TAX ROUND UP

November 2014

The key issues for accountants and advisers over the last month

Contents

There is plenty of reform being pushed through to avoid the Christmas hiatus including employee share schemes, more on non-resident withholding tax, and a tax excise increase by stealth.

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Read on!

Rae Ni Corraidh
Tax Adviser, Knowledge Shop

KNOWLEDGE SHOP

Coming up! Just click on the picture for details…

Brisbane 6 Nov

Sydney 19 Nov, **Brisbane** 21 Nov
Perth 27 Nov, **Melbourne** 1 Dec

Sydney 19 Nov, **Brisbane** 21 Nov
Perth 27 Nov, **Melbourne** 1 Dec

From Government

Reforming tax treatment of Employee Share Schemes

The joint media release on 14 October 2014 provides some hope for those seeking reform of the tax treatment of Employee Share Schemes (ESS). While there is no draft legislation issued at this stage, initial indications are that the proposed reforms will take into consideration many of the concerns raised by start-up companies and their advisers.

The Government's announcement proposes a number of changes to the rules, including:

- Special concessions targeted at shares issued by eligible start-up companies - those with turnover not exceeding $50m, unlisted, and incorporated for less than 10 years;
- Employees of eligible start-up companies can potentially defer tax until the underlying shares are sold, with the entire amount taxed under the CGT rules;
- Employees who are issued with options under a deferred tax scheme will be able to defer the tax until the options are exercised (rather than when the options are received); and
- The maximum time period for deferring the taxing point will be extended from 7 years to 15 years.

While we are not fans of tax change by media release rather than legislation, the announcement recognises the restrictions of the current rules on many companies and seeks to do something about it.

The new rules are intended to apply to shares or options provided from 1 July 2015.

More information

- Encouraging employee share ownership and entrepreneurship

Sales of Australian property by non-residents

A Treasury discussion paper released on 31 October explores how the 10% non- final withholding tax will apply to the disposal by foreign residents of taxable Australian property. The measure will not apply to residential property transactions under $2.5 million or to disposals by Australian residents.

Under the measure, the payer in a transaction will have an obligation to withhold 10% of the proceeds payable in relation to the transaction where: the payee is a foreign resident; and, the transaction involves an asset that is 'taxable Australian property'.

The measure was announced by the previous Government in the 2013/2014 Budget and adopted by the current Government. It is intended to apply from 1 July 2016.

More information

- Non-final withholding tax on transactions involving taxable Australian property

Excess non-concessional contributions tax reform

Treasury exposure draft legislation released on 10 October gives effect to the Budget measure that allows individuals the option of withdrawing superannuation contributions in excess of the non-concessional contributions cap made from 1 July 2013 and associated earnings, with these earnings to be taxed at the individual's marginal tax rate.

Key proposals include:

- Applies to excess non-concessional contributions made in the 2013/14 financial year and later years.
- The member can elect to have the excess amount, together with any associated earnings, released from the fund. The earnings will be calculated from 1 July of the financial year of contribution up until the day the Commissioner makes his determination.
- The payment (refund) from the fund will be treated as a lump sum super payment and will be non-assessable non-exempt (NANE) income. However, the associated earnings component of the payment would be included in the individual's assessable income.
- The earnings will be calculated using an average of the General Interest Charge (GIC) rate for each quarter of the financial year. The interest will compound on a daily basis. For the 2014 year, the rate would average out to be 9.66% and the daily rate would therefore be 0.02646565%.
- Where the excess contributions are released from the fund, excess non-concessional contributions tax will not be imposed.
- If only part of the excess contributions are released then excess contributions tax will apply to the balance remaining in the fund(s).
- Excess non-concessional contributions tax will also not be imposed where the members remaining superannuation interest is nil – for instance where the member has withdrawn all their super benefits. However, the full amount of the associated earnings will still be included as assessable income for the individual.
- Excess non-concessional contributions tax will be imposed on amounts that are not released from the fund.
- The current method for working out non-concessional contribution caps will still apply.
- The commissioner will still have the discretion to disregard or re-allocate non-concessional contributions and excess contributions tax will not be imposed on amounts that are disregarded.

More information

- See [Reforming the superannuation excess non-concessional contributions tax]

GST rate increase debate

A speech by Prime Minister Abbott in Tenterfield sparked a media frenzy over whether the Government is seeking to increase the rate of GST. In the speech, Mr Abbott said “Might the states be prepared to accept responsibility for broadening the indirect tax base; might they be prepared to surrender some of their responsibilities to the Commonwealth; might there be new funding formulas that wouldn’t solve the blame game but could at least give it a new and more realistic starting point?”

In Question Time the next day, the Prime Minister said, “Obviously, if we are going to have a mature debate about our federation, we need to look at spending responsibilities and at revenue capacities…. the GST is a matter for the states but certainly it is something which ought to be looked at as part of the federation reform process and as part of the tax reform process.”

The commentary comes ahead of the promised Tax Reform White Paper.

More information

- Speech: Sir Henry Parkes Commemorative Dinner
- Question time 26 October 2014

Excise change by stealth

From 10 November 2014, fuel excise will increase to 38.6 cents (up from 38.143 cents) with further increases in biannual indexation on 1 February 2015 and 1 August 2015.

The excise indexation increase was originally announced in the Federal Budget but the amending legislation giving effect to the increase has not passed parliament.

Instead, the Government used ‘tariff proposals’ that need to be validated by parliament within 12 months. If parliament does not validate the measures, the excise will need to be refunded to fuel manufacturers and fuel importers.

The Government will need to legislate to ensure there is no negative financial impact on those utilising the fuel tax credit scheme, the Clean Fuels Grant Scheme and the Ethanol Production Grants Scheme.

More information

- Press conference transcript 28 October 2014

From the ATO

Company loss carryback

The ATO has advised that following the repeal of the company loss carry back measures (see *Minerals Resource Rent Tax Repeal and Other Measures Bill 2014*), any 2013/2014 company tax returns lodged with completed loss carry-back labels will not lodge and the tax agent that lodged them will receive an error message to remove the amount from the tax return.

If the company’s 2013/2014 tax return has already been processed claiming a loss, the ATO will write to the taxpayer advising that it will amend their assessment. Where there is a resulting tax balance due, and the company pays the tax by the due date, no interest or penalties will apply.

More information

- Company loss carry back legislation repealed

Rulings, IDs & determinations

GST Motor vehicle incentive payments

GSTR 2014/1: Goods and services tax: motor vehicle incentive payments

This ruling outlines the GST implications of incentive payments made by motor vehicle manufacturers, importers and distributors to motor vehicle dealers, and also covers situations where the manufacturer may provide an incentive payment or rebate to the dealer’s customer.

Broadly, if the incentive payment is third party consideration for a supply made by a dealer to its customers, the dealer is liable for GST on the total consideration (including the manufacturer's incentive payment) and the dealer would not have an increasing adjustment.

The customer's entitlement to input tax credits is less than the GST payable by the dealer, as even if the motor vehicle is a fully creditable acquisition by that customer, that customer is liable to provide only some of the consideration for the purchase, since the rest of the consideration is being paid by the manufacturer.

This ruling was previously released in draft form as GSTR 2014/D1 in April 2014.

In addition to providing more worked examples than the draft ruling, the final ruling is split into two parts, with Part A covering general comments regarding the GST consequences of the incentive payments, and Part B covering information requirements for third party adjustment notes issued by manufactures to dealers.

More information

- GSTR 2014/1

Delivery drivers - contractors or employees?

ATO ID 2014/28: Superannuation Guarantee Status of the Worker – Pizza delivery drivers as employees

This ATO ID outlines the scenario of pizza delivery drivers who are required to provide and maintain their own motor vehicles in order to perform their deliveries. In this case the workers were required to sign an "Independent Contract Driver Agreement" for a fixed rate per delivery and were provided with a delivery instruction booklet. On the job training was provided to the drivers and they were rostered to work in shifts. The drivers were required to have an ABN and issue invoices. They were not obliged to accept work or to work exclusively for the business.

The key issue was whether the delivery drivers were employees for superannuation guarantee purposes.

The Commissioner confirms that the drivers would be treated as employees in this situation. One of the main reasons is that the items being delivered (i.e., the pizzas) are the core business of the employer, which indicates that the drivers are integrated into the business of the employer.

In this case, the Commissioner is of the view that these drivers would be employees under the ordinary meaning of employee set out in the superannuation legislation. The fact that they are using their own vehicles is not a significant factor – they are still employees and the employer would be required to make superannuation contributions on their behalf.

This appears to be a reasonable conclusion, and if the scenario outlined in this ATO ID is compared with the long established principles set out in Vabu's case (*Vabu Pty Limited v. Federal Commissioner of Taxation* (1996) 96 ATC 4898; (1996) 33 ATR 537) a clear distinction is apparent, being that the couriers were not integrated into Vabu's business, however the pizza delivery drivers were essential to the business of making and delivering pizzas.

More information

- ATO ID 2014/28

Subcontractor could result in permanent establishment

ATO ID 2014/29: Income tax – Assessable income of a non-resident subcontracting activities to an Australian resident

This ATO ID explores whether a foreign taxpayer subcontracting work to an Australian resident entity, could result in that foreign taxpayer having a permanent establishment (PE) in Australia for the purposes of the relevant double taxation agreement (DTA).

In the scenario outlined in the ID, a Japanese company entered into a contract to undertake a construction or installation project in Australia that would last for more than 12 months. In broad terms, the Japanese company then enters into a subcontract agreement with an Australian entity to undertake the construction or installation work in Australia. The issue was whether the Japanese company would still be treated as having a PE in Australia if the construction and installation work was actually being performed by another Australian entity.

In this case the ATO found that the Japanese company did have a PE in Australia. This meant that the profits attributable to that PE could be taxed in Australia. The ATO concluded that the company had a PE in Australia because it was considered to have carried on the activities that were performed by the subcontractor which meant that the Japanese company was deemed to have spent more than 12 months on the construction or installation project in Australia.

The ATO also concluded that the Japanese company would have a PE in Australia on the basis that it carried out supervisory activities in connection with the construction or installation project in Australia.

While many of the DTAs that Australia has entered into with other countries are similar, it is important to remember that there can be subtle differences between each DTA which can lead to very different tax outcomes. Careful review is important to get it right.

More information

- ATO ID 2014/29

SG for deceased employee

ATO ID 2014/31: Superannuation – payment of salary and wages after the death of an employee to the deceased estate

This ATO ID confirms that an employer's superannuation guarantee (SG) obligation extends to payments of salary and wages that accrued prior to the date of death of the relevant employee. That is, the SG system applies to former employees, even when that employee has died by the time a SG contribution would have been required to be made.

It is a good reminder for an employer to confirm that they have dealt with all their employer obligations in relation to a deceased employee. While certain accrued and unpaid employee entitlements (e.g. salary and wages, bonus entitlements and leave payments) might end up being paid to the executor of a deceased estate, employers should remember that SG obligations may arise if any of those entitlements represent ordinary time earnings.

More information

- ATO ID 2014/31

Cases

On the wrong side of the CGT concession calculations

Scanlon and Commissioner of Taxation [2014] AATA 725

Several issues were raised in this case that highlight how complex it can be to apply the small business CGT concessions in practice and the disastrous consequences for clients when it all goes wrong.

In this case, the taxpayers negotiated an agreement to sell their business, accepted an initial offer and signed a letter of offer, then proceeded to execute a share purchase agreement. Employment termination payments (ETPs) were made to certain employees at the time of the transaction.

For the calculation of the maximum net asset test, the ETPs reduced the net value of the company's assets under the $5m net asset value test (now $6m).

The key issues were:

- Whether the CGT event occurred to the shares in the company at the time the taxpayers signed a share purchase agreement or at an earlier time when they accepted an initial offer from the purchaser.
- Whether ETPs to be paid by the company were a liability of the company at the time that the CGT event occurred.
- If the ETPs were a liability of the company, whether they related to the CGT assets of the company.
- Whether the right to those ETPs, if any, should have been included in the value of the taxpayers' assets.
- Whether those ETPs should have been included as capital proceeds for the disposal of the shares for CGT purposes.

The AAT affirmed the Commissioner's objection decision denying the taxpayers access to the small business CGT concessions on the basis that the taxpayers did not satisfy the maximum net asset value test.

The AAT held that CGT event A1 occurred at the time that the taxpayers signed the letter of offer (i.e. the earlier date) rather than when the share purchase agreement was executed. Even though the letter stated that it was subject to conditions, it did set out the terms of the sale that had already been negotiated. The AAT held that these 'subject to' conditions only impacted on the performance of the contract rather than its formation.

The Tribunal also found that the company had no liability to pay the ETPs at the time the CGT event was triggered. Even if the liability to pay the ETPs was triggered before the CGT event, the Tribunal found that the liability did not relate to the CGT assets of the company, which meant that they could not be used to reduce the net value of the company's assets under the $5m net asset value test in effect at that time.

Interestingly, the AAT also held that the ETPs simply formed part of the capital proceeds from the sale of the shares in the company (although any impact on the CGT calculation should be reduced to the extent that the ETPs are included in the assessable income of the taxpayer already).

The AAT concluded that the taxpayers did not satisfy the maximum net asset value test. In addition, it also upheld the Commissioner's imposition of penalties for failure to take reasonable care.

All or nothing penalty on late SGC payment

The Trustee for Rane Haulage Trust and Commissioner of Taxation [2014] AATA 733

As you know, if an employer fails to pay their superannuation guarantee contribution obligations by the 28th day following the end of the quarter, the employer must lodge a Superannuation Guarantee Statement to report their late superannuation contribution obligations and the related charges, commonly referred to as the Superannuation Guarantee Charge (SGC). This is the sum of the superannuation contributions, plus the nominal interest component (calculated from the **start of the relevant quarter**, regardless of whether that individual is employed at the start of the quarter or not) plus the administration component.

In this case, the AAT upheld the Commissioner's objection decisions relating to the taxpayer's objection to their SGC assessments following an ATO audit.

The SGC should have been paid to the ATO by the time they lodged the SG statement.

The taxpayer disputed the nominal interest component of the SGC, which is calculated with reference to the date of the lodgement of the superannuation guaranty statement, not the date of payment of any superannuation contribution to an employee's superannuation fund.

The taxpayer believed this was unfair and wanted the Commissioner to amend the assessments to reduce the nominal interest component to represent the period they were late not the entire period from the start of the relevant quarter.

The AAT concluded that the method of calculating the nominal interest component was clearly stated in the legislation, and that the amounts assessed by the Commissioner were valid. As such, the Commissioner has no capacity to reduce the nominal interest component below the start of the relevant quarter.

Penalties for directors of corporate trustee of superannuation fund

Deputy Commissioner of Taxation (Superannuation) v Graham Family Superannuation Pty Ltd [2014] FCA 1101

The Federal Court imposed penalties totalling $40,000 on directors of the corporate trustee of their family superannuation fund.

The directors had caused the trustee company to make unauthorised loans to themselves as members of the family superannuation fund, in contravention of the SIS Act, in addition to leasing residential property owned by the superannuation fund to their son, and did not collect rent in accordance with the terms of the lease, leading to further contraventions.

The directors did not dispute the contraventions and agreed with the level of penalties.

While the Commissioner did not declare the superannuation fund to be non-complying, both directors were disqualified from acting as a trustee, investment manager or custodian of a superannuation entity.

Profits included in assessable income

[Kirkby and Commissioner of Taxation [2014] AATA 759]

In this case the Commissioner had amended the taxpayer's assessment to include a profit on the sale of mining tenements. The taxpayer objected on the grounds that he did not receive any of the proceeds, which were paid to a company associated with him or one of his co-owners.

The Commissioner disallowed the objection on the basis that the taxpayer's share of the proceeds of the sale was income according to ordinary concepts, and he had derived it as he had directed the payment to be made in a specific manner. The Commissioner's view was that it did not matter that the proceeds were not paid directly to the taxpayer, it was sufficient that they were paid as he directed.

The AAT agreed with the Commissioner's approach and confirmed that the taxpayer had derived the income for tax purposes, even though he may not have physically have received the proceeds. It was sufficient that he directed where the proceeds should be paid.

The Court also noted that a "transfer sale agreement" which the taxpayer relied upon, but which did not include any amount of consideration "was obviously drawn up without the benefit of legal advice" and was not a valid transfer document.

This may be a point to remember when a taxpayer wishes to undertake a more informal approach to a transaction with a related entity.

Legislation

Thin capitalisation changes now law

[Tax and Superannuation Laws Amendment (2014 Measures No. 4) Bill 2014]

The changes to the thin capitalisation provisions covered in last month's Tax Round Up are now law, having received Royal Assent on 16 October 2014. The changes apply from 1 July 2014.

In addition, this legislation also reforms the exemption for certain dividends received from foreign companies as contained in section 23AJ ITAA 1936.

In broad terms, section 23AJ provides that dividends paid by a foreign company to an Australian company are non-assessable non-exempt income if the Australian company holds at least 10% of the foreign company. The new rules result in section 23AJ being replaced by Subdivision 768-A ITAA 1997. The main change is that the exemption can apply when an Australian company received the dividends indirectly, for example, through a trust.

Increase in pension age to 70

[Social Services and Other Legislation Amendment (2014 Budget Measures No. 5) Bill 2014]

This Bill seeks to bring into effect many of the Budget announcements including:

- Increase the age pension qualifying age, and the non-veteran pension age, from 67 to 70 years by six months every two years, commencing on 1 July 2025

- Pause indexation of income test free areas for pensions (other than parenting payment single) and deeming thresholds for three years from 1 July 2017;
- Index pensions (other than parenting payment single) to the Consumer Price Index from 20 September 2017
- Reduce social security and veterans' entitlements income test deeming thresholds from 20 September 2017

Excise changes and other amendments

Tax and Superannuation Laws Amendment (2014 Measures No. 6) Bill 2014

- Schedules 4 and 5 to this Bill amend the Fuel Tax Act 2006 and the Energy Grants (Cleaner Fuels) Scheme Regulations 2004. Schedules 4 and 5 ensure that changes to the amount of excise and excise-equivalent customs duty payable by taxpayers as a result of any tariff proposals tabled in the House of Representatives are taken into account in calculating fuel tax credits and the cleaner fuels grant for biodiesel and renewable diesel. Therefore upon Royal Assent to this Bill, fuel tax credit and grant claimants are able to claim the higher rate of fuel tax credits and grant amounts as a result of the Excise Tariff Proposal (No. 1) 2014 and the Customs Tariff Proposal (No. 1) 2014 tabled in the House of Representatives.
- Schedule 1 amends ITAA 1997 to extend the existing business restructure roll-overs available where a member of a company or unitholder in a unit trust can defer the income tax consequences of transactions that occur in the course of a business restructure.
In particular, the amendments permit taxpayers to apply the roll-overs in circumstances where they held the relevant shares or units as revenue assets or trading stock. The amendments also consolidate the separate but effectively identical business restructure roll-overs for shares and units in a unit trust into a single set of provisions.
- Schedule 2 enables foreign pension funds to access the managed investment trust (MIT) withholding tax regime and the associated lower rate of withholding tax on income from certain Australian investments.

Export funding opportunities expanded

Export Finance and Insurance Corporation Amendment (Direct Lending and Other Measures) Bill 2014

This Bill expands EFIC's powers to allow direct lending for export transactions involving all goods, not just capital goods, and provides for competitive neutrality principles to apply to EFIC's operations.

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