# ASHBY ROMA & CO

Client Information Newsletter - Tax & Super

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# Who and what is on the ATO's radar this year?

The ATO has small businesses, trusts, wealthy individuals and self-managed superannuation funds (SMSFs) firmly in its sights this year as it outlined which high-risk businesses and individuals it will focus on in its 2013-14 compliance crackdown. Below are the key scrutiny areas you should know about.

## Payment of superannuation guarantee (SG)

Given the recent increase in the SG rate from 9% to 9.25%, the ATO will monitor employers to ensure they are paying their employees the correct superannuation amounts. Under the new director penalty regime (consult this office for more information), directors of employer companies may be held personally liable for their company's unpaid SG debt. As a result of employee complaints in the following industries, the ATO will contact around 12,000 employers in:

- cafes and restaurants
- carpentry services, and
- real estate services.

## CGT non-disclosure and under-reporting

The ATO is on the lookout for businesses engaged in complex restructuring in attempts to disguise asset sales or manipulate asset valuations to artificially reduce their CGT liabilities, and will conduct a number of audits and reviews to clamp down on these businesses.

"Some businesses attempt to reclassify revenue and capital items so they can inappropriately access concessional tax treatments. Others simply fail to disclose capital gains tax events or they claim the small business concessions when they are not eligible."

## Failure to identify and report fringe benefits

The ATO's recent compliance activity on car fringe benefits revealed that in many cases where there was a fringe benefits tax (FBT) adjustment, employers had simply failed to recognise and report their FBT obligations. The ATO will increase its efforts to identify employers that may have an FBT obligation but are not in the FBT system.

## Goods and services tax (GST)

GST is always on the forefront of ATO compliance activities, but this year it will focus on businesses in the mining, wholesale trade, manufacturing, financial and insurance services, government and retail trade in particular.

The ATO will also continue to monitor and investigate taxpayers that incorrectly report GST when they acquire, use, develop, sell or transfer real property – using external data to match property transactions with business activity statements (BAS) to identify under-reporting of sales.

## Fraudulent phoenix activity in real property

The ATO has identified more than 2,000 property developers who have placed companies into

### About this newsletter

Welcome to Ashby Roma & Co's client information newsletter, your monthly tax and super update keeping you on top of the issues, news and changes you need to know. Should you require further information on any of the topics covered, please contact us via the details below

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### Also in this issue:

liquidation to avoid financial obligations such as PAYG withholding, income tax, GST and super liabilities, and will demand lodgment from these developers, enforce payment and apply penalties.

## Research and development (R&D)

A business's records must clearly demonstrate the necessary direct link between registered R&D activities and expenditure being claimed for the purposes of the R&D Tax Incentive (consult this office to find out more). Where the expenditure is between associates, the ATO will look to ensure that the amounts have been paid and that any mark-ups between connected or affiliated entities have been excluded. Further, the ATO will work closely with AusIndustry to ensure that the new definition of R&D activities is being appropriately applied.

## Taxable payments reporting in the building and construction industry

From July 1, 2012, businesses in the building and construction industry must report the total payments they make to each contractor for building and construction services each year. The ATO will address identified compliance problems including:

- non-lodgment of tax returns
- omission of contract income by contractors in their tax returns, and
- non-compliance with GST obligations.

## Small businesses in the cash economy

Using increasingly sophisticated risk models, industry comparisons, data matching, community information and new audit approaches, the ATO will identify businesses that under-report income tax or GST and unfairly compete with honest businesses.

## Private company schemes

The ATO will continue to focus on tax avoidance schemes that attempt to extract profits from privately-owned businesses in ways that reduce or eliminate the original shareholder's tax liability, including:

- the creation of new share classes to stream dividends to associated entities with lower tax rates or accumulated losses, and
- claiming inflated deductions to reduce reported profits so that funds can be transferred to shareholders or associates without triggering the deemed dividend rules.

## Employers that misreport PAYG withholding

The ATO will also pay attention to those who may not be meeting their PAYG obligations by using intelligence gathering and information matching as well as conducting reviews and audits when it detects discrepancies that indicate employers are not withholding and reporting correctly.

## Australian Business Register (ABR)

The ATO will contact over 600,000 Australian business number (ABN) holders asking them to check that their business details are up-to-date on the register. Further, the ATO will data match to identify businesses that are no longer trading and cancel their ABNs, as well as focus on registrants that it believes are not entitled to ABNs, particularly where the ATO considers they are employees rather than contractors.

## Activity statements

This year, the ATO will increase the number of default assessments issued to businesses that persistently fail to lodge activity statements. Using data matching, the ATO is able to identify whether a business has income or is trading, and then use this information to estimate tax owed. Default assessments are issued with penalties of up to 75% of the tax liability – a clear incentive for taxpayers to lodge before the ATO gets to them.

## Misuse of trusts, including omitted income

The growth in trusts has resulted in an increasingly prevalent scheme where trustees artificially reduce trust income in an attempt to direct tax liabilities to certain beneficiaries, who have little or no capacity to pay the debt while actually using the income for their own benefit. The ATO has introduced new labels in the trust return to help it identify such schemes.

## Unusual refunds

In cases where a refund is unusual or there appears to be some suspicious activity, the ATO will contact the business to understand the nature of the enterprise and what gave rise to the refund. The ATO will identify around 2% of refunds for review.

## Self-managed superannuation funds (SMSFs)

The ATO monitors the registration of SMSFs using information on the ABR. If an SMSF is in its first year of operation and the ATO considers it highly likely that the fund will not operate correctly, the ATO will

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remove its lodgment concession – meaning the fund must lodge by October 31. The ATO will not issue a notice of compliance until after the fund has lodged its first annual return and the ATO is satisfied that the fund is doing the right thing.

When it comes to established SMSFs, the ATO will focus on:

- whether the fund has been established as a genuine super fund
- lodgment obligations
- the use of prohibited loans
- related party transactions
- funds with a history of non-compliance, and
- incorrect reporting of exempt current pension income, tax losses and non-arm's length transactions.

## Wealthy individuals using complex business structures

On the same note, wealthy individuals were found to use strategies to avoid their tax obligations – such as failing to report all income (including dividends, capital gains, and income from foreign sources). As a result, the ATO is set to contact wealthy taxpayers where the distinction between business and personal income and expenses are blurred, asking them to explain situations in which their wealth appears inconsistent with reported tax and economic performance.

## Incorrect claims for work-related expenses

This year, the ATO will pay particular attention to:

- building and construction labourers, construction supervisors and project managers
- sales and marketing managers, and
- high work-related travel expenses across individual income tax returns.

## Individuals who fail to declare income or claim deductions and benefits incorrectly

Apart from identifying discrepancies – such as when individuals do not report some or all of their income – the ATO is set to further expand its information-matching program and check the correct reporting of:

- private health insurance rebate claims
- flood levy exemptions
- taxable government grants and payments, and
- certain payments to contractors in the building and construction industry.

The ATO will continue to provide advice to new rental property owners as well.

## Tax planning schemes

Domestic promoters and participants in illegal tax planning schemes that promise high investment returns and significant deductions to self-funded retirees are in the spotlight as well.

Consult this office on what you can do to avoid the ATO's compliance spotlight. ■

# *Did you know...*

## We're the most generous nation on earth (but the wealthy could help more)

Australia is the most giving country on the planet according to a new global index that measures charitable giving, from both companies and individuals. Compiled by the international Charities Aid Foundation (CAF), the World Giving Index for 2012 put Australia at the top of its list of the 20 best countries in terms of donating money, volunteering time and helping strangers. The index used data compiled by Gallup, and ranked 153 countries according to how charitable are their populations. Australia also topped a new five-year index from CAF, spanning from 2007 to 2011 (the most recent year of research). Overall, 76% of Australians gave money to a good cause in the past month of research data, up on the year before.

However according to the most recent figures released by the ATO (which after all adjustments and finalising is for the 2009-10 financial year), charitable giving by Australia's wealthier individuals has actually plummeted, with those earning more than $1 million a year becoming less generous. ATO statistics showed that claims for tax-deductible donations of those earning more than $1 million annually have dropped from a collective $511 million two years prior to $120 million for 2009-10. While the same 60% of wealthy Australians are still giving, the average donation has shrunk from a high of $100,000 two years ago to $27,450 — which is around 73% less for the 2009-10 year. The remaining 40% of our wealthier citizens seem to have not submitted a deduction claim for giving to charity at all. ■

# How a mortgage offset account works

"Mortgage offset account", "offset home loan", "interest offset account" or simply "offset account" — they are all interchangeable labels for the same financial product provided by banks. It is essentially a savings account that is linked to a loan account.

An offset facility contains two bank accounts: (1) a transaction account (meaning you have access to the funds) that is linked to (2) a loan account. The transaction account offsets the interest that is charged to the loan (hence the consistent use of the term "offset").

So unlike a straight-out loan arrangement, the offset account works like a regular savings account. Also any notional interest on savings may be earned at the same rate as the linked loan.

Savings in your offset account can help to reduce loan principal over time, allowing you to pay off your loan sooner or build up equity. Take for example the scenario of a couple with a $100,000 mortgage (just for simple arithmetic) and $10,000 in a linked offset account:

- the principal on the $100,000 loan is reduced by the $10,000 offset account to $90,000
- as a result, interest only accumulates on the $90,000 balance of the loan
- repayments continue to be made on the entire $100,000 principal and applicable interest
- savings in the offset account are actively working to reduce the loan, while repayments are working more effectively to reduce both the principal and interest it attracts.

## Potential strategies

While the old-school sage advice may have been to pay off the home loan as soon as possible, using a mortgage offset account can provide more benefits, especially when used tax effectively.

One strategy to consider centres on the fact that a mortgage offset account can actually be used as an all-in-one transaction account to manage your cash flow on a regular basis.

If you have an investment loan and a home loan, you could direct your salary as well as any rental income into an offset account that is linked to your home mortgage. This will give you the advantage of having both income sources (salary plus rental income) contribute to offsetting interest on your home loan. In any event, you will continue to pay principal and interest on your investment loan from your personal cash flow. An interest deduction however may be available in respect of the investment loan.

Another tactic (which will very much depend on how financially disciplined you are) can be to put all your monthly living expenses on your credit card, thereby being able to leave aside as much money as possible in an offset account for most of the month. The "plastic" debt is then cleared once a month (and timing is essential) from the funds held in the offset account. Some lenders have a set-and-forget "sweep" function to allow this to be done automatically.

By doing this, your salary and any other income that is directed to the offset account works to reduce your interest bill for the month. When making your regular loan repayment, more of it can go towards paying off the principal as you will have saved a bit of interest.

With both of the above, the icing on the cake comes from the fact that most home loans have interest calculated on a daily basis. Over the month, the days spent with extra funds sitting in the offset account is actively working to reduce your overall interest liability.

## Potential pitfalls

Keep in mind however that not all home loans are offered with an offset facility. Generally the very basic home loans that are on offer do not, so having an offset account may require you to go for a more fully featured mortgage account, and the problem with some of these is that they may come with a higher interest rate. There may also be a difference in fees charged.

Therefore, before deciding to go for the home loan featuring an offset facility, you will probably need to consider your financial situation and calculate whether or not you will expect to generally have enough money placed in the offset account to make it worthwhile. If you don't expect to be able to maintain a decent balance in the offset account, a cheaper home loan may be a better option. Our office can help you with these considerations.

It is also worth noting that the ATO has been cracking down on certain mortgage structuring arrangements whereby increased interest deductions are claimed in respect of investment loans. Particular emphasis has been placed on "split loan" arrangements and other such structures. If an arrangement sounds too good to be true, it could result in you getting into trouble with the taxman. Contact this office to find out more. ■

# Get up-to-date with the July 1 super changes

To help you keep abreast with the latest changes, we have compiled a guide to which reforms did and did not make it as of July 1, 2013 – including ones that affect self-managed superannuation funds (SMSFs).

## What made it?

### *1) SMSF supervisory levy rise*

The supervisory levy increased from $191 in 2012-13 to $259 in 2013-14 and subsequent years. The higher levy will be collected in the year of income.

### *2) Increase in superannuation guarantee (SG)*

As most of you would have heard by now, employers have to pay more into employees' super accounts after the SG rate increased from 9% to 9.25% for 2013-14 and will continue to incrementally increase up to 12% by 2019-20.

For employees who are paid at a rate set by an industrial award and employees who have their pay set by a collective agreement, employers are not allowed to reduce their wages to offset the SG increase. However, employees whose wages are not set by an award or a collective agreement may see their take-home pay affected.

If an employee's contract of employment is a salary package deal (that is, a salary plus superannuation), employers may be able to reduce the take-home salary by 0.25% to keep with the agreement to pay no more than the total package.

As all political parties have agreed to subsequent SG rises in the future – albeit at different times – businesses will not know for certain when the next increase to the SG will be until after the federal election.

### *3) SG age limit abolished*

The maximum age limit for paying superannuation for an employee was removed – meaning that if you employ a worker over 70 years old, it is now compulsory to pay them SG if they earn more than $450 a month.

### *4) Changes to concessional contributions caps and excess contributions tax*

From July 1, there was an increase in the concessional contributions cap from $25,000 to $35,000 for people aged 60 and over. From 2014-15, people who are 50 and over will also benefit from the higher cap of $35,000.

Also from July 1, if you go over your concessional contributions cap, the excess will be taxed at your personal tax rate plus interest – instead of at the highest tax rate of 46.5%.

Additionally, you have the choice of paying the excess contributions tax personally through your superannuation fund, or refunding any amount of excess concessional contributions from your fund. An interest rate charge will apply to this refund, calculated back to the start of the financial year.

### *5) Top earners to have reduced concessions*

Backdated to July 1, 2012, this legislation only recently passed Parliament. Under this measure, individuals earning an adjusted taxable income (consult this office for details and for what makes up your adjusted taxable income) of more than $300,000 will have their contributions tax rate doubled from the flat rate of 15% to 30% (excluding Medicare levy).

### *6) Government co-contributions diminishes*

Backdated to July 1, 2012, the higher income threshold against which co-contributions are assessed has been reduced from $61,920 to $46,920 and the maximum co-contribution matching rate is reduced from 100% to 50% for contributions up to $1,000.

### *7) Low income super contributions (LISC) – tax rebate for low-income earners*

From July 1, 2012 onwards, employed individuals on taxable incomes of less than $37,000 became eligible for a government contribution paid directly to their super account once they lodge their tax return. The contribution matches 15% of total concessional contributions made by or on behalf of the individual up to a maximum of $500. This year however, the government amended the eligibility criteria for LISC in the 2013-14 Budget to now pay individuals with an entitlement below $20. Previously, the LISC was not paid if it would end up being less than $20.

### *8) A new type of super account for people who do not choose a super fund*

From July 1, certain funds will start offering MySuper accounts, which are accounts that have:

- simple features
- basic, comparable fees and restrictions on the type of fees you can be charged
- a single investment option, or investment options based on the life stage you are at, and
- a minimum level of insurance – basic death and total and permanent disablement insurance cover.

If individuals have not nominated a superannuation fund and have just gone with a default fund, their future SG contributions will automatically be paid into

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a MySuper account from January 1, 2014. Conversely, if they have nominated a superannuation fund, they will not be affected by the MySuper change.

People who want their superannuation more tailored to their needs should seek appropriate advice.

***9) New ways to keep track of your super***

From July 1, it is much easier to find your lost superannuation and consolidate your various superannuation account balances into one account. You can check to see if you have any "lost superannuation" by entering your name, date of birth and tax file number on SuperSeeker.

You can also use SuperSeeker to claim small amounts of lost super from the ATO, which manages money collected from superannuation accounts that have not received any contributions for a period of two years.

From July 1, the ATO will also pay interest on small amounts of lost superannuation at a rate equivalent to the consumer price index (CPI).

## What didn't make it?

***1) New penalty regime for SMSFs***

A new range of penalties that would have allowed the ATO to issue rectification and education directions as well as administrative penalties was not introduced as intended from July 1, 2013.

***2) Anti-money laundering and counter-terrorism financing regime***

Part of the same bill as the penalty regime, these measures would have increased the regulatory obligations for superannuation funds that roll over to SMSFs.

***3) Non-complying tax rate for early release benefits***

Also part of the same bill, these measures would have effectively taxed illegal withdrawals of preserved benefits at 46.5% instead of an individual's marginal tax rate.

***4) Prohibition on SMSF in-specie asset contributions***

After the industry's adverse reaction to the proposal to ban in-specie asset transfers, the government backflipped and quietly removed the proposed amendments from legislation so that it passed Parliament (read more in our July newsletter).

***5) Regulations on taxing pensions earning over $100,000 per individual***

The latest inaction is the third time Treasury has considered such a measure to "cap" the tax concessions available to members with larger superannuation balances. ■

# Hurrah! Loss carry-back measures finally law

Businesses can rejoice in the fact that the much talked about loss carry-back measures were finally passed by Parliament just days before 2012-13 ended, in a move to benefit more than 110,000 Australian companies.

The loss carry-back law provides a company with the choice to carry back up to $1 million of losses against profits from a previous income year. This means losses from the current financial year can be offset against tax already paid to the ATO during more profitable years, up to a limit of $1 million of losses for each year – providing companies with a cash injection of up to $300,000 at the current company tax rate of 30% per year. This is known as a loss carry-back tax offset.

A transitional period applies for the 2012-13 income year, so you can only claim a loss carry-back refund against your tax liability for the 2011-12 income year. From the 2013-14 income year however, you can claim a loss carry-back refund against your tax liability for either of the two previous income years. Capital losses don't qualify for this treatment.

While the law is good news for small businesses, business owners should be aware that the initiative is only open to corporate tax entities – which include companies, corporate limited partnerships, corporate unit trusts and public trading trusts – meaning sole traders, trusts and partnerships lose out. It is estimated that around three quarters of all small businesses are not corporate tax entities.

Eligibility for the initiative is also limited to a company's franking account balance and subject to integrity rules – that is, the need to have continuous majority ownership and carry on the same business.

Prior to the loss carry-back legislation becoming law, businesses were able to carry losses forward to offset profits in future years, but this law signals the first time businesses will be able to carry back the losses to gain refunds on previous profits. ■

# Private health insurance – tax return changes

From the 2012–13 financial year (so for your current tax return), the private health insurance rebate is being income tested against three income tier thresholds. This means if you have private health insurance, the amount of rebate you will be entitled to receive is reduced if your income is more than certain threshold income amounts (see table below).

Note however that the income on which these thresholds are based are "income for surcharge purposes", which is not necessarily the same as taxable income.

For the purposes of assessing private health insurance rebate eligibility, your income for surcharge purposes is the total of the following amounts:

- taxable income, including the net amount on which family trust distribution tax has been paid
- reportable fringe benefits, as reported on your payment summary
- total net investment losses, including both net financial investment losses and net rental property losses
- reportable super contributions, including reportable employer super contributions and deductible personal super contributions.

As a result, some taxpayers who have been receiving reduced premiums from their insurer may end up receiving a tax liability.

The ATO has made changes to the private health insurance section in the tax return form that will allow it to determine the amount of rebate taxpayers are entitled to receive. You will need to provide your annual tax statement from your insurer to allow us to complete this question.

Other changes include:

- each adult covered by the policy is income tested on their share of the cost of the policy, regardless of who pays for the insurance policy
- each adult will receive their own statement from their insurer, which will be needed to complete the income tax return.

If you prepaid your private health insurance for 12 or 18 months in 2011-12, you still need to have the private health insurance policy section of your 2012-13 tax return completed using the information on your private health insurance statement (including any "$0" values). ■

| Private health insurance rebate income thresholds for 2012–13 (indexed annually) | | | | |
|---|---|---|---|---|
| | Income thresholds | | | |
| **Singles** | $84,000 or less | $84,001–$97,000 | $97,001–$130,000 | $130,001 or more |
| **Families*** | $168,000 or less | $168,001–$194,000 | $194,001–$260,000 | $260,001 or more |
| | **Private health insurance rebate entitlement** | | | |
| | **Base tier (no change)** | **Tier 1** | **Tier 2** | **Tier 3** |
| **Under 65 years old** | 30% | 20% | 10% | 0% |
| **65–69 years old** | 35% | 25% | 15% | 0% |
| **70 years old or over** | 40% | 30% | 20% | 0% |

*Use combined incomes if applicable. Income threshold is increased by $1,500 for each Medicare levy surcharge dependent child after first child. The tier used is based on the oldest person covered by the policy.

# Take an overseas jaunt, *and* get a tax refund

If you're keen to escape the winter chills and head off to warmer climes overseas, there is a scheme available that may take some bite out of your travelling costs. The Tourist Refund Scheme (TRS) lets you claim a refund on the goods and services tax (GST) and wine equalisation tax (WET) on goods you have bought in Australia.

It is not "duty-free" shopping, which is where you need to actually leave the country before you use the goods you have bought. The TRS allows you to use the items you buy, such as clothing or cameras, before leaving Asutralia, but then get certain amounts back (but not for consumables like wine or chocolates).

There are certain conditions. You need to:

- spend $300 (GST inclusive) or more at one retailer
- buy goods within 60 days of departure
- be sure the retailer provides you with a tax invoice (a refund cannot be given without it)
- wear or carry the goods on board the aircraft or ship and present them along with your original tax invoice, passport and international boarding pass to a Customs officer at a TRS facility within the air or sea port.

You can buy several items from one retailer (that is, one Australian Business Number holder, which means there could be several outlets) over a number of occasions in the 60-day period, as long as the total purchase adds up to $300 GST inclusive or more. You may buy goods from several stores, and claim the GST for each of those, as long as each store's tax invoice totals at least $300 (GST inclusive).

## How much will I get back?

The GST refund: Divide the total amount of the purchase by 11. The WET refund: 14.5% of the price paid for the wine. You can collect your refund through one of the following methods:

- cheque (posted within 15 business days)
- credit to an Australian bank account
- payment to a credit card (this and above, both issued within five business days subject to issuer).

## What can I buy?

Unlike "duty-free" shopping – where you are unable to use the goods within Australia – most goods under the TRS such as clothing, cameras and electrical equipment can be used in Australia prior to departure.

The refund only applies to goods you can take with you as hand luggage or wear on to the aircraft or ship when you leave Australia (subject to aviation security measures regarding liquids, aerosols and gels). It may pay to find out what you can and cannot take on-board as hand luggage before going to the airport.

The following goods are excluded from the TRS:

- Beer and spirits (wine is okay) and tobacco (these can be bought at duty-free shops)
- GST-free goods — no refund can be claimed if no GST was paid
- consumables wholly or partially consumed in Australia
- goods that are prohibited on aircraft or ships for safety reasons.
- goods that fail to meet airline cabin-size or ship hand luggage restrictions
- unaccompanied goods (including freighted or posted goods)
- services such as accommodation, tours and car rental and labour charges
- goods bought online and imported into Australia
- gift cards/vouchers (although goods purchased with these are eligible)

## How do I do it?

- Airport: Once clear of Customs and Immigration, TRS facilities can be found at the international airports at Darwin, Perth, Cairns, Adelaide, Melbourne, Brisbane, Sydney and Gold Coast.
- Seaports: Cruise liner terminals have TRS facilities at Circular Quay and Darling Harbour in Sydney, Melbourne's Station Pier and also Darwin, Brisbane, Cairns, Hobart and Fremantle. Contact Customs to find out where to claim.

It should only take a relatively short time to process the claim, but no-one likes holding up their flights (or worse yet, missing it altogether), so make sure you leave plenty of time to get to the airport, check-in, clear Customs, buy the duty-free perfume you promised your aunty, and queue-up to make your TRS claim.

Time wise, at the airport you have up to 30 minutes before departure. By sea, no later than one hour prior to the scheduled departure time of the vessel.

It is a legal requirement that the person who purchases the goods must be the person who makes the claim for a refund of GST. ■