



NEWSLETTER

2010

Tax IQ

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PLUS

BONUS ISSUE

SUPERANNUATION - WEALTH ACCUMULATION TIPS

TOO MANY AUSTRALIANS OVERLOOK THE FUNDAMENTAL IMPORTANCE OF SUPER AND TAX PLANNING. THIS PUBLICATION IS A MUST READ FOR ALL WHO WANT TO MAXIMISE THEIR OPPORTUNITIES...

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ATO COMMEMORATES 100 YEARS OF SERVICE

On 12th November, 2010 the ATO commemorated 100 years of service to the Australian community.

Recognising this milestone, Commissioner of Taxation, Michael D'Ascenzo was joined by Her Excellency, the Governor-General of the Commonwealth of Australia, Ms Quentin Bryce and Minister for Financial Services and Superannuation and Assistant Treasurer, The Hon Mr Bill Shorten MP.

"Who would have imagined that one hundred years ago, a team of 105 staff in the Land Tax Office would evolve into the modern ATO of today, employing 22,000 people and being recognised internationally as a leader in tax and superannuation administration," Tax Commissioner Michael D'Ascenzo said.

"We've come a long way since 1910 and I am proud to recognise this milestone.

Back in 1910, the Land Tax Office assessed 15,000 returns. Today the ATO is able to process tax returns for around 12.6 million personal taxpayers and two million businesses. Each year they handle over 10 million telephone enquiries, 87 million website visits and receive two million tax return lodgements via e-tax.

A Brief Look at the ATO's History - Events That Shaped Australian History:

- 1910** - Federal Land Tax Branch established with 105 staff - 5,000 returns assessed in first year.
- 1915** - Income Tax Assessment Act introduced.
- 1917** - Female employment introduced due to men away at war.
- 1924** - State tax office branches amalgamated.
- 1930** - The sales tax introduced.
- 1933** - Flour tax introduced for one year, at a time when flour production exceeded sale price.
- 1944** - The Pay-As-You-Earn (PAYE) tax system introduced.
- 1952** - Federal Land Tax abolished.
- 1966** - The decimal currency introduced in Australia.
- 1975** - The first tax computer system-the Central Taxpayer System-commenced operation.
- 1978** - A surge in tax avoidance schemes (known as bottom-of-the-harbour) resulted from soaring inflation and threatened the integrity of the tax system.
- 1986** - Self-assessment introduced.
- 1987** - Electronic Lodgement System (ELS) for tax agent's trialed.
- 1988** - The first 'Tax Help' volunteer program was introduced to help people in need prepare their tax returns.
- 1997** - The Taxpayers' Charter introduced, setting out taxpayers' rights and standards of service.
- 1999** - e-tax launched resulting in 27,000 lodgements.
- 2000** - Introduction of 'The New Tax System' - the ATO delivered the largest range of tax reforms in its history including the introduction of the GST and Pay As You Go system as part of broader business tax reform.
- 2007** - Implementation of 'Better Super' - the biggest reform to superannuation ever.

- 2009** - A one-off tax bonus payment worth \$7.7 billion was distributed to 8.7 million people. It was the largest payment ever made through the tax system and one of the most significant in Australia's history.
- 2010** - Since 1st July the ATO processed over 10 million income tax returns resulting in refunds of more than \$20 billion. The ATO currently employs 22,400 staff.
- 2010** - Over 2.3 million taxpayers lodged online using e-tax, which has evolved to include pre-filing, online help and automatic calculations.

NEW ATO BENCHMARKS FOCUS ON CASH SALES

On 9th November, 2010 the ATO released a new category of small business benchmarks which focus on cash sales within a business.

Coinciding with the fourth annual cash economy international revenue conference in Brisbane, Second Commissioner Bruce Quigley said the new benchmarks are part of a suite of benchmarks used by the ATO to identify and deter activities in the cash economy.

According to Mr Quigley:

- These benchmarks are a useful way to help businesses compare their performance against other businesses in their industry and check they are meeting their obligations, including assessing whether they are likely to be selected for a review or audit.
- The ATO strongly believe prevention is better than cure. This is a timely reminder for people to check that their record keeping and reporting is on track and fix any errors.
- Using these benchmarks, the ATO can determine the average proportion of cash sales a business should be making and which businesses are not reporting as much cash income as others in the same industry.
- Businesses whose performance falls significantly outside one or more of these benchmarks are more likely to be selected for a review or audit.
- This year the ATO are contacting around 100,000 businesses which operate in cash industries.

The ATO regularly shares its cash economy insights and programs with other international jurisdictions as part of a coordinated global information approach and looks forward to continued positive relations and learnings with these groups.

The benchmarks have initially been developed for fifteen industries including; restaurants and takeaways, hairdressing and beauty, clothing retailing, grocery retailing and hardware and building supplies.

The cash sales benchmarks are based on data matching

undertaken with banks to identify credit and debit card sales, as well as information provided by small businesses to the ATO on activity statements.

Background

Small Business Cash Sales Benchmarks

The cash sales benchmarks have initially been developed for the following fifteen industries:

Beauty Services	Hairdressers
Clothing Retailing	Hardware And Building Supplies
Coffee Shop	Retailing
Florists	Meat Retailing And Butchers
Fruit And Vegetable	Newsagents
Retailing	Pubs, Taverns And Bars
Fuel Retailing	Restaurants
Garden Supplies Retailing	Takeaway Food Services
Grocery Retailing And General Stores	

Expanded Data Matching

The ATO will shortly be expanding its data matching program to obtain information from banks about the total credit and debit card sales of small businesses for the 2009-10 financial year.

A copy of the new data matching protocol was issued on 10th November, 2010 via public service gazettal notice.

The cash economy international revenue conference brings together international tax administrations from Canada, Denmark, Indonesia, Mexico, New Zealand, Singapore, Sweden, USA, Vanuatu, and Zimbabwe as well as local professionals, and business and industry representatives to share insights and new approaches being developed to deal with the cash economy.

As part of a global approach in sharing information and using the most effective strategies around the world to deter, detect and deal with the cash economy, the ATO has accepted membership in an OECD Forum on the Taxation Administration study group.

The study group will focus on enhancing risk detection and identifying the more innovative forms of treatments being used to address the cash economy.

ATO INTERPRETATIVE DECISION - ATO ID 2010/164 - INCOME TAX

Deductions: Swimming Instructor (Swimwear)

We have included this recent ID as it may have implications for others working in the health and fitness industries.

The issue is whether expenditure incurred by a swimming instructor in purchasing swimwear is deductible under section 8-1 of the Income Tax Assessment Act 1997 (ITAA 1997).

Unfortunately the decision is **No** - Expenditure incurred by the taxpayer in purchasing swimwear is not deductible under section 8-1 of the ITAA 1997.

Facts

The taxpayer works as a part-time swimming instructor. The taxpayer purchases swimsuits every six to eight weeks as a result of the damaging effect of the chlorinated swimming pool water on the swimsuits.

Reasons for Decision

Generally, expenditure on conventional clothing is treated as private expenditure and therefore not deductible under section 8-1 of the ITAA 1997 (*Mansfield v. FC of T* 96 ATC 4001; (1996) 31 ATR 367 (Mansfield); *Federal Commissioner of Taxation v. Edwards* (1994) 49 FCR 318; 94 ATC 4255; (1994) 28 ATR 87 (Edwards)).

To be deductible under section 8-1 of the ITAA 1997, the expenditure must have the essential character of an outgoing incurred in gaining assessable income or, in other words, of an income-producing expense (*Lunney v. Federal Commissioner of Taxation* (1958) 100 CLR 478). It is not sufficient that the expenditure is a prerequisite to the derivation of assessable income (*Lodge v. Federal Commissioner of Taxation* (1972) 128 CLR 171; 72 ATC 4174; (1972) 3 ATR 254; *Federal Commissioner of Taxation v. Cooper* (1991) 29 FCR 177; 91 ATC 4396; (1991) 21 ATR 1616)

In *Edwards*, the taxpayer was required to wear multiple outfits in one day due to the nature of her work as an attendant to the governor's wife. The Court held that the first outfit for the day satisfied the taxpayer's requirements of modesty, decency and warmth and was private in nature, and that additional clothing worn during the day solely served work-related purposes to allow the taxpayer to carry out her duties. Expenditure on the additional clothing therefore had the necessary nexus to the activities by which the taxpayer produced her assessable income and was deductible.

In *Mansfield*, Hill J found that expenditure by a flight attendant on cabin shoes and hosiery, being items of conventional clothing was deductible. Hill J took a number of matters into account, but important to his decision was that the taxpayer had purchased the cabin shoes for use solely in flight and the shoes were unsuitable for ordinary use as they were a half-size too large to allow for the swelling of the taxpayer's feet in flight. The hosiery was found to be deductible on the basis that it formed part of the taxpayer's uniform and was thus differentiated from ordinary clothing.

In the present case, the taxpayer wears a single swimsuit at work which meets the requirements of modesty and decency. Although specialised, the clothing is conventional clothing. There is nothing to distinguish the swimsuit from that used for private purposes such as training or recreation.

There is no principle that expenditure incurred in replacing clothing worn out during the course of income-earning activities is deductible where the clothing serves a private purpose.

ATO WARNS ABOUT BOGUS SAMOAN OFFSHORE SCHEMES

In October, the ATO warned people about bogus Samoan offshore tax schemes being used to underpay taxes.

“Promoters have established offshore structures based in Samoa designed for people to claim artificial tax deductions and conceal income or assets,” Tax Commissioner Michael D’Ascenzo said.

“Australian residents who use offshore arrangements to conceal assets or income from the ATO face serious penalties, including criminal sanctions or confiscation of assets.”

Anyone who has participated in these arrangements needs to come forward before they are contacted by the ATO. If they do, they will be entitled to a reduction in any tax penalties.

“People who are unsure about their situation should seek independent advice or contact the ATO for a private ruling on their individual circumstances,” Mr D’Ascenzo said.

“The ATO will continue to deal with avoidance and evasion schemes that put an unfair burden on the majority of honest taxpayers.”

Taxpayer Alert 2010/4 - Australian resident entities using promoters to enter into tax arrangements in Samoa to claim purported deductions and conceal income is available from the ATO website www.ato.gov.au/atp

RECENT CASES

Wife Was Not Employed By Husband - France and FCT (2010) AATA 858 (AAT, McCabe SM, 2 November, 2010)

Here the taxpayer was denied deductions for salary and wages paid to and superannuation contributions made on behalf of, his wife, on the basis that the outgoings were of a private and domestic nature, and were not paid to or on behalf of the wife in her capacity of an employee of the taxpayer.

The taxpayer had contended that he had entered into an employment relationship with his wife which required her to look after his investment property. The “employment relationship” was suggested and implemented by the taxpayer’s accountant. However, the AAT said, at paragraph 18:

“One does not transform an existing relationship simply by calling it by a different name, or even adopting some of the forms of a different relationship. Language and form is merely an indicator of the nature of the relationship. Language and form will not be decisive if they do not accurately reflect the character of the relationship. One must look at the totality of

the relationship when characterising it. In this case, the relationship between the parties continued to be what it had always been: a spousal relationship in which one of the spouses attended to the management of the family’s affairs.”

The Fuel Tax Credit Rate for Heavy Vehicles Changed On 1 July, 2010

From 1 July, 2010 the fuel tax credit rate for fuels such as diesel or petrol for use in heavy vehicles on public roads was reduced to 15.543 cents per litre. This change is due to an increase in the road user charge.

A heavy vehicle is either of the following:

- A vehicle with a gross vehicle mass (GVM) of greater than 4.5 tonne
- A diesel vehicle acquired before 1 July, 2006 with a GVM equal to 4.5 tonnes or more.

To substantiate their claims, taxpayers will need to keep records showing they acquired the fuel and how they used it. Acceptable records include fuel dockets, invoices and log books.

Applying Division 7A - Usage of Assets

From 1 July, 2009 the non-commercial loan rules in Division 7A were tightened. This means that the value of benefits private companies provide to their shareholders or associates through the use of company assets, such as houses and cars, may now be taxable as a deemed dividend if they provide them for:

- Free
- Less than their market value

Under Division 7A, the term ‘payment’ now includes providing an asset for use by an entity. Before these changes, only transfers of property were taxed. A transfer of property occurs if ownership of the asset is transferred or there is a lease of real property.

We suggest you review all use of company assets to work out if Division 7A applies. If a Division 7A payment arose in the 2010 income year, it can be converted to a loan before the company’s lodgement day for the 2010 income tax return.

The amount of a payment is the amount that would have been paid for the asset by parties dealing at arm’s length, less any amount actually paid.

The use of an asset will not be a payment if it is covered by one of the following exceptions:

- Minor use of certain company assets
- Certain payments that would otherwise be allowable as a once only deduction
- The use of certain dwellings, subject to certain conditions.

Travelex Ltd V Commissioner of Taxation (2010) HCA 33

On 29th September, 2010 the High Court held that a sale of foreign currency on the departures side of the Customs barrier at Sydney International Airport was a GST-free supply under s38-190(1) of A New Tax System (Goods and Services Tax) Act 1999 (Cth) ("the GST Act").

In November 2007, an employee of Travelex Ltd flew from Sydney to Fiji. After clearing Customs, he went to the Travelex counter in the departure hall and purchased F\$400 in bank notes.

Travelex sought a declaration in the Federal Court that it was exempt from paying GST on the sale of foreign currency to a passenger who had passed through Customs. Item 4(a) of s38-190(1) of the GST Act provides that, except to the extent that it is a supply of goods or real property, a supply that is made in relation to rights is GST-free if the rights are for use outside Australia. The primary judge and, on appeal, a majority of the Full Court of the Federal Court rejected Travelex's argument that the supply was a supply "in relation" to rights, and therefore a GST-free supply. Both the primary judge and the majority of the Full Court took the view that the relevant supply was the supply of bank notes and that the rights attaching to those bank notes, as legal tender in Fiji, were merely incidental to that supply.

The High Court allowed the appeal and substituted for the orders of the primary judge a declaration that the sale was a supply of or in relation to rights and a GST-free supply under the GST Act. A majority of the Court, observing that the value of bank notes is in the rights that attach to them, characterised the transaction as a supply by which the purchaser acquires the rights that attach to the bank notes, rather than simply a supply of bank notes. The Commissioner of Taxation was ordered to pay Travelex's costs.

Practice Statement on Division 7A and Trust Entitlements

On 14th October, 2010, the ATO released practice statement *PS LA 2010/4 on Division 7A of the Income Tax Assessment Act 1936 (ITAA 1936) and Trust Entitlements* which provides practical guidance on how to administer taxation ruling TR 2010/3 Income Tax: Division 7A: trust entitlements.

The ATO's media release on PS LA 2010/4 made it clear they are aware of the importance of this issue to businesses, particularly small business, which use a trust structure. The practice statement provides practical ways for businesses to work towards a compliance structure with minimal impact on their cash flow or how they operate and provided several options to self-correct for past mistakes.

The ATO are allowing concessions in respect of unpaid present entitlements (UPEs) which have been converted to loans (called Section two loans in TR 2010/3 which has retrospective application):

- To allow taxpayers the ability to self correct accounts where a UPE has been misclassified as a loan thereby dealing with the issue of imprecise accounting arising from accounting software packages and subsequent administrative practices;
- To allow certain taxpayers self corrective action in respect of any Section two loan when seeking the Commissioner's discretion under s109rb of the ITAA 1936 for honest mistakes and inadvertent omissions.

Taxpayers must implement the self corrective options by 31st December, 2011.

Commissioner of Taxation V Anstis (2010) HCA 40

On 11th November, 2010 the High Court held that a University student in receipt of youth allowance payments was entitled to claim various self-education expenses as income tax deductions.

Symone Anstis was enrolled as a full-time student in teaching degree at the Australian Catholic University. In the 2006 income year she earned \$14,946 in wages as part-time assistant, and \$3,622 in youth allowance payments. In her tax return for that period she claimed a \$920 deduction for self-education expenses, comprising the depreciation in value of a computer, textbooks and stationary, a student administration fee, supplies for children during her teaching rounds and travel expenses other than to university.

Section 8-1 of the Income Tax Assessment Act 1997 (Cth) ("the 1997 Act") relevantly provides that a person can deduct from their assessable income any loss or outgoing to the extent that is it incurred in gaining or producing their assessable income except to the extent that it is a loss or outgoing of a private or domestic nature.

The Commissioner of Taxation disallowed the deduction, and Ms Anstis was unsuccessful in an application for review by the Administrative Appeals Tribunal ("AAT"). In 2009, the AAT's decision was reversed by the Federal Court. The Full Federal Court dismissed an appeal by the Commissioner against that decision.

The High Court unanimously dismissed an appeal by the Commissioner of Taxation. The Court held that youth allowance payments amounted to assessable income under the 1997 Act as they fell within the concept of "ordinary income." Because Ms Anstis' entitlement to youth allowance arose from her undertaking full-time study, the expenses claimed were incurred in gaining or producing her assessable income. The Court also held that the expenses were not of a private or domestic nature and as such were deductible under s8-1 of the 1997 Act.

The Commissioner of Taxation was ordered to pay Ms Anstis' costs.

ATO INTERPRETATIVE DECISION - ATO ID 2010/195 - INCOME TAX

Car Expenses: Business Kilometres - Travel to Tax Agent

Are kilometres travelled by a taxpayer to consult with a tax agent included in the business kilometres used for determining car expense deductions under Division 28 of the *Income Tax*

The answer is yes and this means more care will need to be taken when making motor vehicle claims.

- The employee taxpayer uses a tax agent to prepare their individual tax return.
- The taxpayer travelled 4500 kilometres by car in the income year in relation to the taxpayer's income-earning activities.
- The taxpayer also travelled 600 kilometres by car in visiting the tax agent for the purposes of managing the taxpayer's tax affairs.

Reasons for Decision

Division 28 of the ITAA 1997 sets out the rules for working out deductions for car expenses. The table in section 28-15 of the ITAA 1997 summarises the basic requirements of the four methods of calculating car expense deductions and subsection 28-12(2) of the ITAA 1997 provides that you must use one of the four methods unless an exception applies, otherwise you cannot deduct anything for car expenses.

For each of the four alternative methods, 'business kilometres' are defined as kilometres the car travelled in the course of:

- (a) Producing assessable income; or
- (b) Travel between workplaces.

Section 25-5 of the ITAA 1997 provides for deductions for tax-related expenses. Subsection 25-5(5) of the ITAA 1997 states:

Under some provisions of this Act it is important to decide whether you used property for the purpose of producing assessable income. For provisions of that kind, your use of property is taken to be for that purpose insofar as you use the property for:

- (a) Managing your tax affairs; or
- (b) Complying with an obligation imposed on you by a Commonwealth law, insofar as that obligation relates to the tax affairs of another entity.

Subsection 25-5(5) of the ITAA 1997 provides the example of a computer purchased for preparing tax returns. Whilst the computer is a capital asset, to the extent it is used for preparing tax returns its decline in value is taken to be an income-producing expense under the subsection.

A car is an item of property that may be used for the purpose of producing assessable income. To the extent that a car held

by a taxpayer is used for managing the taxpayer's tax affairs or complying with an obligation imposed by a Commonwealth law relating to the tax affairs of another entity, its use is deemed by subsection 25-5(5) of the ITAA 1997 to be for an income-producing purpose.

Car travel for the purpose of visiting the tax agent is therefore counted as 'business kilometres' for the purposes of Division 28 of the ITAA 1997.

In the present case, the taxpayer has travelled in excess of 5000 business kilometres in the income year.

If none of the exceptions in Subdivision 28-J of the ITAA 1997 applies, the taxpayer can claim a deduction for the car expenses using one of the following four alternative methods:

- 'Cents per kilometre' method, subject to a limit of 5000 business kilometres with the excess discarded (Subdivision 28-C of the ITAA 1997)
- '12% of original value' method (Subdivision 28-D of the ITAA 1997)
- 'One-third of actual expenses' method (Subdivision 28-E of the ITAA 1997)
- 'Log book' method (Subdivision 28-F of the ITAA 1997)

FRINGE BENEFITS TAX AND CHRISTMAS PARTIES

There is no separate fringe benefits tax (FBT) category for Christmas parties and you may encounter many different circumstances when providing these events to your staff. Fringe benefits provided by you, an associate, or under an arrangement with a third party to any current employees, past and future employees and their associates (spouses and children), may attract FBT.

If you are not a tax-exempt organisation and do not use the 50-50 split method for meal entertainment, the following explanations may help you determine whether there are FBT implications arising from a Christmas party.

The costs (such as food and drink) associated with Christmas parties are exempt from FBT if they are **provided on a working day on your business premises and consumed by current employees**. A taxable fringe benefit will arise in respect of an associate of an employee who attends the party if not otherwise exempt under the minor benefits exemption.

You should note the change in the ATO's view to the application of the minor benefits exemption to Christmas parties and gifts. The minor benefits threshold of less than \$300 applies to each benefit provided, not to the total value of all associated benefits.

Exempt Benefits - Minor Benefits

The provision of a Christmas party to an employee may be a minor benefit and exempt if the cost of the party is less than \$300 per employee and certain conditions are met. The benefit