

TAX TIP

The R&D Tax Incentive is proving very popular amongst companies. The 2016 Federal Budget papers forecast that it would cost the Budget $2.9 billion in 2015/2016 and 2016/2017, eventually rising to $3.9 billion in 2019/2020. When people think of R&D, thoughts generally turn to white coats in laboratories. While activities carried out in laboratories may qualify, so too can activities carried out on the factory floor. If your company is developing cutting-edge products, discuss with your Accountant about whether you are eligible to make a claim.

FTB PART A – INCOME THRESHOLD LOWERED

Families with an adjusted taxable income of $80,000 or more will be ineligible to receive Family Tax Benefit Part A (FTB-A) supplement from 1 July 2016. This $80,000 income qualification limit is down from $100,000.

The $726 per-child supplement is paid to eligible families at the end of each financial year. Close to 400,000 families could be affected by the new income limit on the FTB-A supplement through reduced payment rates. The 'sudden-death' nature of the limit (i.e. if you are even one dollar over, you are ineligible for any payment) will create higher effective marginal tax rates around the new $80,000 threshold, which may lead to work disincentives for some families.

FREEZING OF INCOME ELIGIBILITY THRESHOLDS

Legislation has passed freezing the indexation of the following FTB income test thresholds for a further three years until 1 July 2020:

- FTB-A higher income-free area
- FTB-B primary income earner limit – to be frozen at adjusted taxable income of $100,000.

The FTB-A higher income-free area freeze is expected to see 93,300 families receive a reduced FTB-A rate and for 17,000 families to lose eligibility for FTB-A. The FTB-B primary income limit freeze will see an estimated 5,400 families lose eligibility for FTB-B.

HEALTH CRACKDOWN

As part of the 2014/2015 Federal Budget, the Government announced that it would pause income thresholds for the Medicare Levy Surcharge (MLS) and the Private Health Insurance Rebate at 2014/2015 rates for three years from 2015/2016. As part of the 2016/2017 Budget, the Government announced that it would continue to pause income thresholds for the MLS and Rebate at the 2014/2015 rates until 2020/2021. These changes have now been passed by Parliament.

The continuation of the pause in MLS income thresholds at 2014/2015 levels could result in individuals with incomes currently below each threshold moving into a higher income tier as their incomes increase. As a result:

- Individuals who do not have private health insurance and do not currently pay the MLS (see below table for thresholds) may become liable to pay the MLS once their income for MLS purposes exceeds the relevant threshold. This may encourage those affected to take out private health insurance.
- An individual's current MLS liability may increase, thus encouraging them to take out private health insurance.

Use the following table to determine your possible exposure to MLS or increased MLS over the next 5 years in light of the freezing of the income thresholds:

MEDICARE LEVY SURCHARGE THRESHOLDS 2014/2015 – 2020/2021				
	Base Tier $	Tier 1 $	Tier 2 $	Tier 3 $
Singles	90,000 or less	90,001 – 105,000	105,001 – 140,000	140,001+
Families and Couples				
0 dependants	180,000 or less	180,001 – 210,000	210,001 – 280,000	280,001+
1 dependant	180,000 or less	180,001 – 210,000	210,001 – 280,000	280,001+
2 dependants	181,500 or less	181,501 – 211,500	211,501 – 281 500	281,501+
3 dependants	183,000 or less	183,001 – 213,000	213,001 – 283,000	283,001+
4 dependants	184,500 or less	184,501 – 214,500	214,501 – 284,500	284,501+
5 dependants	186,000 or less	186,001 – 216,000	216,001 – 286,000	286,001+
Each extra child	1,500	1,500	1,500	1,500
Medicare levy surcharge rate[3]				
Rate	0.0%	1.0%	1.25%	1.5%

SINGLE TOUCH PAYROLL

The *Single Touch Payroll* regime has been passed into law. This new regime will streamline the way in which employers report certain tax and superannuation information to the ATO.

1. Salary and PAYG Withholding

Under *Single Touch Payroll,* when employers pay their staff (i.e. each week/fortnight/month as the case may be) the employees' salary or wages and PAYG withholding will be automatically reported to the ATO. Thus, all employers will need to electronically interact with the ATO and report this information online. Employers will also have the option to pay their PAYG withholding to the ATO at the same time they pay their staff (this aspect is not compulsory, as it may cause cashflow issues for employers).

2. Superannuation

There will be changes to the way superannuation is reported to the ATO under this new regime. However, there will be no changes to the way that employers pay employee superannuation. However, when payments are made to employee superannuation funds, the information will be automatically reported to the ATO.

The ATO will be assisting businesses to transition to *Single Touch Payroll.* The important dates are as follows:

- ***Employers with 20 employees or more*** will be able to report to the ATO through *Single Touch Payroll* from 1 July 2017. The regime will become compulsory from 1 July 2018.
- ***Employers with 19 employees or less*** will be able to report to the ATO through *Single Touch Payroll* from 1 July 2017. However, this is not compulsory.

SIMPLIFIED BAS

The ATO's Simplified Business Activity Statement (BAS) will be introduced from 1 July 2017. This initiative is intended to simplify the process of preparing a BAS and reduce the time in doing so. It is a "red-tape" cutting initiative. How the ATO has chosen to simplify the BAS is by reducing the number of reported G labels. The new simplified BAS will see only **G1, 1A** and **1B** being reported and gone will be **G2, G3, G10** and **G11**.

On face value, the savings seem to be in splitting hairs over whether a particular acquisition is GST-free, Input taxed, Nil GST or outside the reporting system altogether or whether a supply is free, export or taxable. You still need to ensure that you have properly identified a supply to get label **G1** right. Care is still needed to properly identify GST on supplies and GST to be properly claimed on acquisitions in order to properly calculate **1A** and **1B**. None of the underlying legislative complexities have been addressed however e.g. food, mixed supplies, Margin Scheme, second-hand dealers etc.

The savings to existing businesses will be primarily in the lesser number of GST codes that need to be used. Perhaps for the new entrants into the GST system the savings will be greater (never having been exposed to the greater array of tax codes and reporting requirements).

Who?

Small Businesses; being those with an aggregated turnover of less than $2 million – potentially increasing to $10 million if the Government's Small Business legislation passes through Parliament (see earlier).

When?

As stated, simplified BAS will be available from 1 July 2017. The process is well-advanced and the ATO is currently working with software providers to ensure they will be ready for the change.

YOUR QUESTIONS TO MTS

The following questions came to us via our complimentary Tax Helpline service. Do you have a tax question that you need guidance on? Our team of qualified Accountants is standing by.

DIRECTOR REMUNERATION AND SUPERANNUATION

We have a small business set up as a company. My partner and I are the directors. We would both rather not pay super. The money could be far better spent in the business. Is there any way to get out of not paying?

TYPES OF PAYMENT TO A DIRECTOR

At the outset, it's worth noting that there are a variety of ways that a director or stakeholder of a company can receive remuneration including via "Directors Fees", Directors Salary, fringe benefits, dividends, even as a contract style payment (in very unusual circumstances) etc.

SUPERANNUATION

All fees paid to a company Director are earnings in respect of the Director's ordinary hours of work. As such, they attract Superannuation Guarantee (SG). Director SG payments must, as with payments to employees, be made to the nominated superannuation fund or a Superannuation Clearing House as the case may be. It's against the law to make them directly to the Director (irrespective of any written agreement in place between them and the company).

YOUR QUESTION

As noted, drawing payments such as a salary from the company would attract SG and this cannot be avoided or contracted out of. To minimise the company's SG obligations, you could discuss with your Accountant the possibility of being remunerated solely by way of a dividend (such remuneration does not attract SG). Alternatively you could consider restructuring into a Partnership or Trust structure (in those cases, distributions of profit generally do not attract SG). To this end, we note the Government's recently introduced Small Business restructure rollover which allows small business owners to change their operating structure without incurring CGT or income tax, subject to various conditions being met.

PROPERTY TRANSACTIONS AND TAX INVOICES

I purchased a block of land for $670,000. GST was worked out in the normal way (10%). We intend to build new residential property on the land and then sell the property. We will not rent the property out or live in it. The company we bought the land from has been wound-up and we cannot obtain a tax invoice in relation to the acquisition of the land.

How can I claim for GST on the purchase of the land? Also, can the Margin Scheme be used on sale?

TAX INVOICE

Because property sales are consummated by a written contract, the obtaining of a tax invoice can sometimes be overlooked. However, like any other supply, to claim GST credits on a property that you purchase, you must be in possession of a valid tax invoice. For property sales, a tax invoice should be issued by the vendor whenever all of the following apply:

- The sale or part thereof attracts GST
- The vendor is registered for GST, and
- The Margin Scheme has not been applied to the sale.

If you are unable to obtain a tax invoice from the vendor (such as in this case where they have been wound up) the only other avenue available to make a GST credit claim is *Section 29-70(1A)* of the GST Act which gives the Tax Commissioner the discretion to treat as a tax invoice a particular document that would not otherwise be a tax invoice. This discretion is discussed in Practice Statement *PS LA 2004/11*. In applying for this discretion to be exercised, the purchaser would typically be seeking to have the contract of sale to be treated as a tax invoice by the Commissioner. In deciding whether or not to exercise this discretion, the Commissioner must consider all of the following factors as set out in *PSLA 2004/11* (paragraph 13). No single factor is determinative. Rather it's a combination of the following factors:

- Did the purchaser make a reasonable attempt to obtain a valid tax invoice from the supplier? The ATO expects the purchaser to make a genuine attempt to contact the supplier and request a valid tax invoice before the purchaser makes a request to the Commissioner to exercise his discretion. However, the purchaser is not expected to go to extraordinary lengths or great expense.
- Does the purchaser have evidence that demonstrates an entitlement to claim a GST credit despite not having a valid tax invoice? This can be any type of evidence that demonstrates that a creditable acquisition was made and that the purchaser was entitled to a GST credit (e.g. sales contract or other documentation such as emails etc.).
- Does the purchaser have a good ATO compliance history? Does the purchaser's prior compliance behaviour and actions point to future compliance?
- Does the purchaser have adequate record-keeping systems? What is 'adequate' will vary according to the case at hand. For example, smaller enterprises will often have different controls or checks from larger enterprises. Good systems could include, for example, frequency of internal audits, training of accounting staff and instruction manuals for staff.
- Considering the purchaser's knowledge, skills and experience, was it reasonable for them to assume that a valid tax invoice was held or to believe that a particular document complied with the tax invoice requirements? For example, if the purchaser is a new business entrant it is likely that their knowledge, skills and experience would be less than that of a purchaser that has an established business that has been operating for a long period of time.

Certainly, if you are unable to obtain a tax invoice for the purchase of taxable property, it is strongly recommended that you apply to the Commissioner to have him exercise this discretion to treat the sale contract as a tax invoice. Failure to do so means that you will be unable to claim the GST credits which, on property purchases such as this, can be a very significant amount.

MARGIN SCHEME

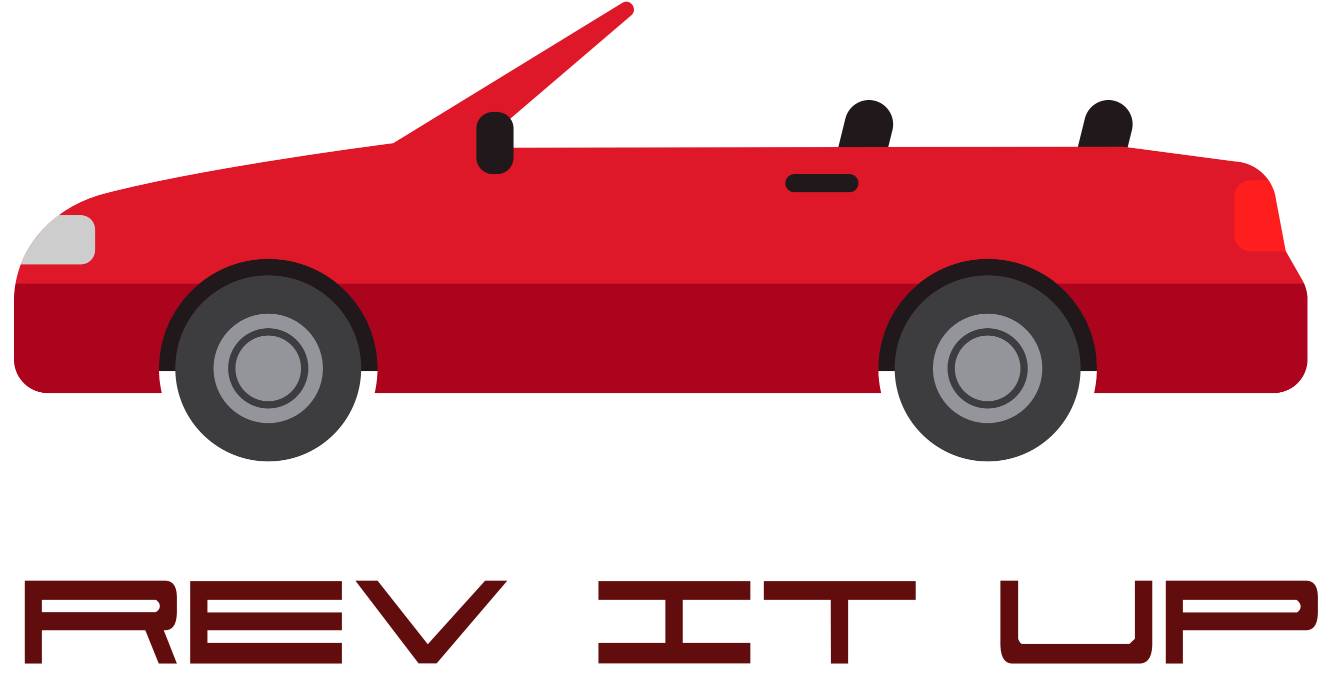
With regards to your next question; by way of background, the margin scheme is a great way to reduce the GST payable on taxable sales of real property. It is typically applicable to new residential property developments, but may also be considered when selling subdivided vacant land you have developed as part of your business.

Whereas normally GST is charged on 1/11th of the sale price, under the Margin Scheme GST is calculated as 1/11th of the margin. Broadly speaking, the margin is calculated as follows:

- For property acquired before 1 July 2000, the margin is the increase in value from that date (the Valuation Method).
- For property acquired on or after 1 July 2000, the margin is the difference between the price you paid for the property, and the price you are selling it for (the Consideration Method).

MARGIN SCHEME	
ADVANTAGES	**DISADVANTAGES**
Less GST charged on sale which is useful when selling to a party who are not GST registered	Purchaser can't claim GST credits (this is only a problem if you are selling to a GST-registered purchaser)
Flow on effects of less finance required, less interest payable over the life of the loan, less stamp duty payable	Can be complex to calculate
	Valuation costs where the property is acquired before 1 July 2000

The sale of real property (which is a taxable supply) may qualify for the Margin Scheme. However the Margin Scheme cannot be used if an entity acquired the entire property through a taxable supply on which the GST was worked out without applying the Margin Scheme. Accordingly, the Margin Scheme cannot be used in your case.



REV IT UP

Whether it be GST or depreciation, taxation claims on motor vehicles are extremely widespread. However, much confusion exists around the caps that apply in this area which may limit your claim. In this first of a three-part article series, we focus on motor vehicle depreciation claims. Over the coming months we will then focus on GST and luxury car tax issues.

WHEN?

Where a motor vehicle is either purchased outright, or financed under a hire purchase or chattel mortgage arrangement, then an income tax deduction may be allowable in respect of the depreciation or decline in value of the motor vehicle. To be clear, the vehicle can not be entirely written-off (claimed in full as a deduction) in the year it is first used or ready for use in your business unless it cost less than the relevant instant asset write-off thresholds (see later).

By contrast, if the motor vehicle is acquired under a lease arrangement, then generally no depreciation is claimable (different for a luxury car that is leased). Instead, each lease payment is a deductible amount to the extent the vehicle is used for income producing purposes, and the financed sum is not typically booked on the balance sheet of your business. The ATO will consider a finance arrangement to be a lease when:

- There is no option to purchase the vehicle written into the agreement, and
- The residual value reflects a bona fide estimate of the vehicle's market value at termination of the lease.

If these two conditions are not met, the ATO considers the finance agreement to be a hire purchase or other instalment type agreement. In effect, a leasing document identifies the owner of the vehicle as being the lessor with the lessee merely renting the vehicle from them for regular fixed instalments – hence no depreciation claim is available.

MORE?

For more information on the merits of outright purchase versus lease versus chattel mortgage versus hire purchase, see November/December 2015 edition of this publication in the subscriber section of our website www.mytaxsavers.com.au

HOW?

In terms of the method of depreciation, this will depend on the type of taxpayer:

1. SBE –

If your business is a "Small Business Entity" (businesses with an annual turnover of less than $2 million including connected entities and affiliates) and the cost of the vehicle for depreciation purposes is $20,000 or more, the vehicle will be placed into your General Small Business Pool to be depreciated at 15% in the first year, and 30% in subsequent years. If and

when the value of your General Pool falls below $20,000 then you can write-off the balance of the pool (and therefore all assets in it) rather than continuing to calculate a decline in value claim each year.

On the other hand, if the motor vehicle your small business acquires cost less than $20,000, then its entire value (assuming 100% business use) can be claimed as a deduction in the year it is first used or ready for use in your business. 2016/2017 is the final year that this $20,000 threshold applies. From 1 July 2017, this threshold will reduce to $1,000. Therefore if your business is an SBE and if you are contemplating purchasing a business vehicle in the near term and its cost is under $20,000, then you may wish to bring forward the purchase of the vehicle to before 1 July (and ensure you are using it in your business by this time). By doing so, all depreciation deductions in respect of the vehicle will be brought forward to 2016/2017 (rather than spread out of several years).

GST?

If your business is GST-registered, the write-off threshold is the GST-exclusive cost of the vehicle. Therefore, the threshold on a taxable vehicle is $21,998 (including GST). By contrast, if your business is not GST registered, the threshold is GST inclusive ($20,000, including GST). Whilst the threshold has been touted as $20,000, the actual vehicle purchased must be $19,999 or less to claim the write-off.

In determining whether the instant asset write-off applies, you take into account the full cost of the asset. Your deduction however, is limited to an estimate of how much you use the asset in earning assessable income. For example, if you buy a motor vehicle for $19,000, and you estimate it is used 50% for business purposes and 50% for private purposes, it can be immediately written-off but your deduction is only $9,500. However if you operate your business through a company or trust structure, you can claim a 100% deduction, and the FBT regime will deal with the private use component.

2. Non-SBE –

If your business's turnover is $2 million or more (or your business is an SBE but you elect not to use the SBE rules) you will depreciate the vehicle under the Uniform Capital Allowances (UCA) system. Under the UCA, there are two depreciation methods that can be used - the **Diminishing Value Method (DVM)** and the **Prime Cost Method (PCM)**. You can generally choose either method for each and every asset that is held, but once a choice is made for an asset, you no longer have the ability to change to the other method.

The **DVM** assumes the decline in value of a depreciating asset each year is a constant proportion of the remaining value of the asset. The **DVM** produces a larger deduction in the early years and progressively gets smaller as the remaining value of the vehicle at the start of each year declines (i.e. the amount that has not been depreciated). The formula for calculating decline in value under the **DVM** is:

$$\text{"Base Value"} \times \frac{\text{days held}}{365} \times \frac{200\%}{\text{asset's effective life}}$$

Where the "Base Value" is:

» In the income year the asset is first acquired: its cost

» In a subsequent income year: its opening adjustable value.

EXAMPLE 1

Clinton purchased a new car for use in his pizza delivery business on 1 May 2017. The car has a GST-exclusive cost of $23,000 and Clinton determines that the car has an effective life of 6 years. Clinton has elected to use the **DVM**.

For the 2016/2017 financial year, the depreciation deduction would be calculated as:

$23,000 x 61 / 365 x 200% / 6 = $1,226

For the 2017/2018 financial year, the decline in value would be calculated as:

$21,774 x 365 / 365 x 200% / 6 = $7,257

This process would continue in subsequent years, using the above formula, until the remaining written-down/adjustable value was claimed in full.

On the other hand, the **PCM** assumes that the decline in value is uniform over the effective life of the asset. The **PCM** therefore delivers the same amount of deduction year in-year out over the asset's effective life. Thus, if you are seeking immediate cashflow relief, the **DVM** may be preferred as the deduction in the immediate years following the purchase will be larger. The formula for the **PCM** is as follows:

$$\text{Asset's Cost} \times \frac{\text{days held}}{365} \times \frac{100\%}{\text{asset's effective life}}$$

EXAMPLE 2

Following on from the earlier example, assume instead that Clinton elects to depreciate the vehicle using the **PCM**.

For the 2016/2017 financial year, the decline in value would be calculated as:

$23,000 x 61 / 365 x 100% / 6 = $613

For the 2017/2018 financial year and subsequent years, the decline in value would be calculated as:

$23,000 x 365 / 365 x 100% / 6 = $3,831

This process would continue in subsequent years, using the above formula, until the remaining written-down/adjustable value was claimed in full.

Both the **DVM** and **PCM** are based on the concept of "effective life" of the vehicle – this is the period of time (expressed as years) that the asset will be depreciated over. The ATO have identified in their latest depreciation ruling **Taxation Ruling TR 2016/1** that a motor vehicle has an effective life of 8 years and may therefore decline in value at the rate of 12.5% if using the **PCM** or 25% if using the **DVM.**

Alternatively, you can estimate your own "effective life" (businesses sometimes use their own estimate where the intended use of the asset is likely to be heavier than would normally be expected. Where your estimated effective life of your vehicle is shorter than the ATO specified rate, this provides cashflow relief for your business as the deductions will be spread out over fewer years). Where you wish to determine your own effective life for the vehicle you should consider things such as:

- The planned usage
- Engineering specifications
- Manufacturer's specifications
- Experience with similar vehicles, and
- Scrapping practices of your business.

If you use an Accountant, you may wish to alert them to whether you think a shorter effective life should be applied due to heavy usage of practices of your business.

HOW MUCH?

Depreciation is claimable on the "cost" of the vehicle. In this instance, the vehicle's cost is made up of the following amounts:

- Basic price
- Cost of bringing the vehicle to its present location
- Incidental costs of purchase
- Any other upgrade to the vehicle which can not be held as a separate asset (e.g. air conditioning).

By contrast, items that have been added to the vehicle but which could be held separately as assets in their own right are treated as a separate asset on your asset register and do not form part of the vehicle's cost for depreciation purposes (see below example). Additionally, ongoing costs of ownership (such as insurance – including compulsory third-party insurance CTP – and registration) are immediately deductible and do not form part of the vehicle's cost for depreciation purposes.

The trade-in value of an older vehicle you have supplied is also disregarded for the purposes of the depreciation you can claim on your new vehicle. The trade-in value does not reduce your claim on your new vehicle:

EXAMPLE 3

Michael acquires outright a new Holden Barina and receives an invoice from the Dealer showing the following:

	$
New Vehicle Price	15,900.00
Air Conditioning	1,809.09
Roof Racks	310.00
Dealer Delivery Charge	695.45
End of Year Discount Given	(1,717.27)
Subtotal	**16,997.27**
On Road Costs:	
Stamp Duty	398
Registration Fee	245.00
CTP Insurance	390.00
Vehicle Total	**18,030.27**
GST in Price	1,699.73
Total Due	**19,730.00**

(CTP Insurance includes $31.62 GST)

The first step in accounting for the acquisition is to identify the different components that make up the total purchase price of $19,730. We need to identify the asset cost, any deductible expenditure, and finally the GST in the transaction.

In this instance, the vehicle's price is made up of a number of amounts. There is the first element cost of the asset being the vehicle itself as well as a number of second element costs being the after-market accessories that have been purchased with the vehicle (air conditioning & roof racks). While the air conditioning would attach to the vehicle, the roof racks could be held separately from the vehicle and hence need to be treated as a separate asset on Michael's asset register. The dealer delivery charge and the discount given are in respect of the vehicle and hence add to and subtract from the cost of the vehicle respectively. In addition, the Stamp Duty paid in respect of the vehicle is also considered an incidental cost of purchase and as such is attributed to the cost of the vehicle.

The assets acquired are therefore:

1. Vehicle for Depreciation Purposes	$
Cost of Vehicle	15,900.00
Air Conditioning	1,809.09
Dealer Delivery Charge	695.45
Less Discount	(1,717.27)
Stamp Duty	398.00
Vehicle Cost for Depreciation Purposes	**17,085.27**
2. Roof Racks	**310.00**
3. Deductible items	
Registration fee	245.00
CTP Insurance	358.38
Total Deduction	**603.38**

(Note that the GST included in the CTP is deducted in order to determine the expense amount).

CAR LIMIT

The car limit imposes a maximum on the cost of a car for the purposes of your depreciation claim. For the 2016/2017 financial year this limit is $57,581 (GST-exclusive) and is indexed from time-to-time. The limit applies regardless of whether a car is new or second-hand.

COMMON ERROR

To be abundantly clear, the car limit for depreciation purposes ($57,581) is separate to the Luxury Car Tax threshold ($75,526 for 2016/2017) which is used to determine whether 33% Luxury Car Tax applies (mostly imposed on businesses that sell or import luxury cars, and also individuals who import luxury cars). Confusing these two very separate rates/thresholds is a common error.

In basic terms, the car limit means that when you first hold a motor vehicle, any future decline in value is capped by reference to the motor vehicle depreciation limit that applied in the year that the vehicle was acquired, irrespective of whether the actual 'cost' of the vehicle (see earlier for what makes up the 'cost') exceeds this limit. Any depreciation in excess of $57,581 is not tax deductible.

The limit is based on the 'cost' – see earlier example. Therefore, it includes the purchase price, plus stamp duty and delivery charges, but excludes registration, and third-party insurance.

EXAMPLE 4

Assume that on 1 March 2016 Bill, a sole trader, purchases a 3 series BMW for $110,000 including GST. The vehicle is used solely for business purposes.

Despite the fact that the vehicle is shown on the balance sheet at $104,765 due to the reduced GST claim that can be made because it is a luxury vehicle, depreciation can only be claimed on $57,581 (the car limit). Therefore, in Example 1 and 2 if Bill was to depreciate his vehicle under the PCM or DVM, the figure of $57,581 would be used as the cost (not $104,765)

Vehicles excluded from the depreciation limit (and therefore depreciation is claimable on the full cost) include:

- Motorcycles
- Vehicles designed to carry a load of more than one tonne
- Vehicles designed to carry more than 9 passengers and
- Vehicles that are fitted out for transporting disabled people in wheelchairs for profit or modified to enable a person with a disability to use the vehicle for a taxable purpose.

In addition, before applying the motor vehicle depreciation limit, any discounts applied as a result of a trade-in and GST tax credits to which you may be entitled are adjusted for. Note there are anti-avoidance rules in place to prevent taxpayers from getting around the cost limit rules by offering a reduction in the price of a traded-in vehicle in exchange for a lowering of the price on the newly acquired vehicle.

EXAMPLE 5

Peter is looking to purchase a vehicle at a cost of $62,000. He currently owns a vehicle with a market value of $30,000. Peter offers to trade his existing vehicle at a price of $20,000 for a lowering in the price of the new vehicle to $52,000. Whilst the changeover figure remains the same ($32,000), Peter believes his new vehicle does not breach the depreciation limit. The anti-avoidance provisions would operate however to gross Peter's vehicle up to its cost of $62,000 (above the 2016/2017 limit of $57,581).

BURNING
ISSUES FOR EMPLOYERS

This article provides a checklist of some of the hot-button tax and finance issues for business as we finish up 2016.

SUPERSTREAM – COMPULSORY FOR ALL

All employers are now required to be *SuperStream* compliant. The 31 October compliance extension granted by the ATO to smaller employers has now passed. Note that there are no general exemptions from *SuperStream* – all employers must comply except for:

- Contributions to your own SMSF (i.e. if you're a related-party employer) – for example, if you're an employee of your family business and your Superannuation Guarantee contributions go to your SMSF.
- Personal contributions – for example, if you're a sole trader and you contribute to a superannuation fund for yourself.

Fines of up to $8,500 can now be imposed by the ATO on employers who are not *SuperStream* compliant. For more information on the *SuperStream* regime including compliance solutions, see the September/October 2016 edition of this publication which is available in the subscriber section of our website www.mytaxsavers.com.au

SUPERANNUATION GUARANTEE

Still on superannuation… although the ATO allows an extra month for businesses to lodge their December quarterly BAS (the due date is February 28 regardless of whether you are lodging online via the Business Portal, by paper or via a Tax Agent/BAS Agent) there is no equivalent extension for the payment of Superannuation Guarantee.

Superannuation Guarantee for the October-December quarter is still due 28 days following the end of the quarter i.e. 28 January 2017. Failure to pay on time (even if you are just one day late) will result in your business being liable for Superannuation Guarantee Charge. For this reason, if you are closed throughout January, you may wish to consider making the October-December contribution in December.

FINANCE

Following yet another recent reduction by the Reserve Bank, interest rates in Australia are now at record lows (the cash rate is currently at just 1.50%). With talk that rates will remain relatively low into the future, it's an opportune time to review if you are making the most of them. Have you considered the following?

Fixed rate options. While rates are at an all-time low there may be opportunities to fix your loans for 3 or 5 years at under 5% per annum. Explore your options. Some borrowers may wish to fix just a portion of their loan.

Review your position. Low interest rates offer an opportunity to refinance or revise your payment schedule to pay your loan off sooner. Talk to your broker to see if there's a home or business loan that better suits your needs.

Debt reduction. With lower rates, your monthly/fortnightly repayments will be less. Rather than pocketing the difference, if you put the difference into extra repayments, you can shave years off your loan and, in doing so, save thousands in interest. For example, a $500,000 home loan at an interest rate of 7% requires repayments of $3,078 per month over 30 years. At 4.5%, the repayments are $2,533, a difference of $545 a month. If you put that $545 into extra repayments, you can potentially take more than 9 years off the home loan term and save almost $140,000 in interest.

Create an offset account. This is effectively a money source sitting beside your mortgage. Any savings inside this account are effectively offset against your loan, which in turn reduces the amount of interest you pay.

Of course, low rates will not be around forever. As a borrower it's important not to become complacent and to make sure that you still have the capacity to meet your repayment obligations in the event that rates increase.

EQUIPMENT PURCHASES

When you combine the current low interest rate environment with the Instant Asset Write-Off, there has rarely been a more favourable time for small businesses to invest in plant and equipment.

The Small Business Instant Asset Write-Off allows small businesses (those with a turnover of less than $2 million including the turnover of related entities) to claim an outright deduction for the full cost of business equipment purchased under $20,000 (GST-exclusive). Most equipment (new or second-hand) is eligible including motor vehicles. To claim a deduction in this financial year, the equipment must be not only purchased but also installed ready for use before 1 July 2017. From that date, the Small Business Write-Off threshold reverts back down to $1,000.

WATCH THIS SPACE

Legislation is currently before the Federal Parliament to increase the Small Business Turnover Threshold from $2 million to $10 million. If this legislation passes through Parliament, Treasury estimates that this change will open the way for an additional 90,000 to 100,000 businesses (i.e. those with a turnover of between $2 million and $10 million) to access the $20,000 write-off, plus a range of other Small Business Concessions. We will keep you posted on the passage of this legislation through Parliament.

ANNUAL LEAVE ISSUES

SHUTDOWNS

It's quite common for businesses as a whole to shut down their operations entirely over the Christmas–New Year period and in some cases extending well into January. In this situation, the question arises as to whether staff can be forced into taking Annual Leave during this shutdown period. The answer is that under the Fair Work Act there are two circumstances where an employee can be directed by their employer to take Annual leave:

1. The employee has accumulated excess Annual Leave *or*

2. The business is closed during slow periods of the year such as Christmas or New Year.

However, under the second of these exceptions an employee can only be directed to take Annual Leave during a shutdown if their Award or registered employment agreement allows for it. If you are uncertain whether this is the case, visit the Fair Work Australia website www.fairwork.gov.au. If an employee has insufficient leave to accommodate the shutdown you may permit them to go into deficit if their employment agreement allows for this, or they may be required to take unpaid leave depending on the circumstances.

CASHING OUT

In order to enjoy some extra cash over Christmas, it's not uncommon for employees to request to cash out some of their Annual Leave at this time of year. Generally speaking however for employees covered by Enterprise Agreements, Modern Awards and Award and agreement-free employees, the employee must be left with an Annual Leave balance of at least four weeks after cashing out has occurred (e.g. if an employee has only 6 weeks of Annual Leave accrued, they are only permitted to cash out 2 weeks).