TAX MATTERS

TAX STRATEGIES FOR YOU AND YOUR BUSINESS

ZM PARTNERS

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What Is Never Tax-Deductible?

There are special provisions in tax law that provide that certain items will never be tax-deductible.

Even if you feel that you have necessarily incurred this expense in earning your income, these items will still not be tax-deductible. In total, there are 35 different items mentioned specifically in this section of tax law, with some of the more common items being:

- Any fines or penalties that are imposed under any laws cannot be claimed (e.g if you receive a parking fine when parking in the city for work-related purposes).
- Payments to reduce your HECS or student debt.
- Travel expenses of a relative when you travel for work-related purposes (unless they are also travelling for their work-related purposes).
- Wages paid to an associate that is more than reasonable for the work they do (e.g. your spouse cannot simply be paid $30,000/year to perform 1 hour of admin work per week for you).
- Payments to maintain your family (this usually applies to farmers, who feed their workers who may also be their family).
- Expenses to obtain or maintain membership of a recreational club.
- Expenses relating to a recreational boat more than the income earned from that boat. There is no negative gearing ('running at a loss') into a boat unless it is for a real and genuine business.
- Bribes to public officials both here and abroad (even if they had to be paid to get something approved).
- Expenditure relating to illegal activities.
- Superannuation guarantee charge- if you are late in paying your employee's superannuation you don't get a tax deduction when you do eventually pay it.
- Interest on borrowings to make non-concessional superannuation contributions.
- Travel expenses related to a residential rental property.
- Expenses associated with holding vacant land
- Where you are required to withhold taxes from certain payments such as interest, royalties or wages and then fail to withhold the required taxes, tax deductions cannot be claimed on these payments.

Some of these expenses are avoidable (such as the superannuation guarantee charge or the failure to withhold taxes from payments). It is important to consult with us to ensure that you are not wasting money on expenses that will not provide you with a valid tax deduction.

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Tax Planning
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What Tax Will Children Pay On Money Left To Them In A Will?

Children may seem to get the short stick of tax law when it comes to taxation. Children under the age of 18 years can only earn $416 in a year before they pay the top rate of tax (47%) on their income.

For example, if a 15-year-old earns $2,000 in interest for the year, they will pay close to $1,000 in tax on those earnings. The reason for such a high tax price is to prevent people from investing money in their children's names, so that they won't pay any tax on the earnings.

This may not seem fair though, as children may earn money from investments that haven't been put there to benefit someone else with tax savings. One such example is the money that may have been received in a will.

The tax law provides a few exemptions to the rule that taxes minors at the top rate of 47%. One such exemption is for earning from assets left to them in a will or earning from distributions from a trust established under a will. A trust that is established under a will is known as a **testamentary trust.**

If a child earns $2,000 in interest from money left to them under a will, the special rules for minors would not subject them to the 47% rate of tax. Insteas, as those earnings came from money left to them in a will, they would simply pay the normal adult rates of tax on the interest. If this was their only income, they would be well below the tax-free threshold and would not pay any tax on the earnings.

There are a lot of rules around what can be done with investments, which is why starting a conversation with us if your child is to receive an inheritance is a step in the right direction.

If you are thinking about leaving assets to a child or grandchild in your will, we can also assist you with tax planning for this eventuality.

Lawyers may be the key to drafting strong and valid wills, but there are great tax-planning opportunities for nearly everyone when it comes to planning for your estate.

One Of The Last Great Tax Benefits: The Special Building Write-Off

One of the most common things that people approach accountants about is tax, or rather, that they're paying too much of it. How can they reduce it?

However, if your only goal is to reduce tax, that's easy. There are plenty of ways to realise this, such as making most of your taxable income into a charitable donation (e.g. $200,000 taxable income, $180,000 donation to charity).

But this isn't really a realistic approach. You may pay no tax in this manner, but you will also be without money. Tax deductions and tax savings do however require you to spend more money than you'd save. This would be fine, but only if that money was originally going to be spent anyway.

There are still a few areas of tax law that offer true tax savings. The best one of all could arguably be the depreciation allowed on buildings and plant and equipment in rental properties.

But why is that? Yes, you can buy a building, write it off (claim the remaining value as depreciation) and then pay tax when selling the building. But the advantage with this particlar item is that you can get a full tax deduction for the depreciation BUT only pay tax on half of the capital when you eventually sell the property.

If Peter is in the top marginal tax bracket and paying 47% on each extra dollar that he earns, he is also conversely saving 47% tax on each dollar he spends. Let's assume that an investment property he purchases cost $1 million. From a quantity surveyor, he receives a depreciation report entitling him to $15,000 in special building write off, with another $15,000 in depreciation on his plant and equipment.

In the first year of ownership, Peter should receive a tax deduction for the $30,000 in building write off in depreciation, which means that he should receive a tax refund of $14,100 on those expenses (47% of the write off). No additional money needs to be spent to receive that deduction.

However, if he were to sell the property instead after 12 months for the same amount ($1 million), that is when it can get a little complicated.

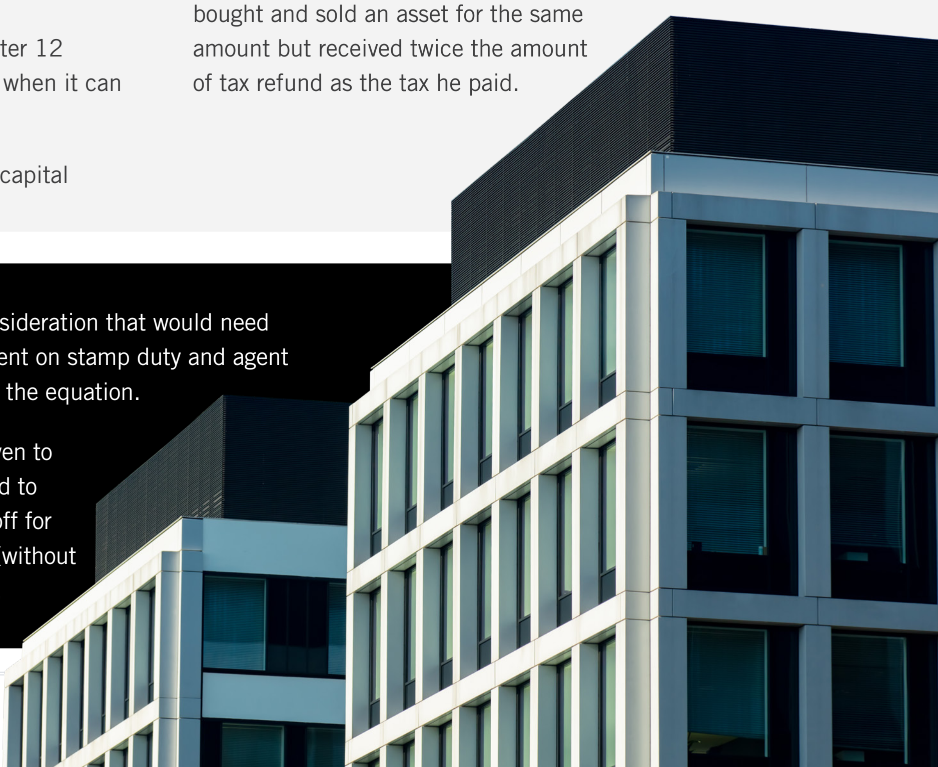
As Peter has held the property for at least a year, capital gains tax only has to be paid on half of the capital gain. Selling it for the same amount that it was purchased for may have implied that no capital gain was made - sadly, that's not how tax law works.

Since Peter has also claimed $30,000 in building write off and depreciation which was made back as a capital gain, this means that he has actually made a capital gain of $30,000. From this, Peter would only have to pay tax on half of the capital gain ($15,000), which is then added to his taxable income, incurring a 47% tax on that gain.

This means that Peter will pay $7,050 in extra tax. With his previous year's tax refund of $14,100 he will have in effect bought and sold an asset for the same amount but received twice the amount of tax refund as the tax he paid.

In this example, taxation is just one consideration that would need to be taken into account. The money spent on stamp duty and agent fees would also need to be factored into the equation.

While overall this example may not have been proven to be a feasible and worthwhile project, it is designed to demonstrate that depreciation and building write off for rental properties can provide a real tax advantage (without having to spend two dollars to save a dollar in tax).



Thinking Of Moving Overseas? Now Might Be The Time To Sell Your House

The rules regarding the capital gains exemption for your main residence have changed, which could impact your current situation (if you are not already aware of them).

You may already be aware that purchasing a house to live in as your main residence will result in no capital gains tax when you eventually choose to sell it. Your main residence could prove to be a very tax-effective investment, but there are strict rules surrounding how to claim this exemption.

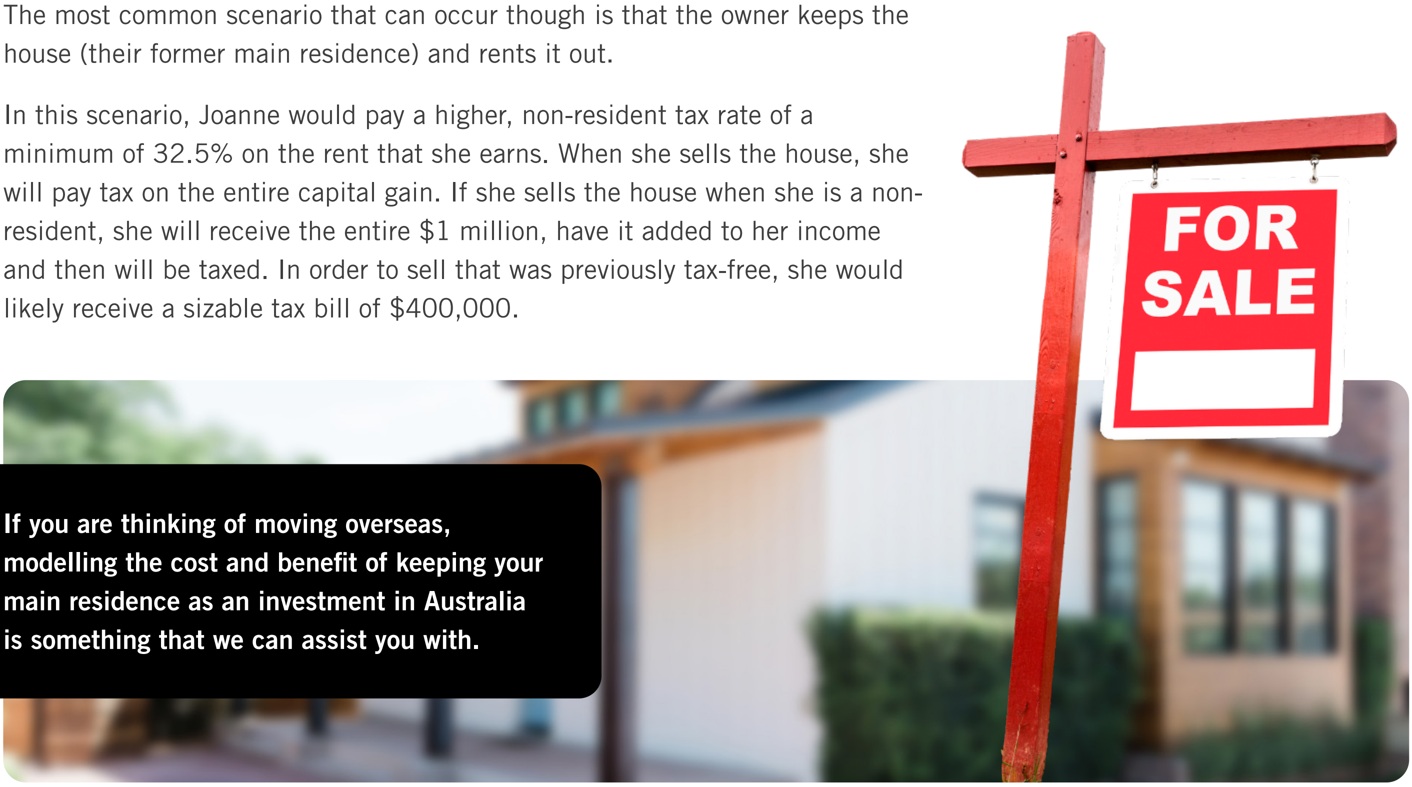
Under the new changes, only Australian tax residents may be allowed to claim the main residence exemption. Not only that, but they are also the only eligible residents to claim the 50% discount for any capital gains they make on assets that they have held for more than 12 months.

Many people may leave Australia to move to low tax countries. In the case of ownership of a former main residence in Australia, the tax savings you could make in the move could get eaten up if you sell that main residence **after** you cease to be an Australian tax resident.

For example, Joanne buys her property in Sydney in 1997 for $300,000 and has lived in it since. It is now valued at $1.3 million. She is about to move overseas and will cease to be a tax resident. If Joanne sells the house **before** moving overseas, she will pay no tax on the $1 million capital gain from selling the house.

The most common scenario that can occur though is that the owner keeps the house (their former main residence) and rents it out.

In this scenario, Joanne would pay a higher, non-resident tax rate of a minimum of 32.5% on the rent that she earns. When she sells the house, she will pay tax on the entire capital gain. If she sells the house when she is a non-resident, she will receive the entire $1 million, have it added to her income and then will be taxed. In order to sell that was previously tax-free, she would likely receive a sizable tax bill of $400,000.



If you are thinking of moving overseas, modelling the cost and benefit of keeping your main residence as an investment in Australia is something that we can assist you with.

Who Are You Getting Your Tax Advice From?

Advertisements on the internet might use buzzwords from the taxation and superannuation industry to pique your interest. However, they can be misleading in how they represent your actual benefits.

An advertisement for a car on the internet could point out that if you buy it (a $150,000 car) in your business, you would be entitled to the Instant Asset Write-off. While this statement is technically correct, it is also misleading in how the Instant Asset Write-off works.

Under current tax law, if you are a business and purchase an asset to use in your business you can get a tax deduction for the full value of the asset. This is as opposed to depreciating the asset over a number of years.

The same applies to cars. If you purchase a car now, you can get an instant tax deduction (as opposed to depreciating the car over a number of years. However, your tax deduction is still limited to the car cost limit (which sits at around $60,000). So, while the advertisement is technically correct, the most that you could claim as a tax deduction on that $150,000 car is $60,000.

Plus, after the car is purchased you may also have a fringe benefits tax liability every year based on the full value of $150,000. This means that you'd miss out on the tax deduction but would still pay the fringe benefits tax, which restricts the tax advantages of providing cars as an employee benefit.

Other organisations may benefit from tax-effective buyers purchasing their products. While the advertising is often technically correct, it can be misleading in how it is represented. We suggest always coming to us for tax advice or clarification on your actual benefits.

Logbooks For Your Cars

There are a number of methods that tax deductions can be calculated for car usage or the fringe benefits value of a car. One of these methods requires that a logbook is to be completed.

The purpose of the logbook is to help determine what proportion of the usage of the car is business use. For an individual, this will then give you a percentage of your overall expenses that are tax-deductible. For an employer, it will tell you what percentage of use of the car is subject to fringe benefits tax. It is important to understand though that even if you complete a logbook, you don't necessarily have to use the logbook method for claiming your tax deductions.

What Goes Into A Logbook?

Your logbook must contain:

- when the logbook period begins and ends
- the car's odometer readings at the start and end of the logbook period
- the total number of kilometres the car travelled during the logbook period
- the number of kilometres travelled for each journey. If you make two or more journeys in a row on the same day, you can record them as a single journey
- the odometer readings at the start and end of each subsequent income year your logbook is valid for
- the business-use percentage for the logbook period
- the make, model, engine capacity and registration number of the car.

For each journey, you need to record the:

- reason for the journey (such as a description of the business reason or whether it was for private use)
- start and end date of the journey
- odometer readings at the start and end of the journey
- KM kilometres travelled

Other Important Notes For Logbooks

- The log book must be maintained for at least 12 continuous weeks and will be valid for up to five years. If your circumstances change though, you should complete a new log book.
- If you have two cars that you use and wish to keep a log book for both cars, then the 12 week period must be the same for both cars.
- You will need to keep evidence of all of your car expenses (including receipts). You can estimate fuel costs but will need to keep odometer readings.

A logbook cannot simply be written up at the end of the time period (12 weeks). The ATO have access to data (such as toll history) and will match what they find against your logbook. If they discover a discrepancy, all of your car expenses claimed as a tax deduction may be completely disallowed.

Western Australian Doctor Prescribed Jail Time For Failing To Comply With Court Orders

A Western Australian doctor has recently been sentenced to seven months jail, and placed on a good behaviour bond for failing to comply with court orders to lodge 18 outstanding income tax returns and business activity statements (BAS).

The doctor failed to lodge their income tax returns for the 2013 to 2017 income years, and BAS for 13 of the months between May 2017 and June 2018 inclusive.

In February 2020, he was convicted at the Perth Magistrates Court and fined $50,000 for failing to provide the Commissioner of Taxation with the outstanding income tax returns and BAS. In sentencing, the taxpayer was ordered to make the outstanding lodgments within two months.

However, he still failed to lodge and was prosecuted once more.

On 11 April 2022, the doctor was convicted of 18 charges of failing or refusing to comply with court orders. During sentencing, the Magistrate stressed that **complying with tax obligations is not optional and that a failure to do so places a burden on the rest of the community.**

He will be released from jail after two months, upon entering into a $10,000 recognisance to be of good behaviour for the remainder of his sentence. As part of the good behaviour bond, he will need to lodge each of the outstanding tax returns and BAS by 30 September 2022.

The ATO's Acting Assistant Commissioner welcomed the sentence, reiterating that those who deliberately try to evade the tax system will be held to account.

If you are falling behind on your obligations, or have made an honest mistake, the ATO's focus is on supporting you if you are doing the right thing. They will work together with you to find a solution and get you back on track.

However, where people continue to do the wrong thing or refuse to engage with them, the ATO will initiate stronger action.

The ATO make multiple attempts to contact taxpayers to provide support to those who are behind with their lodgment obligations.

This specific instance involved a history of both failing to lodge information as required, and subsequently failing to comply with court orders. This represents sustained disregard for one's tax obligations and damages the integrity of the tax system.

Who Am I Connected To Tax-Wise?

*There are instances throughout tax law where you are required to know who the '**entities connected with you**' are. This is used in determining if you are a Small Business Entity or what the value of your assets is if you wish to claim the Small Business CGT Concessions. It is also important in instances where you have sold an asset and claimed that it was used by an '**entity connected with you**'.*

Sometimes, having an entity connected to you can be a good thing. If you were to sell a factory unit and a company connected with you ran a mechanics business out of that factory unit for example, this would allow you to claim the Small Business CGT Concessions on the sale of that factory unit.

Conversely, the value of the assets of a connected entity are added to yours when looking at certain asset tests. In that sense, you do not want entities to be connected with you.

If you have a family trust and make a distribution to your adult daughter, you may have to add her assets to your asset pool for determining if you have access to tax concessions. Anyone that has received 40% of the income or capital of a trust in the previous four years is thus connected to that trust.

Two entities controlled by the same person or entity will also be connected with each other. If you have two trusts that you control, those two trusts are also connected to each other as well as to you.

Interestingly, you and your spouse are not automatically connected to each other, nor would you normally be. If you control a company and your spouse controls their own separate company, then the two companies will most likely not be connected to each other. Depending on the situation, this could be good or bad.

While this may sound complex, your connections are something that needs to be addressed on an ongoing basis. Using the example of the factory unit above, circumstances surrounding its disposal could change the connection. You may have kept the factory unit, but given the company to your son instead five years ago. This means that the company is no longer connected with you which could impact your access to certain tax concessions.

Keeping us apprised of your future plans for your assets and of changes that could impact your connections means that we can ensure that you do not inadvertently miss out on any of the tax concessions that may be available to you.