T AX UPDATE – SEPTEMBER 2023

What did I miss?

Why is the ATO targeting self-education expenses? There had to be a reason for the release of a new draft ruling, right? We look at what TR 2023/D1 reveals.

Plus, some clarity from the ATO on the Technology Boost. Speaking of the 'boost', we also delve into the flow through impact for shareholders of the boost and other similar initiatives.

And, the latest from the recent session of Parliament. New legislation seeks to implement a number of Budget measures and other announcements including the $20k instant asset write-off, small business energy incentive, and the changes to non arm's length expenses for super funds.

Regards,
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INSIDE

From Government

The objective of super

Following the release of a consultation paper released in February 2023, Treasury has issued exposure draft legislation for consultation with the aim of enshrining the following objective of superannuation into the legislation:

> *'To preserve savings to deliver income for a dignified retirement, alongside government support, in an equitable and sustainable way.'*

The significance of legislating the objective of superannuation is to ensure any future legislated changes to the system are consistent with this objective.

The legislated objective contains some key concepts, including:

- 'Equitable' seeks to underscore the distributional impact of superannuation policy. In this context, policy-makers when making changes to the superannuation system should be aware of its impact to different groups of varying needs including women, First Nations Australians, vulnerable members and low-income earners.
- 'Sustainable' encapsulates the changing needs of an ageing population and recognises the role of superannuation in reducing reliance on the Age Pension. The explanatory materials also allude to the cost of tax concessions that are used to incentivise Australians to save for retirement. Legislated change should focus on sustainability by targeting concessions to where they are needed most.
- 'Deliver income' reinforces the idea that superannuation savings "should be drawn down to provide individuals with a source of income during their retirement."

More than 15 million Australians now have a superannuation account. Australia's superannuation pool has grown from around $148 billion in 1992 to $3.5 trillion in 2023 and will continue to grow. Total superannuation balances as a proportion of GDP are projected to almost double from 116% in 2022–23 to around 218% of GDP by 2062-63.

In that context, the explanatory materials recognise the value of the superannuation system as a source of capital, "which can support investment in capacity-building areas of the economy where there is alignment between the best financial interests of members and national economic priorities."

More information
Legislating the objective of superannuation

Combating tax adviser misconduct

The Government has released exposure draft legislation and materials for consultation in response to recent scandals involving tax adviser misconduct and the leaking of confidential information to their clients.

These proposed reforms target several priority areas, with the aim of strengthening the integrity of the tax system and increasing the power of regulators. The main proposals contained in the various exposure draft materials are set out below:

Tax Practitioners Board (TPB)

- Extending the time period for the TPB to conduct investigations into potential breaches of the Tax Agent Services Act from a maximum of 6 months to 24 months.
- Changes to the Register of tax practitioners to improve its functionality and utility. Also, providing an option for the TPB to publish tax practitioner misconduct on the Register.

Information sharing

- Allowing the ATO and TPB to share protected information with Treasury and to the Minister on misconduct arising out of suspected breaches of confidence by intermediaries engaging with the Commonwealth.
- Allowing the ATO and TPB to share protected information with prescribed professional associations where they reasonably believe a person's actions may constitute a breach of their disciplinary body's code of conduct or professional standards.

Reform of promoter penalty laws

- Increasing the time the ATO has to bring an application for civil penalty proceedings in the Federal Court of Australia in response to a contravention of the promoter penalty laws from 4 years to 6 years.
- Strengthening the penalty provisions in relation to a contravention of the promoter penalty laws and aligning the maximum penalties with those in the Corporations Act 2001.
- Expanding the application of the promoter penalty regime, including the broadening the scope of certain definitions, to overcome difficulties in applying this penalty regime.

Whistleblower protections

- Extending whistleblower protections for disclosures to the TPB, as well as a number of bodies that provide assistance in relation to whistleblower disclosures.
- Aligning some protections in the tax whistleblower regime with the Public Interest Disclosure regime.
- Enabling the ATO, ACNC and TPB to share disclosed information more effectively.

More information

- Response to PwC – Tax Practitioners Board reforms
- Response to PwC – Information sharing
- Response to PwC - Reform of promoter penalty laws
- Response to PwC - Whistleblower protections

From the Regulators

ATO rental property focus areas

With ATO reviews indicating that 9 out of 10 rental property owners are making mistakes in their tax returns, rental property owners remain a key focus of the ATO this tax time.

In that context, the ATO has set out reminders on some of the key issues for rental property owners.

First, the ATO notes that all rental income should be included in the return. This includes income from short-term rental arrangements, renting part of a home and other rental related income like insurance payouts and rental bond money retained.

When reviewing rental property expenses, the ATO is reminding practitioners and taxpayers that not all expenses are necessarily treated in the same way for tax purposes. There will be cases where expenses are deductible up-front, while other types of expenditure might only be claimed as deductions over time.

In some cases, expenditure may not be deductible at all. A good example of this is when it comes to depreciation deductions for certain second-hand depreciating assets used in residential rental properties.

The ATO has issued warnings around correctly making the distinction between repairs and maintenance versus improvements. While genuine repairs and maintenance on a rental property can often be claimed as a deduction immediately, deductions for capital works are claimed over time.

To be considered a repair, the work must relate directly to the wear and tear resulting from the property being rented out. This means repairs and maintenance to fix issues that existed at the time of purchasing the property are not immediately deductible. Also, where an entire structure is being replaced or where the works are considered improvements, this should not normally be considered a repair.

With the ATO recently stepping up its focus by commencing a data matching program on residential investment property loans, interest expenses will be a particular focus area for the ATO. The ATO is concerned that some taxpayers are not correctly apportioning interest deductions for loans where part of the loan is used or the loan was re-financed for a private purpose.

The ATO has also provided a reminder that there will be other situations where rental expenses may not be available in full. For example, when a holiday home is used both by the owner personally and as a rental property, there is a need to apportion deductions for rental expenses. Also, if a rental property is being rented to relatives at less than market rate, then the

ATO will generally only allow deductions for rental property expenses up to the amount of the assessable rental income.

More information
Get your rental right this tax time

Clarity on technology investment boost

Many practitioners have been recently turning their minds to the bonus 20% deduction that is available to some clients under the technology investment boost.

For a particular cost to qualify for the boost, one of the key conditions is that the expenditure needs to be spent wholly or substantially for the purpose of the client's digital operations or digitising their operations.

In many cases, the key challenge is working out whether the expenditure meets this condition.

While there are some examples of costs that might qualify in the explanatory materials accompanying the legislation and in the existing ATO fact sheet in this area, there are still significant areas of uncertainty.

Recognising the difficulty in this area, the ATO has released some additional guidance. Although the guidance does not provide a full or exhaustive list of eligible costs, it does make some comments on certain expenditure and confirms the following:

- An ongoing subscription to an accounting software platform for a client's business would be within scope of the boost; and
- A multifunction printer and scanner would not qualify if it was intended to be used only to make copies of paper copies, but it would be within the scope of the rules if used to scan paper documents for digital use and storage.

Outside of this, the ATO suggests that a good indicator of whether an expense is within scope of the boost is to consider whether the business would have incurred the expense if they didn't operate digitally.

The ATO also confirms that the expenditure does not need to be new to qualify. An ongoing and existing subscription can qualify for the technology boost if the subscription costs are incurred between 7:30pm AEDT 29 March 2022 and 30 June 2023, subject to the other conditions being met.

More information
Questions about the technology boost?

Steps to authorise and nominate agents expanding to more business clients

To improve the security of its online services, the ATO introduced additional steps requiring taxpayers to authorise and nominate their agents through 'Online services for business'.

These additional steps are relevant to taxpayers that are either:

- Appointing a new agent as their representative; or
- Providing an existing agent with authority for a new tax obligation.

Taxpayers that are maintaining their current arrangements with their existing agents should not be impacted.

Currently, these additional steps apply only to public and multinational businesses, certain businesses in the Top 500 privately-owned wealthy groups and government entities.

This is progressively being rolled out and expanded to other taxpayers. From 13 November 2023, the ATO intends that these additional steps will apply to all business taxpayers with an ABN, but excluding sole traders.

More information
We're expanding the client-to-agent linking process

Rulings, Determinations & Guidance

Self-education expenses for individuals

A new draft ruling TR 2023/D1 has been issued by the ATO which looks at when deductions for self-education expenses are available for individuals. The new ruling effectively replaces TR 92/8 and TR 98/9 which have now been withdrawn.

While there aren't any significant changes to the ATO's approach in this area, the ATO does provide more detailed and specific guidance in certain areas. Also, the ATO has updated its guidance to incorporate more recent court decisions.

The draft ruling provides more clarity by setting out factors to consider that can help determine when self-education expenses are deductible in certain scenarios. A good example of this is determining when overseas study tours have a sufficient connection with an individual's income earning-activities. This is often a challenging area to work through in practice.

Some of the key points from the ATO's draft ruling are summarised below:

- While this is not always the case, one of the key challenges in claiming deductions for self-development or personal development courses is that the knowledge or skills gained are often too general.
- If someone ceases their employment or income earning activity part-way through completing a course, the expenses would be deductible only when incurred up to the point when the income producing activity ceased.
- If a particular course is not entirely deductible, a deduction may still be available for some of the course fees where there are particular subjects or modules in that course that are sufficiently related to the individual's employment or income earning activities. The course fees may need to be apportioned.
- A distinction needs to be made for course fees relating to enrolment in a full fee-paying place versus a Commonwealth supported place. This is because course fees are not deductible if they relate to a Commonwealth supported place.
- The deductibility of course fees is not impacted by the individual borrowing money to pay for those fees. The ATO provides the example of a full-fee paying student using a FEE-HELP loan to pay for course fees. However, a deduction isn't available for repaying the principal amount borrowed or any indexation of the government loan.

More information
TR 2023/D1

Preventing deductions for holding costs relating to vacant land

TR 2023/3 is the ATO's finalised ruling on the provisions in section 26-102 ITAA97, which can sometimes prevent deductions from being claimed for holding costs relating to vacant land.

These provisions apply from 1 July 2019 and can operate to deny a deduction for losses or outgoings relating to holding land if there is no substantial and permanent structure in use or available for use on the land. These provisions can also prevent deductions from being claimed for holding costs when residential premises are being constructed or substantially renovated until both:

- The premises can be lawfully occupied (e.g., the occupancy certificate is issued); and
- The premises are actually used to earn rental income or they are genuinely available for rent.

There are some exclusions from the operation of these rules, such as where the land is used in carrying on a business by certain parties or if the taxpayer is a particular kind of entity (e.g., a company).

Consistent with the position taken in the draft ruling, one of the key points is that there is still a need to distinguish between expenses associated with holding land versus expenses associated with constructing a building or other structure on the land.

The ATO's view remains that interest expenses and borrowing costs associated with acquiring land, as well council rates, land tax and maintenance costs, fall within the scope of these provisions.

However, expenses associated with renovating or constructing a structure on land, including any interest or borrowing costs on loans used to fund such activities, are outside the scope of these provisions. The ATO has now further clarified that this extends to costs in relation to repairing structures.

For example, if a client borrows money to acquire vacant land and they take out an additional loan to finance the construction of a new rental property then section 26-102 will only apply to the interest expenses on the original loan which relates to the land.

While holding costs associated with a building fall outside the scope of these provisions, it is still necessary to ensure that the expenses can be claimed under the general deduction provisions or another provision of the tax law. TR 2004/4 provides guidance in this area.

In some limited respects, the ATO's final view is more favourable than the position taken in the draft ruling. For example, the ATO considers that if there are certain holding costs associated with land comprising of multiple titles, then for the purposes of determining whether there is a permanent and substantial structure, it is sufficient that such a structure exists somewhere on that area of land. This could apply to situations involving interest costs incurred on a loan to acquire a single block that has subsequently been subdivided into multiple titles.

However, there are some situations that aren't addressed in detail in the final ruling. For example, if a client undertakes relatively minor renovations to a rental property it isn't clear whether holding costs incurred in relation to the land while the property isn't rented or available for rent can be deducted. The ATO indicates in the ruling that a property will be considered available for use unless it has been deemed unsafe to occupy by a council, relevant body or relevantly qualified professional. However, the ruling contains an example suggesting that section 26-102 might impact on the deductions that can be claimed if the gap between tenants is 'brief'. Practitioners need to be careful when dealing with situations like this.

More information
TR 2023/3

Commissioner's discretion on the control rules for connected entities

TD 2023/5 sets out the ATO's final approach when it comes to the Commissioner exercising discretion to determine that an entity does not control another entity for the purposes of the connected entity rules. There are no substantial changes in the final determination compared to the draft determination.

The connected entity rules are mainly applied when calculating an entity's aggregated turnover. This calculation can be relevant in determining whether an entity has access to various concessions in the tax system such as the small business CGT concessions, the simplified depreciation rules and the technology investment boost.

As a starting point, an entity (the 'first' entity) will normally control another entity (the second entity) and they will be treated as connected entities if the first entity (together with its affiliates) holds at least 40% of the membership interests in the second entity.

However, where the control percentage is at least 40% but less than 50%, the Commissioner can potentially exercise discretion to determine that the first entity does not control the second entity. In order to exercise this discretion, the Commissioner must conclude that the second entity is controlled by a third entity or entities that do not include the first entity or its affiliates.

Control refers to matters typically associated with ownership of a business such as entitlements to income and capital, as well as decision making on key matters impacting the entity's constitution, funding, structure and management.

While the approach in the final determination remains largely unchanged, it is worth reiterating the key observations from the ATO in this area:

- A higher ownership percentage is an indicator of control by a third party. However, it is not always necessary for the other controlling entity identified by the Commissioner to have a formal control percentage interest of 40% or more under the 'normal' tests (for example, where the third party has been assigned voting rights in a legal agreement).
- Another party having sole or primary responsibility for the day-to-day management of the affairs of the second entity, while not irrelevant, does not of itself constitute control for the purposes of the Commissioner's discretion.
- It can be possible to show that an entity is controlled others by reference to a group. The ATO would generally expect to see that group has agreed to and does operate as a single controlling mind (for example, legal arrangements are entered into where the parties agree to act jointly in relation to the affairs of the entity).

Typically, the Commissioner's discretion would only become relevant in limited scenarios where the client (or their group) has a significant interest in a business entity (i.e., at least 40%) without a majority interest, but where it is possible to show that there is an unrelated party (or parties) that in fact controls the entity.

More information
TD 2023/5

Liability of executor to the deceased's tax obligations

The ATO has released some draft updates to PCG 2018/4 which is intended to provide certainty to the legal personal representative (LPR) of a deceased individual in terms of their personal liability for any outstanding tax obligations of the deceased individual.

When an individual dies, their LPR is generally responsible for ensuring that any outstanding tax obligations and liabilities are dealt with as part of the administration of the estate. In general terms, the LPR's liability to pay outstanding tax liabilities of a deceased person is limited to the value of the deceased's assets which form part of the estate. However, in some cases a LPR may have to meet liabilities personally if they distribute the assets of the estate with notice of a claim or potential claim by the ATO.

The guideline sets out the situations where the ATO will treat the LPR as having notice of a claim and when they will not be regarded as having such notice. However, the guideline only applies if certain conditions are met.

One of the conditions required that the total market value of the assets of the deceased estate at the date of the deceased person's death was less than $5 million, but the draft update has uplifted this threshold to $10 million.

The ATO has also included additional examples to provide greater certainty to LPRs seeking to rely on the guideline.

More information
PCG 2018/4DC1

Communications between objection officers and original decision makers

If taxpayers are dissatisfied with an original decision made by the ATO, one of the main options for dealing with this is to lodge an objection with the ATO. An objection involves a reconsideration of the original decision by an objection officer within the ATO.

While objection decisions should be made independently, the objection officer may contact the original decision maker to ensure they are fully informed in coming to their decision.

With that context in mind, the ATO has released PS LA 2023/2 which sets out a communication framework between objection officers and other ATO officers involved in making the original decision.

Some of the key points made in the practice statement are summarised below:

- Discussions between the objection officer and the original decision maker on any new information received in connection with the objection should generally involve how it would have been taken into account had it been available at the time of the original decision and whether that would have resulted in a different decision.
- The objection officer should advise the taxpayer of the general nature of any of their discussions with the original decision maker unless it is inappropriate to do so.
- The original decision maker has a responsibility to discuss the basis of their original decision with the objection officer while not attempting to influence the objection decision.

More information
PS LA 2023/2

Cases

Determining whether a worker is an employee when there is no written contract

Many practitioners would be aware that the High Court handed down some key decisions on the employee / contractor distinction which has impacted on the way issues in this area need to be approached.

To determine whether someone is an employee or contractor, the High Court confirmed it is necessary to focus on the terms of the written contract between the parties at the time it was entered into. In certain circumstances, regard can be given to the subsequent conduct of the parties to determine the terms of their agreement, including in situations where the parties have not entered into a comprehensive written contract.

This AAT case dealt with a worker who was engaged to design and sell kitchens, but there was no written agreement between the parties. In the absence of a written agreement, the AAT approached the issue by ascertaining the terms of the agreement with regard to the matters known to the parties at the time and by looking at how the worker and business subsequently conducted themselves.

The AAT concluded that the worker was an employee for superannuation guarantee under the ordinary meaning of the term, as well under the extended definition in section 12(3) of the *Superannuation Guarantee (Administration) Act 1992*. The following factors were relevant in reaching this conclusion:

- The business controlled the worker in many aspects of their role (e.g., who the worker would see, how pricing was quoted, permission to take time off, etc).
- The worker was required to represent himself as part of the payer's business.
- The worker was required to perform the work personally.
- The worker worked regular hours over set days, worked at the payer's place of business at times and seemingly was paid a fixed amount each week.

With some of the events transpiring almost ten years ago, one of the key issues was that the parties did not have a strong or consistent recollection of certain matters. This meant the AAT was required to make findings of certain facts.

This case highlights the difficulty in approaching this issue in practice when there is a lack of documentation around the rights and obligations of the parties. Clients should be encouraged to clearly document the key terms of any agreements reached with their workers, especially if they are taking the position that the worker is a genuine independent contractor.

More information
Trustee for the Kitchen Unit Trust and Commissioner of Taxation (Taxation) [2023] AATA 2831

Legislation

Parliament was in session between 4 and 14 September 2023.

Treasury Laws Amendment (Support for Small Business and Charities and Other Measures) Bill 2023

This Bill contains some previously announced measures from the Federal Budget in May as well as some additional measures.

$20k instant asset write off

With temporary full expensing having expired on 30 June 2023, the instant asset write-off threshold for small businesses was originally due to drop back to $1,000.

However, in line with the announcement in the May 2023 Federal Budget, the Bill introduces amendments which allow small business entities to claim an immediate deduction for eligible depreciating assets (or eligible improvements) costing less than $20,000 for the 2024 income year.

This applies only to small businesses with an aggregated annual turnover of less than $10 million where they have chosen to apply the simplified depreciation rules in the 2024 income year.

The $20,000 threshold also applies in determining whether the full balance of the general small business pool is written off in the 2024 year.

The 'lock out' rules that prevent small businesses from re-entering the simplified depreciation regime for five years if they opt out of the regime continue to be suspended until 30 June 2024.

Small business energy incentive

The Bill also introduces amendments for the small business incentive announced in the May 2023 Federal Budget.

In broad terms, the incentive allows businesses with aggregated annual turnover of less than $50 million to access a bonus deduction equal to 20% of the cost of eligible depreciating assets or improvements to existing depreciating assets that support electrification or more efficient energy use.

The maximum bonus deduction is $20,000 (i.e., up to $100,000 of qualifying expenditure).

To be eligible for the bonus deduction:

- The expenditure must be eligible for a deduction under another provision of the tax law; and
- The asset must be first used or installed ready for use, or the improvement cost incurred, between 1 July 2023 and 30 June 2024.

If a new depreciating asset is being acquired, the following additional conditions need to be satisfied:

- The asset must use electricity; and
    - There is a new reasonably comparable asset that uses a fossil fuel available in the market; or
    - It is more energy efficient than the asset it is replacing; or
    - If it is not a replacement, it is more energy efficient than a new reasonably comparable asset available in the market; or
- It is an energy storage, time-shifting or monitoring asset, or an asset that improves the energy efficiency of another asset.

If improvements are being made to an existing depreciating asset, the expenditure needs to satisfy at least one of the following conditions:

- It enables the asset to only use electricity, or energy that is generated from a renewable source, instead of a fossil fuel;
- It enables the asset to be more energy efficient, provided that asset only uses electricity, or energy generated from a renewable source; or
- It facilitates the storage, time-shifting or usage monitoring of electricity, or energy generated from a renewable source.

There are a range of exclusions from the bonus deduction, including expenditure on assets that can use fossil fuel, assets which have the sole or predominant purpose of generating electricity (e.g., solar panels), capital works, and motor vehicles. Financing costs, including interest and borrowing expenses, are also excluded.

Non-arm's length expenses

Following consultation on exposure draft legislation released in or around June 2023, the Bill also introduces amendments for rules around non-arm's length expenses for superannuation funds (excluding large APRA-regulated funds, exempt public sector superannuation funds, PSTs and ADFs).

The approach depends on whether the expense is either:

- A general expense – an expense that is not related to gaining or producing income from a particular asset of the fund; or
- A specific expense – any other expense.

General expenses

Currently where general expenses incurred by the superannuation fund are below market rates, any income derived by the fund could be deemed to be non-arm's length income and taxed at the top marginal tax rate.

Instead, the amendments propose that general non-arm's length expenses will result in a maximum of twice the difference between the amount that would have been expected at arm's length and the amount actually incurred being treated as NALI, with no deductions applying against that amount.

The total amount taxed at the highest marginal rate is then capped to no more than the income of the fund minus deductions, excluding assessable contributions and deductions against them.

General expenses most commonly include:

- Actuarial costs
- Accountant fees
- Auditor fees
- Administrative costs in managing the fund
- Trustee fees
- Costs of complying with the regulatory obligations of the fund
- Investment adviser fees, where those fees relate generally to the operation of the fund and not to a specific investment or a particular pool of investments

Specific expenses

For specific expenses, the existing treatment will continue to apply. The amount of income that will be taxed as NALI will be the amount of income derived from the 'scheme' in which the parties were not dealing at arm's length.

Specific expenses (related to gaining or producing income) could include:

- Maintenance expenses for a rental property
- Investment advice fees for a particular pool of investments
- A limited recourse borrowing arrangement for the purchase of a specific asset
- The purchase of an asset such as a rental property or shares
- An expense incurred in relation to gaining or producing income as a beneficiary of a trust through holding or acquiring a fixed entitlement to the income of a trust will always be a specific expense.

Date of application

The amendments are proposed to apply expenses incurred or expected to be incurred from 1 July 2018.

Other measures

The Bill also introduces the following other measures:

- Creating a new class of community charities consisting of community charity trusts and community charity corporations that can apply for deductible gift recipient (DGR) endorsement with the ATO.
- Adding the Justice Reform Initiative Limited and Transparency International Australia as listed DGRs and extending the period in which the Victorian Pride Centre Ltd and the Australian Sports Foundation Charitable Fund is a DGR.
- Broadly aligning the income tax treatment for general insurance with the new accounting standard AASB 17.

More information
[Treasury Laws Amendment (Support for Small Business and Charities and Other Measures) Bill 2023]

Treasury Laws Amendment (2023 Measures No. 3) Bill 2023

This Bill has passed through Parliament and received Royal Assent on 20 September 2023.

Education for financial advisers

The legislation contains a number of measures that may impact on financial advisers and their clients, including:

- Experienced financial advisers who have been authorised to provide personal advice to a retail client for a minimum of 10 years and have a clean disciplinary record, are not required to complete an approved qualification (i.e., at most eight units) by 1 January 2026 to meet the qualifications standard.
- Financial advisers who are also registered tax agents are not required to meet the additional education requirements to be a ‘qualified tax relevant provider’.

First home super saver scheme

The legislation also contains changes to the first home super saver (FHSS) scheme, including:

- Individuals being able to amend or revoke their FHSS applications provided a FHSS scheme amount has not already been paid to the individual.
- Individuals also having up to 90 days to request a release authority after they enter into a contract to purchase or construct a home (previously this was just 14 days).

More information
Treasury Laws Amendment (2023 Measures No. 3) Bill 2023