Coster Galgut
Chartered Accountants

TAX UPDATE – AUGUST 2024

What did I miss?

The new draft practical compliance guideline on the potential application of Part IVA to arrangements where personal services income is derived through a company or trust will create a stir.

We explore the issues and the impact of the new risk ratings.

Plus, the ATO's focus on the withholding tax obligations on payments to non-residents for interest, dividends or royalties. The ATO has issued a number of alerts specifically aimed at arrangements dealing with withholding tax.

And finally, the state of play for tax practitioners trying to work out the implications of the additional eight Code of Conduct changes.

Regards,
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From Government

Additional time for Code of Conduct reform compliance

The 8 additional tax practitioner Code of Conduct obligations introduced by *Tax Agent Services (Code of Professional Conduct) Determination 2024* were due to take effect from 1 August. Following lobbying by the professional bodies, the Assistant Treasurer announced transitional rules pushing the start date of the reforms to:

- 1 July 2025 for firms with 100 employees or less, and
- 1 January 2025 for larger firms with 101 employees or more.

In response to industry concerns, WA Liberal Party Senator Dean Smith moved to disallow the determination on 10 September 2024. We'll bring you more when we know the outcome.

And most recently, the Assistant Treasurer circulated the amended determination with the detail of the transitional rules. He also flagged that there will be consultation on the more contentious measures:

- False and misleading statements – which prohibits agents from making, preparing, permitting, or directing false or misleading statements to be made to the TPB, the Commissioner of Taxation, or other Government agencies.
- The requirement to keep clients informed of relevant matters -- which requires practitioners to advise clients if they are subject to, "any matter that could significantly influence a decision of a client to engage you, or to continue to engage you, to provide a tax agent service."

The transitional measures only apply to the additional Code obligations introduced by the legislative instrument. They do not apply to other legislated measures including:

- Breach reporting which came into effect on 1 July 2024, or
- The rules prohibiting partitioners from working with disqualified entities unless they have TPB approval to do so, which came into effect on 1 January 2024.

More information

- Albanese government lifts professional standards for tax practitioners
- Letter from the Assistant Treasurer

Data-matching property data and lifestyle assets

The ATO has initiated a data matching program, obtaining property management data from property management software companies for the 2018–19 income year through to 2025-26.

As part of the program, the ATO will receive:

- Property owner identification details (names, addresses, phone numbers, dates of birth, email addresses, business name and ABNs, if applicable)
- Property details (property address, date property first available for rent, property manager name and contact details, property manager ABN, property manager licence number, property owner or landlord bank details)
- Property transaction details (period start and end dates, transaction type, description and amounts, ingoings and outgoings, and rental property account balance).

This ramps up ATO's continued focus on landlords, with the ATO specifically targeting taxpayers with rental properties who fail to lodge rental property schedules when required, who omit or incorrectly report rental property income and deductions, and who omit or incorrectly report capital gains tax details.

Separately, the ATO will obtain lifestyle asset data from insurance providers for the 2023-24 income year through to 2025-26.

Under the program, the ATO will collect insurance policy data for certain classes of assets where the asset's value is above certain thresholds:

- Caravans and motorhomes - $65,000
- Motor vehicles including cars & trucks and motorcycles - $65,000
- Thoroughbred horses - $65,000
- Fine art - $100,000 per item
- Marine vessels - $100,000
- Aircraft - $150,000

The data will include detailed client identification information (names, addresses, phone numbers, dates of birth, Australian business number, email address) and policy details (insurance brand name, policy number, policy inception date, start date of current policy, end date of current policy, last date policy was updated, total value insured, purchase price of the property insured, registration or identification number of the property, vehicle details (year, make, model), finance, policy cost, description of the property insured, primary use type).

The ATO will use this data to focus on taxpayers accumulating or improving assets with insufficient income reported in their tax returns, taxpayers disposing of assets and not declaring the income and/or capital receipts, incorrect claiming of GST credits and omitted or incorrect reporting of FBT from taxpayers purchasing assets for personal use through their business entities.

More information

- Notifying the public of the data-matching program
- Property management data-matching program overview
- Commissioner of Taxation - Notice of a lifestyle assets data-matching program 26 August 2024

From the Regulators

Record-keeping for work-related expenses

The ATO has issued a reminder of the need to gather the retain appropriate records for work-related expenses this financial year - a key focus area for the ATO.

Records can be kept on paper, an electronic copy or a true and clear photo of an original record. Electronic records should be backed up regularly.

It is important to note that bank statements, on their own, are generally not a sufficient level of evidence to substantiate work-related expense expenses.

Taxpayers must keep records for 5 years from the lodgment date of the tax return.

Working from home expenses

With respect to working from home expenses, if the individual is using the fixed rate method (67c per hour), they need a record of the actual number of hours worked from home for the full financial year and at least one record for each of the additional running expenses incurred that the fixed rate includes (e.g., home and mobile internet or data expenses, mobile and home phone usage expenses etc.). This can be recorded through a diary, spreadsheet, rosters or timesheets and must be recorded contemporaneously.

If the individual is using the actual cost method, they will need to keep records for any additional running expenses incurred and details of depreciating assets they purchased, and how these are apportioned for their work-related use. The records also need to show the time worked from home for the year.

Car expenses

If an individual is able to claim deductions for car expenses and they are applying the logbook method, they need to keep a logbook that shows their actual work-related trips for a continuous period of at least 12 weeks that is representative of travel throughout the year. Each logbook is valid for up to 5 income years, subject to changes in circumstances.

The logbook needs to include:

- The destination and purpose of every journey,
- Odometer reading at the start and end of each journey
- Total kilometres travelled during the period
- Odometer readings for the start and end of the logbook period, and
- Odometer readings for the start and end of the income year you use the logbook.

Taxpayers also need to keep receipts for their car expenses.

If the individual is applying the cents per kilometre method they don't need to keep receipts of actual expenses incurred, but there is a requirement to keep a record of how the work-related kilometers have been calculated for the year. This could be done by using a diary or using the ATO myDeductions tool.

More information

- How do you store your record collection
- ATO record-keeping guide

Non-resident withholding tax obligations

The ATO is focusing on withholding tax obligations on payments to non-residents for interest, dividends or royalties.

If withholding tax obligations apply, taxpayers need to register with the ATO for PAYG withholding and will need to lodge a PAYG annual report or an annual investment income report.

When determining withholding obligations, it's important to recognise whether the client is a small, medium or large withholder, and any applicable tax treaties or withholding tax exemptions. For example, some tax treaties ensure that withholding tax doesn't apply to interest that is paid to an unrelated bank that is a resident of the relevant foreign country.

Australian residents who are required to pay withholding tax on interest or royalties won't normally be able to claim a deduction for these expenses until the appropriate withholding amount has been paid to the ATO.

The ATO has issued a number of alerts specifically aimed at arrangements dealing with withholding tax, including:

- Taxpayer Alert TA 2018/4 Accrual deductions and deferral or avoidance of withholding tax
- Taxpayer Alert TA 2020/3 Arrangements involving interposed offshore entities to avoid interest withholding tax
- Taxpayer Alert TA 2022/2 Treaty shopping arrangements to obtain reduced withholding tax rates

More information

- Our focus – withholding tax obligations on certain payments to non-residents

Self-review guides for GST treatment of food and health products

The ATO has issued two self-review checklists to assist with determining the GST classification of supplies relating to food and health products.

While the use of the guides is not mandatory, the checklists provide a practical set-by-step approach for clients to self-review the GST classification of their supplies and to assess the processes and controls that are in place.

For small to medium businesses, the ATO states that it is considered "better practice" to assess GST processes and controls annually, subject to the size and frequency of product turnover or changes, and any errors in GST classification.

Small business food retailers with turnover below $2m, can potentially use one of the simplified accounting methods for GST purposes.

More information

- Self-review checklist for small to medium business
- Self-review guide for medium to large business

Updated thin capitalisation guidance

The ATO has updated its website guidance to reflect the significant changes that apply to the thin capitalisation regime for the income years starting on or after 1 July 2023.

Under the changes implemented by the *Treasury Laws Amendment (Making Multinationals Pay Their Fair Share-Integrity and Transparency) Act 2024*, three new earnings-based tests were implemented:

- Fixed ratio test (which replaces the 'safe harbour test') - limits net debt deductions to 30% of earnings before interest, taxes, depreciation, and amortisation (**EBITDA**)
- Group ratio test (which replaces the 'worldwide gearing test') – allows debt deductions up to the same proportion of tax EBITDA as the worldwide group's net third party interest expense as a share of earnings
- Third-party debt test (which replaces the 'arm's length debt test) – limits debt deductions to qualifying external third party debt.

The amendments also provide a new integrity provision (also known as 'debt deduction creation rules') that will apply to debt creation schemes from income years starting 1 July 2024.

The updated guidance provides detailed guidance on key aspects of the new rules and is likely to be a valuable resource for clients (and their advisers) who have interest and other debt deductions of more than $2 million in the relevant income year and need to work through the thin capitalisation rules in detail to determine whether any debt deductions will be denied.

More information

- New thin capitalisation rules: web guidance available
- Thin capitalisation

Debt deduction creation rules for private businesses

In addition to the updated guidance on the thin capitalisation rules, the ATO has also issued guidance on how the new 'debt deduction creation rules' (**DCCR**) apply to private businesses and privately owned groups, including Division 7A loans. Importantly, the ATO has confirmed that entities in privately owned groups are not exempt from the operation of the DCCR, even where the loans are placed under complying Division 7A loan agreements.

A number of the exemptions that normally apply for thin capitalisation rules do not apply for the DCCR, such as the 90% Australian assets threshold exemption. Therefore, the DDCR can apply to domestically owned private groups that carry on business overseas (including through a permanent establishment) or have a controlling interest in any offshore entity (irrespective of size or turnover).

Broadly, where the conditions are met, the rules can operate to disallow debt deductions for certain related party arrangements. This includes debt deductions even where the arrangement is wholly domestic, as well as interest paid or payable under complying Division 7A loans where the loan has been used to acquire or fund certain related party arrangements. The DDCR also applies to arrangements entered prior to 1 July 2024 where the debt deductions continue to arise from the historical arrangements.

However, there are some important exceptions to the rules. First, the DDCR should not apply if the group has less than $2 million of debt deductions in the relevant income year. Also, the rules should not normally apply to groups that only operate in Australia and don't have any foreign owners.

More information

- Debt deduction creation rules and Division 7A

Rulings, Determinations & Guidance

Personal services businesses and Part IVA

The ATO has issued a draft practical compliance guideline on its approach to the potential application of the general anti-avoidance rules in Part IVA to arrangements where personal services income (**PSI**) is derived through a personal services entity (**PSE**) conducting a personal services business (**PSB**).

The guideline is relevant for taxpayers who are generating PSI through an interposed entity (e.g., company or trust) and the PSI attribution rules don't apply because the entity is able to pass the PSI tests so that it is classified as a PSB.

The ATO's long-standing position is that when a company or trust is used to generate PSI, the net profits relating to this activity should generally end up being taxed in the hands of the individual who is performing the work, even if the PSI tests can be passed. If any of the profits are distributed to other related parties or are retained in a company and this results in those profits being taxed at a lower rate, then there is a risk that Part IVA could apply to cancel the tax benefit.

The draft PCG sets out some specific indicators of arrangements that the ATO considers "low-risk" and "higher-risk", along with examples of such arrangements. For example, where the full PSI profit amount is paid to the individual who performed the work and is taxed at their own marginal rate, this arrangement would likely be low-risk and unlikely to be reviewed by the ATO.

The ATO indicates that arrangements can still be classified as low-risk where amounts are paid to related parties for administrative work performed in

the business, as long as the amounts paid are not excessive. The ATO also indicates that an arrangement could be low-risk where an amount is retained in a company so that specific business assets can be purchased by the company in the short-term.

Arrangements will be considered higher-risk where a tax benefit is obtained by the individual due to some of the net PSI profit being distributed to another entity, resulting in a lower overall tax rate being applied to this amount. The draft PCG also provides an example of a situation where the business is operated through a company with historical tax losses and the full net PSI profit for the current year isn't paid out to the individual, indicating that this would be a higher-risk scenario. These higher-risk arrangements are more likely to be received by the ATO.

It is important to note that an arrangement won't automatically trigger the application of Part IVA just because it is classified as a higher-risk scenario. The draft PCG is simply explaining scenarios that are more likely to be reviewed by the ATO on the basis that Part IVA is brought into question.

More information

- PCG 2024/D2

Guide to employee expenses updated

The ATO has updated its "Employees guide for work expenses" that aims to help employees determine if an expense is deductible, how to apportion expenses that aren't fully deductible, how to approach commonly claimed expenses, and to help employees understand the substantiation requirements for work expenses.

The guide has been updated to include further information on the electric vehicle home charging rate for electric vehicles with reference to the *PCG 2024/2 "Electric vehicle home charging rate – calculating electricity costs when a vehicle is charged at an employee's or individuals home"*. In the PCG, the ATO notes that individuals who meet certain conditions can claim deductions using the electric vehicle charging rate of 4.20 cents per kilometre.

The guidance has also been updated to include references to the ATO's updated ruling on the treatment of self-education expenses, *TR 2024/3 "Income tax: deductibility of self-education expenses incurred by an individual"*.

The guide also sets out a number of common myths surrounding work expense deductions and the ATO's guidance on how the rules actually work in these areas. This includes guidance on expenses relating to clothing, laundry, transport, gym fees, working from home and subscriptions.

More information

- Employees guide for work expenses

GST and sunscreen

Draft determination *GSTD 2024/D2 Goods and services tax: supplies of sunscreen* sets out the ATO's preliminary views on when a supply of sunscreen can be GST-free.

At a high-level, supplies of products that contain sunscreen are GST-free if the product has the following four attributes:

- It is a sunscreen preparation for dermal application
- It has a SPF of 15 or more
- It is required to be included in the Australian Register of Therapeutic Goods (ARTG) under the Therapeutic Goods Act 1989 (TGA), and
- It is marketed principally for use as a sunscreen.

Applying the rules in this area becomes more difficult in situations when it comes to supplies of 'multi-use' sunscreen products with additional features beyond being a sunscreen. The determination considers how to determine whether the product is marketed principally for use as a sunscreen. While there is no single determinative factor, the labelling and packaging of a product will be of particular importance to the formation of an overall impression of the product's marketed use.

Other factors for determining a product's primary use include the name of the product, product descriptions (e.g. 2-in-1), ordering and sizing of marketing content

on labels and packaging, how the product is promoted or advertised, the overall impression of the product based on marketing, product placement, etc.

The determination includes examples of sunscreen products that are also marketed as being anti-aging, moisturisers, colour correcting (**CC**) creams, tinted sunscreens and lip balms.

The draft Determination replaces the (now withdrawn) GSTII PH5 *What are 'sunscreen preparations for dermal application'?* and GSTII PH6 *When is a sunscreen preparation marketed principally as a sunscreen?* The ATO's view in the draft Determination is consistent with those in the issues register.

More information

- GSTD 2024/D2

Fine tuning promoter penalty laws

PS LA 2021/1 looks at the application of the promoter penalty laws in Division 290 of Schedule 1 to the *Taxation Administration Act 1953* and section 68B of the *Superannuation Industry (Supervision) Act 1993* (**SISA**). These laws were originally introduced to deter the promotion of tax exploitation schemes and have been updated recently to assist the ATO target promoters.

While the practice statement remains largely the same, the ATO has updated the existing indicators of promoter behaviour that might cause someone to be referred to the Promoters Program, including specific reference to schemes involving early access to superannuation. The ATO has also added an additional indicator for schemes claiming to conform with a public, private or oral ATO ruling, where there is a material difference between the scheme and the ATO ruling.

More information

- PS LA 2021/1

Draft excise determination for spirits

Excise (Concessional Spirits – Class of Persons) Determination 2024 specifies the maximum quantities of spirit that certain classes of persons can use for an industrial, manufacturing, scientific, medical, veterinary or educational purpose, without paying duty. The classes of persons covered are health care practitioners, veterinary practitioners, medical institutions, government-related entities and education institutions.

The Determination is proposed to commence from 1 January 2025. If implemented, this should reduce the compliance burden for affected entities that are currently required to make applications to the ATO for approval to use up to the specified quantity of spirit without paying duty.

The Determination will replace the current *Excise (Concessional spirits – class of persons) Determination 2014 (No.1)*.

More information

- LI 2024/D8
- LI 2024/D8 – Explanatory Statement

Cases

No remission of penalties even though taxpayer hadn't received a refund

In Bootlis v FC of T [2024] AATA 2723, the AAT affirmed the ATO's decision and denied a remission of administrative penalties imposed on a taxpayer who claimed deductions relating to a family trust that did not exist.

In 2022, without the knowledge of her tax agent, the taxpayer lodged amended tax returns online and claimed deductions of $60,766 for the 2020 income year and $75,782 for the 2021 income year in respect of a family trust that did not actually exist.

After an audit, the Commissioner issued a decision that denied the deductions in full and imposed a 50% base rate penalty in respect of the tax shortfall, because she had made a false or misleading statement in the amended tax returns.

The taxpayer objected to the penalties, with reasons including that she elected to not proceed with creating the family trust, she and her husband were experiencing financial difficulties due to Covid-19 and loss of employment, and in her view, the payment of income tax in Australia was voluntary.

The AAT found the applicant was 'reckless'. While the taxpayer's original claim was rejected before any refund was paid to her, this does not change the fact that she blatantly tried to obtain a deduction she wasn't entitled to. She did not seek her previous tax agent's advice before lodging the amended returns.

Having previously used tax agents to lodge the tax returns, she had not sought their advice about lodging the amended returns. Even if the trust did exist, the taxpayer had not advanced any basis upon which she would have been entitled to those deductions.

The AAT also held that it was open to the Commissioner not to remit the penalties. The fact that there is no harm to the revenue (as her claim was unsuccessful), or an incapacity to pay the penalty (e.g. she is on the pension and has a son at university), are not matters which would normally be considered in respect of considering whether to remit a penalty.

The AAT referred to *Dixon Holdsworth Superannuation Fund v Commissioner of Taxation* [2008] FCAFC 54 which states "*whether or not the Commissioner suffers financial detriment by reason of the fact that there is a shortfall amount has nothing to do with the imposition of administrative penalties or their remission*."

More information

- Bootlis v FC of T [2024] AATA 2723

$1.8 million penalty for unregistered tax agent

In Tax Practitioners Board v Van Dyke [2024] FCA 899, the Federal Court found that the respondent, Mr Van Dyke, performed tax agent services without being registered under the *Tax Agent Services Act 2009* (Cth) (**TASA**). The Court imposed a civil penalty of $1.8 million for contravening the Act.

Mr Van Dyke, who had never been a registered tax agent, prepared and lodged 3,359 income tax returns between 29 September 2019 and 11 July 2023 for a fee. He had falsely held himself out to be a registered tax agent. Over the period he obtained significant financial gain or $1,658,000 from his activities.

On his own tax returns, the respondent listed his main occupation as a 'Radio Traffic Controller' and did not report any of his income from the lodgment of the tax returns. He had received a cease-and-desist letter in September 2022 from the Tax Practitioner's Board, however, continued to engage in the conduct for months afterwards.

The Court emphasised the seriousness of the respondent's conduct in contravention of the TASA in determining an appropriate penalty.

More information

- Tax Practitioners Board v Van Dyke [2024] FCA 899

Legislation

Parliament sits on 9 to 12 September 2024.

Abolishing the AAT

The *Administrative Review Tribunal (Miscellaneous Measures) Bill 2024*, introduced into Parliament on 21 August, proposes establishing the Administrative Review Tribunal (**ART**) as a federal administrative review body, and abolishing the existing Administrative Appeals Tribunal (**AAT**).

The bill proposes to amend references to the 'AAT' in existing legislation, and forms part of a package of other legislation that establishes the ART in place of the AAT.

More information

- Administrative Review Tribunal (Miscellaneous Measures) Bill 2024

Superannuation on paid parental leave

The *Paid Parental Leave Amendment (Adding Superannuation for a More Secure Retirement) Bill 2024*, introduced into Parliament on 22 August 2024, adds superannuation contributions to paid parental leave under the Commonwealth-funded Paid Parental Leave Scheme for Parental Leave Pay (**PLP**). The intention is for the contributions to apply in connection with children born on or after 1 July 2025.

If enacted, eligible PLP recipients will receive the Paid Parental Leave Superannuation Contribution (**PPLSC**) as a lump sum payment after the end of each financial year, comprising:

- A core component, which will be calculated by multiplying the total amount of PLP paid for the person in an income year by the superannuation guarantee rate for that income year; and
- A nominal interest component to address the foregone returns resulting from the annual payment of the PPLSC.

More information

- Paid Parental Leave Amendment (Adding Superannuation for a More Secure Retirement) Bill 2024