MY TAX SAVERS

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MAR/APR
2017

LATEST TAX DEVELOPMENTS

FBT TIPS & TRICKS

YOU & THE ATO

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KEY DATES
FOR BUSINESS

Many lodgement and payment deadlines are looming for business including those relating to Activity Statements, superannuation, and more.

MARCH 2017

21 MARCH
February monthly Activity Statements - due for lodgement and payment.

31 MARCH
Lodge tax return for companies and super funds with total income in excess of $2 million in the latest year lodged (excluding large/medium taxpayers), unless due earlier. Payment for companies and super funds in this category is also due by this date.

31 MARCH
Lodge tax return for the head company of a consolidated group without a member who has been deemed a large/medium entity in the latest year lodged, but with a member who had total income in excess of $2 million in their latest year lodged, unless due earlier. Payment for companies in this category is also due by this date.

31 MARCH
Lodge tax return for individuals and trusts whose latest return resulted in a tax liability of $20,000 or more, excluding large/medium trusts. Payment for individuals and trusts in this category is due as advised on their notice of assessment.

APRIL 2017

21 APRIL
March monthly Activity Statements - due for lodgement and payment.

21 APRIL
Quarter 3 (January-March) PAYG instalment Activity Statements for head companies of consolidated groups – due for lodgement and payment).

28 APRIL
Lodge and pay quarterly Activity Statement for quarter 3, 2016–17 – paper lodgments.

28 APRIL
Pay quarterly instalment notice (form R, S or T) for quarter 3, 2016–17. You only need to lodge if you are varying the instalment amount.

28 APRIL
Quarter 3 (January-March) Superannuation Guarantee contributions to be made to a complying fund on behalf of your workers.

30 APRIL
Final date for lodgement of January-March 2017 TFN report for closely held trusts for TFNs quoted to a trustee by beneficiaries.

30 APRIL
Lodge lost members report for the period 1 July 2016 to 31 December 2016.

Where one of these dates falls on a weekend or a public holiday, the due date is extended to the next business day.

DIVISION 7A

TAKING MONEY FROM A PRIVATE COMPANY

This article is a must-read for all private company shareholders. Specifically it is aimed at individuals who operate their business through a company structure and from time-to-time take money from the company for personal use. Are you aware that there can be significant tax consequences when doing so?

RELEVANCE

The vast majority of companies in Australia are run by one or two Directors. These people are invariably also the shareholders of the company; operating a small or medium business. It's not an uncommon practice for the Directors to arrange for their company to 'loan' them or their Associates (e.g. spouses, related trusts, related companies etc.) money instead of paying them wages, a franked dividend, or Directors Fees. The benefit of this is that no PAYG Withholding or income tax is applied, and no Superannuation Guarantee is paid. As amounts are informally taken as a 'loan', the ATO will not necessarily become aware of these 'transactions' in the absence of an audit, and therefore these amounts may never need to be paid back to the company…. or so you might think!

This is where Division 7A of the Tax Act steps in!

OVERVIEW

Division 7A was introduced into the tax legislation with effect from 4 December 1997. In essence, it is an integrity measure designed to ensure that private companies can not make tax-free distributions to shareholders or their Associates in the form of payments, loans and debts forgiven etc. Division 7A is one of the most commonly encountered problems for Accountants when taking on new clients, and is a tax 'time-bomb' waiting to go off for a number of company owners/shareholders as they are simply unaware of this aspect of the tax law.

The introduction of the Division 7A legislation means that previous practices of "loaning" shareholders or their Associates money, interest-free, and never repaying that debt is a thing of the past. In bringing in the Division 7A legislation, the ATO has ensured that any informal loans or payments made to shareholders or Associates are either:

1. Treated as unfranked dividends or
2. Treated as a loan, with a loan agreement in place and with interest and principal repayments being due each year.

CONSEQUENCES

INCOME TAX
If Division 7A is not dealt with properly a deemed dividend may arise for the amount of the loan to the extent of the company's distributable surplus for the year.

That is, an unfranked dividend (with no franking credits) will be deemed to have been earned by the recipient who received the loan or payment from the company (even if this person/entity is not a shareholder of the company). If this amount has not been declared in the recipient's tax return in the relevant year (the amount paid/lent/taken) then their tax return may be amended to include this amount – to be taxed at the recipient's marginal tax rate. ATO General Interest Charge and in some cases penalties may also be applied if the amount was not declared and the tax return is amended.

PERSONAL LIABILITY
Aside from this income tax cost, if the company you own gets into financial difficulty and gets wound up (for example, after an application from a Creditor) you could be left exposed personally. If a Liquidator is appointed and examines the company's books they will be intent on "clawing back" any money owed to the company – including any 'loans' made to Directors or their Associates.

Where there is a loan in your name or money is owed, the Liquidator will generally demand that it be paid back. Where the loan/payment is significant, the Liquidator may seek to bring legal proceedings against you which in the worst-case scenario could possibly bankrupt you.

Suddenly, this tax-free "loan" has come back to haunt you!

"LOANS" AND "ASSOCIATES"

Division 7A has wide scope, and catches a range of 'payments' (that are not franked dividends, Director's Fees, or salary and wages) made to shareholders and their Associates:

LOANS
Although the main loans and amounts caught by Division 7A are in the form of cash, Division 7A may apply to the following transactions and events:

- Private use of company assets
- Transfer of company assets
- Gifts
- Loans and other forms of credit
- Writing-off (forgiving a debt)
- Guarantees
- Payments or loans by a trust where a company has unpaid present entitlements
- Payments and loans through interposed entities.

Where any of these are made to a Shareholder or an Associate, Division 7A may have application.

It is also important to note there are a number of transactions which do NOT fall foul of Division 7A. These include:

- A payment, including a fringe benefit, made to a shareholder or shareholder's associate in their capacity as an employee or associate of an employee
- A payment to the extent that it discharges an obligation of the private company to pay money to the shareholder or shareholder's associate and is not more than would have been required to discharge the obligation had the two parties been dealing with each other at arm's length
- A payment to another company, otherwise than in its capacity as trustee
- A payment that is otherwise assessable or specifically excluded from assessable income
- A distribution by a Liquidator in the course of winding-up the company
- For provision of asset payments (other than transfer of property), minor use of company assets, certain payments that would otherwise be allowable as once-only deductions and the use of certain residences.

ASSOCIATES
Although the focus of this article is Directors who extract money from their companies for their own use (the most common Division 7A case), Division 7A can also apply where the recipient is an "Associate". For an individual shareholder of a company, an Associate includes:

- A relative of the individual
- A partner of the individual or a partnership in which the individual is a partner
- The spouse or child of an individual partner
- A trustee of a trust under which the individual or an Associate benefits
- A company under the control of the individual or Associate.

We note that where the shareholder is a company, trust or a partnership, any Associates of theirs may also be caught by Division 7A if they are a recipient.

CORRECTIVE ACTION

So, you've taken money from your company during 2016/2017 and Division 7A may apply…what can you do to avoid this? In this situation Division 7A will not apply where:

- The company from which the amount was taken/loaned does not have a "distributable surplus" in the year the amount is taken/loaned
- A written loan agreement (formal Division 7A agreement) is put in place – annual minimum interest and principal repayments are required in subsequent income years
- You repay the amount before the lodgement date or due date for lodgement (whichever is earlier) of the company's income tax return in the year in which the loan is made.

We now address each of these "Division 7A solutions" in turn.

DISTRIBUTABLE SURPLUS
For an unfranked dividend to arise and be assessable to the recipient, the Company from which the amount was paid/loaned must have a "distributable surplus" in the year the amount was paid/loaned. That is, the deemed dividend is limited to the amount of the distributable surplus in that year.

EXAMPLE

During 2016/2017 an interest-free amount of $40 000 was paid to Dave who is the sole Director and Shareholder of a publishing business (this amount was not a dividend, Director's fees or salary and wages from which tax was withheld). At the end of the financial year it was calculated that the company's distributable surplus for 2016/2017 was $35 000. The amount of the deemed dividend assessable to Dave (without any corrective action) is limited to $35 000 even though $40 000 was loaned.

If the private company has no distributable surplus in an income year, the amount of any deemed dividend for that income year is nil. If a deemed dividend in an income year in which the company's distributable surplus is nil, such an amount is not treated as a dividend in any future income year that there is a distributable surplus.

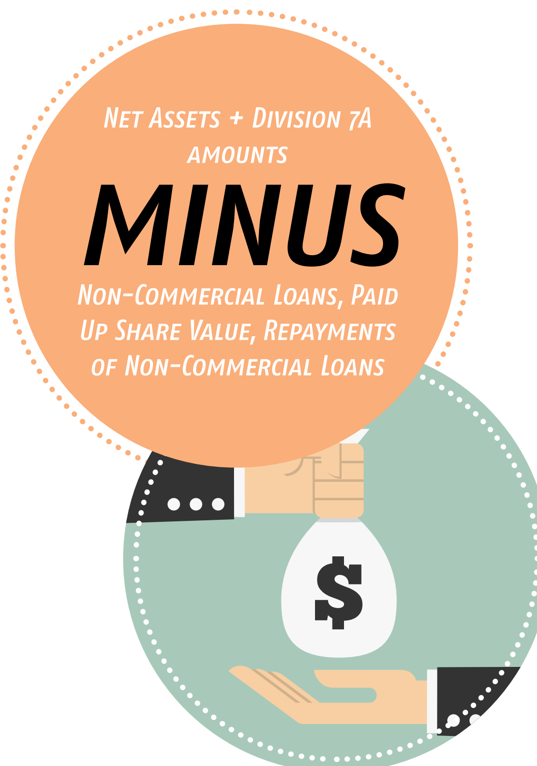
EXAMPLE

Continuing on from the above example, assume instead that the company's distributable surplus in 2016/2017 was nil, but was $20 000 in the following income year 2017/2018.

Despite the eventual existence of a distributable surplus in 2017/2018 (occurring after the payment is made) as the dividend was reduced to nil in the year the payment was made (2016/2017) the payment will not be treated as a dividend in any future year.

Where a private company has more than one Division 7A deemed dividend for an income year, the sum of which exceed the company's distributable surplus, the amount of each deemed dividend is proportionately reduced.

Although calculating the exact amount of the distributable surplus is largely a matter for your Accountant, broadly a distributable surplus is calculated as.



WARNING

While the existence of a nil distributable surplus will generally mean that there are no Division 7A consequences for that income year, where the recipient of a loan/ payment is an employee of the company and the recipient received the amount in their capacity as an employee, the ATO may deem the amount to be a loan fringe benefit.

Where the amount is deemed a loan fringe benefit, this is arguably the lesser of two evils as minimum principal repayments are not required. That is, FBT may be avoided if minimum interest payments are made every six months using the ATO specified interest rate.

LOAN AGREEMENT IS IN PLACE
Loans/payments which are put under a complying Division 7A loan agreement before the private company's tax return lodgement day (which may be as late as 15 May in the following year) and meet the minimum interest rate and maximum term criteria (explained below) will not be treated as a dividend in the income year the loan is made. To be clear, no minimum repayment or interest is required in the year in which the payment is made – only that the loan agreement be put in place. In subsequent years, annual repayments of principal and interest are required by the end of the financial year to prevent a deemed dividend arising in a later income year.

The agreement does not need to be in a prescribed form. However it should as a minimum identify the parties and set out the terms of the loan (i.e. the amount, the requirement to repay, the applicable interest rate, the term of the loan etc.). It should also be signed and dated by both parties. When drafting an agreement, input from your Accountant is recommended.

The interest rate on the loan for each year after the year in which the loan was made must be greater than or equal to the ATO benchmark interest rate for each year (currently 5.4% for 2016/2017).

The maximum term for a loan is 7 years. However where the loan is secured by a mortgage over real property, the maximum term is 25 years. In this case, the whole of the loan must be secured by a registered mortgage over the real property. At the time the loan is first made, the market value of the property (less liabilities secured over the property in priority to the loan) must be at least 110% of the amount of the loan.

TAX TIP

The option of putting a loan on a term of 25 years can provide the recipient with cash-flow relief in the sense that the repayments each year will be significantly smaller than a loan over a 7 year period. This can be useful where the loan amount is large.

WARNING

A repayment is not considered to be met (and therefore a deemed dividend may arise) where:

- You simply debit a new loan to the books of the company and credit that amount to Division 7A loans that were made in an earlier income year.
- Cash is withdrawn from the company's bank account (as a new loan) and that cash is used to repay a loan made in a previous income year.

REPAY
The simplest way to avoid the clutches of Division 7A is to repay the loan by the company's lodgement date for the year in which the loan was made (which can be as late as 15 May in the following year).

CASE STUDY

Bayside Plumbing Pty Ltd is owned by its two co-founders, Ted and Lewis, who each have a 50% shareholding and are both subject to the 47% top marginal tax rate on their income. Bayside Co pays tax at the 30% corporate tax rate.

During 2016/2017, Ted borrows $15 000 from the company's bank account. Ted does not pay tax on the $15 000 as it is not a dividend, Director's fees, or salary paid to him by Bayside Co.

As a result of this borrowing, there has been a 17% income tax shortfall (between Ted's 47% personal tax rate, and the 30% company rate) on the borrowed $15 000 as only Bayside has paid tax on this amount. The company lodges its 2016/2017 tax return on 10 January 2018, even though it's not due until 15 May 2018.

If Ted takes no action before 10 January 2018 an unfranked dividend of $15 000 will be deemed to have been paid to him, assuming Bayside Co. has a 2016/2017 distributable surplus of more than this amount. The $15 000 unfranked deemed dividend must be included in Ted's 2016/2017 personal income tax return (on which $7 050 tax will be payable, not including Medicare Levy). To avoid this, Ted has several options which he may exercise before 10 January 2018:

- Repay the $15 000 to the company
- Put the $15 000 under a complying Division 7A loan agreement over 7 years or 25 years (see earlier). Note that no repayments are due until 30 June 2018 and then each financial year until the loan is repaid.

TAKE-HOME MESSAGES

Company owners should be aware of the following:

- In taking money from your company for your personal use or for an Associate (other than as a dividend, salary and wages, Director's Fees etc.) there can be Division 7A consequences.
- If you have taken money from your company in this manner in 2016/2017, do you need to take corrective action (i.e. repay the amount or put it under a Division 7A agreement) before the earlier of the due date of your company's 2016/2017 tax return or before your company lodges its return?
- Have you taken money from your company in previous income years in this manner? Your Accountant can help you review your prior year financial statements. Does corrective action need to be taken for prior years? If so, seek direction from your Accountant.

SUPERANNUATION CHANGES – NOW LAW

On 23 November 2016 the Government passed The Fair and Sustainable Superannuation Bill into law. The Government estimates that 96% of individuals with superannuation will either not be affected by these changes or will be better off. The majority of the 4% of individuals that are adversely affected are in any case unlikely to rely on the Age Pension in retirement.

With the majority of the changes to take effect from 1 July 2017, this article examines how these measures may impact you, and any action you may wish to consider before this time.

NON-CONCESSIONAL CONTRIBUTIONS CAP REDUCED TO NIL WHERE TOTAL SUPER BALANCE EXCEEDS $1.6 MILLION

Commencing in July 2017, where your "total superannuation balance" is equal to or greater than $1.6 million at 30 June of the prior year, your non-concessional contribution cap in the following financial year will be nil. That is, you will be unable to make any non-concessional superannuation contributions. This type of contribution includes after-tax personal contributions for which you can not claim a deduction (as you fail the 10% Rule – see later); contributions made for you by your spouse; amounts transferred from foreign superannuation funds (excluding amounts included in the fund's assessable income); and contributions made for the benefit of a person under the age of 18 that are not employer contributions.

For the purpose of this new rule, an individual's "total superannuation balance" is the sum of:

- The market value of all your accumulation accounts
- The market value of all of your account-based income streams (including Transition to Retirement Income Streams)
- The total value of all non account-based income streams included in your transfer balance account – see later
- The value of any benefits that are not included in either your accumulation accounts or your transfer balance account as they have been rolled over and are in transit.

TAX TIP

If your "total superannuation balance" is $1.6 million or more on 30 June 2017, you will not be permitted to make non-concessional superannuation contributions in 2017/2018. Therefore, 2016/2017 may be your final opportunity to make non-concessional contributions. You may therefore wish to make a contribution by 30 June 2017, and take advantage of the concessionally taxed superannuation environment.

REDUCED NON-CONCESSIONAL CONTRIBUTIONS CAP

For individuals who are still eligible to make non-concessional contributions (i.e. your "total superannuation balance" is less than $1.6 million) your annual cap will be reduced from $180 000 to $100 000 from 1 July 2017.

TAX TIP

There is no change to the 2016/2017 cap. Therefore the current $180 000 per year cap (or $540 000 three-year, bring forward cap) continues to apply until 30 June 2017.

The reduced $100 000 annual cap means that from 1 July 2017, the three-year bring forward cap will be reduced to $300 000 of contributions over three years. However transitional rules will apply. Where you have triggered the bring forward rule in either 2015/2016 or 2016/2017, your remaining 3 year cap will be reduced depending on when you triggered your bring-forward period as follows:

2015/2016	2016/2017	2017/2018	2018/2019	2019/2020
More than $460 000		Nil	End of Transition Period, so $100 000 or 3 year bring forward	
More than $180 000 but less than $460 000	Cannot exceed $460 000 from 2015/2016 to 2017/2018		End of Transition Period, so $100 000 or 3 year bring forward	
	More than $380 000	Nil	Nil	End of Transition Period, so $100 000 or 3 year bring forward
	More than $180 000 but less than $380 000	Cannot exceed $380 000 from 2016/2017 to 2018/2019		End of Transition Period, so $100 000 or 3 year bring forward

EXAMPLE

Dirk is aged under 65, and is therefore eligible for the three-year bring forward cap. In 2016/2017 he sells an investment property and contributes $300 000 of the proceeds in May 2017 to superannuation.

From 1 July 2017, Dirk's total contributions in 2017/2018 and 2018/2019 cannot exceed $80 000.

TAX TIP

Where you make non-concessional contributions prior to 1 July 2017 which exceed the above reassessed bring-forward cap, you will not be penalised or required to withdraw any excess amounts. Therefore, those in a position to do so may wish to consider using up your entire $540 000 current bring-forward cap in 2016/2017 so that the transitional rules do not apply.

Going forward, the annual non-concessional contribution cap will be set at four times the concessional contribution cap. The concessional contribution cap, which will be reduced to $25 000 on 1 July 2017 (see later) is indexed in increments of $2 500. Therefore the non-concessional contributions cap will increase in line with increases in the concessional cap, in increments of $10 000.

PERSONAL DEDUCTIBLE CONTRIBUTIONS – EMPLOYEES TAKE NOTE!

From 1 July 2017 all individuals up to age 75 will be allowed to claim an income tax deduction for personal superannuation contributions. Before this date, you can only claim a deduction for your personal contributions 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.

EXAMPLE 10% RULE

For the first nine months of 2016/2017, Zoe operated a florist business as a sole trader and earned $18 000. Nearing retirement, she contributed $20 000 to superannuation in May 2017. Zoe sold her business later that month, and for the last two months of the financial year was an employee at a local nursery where she earned $3 000 from her employment. Zoe now wonders whether she will be able to claim a $20 000 deduction for her personal superannuation contribution in 2016/2017?

ANSWER

Zoe is not entitled to a deduction as more than 10% of her assessable income, reportable fringe benefits and reportable employer superannuation contributions came from being an employee ($3 000 from being an employee is more than 14% of her total assessable income of $21 000).

As a consequence of the change to the law in this area, if you are contemplating making a personal contribution to superannuation but, like most employees you are currently ineligible to claim a deduction, you may wish to delay your contribution to after 30 June 2017. By doing so, you will be able to claim a deduction.

EXAMPLE 10% RULE

Continuing on from the earlier example, if Zoe delayed her contribution until after 30 June 2017, she would be eligible to claim a full $20 000 tax deduction (irrespective of whether all of her 2017/2018 income is from being an employee). Her concessional contribution cap for the 2018 year is $25,000 thus her contribution of $20,000 is within her cap. This would reduce her 2017/2018 taxable income by the same amount, and result in a substantial personal income tax saving. To claim the deduction she must provide her superannuation fund with a *Notice of intention to claim a deduction* form before she lodges her 2017/2018 tax return.

REDUCED CONCESSIONAL CONTRIBUTIONS CAP

From 1 July 2017, the concessional contributions cap will be reduced to $25 000 for all taxpayers.

Currently (in 2016/2017) the cap is $30 000 (or $35 000 for taxpayers aged over 49). Concessional contributions include:

- Employer contributions (including the compulsory 9.5% Superannuation Guarantee (SG) and salary sacrifice)
- Personal contributions claimed as a tax deduction; and
- Certain amounts transferred from a foreign superannuation fund to an Australian superannuation fund (this won't affect most taxpayers).

Most employees are currently not eligible to claim a deduction for their after-tax superannuation contributions (see earlier). If you are currently eligible to claim a deduction under the "10% Rule" (see earlier), you may wish to consider bringing forward any planned contributions to before 1 July 2017 and take advantage of the larger cap.

The reduced $25 000 cap will also impact those employees who salary sacrifice. From 1 July 2017, for example, an employee who earns $80 000 and is paid Superannuation Guarantee by their employer will – all other things being equal – only be able to salary sacrifice $12 400. Currently, they can sacrifice $22 400 (provided no other concessional contributions are made during the year).

From 1 July 2017, you may need to review the amount you are sacrificing to superannuation to ensure you do not exceed the reduced $25 000 concessional cap. The annual cap is per taxpayer (not per superannuation fund)

CHANGED ELIGIBILITY FOR GOVERNMENT CO-CONTRIBUTION

The Government has tightened eligibility for the Superannuation Co-Contribution.

By way of background, the superannuation co-contribution was introduced on 1 July 2003 as an incentive for low-income earners to make personal contributions to superannuation, and have the Government match that contribution at least in part; up to a maximum of $500.

Eligibility for co-contribution is based on six criteria being met:

- You make personal, after-tax contributions to a complying fund or Retirement Savings Account (RSA)
- For 2016/2017 your income for co-contribution purposes is less than $51 022
- 10% or more of your total income is from eligible employment
- You do not hold a temporary resident visa at any time during the year
- You lodge an income tax return for the year of income and
- You are less than 71 years old at the end of the income year.

In addition to these existing eligibility requirements, from 1 July 2017 taxpayers will not be eligible for the Government co-contribution in a year if:

- Their non-concessional contributions exceed their new non-concessional cap for that year (see earlier), or
- Their total superannuation balance was equal to or greater than $1.6 million as at 30 June at the end of the previous income year (see earlier for details).

REDUCING THE INCOME THRESHOLD FOR EXTRA TAX ON CONCESSIONAL CONTRIBUTIONS

Individuals whose total income (defined as income for surcharge purposes) exceeds $300 000 are currently taxed an extra 15% on concessional contributions made by them or on their behalf. From 1 July 2017, this income threshold will be reduced to $250 000. To be clear, the extra 15% tax will apply where an individual's total income (consisting of income for surcharge purposes minus reportable superannuation contributions) plus concessional contributions for the year exceeds $250 000. If this threshold is exceeded, 15% additional tax will be imposed on the lesser of **(a)** your concessional contributions (excluding excess contributions) or **(b)** the excess amount over the $250 000 threshold.

EXAMPLE

In 2017/2018, Jacob earns $270 000 in salary and wages. In the same year he has concessional contributions of $28 000.

Jacob's fund will pay the standard 15% tax on these contributions. Jacob will pay an additional 15% tax on $25 000 of the concessional contributions. This will result in these amounts effectively being taxed at 30%. This increases Jacob's tax burden by $3 750 (15% of $25 000).

Note that where this tax is imposed, taxpayers will typically not receive notice from the ATO until up to 18 months after making the concessional contributions – thus the extra tax may come as a surprise.

Treasury estimates that cutting the threshold to $250 000 will impact approximately 110 000 taxpayers, doubling the tax on their concessional contributions from 15% to 30%. If your income for surcharge purposes is set to be above this threshold in 2017/2018 but below $300 000 this year, then over the coming months before 1 July you may wish to consider bringing forward any planned concessional contributions to this financial year if possible, and benefit from a lower contributions tax rate.

CARRY-FORWARD CONCESSIONAL CONTRIBUTIONS

From 1 July 2018, taxpayers with a "total superannuation balance" (see earlier definition) below $500 000 will be permitted to carry forward any unused concessional cap amounts for up to five financial years.

This will allow taxpayers who do not use all of their concessional cap in a particular financial year, to carry forward their unused concessional cap amounts to future years. This new measure may assist taxpayers with breaks in employment (e.g. new parents) to make 'catch-up' contributions when they return to work. To be eligible to make catch-up concessional contributions in a year taxpayers must have a 'total super balance' (see earlier) of less than $500 000 as at 30 June at the end of the financial year immediately preceding the financial year in which the contribution is to be made. If you are eligible to make catch-up contributions you can add any previously unused concessional cap amounts from the previous five financial years to your current year's concessional cap. Only unused amounts accrued from 1 July 2018 can be carried forward.

As well as assisting those who take time out of work, this measure will also assist those whose income varies considerably from one year to the next, or those who find their circumstances have changed (e.g. mortgage payments or school fees have ceased) and are in a position to increase their contributions to superannuation. Note that for individuals aged 65 to 74 you will only be eligible for this new measure if you meet the "work test" (this broadly requires that you must be gainfully employed for at least 40 hours in a period of not more than 30 consecutive days in the income year that you wish to make a contribution).

EXAMPLE

Brad has a superannuation balance of $300 000 but did not make any concessional superannuation contributions in 2017/2018 or 2018/2019 as he took time off work to care for his newborn child. In 2019/2020 he will have the ability to contribute $50 000 in concessional contributions into superannuation (the 2019/2020 cap, plus the unused $25 000 cap from 2018/2019). The unused 2017/2018 cap is not counted as it predates the 1 July 2018 start date.

Note that personal, after-tax catch-up contributions are also eligible for a deduction even where the individual does not pass the 10% test (see earlier). Therefore, in this case, Brad could claim a deduction of up to $50 000 in 2019/2020 depending on his level of after-tax personal contributions.

SPOUSE CONTRIBUTION TAX OFFSET EXTENDED

The superannuation spouse contribution tax offset provides a tax offset of up to $540 for a contributing spouse where they make eligible spouse contributions of up to $3 000. Under current rules the receiving spouse must have

'total income' (assessable income, reportable fringe benefits amounts and reportable employer superannuation contributions) not exceeding $10 800 in order for the contributing spouse to receive the maximum $540 offset.

Under the new rules from 1 July 2017 the receiving spouse can have 'total income' not exceeding $37 000 in order for the maximum offset to apply – a partial offset may apply where the receiving spouse has 'total income' of less than $40 000.

EXAMPLE

In 2018/2019, Bill has total income of $38 500. Jane makes a spouse contribution for Bill of $2 500. Jane is entitled to a tax offset of 18% of the lesser of:

- $1 500 - [(receiving spouse's assessable income + Reportable Fringe Benefits + Reportable Employer Superannuation Contributions) - $37,000], and
- The amount of the spouse contribution actually made.

Jane is therefore entitled to a tax offset of $270.

The increase in the spouse income thresholds from $10 800 to $37 000 will make this tax offset more widely available, and thus provide spouses with more incentive to contribute to their low-income earning partner's account and in doing so not only provide for their retirement but reduce their own personal income tax liability in the year the contribution is made.

$1.6 MILLION BALANCE TRANSFER CAP

From 1 July 2017, there will be a $1.6 million transfer balance cap on the total amount of accumulated superannuation an individual can transfer into the tax-free retirement phase to support a retirement phase income stream. "Retirement phase income streams" include all superannuation pensions and annuities (including account-based pensions, which is the most common form of income stream) other than:

- Transition to Retirement Income Streams
- Non-Communtable Allocated Pensions and Annuities.

It is important to note that subsequent earnings on these balances in the retirement phase will not be capped or restricted.

Savings beyond this $1.6 million transfer balance cap can remain inside superannuation in an accumulation account (where your earnings on those amounts will be taxed at 15%). Alternatively you can withdraw them from superannuation (provided you meet a condition of release such as turning 65 and retiring).

TAX TIP

If you have retired and have more than $1.6 million inside superannuation, the 15% tax that will now apply to the earnings on the excess is still in many cases lower than the marginal tax rates that will apply to those earnings outside of superannuation. Therefore, rather than withdrawing the excess in response to this new tax, you may wish to consider keeping the savings inside superannuation and by doing so enjoy the generous 15% tax rate.

While the general transfer balance cap for 2017/2018 will be set at $1.6 million, this will be indexed in line with the Consumer Price Index (CPI), meaning that the cap will increase to approximately $1.7 million by 2020/2021.

EXAMPLE

Joe retires on 1 July 2017 and immediately commences a $400 000 account-based pension.

As Joe commenced his first retirement phase income stream in 2017/2018, his personal transfer balance cap is equal to the cap as that financial year ($1.6 million). Therefore, Joe will be taken to have used 25% ($400 000/$1.6 million) of his personal transfer balance cap, and will be taken therefore to have an unused cap of 75%.

On 1 July 2021, the cap is increased because of CPI by $100 000 to $1.7 million. Assuming that Joe has not commenced any other retirement income stream, his personal balance cap will be indexed by 75% (his unused portion) of the CPI increase amount and thus increase by $75 000 ($100 000 increase x 75%). This will take the dollar value of his unused cap to $1 275 000.

It follows that once an individual has fully utilised their personal cap, they will not be eligible for any further increases where indexation lifts the cap, as their remaining/unused portion will be zero. For example, if Joe commenced his account-based pension with a $1.6 million balance, the $100 000 indexation increase would not lift this cap as his unused portion is nil.

TRANSITIONAL RULES

Transitional arrangements will apply. Individuals already retired with a balance below $1.7 million but more than $1.6 million on 30 June 2017, will have six months from 1 July 2017 to bring their retirement balances under $1.6 million. Individuals with balances above $1.7 million will not enjoy this six-month transition period, and must take action before 1 July 2017 to bring their account balances below $1.6 million.

VALUE OF AN ACCOUNT

To determine when an individual has exceeded their personal transfer balance cap, a transfer balance account system will be implemented from 1 July 2017. Transfer balance accounts will work like a general ledger, with amounts being credited and debited depending on a taxpayer's circumstances.

An individual will have a transfer balance account created for them when they first commence a retirement phase income stream. Alternatively, where an individual is receiving a retirement phase income stream on 1 July 2017, a transfer balance account will be created for them on that date. The value of an individual's transfer balance account will then change depending on whether amounts are credited or debited from the account on any particular day. The net value of the account at the end of each day will then be used to determine whether an individual has exceeded their transfer balance cap at that time.

CONSEQUENCES OF EXCESS ACCOUNT

Where an individual has an excess transfer balance amount, the ATO will issue an excess transfer balance determination to them.

The amount of the excess plus a notional earnings amount will be required to be commuted and removed from the retirement phase. In addition, the individual will also be required to pay excess transfer balance tax on the amount of notional earnings.

TAXING EARNINGS ON TRANSITION TO RETIREMENT INCOME STREAMS (TRIS)

The tax exemption on earnings from assets supporting Transition to Retirement Income Streams (TRIS) will be removed from 1 July 2017. Currently earnings on assets supporting TRIS are tax exempt. Once this exemption is removed, earnings will be taxed at the usual concessional rate of 15%. This change will apply regardless of when the TRIS commenced. Again, as stated earlier, although a new tax on earnings, the 15% tax rate still in most cases compares favourably to the marginal tax rates that would apply if these earnings were made on savings/investments held outside of superannuation.

ACT NOW!

As this article highlights there are many opportunities and plans to be made by 30 June 2017. Now is the time to book an appointment with your licensed advisor to develop your roadmap of action which needs to be taken.

IT'S FBT TIME

31 March marks the end of the Fringe Benefits Tax year. This article aims to assist employers to get their affairs together with a view to ascertaining and minimising their 2016/2017 FBT liability.

COLLATION AND SOFTWARE FILE

While it will generally fall to your Accountant to:

- Determine whether a fringe benefit has been provided by you to an employee or their associate (e.g. spouse)
- Determine whether an FBT exemption applies
- Determine the taxable value of your fringe benefits
- Ascertain your FBT liability
- Complete and lodge your FBT return…

…there is something you can do to assist with this process. You may wish to collate/detail all the instances where a private expense of an employee has been paid for by the business. If you or one of your employees is responsible for maintaining the accounting software file (entering in and coding each transaction undertaken by your business) ensure that the file is in good order. From an FBT perspective this involves coding personal expenses paid by the employer to an "employee benefits (FBT)" account in the management accounts. This will alert your Accountant to the existence of a potential fringe benefit.

CAR FRINGE BENEFITS

OPERATING COST METHOD

If you use the Operating Cost Method to calculate FBT on motor vehicle usage, in order to calculate the private use percentage (and therefore the FBT payable), you will need to maintain a valid log book recording your usage of the vehicle over a 12-week sample period. Failure to do so will result in the entire use of the vehicle being subject to FBT (therefore, it's vital to have a valid log-book).

Provided there has been no substantial change in the usage of your vehicle (in terms of the mix between work and personal use) a new log book must be prepared if one was not prepared for any of the previous four years.

Therefore, if you first kept a log book for the 2011/2012 FBT year, you are required to have kept a new log book for the current 2016/2017 FBT year. Leading up to the end of March, if you do not yet have a valid 2016/2017 log book, don't panic! Although we are now right at the end of the FBT year, it is not too late to keep a log book to substantiate the private use of the vehicle for 2016/2017.

Log books can commence as late as right at the end of the FBT year even though the end of the 12-week period for which it needs to be maintained may extend beyond the end of the FBT year in which the log book commenced. You can purchase a log book from your local Newsagent or you can download one of the innumerable log book apps on the market, either from the AppStore or GooglePlay as the case may be.

Upon completion, ensure the log book contains the following information, in English:

- Car details, including registration number
- The date the journey began and the date the journey ended
- Odometer readings at the commencement and conclusion of each journey
- Number of kilometres travelled by the car in the course of the journey
- A description of the purpose or purposes of the journey (generic descriptions such as 'business trip' are not adequate)
- Business and private kilometres travelled (although this is not a legislative requirement, it may help with collating data for FBT purposes).

COMMON MISTAKES

According to the ATO the most common log book mistakes uncovered during audits are:

- Entries not made in a timely manner
- Drivers fail to enter opening and closing kilometres of each trip
- Details of registration and model of car not included
- The 3 month sample is not a representative sample of the true business/private usage
- Purpose of the journey is omitted
- Name of the driver is omitted.

Also ensure that if using the Operating Cost Method, you capture the odometer reading at every 31 March. Furthermore the Statutory Formula Method is the default option therefore to use the Operating Cost Method the employer should have an election in place.

STATUTORY FORMULA METHOD

If you use the Statutory Formula Method to calculate car fringe benefits (the only alternative method to the Operating Cost Method) the transitional rules accommodating 'pre-existing commitments' are now largely redundant.

Cars provided under a 'pre-existing commitment' are required to calculate the FBT payable using rates ranging from 7% to 26% (the Statutory Fraction) rather than at the flat 20% rate. Employers are deemed to have entered into a 'pre-existing commitment' in respect of a car fringe benefit if it was entered into with the employee on or before 7:30pm on 10 May 2011 and there have been no 'material variations' to that agreement since then. 'Material variations' include:

- Refinancing a car
- Where accessories are fitted to a leased car after the lease has started (such as tinted windows, DVD players, luggage racks, bull bars etc.) and the lease is altered with the lease payments increased to reflect the addition of these items
- Altering existing lease contracts e.g.changing the duration of a lease or changes to a lease to reflect a revised residual value
- Change of employer, even within the same group of companies
- Change of car
- Employer pays out a lease residual and continues to provide the car as a fringe benefit.

These are quite common events, and are likely to have occurred to arrangements entered into before 7:30pm on 10 May 2011 (nearly 6 years ago). Therefore, most employers using the Statutory Formula Method will now apply a flat rate of 20%.

The following table sets out the Statutory Fraction that applies under the old rules where there is a 'pre-existing commitment' still in place, as well as the rate that applies for the 2016/2017 FBT year where no such commitment was in place:

DISTANCE TRAVELLED DURING THE FBT YEAR (1 APRIL – 31 MARCH	CALCULATING THE FBT FOR THE 2016/2017 FBT YEAR	
	STATUTORY FRACTION IF UNDER A 'PRE-EXISTING AGREEMENT	STATUTORY FRACTION UNDER THE STANDARD RULES
0-14 999 KM	0.26	0.20
15 000 – 24 999 KM	0.20	0.20
25 000 – 40 000 KM	0.11	0.20
MORE THAN 40 000 KM	0.07	0.20

If like the vast majority of employers you now calculate the FBT using the flat 0.20 rate, this means that:

- Odometer records are now no longer required to be kept
- The once-popular tax saving strategy of driving extra kilometers leading up to 31 March in order to cross one of the above distance thresholds (and therefore reducing the Statutory Fraction and in turn reducing the FBT payable) is now redundant as a flat 0.20 rate applies irrespective of the distance travelled. However, for those relatively few taxpayers with 'pre-existing commitments' in place, by all means if you are nearing a kilometer threshold you may wish to drive those extra kilometers leading up to 1 April (business or personal) and reduce the FBT liability.

LOANS AND PROPERTY

Loan and property fringe benefits are notoriously difficult for your Accountant to pick up from your financial records. Therefore, you may need to separately advise your Accountant if you have provided either of these benefits to your employees during the FBT year.

For FBT purposes, the definition of a 'loan' is very broad and includes:
- Overpaid salaries that are to be repaid over a number of periods
- FBT contributions owed by an employee who was salary packaging that are repaid in post-tax dollars over a number of periods (for example, in the event that an employee has ceased employment prior to the discrepancy being identified)
- A repayable outlay allowance/advance
- A loan for a security deposit/bond
- Loans to employees to purchase housing in a remote area.

Property fringe benefits arise where employers provide employees with free or discounted property. For FBT purposes, 'property' means tangible property and intangible property. It includes:
- Goods such as a computer, furniture or a gift voucher
- Real property, such as land and buildings
- Choses in action such as shares or bonds.

DECLARATIONS

Coming up to year-end, ensure that your employees have completed ***Employee Declarations*** where appropriate.

Employee declarations must be completed in order to reduce FBT on certain benefits provided to employees or in some cases exempt these benefits from FBT altogether. These declarations require the employee to substantiate the purpose for which an expense was incurred on their behalf, as well as the extent to which the expense was incurred for work-related purposes. For example, if you have purchased a laptop for an employee during the year or reimbursed them for the cost of it, they will need to complete a Declaration detailing the extent to which they have used that laptop for work purposes. This in turn may result in an exemption from FBT on this item.

You must obtain these declarations from the employee no later than the day on which your FBT return is due to be lodged with the ATO or, if you do not have to lodge an FBT return, by 21 May 2017. Failure to do so by these dates may mean an increased FBT liability. Some of the more common benefits for which a declaration may be required include:
- Expense payment benefits
- Loan fringe benefits
- Property benefits
- Living away from home benefits (particularly where a Living Away From Home Allowance LAFHA) has been paid
- Fuel expenses.

A full list of declarations including accompanying samples is available on the ATO website: http://www.ato.gov.au/Forms/Declarations/

TAX TIP

Rather than chasing these declarations up at year-end, it's recommended that you establish internal procedures ensuring that these declarations are provided to employees when the benefit is provided and are completed by the employee as soon as they have all required information to complete the declaration. Leaving it all until year-end leaves an employer open to forgetting about benefits that have been provided earlier in the year, and it also may be difficult to obtain a declaration at year-end if an employee to whom you provided benefits has left your organisation during the year.

WHAT'S HOT?

This article examines some topical issues that taxpayers and employers should be aware of at this time. Areas covered include ATO compliance, the instant asset write-off, Airbnb tax consequences, and more.

NEW ATO RULES

The ATO is currently on the look-out for and taking action against employers who are not complying with two new regimes:

BACKPACKER TAX

Employers who employ workers in Australia on a 417 or 462 visa must now be withholding 15% tax from every dollar that they earn up to $37 000 (from the first dollar that they earn). These workers can no longer claim the tax-free threshold. Beyond $37 000, the normal tax rates apply.

Employers who currently have these workers on their books, must have registered online with the ATO by 31 January 2017 at www.ato.gov.au/twhm/ to be able to withhold at this new rate. Employers who won't have this class of worker on their books until later in the year can register their business at that time. When you register with the ATO, you will typically not receive an acknowledgement, however the ATO advises that they will eventually include your registration information in your business's ATO profile. To confirm that your registration has been successful, at this stage you will need to phone the ATO. Employers who cannot register online, can register with the ATO by phoning their business info line on **13 28 66**. Employers with this type of worker on their books who do not register with the ATO will be required to withhold at the 32.5% rate and may be subject to ATO penalties.

Employers currently employing these workers will need to issue two PAYG Payment Summaries with different rates at the end of 2016/2017 – one for the period 1 July 2016 to 31 December 2016; and another for the period 1 January to 30 June 2017. To do this, employers may need to 'terminate' their employee on their payroll system, and reinstate them under a new record. However, some payroll software will apply the new rate as a manual override of the default rate. This change may also cause issues when you provide your annual Payment Summary Report to the ATO. You should contact your payroll software provider or the ATO for more advice.

SUPERSTREAM

Despite the deadline having passed months ago, *SuperStream* non-compliance among employers is still relatively high. By way of background, *SuperStream* is a Government initiative that aims to improve the efficiency of administering Australia's superannuation system. The system requires employers to remit employee contributions (including Superannuation Guarantee) and other relevant data in an electronic, standardised format. The data is linked to the payment by a unique payment reference number. All employers are now required to be *SuperStream* compliant 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**

CASH WAGES

Over the Summer months just passed it's not uncommon for people to have earned some extra money by taking on casual jobs where they are paid cash. Of itself there is nothing wrong with this, however both employees who receive cash payments and employers who make them need to be aware of some basic rules:

EMPLOYEES

If you are paid in cash, you should request a pay-slip from your employer if they have not provided you with one. You should then check the pay-slip to ensure that tax is being withheld, and withheld at the correct rate. If you are uncertain as to the rate that should be withheld, use the ATO's 'Tax withheld for individuals calculator' by entering those words into the search box on the ATO's home page **www.ato.gov.au**

If you are paid cash without tax being withheld, you will be required to pay tax on these amounts when you lodge your 2016/2017 tax return from 1 July 2017. This could result in a significant tax bill (all other things being equal). If you determine that tax is being withheld, then if the employer is not forwarding the withheld amounts onto the ATO…they will be targeted by the ATO, not you. You will still receive the withholding credit when you lodge your tax return.

At financial year-end, you should also receive a Payment Summary from your employer setting out how much tax has been withheld and your salary for the financial year. You then use this as a basis for preparing your tax return. Ensure on your return that you declare all cash payments you have received

Employees should also check with their nominated superannuation fund that they are receiving superannuation from their employers. Even casual employees paid cash for work over the Summer months are generally entitled to superannuation provided they earn $450 or more per month (before tax) and are over 18 years of age or under 18 and work at least 30 hours per week. Superannuation is paid by employers every three months on 28 January, 28 April, 28 July, and 28 October (for the previous quarter).

EMPLOYERS

It's not illegal to make cash wage payments. However you must retain accurate records of the cash payments made. You also must withhold PAYG tax and remit the withheld amounts to the ATO on your business's Activity Statement.

Superannuation Guarantee must also be paid on cash payments, and employees paid in cash must also be provided with a Payment Summary from their employers by 14 July (for the previous financial year) setting out these cash payments and the tax that has been withheld.

As stated earlier, employees who are paid in cash nonetheless must receive pay-slips from their employer.

RENTING OUT YOUR HOME

With the advent of Airbnb many more residential home owners are now landlords – renting out their entire house, or one or two rooms. The ATO is at the moment is particularly targeting those that rent out part of their property via Airbnb.

Whether you are renting out your entire home or part of your home through Airbnb or just traditionally by advertising it or through a real estate agent…the tax consequences are broadly the same as follows:

INCOME

Any rental income will be assessable. You should keep records of your rental income, even where it is paid by the tenant in cash.

RENTAL EXPENSES

Where your rental income is assessable, you are generally entitled to tax deductions for expenses incurred in deriving that income. For landlords these generally fall into 3 categories:

1. *Expenses claimable in full*

These may include repairs and maintenance relating to the rented area, depreciation of furniture and other items in the rented area, commercial cleaning of the rented area, commissions charged by real estate agents or by Airbnb.

2. *Expenses that relate to the entire property*

These may include mortgage interest, council rates, utilities and insurance. These will need to be apportioned if only part of the home is being rented (as is typically the case with Airbnb). Apportionment is generally done on a floor area basis (for example, if an Airbnb tenant has access to 70% of the house, but 30% is for your exclusive use such as your bedroom and ensuite, then only 70% of the above expenses are claimable).

3. *Expenses of private areas*

If only you as landlord have access to part of the residence (as is typically the case with Airbnb where the host may retain sole use of their ensuite and bedroom for example) expenses relating to this portion of the house cannot be claimed.

WARNING !

Where non-commercial rent is being charged (for example, you may be renting out to a family member or relative at a discounted rate), the ATO will generally cap your deductions to the amount of rental income you declare (i.e. you will not be permitted to negatively gear the property).

GST

The renting out of a residential property is an input taxed supply and therefore you are not required to register for GST or charge GST on the rent – even where your rental income exceeds the $75 000 GST registration threshold. Accordingly, you can not claim GST on any expenses you incur in renting out the property (e.g. electricity, repairs etc.).

CGT

In most cases where you sell your main residence it is free from capital gains tax (CGT). However where you have used it for income-producing purposes (such as deriving rent) part of any capital gain will be taxable. This is an issue that you should consider before you commence renting your home or part of your home – are you prepared to pay CGT on a portion of it at sale? Or is this future CGT liability outweighed by the attractiveness of the rental income in the meantime?

If you are renting out only part of your home the floor area calculation used earlier for deductions will also be used to apportion any capital gain on the property. Starting from the date on which the property was first rented, a proportion of the gain based on the floor area of the property will be liable to CGT. This gain will generally qualify for the 50% CGT discount if the property has been owned by you for 12 months or more.

No capital gain will apply upon sale where you purchased the property before 20 September 1985 even where it was not your main residence during any period of ownership. Also, CGT may be avoided if you are operating under the "Six-Year Rule" which allows you to rent out your main residence or part of your main residence for 6 years provided you have moved out and you are not treating any other property as your main residence for CGT purposes. The requirement to have moved out means that the Six-Year Rule CGT exemption will not apply where you rent out only part of your property but remain living in the residence (common with many Airbnb arrangements).

EXAMPLE *

Hugo purchased his three bedroom home on 1 January 2014 for $580 000.

After hearing about Airbnb from his friends, exactly one year later on 1 January 2015, Hugo decided to rent one of the rooms out. The tenant is entitled to the use and enjoyment of the whole house (their bedroom and common areas) except for Hugo's ensuite and bedroom which occupies 10% of the floor area).

Although not tenanted all of the time, the property is rented or available for rent via Airbnb right up until Hugo sells it on 1 January 2017 for $670 000.

For the purposes of simplicity if it is assumed that $580 000 is the cost base of the property, this is then deducted from the sale proceeds of $670 000 which means a gross capital gain of $90 000.

This is then reduced by 10% to take account of Hugo's exclusive use of some of the property = $81 000.

This is then further reduced by 1/3rd to take account of the period where the property was not available for rent as it was exclusively the main residence of Hugo = $54 270.

This is then further reduced by the 50% CGT discount as the property was held for 12 months or more.

Therefore, a capital gain of $27 135.

INSTANT ASSET WRITE-OFF

If you are a small business (aggregated turnover of less than $2 million) contemplating buying machinery or equipment, be aware that these are final months of the $20 000 instant asset write-off.

With a sunset date of 30 June 2017, small businesses may wish to start considering bringing forward any planned asset investments to the next few months – particularly in this current low interest-rate environment. You can read more about the cashflow benefits of the instant asset write-off in the previous edition of this publication (January/February 2017). Note that legislation is currently before the Parliament to increase the turnover eligibility threshold from $2 million to $10 million (to be backdated to 1 July 2016) however at the time of writing this has not yet been passed into law. We will immediately notify you via email if and when this increase becomes law.

YOU AND THE ATO

This article provides advice to assist you in dealing with the ATO. Areas covered include debt management, tax advice, digital interaction...and more!

DEBT

Latest available statistics reveal that collectable debt owed to the ATO has soared to more than $20 billion. 60% of this debt is owed by small business. If you owe the ATO money you should be aware of the following:

HARDER LINE

The ATO is now taking a harder line on individuals and businesses that do not pay their debts on time. The ATO may now move to take recovery action sooner than in the past. Previously, the ATO had waited for a company's outstanding debt to reach more than $340 000 before acting, this could be slashed to $93 000. For individuals, the benchmark may be reduced to $35 000 (down from $300 000). Recovery action may include:

- ***Statutory demands*** – the ATO can issue these to demand the payment of debts owed by companies. They require the company to pay the entire debt or enter into a payment plan with the ATO within 21 days. If a company fails to comply, the ATO may use the non-payment as evidence the company is insolvent, and then apply to the Federal Court to have it wound up.
- ***Wind-up action*** – When a court orders a company to be wound up, a liquidator is appointed to sell the company's assets and distribute the proceeds to the company's creditors.
- ***Bankruptcy notice*** – If you receive this, you must pay your debt or enter into an ATO payment arrangement within 21 days. Failure to do so may result in the ATO filing a creditor's petition to make you bankrupt.
- ***Creditors petition*** – This is an application to the Federal Court for a sequestration order to declare you bankrupt. If granted, you will become bankrupt and a trustee will be appointed to manage your estate – this typically involves the sale of your assets to pay your creditors including the ATO.

GENERAL INTEREST CHARGE

Often when businesses or individuals are struggling financially, one of the first debts they let slide is money owed to the ATO. From a financial perspective, this is not necessarily a wise move! In most cases interest will be charged on your debt (the ATO refers to this as General Interest Charge). The ATO interest rate is currently one of the highest going around at 8.76% and, furthermore, it compounds daily!

PAYMENT PLANS

With the ATO taking a harder line on outstanding debt, taxpayers with amounts owing should ensure that they engage with the ATO with a view to repayment. This will typically involve entering into a formal payment arrangement (the ATO is usually very flexible, and allows amounts to be repaid progressively to take into account a business's cashflow) and ensuring that you comply with the repayment plan by making the repayments when required. Extreme ATO recovery action is typically only taken when a taxpayer fails to engage with the ATO or does not comply with the terms of their payment arrangement.

The good news is that entering into an ATO payment arrangement to pay your debt off by instalments is now easier than ever. If you are an individual or sole trader with a income tax or activity statement debt of less than $100,000, or a company or trust with a debt of less than $25 000 and you meet the following conditions:

- You are unable to pay the debt in full by the due date
- The debt can be paid off within two years
- You have a good ATO compliance history

...then you may be able to set up a payment plan using the ATO's online services.

Alternatively, payment arrangements can be organised by taxpayers/businesses themselves or by their Accountant on their behalf simply by calling the ATO's automated self-help numbers and following the prompts – there is no need to talk with an ATO Officer. To set up a payment arrangement, call the ATO on:

- Business - **13 72 26** (and enter 2), or
- Individual - **13 28 65** (and enter 3).

If you are ineligible to enter into an automated payment arrangement, you should contact the ATO directly.

BUSINESS PORTAL

Is your business signed up to the ATO's Business Portal? It's the most convenient way to interact with the ATO. The Business Portal is a secure web-based application that affords business taxpayers the opportunity to access a range of ATO forms and information. The Business Portal can be used to:

- Lodge an Activity Statement and receive confirmation that the activity statement has been successfully lodged
- View previously lodged Activity Statements
- Revise previously lodged Activity Statements
- View certain business registration details
- Update certain business registration details
- View details of the business's various tax accounts
- Request transfers between the different tax accounts
- Request a refund for tax accounts that may be in credit and
- Send messages to the ATO on selected topics and receive a response in a secure environment.

To register for the portal you will need an AUSkey. To register, visit www.ato.gov.au/register.

ADVICE

What's your approach to uncertain tax positions? Whilst your Accountant is a great resource, the ATO offers free advice in many forms. The following table sets out the most common forms of advice and the level of protection each affords you:

	ARE YOU PROTECTED FROM...		
TYPE OF ATO ADVICE	TAX SHORTFALL?	FALSE OR MISLEADING STATEMENT PENALTY?	INTEREST CHARGES?
ATO GUIDES AND PUBLICATIONS	NO	YES	YES
CALL CENTRE	NO	YES	YES
PRIVATE RULING	YES	YES	YES
PUBLIC TAXATION RULINGS	YES	YES	YES
CLASS RULING	YES	YES	YES

Call Centre (or other informal ATO phone advice)

As with most large organisations, the quality of ATO phone advice varies – this also depends on the level of complexity of your enquiry. When asking your question, we recommend not giving your opinion on the answer to your question before the ATO officer has, and also to avoid phrasing your question so that a 'yes' or 'no' answer can be given. Otherwise the ATO officer may just agree with you in order to get you off the phone or take a guess of 'yes' or 'no' when in actual fact they may be uncertain of the answer themselves. Be aware that you can also ask to speak to the team leader if you are not confident that the ATO officer in the call centre knows what they are talking about.

As per the above table, provided you have described your circumstances correctly, you are afforded protection from penalties and interest if you rely on incorrect phone advice. In view of this, ensure you ask the ATO officer for their name and team number and record the date that you phoned.

ATO Guides and Publications

The quality of these is generally very good. However, some of the information is necessarily general in nature and may not be tailored to your particular, unique circumstances. Problems can arise when a taxpayer then seeks to apply the general information to their circumstances. Overall though, the quality of ATO publications is very good.

Private Binding Ruling (PBR)

A private ruling is a written expression of the ATO's opinion on how the tax law applies, or would apply, to your (or your business etc.) specific circumstances. Provided you have described your circumstances correctly, a private ruling is binding on the ATO and (as per the above table) affords you complete protection even where the law changes in the future. It is important however that you describe your circumstances correctly in your ruling application – this may require input from your Accountant who can apply for your ruling online.

Taxpayers typically opt for a private ruling when the tax law is uncertain, or the facts of their situation are sufficiently complex so as to make the application of the law uncertain. Another major factor that prompts taxpayers to apply for a ruling is where the dollar amount at stake is significant.

ONLINE CALCULATORS AND TOOLS

The ATO website houses a range of useful tools and calculators that many taxpayers and businesses are unaware of. These tools can save you large amounts of time and help you get things right. There are tools covering most tax areas. Whether you are a business owner, employee, contractor or have your own super fund etc. there is bound to be a tool or calculator that can help you. Simply go to go the bottom of the ATO's home page www.ato.gov.au and select 'calculators and tools' and then view the many that are on offer.

EMPLOYEE PACKAGES

Providing multi-faceted employment packages – a mix of cash and non-cash benefits and also various allowances and overtime payments – can make for a happy workforce and can therefore be a crucial staff retention and recruitment tool. However, there can be a downside for employers, for example Fringe Benefits Tax and other liabilities. This article examines some common non-salary facets of employee packages, and how employers can optimise their financial position.

OVERTIME

It's quite common across a range of industries for employees to work overtime. An employer can request an employee to work reasonable overtime (paid or unpaid). Overtime can be 'reasonable' provided the following factors are taken into account:

- Any risk to health and safety from working the extra hours
- The employee's personal situation, including their family responsibilities
- The needs of the workplace
- If the employee is entitled to receive overtime payments or penalty rates for working the extra hours (check their employment agreement including any applicable Award)
- If they are paid at a higher base rate on the understanding that they work overtime
- Any notice given by the employer to work the additional hours
- Any notice given by the employee of his or her intention to refuse to work the additional hours
- The nature of the employee's role and the employee's level of responsibility
- The usual patterns in the industry
- Whether the additional hours are in accordance with averaging provisions included in an Award or agreement that is applicable to the employee, or an averaging arrangement agreed to by an employer and an Award/agreement-free employee
- Any other relevant matter.

An employee can refuse to work overtime if the request is – by reference to the above factors – 'unreasonable'.

The good news for employers is that overtime payments for work performed outside of ordinary hours do not attract the ATO's Superannuation Guarantee Levy (SGL). If you make such payments, ensure that they appear separately in your payroll records, and do not pay the ATO's SGL on them. By contrast, if you pay employees at a higher rate on the understanding that they work overtime, the whole of their salary (including the higher rate) will attract the SGL . In view of this, employers in the latter category may wish to reconsider how they structure overtime remuneration.

LIVING AWAY FROM HOME ALLOWANCES

Living Away From Home Allowances (LAFHA) are quite a popular payment made by employers to workers who are temporarily required to live away from home to undertake work, particularly in the construction and mining industries. In recent times the rules around the FBT exemption that exists for employers who pay a LAFHA to their workers have been tightened; with the following conditions now being required to be met:

1. The employee must maintain an ownership interest in a private residence in Australia which is available for their immediate use and enjoyment should they be required to move back in tomorrow

2. The LAFHA can only be paid for 12 months, per employee, per work location

3. Substantiation of the meal/drink and accommodation expenses must be provided by the employee

You can read more about these and other LAFHA conditions in our 2016 *Income Tax / FBT* Savers publication which is available for download on our website **www.mytaxsavers.com.au**

In the quite common case where these conditions are not met, the employer will not receive an FBT exemption on the meal and accommodation component of the allowance – FBT will therefore be payable on the full amount. This can be a significant impost where the employee is living away for extended periods or where you are paying the LAFHA for multiple employees.

Where the LAFHA attracts FBT, consider paying the equivalent amount as salary and wages instead – don't separate the LAFHA amount out in your payroll records or on the employee's Payment Summary. Instead, incorporate the amount into the employee's weekly/fortnightly wages. Adopting this strategy shifts the taxation of the amount onto the employee often at a lower rate – and therefore no FBT is payable by the employer. The end result is that the employee still receives the compensation, but the FBT impost does not apply as no Fringe Benefit is provided.

SALARY SACRIFICE

Although there is no general legal requirement for employers to do so, a significant number nonetheless offer their employees the opportunity to salary sacrifice. In simple terms, salary sacrifice (also known as salary packaging) is an arrangement between an employer and employee where the employee pays for some items or services which they desire, straight from their pre-tax salary instead of after-tax dollars. The main advantage for an employee in salary sacrificing is that the money that they are using to purchase their desired item or service is not being taxed. Therefore, they are paying less tax overall than if they purchased that same item or service in the normal way with post-tax dollars. Aside from this income tax saving, other advantages in salary sacrificing include:

- ***Save on GST*** – For items or services which attract GST, the employee salary sacrifices the GST-exclusive amount, with the employer claiming the GST credit on their BAS.
- ***Discounts*** – Employers are sometimes able to secure discounts (on trade accounts, for example, or on fleet vehicles) not available to individuals.

Whilst this is great for the employee, for the employer there can be a 'sting in the tail'. Because salary sacrifice payments are made from pre-tax dollars, they are deemed to be made by the employer. Therefore, the services and items sacrificed can attract FBT. Common sacrificed items which attract FBT include:

- School fees
- Gym memberships
- Home electricity
- Health insurance
- Loan repayments on non-income producing assets (such as the family home)
- Car-parking fees
- Cars (novated lease)
- Childcare fees
- Credit card repayments
- Electronic equipment (e.g. laptops etc.) for personal use
- Holiday accommodation.

With FBT now payable at 49%, employers can be left in an unsatisfactory tax position if they allow employees to salary sacrifice these and other items which attract FBT. The good news is that employers can still offer salary sacrifice – multi-faceted employment packages – but avoid the FBT impost. Items which can be salary sacrificed which are FBT exempt include:

- Superannuation
- Work-related 'portable electronic devices' such as laptops, computers, tablets, iPads, iPhones etc.
- Briefcases
- Work tools
- Home-office equipment/expenses
- Self-education expenses where the course is related and directly relevant to the employee's current position
- Work-related travel expenses
- Interest on a loan for an investment property
- Repairs to rental properties
- Compulsory work clothing
- Subscriptions to work-related journals/ magazines
- Income protection insurance premiums
- Cost of managing tax affairs
- Work-related motor vehicle expenses
- Protective clothing
- Trade union fees
- Fees to professional associations.

EMPLOYER TIP

If there is any FBT payable on the benefits packaged, factor that FBT cost into the total cost of the Salary Package so the employee pays or the employer is at least aware of the true employment costs.

EXPENSE PAYMENT FRINGE BENEFITS

In a similar vein to salary sacrifice, employers often provide their employees with expense payment fringe benefits. This is where the employer:

- Reimburses an employee for an expense incurred by the employee, or
- Pays from their own pocket a third-party provider (e.g. a shop) in satisfaction of an expense incurred by an employee. If the payment is from pre-tax dollars of the employee, then it is salary sacrifice (see earlier).

Similar FBT rules apply to the above-listed items. If you are providing an expense payment fringe benefit, by restricting the benefits to the items listed above, you can provide a much-appreciated benefit to your employees, but not be left with an 'FBT headache'.

Where an item listed above does attract FBT, then instead of providing the benefit by way of an expense payment, you may wish to consider paying the employee the equivalent amount as a bonus cash payment for example. That way, FBT doesn't apply, but the employee is able to obtain the desired item.

EMPLOYEE SHARE SCHEMES

If you operate your business through a company structure, from a tax perspective there has never been a better time to establish an Employee Share Scheme arrangement.

Employee Share Schemes (ESS) give employees an opportunity to purchase shares in the company they work for at a discounted rate. Shares can either be standard full voting shares in the company, or dividend access shares (whereby the employee is only entitled to dividends at the discretion of the company – they have no equity or voting rights). Note that offering dividend access shares may in some cases jeopardise access to the CGT Small Business Concessions for the owners of the business (you can read more about this in the March/April 2016 edition of our bimonthly magazine which can be downloaded from our website www.mytaxsavers.com.au).

On a strategic level, ESS are a means to aligning the interests of employees and employers. By giving employees a stake in the business, their overall remuneration is in part inextricably tied with the performance of the business. This can in turn result in more productive working relationships, higher motivation, as well as reduced staff turnover. Providing ESS instead of salary increases for example, can also assist employer cash flow.

In October 2014 and in the May 2015 Federal Budget, the Government announced a series of changes to make ESS even more attractive from a tax perspective. You can read more about these favourable changes – and the tax treatment of ESS generally – in our 2016 *Income Tax/FBT Savers* publication which you can access on our website **www.mytaxsavers.com.au**

STAFF ENTERTAINMENT

Some employers regularly entertain employees with quarterly functions (including Melbourne Cup, End-of-Financial-Year, Christmas Party etc.) and other more informal events such as Friday after-work drinks. Such events help foster workplace camaraderie and morale.

If you are paying FBT on these events, then you should discuss with your Accountant slight alterations you can make so no FBT applies. For instance subject to other conditions:

- ***Friday night drinks after work*** – FBT will not apply if the employer holds the event on the work premises
- ***Christmas Party*** – FBT will not apply if the employer keeps the function under $300 per head.

Staff entertainment is a valuable tool employers can use to maintain a happy, cohesive workplace. If you are paying FBT on staff functions, talk with your Accountant about ways to minimise this tax liability.

SHARE SALE OR
OFF-MARKET BUY-BACK?

Although share buy-backs are normally associated with listed (public) companies, they can also be useful for private companies where one of the owners is seeking a tax-effective shareholder exit (they may be retiring) or where the existing shareholders do not personally have the necessary funds to buy the shares in their own right.

This article examines the two main options for a private company and its owners when a shareholder is looking to exit the company – share sale or share buy-back?

BACKGROUND

When a shareholder of a private company is seeking to exit the company, their shares must be dealt with in accordance with the rules set out in either **(a)** any Shareholder's Agreement **(b)** the company's Constitution, and /or **(c)** the Corporations Act.

To this end, the Shareholder's Agreement may allow the exiting shareholder to sell their shares to the remaining shareholders or alternatively to the company itself (otherwise known as a share buy-back).

SHARE SALE

Share sales are the most common way to exit shareholders from private companies. Most typically, rights of pre-emption exist and the shares are offered and then bought by the existing shareholders. In the rare case of where these rights are not exercised, the shares may be offered to non-shareholders. Where the existing shareholders purchase the shares, their ownership percentage in the company (and therefore their voting rights, and their rights to dividends and capital) commensurately increase.

SIMPLICITY

Share sales are typically much easier to arrange than share buy-backs. A valuation of the company is undertaken (which can be done by independent experts or the party's themselves) which ultimately determines the price of each share. The agreed price is then paid to the exiting shareholder.

In terms of compliance requirements, ASIC must be notified of the share transfer by completing *ASIC Form 484*. Any relevant requirements as set out in the company's Constitution or the Shareholder Agreement must also be met.

FUNDING

Under a share sale arrangement, the continuing shareholders must raise their own funds to purchase the exiting party's shares. This can be problematic, and may require borrowed finance. If money is borrowed from the company itself to fund the purchase, Division 7A issues may arise (which may result in the borrowed amount being assessed to the borrower as an unfranked dividend, unless the amount is repaid under a formal Division 7A loan agreement).

STAMP DUTY

Stamp Duty is a State-based tax with each jurisdiction having its own set of rules. While in some States and Territories (including New South Wales and Victoria) Stamp Duty will apply on the transfer of the exiting party's shares, in other some jurisdictions no duty is payable. For the rules and any exemptions that apply in your local jurisdiction, consult your Accountant.

TAXATION

Where the shares are not trading stock (the vast majority of cases) the exiting shareholder will make a capital gain to the extent the sale price exceeds the 'cost base' of the shares. The main element of the 'cost base' is the price for which the shares were acquired. However, the 'cost base' also includes such things as the incidental costs of acquiring the shares such as Stamp Duty and the remuneration services of a valuer who may be used when the shares are sold to the existing shareholders. On the other hand, if the capital proceeds received are less than the cost base, a capital loss will be made.

Any capital gain that is made by the exiting shareholder (where they are an individual or where the gain flows through a trust) can be reduced by the 50% CGT discount where the shares have been owned for 12 months or more.

This discount however is not available where the exiting shareholder owns the shares in a company structure – which can sometimes be the case, chiefly for asset protection reasons. Any remaining capital gain may be further reduced by the Small Business CGT Concessions if available. Note that as the sale involves a share in a company extra conditions must be met in order to access the CGT concessions in relation to the capital gain. Namely, just before the CGT event either:

(a) The exiting individual is a CGT concession stakeholder in the company or trust or

(b) The CGT concession stakeholders in the company or trust together have a small business participation percentage (SBPP) in the company or trust of at least 90%.

Where the taxpayer seeking to access the concessions is an individual, they will need to satisfy extra condition **(a).** Where the taxpayer seeking to access the concessions is a company or trust, it will need to satisfy extra condition **(b).** For more information on these Small Business CGT criteria, see our ***CGT Savers*** publication on our website www.mytaxsavers.com.au

On the other hand, there are no immediate tax consequences for the purchasing shareholders. The price that they acquire the shares for (plus any incidental costs of acquisition) becomes the cost base of the shares which – as outlined above – is used to determine their ultimate capital gain when they later dispose of those shares.

BUY-BACK

Where the company's Constitution or Shareholder Agreement allow, the company can make an offer to buy back some or all of its own shares. Where the offer is accepted, the company buys back and immediately cancels the shares. As a consequence of the cancellation, the number of shares in the company is reduced and therefore the ownership percentage of the continuing shareholders increases accordingly.

ADMINISTRATION

Any buy-back must be approved by shareholders by way of an Ordinary Resolution. Additionally, any relevant requirements in the company's Constitution or Shareholder Agreement must also be met.

A range of ASIC obligations must also be met including the lodgement of *ASIC Forms 484 and 280.* Depending on the type of buy-back, the company may be required to lodge offer documents and Shareholder Resolutions as well as disclosing other relevant information.

FUNDING

One of the advantages of a share buy-back is that the private company itself funds the acquisition from its own financial resources. Therefore, the purchasing shareholders are not financing the arrangement personally. This also prevents any Division 7A issues from arising.

EXCESS FRANKING CREDITS

If your private company has significant franking credits which are not otherwise being used, a share buy-back in effect "unlocks" the value of those credits (see later example).

TAXATION

There are no direct income tax or CGT consequences for the purchasing company or its existing shareholders.

Unlike the sale of shares, the proceeds received under a share buy-back are split into two separate components – a dividend component, and a capital component.

For the majority of private companies with limited paid up capital (for example, $2), the capital component of a share buy-back will be negligible. Therefore the majority of the proceeds will be a dividend (which may be franked).

For other companies where the paid up capital is more substantial, the split will be nominated by the company itself. That said, the ATO will carefully scrutinise that the split if it is unrealistic and designed to result in the inappropriate streaming of capital and dividend amounts to participating shareholders. A split where the capital component is too high, may stream capital benefits to existing shareholders. On the other hand, a split where the capital component ascribed is too low may stream dividends and franking credits and in doing so artificially increase the capital losses of existing shareholders. You should seek the advice of your Accountant when determining the split between any capital and dividend component.

The shareholder will typically incur CGT on the disposal of their shares (there is no entitlement to franking credits). The 50% CGT discount and the Small Business CGT Concessions may be available (see earlier) to reduce any capital gain.

CASE STUDY

THE FOLLOWING CASE STUDY ILLUSTRATES THE BENEFITS OF A SHARE BUY-BACK:

Company XYZ was formed 20 years ago with two shareholders – Edwin and Matthew – owning 50% of the shares on issue for $1 each. Assume the shares are not eligible for the Small Business CGT Concessions as they do not meet the Active Asset Test.

Edwin has decided to retire at the end of 2015/2016 and does not anticipate having any other assessable income in the following financial year. The shares will be disposed of just after 1 July for their market value of $84 000.

Assume the company has sufficient franking credits to fully frank its retained earnings. The comparison opposite shows the tax consequences for Edwin of using a share-buy back versus a traditional sale to exit the business:

	SALE	BUY- BACK
CAPITAL TREATMENT		
-CAPITAL COMPONENT OF PROCEEDS	$84 001	
-COST BASE	$1	$1
-CAPITAL GAIN/LOSS	$84 000	0
-50% DISCOUNT	($42 000)	0
ASSESSABLE CAPITAL GAIN	$42 000	0

DIVIDEND TREATMENT	SALE	BUY- BACK
BUY-BACK PROCEEDS – DIVIDEND	$0	$84 000
BUY-BACK PROCEEDS – FRANKING CREDITS	$0	$36 000
ASSESSABLE DIVIDEND COMPONENT	$0	$120 000

ASSESSABLE INCOME	$42 000	$120 000
TAX (2016/2017)	$5 197	$32 032
MEDICARE LEVY	$840	$2 400
LOW INCOME TAX OFFSET	($370)	$0
LESS FRANKING CREDITS	0	$36 000
TOTAL TAX PAYABLE	$5 667	($1568)

Therefore, the net tax benefit in using a share buy-back as compared to a share sale is $7 235.

The benefit would be even greater if Edwin owned the shares through a company structure as the CGT discount would not be available under the share sale option.

CONSIDERATIONS

Exiting a private company can have significant tax implications for the individual exiting shareholder and the company itself. The purpose of this article is to alert readers to an alternative method to exit a company other than the traditional method of selling your shares. Sometimes the latter method will be more advantageous than the former, and vice versa. When weighing up a share buy-back versus share sale various factors should be considered including:

- The tax position of the exiting shareholder (e.g. do they have any capital losses? What's their assessable income in the year of sale)?
- The application of the Small Business CGT Concessions (e.g. is the taxpayer eligible?)
- Have the shares been owned for 12 months or more?
- Does the company have unused franking credits that it needs to unlock?
- The complexity of a buy-back, including the cost (which will require legal and accounting input)
- Whether or not the remaining shareholders can fund the purchase of the shares themselves, and whether they will need to borrow from the company.