



2011 CLIENT UPDATE

summer tax insight



EMPLOYING YOUR SPOUSE?

ENSURE THERE'S AN "EMPLOYMENT RELATIONSHIP"

Two recent cases before the Administrative Appeals Tribunal dealt with the scenario of a husband employing his wife to assist with looking after rental properties.

The question before the Tribunals was whether there was a "genuine employment relationship". As the two cases show, if it is found that there was no employment relationship in the circumstances, the taxpayer would not be entitled to deductions for salary or wages, fringe benefits, and superannuation contributions paid in relation to "employing" the spouse. Rather, the outgoings would be considered to be private or domestic in nature.

“ *It is not against the law to employ your spouse. However, the arrangement must be genuine and this requires examining the totality of the relationship when characterising it. As demonstrated by the cases, one cannot transform an existing domestic relationship simply by calling it a different name, or by adopting some aspects of an employment relationship.* **”**

TAX OFFICE HIGHLIGHTS COMMON PAYG INSTALMENT ERRORS

The Tax Office has been calling selected business operators in the \$2 million to \$100 million annual turnover range to discuss instances where the pay-as-you-go (PAYG) instalment amount received for the quarter under review is significantly different to the PAYG instalment amount received in a previous quarter.

The Tax Office has noted common errors that preparers make when completing PAYG instalment details on business activity statements – for example, instalment income amounts being adjusted rather than instalment rates varied.

If you are experiencing difficulty with correctly completing your instalment activity statements, please contact our office.

REFUNDS FOR OVERPAYMENTS OF GST

The Tax Office has released a ruling which sets out the Commissioner's views on the tax provisions which restrict refunds that can arise from the overpayment of GST.

The ruling also sets out the guiding principles the Commissioner will follow in exercising his discretion to pay a refund in appropriate circumstances. A circumstance where the Commissioner may consider exercising his discretion is where the overpayment of GST occurred as a result of an arithmetic error made by a supplier.

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If you believe you are eligible to claim a higher amount than the automatic \$550 deduction, please contact our office. However, you must have the documentation to support your claim.



AUTOMATED TAX DEDUCTION FOR YOUTH ALLOWANCE RECIPIENTS

The Tax Office has released its long-anticipated response to a recent High Court decision which held that a student taxpayer was entitled to a deduction for education expenses incurred in receiving Youth Allowance income.

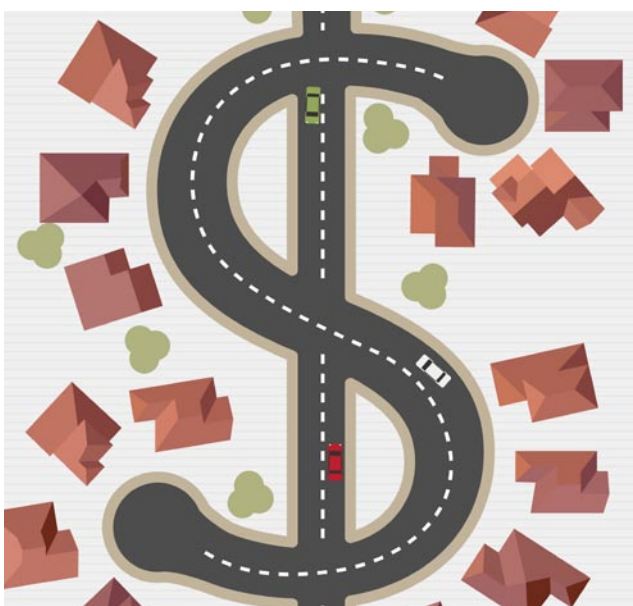
The Tax Office said it recognises that the High Court found that the expenses in this case were incurred in gaining or producing the Youth Allowance income received, and were not of a private nature. The Tax Office said it accepts that similar expenses would also be deductible to other full-time students receiving Youth Allowance income.

As a result, affected full-time students who received Youth Allowance and paid tax in the 2007, 2008, 2009 or 2010 income years will receive a notice from the Tax Office advising that their assessments will be amended to include a \$550 tax deduction for study expenses for each year they are eligible.

RETIREMENT VILLAGE SCHEME DEDUCTIONS WRONG, BUT TAXPAYERS TOOK “REASONABLE CARE”

In a recent case, the Administrative Appeals Tribunal remitted penalties imposed on a retired couple by the Commissioner for failing to take reasonable care in preparing their tax returns. Broadly, the Commissioner disallowed some deductions claimed by the taxpayers in relation to their retirement village scheme investment. Consequently, the Commissioner issued amended assessments and imposed the penalties.

The Tribunal noted the taxpayers spoke limited English. It also noted there was evidence that the taxpayers’ solicitor had also invested in the retirement village scheme. After having regard to the circumstances, the Tribunal formed the view that the position adopted by taxpayers in their returns could be argued on rational grounds to be right (ie a reasonable arguable position). Therefore, it concluded the taxpayers had exercised reasonable care in preparing their returns.



WHETHER A PROPERTY CONSTITUTES RESIDENTIAL PREMISES FOR GST PURPOSES

Under the GST Act, a sale of real property is “input taxed” (ie no GST is payable on the sale), if the property is “residential premises to be used predominately for residential accommodation”, and other requirements are met. Although the phrase from the GST Act appears straightforward, it has been subject to lengthy arguments before the courts.

In the most recent case, the Full Federal Court held that whether a property was residential premises to be used predominately for residential accommodation, and therefore input taxed, was to be determined objectively by reference to the physical characteristics of the property as at the date of acquisition.

Are you planning on selling a residential property? GST should be part of any tax planning considerations. Please contact our office for further advice.



trust update ▶▶▶▶▶▶

SMSFs AND PRIVATE COMPANIES INVESTING IN TRUSTS

TAX OFFICE WARNING

The Tax Office has warned self-managed super funds (SMSFs) not to invest in trusts with the intention of making funds available for lending to members.

The warning comes in a taxpayer alert which describes an arrangement where an SMSF invests money in an unrelated trust that then on-lends the funds to an SMSF member or relative. The Tax Office says such arrangements attempt to circumvent strict rules prohibiting SMSF trustees from lending money or providing financial assistance to a member or a relative using the resources of the fund.

In another similar taxpayer alert, the Tax Office warned private companies against investing in trusts with the intention of making funds available for lending to shareholders. The taxpayer alert describes an arrangement where a private company invests funds in an unrelated trust that then on-lends the funds to a shareholder or an associate of a shareholder. The Tax Office warns the arrangement may be an attempt to circumvent tax rules which are aimed at preventing private companies from making tax-free distributions of profits to shareholders or their associates.



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TRUST ENTITLEMENTS AND LOANS: TAX OFFICE ISSUES GUIDANCE

The Tax Office has released its keenly awaited guidance on the tax treatment of trust entitlements and loans.

The guidance, known as a practice statement, explains how the Tax Office will apply its ruling on when a private company with an unpaid present entitlement makes a loan to the trust estate which generated the entitlement. The Commissioner of Taxation said he was aware of the importance of this issue to businesses, particularly small businesses, which use a trust structure.

The Commissioner said the practice statement provides practical ways for businesses to work towards a compliant structure with minimal impact on their cash flows or how they operate. He said that where businesses had made mistakes in the past, the practice statement provides several options for private companies to self-correct.

THE OPPORTUNITY TO SELF CORRECT IS AVAILABLE FOR A LIMITED TIME ONLY. PLEASE CONTACT OUR OFFICE IF YOU THINK YOU MAY BE AFFECTED.

DECLARATION OF TRUST OVER LAND SOLD, SO NO PERSONAL TAX LIABILITY

A taxpayer has been successful in obtaining a declaration from the Supreme Court of Western Australia that a valid trust had been created over a property he had originally bought in 1990 under his own name. The trust had been declared in favour of a family trust at the time of the land's subdivision five years later. As a result, the Commissioner of Taxation could not argue that the taxpayer was personally liable for capital gains tax on one of the lots sold in 2006. Instead, the profit had been included in the family trust's tax return in that year and had been offset by the trust's carried forward losses.



STRONGER SUPER REFORMS ON THE HORIZON



The Government has announced its support for most of the wide-ranging Cooper Super System Review recommendations by releasing a package of reforms known as “Stronger Super”.

The proposed reforms feature a new low-cost and simple default superannuation product called “MySuper” which is marked to commence from 1 July 2013.

The Government also supports the Cooper Review’s “SuperStream” proposals. One of the proposals involves extending the use of an individual’s tax file number (TFN) as the primary identifier of member accounts from 1 July 2011. The proposal is said to assist individuals and trustees to locate and consolidate lost accounts. However, a member’s right to not quote a TFN will be maintained.

The Government also agreed with most of the recommendations dealing with self-managed super funds (SMSFs). One proposal is to provide the Tax Office with new powers to issue administrative penalties against SMSF trustees on a sliding scale according to the seriousness of the breach.

SUBSIDY PAID FOR LOSS-MAKING CONTRACTS ASSESSABLE AS INCOME

In a recent case, the Administrative Appeals Tribunal ruled that a taxpayer in the waste disposal business was assessable on a “subsidy” paid to it by a competitor in connection with the taxpayer assuming unprofitable waste disposal contracts that it acquired from the competitor under an agreement. Even though the transaction was a one-off, the Tribunal found it was assessable as ordinary income as the agreement was entered into in the ordinary course of the taxpayer’s business with a view to making a profit.

TRIBUNAL CAN’T REVIEW PRIVATE RULING DECISION AS RULING GIVEN FOR WRONG YEARS

A taxpayer has been unsuccessful before the Administrative Appeals Tribunal in seeking a review of the Commissioner’s decision to disallow its objection against a private ruling. Broadly, the Commissioner had made an adverse private ruling

regarding the deductibility of certain capital appreciation payments covering the 2003 to 2009 income years. However, the taxpayer had originally only sought a ruling covering the 2004 to 2008 income years.

In making its decision, the Tribunal held it lacked the jurisdiction to review the Commissioner’s decision because the ruling was made in respect of the wrong years of income which invalidated the ruling. As a result, the Tribunal concluded there was no decision capable of being reviewed.

“LOAN” FROM PRIVATE COMPANY AN “HONEST MISTAKE”?

Under the tax law, certain payments and loans made by a private company to its shareholders or associates, and debts owed by its shareholders or associates that are forgiven by the private company, are taken to be unfranked dividends paid by the private company. However, there are specific exceptions to this rule.

In addition, the Commissioner has the general discretion to disregard the rule if the operation of the rule has arisen as a result of an “honest mistake” or “inadvertent omission” caused by the recipient of the dividend or the private company.

To assist taxpayers, the Tax Office has released a ruling which sets out the Commissioner’s views on the terms. The ruling notes that the onus is on the taxpayer to demonstrate that an honest mistake or inadvertent omission has occurred. The ruling states that the actual state of mind or belief of the person making the mistake or omission is in issue.

INCREASING ADJUSTMENTS IN BASS AS DEBTS REMAIN UNPAID

In another case, the Administrative Appeals Tribunal held that three taxpayers were required to reverse earlier claims for input tax credits in their later Business Activity Statements. As the taxpayers accounted for GST on an accruals basis, the credits were attributed to the tax period in which the tax invoices were received. However, those invoices remained unpaid after 12 months. Under the GST legislation, if an invoice remains outstanding after 12 months, a recipient is required to reverse any input tax credits previously claimed. The Tribunal noted there was little evidence of the invoices being paid, and therefore affirmed that the taxpayers had an increasing adjustment.