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Tax Newsletter

May 2010

Deferring Income

- Income received in advance of services to be provided will generally not be assessable until the services are provided.
- Taxpayers who provide professional services may consider, in consultation with their clients, rendering accounts after 30 June to defer the income.
- Consider whether the requirements to be classified as a small business entity are satisfied to access various tax concessions such as the simpler depreciation rules and the simpler trading stock rules.
- Individuals operating personal services businesses should ensure that they satisfy the relevant test to be excluded from the Personal Services Income regime or seek a determination from the Commissioner.

Maximising Deductions

Business taxpayers

- Debtors should be reviewed prior to 30 June to identify and to write off any bad debts.
- Review the asset register to identify any low-cost and/or low-value assets that may be pooled to access an accelerated rate of depreciation.
- Write off any depreciating assets which are no longer being held for use because a deduction may be available.
- Review trading stock for obsolete stock for which a deduction is available.
- Employees' superannuation contributions should be paid before 30 June to obtain a deduction and to avoid the Superannuation Guarantee Charge.
- A one-off bonus deduction for new investment in tangible depreciating assets purchased between 13 December 2008 and 31 December 2009 may be available. The bonus deduction is in addition to the depreciation deductions available to taxpayers.
- From 1 July 2009, losses incurred by individuals with an adjusted taxable income of $250,000 or more from non-commercial business activities will be quarantined even if they satisfy the four commerciality tests.

Non-business taxpayers

- Investors should consider prepaying interest on margin loans to obtain a deduction.
- Outgoings incurred for managed investment schemes may be deductible following a Full Federal Court decision.
- A recent decision of the Full Federal Court held that a taxpayer deriving Youth Allowance was allowed a deduction for various self-education expenses. (The Commissioner has sought special leave to appeal to the High Court against the decision.)
- Assets costing $300 or less may qualify for an immediate deduction subject to certain conditions.
- A deduction for personal superannuation contribution is available where the 10% rule is satisfied.

Capital Gains Tax

- Consider deferring the disposal of shortly-held assets to access the CGT discount, where available.
- Individual taxpayers can consider contributing some or all of capital gain to their superannuation fund because a deduction may be available for personal superannuation contributions.
- Consider whether a rollover relief is available to defer any capital gains.
- Consider the availability of the small business CGT concessions which can disregard, reduce or defer a capital gain arising from the disposal of an asset which has been used by an entity in the course of carrying on its business.

Companies

- The franking percentage for distributions to shareholders should be the same for each franking period to avoid a franking deficit tax.
- A private company has four months after the end of the income year to provide its shareholders with a distribution statement for dividends paid.
- Loans, payments and debt forgiveness by private companies to their shareholders and associates should be repaid by the earlier of the due date for lodgment of the company's return for the year or the actual lodgment date. Alternatively, appropriate loan agreements should be in place.

Trusts

- A minor (ie aged under 18) can receive up to $3,000 in non-taxable distribution for the 2009/10 income year.
- If a company is owned by a discretionary trust, consider whether a family trust election (FTE) is needed to ensure any losses or bad debts incurred by the company will be deductible.
- If shares are owned by a discretionary trust, consider the necessity for the trustee to make a FTE to ensure any franking credits attached to the dividends will not be 'wasted'.
- If a FTE has been previously made, avoid distributing outside the family group to avoid the family trust distributions tax.
- A recent High Court case confirmed that it is correct to apply the proportionate approach if the net income of a trust for tax purposes exceeds its accounting income.
- The Court also affirmed that the trustee can distribute capital gains as income of the trust for tax purposes if the trust deed permits it.
- Avoid retaining income in a trust because the income may be taxed at 46.5%.

Superannuation

- A re-contribution strategy may produce tax benefits for taxpayers under age 60.
- Low-income earners (including self-employed persons) should consider making a personal superannuation contribution to qualify for the government superannuation co-contribution payment.
- The concessional contributions cap for the 2009/10 has been reduced to $25,000 or $50,000 if over 50 years of age.
- For the 2009/10 income year, pensioners have the option to draw half of the year's minimum required pension amount.
- From 1 July 2009, a person's 'reportable superannuation contributions' is included in their 'adjusted income' when determining their eligibility for various tax offsets and social security benefits, such as the, the pensioner tax offset, senior Australians tax offset, and the spouse superannuation tax offset.
- From the 2009/10 income year, a spouse also includes a same sex partner where they live together on a genuine domestic basis in a relationship as a couple, or a partner (whether of the opposite or same sex) where the relationship is registered under a State or Territory law.

Developments Since 1 July 2009

Taxpayers should note recent tax law changes, which include:

- the foreign employment income derived by Australian resident individuals is not exempted from income tax, except in specified circumstances;
- the availability of an optional CGT roll-over for the transfer of assets between 'fixed trusts' and thus deferring the making of any capital gain or loss in respect of the transfer; and
- the changes to the tax treatment of employee share schemes (ESS), eg the $1,000 discount for upfront taxation of an ESS interest is only available if an individual's adjusted income is less than $180,000.

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PERSONAL TAXATION

50% Savings Discount for Interest Income

From 1 July 2011, the Government will provide individuals with a 50% tax discount on up to $1,000 earned on interest.

This includes interest earned on deposits held with any bank, building society or credit union as well as on bonds, debentures or annuity products.

The discount will be available for interest income earned directly as well as indirectly, such as via a trust or a managed investment scheme (MIS).

Adjusted taxable income

The Government states that taxpayers claiming the discount for interest income will have a reduced adjusted taxable income for the purpose of determining eligibility for transfer payments and other concessions.

This may result in some individuals and families becoming eligible for transfer payments or for a larger transfer payment.

The Government notes that the consequential expense primarily affects Family Tax Benefit, but will also affect other payments such as:

- the Baby Bonus;
- Child Care Benefit;
- the Education Tax Refund;
- the Commonwealth Seniors Health Card (CSHC); and
- the Pensioner Supplement (which is linked to eligibility for the CSHC).

The measure will apply from 1 July 2011.

Standard Deduction for Work-related Expenses

The Government will provide individual taxpayers with a standard deduction of $500 for work-related expenses and for the cost of managing tax affairs from 1 July 2012.

The standard deduction will increase to $1,000 from 1 July 2013.

Those taxpayers with deductible expenses greater than the standard deduction amount will still be able to claim their higher expenses, in lieu of claiming the standard deduction amount.

The standard deduction will reduce individuals' and families' adjusted taxable income for the purpose of determining their eligibility for transfer payments and other concessions (eg the Family Tax Benefit, the Baby Bonus, Child Care Benefit, the Commonwealth Seniors Health Card (CSHC) and the Seniors Supplement).

This will make some individuals and families eligible for transfer payments or for a larger transfer payment.

Medical Expenses Rebate Threshold Raised

From 1 July 2010, the medical expenses rebate threshold will increase from $1,500 to $2,000.

Taxpayers presently receive a rebate equal to 20% of net un-reimbursed eligible medical expenses above $1,500. This $1,500 threshold will increase to $2,000.

In addition, from 1 July 2011, the threshold will be indexed annually to the Consumer Price Index (CPI).

Medicare Levy Thresholds Increased for 2009/10

From the 2009/10 income year, the Medicare levy low-income thresholds will be increased to $18,488 for singles (up from $17,794 for 2008/09) and to $31,196 for those who are members of a family (up from $30,025 for 2008/09).

The additional amount of threshold for each dependent child or student will also be increased to $2,865 (from $2,757).

From 1 July 2009, the Medicare levy low-income threshold for pensioners below Age Pension age will be increased to $27,697 (from $25,299).

This increase will ensure that pensioners below Age Pension age do not pay the Medicare levy while they do not have an income tax liability.

SUPERANNUATION

Co-contribution Matching Rate Permanently Reduced to 100%

The Government has announced that it will seek to permanently set the matching rate for the superannuation co-contribution at 100% and the maximum co-contribution that is payable on an individual's eligible personal non-concessional superannuation contributions at $1,000.

As a result, the previously-legislated increase in the matching rate to 125% for the 2012/13 and 2013/14 years (and to 150% for 2014/15 and later years) will not proceed.

Eligible income thresholds frozen

In addition, the Government says that for 2010/11 and 2011/12 it will freeze the indexation applied on the income threshold above which the maximum superannuation co-contribution begins to phase down.

Under the superannuation co-contribution scheme, the Government currently provides a matching contribution for contributions made into superannuation out of after-tax income. The matching contribution is up to $1,000 for individuals with incomes of up to $31,920 in 2009/10 (with the amount available phasing down for incomes up to $61,920). The new measure will freeze these thresholds at $31,920 and $61,920 for two years.

The Government says this measure follows its earlier announcement in response to the Henry Tax Report, proposing a $500 annual superannuation contribution for individuals with an adjusted taxable income up to $37,000.

Superannuation Fund Deductions for Terminal Medical Condition Benefits

The Government has announced that it will seek to extend the range of benefits that are deductible by complying superannuation funds and retirement savings account providers to include terminal medical condition (TMC) benefits.

The Government says that this proposal addresses an anomaly in the taxation law regarding deductibility by superannuation funds and retirement saving account providers of the costs of providing certain benefits to members or holders.

Currently, the Government says deductions are allowable for the costs of providing benefits relating to the death, permanent incapacity and temporary incapacity conditions of release, but not those relating to the TMC condition of release.

This measure is proposed to have effect from 16 February 2008, the date the TMC condition of release was introduced into the superannuation legislation.

BUSINESS TAXATION

Look-through Treatment for Earnout Arrangements

All payments under a qualifying ‘earnout’ arrangement will be treated as relating to the underlying business asset.

Earnout arrangements are used to structure the sale of a business (or business assets) to manage uncertainty regarding the value of the business.

Under the earnout arrangement, an earnout right may entitle the buyer or seller to additional payments, depending on the subsequent performance of the business.

The proposed amendment will have effect from the date of the Royal Assent of the enabling legislation, with transitional provisions available for certain cases from 17 October 2007.

Increased Funding to Counter Cash Economy

The Government will provide $107.9 million over four years to the Tax Office, to address small business operators who use cash transactions to avoid tax. The Government states that this is expected to increase the "visibility of the Tax Office in the community".

This measure is expected to result in:

- an additional $491.8 million in revenue in fiscal balance terms over four years; and
- an increase of $39.9 million in Tax Office-administered expenses over the same period.

In underlying cash terms, the expected increase in revenue is $366.5 million over four years, including $146.7 million in GST collections that will be paid to the states and territories.

GST Compliance Program — funding for the Tax Office

The Government states that it will provide $337.5 million over four years (from the 2010/11 to the 2013/14 income years) to the Tax Office to fund additional activities that will promote voluntary GST compliance and provide a level playing field for Australian businesses.

The Government also states that the funding will address issues relating to:

- fraudulent GST refunds;
- systematic under-reporting of GST liabilities;
- non-lodgment of GST returns; and
- non-payment of GST debts.