



Chartered Accountants

LABOR'S TAX REFORMS

24 November 2007 ushered in a new era for the Australian political landscape with the Labor party winning the Federal election. As part of its election campaign, Labor promised various tax reforms which included changes to personal income tax, and measures to assist families with the increasing cost of raising children. A brief discussion of the various reforms follows.

PERSONAL INCOME TAX

Labor has stated that it will support the tax cuts outlined in the 2007/08 Budget. However, tax cuts for individuals earning more than \$180,000 will be deferred until the 2013/14 income year. Labor's proposed reforms will see the personal income tax system having three tax rates by the 2013/14 income year (from the current four), and the reduction of the highest marginal tax rate to 40%.

The reduction in the highest marginal tax rate will result in a reduction of the 'top up' tax on fully franked dividends from 23.60% to 16.40%.

The Low Income Tax Offset (LITO) will be gradually increased. The Senior Australians Tax Offset (SATO) will be adjusted in line with the increase in the LITO. These changes have not yet been legislated.

ASSISTING FAMILIES

A range of 'family friendly' measures will be introduced, and scheduled to go into effect on 1 July 2008, including:

- increasing the child care tax rebate to 50%, payable quarterly;
- providing a limited 50% Education Tax Refund for families receiving Family Tax Benefit Part A (FTB-A) or who have school-attending children receiving Youth Allowance; and

- limiting eligibility for Family Tax Benefit Part B (FTB-B) to families with a combined adjusted taxable income of less than \$250,000.

REVERSE CHANGES TO FAMILY TRUSTS

Labor is proposing to reverse the changes made to family trusts that were introduced in September 2007.

The changes saw the broadening of the definition of 'family' and 'family group', changing the test individual for a family trust in limited circumstances, and allowing the revoking of family trust elections and interposed entity elections in limited circumstances. The proposed date of effect is 1 July 2008.

➤ **TIP:** Labor's proposed reversal means taxpayers will only be able to access the changes introduced in September 2007 in the current income year.

TRUST CLONING

Trust cloning refers to the practice of transferring an asset between two trusts that have the same beneficiaries and terms. Generally, when an asset is transferred between two trusts, CGT implications will be triggered. However, where the beneficiaries and terms of the two trusts are similar, a CGT exception applies.

The Tax Office previously released a Taxation Ruling which provides its view on when the CGT exception applies. Since the release of the ruling, the Tax Office has become aware of examples where trusts, particularly discretionary trusts, may not be the same and therefore assets transferred between the trusts will trigger a CGT event.

The Tax Office is encouraging taxpayers or their advisers who have relied on the exception, but who are now concerned that the exception test was not satisfied, to contact it or lodge a private ruling request.

ABOLISHING TAX DEDUCTIONS FOR POLITICAL DONATIONS

Labor is proposing to abolish tax deductions for donations or contributions to political parties, including membership fees, from 1 July 2008.



FINANCIAL PLANNING

Mel James and Bob Kolevski are Authorised

Representatives for Professional Investment

Services Pty Ltd Australian Financial Services

Licence No. 234951 A.B.N. 11 074 608 558.

For an independent review of your savings, retirement and asset protection strategies, please contact either Mel or Bob.

BDJ TAKES ON NEW PARTNER

We are pleased to announce the appointment of Michael Galouzis as a Partner of our firm, effective from 1 January 2008.

For those clients not familiar with Michael, he has been a Manager with our firm for the last three and a half years providing accounting, taxation and general business advice to clients.

Michael is a Chartered Accountant and tax agent and has ten years experience in public practice, with broad experience dealing with clients in a range of industries.

PERSONAL SERVICES INCOME (PSI) CASE

The Tax Office has released a Decision Impact Statement (DIS) regarding an Administrative Appeals Tribunal (AAT) case concerning whether a taxpayer generating PSI satisfied the business premises test and, as a result, was entitled to a personal services business (PSB) determination from the Commissioner.

In this case, the AAT decided the private use of a garage which was part of a building used in the generating of PSI was not so slight that it should be ignored. The garage was used to store personal items and a motor vehicle which was not exclusively used for business. Consequently, the AAT was satisfied that the taxpayer did not use the premises exclusively for a business purpose, and did not meet the requirements of the business premises test.

PSI is ordinary or statutory income which is mainly derived, directly or indirectly through an interposed entity (company, trust or partnership) from an individual's personal exertion. However, the PSI regime does not apply when an individual is carrying on a PSB.

If a taxpayer passes the business premises test, they will be considered as carrying on a PSB and be excluded from the PSI regime. A taxpayer may seek a PSB determination from the Commissioner to be excluded from the PSI regime.

➤ **TIP:** Taxpayers who are deriving PSI and working from home should ensure that the business part be physically separate from their residence to satisfy the business premises test.

PSI AND THE RESULTS TEST

In a recent Federal Court case, two taxpayers generating PSI lost their appeals against the Commissioner. The case concerned the Commissioner's refusal to grant the taxpayers PSB determinations on the basis that they did not satisfy the results test.

The Court found that the relationship between the taxpayers and the company engaging their services was that of an employer-employee because:

- the taxpayers were not liable to rectify any defects in the work performed;
- payment for the services rendered was not pegged to the completion of any specific tasks; and
- no further equipment was required to be provided by the taxpayers for the efficient performance of the tasks.

If a taxpayer meets the requirements of the result test, they will be regarded as carrying on a PSB and be excluded from the PSI regime. The results test requires a taxpayer to meet three conditions:

- the income is paid to achieve a specific result or outcome;
- the taxpayer provides any necessary tools or equipment to do the work; and
- the taxpayer is liable to rectify any defects in the work.

➤ **TIP:** In determining whether a taxpayer meets the conditions of the results test, it is the economic substance and not the legal substance that is important.

WESFARMERS' ACQUISITION OF COLES

The Tax Office has released a Class Ruling providing its view on the tax implications for a Coles shareholder following the acquisition of Coles by Wesfarmers.

The ruling provides that Coles shareholders are able to disregard any capital gains arising from the acquisition by accessing the script for script rollover relief. However, the capital gains are not disregarded to the extent that the capital proceeds include the cash consideration received.

GIC AND SIC RATES RELEASED

The Tax Office has released the general interest charge and shortfall interest charge rates for the third quarter of the 2007/08 income year. The rates are as follows:

Rate	Annual(%)	Daily(%)
GIC	14.15	0.03866120
SIC	10.15	0.02773224

The Tax Office has also released the interest rate for overpayments (IOP), early payments (IEP) and delays in refund (DRI) for the third quarter of the 2007/08 income year. The applicable interest rate is 7.15%.

TAX OFFICE ASSISTANCE

In two separate but related media releases, the Tax Office has stated that farmers, businesses and individuals who are experiencing difficulty in complying with their tax obligations as a consequence of the drought, floods, bushfires and storms to contact its office either through their tax agents or directly.

FBT AND MINOR BENEFITS

In a recent Taxation Ruling, the Commissioner expressed that a fringe benefit provided by an employer to their employees (or associate) will only attract the minor benefits exemption where: the notional taxable value of each benefit is less than \$300; and

having regard to the circumstances, including a consideration of the infrequency and irregularity, it would be unreasonable to treat the benefit as a fringe benefit.

Further, the Ruling states that even if the notional taxable value of a benefit is less than \$300, the benefit is not necessarily an exempt benefit. There are certain fringe benefits that are specifically excluded from the operation of the minor benefits exemption.

If the minor benefits exemption applies to a benefit, no FBT liability arises from the provision of that benefit.

WASH SALE ARRANGEMENTS

The Tax Office has stated recently in a Taxation Ruling that the Commissioner may make a determination to cancel any tax benefits obtained in connection with a 'wash sale' arrangement. Whether the Commissioner makes a determination to cancel any tax benefits obtained will depend on the facts of the particular situation.

An arrangement where a taxpayer disposes of an asset in order to apply a resulting capital loss against a capital gain previously incurred (or deduction against assessable income), and both capital assets are significantly similar, may attract the Commissioner's adverse attention.

PROVISION OF TRADE CREDIT

The recently released Taxation Determination TD 2008/1 discusses the consequences of a private company providing trade credit to a shareholder (or their associate) on the usual terms it gives to parties at arm's length, and the shareholder fails to repay an amount within the agreed payment term. The Tax Office states that provided the private company deals with the failure to repay in the same manner in which it deals with defaults on similar loans made to parties at arm's length, the tax law does not automatically deem that a loan has been made by the private company to the shareholder (or their associate).

If the private company does not deal with a failure to repay on time by a shareholder (or their associate) in the same manner in which it deals with defaults of similar loans made to parties at arm's length, potentially a loan can be deemed to have been made.

A private company may be taken to pay a dividend at the end of the company's income year if it lends an amount to a shareholder (or their associate) during the year.

The dividend needs to be included in the assessable income of the shareholder (or their associate) as an unfranked dividend. (The definition of loan includes the provision of credit or any other form of financial accommodation.)

However, if the shareholder (or their associate) fully repays the amount by the earlier of either the due date for lodgment of the private company's tax return for the income year or the lodgment day of the private company's tax return for the income year, a loan does not arise between the private company and the shareholder (or their associate).

TIMING OF RECEIPTS

The Tax Office has issued a Self Managed Superannuation Funds (SMSF) Determination that provides its view on the timing of when a dividend or trust distribution is received by a SMSF for the purposes of the in-house asset rules. The Determination states that the timing depends on the payment option that is either chosen by the SMSF or prescribed by the company or trust respectively.

The in-house asset rules govern the proportion of a superannuation fund's assets that may be lent by the trustee to or invested in an employer-sponsor of the fund or an associate of the employer. The rules state that a trustee of a superannuation fund must not acquire in-house assets if to do so would increase the ratio of such assets to over 5% of total assets, or if the ratio already exceeds 5%. However, transitional provisions can apply to exclude investments in related entities as being in-house assets. One of the transitional provisions seeks to exclude investment made in related entities between 12 August 1999 and 30 June 2009 as being classified as in-house assets. This transitional provision requires a taxpayer to test when a dividend or trust distribution is received by the SMSF.

UK WAR WIDOWS PENSION

In two separate but related Interpretative Decisions, the Tax Office expresses its view that the UK War Widows pension and supplementary pension received by a taxpayer are not assessable income for the purpose of Australian tax. This is because the pensions are similar to a pension for defence caused death or incapacity paid under the Veterans' Entitlement Act, which is listed as an exempt payment for income tax purposes.

ALERT ON STAPLED SECURITIES

The Tax Office has issued a Taxpayer Alert warning taxpayers investing in stapled securities that it is considering whether they are entitled to a deduction when the stapled securities are sold on the ASX at a loss, or on the occurrence of an Assignment Event.

In particular, the Tax Office is considering whether the structure of a stapled security constitutes a scheme to obtain a tax benefit therefore denying any deductions arising from its disposal.

A stapled security is an arrangement where a company issues a security consisting of a note and a preference share to resident investors. The Tax Office said that in these arrangements the company issuing the securities suggests that an investor may claim deductions for losses in certain circumstances. These circumstances include the assignment, transfer or surrender of the note, or conversion or disposal of the stapled security.

ENTREPRENEURS' TAX OFFSET

Partners in a Partnership

In a recent Interpretative Decision, the Tax Office states its view that a taxpayer whose assessable income includes personal services income (PSI), which is attributed to being a partner in a partnership that is not conducting a personal services business (PSB), is entitled to the entrepreneurs' tax offset (ETO).

Company and Eligibility

In another recent Interpretative Decision, the Tax Office has provided its view that a company that is not conducting a PSB is entitled to the ETO. However, if the company is only deriving PSI, the ETO will be nil. This is because any PSI derived by a company does not form part of its assessable income but is included in the assessable income of the individual generating the PSI.

ETO and PSI

The ETO is available to eligible taxpayers. The offset is equal to 25% of the income tax liability that is attributed to a small business entity income. If the annual turnover is more than \$50,000, the

offset is phased out until it equals zero at turnover of \$75,000.

PSI is income that is mainly derived from an individual's personal exertion. The income can be derived either directly by the individual or indirectly through an interposed entity (company, trust or partnership). However, the PSI regime does not apply when an individual is carrying on a PSB.



We would like to remind clients that we are able to provide competitive residential mortgages via our alliance with Mortgageport.

Our firm works with Mortgageport in providing fully featured mortgage products, that are structured to reduce the after tax cost of debt. We are in many cases able to process your application from our office ensuring quick responses to all inquiries.

This service has been a great benefit to many of our clients already and we encourage all clients to call for more information.

Barnes Dowell James Chartered Accountants and Business Advisers

specialising in business services, tax, audit and wealth creation.

All Correspondence:
PO Box 1664
NORTH SYDNEY NSW 2059

Phone: 61 2 9956 8500
Fax: 61 2 9929 7428
Email: bdj@bdj.com.au
Website: www.bdj.com.au

North Sydney Office
Level 13 122 Arthur Street
NORTH SYDNEY NSW 2060

Manly Office
Level 5, 22 Central Avenue
Manly National Building
MANLY NSW 2095

Partners: C H Barnes
FCA

A J Dowell
B Com (UNSW), CA, JP

M W James
B Bus, FTIA, FPA (Aff)
CA - Financial Planning Specialist

B Kolevski
B Com, Affiliate ICAA, FPA (Aff) Dip FP

M Galouzis
B Com, CA,

Associates: M A Nakkian
CA

Consultants: P J Hennessy
FCA

Professional Investment Services Pty Ltd

Australian Financial Services Licence No. 234951

Authorised Representatives Mel James
Bob Kolevski

Important: This newsletter does not constitute advice. Clients should not act solely on the basis of the material contained in this newsletter. Items herein are general comments only and do not constitute or convey advice per se. Also changes in legislation may occur quickly. We therefore recommend that our formal advice be sought before acting in any of the areas. The newsletter is issued as a helpful guide to clients and for their private information. Therefore it should be regarded as confidential and not made available to any person without our prior written approval. Editor: M W James

© Barnes Dowell James March 2008 newsletter may not be reproduced without express permission

www.bdj.com.au