Coster Galgut
Chartered Accountants

TAX U PDATE – SEPTEMBER 2022

The important details for accountants & advisers across September 2022

What did I miss?

Of note in September was the guidance from the ATO on CGT and non-residents – an area that is confusing primarily because of the differing approaches.

Further work has been released on the section 100A integrity rules with a proposal to remove the "blue zone" and bolster the examples in the "green zone".

And, the ATO has taken pre-emptive action on the allocation of profits in professional services firms.

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INSIDE

From Government

Cryptocurrency won't be treated as a foreign currency

Treasury released exposure draft legislation that ensures digital currencies such as Bitcoin are not treated as a foreign currency for income tax purposes. The proposed change is driven by the uncertainty that has arisen following the decision by El Salvador to adopt Bitcoin as a legal tender.

The changes amend the definition of foreign currency to exclude digital currency (as defined in the GST Act). Further, the definition of digital currency in the GST Act is modified to ensure it excludes government-issued digital currencies and includes digital currencies that are not government-issued but have been adopted as a legal tender.

If digital currency was treated as a foreign currency, then it would normally be taxed on revenue account regardless of whether it was held for short term gain or as part of a longer-term investment portfolio. This proposed change ensures the taxation of digital currencies depends on the taxpayer's circumstances.

More
Clarifying crypto not taxed as foreign currency

FBT record keeping consultation

Treasury has released exposure draft legislation aimed at reducing FBT compliance costs by softening the record keeping requirements in some areas. Broadly, the proposed legislation allows employers to rely on alternative records instead of needing to obtain specific documents such as employee declarations.

Currently, employers are required to retain certain documents in a specific form, which involves additional costs and sometimes forces employers (and employees) to create duplicate records.

The draft legislation allows the Commissioner of Taxation to issue legislative instruments which specify the cases in which appropriate alternative records can be relied on and set the minimum standards for those records.

These changes should reduce the effort required by clients to meet their FBT record keeping obligations although it is likely that at least some FBT-specific records will still need to be created and retained by employers.

Draft legislative instruments relating to travel diaries and relocation transport have been released and provide an indication of how the system will operate if the legislation is passed.

More
Fringe benefits tax - record keeping exposure draft legislation
Draft travel diary legislative instrument
Draft relocation transport legislative instrument

Franked distributions and capital raising

The Government is seeking to prevent shareholders from taking advantage of franking credits attached to dividends that are funded by capital raisings. Treasury has released exposure draft legislation relating to this proposed change, which was first announced by the Government back in the 2017 Mid-Year Economic and Fiscal Outlook.

A distribution (dividend) paid by an entity will be treated as being funded by capital raising if:

- The distribution is not consistent with an established practice of the entity of making distributions of that kind on a regular basis;
- There is an issue of equity interests in the entity; and
- It is reasonable to conclude, having regard to all relevant circumstances, that either:
    - The principal effect of the issue of any of the equity interests was to directly or indirectly fund all or part of the distribution; or
    - An entity that issued or facilitated the issue of the interests did so for a purpose of funding all or part of the distribution.

The proposed changes seek to prevent the use of artificial arrangements where capital is raised to fund the payment of franked dividends to shareholders and therefore enable the distribution of franking credits. The Government is concerned that these arrangements can involve a manipulation of the system to allow existing shareholders to obtain the benefit of both the franking credits and the profits that generated those credits being retained in the company.

The effect of the proposed amendments is that direct or indirect recipients of affected dividends are not entitled to a tax offset, and the amount of the franking credit is not included in the assessable income of the recipient. The dividends are also not exempt from non-resident withholding tax.

The draft legislation is intended to apply to dividends paid on or after 19 December 2016 (i.e., it applies retrospectively), in line with the announcement made in the 2017 Mid-Year Economic and Fiscal Outlook.

More
Franked distributions and capital raising

From the Regulators

Streamlining application of section 100A integrity rules

The ATO has released new materials relating to the application of the integrity rules in section 100A which deal with income that has been appointed to a beneficiary in connection with a reimbursement agreement. The ATO has indicated that the materials released earlier this year should be finalised by the end of the year.

The ATO intends to remove the "blue zone" in order to streamline the guidance and plans to include some further examples of situations that would fall within the "green zone" and "red zone".

The ATO has released draft versions of some additional "green zone" examples (i.e., scenarios that would be considered at low risk of attracting ATO compliance resources) that it is considering including in the final version of PCG 2022/D1. These include examples dealing with the following scenarios:

a) A loss trust or company is made presently entitled to trust income and the beneficiary entity is a member of the same family group as the distributing trust. The ATO indicates that this could potentially be considered low risk if the entity receiving the distribution continues to be solvent and it receives the benefit of the income appointed to it.
b) There is a time lag of no more than 2 years between when a beneficiary becomes entitled to trust income and that entitlement being satisfied.
c) There is a testamentary trust that is maintained for the benefit of an individual where the trustee reinvests income to which the individual is presently entitled.
d) There is a business carried on by a trust where two generations of the same family manage that business.

Pre-emptive action on profits of professional firms

The ATO has contacting individual professional practitioners who have been identified as high risk under the recently updated guidance on the allocation of professional firm profits. While the updated guidelines only apply from 1 July 2022, the ATO appears to be making an advance attempt to ensure that these practitioners are aware of the new guidance and are considering changes that might need to be made to their arrangements to fall within a lower risk category.

If you have a client who is contacted by the ATO on this issue, it would be prudent to discuss the guidance in PCG 2021/4 with them and confirm whether their existing arrangements would be treated as high risk. If the client's existing arrangements fall within the high-risk category and the client wants to move into a lower risk category, then it will be necessary to make these potential changes in the 2023 income year.

More
Professional firm profit allocation arrangements

The knowledge base on the member-only website has a series of standards and tools to assist. Log in to access:

- Procedure Allocation of professional firm profits
- Workpaper Allocation of professional firm profits
- Letter Allocation of professional firm profits - high risk
- Letter Allocation of professional firm profits - low risk
- Letter Allocation of professional firm profits - moderate risk

CGT basics for non-residents

The ATO has published new guidance on two of the key issues that arise when non-resident individuals are selling property located in Australia.

The first issue relates to the main residence exemption. From 1 July 2020, individual taxpayers cannot generally access the main residence exemption (at all) if they are classified as a non-resident when the CGT event happens. The only real exception to this is where the individual has been a non-resident for 6 years or less and can satisfy the 'life events test'. If the main residence exemption is not available because of the recent changes in this area, then the cost base of the property should generally be based on the original purchase price.

Second, taxpayers cannot apply the CGT discount to the extent that they have been classified as a non-resident or temporary resident. However, these rules look at the individual's residency status across the ownership period rather than focusing on their residency status at the time of the CGT event. For example, if the individual has been a non-resident for part of the ownership period, then the CGT discount could still be available, but the discount percentage might be less than 50%. The method for calculating the discount percentage depends on when the asset was acquired and the individual's residency status on 8 May 2012.

More
Getting CGT right for foreign residents

Market valuations for tax purposes

The ATO has released a new guide that updates and replaces the 'Market valuation for tax purposes' web content. The new guide provides more contemporary guidance on the Commissioner's expectations when taxpayers are determining the market value of an asset for tax purposes, including evidence that can be used to support a market valuation.

The ATO focuses more on the process that is undertaken to determine the market value of an asset rather than who undertakes the valuation (i.e., there is not normally a specific requirement to obtain use a qualified valuer). However, the ATO notes that a valuation carried out by a suitably qualified valuer following industry standards and professional codes of conduct is generally considered reliable.

The guide sets out a range of approaches that might be appropriate in valuing different asset classes if clients decide to undertake their own valuation instead of engaging a qualified valuer.

More
Market valuation for tax purposes

Common errors with STP phase 2 reporting

Many employers have started reporting under STP Phase 2 since the commencement on 1 January 2022 and the ATO has provided some initial feedback on common errors that are being made. These include:

- Using incorrect pay codes or categories. Employers and advisers should check if they are using the right pay codes for items that need to be listed separately, such as bonuses, commissions and overtime.
- Calculation errors in year-to-date reporting. It seems that some software requires year-to-date amounts

to be input manually and employers / advisers are making calculation errors.
- Incorrectly categorising allowances. These must all be reported separately under STP Phase 2 (which includes 8 allowance categories and one for 'other allowances').

As this is a new area, and the rules are finicky, it is important for advisers to take a little more time to ensure that the reporting is completed correctly.

More
Getting your STP Phase 2 reporting right
Single Touch Payroll Phase 2 employer reporting guidelines

Input tax credit estimators

The ATO has issued a warning about the use of input tax credit estimators in calculating GST claims. These estimators increase the risk that clients may over-claim their GST credit entitlements, which means they are more likely to be reviewed or audited.

The estimators rely on data to calculate an estimate, average, or percentage of GST credits for the unprocessed tax invoices of a business for a tax period. They are usually used by large organisations that can bear the time and cost to review the use of the estimator and complete any additional compliance work required (such as amending activity statements etc.).

Further, the ATO states that the use of these estimators can lead to an increased risk of penalties for lack of reasonable care, recklessness, or even intentional disregard of the law.

If you have clients that use input tax credit estimators, it is important to review the guidance released by the ATO on how these should be used. It is also important to ensure that the estimates and any additional calculations are being reviewed.

More
Input Tax Credit estimators

Robodebt settlement payments

The ATO has confirmed that settlement payments received by taxpayers as eligible participants in the Services Australia income compliance (Robodebt) class action are not included in assessable income. These payments do not need to be included in the individual tax return.

More
Services Australia income compliance class action settlement payments
Class action settlement

Rulings, determinations & guidance

Games and sports income tax exemption

TR 2022/2 the games and sports exemption

There do not appear to be any significant differences between the draft (TR 2021/D6) and the finalised ruling on the games and sports income tax exemption.

The ruling sets out the requirements for sports club entities to validly self-assess as being exempt from income tax. The principal requirements are:

- The entity must be a not-for-profit entity (generally requires that the organisation must not be able to distribute profits or assets to members); and
- The entity must have a main purpose of the encouragement of a game or sport.

The ruling examines the second requirement in detail, particularly with reference to situations where the entity also has a level of commercial operations. While earning revenue from commercial operations will not necessarily mean a club does not qualify for the income tax exemption under this category, there needs to be an objective determination of the extent to which commercial operations are a means to the end of advancing the sporting purpose, or if they are advancing some other purpose.

Advisers with clients operating in this area that have self-assessed their income tax exempt status should carefully review their client's operations in light of the new ruling, especially if the organisation has a material level of commercial operations.

Non-commercial loss 'Special circumstances' safe harbour

PCG 2022/1 Non-commercial business losses - Commissioner's discretion regarding flood, bushfire or COVID-19

The ATO has finalised its practical compliance guideline that provides a safe harbour position for taxpayers looking to rely on the Commissioner's discretion in relation to the non-commercial loss rules on the basis that the business has been impacted by 'special circumstances'.

A taxpayer that is not able to pass the non-commercial loss rules to utilise a business loss against their other income has the option of applying for the Commissioner's discretion to allow the use of the tax losses. The taxpayer generally needs to convince the Commissioner that the business activity was affected by special circumstances that were outside the control of the operators of the business.

The PCG sets out a safe harbour position that allows taxpayers to utilise the losses as if the Commissioner had exercised discretion, without needing to apply for this. The safe harbour approach applies for the 2020, 2021 and 2022 income years and is primarily aimed at businesses that have been affected by flood, bushfire and/or COVID-19.

All of the following conditions must be satisfied to qualify for the safe harbour:

- The individual must satisfy the $250,000 adjustable income test;
- The individual must make a loss from the business activity (excluding losses deferred from a previous income year);
- The business activity was affected by one or more of the following events:
    1. Flood (including where receiving ATO flood support);
    2. Bushfire (including where the business qualified for an ATO bushfire lodgment and payment deferral); or
    3. Aa government-imposed lockdown, business closure and/or restriction due to COVID-19;
- The relevant event meant that the taxpayer was not able to carry on the business activity, or unable to carry it on to the same scale as was usual, or some or all of the customers of the business were not able to access the business activity, or access it in the same way as usual;
- The individual has not applied for a private ruling requesting the Commissioner exercise the 'special circumstances' discretion in relation to the business activity in the relevant income year; and
- The taxpayer has evidence to support that they are eligible for the safe harbour.

The safe harbour will only apply to losses that have been incurred during the 2020, 2021, or 2022 income years and where the safe harbour conditions are met for the relevant income year. Losses that have been generated in earlier years (i.e., and not due to the special circumstances) will continue to be deferred until the individual can pass the $250,000 adjustable income test and the business can satisfy at least one of the commerciality tests (or have the Commissioner exercise the discretion outside the terms of the safe harbour).

Clarity on GST and residential colleges

PCG 2022/D3 Goods and services tax and residential colleges

This draft PCG is aimed at residential colleges that are endorsed charities, and which make supplies of accommodation, meals, tertiary residential college courses and religious services, and the extent to which the supplies can be treated as GST-free.

There are a number of GST concessions available to endorsed charities, including some provisions in section 38-250 GST Act which allow these entities to treat certain supplies as GST-free, rather than taxable or input taxed, if certain requirements are satisfied. Section 38-250 provides that supplies are GST-free if the consideration for:

- A supply of accommodation is less than 75% of the GST-inclusive market value of the supply (accommodation market value test);
- A supply other than a supply of accommodation is less than 50% of the GST-inclusive market value of the supply (non-accommodation market value test);
- A supply of accommodation is less than 75% of the cost to the supplier of providing that accommodation (accommodation cost test); or
- A supply other than a supply of accommodation is less than 75% of the consideration the supplier provided, or was liable to provide, for acquiring the thing supplied (non-accommodation cost test).

The draft PCG provides guidance on applying the market value tests, as these are particularly difficult to apply given the various components of the supplies being made. The nature of the various supplies made, and how the fees for these need to be apportioned and compared against their market values, is discussed in detail with reference to the ATO's charity benchmarks.

Withholding variation for minors

LI 2022/28 Withholding Variation to Nil for Low Income Minors Legislative Instrument 2022

The ATO has released a legislative instrument that reduces the amounts required to be withheld from certain payments to minors where a TFN has not been provided. The legislative instrument varies the withholding obligation to nil in the following cases:

- Payments relating to work and services, termination of employment, and compensation where the recipient:
  - Is an individual under 18 years of age at the time of payment,
  - Has not provided the payer with a TFN declaration that is in effect, and
  - Is to receive an amount which does not exceed:
    a) $350 where the payer pays the payee on a weekly basis,
    b) $700 where the payer pays the payee on a fortnightly basis, or
    c) $1,517 where the payer pays the payee monthly.
- Payments relating to supplies made as part of an enterprise where:
  - The supplier is an individual under 18 years of age at the time of payment,
  - The supplier does not quote an ABN to the payer, and
  - The amount paid to the supplier does not exceed $350 per week.

Cases

Wine equalisation tax – is the full price paid for the wine?

Lubiana Family Trust (Trustee of) v FC of T [2022] AATA 2826

Although dealing with a specific provision of the wine equalisation tax legislation, this case is instructive from a statutory interpretation perspective, and demonstrates the perils of attempting novel interpretations without a solid legal basis.

The case involved the determination of the taxable value of wine, which impacts on the wine equalisation tax (WET) liability. The case focused on the phrase in the legislation which states, *"the taxable value is the price (excluding wine tax and GST) for which the wine was sold".*

In assessing the taxpayer for WET, the Commissioner based the assessment on the full sale price of the wine. The taxpayer objected to this, arguing that the price should be dissected on the basis that the full sale price partly represented consideration for the wine, but also represented consideration for the packaging /

container, delivery, and the "goodwill, reputation and romance" attributable to the brand. As a result, the taxpayer argued that the WET liability should be based on a lower amount.

In dismissing the taxpayer's arguments and finding for the Commissioner that WET should be payable on the full invoice amounts, the AAT referred to both precedential case law and specific provisions of the WET legislation which indicated that it was not possible to dissect the sale price.

It was also noted that the taxpayer had invoiced the wine as a single sale, consistent with a characterisation of a single transaction. As a result, the argument that an element of goodwill could be separated out of the sale price, and that the purchasers were partly paying for this rather than just paying for the wine, could not be supported.

Nice try from an excellent wine producer but it's a no go on the argument.

Legislation

Lifting the income limit on Seniors Health Card

Social Services and Other Legislation Amendment (Lifting the Income Limit for the Commonwealth Seniors Health Card) Bill 2022

This Bill passed Parliament on 28 September 2022.

The amendments increase the income test limits for the Commonwealth Seniors Health Card (CSHC) that provides subsidised pharmaceuticals and other medical benefits for self-funded retirees that have reached aged pension age.

	Current ($ per annum)	New ($ per annum)
Single	$61,284	$90,000
Couples combined	$98,054	$144,000

The income test captures adjusted taxable income plus deeming on account-based pensions unless grandfathered under the pre-1 July 2015 rules.

The CSHC is not asset tested.

The amendments come into effect 7 days after Royal Assent.

Asset test extended on proceeds of sale of main residence

Social Services and Other Legislation Amendment (Incentivising Pensioners to Downsize) Bill 2022

This Bill was introduced into the House of Reps on 7 Sept 2022.

If enacted, the amendments will extend the standard assets test exemption on proceeds received from the sale of a main residence from 12 months to 24 months. The proceeds if invested in a financial asset will still be deemed under the income test, however, the entire sale proceeds will be deemed at the lower deeming rate of 0.25%.

The exemptions apply until the income support recipient acquires another main residence or the 24-month period expires.

Reducing tax rates on the Pacific Australia Labour Mobility scheme and other amendments

Treasury Laws Amendment (2022 Measures No. 3) Bill 2022
Income Tax Amendment (Labour Mobility Program) Bill 2022

This Bill was introduced into the House of Reps on 8 Sept 2022.

These two bills combine to reduce the tax rate on certain income earned by foreign resident workers participating in the Pacific Australia Labour Mobility scheme and the Australian Agriculture Worker Program.

The amendments would reduce the marginal rates of tax applying to income derived by foreign resident workers under the Pacific Australia Labour Mobility scheme to a flat rate of 15%. Taxpayers participating in the Australian Agriculture Worker Program will be eligible for a tax offset that will ensure that a 15% tax rate effectively applies to the first $45,000 of program income (less related deductions).

The proposed changes will take effect from 1 July 2022.

Other changes contained in the Treasury Laws Amendment (2022 Measures No. 3) Bill include:

- Doubling the financial penalties for contraventions of foreign acquisition and investment provisions relating only to residential land (from 1 January 2023);
- Allowing protected information to be shared with Australian government agencies for the purpose of administering major disaster support programs; and

Faith based superannuation

Treasury Laws Amendment (2022 Measures No. 3) Bill 2022

This same Bill, if enacted, will amend the Superannuation Industry (Supervision) Act 1993 to provide for an alternative annual performance test for faith-based superannuation products.

The annual performance tests hold superannuation trustees to account for product underperformance. The performance test measures investment performance (including investment fees and taxes) and administration fees for individual products.

The Bill provides introduces a supplementary performance test for faith-based products that allows investment in accordance with faith-based principles to be taken into account when assessing the performance of a product against benchmarks. APRA will determine the parameters of the supplementary performance test.