T.H. White Newsletter - August 2023

Welcome to T.H. White's newsletter, your monthly tax and super update keeping you up to date on current issues, news and changes you need to know. Should you require further information on any of the topics covered, please do not hesitate to contact us.

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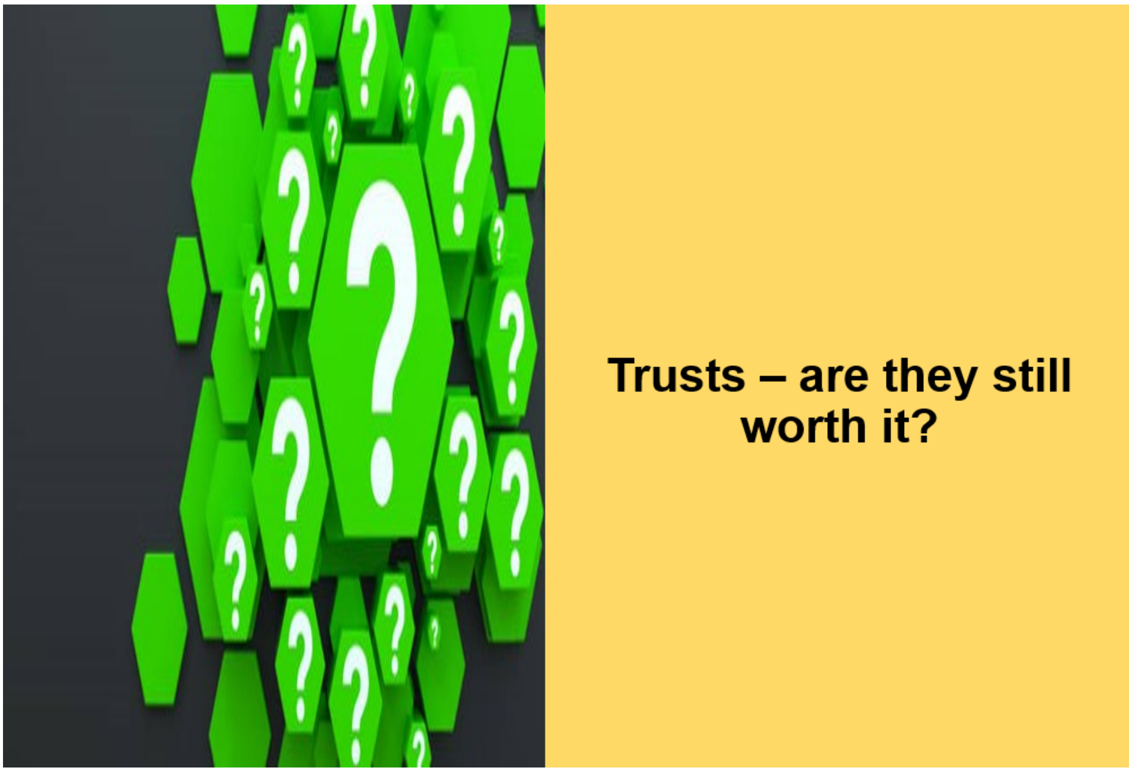


The recent ATO crackdown on trusts will no doubt have some business owners (and even some advisors) asking themselves the question: Is this structure for business purposes still worth it?

To recap, trust distributions have been under the ATO microscope in recent years. The latest ATO crackdown was in February 2022 when it updated its guidance around trust distributions especially those made to adult children, corporate beneficiaries and entities that are carrying losses.

Depending on the structure of these arrangements, the ATO may potentially take an unfavourable view on what were previously understood to be legitimate distribution

Act, specifically, where trust distributions are made to a low-rate tax beneficiary, but the real benefit of the distribution is transferred or paid to another beneficiary usually with a higher tax rate. In this regard, the ATO’s Taxpayer Alert (TA 2022/1) illustrates how section 100A can apply to the quite common scenario where a parent benefits from a trust distribution to their adult children.

Despite this new ATO interpretation and the wider crackdown on trusts in recent years, the choice of a trust as a business structure still has a range of benefits including:

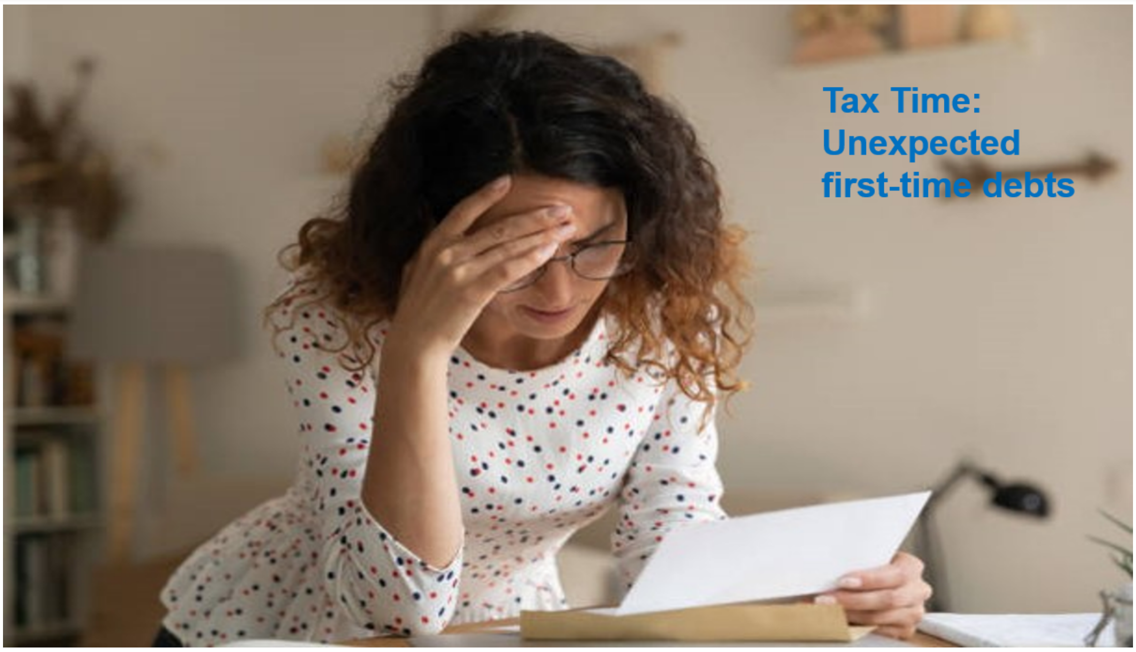
- ***Asset protection –*** limited liability is possible if a corporate trustee is appointed. Usually, when a person owes money and cannot meet the repayment requirements, the creditor can access the person’s personal assets to recoup the debt payable. However, if a trust is in place, there is no access to beneficiary assets

- ***50% CGT discount –*** A family trust receives a 50% discount on capital gains tax for profits made from selling any assets the trust has held for more than 12 months. This contrasts with a company structure. Companies cannot access the 50% CGT discount.

- ***Tax planning –*** Income that sits in the family trust that is not distributed by year-end is taxed at the highest income tax rate. However, any trust income distributed to the beneficiaries is taxed at the income tax rate of the beneficiary who receives the distribution. The way to definitely get around the ATO’s aforementioned section 100A crackdown is to ensure the distributed money actually goes to the nominated beneficiary and is enjoyed by the beneficiary rather than another taxpayer.

- ***Carry-forward losses –*** A trust does not distribute losses to beneficiaries. This means the beneficiaries will not be called upon to contribute money to the trust to meet any loss. Instead, losses from each year can be carried forward to the following year, subject to certain conditions being met.

If you have questions around your trust structure, or your business structure more generally, touch base with us.



For the first time, many Australians are finding themselves in a position where they are being told they owe the ATO money after completing their tax return this year.

A significant number of taxpayers in this position are those that are still paying off their HECS/HELP debts – many of them young Australians. Following are some myths and facts around why this may be the case.

We also tackle the LMITO myth.

When PAYGW is deducted from salaries and wages to take account of HELP liabilities, the withheld amount is not applied against the HELP debt until after the end of the income year, when the tax return is lodged. This means that indexation is applied to the debt without taking into account any PAYGW withheld during the year.

Fact or myth?

This is a myth.

Indexation only affects the loan balance, it doesn't affect the amount of the year-end tax liability.

Where an employee has salary sacrificed, the lower salary will reduce the PAYGW *used to determine liability to HELP repayments.*

This is not likely to be understood or expected by affected taxpayers.

Fact or myth?

This is a fact.

HELP repayment income is the total sum of the following amounts from a person's income tax return for the income year:

- **total net investment loss**
- **reportable fringe benefits (as reported on their payment summary)**
- **total net investment loss (which includes net rental losses)**
- **reportable super contributions (including salary sacrificed contributions); and**
- **any exempt foreign employment income amounts**

Negative gearing amounts are added back and included in HELP repayment income. The rapid rise in interest rates will flow through to negative gearing amounts which increase the repayment income.

This is not likely to be understood by affected taxpayers and will have caught them off-guard.

Fact or myth?

This is a fact.

However, this will only affect those engaged in negative gearing which may not be many young Australians with a HELP debt.

The high indexation applied to HELP debts this year of 7.1% compared to prior years (3.9% in 2022 and 0.6% in 2021) has caught taxpayers off-guard. Prior to 2022, over the last 10 years, the rate had not exceeded 2.6% and was often around 2%.

Fact or myth?

This is a myth.

Again, indexation only affects the loan balance, it doesn't affect the amount of the year-end tax liability.

The end of LMITO after 2021/22 is only just being realised by taxpayers now, despite two years of talking about this. The message did not get through, or the impact was not fully understood.

Fact or myth?

This is a myth.

For employees, the PAYGW rates were increased to take the LMITO abolition into account, so yes no refund, but there shouldn't be tax payable as a result of just the LMITO ending.

ATO Tax Time focus areas

key focus areas for 2022-23 Tax Time – rental property deductions, work-related expenses, and capital gains tax (CGT). To maximise your claims in this area and protect yourself from ATO audits and adjustments, be sure to keep the appropriate records.

Work-related expenses

This year the ATO is particularly focused on ensuring taxpayers understand the changes to the working from home methods and are able to back up their claims. To claim your working from home expenses as a deduction, you can use the actual cost method, or the revised fixed rate method, provided you meet the eligibility and record-keeping requirements as follows:

RECORD-KEEPING - REVISED FIXED RATE METHOD	RECORD-KEEPING - ACTUAL COST METHOD
• A record of all the hours you work from home for the entire year (e.g. a timesheet, roster, diary or similar document)	• You will need to keep a record for every expense you claim
• Evidence you paid for the expenses covered by the revised fixed rate method (for example, if you use your phone and electricity when you work from home, keep one bill for each of these expenses)	• Receipts, bills or invoices which show the supplier, amount of the expense, nature of the goods, date it was paid and the date of the document
• Records for items you claim as a separate deduction	• Evidence of your personal and work-related use of the items or services you buy and use
• From 1 July 2022 to 28 February 2023, the ATO will accept a record which represents the total number	• You can work out your work-related expenses using records for the entire year or over a four-week period that represents your work

example, a four-week diary).	itemised bill
• From 1 March 2023, a contemporaneous record of all the hours you worked from home is required (e.g. a timesheet)	

In relation to depreciating of assets and equipment you will need records that show:

- when and where you bought the item and its cost
- when you started using the item for a work-related purpose
- how you work out your percentage of work-related use, such as a diary that shows the purpose of and use of the item for work.

Chat to us if you have any questions around which method to use and the records to keep.

CGT

Capital gains tax (CGT) comes into effect when you dispose of assets such as shares, crypto, managed investments or properties. Inform us as your accountant if you have disposed of such assets between1 July 2022 to 30 June 2023.

On the disclosure front, be mindful that the ATO has extensive data-matching capabilities and, as such, will likely be able to detect the sale of most CGT assets.

Rental property deductions

Many landlords will expect large amounts of deductions to be claimed when their returns are lodged. However, your record keeping will significantly impact the deductions that can be claimed. Talk with us around the record keeping requirements if you are unsure.

Keep records of the following:

rental/commercial property

- loan documents
- land tax assessments
- documents or receipts that show amounts you paid for:
    - advertising (including efforts to rent out the property)
    - bank charges
    - council rates
    - gardening
    - property agent fees
    - repairs or maintenance etc
- documents showing details of expenses related to:
    - the decline in value of depreciating assets
    - any capital work expenses, such as structural improvements
- before and after photos for any capital works
- travel expenses documents, if you are eligible to claim travel and car expenses such
  as:
    - travel diary or similar that shows the nature of the activities, dates, places, times and duration of your activities and travel (you must have this if you travel away from home for six nights or more)
    - receipts for flights, fuel, accommodation, meals and other expenses while travelling
    - receipts for items you used for repairs and maintenance that you paid for when you travel to, or stayed near, the rental property.
- documents that show periods of personal use by you or your friends
- document that show periods the property is used as your main residence
- loan documents if you refinance your property
- documents, receipts and before and after photos for capital improvements
- tenant leases
- when you sell a property:
    - contract of sale
    - conveyancing documents

This year, the ATO is particularly focused on interest expenses and ensuring rental property owners understand how to correctly apportion loan interest expenses where part of the loan was used for private purposes (or the loan was re-financed with some private purpose).

Read More

Gifting to employees

Some employers, especially at Christmas time or for birthdays, give small gifts to their employees or the employee's associates (i.e. spouses). These gifts typically take the form of bottles of wine, movie tickets, gift vouchers etc. The tax treatment of these gifts from an employer standpoint, depends upon a range of factors including:

- To whom the gifts are provided (e.g. employees or clients?)
- Whether the gifts constitute entertainment
- The dollar value of the gifts, and
- The frequency with which they are provided.

Use the following steps as a guide:

1. Does the gift constitute entertainment?

- If yes, go to 2

(gifts that constitute entertainment include: tickets to the movies/plays/theatre, restaurant meals, holiday airline tickets, admission tickets to amusement parks etc.)

(gifts that do not constitute entertainment include: Christmas hampers, bottles of alcohol, gift vouchers, perfume, flowers, pen sets)

2. Does it cost less than $300 (GST-inclusive) and is provided infrequently?

- If yes…no FBT, no deduction, no GST credit
- If no…FBT applies, is deductible and can claim any GST
-

3. Does it cost less than $300 (GST-inclusive) and is provided infrequently?

- If yes…no FBT, deduction can be claimed as can any GST credits
- If no…FBT applies, deduction can be claimed as can any GST credits

All told, from a tax standpoint it's best to buy employees and their associates non-entertainment gifts that cost less than $300. That way, no FBT is payable yet a deduction and GST credits can be claimed. Alternatively, you can put the tax burden back on the employee and pay them a cash bonus, in which case the amount will be assessable to the employee, and deductible to the employer.

Touch base with us if you require further clarification.

SMSF trustees with limited recourse borrowing arrangements (LRBAs) are now feeling the impact of 10 interest rate rises since May 2022 in one hit, from July 2023.

SMSF trustees relying on the ATO's safe harbour terms to ensure that an LRBA remains, at all times, at arm's length will face an increase in monthly repayments of interest and principal from 1 July 2023.

The arm's length annual interest rate for 2023/24, as determined under the ATO's safe harbour terms is based on the published rate for the month of May 2023 of the Reserve Bank of Australia's Indicator Lending Rate for banks providing standard variable housing loans for investors.

In accordance with the ATO's safe harbour interest rate for SMSFs with a related-party LRBA that is funding the purchase of real property, the relevant interest rate for 2023/24 will increase to 8.85%. This is an increase of 3.5% from the former rate of 5.35%.

Where the LRBA is funding the purchase of listed shares or listed units in a unit trust, the safe harbour rules require an additional margin of 2%, meaning the relevant interest rate for 2023/24, has increased to 10.85%.
This will make SMSF cashflow more important than ever. Speak to your SMSF advisor around how to maximise cashflow, including making additional contributions to your fund

On the flip-side, higher interest rates are resulting in super funds pilling more money into cash and bonds as they look for low risk investments. Funds have been increasing their exposure to cash and cash products from
18% of their savings pools last year to 22% so far this year, a new report shows.

Their exposure to the share market through direct investment dropped by 5% at the same time, as they funnelled their money into less volatile assets such as term deposits.

A reminder though that such a change in strategy must be consistent with your overall SMSF investment strategy, and may or may not be in the best interests of younger members whose circumstances may call for a higher risk, bolder investment strategy.

[1] The Vanguard and Investments Trend annual survey of SMSFs

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R&D reminder

The ATO has issued a reminder for companies wishing to claim a tax offset for their R&D (research and development) activities. The reminder was issued in the context of the ATO's success in the Federal Court decision *T.D.S. Biz Pty Ltd v FCT*[1].

By way of background, the research and development tax incentive (R&DTI) helps companies innovate and grow by offsetting some of the costs of eligible R&D.

The incentive aims to boost competitiveness and improve productivity across the Australian economy by:

- encouraging industry to conduct R&D that they may not otherwise have conducted
- improving the incentive for smaller firms to undertake R&D
- providing business with more predictable, less complex support.

Broadly speaking, your eligibility to claim the tax offsets will depend on whether you:

- are an R&D entity
- incurred notional deductions of at least $20,000 on eligible R&D activities.

You are not eligible for an R&D tax offset if you are either:

- an individual
- a corporate limited partnership
- an exempt entity (where your entire income is exempt from income tax)
- a trust (with the exception of a public trading trust with a corporate trustee).

For income years commencing on or after 1 July 2021, entities engaged in R&D may be entitled to:

- A refundable offset of 18.5% above the company's tax rate.
- A flat non-refundable offset based on a progressive marginal tiered R&D intensity threshold. Increasing rates of benefit apply for incremental research and development expenditure by intensity:
    - 0 to 2% intensity: an 8.5% premium to the company's tax rate
    - greater than 2% intensity: a 16.5% premium to the company's tax rate.

Turning back to the aforementioned case, the ATO successfully contended that the taxpayer conducted significant R&D activities outside Australia by purchasing components designed, developed and fabricated overseas without an Advance Overseas Finding from the Department of Industry, Science and Resources.

them on R&D activities conducted overseas, there is a requirement to hold an Advance Overseas Finding for those activities.

If your company is conducting R&D, contact us to determine if you are eligible for the offset.

Super withdrawal options

For individuals who have retired and met a condition of release, or who have turned 65 and are still working, you can receive your superannuation as a super income stream, as a lump sum, or a combination of both. This third option is quite popular for those who have yet to pay out their house, for example – a lump sum is withdrawn to pay off the remainder of the mortgage, and the balance used to commence a super income stream.

1. Lump sum

If your super fund allows it, you may be able to withdraw some or all of your super in a single payment. This payment is called a lump sum.

You may be able to withdraw your super in several lump sums. However, if you ask your provider to make regular payments from your super it may be classed as an income stream.

The downside to lump sums from a tax perspective is that once you take a lump sum out of your super, it is no longer considered to be super, and thus no longer enjoys the superannuation tax concessions (15% on earnings and capital gains, and tax-free if you convert your super into an income stream). That is, if you invest the lump sum outside of super, earnings on those investments are not taxed as super and may need to be declared in your tax return.

Further, if you're over age 60, super money you access from super will generally be tax free, but if you're under 60, you might have to pay tax on your lump sum.

2. Super income stream

You receive a super income stream as a series of regular payments from your super provider (paid at least annually). The payments must be made over an identifiable period of time and meet the minimum annual payments for super income streams. To find out what will happen if the income stream doesn't meet the minimum annual payment, see Minimum annual payment not made.

The payments don't need to be at the same interval, and the amount paid may also vary.

Super income streams are a popular investment choice for retirees because they help you manage your income and spending. Super income streams are sometimes called pensions or annuities.

One of the most common income streams is an account-based income stream. This is an account made up of money you've accumulated in super, which allows you to draw a regular income once you retire. An account-based income stream includes market-linked pensions that started on or after 1 July 2017.

Your provider or SMSF normally continues to invest the money in your super account and adds returns from investments to your account. Your account balance fluctuates with market performance.

Each year you can withdraw as much as you like through your account-based super income stream (unless you're receiving a transition to retirement income stream).

You must withdraw a minimum amount each year – based on your age and account balance. There may be income tax implications if your provider does not pay you the minimum amount each year.

You can continue to receive your super income stream until there is no money in your account. How long your super income stream lasts depends on how much you take out each year and what investment returns you receive. There is a limit on the amount you can transfer into retirement phase; this is known as the transfer balance cap.

The chief advantage of this type of withdrawal is that earnings on the remainder of your

Take-home message

Check with your super provider and adviser to find out what options are available to you, and which are best for your circumstances.

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