Coster Galgut
Chartered Accountants

# Tax Update – June 2022

## Inside



**Does the ATO's latest guidance on section 100A help? We explore the guidance and the issues.**

Plus, what's new for 2022-23 that you need to know.

As change occurs, we'll keep you posted!!

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# From the Regulators

## Section 100A guidance for the 2022 income year

Following the release of guidance earlier in the year concerning the trust distribution integrity rules in section 100A the ATO has provided some further comments on how it will be approaching section 100A in relation to the 2022 income year.

While the ATO had previously indicated that this guide would provide further examples, the guidance really just summarises some of the key points made in the draft ruling, draft practical compliance guidance and taxpayer alert issued earlier in the year.

At a very high level the ATO indicates that section 100A does not apply if the beneficiary who is presently entitled to the income simply receives or enjoys the benefit of the distribution. The ATO indicates that the majority of small business trust arrangements involve nothing more than presently entitled beneficiaries receiving their entitlement, or controllers re-investing the profits of the trust into the working capital of the business, which present a very low risk of section 100A applying.

For the 2022 year the ATO will be focusing its compliance resources to high-risk arrangements. In determining whether arrangements are high risk it is important to refer to the ATO's 2014 website guidance and PCG 2022/D1.

The guidance indicates that arrangements should be low-risk where:

- A beneficiary simply uses their entitlements to benefit themselves, their spouse and dependents, or
- The beneficiary's entitlement is retained by the trustee for use in commercial or income earning operations of the trust, provided that either:
    - The beneficiary is an individual who is employed in managing the business conducted by the trust or the beneficiary (or their spouse) controls the trustee; or
    - The beneficiary is a private company that enters into a loan agreement with the trustee that complies with Division 7A.

The ATO suggests that where arrangements fall within the above categories it is unlikely that the ATO will be reviewing the distributions. Having said that, even if an arrangement is consistent with a low-risk example provided by the ATO it is important for clients to maintain good records to prove what has happened and that beneficiaries have received the ultimate benefit of the funds that have been appointed to them.

It is important to remember that the position in this area may change once the ATO finalises the draft ruling and draft practical compliance guideline.

#### More information

- Managing section 100A for the 2021–22 income year
- Trust taxation - reimbursement agreement (2014 website guidance)
- PCG 2022/D1

## Small business focus areas

A list of items that the ATO will be paying particularly close attention to in processing small business returns this year has been published on the ATO website. The items include:

- The claiming of deductions for expenses that are private in nature and not related to business income, as well as overclaiming of business expenses (especially for taxpayers running a home-based business).
- Omission of business income, for example income from the sharing economy or new

business ventures. The key point with this item is that small businesses should include all income in their income tax return, including cash, coupons, EFTPOS, online, credit or debit card transactions, and income from platforms such as PayPal, WeChat or Alipay.
- Government payments or financial support received as a result of COVID-19 will normally need to be included as assessable income unless a specific exemption applies. Not all state and territory government payments that relate to COVID-19 qualify for tax-free treatment.
- Like all taxpayers, those running a business need to ensure that they gather and retain appropriate records to substantiate claims that will be made.

#### More information

- Tax time for small business: how to nail your tax return

## Fuel tax credits and the excise reduction

The ATO is reminding taxpayers that during the period from 30 March 2022 until 28 September 2022 businesses using fuel in heavy vehicles for travelling on public roads will not be able to claim fuel tax credits. This is because the road user charge exceeds the excise duty paid as a result of the Government's temporary reduction in the fuel excise payable for that period.

The reduction will also impact on the fuel tax credit rates for other uses of fuel.

The ATO recommends using the fuel tax calculator on the ATO website to ensure that the correct rates are used when completing the June activity statement labels for fuel tax credits.

#### More information

- From 30 March 2022 to 30 June 2022
- Fuel tax credit calculator

## Professional firm profit allocation reminder

The ATO has issued a reminder that professional firms should review their profit allocation arrangements using the risk assessment factors set out in PCG 2021/4. While the approach in the PCG technically applies from 1 July 2022, it would be prudent for professional practitioners to examine how their current arrangements would be treated under the guidelines to ascertain whether any significant changes may be needed.

The PCG focuses on whether principal practitioners who are involved in professional services firms are personally being taxed on an appropriate portion of the profits generated by the firm.

Practitioners are reminded that the guidelines only apply if the firm generates its income from a business structure and is not applicable for entities which generate income from the personal services of one or more individuals.

#### More information

- Professional firm profit allocation arrangements

## Guidance on COVID-19 related deductions

In completing individual tax returns for the 2022 income year practitioners should be aware that there have been some changes with respect to claiming deductions for expenses relating to COVID-19.

One of the key things to remember is that individuals can claim a deduction for the cost of COVID-19 tests that were required for work-related purposes (e.g., to determine if they can attend or remain at work).

Further, some individuals may be able to claim a deduction for the cost of protective items that protect against the risk of illness or injury while performing work duties. This can apply for workers in close proximity to customers and at risk of contracting COVID-19, who may be able to claim a deduction for protective items such as gloves, face masks or sanitiser.

The ATO also confirms the tax treatment of various support payments that may have been received by individual clients including:

- JobSeeker: this is included in assessable income
- COVID-19 disaster payment (delivered through Services Australia): this is not taxable
- Pandemic Leave Disaster Payment: this is assessable income

**More information**

- COVID-19 and getting your tax right

## Cents per km rate for cars

A new legislative instrument (LI 2022/24) has been issued by the ATO which states that the cents per kilometre rate for the **2023** income year (i.e., from 1 July 2022) is 78 cents per kilometre. This will be relevant for taxpayers who choose to apply the cents per kilometre method when calculating income tax deductions for their work-related car expenses.

## ESS deferred taxing point change

Employers and employees who participate in employee share scheme (ESS) arrangements should note that there has been a recent change to the rules regarding when a deferred taxing point occurs for shares or rights acquired under ESS arrangements which are subject to deferred taxation. Employees will no longer have a taxing point simply because they cease their employment with the relevant employer if this occurs on or after 1 July 2022.

The change will assist in preventing a problem that can arise for employees where they may be assessable on a large amount under the ESS tax rules as a result of ceasing employment, even if they may not be able to access or dispose of the shares or rights and may not have the financial resources available to satisfy the tax liability.

**More information**

- Changes to tax-deferred employee share schemes

## Working from home deductions

The ATO has updated its website guidance on claiming deductions for expenses incurred while working from home.

The first key reminder is that taxpayers must genuinely be working from home to fulfil their employment duties or to carry on a business activity in order to claim deductions. Merely carrying out minimal tasks such as occasionally checking emails or taking calls is not sufficient.

The other key reminder is that the taxpayer must personally incur additional expenses as a result of working from home in order to claim deductions.

Three methods are available to calculate the working from home deductions for the 2022 income year:

- Fixed rate method: An amount per work hour for additional running expenses, plus expenses not covered by the fixed rate (phone and internet, depreciation on assets other than furniture, stationery)
- Actual cost method: The actual expenses incurred as a result of working from home
- Shortcut method: An all-inclusive rate per work hour, only available from 1 March 2020 to 30 June 2022

From 1 July 2022 the 'shortcut' method can no longer be used.

It is important to remember that taxpayers are not able to claim deductions for general household items (such as coffee, tea, milk), private expenses or for costs that are reimbursed by the employer.

The employees guide to work expenses includes a section dealing with common myths that relate to claiming deductions for work related expenses. This includes clarifying the position when it comes to the substantiation exemption (ie, confirming that taxpayers are not automatically entitled to a deduction of $150 for laundry expenses or for 5,000 kilometres under the cents per kilometre method for car expenses), guidance on claiming deductions for gym memberships and comments on the treatment of ordinary clothing expenses.

**More information**

- Working from home expenses
- Employees guide for work expenses

## Legal professional privilege protocol

The ATO has released the final version of a legal professional privilege (LPP) protocol which explains how taxpayers should go about making LPP claims to the ATO in connection with requests for information and/or documents.

The ATO has become increasingly concerned with LPP being asserted over large numbers of documents. The protocol has been released in order to guide taxpayers and their advisers on the process the ATO follows when considering whether to accept that documents are privileged, or to challenge the claim.

Some of the ATO's major concerns in relation to LPP claims include:

- Contrived arrangements or relationships which purport to attract LPP where there is a purpose of concealing communications;
- Routing advice through a lawyer merely for the purpose of obtaining privilege;
- Legal engagements entered into after the substance of advice was provided by non-legal persons;
- Communications exclusively between non-legal persons in circumstances where the involvement of a lawyer is not apparent.

Another major point made by the ATO is that the protocol will generally be more relevant for larger businesses where documents are subject to formal production notices, and that in most cases involving smaller businesses the ATO does not rely on their information gathering powers unless this becomes necessary (e.g., after other attempts to obtain information using a co-operative approach have failed).

**More information**

- Legal professional privilege (LPP) protocol

## ATO warning on 'wash sales'

The ATO has issued a warning in relation to taxpayers entering into wash sales in order to artificially create or increase their tax or capital losses before year-end.

Wash sales typically involve the disposal of assets such as cryptocurrency or shares just before the end of the financial year, with the taxpayer reacquiring the same or substantially similar assets a short time later.

Typically, this is done to artificially crystallise capital losses so that they can be offset against capital gains already derived in the income year, or that are expected to be derived before year end.

When taxpayers enter into wash sale arrangements this can trigger the general anti-avoidance rules in Part IVA. If Part IVA applies the taxpayer can lose the benefit of the capital loss and can be subject to penalties.

**More information**

- Wash sales: The ATO is cleaning up dirty laundry

# Rulings, determinations & guidance

## Certainty on Division 7A sub-trust arrangements

**PCG 2017/13**

This PCG deals with the maturity / termination of sub-trust arrangements relating to unpaid present entitlements (UPEs) owing to company beneficiaries. The ATO has indicated previously that where a 7-year interest only sub-trust loan has been used and is expiring but the trust does not have sufficient funds to pay this out, the trust and the company can potentially then use a normal 7 year (principal and interest) Division 7A loan agreement for the remaining balance. This can often be effective in preventing a deemed dividend from being triggered in relation to the UPE balance.

Until recently the guidance has applied to sub-trust arrangements expiring in the 2017, 2018, 2019, 2020 and 2021 income years.

The ATO has amended the PCG to confirm that it applies to:

- Sub-trust arrangements maturing during or after the 2016-17 income year that have been dealt with in accordance with either 7 year or 10 year interest only sub-trust loan; and
- UPEs arising on or before 30 June 2022.

This means that the position taken in the PCG applies to any sub-trust arrangement created in respect of UPEs arising between the 2010 to 2022 income years (inclusive).

## Effective lives of depreciating assets

**TR 2022/1 effective life of depreciating assets (applicable from 1 July 2022)**

The Commissioner has released the annual ruling which sets out the effective lives of depreciating assets from 1 July 2022. In most cases taxpayers can choose to use the effective lives set out in the ATO ruling or make their own estimate of the effective life of a depreciating asset.

## Reasonable travel and overtime meal allowances

**TD 2022/10 what are the reasonable travel and overtime meal allowance expense amounts for the 2022-23 income year?**

The ATO has released its annual determination setting out the Commissioner's reasonable amounts for the purposes of the substantiation exception for the 2023 income year in relation to claims made by employees for:

- Overtime meal expenses - for food and drink when working overtime;
- Domestic travel expenses - for accommodation, food and drink, and incidentals when travelling away from home overnight for work; and
- Overseas travel expenses - for food and drink, and incidentals when travelling overseas for work.

In broad terms, an employee does not need to satisfy the normal strict record keeping rules if they receive a bona fide travel or overtime meal allowance and the deduction they are claiming does not exceed the ATO's reasonable rates. However, it is important to recognise that appropriate records still need to be met to justify any deductions that are being claimed and deductions can only be claimed for expenses that have actually been incurred.

### Hybrid mismatches and the US tax system

**TD 2022/9**

This determination relates to a specific provision in the US tax code, section 951A, and how it interacts with the hybrid mismatch provisions in the Australian tax system.

Broadly, the hybrid mismatch provisions can operate to prevent entities that are liable to income tax in Australia from obtaining a tax benefit by exploiting differences in the treatment of entities and instruments across different tax jurisdictions.

Section 951A of the US tax code operates to include certain income or profits of a controlled foreign corporation in working out the tax base of a US shareholder. This TD looks at whether section 951A corresponds to sections 456 or 457 of the ITAA 1936, which form part of the Australian controlled foreign company provisions. While there might appear to be some similarities between these provisions, the ATO concludes that the substance of section 951A is not the same as the substance of sections 456 or 457.

That is, the fact that an amount might be taxable in the US due to the operation of section 951A will not prevent the hybrid mismatch rules from applying.

### Company residency – central management and control

**PCG 2018/9**

The ATO has amended this PCG to extend the transitional period for companies to change governance arrangements and ensure that central management and control is outside Australia. The transitional period has been extended until 31 December 2022.

During the transitional period the Commissioner won't apply resources to review a foreign-incorporated company's residency status if it meets certain criteria and during this period it:

- Changes its governance arrangements, so that its central management and control is exercised outside Australia by the end of the transitional period
- Does not commence carrying on business in Australia (other than because its central management and control is exercised in Australia), and
- Does not undertake or enter:
  - Any artificial or contrived arrangements that affect the location of its central management and control, or
  - Any tax avoidance scheme whose outcome depends, in whole or part, on whether it is a resident or non-resident.

## Cases

### Disclaiming trust entitlements

**Decision Impact Statement – Carter**

The ATO has released a decision impact statement relating to the recent High Court decision in the *Carter* case from April 2022, which was discussed in the April 2022 Tax Update from Coster Galgut.

Briefly, the High Court confirmed that the tax rules focus on whether beneficiaries are presently entitled to trust income at the end of the relevant income year. Actions taken by beneficiaries after this time cannot really alter the tax position, even if they are effective from a legal perspective.

In the Carter case some beneficiaries of a trust took steps to disclaim their interest in some trust distributions. However, because the disclaimer was undertaken after the end of the relevant income year it had no impact on the tax outcome for the beneficiaries, who were still assessed on a proportionate amount of the trust's net income for tax purposes for that year.

Practically, this means that if a beneficiary wants to disclaim an entitlement to a trust distribution and avoid being taxed on a share of the trust's net income for tax purposes then this would need to be done before the end of the relevant income year, which could be difficult (e.g., knowledge of the distribution might not arise until after the income year has ended).

Beneficiaries who are considering disclaiming an entitlement to trust income need to be aware of the tax outcome. For example, a beneficiary might still be assessed on some of the trust's net income even though they have taken steps to effectively disclaim the entitlement and won't end up receiving any funds from the trust.

The ATO has already withdrawn ATO ID 2010/85 which previously indicated that a beneficiary who has validly disclaimed an entitlement to trust income is not presently entitled to a share of the income of the trust for tax purposes. The ATO will also update commentary on the ATO website to reflect the High Court decision.