client alert | explanatory memorandum

February 2019

CURRENCY:

This issue of **Client Alert** takes into account developments up to and including 18 January 2019.

Tax clinic trial to reduce tax regulatory burden

To help reduce the regulatory burden on businesses, including the tax burden, Assistant Treasurer Stuart Robert has announced that the Federal Government has allocated $1 million to set up 10 tax clinics under a trial program based on the Curtin University Tax Clinic.

Each clinic will receive up to $100,000 for 12 months to support unrepresented individual or small business taxpayers by providing general taxation advice and helping them with their tax obligations and reporting requirements. The clinics, through identifying issues and building greater understanding of the tax system in operation, are also designed to improve the interactions that small businesses and individual taxpayers have with the ATO. The clinics will cover advice, representation, education and advocacy.

The 10 clinics will be established in major and regional universities across the country that already have complementary courses and faculties, providing broad coverage across Australia. The shortlisted universities are: ANU, Charles Darwin University, Curtin University, Griffith University, James Cook University, University of Adelaide, University of Melbourne, UNSW, University of Tasmania and the University of Western Sydney.

While this trial includes 10 universities to keep the size manageable, the government wants broad involvement, and to work with other universities as well in future. This could include looking at partnership models, small grants, research proposals and fresh ideas.

Mr Robert said the government hopes the trial tax clinics will "fill a gap in the market for those individuals and small businesses that may not be able to afford proper advice and representation".

The tax clinics are also designed to build practical experience for students who are the future of the tax profession. The trial will offer student volunteers the opportunity to work with unrepresented taxpayers under the direct supervision of qualified tax professionals.

The tax clinics are expected to be up and running by March 2019, and the trial will wind up by December 2019.

Source: http://srr.ministers.treasury.gov.au/speech/001-2019/.

New "work test" exemption for recent retirees

The Federal Government has created a new opportunity for some recent retirees to make additional superannuation contributions. From 1 July 2019, a 12-month exemption from the "work test" for newly retired individuals aged between 65 and 74 years with a total superannuation balance below $300,000 means many older Australians will now have an extra year in which to boost their superannuation savings. If you wish to take advantage of this measure, you should plan carefully to manage the relevant timing issues, your contributions caps and interaction with other contributions measures that may be available to you.

Many superannuation members are surprised – and sometimes frustrated – to learn that Australia's superannuation system places tight restrictions on who can make contributions after age 65. Generally, people aged between 65 and 74 years must satisfy a "work test" in order to make:

- non-concessional contributions (ie personal contributions for which the member does not claim a deduction); and
- concessional contributions above mandatory employer superannuation guarantee contributions (eg personal contributions for which the member claims a deduction or extra salary-sacrificed employer contributions).

The work test requires that the person is "gainfully employed" for at least 40 hours in any 30-day consecutive period during the financial year in which the contributions are made.

A person is "gainfully employed" if they are employed or self-employed for gain or reward in any business, trade, profession, vocation, calling, occupation or employment.

Satisfying the test can be difficult for retirees who want to build their superannuation savings. Passive income (eg rent or dividends) and unpaid work are not considered to be "gainful employment". Frustratingly, even those engaged in paid work may not meet the work test if their work is more irregular than the "40-hours-in-30-days" rule permits.

To assist these members with their superannuation planning, the government has recently created a new 12-month exemption from the work test for recent retirees aged between 65 and 74 years with a total superannuation balance below $300,000.

This measure will be available from 1 July 2019. For qualifying individuals, the exemption applies for 12 months following the end of the financial year in which the person last met the work test, giving these retirees an extra year in which to boost their superannuation savings.

Here are some important points to consider:

- The $300,000 balance threshold is tested on 30 June of the previous financial year.
- The exemption is only available for one 12-month period in an individual's lifetime. If a person utilises the exemption and later returns to work, they cannot utilise the exemption a second time when they subsequently retire again. However, if they did not rely on the exemption to make any contributions the first time they stopped working, they are entitled to utilise the exemption the next time they retire.
- The exemption is not available to members aged 75 and over. These members are subject to separate (and much more restrictive) rules about making contributions.

So, how much can a member contribute during the 12-month grace period? Fortunately, the individual may make contributions up to the usual concessional and non-concessional contributions caps for the particular year ($25,000 and $100,000 respectively). Also, people who turn 65 during the year in which they utilise the work test exemption may benefit from accessing "bring forward" arrangements (still in draft form) to make non-concessional contributions of up to three times the usual annual cap (currently $300,000, ie three times the $100,000 cap).

Source: https://www.legislation.gov.au/Details/F2018L01682.

ATO issuing excess super contributions determinations

The ATO has begun issuing determinations for excess concessional contributions (ECC) of superannuation for the 2017–2018 financial year. The ATO said it will be issuing a higher volume of ECC determinations for 2017–2018 compared to previous years, following the reduction in the concessional contributions cap to $25,000 for all taxpayers.

Taxpayers who receive an ECC determination should also expect an amended tax assessment, as ECCs are automatically included in an individual's assessable income (and subject to a 15% tax offset). An ECC charge (4.96% for July to September 2018) is also payable to take account of the deferred payment of tax.

Electing to release excess contributions

Individuals who receive a determination then have 60 days to elect to release up to 85% of their excess contributions from their super fund to the ATO as a "credit" to cover the additional personal tax liability.

Once made, the election cannot be revoked. Therefore, taxpayers should ensure that their super fund has correctly reported their contributions to the ATO for the correct person and financial year before making an election to release any excess contributions.

Electing to release an amount of ECCs can also be important for some taxpayers who wish to prevent the automatic operation of the bring-forward rule for non-concessional contributions.

The proportioning rule does not apply to a release authority payment, so such an amount paid from a super fund will always reduce the taxable component of a superannuation interest in accumulation phase. Therefore, a taxpayer with multiple superannuation interests should consider nominating the release amount to be paid from the interest with the largest taxable component. However, take care if looking to maintain an unrestricted non-preserved component – any benefit payment from a particular superannuation interest will be cashed out first from the unrestricted non-preserved component.

Release authorities

The ATO says tax practitioners and super funds should be prepared for increased numbers of calls from clients about ECC determinations, and funds should anticipate the receipt of release authorities that will require prompt action.

From 1 July 2018, the ATO issues release authorities directly to the taxpayer's super fund so that the individual is no longer involved in releasing such amounts (apart from requesting that the ATO issues a release authority to a specific super fund). The fund must then pay the amount to the ATO within 20 business days (this period has been temporarily extended from 10 business days).

Defined benefit funds

Determinations for taxpayers with a constitutionally protected fund or defined benefit fund will issue at a later time. Determinations for excess non-concessional contributions and assessments for Div 293 tax also began issuing throughout December 2018.

Source: www.ato.gov.au/Super/APRA-regulated-funds/In-detail/News/CRT-Alerts/2018/CRT-Alert-083/2018---Expected-increase-in-ECC-determinations/.

Reviewing the tax treatment of granny flats

Assistant Treasurer Stuart Robert says the Federal Government has asked the Board of Taxation to undertake a review of the tax treatment of "granny flat" arrangements, and to recommend potential changes. This request for review is in response to the 2017 Australian Law Reform Commission's report *Elder abuse: a national legal response*, which identified the development of formal and legally enforceable family agreements as a measure to prevent elder abuse.

Under current tax laws, homeowners may have to pay CGT where there is a formal agreement for a family member to reside in their home – for example, when an older parent lives with their child, either in the same dwelling or a separately constructed dwelling (ie a granny flat). In some cases, the tax consequences have deterred families from establishing a formal and legally enforceable family agreement, which leaves no protection of the rights of the older person if there is a breakdown in the agreement.

The Board of Taxation's review will consider and make recommendations on the appropriate tax treatment of these arrangements, taking into account the interactions between the current tax laws and treatment of "granny flat interests" under the social security rules. In making the recommendations, the review will consider how any changes could raise awareness and provide incentives for older people and their families to enter formal and legally enforceable family arrangements.

The Board is expected to commence the review in early 2019, including broad consultation with stakeholders, with a final report due to the government in the second half of 2019.

Source: http://srr.ministers.treasury.gov.au/media-release/047-2018/.

Resolving tax disputes: government to help small businesses

In late 2018, Assistant Treasurer Stuart Robert announced that the Federal Government intends to make it easier, cheaper and quicker for small businesses to resolve tax disputes with the ATO. The government will establish a Small Business Concierge Service within the Australian Small Business and Family Enterprise Ombudsman's office to provide support and advice about the Administrative Appeals Tribunal (AAT) process to small businesses before they make an application.

The government will also create a dedicated Small Business Taxation Division within the AAT, with key features including:

- a case manager supporting them throughout the process;
- a standard application fee of $500;
- fast-tracked decisions, to be made within 28 days of a hearing; and
- where the ATO appeals the AAT decision to the Federal Court, it will pay the small business reasonable costs.

Source: http://srr.ministers.treasury.gov.au/media-release/046-2018/.

Small business tax offset: avoiding errors when claiming

The ATO has issued tips for avoiding common errors when reporting net small business income and claiming the small business income tax offset for unincorporated small businesses.

While the aggregated turnover threshold to qualify as a small business entity is $10 million, the threshold for accessing the small business income tax offset is $5 million. The offset (up to $1,000) is worked out by the ATO on the proportion of income tax payable on an individual's taxable income that is net small business income. For 2018–2019 and 2019-2020 the rate of offset is 8%; this will increase to 13% for 2020–2021 and 16% for 2021–2022 onwards (to complement the reductions in the company tax rate for base rate entities).

ATO tips

To avoid errors when reporting net small business income in a tax return, the ATO offers the following tips:

- *Item 13:* Include net income derived by the small business partnership or trust at either item 13D or 13E, not at 15A. The amounts to include at item 13D or 13E are the: (i) share of net small business income from a small business partnership (in which they are a partner); and (ii) share of net small business income from a small business trust (in which they are a beneficiary). The amounts reported at these items must be reduced for any related deductions, such as landcare operations, decline in value for water facilities and prior year deferred non-commercial losses of partners claimed this year. The ATO says it uses these labels to calculate the offset but they are not counted towards the taxpayer's taxable income. This means that a distribution from a partnership or a share of net income from a trust must be included at the relevant item – 13N, 13L, 13O or 13U.
- *Item 15A:* Don't include the following types of income at item 15A, as they are not eligible for the offset: (i) personal services income – this is reported at item 14A (although income from carrying on a personal services business is included at item 15A); (ii) salary, wages or directors fees; (iii) dividend income of directors. Also, don't include any share of net small business income from partnerships and trusts at item 15A. This is reported at item 13D or 13E.
- *Complete all relevant fields:* Enter the taxpayer's net small business income from sole trading activities at item 15A so the ATO can calculate the offset. This item does not contribute towards their taxable income. This means that sole trader business income must be included at item 15A, as well as at P8 (Business income and expenses) and 15B or 15C (Net income or loss from business).
- *Net income, not gross income:* Include the taxpayer's net small business income at item 15A for sole traders (and share of net small business income at item 13D or 13E for partnerships and trusts). Do not use gross income.

Source: www.ato.gov.au/Tax-professionals/TP/Claiming-the-small-business-income-tax-offset/.

Home office running expenses and electronic device expenses

On 16 January 2019, the ATO released an updated version of Practice Statement PS LA 2001/6, its guidance on calculating and substantiating home office running expenses and electronic device expenses. PS LA 2001/6 has been significantly rewritten, as follows:

- the basic principles (prerequisites for deductions) have been amended to emphasise that a taxpayer must *actually* incur the expense and that there must be a *real* connection between the use of the home office or device and the taxpayer's income-producing work;
- the requirement that the income-producing use must be substantial and not merely incidental has been removed;
- there is new commentary on what type of evidence needs to be kept;
- the cents per hour rate for home office running expenses has been increased from 45 cents to 52 cents per hour, effective from 1 July 2018;
- there is new commentary on claiming up to $50 for all device usage charges where work use is incidental and detailed documentation is not kept;
- there is some change in terminology (eg from "home office expenses" to "home office running expenses" and from "business" to "work-related");
- the ATO specifically refers to cleaning expenses and the decline in value of furnishings as examples of home office running expenses;
- PS LA 2001/6 now specifies what it does not apply to (computer consumables, stationery, home office occupancy expenses and the decline in value of electronic devices); and
- commentary on ATO benchmarks and safe harbours has been removed.

Evidence of expenditure and extent of deductibility

PS LA 2001/6 now states that the level of evidence required to prove that expenditure has been incurred is less than that needed to substantiate the expense. In particular, the ATO accepts that bank and credit card statements can be used to demonstrate that expenditure has been incurred. For example, a bank statement in the taxpayer's name clearly showing a payment to a gas provider is acceptable evidence that gas expenditure has been incurred.

The ATO says that taxpayers can substantiate their deductible (work) use proportion by providing:

- evidence of the proportion of deductible use for the whole income year, such as itemised supplier records which have the taxpayer's work use proportion for the applicable period marked on each record as evidence of their annual claim for deduction;
- records showing their detailed usage pattern over a representative period (eg a diary record of use over a representative four-week period) – although the ATO warns that taxpayers can only use a representative period if they have one; or
- a reasonable estimate, but only in relation to a small claim for home office running expenses where the taxpayer can demonstrate that the estimate was reasonably likely under the given circumstances.

Special rules for home office running expenses

The ATO says that taxpayers can use one of two methods to calculate their home office running expenses:

- keep records and written evidence to determine their work-related proportion of actual expenses incurred, or
- use a rate of 52 cents per hour – this method incorporates all of the items that can be claimed as home office running expenses, including lighting, heating, cooling, cleaning costs and decline in value of home office items such as furniture and furnishings in the area used for work. The ATO says that taxpayers only need to keep a record to show how many hours they work from home. They can do this over the course of the income year, or if the work-from-home hours are regular and constant, by keeping a record for a representative four-week period.

Device usage expenses

Similarly, taxpayers can use one of two methods to calculate their device usage expenses:

- keep records and written evidence to determine their work-related proportion of actual expenses – expenses can be apportioned on a time basis or data basis; or
- claim up to $50 in total for all device usage charges where detailed written evidence is not kept. The ATO says this method is appropriate where work use is incidental. Taxpayers can keep basic records that are based on rates of 25 cents per work call from a landline, 75 cents per work call from a mobile and 10 cents per work-related text message.

Genuine redundancy payments: alignment with Age Pension age

The Federal Government has announced that it will amend the law to extend the concessional tax treatment for genuine redundancy payments and early retirement scheme payments to align with the Age Pension qualifying age.

Currently, an individual must be below age 65 at the time their employment is terminated to qualify for a tax-free component on a genuine redundancy payment or an early retirement scheme payment. Genuine redundancy payments are made when a job is abolished, and early retirement scheme payments are made when a person retires early, or resigns, as part of a scheme put in place by an employer. Where an individual is under age 65 and meets the other requirements in Subdiv 83-C of the *Income Tax Assessment Act 1997*, they receive tax-free a base amount of $10,399 (for 2018–2019), plus $5,200 for each whole year of service.

The government said it will amend the law to align genuine redundancy and early retirement scheme payments with the Age Pension qualifying age from 1 July 2019. The Age Pension age will be 66 on 1 July 2019, rising to 67 by 1 July 2023. The change will mean that all individuals aged below the Age Pension qualifying age will be able to receive a tax-free component on the payment they receive from their employer in these circumstances.

Take, for example, a 65-year old with 10 years of service whose job is abolished, and who receives a $100,000 redundancy payment. Currently, as they are aged over 65 years, they would not receive a tax-free component and would pay $15,000 tax. Under the proposed changes, the individual would pay $5,640 in tax, saving $9,360.

Source: http://jaf.ministers.treasury.gov.au/media-release/073-2018/.

GST on property developments involving government

In late 2018, the ATO released Taxpayer Alert TA 2018/3 *GST implications of certain development lease arrangements*.

The ATO says it is reviewing arrangements involving property developers acquiring land from government entities, specifically where the developer provides development works to the government entity as payment for the land.

The ATO is concerned that some developers and government entities are not reporting the value of their supplies under these arrangements in a consistent manner, resulting in GST being underpaid.

One of the scenarios under review has the following features:

- A government entity agrees to supply land to a property developer. The agreement requires the developer to pay an amount of money, and also to do certain development works, as payment for the supply of land.
- The developer pays the amount of money to the government entity.
- The government entity may grant the developer a short-term lease, or licence, to allow the developer to complete the development works on the land.
- Upon completing the development works, the developer invoices the government entity for the value (including GST) of the development works.
- The government entity then supplies the land to the developer by granting the developer a long-term lease, or transferring title, over the land.

Following from this, when reporting their GST obligations in their activity statements:

- The government entity claims an input tax credit for the amount of GST included on the developer's invoice for the supply of development works. However, the government entity only reports the monetary payment received for the land, not including the value of the development works the developer provided as payment for the land.
- The developer does not report the supply of the development works it invoiced to the government entity. This results in the developer not paying GST on the development works provided to the government entity, despite having claimed input tax credits on all the acquisitions it used in completing those development works.
- The developer may include the value of all the development works completed on the land (including those it invoiced to the government entity) in the cost of the development when applying the margin scheme. This significantly reduces the amount of GST the developer pays on its supply of the property (as vacant land or a residential unit) to a customer.

The ATO is engaging with taxpayers and government entities to examine the issues of concern and ensure that all parties correctly account for their GST and income tax obligations in such situations. Fraud or evasion provisions "may be considered" where there is a change in how the arrangement is accounted for after the fact, so as to gain an advantage due to the lapse of the statutory periods for amending activity statements.

Source: www.ato.gov.au/law/view/document?docid=tpa/ta20183/nat/ato/00001.

Thomson Reuters would like to hear from you

Subscribers are invited to submit topics for articles for future publication. Information should be sent to:

Publisher – **Client Alert**
Thomson Reuters (Professional) Australia Limited ABN 64 058 914 668
PO Box 3502, Rozelle NSW 2039
Tel: 1800 074 333
Email: contentfeedback@thomsonreuters.com
Website: www.thomsonreuters.com.au