

RECORDS, INFORMATION & TRANSPARENCY

Revenue collection bodies of high taxing countries around the world have expressed concern and frustration because some countries (often called tax havens) allow people to conduct their banking and financial affairs in those countries in secret. They hold that individuals are entitled to rely on banking and other institutions to maintain confidentiality.

The need for confidentiality is, of course, enshrined in privacy legislation in Australia and in other countries. However, these privacy requirements are not applicable to revenue collection agencies such as the Australian Taxation Office.

Organised by the Organisation for Economic Co-operation and Development (OECD) a Global Forum, attended by 130 representatives of 55 governments, was held in Melbourne mid-November 2005. This Forum reviewed progress towards "a level playing field based on high standards of transparency and effective exchange of information for tax purposes."

Of 81 countries reviewed it was found that virtually all of them had mechanisms in place to permit exchange of information relating to criminal tax matters. A majority also permitted exchange of information for civil tax matters but, importantly, a number did not. Pressure is being placed on those countries to modify existing laws so that tax information can be exchanged with other countries. In the report published after the conclusion of the Forum it was noted "Until all countries adopt and implement high standards of transparency and effective exchange of information, there will continue to be a risk that the public will perceive that secure tax evasion opportunities exist abroad."

Based on the "high principle" words of creating a "level playing field", high taxing countries are doing their best to convince low taxing countries to open their records to revenue collection agencies and to eliminate the confidentiality principles on which much of their economies are based.

Yet, at the same time, high taxing countries are amending their taxation laws to encourage companies to relocate to them. An example of this is a recent change to Australian taxation laws intended to encourage foreign companies to set up holding companies in Australia. Where an Australian holding company has a subsidiary operating in another country in which it holds at least a 10% voting interest, all dividends received will be completely tax free. This is the case even if the foreign company is on a low or nil tax rate in the foreign country.

There are similar CGT exemptions if most of the assets of the subsidiary are active (used in an operating business). These exemptions do not apply to investment type income. They are designed to attract businesses away from other countries to Australia.

Australia has also recently agreed to changes in double tax agreements between itself and the UK and US. Changes are reductions of royalty withholding taxes to a maximum of 5% and a reduction of dividend withholding tax on corporate shareholdings of 80% or more from 15% to nil. These changes are designed to encourage investment in Australia.

It seems that the high taxing countries such as Australia, while talking about level playing fields, high standards of transparency and effective exchange of information are, in truth, motivated by self interest. This is further evidenced in a couple of recent court cases which show a significant lack of transparency on the part of the Tax Office.

Rio Tinto Limited v. FCT This case relates to a claim for a dividend rebate where the court ordered the Tax Office to produce a range of documents. This has been appealed by the Tax Office and a stay has been granted pending a further appeal by the Tax Office to the Full Federal Court.

Chapman & Morgan Pty Ltd v. ACT Revenue Office In this case the Administrative Appeals Tribunal (AAT) reduced an unimproved valuation by the Revenue Office of land on which a motel had been built.

The AAT impliedly criticised the Revenue Office for failing to provide the taxpayer with access to comparable sales evidence both at the assessment stage and during the subsequent objection and appeal process. The Tribunal commented that apart from the statutory requirement to do so, notions of "ordinary fairness" suggested that such information should be made available to prospective objectors.

SUPERANNUATION SPLITTING

Commencing from 1 January 2006 you can divert superannuation contributions made on your behalf to your spouse. Details were published in *Tax IQ Monthly* November 2005 issue.

Draft regulations allowed a member to split up to 100% of contributions. These have now been revised to define the *maximum splittable amount* as:

- 85% of the *deductible contributions* made in the financial year (e.g. employer contributions, super guarantee contributions or salary sacrificed contributions); and
- 100% of *personal contributions* made in the financial year for which no tax deduction is allowable and hence which are not subject to contributions tax (e.g. undeducted contributions).

OUR VIEW

Welcome to a brand new year with a brand new Tax Commissioner! Part way through his second seven-year term, Commissioner Michael Carmody departed to become CEO of Customs. Michael D'Ascenzo has been appointed Commissioner of Taxation effective from 1 January this year. Michael D'Ascenzo is well respected among taxation professionals and it is hoped that under his leadership we will see a change of attitude in the Tax Office and a greater understanding of the need to simplify the Tax Act and reduce the bureaucratic burden suffered by all businesses.

An ex-audit manager of the Tax Office writing in the *Australian Financial Review* said he is a good listener, well liked by staff. He understands the importance of the audit group's role in establishing voluntary compliance for taxpayers.

A good omen is that Mr D'Ascenzo's first public message as Commissioner was to people affected by bushfires. He said not to worry about tax obligations as the Tax Office realises it may be a while before you can focus on such matters. They will help those affected by bushfires, also those involved in fire control and support services to:

- Fast track refunds;
- Give people extra time to pay tax debts without interest;
- Give people more time to lodge activity statements and returns;
- Help reconstruct tax records destroyed in fires; and
- Offer visits from field officers to help reconcile lost records.

Mr D'Ascenzo's long experience in audits may help to solve severe problems in the Audit Section which has recently been stringently criticised by the Inspector General of Taxation, David Vos.

Mr Vos said that the Tax Office was more focused on its own administrative efficiency such that it would not provide individual treatment for taxpayers. His comments indicate a need for a fundamental overhaul of the Tax Office's operations.

Increasing tax debt owed by small businesses has alarmed business groups and there is urgent need for a different method of dealing with small businesses struggling to cope with the tax system.

The amount of collectable tax debt owed to the Tax Office has increased from \$5.5 billion in 2001/02 to \$9.6 billion despite numerous Tax Office campaigns, mail outs and extra resources from Federal Government funding.

Tony Lovett

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The limit for deductible contributions was previously stated at 100%. The reduction to 85% was made because the super fund will only have that amount available after payment of contributions tax. Application to transfer or "split" contributions are made in respect of a financial year after the end of that year.

The application must include a statement by the spouse to the effect that he or she is aged less than 55 or alternatively is under 65 and not permanently retired.

The application must specify the amount to be split.

CGT – COST BASE CALCULATION

When calculating a capital gain you deduct the cost base from the sale proceeds. The cost base is made up of five elements.

- **First Element** – the purchase or cost price of the asset.
- **Second Element** – acquisition costs including legal fees, valuation fees, consulting fees, stamp duty, etc. Second element costs also include agents commission and selling expenses on disposal of the asset.
- **Third Element** – non-capital costs of ownership such as rates, insurance and interest on assets acquired after 20 August 1991, provided these items have not been claimed as ordinary tax deductions.
- **Fourth Element** – enhancement costs including costs of improvements and extensions. Also non-deductible initial repairs.
- **Fifth Element** – costs incurred to establish, preserve or defend your title to the asset.

For assets acquired after 13 May 1997 you cannot include an amount in any cost base element if you have claimed or can claim a tax deduction for the amount. This means that if a particular amount was tax deductible but you have not claimed a tax deduction you still cannot add it to the cost base for CGT purposes.

This rule has been relaxed somewhat by the issue of Taxation Determination TD 2005/47. In this determination the Tax Office states that the question of "can deduct" is determined at the time of lodging the tax return which discloses the sale of the asset.

You may have earlier incurred an expense which is tax deductible but failed to claim a tax deduction. If the four year amendment period has expired when you lodge the tax return disclosing the sale you can safely include that amount as part of the cost base because you no longer "can deduct" the amount.

If the four year amendment period has not expired you cannot include the amount in the cost base but you can lodge an amended return and claim the amount as a tax deduction in the relevant year.

DATA MATCHING PROJECTS

Queensland WorkCover

The Tax Office advises that it will collect business names and addresses from WorkCover Queensland and electronically match those with Tax Office data to identify non-compliance with registration, lodgement and payment obligations.

Records of approximately 120,000 entities registered with WorkCover Queensland will be matched.

Tradespeople

The Tax Office has announced that it will collect details of licensed builders, electricians, plumbers and gasfitters from the Office of Consumer and Business Affairs in South Australia. These will be electronically matched with Tax Office data to identify non-compliance with registration, lodgement and payment obligations. This will cover income tax, GST and PAYG Withholding obligations.

The Tax Office says that approximately 50,000 entities including 5,000 individuals will be matched. This programme will be called the Trades Compliance Data Matching Project.

PAYG WITHHOLDING

The Tax Office has issued six withholding schedules to be used to calculate amounts required to be withheld under the PAYG system. These cover:

- Employees in the horticultural industry;
- Employees in the shearing industry;
- Return to work payments;
- Eligible Termination Payments (ETPs);
- Unused leave payments on termination of employment;
- Payments made under voluntary agreements.

These schedules apply from 1 January 2006 and can be obtained by visiting www.ato.gov.au. Then search for *PAYG Withholding*. Other tax tables can be obtained by searching *PAYG Tax Tables*.

PERSONAL SUPERANNUATION

Under draft Ruling TR 2005/D9 if a person's total assessable income, exempt income and reportable fringe benefits attributable to employment is less than 10% of total assessable income plus reportable fringe benefits then that person is eligible for deductions for personal superannuation contributions up to the age based limits.

Deductions are at the rate of 100% for the first \$5,000 and 75% of the remaining contributions.

The superannuation contribution work test was abolished from 1 July 2004. Personal superannuation contributions are now a popular option for people who have investment income if less than 10% of their total income is attributable to employment.

At a recent meeting the Tax Office indicated that it was considering a test case dealing with the operation of the 10% test and that it may defer finalising draft Ruling TR 2005/D9.

In *Re Norris and FCT* (2002) 50 ATR 1250 the Administrative Appeals Tribunal held that for the purposes of the 10% test, only amounts that attract employer superannuation support should be taken into account. The Tax Office appealed that decision but later withdrew its appeal. Yet the Tax Office "respectfully rejects" this finding.

Yet another example of the Tax Office deciding whether or not it will accept a Court decision. Presumably it will select another case to run where the facts are more likely to produce a result favourable to the Tax Office!

LABOUR HIRE

Labour Hire Firms

Employee services are not always obtained by the traditional means of direct employment. Labour hire firms, service firms or employment agencies can be contracted to provide needed personnel.

This creates complications. It is sometimes difficult to decide who is the actual employer and who should comply with superannuation guarantee requirements.

The Tax Office has issued Superannuation Guarantee Ruling SGR 2005/2 which outlines superannuation guarantee obligations in respect of what it calls *tripartite employment arrangements*.

The Ruling talks about workers, intermediaries and end users. We will refer to these as workers, labour hire firms and businesses.

The Ruling states that you need to look beyond the actual wording of any contract and the labels used by the parties. It is necessary to determine whether there is a contract (written, oral or implied) between:

- The worker and the labour hire firm;
- The worker and the business; and
- The labour hire firm and the business.

To determine this, look to:

- Who would the business sue if the worker failed to appear or failed to work in an acceptable standard?
- Who would the worker sue if they worked but didn't get paid?

If the answer to these questions is that the business holds the labour hire firm responsible for non-appearance of the worker and the worker holds the labour hire firm responsible if they don't get paid, there is no contract or employment relationship between the business and the worker.

The Ruling emphasises that it is the ultimate or legal control over the worker which is relevant rather than day to day direction and control of the worker.

Agencies

There are other cases where an employment agency, recruitment firm or placement firm is authorised by the business to act on its behalf.

Where an agency relationship exists between the agency and the business or the worker, and the agency brings about a contractual relationship between the business and the worker, a contract is then established between the business and the worker.

Accordingly, the worker is an employee of the business and not of the agency.

Again, the Ruling states that the relationship description in a document is not conclusive. Rather it is determined by an examination of the facts, the actions and conduct of the parties and other documentary evidence. A clause in an agreement that an agency relationship exists cannot receive effect according to its terms if it contradicts the effect of the agreement as a whole. In other words, the parties to the agreement cannot alter the true substance of the relationship by simply giving it a different label.

Service Trusts and Companies

If the worker is contracted to provide work for a business via an interposed entity, e.g. a family company or trust, the contract is between the worker and the family company or trust and not between the worker and the business.

A SORRY TALE

An elderly couple, Mr & Mrs Jacob, were directors of Fraser Escape 4x4 Tours Pty Ltd which operated a caravan park.

They retired and the business was then run by family members. Those family members did not do the right thing, they took money from the company for themselves without paying company liabilities.

When the day of reckoning came, the daughter-in-law committed suicide and Mr & Mrs Jacob were forced to resume running the caravan park. They sold their home to pay company debts, including outstanding tax, and also sold the land on which the business was conducted.

There was still a debt of \$193,000 and they were paying that off at the rate of \$4,000 per month. They told the Tax Office that they could settle the outstanding tax in full when the next instalment of the purchase money for the land was paid.

Despite this, the Tax Office took action to wind up the company. This was opposed by Mr & Mrs Jacob but unfortunately the law required the Court to confirm the winding up.

The moral of this story is that if you, as directors, are responsible for your business operations, do not hand the business over to others while retaining that responsibility.

As directors you must, at all times, keep firm control of your business. When it comes time to retire you should hand the business over or sell it to your successors and ensure that they take full responsibility for future operations.

GENERAL INTEREST CHARGE

The general interest charge for the quarter ended 31 March 2006 is 12.63%. The rate for the previous quarter was 12.62%.

SUPERANNUATION – CHOICE OF FUND

The Government proposes to extend the superannuation choice of fund regime to employees covered under State Awards.

This change is subject to appropriate legislation being passed and is anticipated to commence from 1 July 2006.

The Government intends this legislation to override State Awards in relation to superannuation and for constitutional reasons it will only apply to employees of companies.

MEDICAL EXPENSES

Legislation has been introduced to exclude medical and dental procedures which are solely cosmetic from tax deductibility.

This change applies to the 2005/2006 income year and later income years.

BANKRUPTCY

There are provisions in the bankruptcy legislation which enable a trustee in bankruptcy to "claw back" monies or assets which the bankrupt may have disposed of prior to bankruptcy.

These claw back provisions enable a trustee to force creditors to repay monies they may have received from the bankruptcy during the six months prior. Any property transfers for less than market value which may have occurred within two years prior to bankruptcy can also be recovered.

These provisions have often been utilised by high income earners who have transferred assets to their spouses and then managed to delay bankruptcy by protracted litigation.

Often the major creditor trying to recover assets from the bankrupt is the Tax Office.

The Government has introduced legislation into Parliament which is intended to strengthen the claw back provisions of the Bankruptcy Act. These amendments will:

- Increase the claw back period from two years to four years for transfers of property to partners, relatives, etc for less than market value;
- Enable the trustee to presume that the bankrupt was insolvent at the time of the transfer if he did not keep proper books, accounts and records. Such a presumption can be rebutted by the bankrupt if he can provide appropriate evidence;
- Enable the trustee to seek recovery from another person who has acquired property with the assistance of the bankrupt up to five years prior to bankruptcy and the bankrupt has derived a direct or indirect benefit therefrom.

THE GOLD BULL

Congratulations to the Tax Office! It has taken first prize in an international award for gobbledegook!

The Tax Office has collected the Gold Bull award for a section in the GST Act which states that the Taxation Commissioner may "*treat a particular event that actually happened as not having happened; and a particular event that did not actually happen as having happened.*" The award was presented by Mr Ben Beer, spokesman for Plain English Campaign in the United Kingdom.

PART IVA

The Tax Office has released a guide entitled *Part IVA: The General Anti-Avoidance Rule for Income Tax*. When releasing this guide the then Commissioner, Michael Carmody, said that it provides practical guidance for deciding whether Part IVA is likely to apply to a particular arrangement. You can download this guide by visiting www.ato.gov.au. Enter the above title in the search bar.

In a rather caustic editorial the *Australian Financial Review* calls it *Part IVA for Dummies* and says that it reveals who are the real dummies.

"Part IVA is the general anti-avoidance clause introduced in the early 1980s in response to an epidemic of tax avoidance. It cancels tax schemes that technically comply with the Tax Act but have a sole or dominant purpose of obtaining a tax benefit, or avoiding tax. To fall foul of this catch-all, a scheme must be artificially contrived in ways that would not normally be necessary to achieve the commercial substance of the transaction in question."

The language is Byzantine and the *Dummies* guide is not much better, as the following sentence confirms:

"If, after reading this guide you feel uneasy about an arrangement you could consider getting advice from your tax adviser, or you could apply for a Ruling."

The editorial goes on to talk about the complexity of the Tax Act and to acknowledge that it is the right of every citizen to minimise his or her tax bill but that this is not available to ordinary wage and salary earners.

"Punitive rates and complexity are the enemies of fair and efficient taxation, and the raison d'être for Part IVA. The new guide confirms what everybody but Prime Minister, John Howard, and Treasurer, Peter Costello, knows in their bones – that the Tax Act needs radical reform, not just tinkering with rates and scales."

POLITICAL CONTRIBUTIONS

Legislation has been introduced to increase the tax deductible thresholds for political contributions from \$100 to \$1,500. Companies, as well as individuals, will be able to claim tax deductibility for contributions made to political parties registered under Federal, State and Territory electoral legislation as well as gifts to independent candidates and members. These changes will take effect as from the date of Royal Assent to the Bill which is currently before Parliament. If you are contemplating a donation to a political party or candidate, it might be a good idea to hold off for a little while.

DIRECTOR'S LIABILITY

The amendment to the Corporations Act to remove personal liability for directors of corporate trustees has now received Royal Assent. This was discussed in *Tax IQ Monthly* July 2005 at page 3. Under the wording of old Section 197 of the Corporations Act a South Australian court case (*Hannel v. O'Neill*) held that a director of a corporate trustee was personally liable for trust debts.

That section has now been removed and new Section 197 imposes personal liability on a director of a corporate trustee only where trust assets cannot be applied because:

- The corporate trustee has acted in breach of trust and has incurred the liability itself;
- The corporate trustee has acted outside the scope of its powers under the trust deed; and/or
- There is a term in the trust deed which denies or limits the corporate trustees right to utilise trust assets to pay debts.

GST – WHAT IS AN ENTERPRISE?

Twelve months ago, the Tax Office issued draft Miscellaneous Taxation Ruling MT 2004/D3 to explain what is meant by "carrying on an enterprise". This is important because your entitlement to an ABN depends on whether you are carrying on an enterprise and your requirement to register for GST purposes depends on whether you are:

- Carrying on an enterprise; and
- Your annual turnover meets the turnover threshold (except for taxi operators).

Following some criticism about the definitions and explanations contained in MT 2004/D3 this has now been withdrawn and a new draft Ruling has been released. This is MT 2005/D1. The Ruling discusses the different types of bodies which are defined as entities for GST purposes. These include:

- An individual;
- A body corporate (created by Common Law, by Statute, e.g. a company, or by registration, e.g. a building society credit union, etc.);
- A Corporation Sole (established by Act of Parliament);
- A Body Politic (a Territory, State or Federal Government);
- A trust;
- A superannuation fund
- A partnership;
- Other unincorporated associations or bodies of persons.

Under Section 38 of the GST Act an enterprise is an activity, or series of activity, done:

- In the form of a business, or
- In the form of an adventure or concern in the nature of trade, or
- On a regular or continuous basis, in the form of a lease, licence or other grant of an interest in property, or
- By the trustee of a fund that is covered by, or by an authority or institution that is covered by the deductible gift recipient rules, or
- By a charitable institution or by a trustee of a charitable fund, or
- By a religious institution, or
- By the Commonwealth, a State or a Territory, or by a body corporate or corporation sole.

The definition of carrying on an enterprise is extended to include activities done in the course of commencement or termination of the enterprise. This could include feasibility studies involving genuine business activities. However, activities that are of a private nature or too remote from fruition are not considered to be commencement activities. The Ruling regards an enterprise as terminating when the enterprise ceases, as indicated by disposal of its assets or conversion to another purpose.

The main indicators of carrying on a business are set out in Taxation Ruling TR 97/11. These are:

- A significant commercial activity;
- A purpose and intention of the taxpayer to engage in commercial activity;
- An intention to make a profit from the activity;
- The activity is carried on in a similar manner to that of other businesses in the same or similar trade;
- Activity is systematic, organised and carried on in a businesslike manner and records are kept;
- The activities are of a reasonable size and scale;
- A business plan exists;
- Commercial sales of produce; and
- The entity has relevant knowledge or skill.

There is no single test to determine whether a business is being carried on. TR 95/11 states that whilst each case might turn on its own particular facts, the determination of the question is generally the result of a process of weighing all the relevant indicators.

REAL PROPERTY TRANSACTIONS

Two recent cases *Statham and Anor. v. FCT* and *Casimaty v. FCT* provide some guidance on when activities to subdivide land amount to a business or profit making undertaking or scheme. In these cases, farmland was subdivided and sold. Minimal development work was undertaken to meet Council requirements and improve the presentation of certain allotments. On the particular facts of these cases the Courts held that the sales were a mere realisation of a capital asset rather than the carrying on of an enterprise.

There are a number of factors which can assist in determining whether activities are a business or an adventure or concern in the nature of trade (a profit making undertaking or scheme). If a number of these factors are present it may be an indication that a business or adventure or concern in the nature of trade is being carried on. The factors are:

- There is a change of purpose for which the land is held;
- Additional land is acquired to be added to the original parcel;
- The parcel of land is brought to account as a business asset;
- There is a coherent plan for the subdivision;
- There is a business organisation – e.g. a manager, office and letterhead;
- Borrowed funds financed the acquisition or subdivision;
- Interest on money borrowed to defray subdivisional costs was claimed as a business expense;
- There is a level of development of the land beyond that necessary to secure Council approval for the subdivision; and
- Buildings have been erected on the land.

Are the activities related to isolated transactions, the carrying on of an enterprise or the mere realisation of a capital asset? You need to look at the facts and circumstances in the light of the above factors and any other relevant factors. No single item is in any way decisive. However, where land is purchased with a view to resale at a profit, the purchase and subsequent sale of that land is an enterprise. This is the case whether the land is sold as it was purchased or whether it was subdivided before sale.

The Ruling provides the following examples which the Tax Office considers are the carrying on of an enterprise:

- The purchase of a block of land with the intention to subdivide it into two lots and sell them for a profit;
- The purchase of an oceanfront block of land with the intention of building a duplex, selling one and living in the other;
- The purchase of a large property with the intention of building a resort but subsequently changing this and obtaining subdivisional approval for a large number of lots and attending to the obtaining of all necessary Council approvals, construction work and marketing;
- After moving out of their main residence, they decide to demolish the house, subdivide the land into two lots, build a house on each lot, connect water, phone and electricity and market the two newly constructed houses.

The following activities are excluded from being an enterprise:

- By a person as an employee;
- As a private recreational pursuit or hobby;
- By an individual (other than trustee of a charitable fund) or a partnership (all or most of the members of which are individuals) without a reasonable expectation of profit or gain; or
- As a member of a local governing body established under a State or Territory law.

Although replacing an earlier draft Ruling, this Ruling is still in draft form and will not have legal force until a final Ruling is eventually issued.

TAX OFFICE OVERCHARGES

In what has been termed by the Treasury as a risk to revenue, the Tax Office has been found to have incorrectly calculated the General Interest Charge (GIC) during the years between 1993 to 1999. Taxpayers affected are:

- 218,508 individuals;
- 5,570 companies;
- 1,305 super funds.

The Tax Office will be required to refund the overcharge to taxpayers involved together with interest at the rate of 5.62%. Cost to revenue will be in the order of \$150 million-\$180 million. The Tax Office does not yet know how it proposes to make the refunds and will make another public announcement soon. The Tax Office says it now has systems in place to ensure this does not recur.

COMPUTERS V. CARS

For all of us who feel only the deepest love and affection for the way computers have enhanced our lives and go some little way towards climbing the mountain of red tape imposed on us, read on. At a recent computer expo, Comdex, Bill Gates reportedly compared the computer industry with the auto industry and stated, "If GM had kept up with technology like the computer industry has, we would all be driving \$25 cars and get 1,000 miles to the gallon". In response to Bill's comments, General Motors issued a press release stating:

"If GM had developed technology like Microsoft, we would all be driving cars with the following characteristics:

- *For no reason whatsoever, your car would crash twice a day.*
- *Every time they repainted the lines in the road, you would have to buy a new car.*
- *Occasionally your car would die on the freeway for no reason. You would have to pull to the side of the road, close all of the windows, shut off the car, restart it and re-open the windows before you could continue. For some reason you would simply accept this.*
- *Occasionally, executing a manoeuvre such as a left turn would cause your car to shut down and refuse to restart, in which case you would have to re-install the engine.*
- *Macintosh would make a car that was powered by the sun, was reliable, five times as fast and twice as easy to drive – but would run on only 5% of the roads.*
- *The oil, water, temperature and alternator warning lights would all be replaced by a single "this car has performed an illegal operation" warning light.*
- *The air bag system would ask "are you sure?" before deploying.*
- *Occasionally, for no reason whatsoever, your car would lock you out and refuse to let you in until you simultaneously lifted the door handle, turned the key and grabbed hold of the radio antenna.*
- *Every time a new car was introduced, car buyers would have to learn how to drive all over again because none of the controls would operate in the same manner as the old car.*
- *You'd have to press the "start" button to turn the engine off."*

SUPERANNUATION GUARANTEE

You are required to make superannuation contributions for employees at a rate of not less than 9% of ordinary time earnings. Superannuation contributions must be paid within 21 days after the end of each quarter. If you fail to pay these contributions within the time limit you have to pay an equivalent amount direct to the Tax Office as a superannuation guarantee charge.

This payment becomes non tax deductible and you are required to pay an additional amount to cover the Tax Office's costs of receiving that money and passing it on to the employee's superannuation fund.

While, on pain of penalties and loss of tax deductibility, you must meet these deadlines, is the Tax Office similarly obligated? The Tax Office has issued a statement indicating that significant delays have occurred in relation to its administration of this legislation. It is currently addressing the issue and has started forwarding employee entitlements to their superannuation funds.

The Tax Office has given an assurance that superannuation payments collected by it will be paid to employee funds (or direct to employees where they have retired) "as soon as possible". Additional payments will be made to recompense funds for loss of interest earnings. But no GIC and penalties!

READER QUESTIONS:**TAX DEDUCTIONS – MARKETING EXPENSES****Question:**

We have been invoiced for food description tags for our new supermarket. The charge is 200 @ \$2 = \$400, can this be expensed?

Answer:

Expenditure on food description tags in a supermarket is most definitely tax deductible. If the tags form part of and are attached to the goods being sold, the Tax Office may consider that they form part of trading stock and their value must be included in the closing stock on hand. If the tags are kept separate from the stock being sold, the cost is tax deductible and no amount need be brought to account as stock on hand.

DEPRECIATION POOLS**Question:**

If I pool expenditure, does it need to be entered on the fixed asset register?

Answer:

We assume you mean the pooling of fixed assets or plant. If you are an STS taxpayer you can pool all plant items and you do not have to account for them separately in a fixed asset register. If you are not an STS taxpayer you can pool all items costing less than \$1,000 and, again, you do not have to account for those items in a fixed asset register. You do need to retain evidence of purchase for the required five year period (or two years for STS taxpayers).

LUXURY VEHICLES**Question:**

Just wondering if you could provide a working example of tax depreciation and GST on the purchase of a luxury vehicle costing, say, \$88,000 including GST.

Answer:

Let us give you an actual example of a Lexus purchased under hire purchase for an all up cost of \$114,922 including registration, insurance and GST. First deduct the registration and insurance as these are fully deductible expenses (if the vehicle is 100% business use), then deduct the maximum input tax credit which is one-eleventh of \$57,009. That amounts to \$5,182.64. You have the following sum:

Total cost of vehicle	\$114,922.00
Less registration and insurance	828.00
Less input tax credit	5,182.64
Net vehicle cost	\$108,911.36
Less depreciation cost limit	57,009.00
Balance of cost not depreciable	51,902.36

In addition, the hire purchase agreement shows that total terms charges amounted to \$24,082.96 and the total amount payable to the finance company was \$139,004.96. Your accounting entry would therefore be as follows:

	Debit	Credit
Motor vehicle (depreciable)	\$57,009.00	
Motor vehicle (non depreciable)	51,902.36	
GST – input tax credit claimed	5,182.64	
Registration and insurance	828.00	
Unearned terms charges	24082.96	
Finance Company		139,004.96

TAX DEDUCTIONS – INTEREST, RATES, ETC**Question:**

I am a director and shareholder of my company. The company purchased an investment property with a view to develop and sell it later at a profit. The borrowing to fund the purchase was in my name. I also paid the interest as well as many of the development expenses on behalf of the company.

The property was not sold within the intended time due to the property market slow down. There was no income derived from the property and costs such as interest, rates, land tax, building costs, etc were paid by me. The company had no income or financial means to make these payments. Can I claim the interest against other income I have received? Or must I wait until the property is sold and the company work out if there was any gain or loss on disposal? Can I claim for any capital costs paid on behalf of the company?

Answer:

It is important to remember that you and your company are treated separately for taxation purposes. When you consider tax deductibility of payments that you make you need to consider whether they were payments necessarily incurred to earn income (for yourself).

You have borrowed money at interest and (presumably) on lent that to your company, interest free. If that is the case, it would be difficult to claim a deduction for the interest as you cannot say it was incurred in order to earn income. If you lent the money to the company subject to interest (which will accrue pending sale of the property) you can claim the interest costs which will be offset by the interest earned from the company. In turn, the company can claim the accrued interest thereby incurring a loss which will be deductible against a future profit.

Alternatively, if you borrowed the money then paid it to the company as allotment money for the issue of additional shares you could claim the interest expense on the basis that it is an investment for purchase of shares in your company intended to earn income by way of future dividends. You cannot personally claim deductions for rates and land tax paid on behalf of the company. These are company expenses and must be claimed as deductions in the company tax return.

Building and any other capital costs which you have paid cannot be claimed at this stage. They must be treated as advances to the company, recorded as additional costs in respect of the land. These costs will eventually reduce the taxable gain when the property is sold.

PAYG WITHHOLDING**Question:**

We have been asked to pay an invoice for lawn mowing at a property we manage. The invoice does not include an ABN but we believe that the person would not earn over \$50,000. Do we have to withhold 48% from the account and remit this to the Tax Office? The landlord believes we don't. Can you refer us to a web page where we can find information on this type of situation?

Answer:

The \$50,000 threshold only relates to a requirement to register for GST. If an ABN is not quoted you must deduct PAYG Withholding Tax of 48.5% unless:

- The total payment is \$50 or less (excluding GST);
- The supplier is an individual under 18 and payments to that person do not exceed \$120 per week;
- The supply is wholly input taxed (e.g. financial supplies, residential rental or premises supplies, precious metals, food in tuckshops and canteens).

Provided you get a supplier statement you need not withhold if:

- The supply is made in a private capacity or as a hobby;
- The payment is exempt income to the supplier;
- The supplier is a non-resident, not carrying on a business in Australia;
- The supplier is not expecting to make a profit or gain.

For more information on this topic, visit www.ato.gov.au and type *statement by a supplier* in the search box.

GST – TRANSFER TO COMPANY

Question:

I was trading as a sole trader and incurred a GST liability of \$25,000. At the end of financial year 2004/05 I transferred the business to a company with a similar name. Is the company able to take on the GST debt which I incurred as a sole trader? If not, is there any way to incorporate the debt to make the company liable? I am the sole director and sole shareholder of the company.

Answer:

As explained in an answer to an earlier question, you and your company are treated as entirely separate entities for taxation and other purposes. The GST debt is your personal debt. The company can, of course, pay that debt if you wish but it will be paying the debt on your behalf and instead of owing the money to the Tax Office you will owe it to your company.

Your company will then need to consider the rules of Division 7A and FBT considerations if it is taken to have lent money to you as an employee and not charged interest. Check these out in *Australian Taxation Manual* at pages 48 and 78.

CGT AND TAX PLANNING

Question:

In the past two financial years we have sold two properties which attracted capital gains tax. For the tax year 2004/05 our accountant, who has acted for us for some years, "inadvertently" quoted on our return to the Tax Office the date of settlement rather than the contract date. He admitted to this oversight and subsequently we completed an amended return and paid the CGT which became due.

During this time we asked his advice about minimising the next amount of CGT payable as this would put us in a much higher tax bracket. He said he was unable to give specific financial advice. We subsequently went to a registered financial adviser who suggested investing the money through his firm in managed funds. I asked if this would be tax effective and he replied that we could take a look at the overall result before 30 June and then make a decision.

The due date passed without further advices from the financial adviser. We have since found that had some of the profit been placed in our superannuation fund, our tax liability would have been somewhat less as we are nearing 60 and there are special tax benefits available to near future retirees.

Our accountant has recently presented us with our latest return that is due for lodgement soon. Unfortunately, due to the overall confusion caused by the accountant and financial adviser not communicating we have missed our opportunity to place the required amount of funds into super.

Is there some provision in the Tax Act that will allow for an amendment of a return retrospectively as we are attempting to be self funded retirees and the amounts paid and payable could represent at least two years' income in retirement.

Answer:

Unfortunately, no. Superannuation contributions are deductible only if paid within the relevant income year.

NON CASH BUSINESS BENEFITS

Question:

We are a software company. A client issued us with a 5% shareholding in their new company in recognition of the contribution we made in relation to the restructure from a partnership to a company. We did not pay anything for the shares but since their issue, we have declared all dividends received as income.

We have recently been advised that we should have declared the value of those shares received as income based on their market value.

- We find it difficult to accept that we should be taxed on the value of the shares received because:
- We did not outlay any funds nor receive any funds from the transaction;
- We would have to pay tax on an amount which was not received in cash. This would have a significant adverse affect on our cash flow;
- In past years we could adjust our books for the value of invoices raised but not paid, surely these shares would be seen in a similar way?

Answer:

The advice you were given is correct. Section 21A of the Tax Act 1936 relates to non cash business benefits. These represent property or services provided to a business taxpayer wholly or partly in connection with a business relationship. Accordingly, the benefit is treated as income according to ordinary concepts even if it is not convertible into cash and you are required to include the arm's length value of the benefits as income in the year in which the benefit was received.

As the benefit was provided to you in a past year you should keep in mind that the Tax Office can only amend a past assessment within four years after the tax became due and payable under the original assessment. For companies this is deemed to be the date of lodgement of the original return and payment of the original tax.

PAYG WITHHOLDING - EXPATRIATES

Question:

I am writing this from our church headquarters in a suburb of Sydney. We have Australian citizens who go overseas to work as expats. During this tenure of work they are paid from the USA. At the completion of this tenure they get PR allowances and a couple of weeks' wages. Very often they come to us here in Australia to receive these wages and allowances. We make payment and we send the charge back to the USA. We do this because these payments relate to their service overseas.

When we pay these allowances, which we charge back to the USA, do we have to deduct tax?

Answer:

You are required to deduct PAYG Withholding only if they are entitled to the payments under a contract for service between the expats and the Australian church. Without going deeply into the structure of your church, it would appear this is not so. They travel overseas under contract between themselves and the church in the USA which is responsible for payment of emoluments.

When they return to Australia, the Australian church makes the payments, not under a contract between itself and the expats, but as agent for the USA church.

Look to the legal relationship between the expats and the Australian church. If the expats have no legal claim against the Australian church, they are not receiving payment for services rendered to the Australian church. Accordingly, we believe that the Australian church is not required to deduct PAYG Withholding.

FBT – TAX EXEMPT BODIES

Question:

When providing comment on FBT, can the tax exempt body point of view also be considered? Office Christmas parties are not exempt from FBT for tax exempt bodies.

Answer:

A tax exempt body is one which is wholly exempt from income tax or partially exempt (such as a club earning income from members and non members).

Non deductible entertainment expenses are subject to FBT when provided to employees or their associates.

Entertainment can be provided by way of food, drink or recreation or accommodation or travel in connection with such entertainment. This includes the provision of a Christmas party for employees and their associates.

The taxable value of meal entertainment fringe benefits can be determined by the 50/50 split method or the 12 week register method.

The 50/50 split method is determined by taking 50% of total meal expenditure for all persons (whether employees, clients or otherwise) for the FBT year and treating that amount as being subject to FBT.

The 12 week register method requires you to calculate the total meal entertainment costs for employees over a 12 week period and determining what that amount is as a percentage of total meal entertainment costs provided to all persons over that same period.

FBT – LAPTOP COMPUTERS

Question:

My Department (State Government) is considering an employment package proposal for provision of a laptop and some external accessories (listed below) to make it more user friendly. Could you please advise whether any of the items listed in the package would be excluded from the FBT exemption?

IBM Model 18605EM with:

- CPU – Intel 1.7GHz Pentium – M
- Memory – 512MB
- Disk – 40GB
- Wireless Network Adaptor
- Microsoft Windows XP
- Microsoft Office XP
- Instant Security Lock
- Warranty
- 17" LCD Monitor
- External Keyboard
- External Mouse
- Port Replicator
- Carry Case

Answer:

Section 58X of the FBT Act exempts the following items:

- Mobile Phone or Car Phone (if primarily used in employment);
- Protective clothing required for employment;
- Briefcase;
- Calculator;
- Tool of Trade;
- An item of computer software for use in the employee's employment;
- An electronic diary or similar item;
- A notebook computer, a laptop computer or a similar portable computer (only once per year).

The government has announced the exemptions will be extended to personal digital assistants (PDAs).

Clearly, a laptop computer is exempt, provided not more than one is supplied to each employee each year. Questions may arise in respect of the software components – Microsoft Windows and Microsoft Office as there is a condition in relation to the provision of computer software in that it must be for use in the employee's employment. If this condition is met, it is clearly exempt.

We believe that the part of the cost applicable to Microsoft Windows would retain an exemption because it is an integral part of the laptop computer. Without Microsoft Windows or a similar operating system, the computer would simply be inoperable and of no use. Hence, you can safely argue that it is part of the cost of the computer.

The provision of Microsoft Office however would be exempt only if it is for use in the employee's employment.

External keyboard and external mouse are accessories, whilst not necessities are of sufficiently common use to argue that they are a standard component of a laptop computer and therefore form part of its cost.

Similar arguments apply in relation to the carry case.

DIRECTOR'S QUOTE OF THE MONTH:

"Success is the Journey; not just the Destination"

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