



R U N D L E S

C H A R T E R E D   A C C O U N T A N T S

# The Report

tax news | views | clues

September 2014

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## Tax debt release on serious hardship grounds refused

In a recent case, the Administrative Appeals Tribunal (AAT) refused an individual's application to be released from his tax debt of \$58,000 on the grounds of serious hardship.

The AAT noted that no explanation was offered for the taxpayer's failure to meet his tax liabilities as they arose. The AAT said that instead of paying what it considered to be manageable tax assessments, the taxpayer "largely ignored his tax liabilities over the last five or six years, and has allowed the amounts due to accumulate with interest".

**TIP:** The Tax Commissioner has discretion to release individuals from eligible tax debts. However, even if the Commissioner is satisfied that serious hardship would result from payment of the tax debt, he is not obliged to exercise the discretion in the taxpayer's favour.

Broadly, serious hardship is said to exist when payment of a tax debt would leave an individual unable to provide basic living necessities for themselves and their dependants. Ultimately, it is a question of fact whether payment of an eligible tax liability would result in serious hardship – and the onus is on the taxpayer to prove their case before a tribunal.

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## GST credits for property development project managers denied

Two taxpayers have been denied GST input tax credits they had claimed in respect of purported acquisitions made in relation to property developments. The Commissioner had refused the taxpayers' claims for input tax credits on the basis that neither taxpayer carried on an enterprise.

The AAT heard from the taxpayers that they were "principal contractors" in relation to the property developments. However, the AAT said that exactly what the "principal contractors" did in respect of the properties remained the subject of "quite profound mystery".

It said that an entity is not a "project manager" simply because someone says it is. Further, the AAT said that to carry on an enterprise, an entity must "do" something, and that in this case, the AAT was unable to identify the activity that the taxpayers were doing in respect of the properties.

**TIP:** This case demonstrates the need for multiple parties, and in particular related parties, who are involved in large property development projects to clearly articulate and document the role of each party and the agreements they have with each other, particularly if one party intends to seek GST input tax credits.

[www.rundles.com.au](http://www.rundles.com.au)

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## Individual working overseas not a tax resident

An individual has been successful before the AAT in arguing that he was not a "resident" of Australia for tax purposes for the 2009 and 2010 income years. This was despite being an Australian citizen, maintaining an Australian bank account for his salary, and retaining his house in Queensland.

During the years in question, the taxpayer had signed up with a company to work on a project in Saudi Arabia. The project was expected to last three years and the taxpayer had an expectation that upon completion of the project, he would move on to another project located in Saudi Arabia.

In making various findings of fact, the AAT largely accepted the taxpayer's evidence. It said that the taxpayer's presence in Saudi Arabia "was hardly casual or passing". The AAT accepted that the taxpayer had formed an intention to make Saudi Arabia his home for the duration of the project and beyond.

**TIP:** This case demonstrates that proving tax residency requires a detailed examination of various facts, and the weighing up of those facts, to come to a conclusion that an individual is (or is not) a tax resident. It also demonstrates the importance of having corroborating evidence to prove the taxpayer's case.

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## ATO debt collection approach under review

The Inspector-General of Taxation, Mr Ali Noroozi, has announced that he will review the ATO's approach to debt collection. "Despite the ATO's debt assistance programs, its approach to collecting taxes has been a persistent source of taxpayer complaint", Mr Noroozi said. He noted that the ATO's approach to collecting debts accounted for 23% of all ATO-related complaints received by the Commonwealth Ombudsman in 2012–2013.

Furthermore, Mr Noroozi said some stakeholders believe that the ATO has recently taken a firmer approach to debt collection despite continuing economic pressures, while others are of the view that the ATO allows debts to accumulate for too long before taking action.

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## New ATO approach to identifying SMSF risks

Trustees of self managed superannuation funds (SMSFs) need to be aware of how the ATO gathers information about them in order for the ATO to assess whether their SMSF poses a tax compliance risk, and how the ATO may respond if it perceives a risk.

The ATO has recently announced that it will take a new risk-based approach to how it treats auditor contravention reports (ACRs). This approach will be based on the overall risk posed by the SMSF. Using new risk models, the ATO will analyse multiple indicators of possible non-compliance, including regulatory and income tax matters, information from the SMSF annual return, ACRs and other data such as trustee and member records. The ATO will then use this information to determine appropriate actions to take regarding each SMSF.

The ATO has also reminded SMSF trustees that since 1 July 2014 it has more flexibility in how it deals with SMSFs that breach the super law – including new powers to issue penalties. The ATO says that SMSF trustees should therefore rectify any contraventions of the law as soon as possible.

**TIP:** While the new SMSF trustee penalties started on 1 July 2014, the ATO has noted that contraventions of the law (such as loans to members or relatives) that existed on 1 July 2014 will come under the new penalty regime.

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## Administrator of deceased estate breached duty

The Supreme Court of Queensland has ruled that an administrator of a deceased estate breached her fiduciary duty by applying for her deceased son's superannuation benefits to be paid to her personally, rather than on behalf of his estate.

The Court had granted the woman Letters of Administration over her son's estate after he died, aged 40, intestate and without a spouse or children. However, she applied to her deceased son's superannuation funds to pay his death benefits to her personally.

The deceased's father (the woman's ex-husband) submitted that she had allowed a conflict of interest to occur by seeking the superannuation death benefits for her personally. In finding against the woman, the Court ordered that she transfer all of the superannuation death benefits in dispute (approximately \$450,000) to the son's estate, where it would be shared equally with her former spouse under the rules of intestacy.

## **Budget Levy from 1 July 2014**

The Government's Temporary Budget Repair Levy is now law. The levy is payable at the rate of 2% of each dollar of an individual's annual taxable income over \$180,000. The levy is active for three financial years, starting on 1 July 2014 and ending on 30 June 2017. That means the top marginal tax rate is effectively 49% (including the 2% Temporary Budget Repair Levy plus the 2% Medicare levy).

For example: Individuals with taxable income of \$200,000 will pay 2% of \$20,000 (ie a levy of \$400). Those with taxable income of \$300,000 will pay 2% of \$120,000 (ie \$2,400 of levy).

A number of other taxes are also affected by the levy. According to the Government, these other changes are important to maintain integrity and fairness in the tax system. Notably, the fringe benefits tax (FBT) rate will be increased from 47% to 49%. As the FBT year commences on 1 April and concludes on 31 March, the increase in the FBT rate is to be applied from 1 April 2015. The increase in the FBT rate will cease on 31 March 2017.

**TIP:** High-income earners may want to review salary sacrificing arrangements and the possible effect of the levy. Please contact our office for further information.

## **PAYG instalment threshold changes**

The ATO has confirmed the Government's recent announcement that the pay-as-you-go (PAYG) instalment thresholds will change with effect from 1 July 2014. Following the Minister's announcement, the ATO advised the following instalment threshold changes:

- the business or investment income threshold is increased from \$2,000 to \$4,000;
- the balance of assessment threshold is increased from \$500 to \$1,000;
- the notional tax threshold is increased from \$250 to \$500; and
- the requirement for entities registered for GST to remain in the system even if they have a zero instalment rate is removed.

As a result, many taxpayers will no longer have to pay PAYG instalments. According to the Minister of Small Business, around 32,500 small businesses that have no GST reporting requirements will no longer have to lodge a business activity statement (BAS) where to date lodgements have been made only to report PAYG instalments. In addition, around 340,000 small businesses with modest or negative income which are required to lodge a BAS will no longer have to interact with the PAYG instalment system.

**TIP:** If taxpayers still wish to pay instalments towards their end-of-year tax liability, they may voluntarily re-enter PAYG instalments by contacting the ATO. Please contact our office for further information.

## **ATO mining data to find offshore tax evaders**

The ATO says it is mining data to identify individuals with undisclosed offshore income and assets. "The net is closing for people who have undeclared offshore income – we're looking at all our data and will be in touch with financial institutions, advisers and thousands of people over the coming months," said Deputy Commissioner Michael Cranston. As at 30 June 2014, the ATO's Project DO IT initiative to encourage voluntary disclosure has received 166 disclosures, raising an additional \$13 million in tax liabilities. The ATO has also obtained more than 250 expressions of interests from taxpayers indicating that they will be making a disclosure.

**TIP:** The last day to make a disclosure under Project DO IT is 19 December 2014. The ATO had previously warned that, until it receives a disclosure, its normal compliance activities will continue. Individual taxpayers detected first by the ATO will not be able to participate in Project DO IT.

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## **Deductions for employee welfare fund denied**

The Administrative Appeals Tribunal (AAT) has refused a taxpayer's claim for deductions for contributions made to an offshore "employee welfare fund". The taxpayer and a number of related companies carried on an automotive repair and spare parts business. The fund was set up in 1998 and its beneficiaries were the two employee-operators of the business and a spouse. In 1998 the taxpayer contributed \$400,000 to the fund. In 1999 the taxpayer contributed a further \$25,000 and also claimed carried-forward losses resulting from the contribution from the previous year.

The AAT rejected the taxpayer's claim that the contributions to the fund were deductible. It also highlighted a number of concerns in the way the fund was set up and how it operated. Among other things, the AAT noted there were no documents to show that the trustee ever admitted anyone as a member of the fund and, furthermore, there was doubt and confusion about the identity of the trustee. However, the AAT found that while the Commissioner could issue amended assessments for the 1998 and 1999 income years in 2012, an amended assessment issued for the 2002 income year was out of time to deny a deduction for further carried-forward losses.

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## **Damages assessable to director personally**

The High Court has affirmed that damages received by an individual following a failed joint venture project were assessable to him personally. Broadly, the individual and others had sought for the company of which they were the directors to become an equity participant in the project and become the ultimate purchaser of the golf course. However, the other joint venturers in the project disputed this and made other arrangements to purchase the golf course.

The individual then successfully sued the other joint venturers and was awarded damages by the Victorian Supreme Court for the loss of a business opportunity. The Commissioner then assessed the individual on this amount (around \$860,000). The individual argued that he had received the money as trustee of the company and it was therefore assessable to the company.

The High Court held the individual was liable to income tax on the damages received in satisfaction of the Supreme Court judgment. It was of the view the individual did not receive the amount as a constructive trustee of the company.

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## **Winemaker not taxable on property sale**

The Administrative Appeals Tribunal (AAT) has held that an individual taxpayer, who was the controller of several trusts through which he operated a winemaking business, and who was also a beneficiary of the trusts, was not presently entitled to an amount of over \$480,000 in profit that one of the trusts made from the sale of business premises.

The profit had been deposited into accounts which the taxpayer controlled for his personal benefit. The Commissioner had issued an assessment to include the profit in the taxpayer's assessable income on the basis that the amount represented revenue profit of the trust and that, as a beneficiary of the trust, the individual was presently entitled to the amount under certain rules concerning the tax treatment of trust income.

However, the AAT did not agree with the Commissioner's decision. It concluded that another of the trusts (of which the taxpayer was trustee) was beneficially entitled to the profit as a beneficiary of the trust that made the profit from the sale and not the taxpayer in his personal capacity.

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## **Share transfer to family partnership ineffective**

A husband and wife have been unsuccessful before the Administrative Appeals Tribunal (AAT) in arguing that they had transferred shares in a family company to a family partnership, and that therefore they should not be assessed on dividends issued by the company to themselves. The AAT examined the partnership agreement and was of the view that, under the terms of the agreement, the couple was not required to actually transfer their shares in the family company to the family partnership. It was also emphasised that the couple remained the full registered owners of the shares. In doing so, the AAT affirmed the Tax Commissioner's decision that the couple were each assessable on the dividends of some \$1.8 million. The taxpayers are seeking to appeal the decision in the Federal Court.

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## **Property developers and use of trusts under scrutiny**

The ATO is examining arrangements where property developers use trusts to return the proceeds from property development as capital gains instead of income on revenue account. ATO Deputy Commissioner Tim Dyce said the ATO has “begun auditing property developers who are carrying out activities which conflict with their stated purpose of capital investment”. He said a “growing number of property developers are using trusts to suggest a development is a capital asset to generate rental income and claim the 50% capital gains discount”. Mr Dyce warned that penalties of up to 75% of the tax avoided can apply to those found to be deliberately using special purpose trusts to mischaracterise the proceeds of property developments. The ATO said it has made adjustments to increase the net income of a number of trusts. It said penalties will be significantly reduced if taxpayers make a voluntary disclosure.

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## **Billions in lost super waiting to be claimed**

According to the ATO, more than \$14 billion in lost super is waiting to be claimed. The ATO said \$8 billion in super was sitting in accounts that have not received a contribution in five years. A further \$6 billion in super was sitting in accounts where funds have not been kept up-to-date with changes to personal details. ATO Assistant Commissioner John Shepherd said it was “easy for this to happen because when people get married or move house, the last thing on their mind is updating their name and address details with a super fund”. However, he said it was important to provide funds with tax file numbers (TFNs) which can help individuals be reunited with their super.

**TIP:** The ATO’s Superseeker service enables individuals to enter their name, TFN and date of birth to conduct an online search of the Tax Office’s Lost Members’ Register available at [www.ato.gov.au/Calculators-and-tools/SuperSeeker](http://www.ato.gov.au/Calculators-and-tools/SuperSeeker).

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## **ASIC eye on SMSF property investment advice**

The Australian Securities and Investments Commission (ASIC) have raised concerns about advice being given to self managed superannuation funds (SMSFs) to invest in property. ASIC Commissioner Greg Tanzer said the regulatory body was aware there had been a sharp rise in promoters recommending that investors either set up or use an existing SMSF to invest in property. ASIC is concerned these promoters may not be complying with the law. Mr Tanzer said ASIC was concerned that, with the increased popularity of SMSFs and property investment, real estate agents and property advisers may not realise they may be carrying on a business of providing financial product advice and may need an Australian financial services (AFS) licence, or authorisation under an AFS licence, when making recommendations or statements of opinion to a person to use an SMSF to invest in property. Mr Tanzer said ASIC is now working with individual businesses suspected of engaging in unlicensed conduct to help them understand their obligations.

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## **Bad debt deduction for “unpaid trust entitlements” refused**

A taxpayer has been unsuccessful before the AAT in a matter concerning bad debt deduction claims for the 2012 income year in relation to certain trust distributions. The taxpayer, a beneficiary of a trust, had claimed bad debt deductions under the tax law for debts he argued were unpaid trust entitlements. He argued the debt written off had the same character as the trust distributions included in his assessable income in the 2005 and 2007 income years. Following analysis of the distribution transaction and the trust deed, the AAT was of the view the taxpayer’s entitlement was paid in the manner prescribed by the deed, and once paid, lost its character as unpaid entitlement. The AAT concluded the debt written off was different in character to the income included in the taxpayer’s assessable income in the 2005 and 2007 income years.

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## **Family fails to prove assessments excessive**

Six members of a family have been unsuccessful before the AAT in arguing that various amended and default tax assessments were excessive. The AAT heard details of unexplained moneys flowing through family bank accounts, sums paid from an overseas business

arrangement, as well as the acquisition of various residential properties in the names of family members, despite the taxpayers' claim they earned very little income. The Tax Commissioner used the "asset betterment" analysis to raise the assessments. Despite acknowledging inherent flaws in the method used by the Commissioner to derive the tax assessments, the AAT found the family members had failed to establish that the assessments were incorrect and that the amount of money for which tax was levied by the assessment exceeded the actual substantive liability of the taxpayers.

**TIP:** In making a default assessment, the Commissioner is not required to follow the ordinary processes of ascertaining assessable income and allowable deductions and need not make inquiries of the taxpayer (or the taxpayer's agent). However, the assessment may be invalid if the Commissioner estimates the taxpayer's assessable income upon no intelligible basis or simply plucks a figure out of the air.

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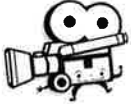
## **Tax consequences following marriage break-up**

The ATO has recently released a taxation ruling on the tax effects of matrimonial money or property transfers. According to some commentators, the game-changing ruling may affect the manner in which property settlements are able to be arranged for family groups under s 79 of the *Family Law Act 1975*.

In Taxation Ruling TR 2014/5, the ATO confirmed that payments or transfers of property under Family Court orders to a husband or wife from a private company will be considered a distribution of profits from the company. Such transactions will therefore be assessed as dividends either pursuant to the ordinary dividend assessing provisions (s 44 of the *Income Tax Assessment Act 1936*) or Div 7A in almost every matrimonial property or cash settlement, regardless of whether the parties are shareholders (or associates of the shareholders) in the private company or whether the private company is a party to the Family Court order.

**TIP:** The rules can be complex and various different taxation consequences could arise depending on the type of Family Court order that has been made. Please contact our office if you have any questions.

# Noel's News



**Film Review – by Maria Marson**

## **THE HUNDRED FOOT JOURNEY**

Starring: Helen Mirren, Manish Dayal, Om Puri, Charlotte Le Bon

French Indian cuisine is the main ingredient of this movie.

The film is about a young chef, Hassan (*Manish Dayal*), who with his family travels from India to the South of France with a grand plan of opening an Indian restaurant.

Undeterred by the fact that across the road (100 feet distance) is a classical award winning French restaurant run by a widowed owner, Madame Mallory (*Helen Mirren*), they settle down and open an Indian restaurant in the quaint little village of St-Antonin-Noble-Val.

Outraged by the new Indian restaurant opening up across the road, Mme Mallory is determined to have their business shut down. Madame believes the Indian place across the road will damage her chances of earning a second “Michelin” star rating for her restaurant.

As the two cultures clash, an all out war escalates between Hassan's widowed father, Papa Kadam (*Om Puri*) and Mme Mallory until Mme Mallory realises Hassan's talent as a great chef and invites him to work for her with thoughts of earning another “Michelin” rating.

Along with Hassan's love interest, Marguerite (*Charlotte Le Bon*), Madame starts to weave a magic between the two cultures and discovers an unlikely recipe for success.

It is a mouth watering movie leaving you wanting to taste the delicious meals prepared.



**Restaurant Review – by Mark Lisle**

## **Barca - 1007 High Street, Armadale**

Barca, as the name suggests, is Spanish cuisine but there are other European influences in the menu. There is a lot to like about this classy little restaurant in the middle of the High Street shopping precinct. The menu is varied and of a high quality. The steaks are great, as is the paella. The service is attentive and professional and the wine list has something for everyone.

There is also a groovy little wine bar just down the road (963 High St), called Lona, which is part of the same establishment. (Get it...“Barca-Lona”) An ideal spot to have a drink, or aperitif, before walking down the road for dinner.



Barca is the perfect place to go for a nice meal without having to go into the city. It isn't cheap but not over the top either. I don't think you will be disappointed.

### ***The Glenferrie Hotel - 324 Burwood Road, Hawthorn***

Continuing with our theme of hotels that have restaurants or bistros that are a bit better than your average pub, I suggest that you give the Glenferrie Hotel a try. The Glenferrie has undergone a bit of a transformation in recent times. It has gone from a local pub with pool tables in the eating area to a quality bistro with table service and an elegant period charm. The food is good, as is the wine list and the beers on tap. It is equally suitable for dinner with the family or a quiet dinner for two. There is also a large courtyard outside, which is very popular in summer.



***Sporting Predictions – as seen by Brad Roach***

### ***Horse Racing***

The Spring Racing Carnival is fast approaching. The winner of the major races will be:

Cox Plate – Dissident

Caulfield Cup – Dear Demi

Melbourne Cup – Bande

### **Rugby League**

The NRL final series has seen some upsets with the South Sydney Rabbitohs to meet the Canterbury Bulldogs in the NRL grand final. With some injuries to key players for the Bulldogs I predict a victory for the South Sydney Rabbitohs. The final scores South Sydney 18 over the Bulldogs 10.

### **Cricket**

The Australian Cricket team heads to the UAE for a two test series against Pakistan. Hopefully Australia continues the improvement shown by the younger players over the past 12-18 months. Australia won't have it all their own way but will win the series 2-0.