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client alert | explanatory memorandum

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Tax Laws Amendment (2009 Measures No 1) Bill

On 12 February 2009, the Government introduced Tax Laws Amendment (2009 Measures No 1) Bill into the House of Representatives.

The Bill will amend:

- section 45-400 of Sch 1 to the *Taxation Administration Act 1953* (the TAA) to provide for the PAYG instalment reduction for small businesses;
- Schedule 1 to the TAA to require 'reportable employer superannuation contributions' (RESC) are reported on PAYG summaries;
- various Acts as a result of the payment of temporary residents' unclaimed superannuation to the Government;
- relevant legislation to introduce new key concepts and definitions, which are to be added to income for means-test government assisted programs; and
- various tax and social security programs to give effect to expand the income tests used in those programs.

A discussion of some of the amendments contained in the Bill follows.

PAYG instalment for small businesses

The Bill will amend s 45-400 of Sch 1 to the TAA (which provides how the Commissioner works out the amount of the PAYG quarterly instalments on the basis of GDP-adjusted notional tax) to provide for:

- a 20% reduction for the December 2008 quarter PAYG instalment, payable by certain small business entities; and
- a regulation-making power to allow the amount of the PAYG instalment worked out under the section to be reduced in the future in circumstances specified by regulations.

The 20% reduction was previously announced by the Government in December 2008.

PAYG reduction for December 2008 quarter

The reduction applies to taxpayers that report and pay their PAYG instalment either on a monthly or a quarterly basis. (For practical reasons, most eligible taxpayers would have already claimed the 20% reduction.)

The Bill clarifies that the reduction does not apply to small business entities who:

- calculate their PAYG instalments based on the instalment rate notified by the Tax Office;
- voluntarily varied their PAYG instalment for the December 2008 quarter; and

- pay two instalments annually (for example, a professional sports person).

The Explanatory Memorandum to the Bill states that the reduction is not clawed back through subsequent instalment amounts.

Variation of instalment amounts by regulation

The Bill will insert a regulation-making power to allow PAYG instalment amounts as worked out under s 45-400 to be reduced in the future in certain circumstances as prescribed by the regulations.

This amendment will apply to quarterly taxpayers who pay four instalments annually on the basis of GDP-adjusted notional tax.

Date of effect

This measure applies in relation to instalment quarters in the 2007/08 income year and later income years.

Tax Office administrative treatment

The Tax Office has released a publication setting out top issues for tax practitioners on the Government's PAYG instalment 20% reduction for small business in respect of the December 2008 quarter.

The Tax Office notes that the PAYG instalment reduction is a permanent 20% reduction to the PAYG instalment amount for the quarter that includes 31 December 2008.

The Tax Office says it has already written to those taxpayers that it has identified as being eligible for the 20% reduction. However, if tax practitioners think that one of their clients is eligible and have not received a letter from the Tax Office, to phone the Tax Office on 13 72 86 Fast Key Code 1 4 1, to determine their client's eligibility prior to advising them to pay only 80% of the instalment amount.

The Tax Office says that if a client has already paid the full instalment amount advised on their activity statement/instalment notice, tax agents may choose to:

- do nothing in which case the Tax Office says it will treat the extra 20% amount as a voluntary payment the client has made towards its income tax liability, or
- contact the Tax Office on 1300 308 217 to have the 20% amount either applied to the client's next PAYG instalment or refunded.

PAYG summary amendments

The Bill will amend Sch 1 to the TAA to provide the mechanism for reporting of 'reportable employer superannuation contributions' (RESC) (*see* **Key concepts and definitions**, below).

Payment summary provisions

The Bill will amend s 16-155 of the TAA to require payers to disclose RESC made on behalf of an employee during a financial year, or part of a financial year, on part year payment summaries and the annual payment summary provided to that employee for the financial year. Payers will also need to provide an annual payment summary to an individual where they have made RESC for that individual during the year in respect of the individual's employment.

The amendments also alter the part-year payment summary provisions in s 16-160 to include RESC. As a result, payers will need to provide a part-year payment summary if a recipient asks for one, covering any RESC made by the payer in respect of the recipient's employment during the financial year

Annual report content requirements

The Bill will also amend s 16-153(2) of Sch 1 to the TAA to require payers to provide an annual withholding report to the Commissioner where they have made RESC during the financial year. Payers will need to provide this annual withholding report to the Commissioner, no later than 14 August after the end of the financial year in which the RESC were made.

This means that entities may provide the Commissioner with a payment summary or payment summaries they have issued in respect of RESC made during the financial year as an alternative to providing the approved form. The entity needs to provide an accompanying statement in the approved form as well.

Date of effect

These amendments apply in relation to income years starting on or after 1 July 2009.

Key concepts and definitions

The Bill will amend ITAA 1936, ITAA 1997 and Sch 1 to the TAA to provide the key concepts and definitions that will apply as part of the income tests reforms (*see* **Amendment of income tests**, below).

The Bill will insert and define the following terms into the relevant legislation:

- adjusted fringe benefits;
- reportable superannuation contributions;
- reportable employer superannuation contributions;
- total net investment loss;
- rebate income; and
- income for surcharge purposes.

Adjusted fringe benefits

The Bill will insert a definition of 'adjusted fringe benefits total' into s 6(1) of ITAA 1936. This term is defined as the 'gross-down' amount of reportable fringe benefits paid to an employee and is calculated using the formula:

Taxpayer's reportable fringe benefits total x (1 - FBT rate)

A taxpayer's 'adjusted fringe benefits total' will be assessed in determining eligibility for the senior Australians tax offset (SATO) and pensioner tax offset. The adjusted fringe benefits total of a beneficiary and the beneficiary's spouse will also be assessed in determining a trustee's eligibility for the offset contained in s 160AAAB of ITAA 1936.

Note that the current definition of 'reportable fringe benefits total' contained in s 6(1) will be repealed. However, the definition of 'reportable fringe benefits total' which is contained in s 136 of the *Fringe Benefits Tax Assessment Act 1986* (the FBTAA) will be retained.

Reportable superannuation contributions

The Bill will insert a new definition of 'reportable superannuation contributions' in s 995-1 of ITAA 1997, which will be applied to income tests for a range of tax and social security programs.

The reportable superannuation contributions for an income year of an individual will include the total of the individual's 'reportable employer superannuation contributions' (see below) and deductions for personal contributions under Subdiv 290-C of ITAA 1997.

Reportable employer superannuation contributions

Reportable employer superannuation contributions (RESC) will be defined in s 16-182 of Sch 1 of the TAA to include contributions to a superannuation fund or a retirement savings account, made on behalf of an individual during an income year, by their employer or an associate of their employer. (*See* **GST and Uncommercial Property Arrangements** for the definition of associate.)

Only contributions made on behalf of an individual in circumstances where the individual had some capacity, or might reasonably be expected to have some capacity, to influence the size of the contribution or the way in which the contribution was made are RESC. In these circumstances, the burden of proving that an employee had no capacity to influence falls on the employer. From 1 July 2009, employers will be required to report RESC on payment summaries (see above).

A key example of RESC is amounts that an individual has elected to have contributed to superannuation as part of a salary sacrifice arrangement. In these circumstances, the amount of contribution in excess of the amount required to be made under superannuation guarantee legislation (9% of ordinary time earnings) would be RESC. Contributions equating to what an employer is required to make on behalf of an employee under the superannuation guarantee regime are not RESC.

However, it is not necessary for contributions to be compelled by law for them to fall outside the definition of RESC. To the extent that an employer makes contributions above those mandated by law for administrative or other considerations (eg payroll system limitations), over which the employee has no, and could not reasonably be expected to have, capacity to influence, then those contributions will not be RESC.

For a contribution made pursuant to the terms of an industrial agreement to be excluded from RESC, it must be demonstrated that the employee had no capacity to influence the terms of the agreement and could not reasonably be expected to have capacity to influence those terms.

Member contributions made from an individual's pre-tax salary or wages are excluded from the RESC definition: s 16-182(2) of Sch 1 of the TAA.

The examples, which are modified from the Explanatory Memorandum, explain the operation of RESC.

> Example One
>
> *Lisa is an employee of FJH Pty Ltd. FJH contributes 9% of Lisa's total remuneration to superannuation under an industrial agreement that was negotiated between the company and the union representative. Lisa was not involved in these negotiations and had no involvement in the preparation of the agreement, aside from voting on it. As such, she would have no capacity to influence this amount of contribution.*
>
> *However, under the agreement, employees may elect to have an amount of salary paid to superannuation. This is in addition to the 9% contribution required under the agreement. During the year, Lisa approached FJH to have $5,000 contributed to her superannuation fund as part of an effective salary sacrifice arrangement.*
>
> *The $5,000 contribution will be considered RESC.*

> Example Two
>
> *Rhonda's employer makes superannuation contributions on Rhonda's behalf to a defined benefit fund. The employer contributions are applied to a pool to fund the liability of the entire fund. In addition, the rules of the fund require Rhonda to make a member contribution equal to 7% of ordinary time earnings. Ordinarily, this member contribution would be made from Rhonda's assessable income.*
>
> *However, the rules of the defined benefit fund were recently amended to enable individuals to contribute their member contribution from pre-tax salary or wages. Rhonda exercises this option and the 'grossed-up' amount of her member contribution is deducted from her pre-tax salary or wages so that Rhonda makes the same net contribution to her employer's defined benefit fund as she would have made if the member contribution were made from assessable income.*
>
> *The total grossed-up amount of the contribution is RESC because it represents the amount that Rhonda has elected to have made from pre-tax salary with the effect that her assessable income is reduced.*

Total net investment loss

The Bill also proposes to insert a definition of 'total net investment loss' into s 995-1 of ITAA 1997. The definition of this includes the sum of the amounts by which the individual's deductions attributable to 'financial investments' and 'rental properties' exceed the individual's gross income from those sources.

The definition is intended to capture net losses from financial investment. Therefore, the Bill will also insert a definition of 'financial investment' in s 995-1 of ITAA 1997. A financial investment will include:

- a share in a company (whether those shares are in an Australian company or foreign company);

- an interest in a managed investment scheme (MIS) for the purposes of the *Corporations Act 2001*. Note that the requirement for the MIS to have more than 20 members (which is an element of the definition in the ITAA 1997) does not apply;
- a forestry interest in a forestry MIS;
- a right or an option in respect of a company, MIS and forestry MIS; and
- an investment of a like nature to those described above.

Relevant considerations in determining whether an investment is of a like nature to the other investments are whether the investment is traded in a manner similar to the other investments and the similarities between the type of investors in that investment. It is intended that the 'financial investment' definition captures as many investments subject to investment loan, or margin loan arrangements as is appropriate.

Rebate income

The Bill will introduce the term 'rebate income' into s 6(1) of ITAA 1936. The rebate income of a taxpayer for an income year is the sum of:

- the taxpayer's taxable income for the year; and
- the taxpayer's reportable superannuation contributions for the year; and
- the taxpayer's total net investment loss for the year; and
- the taxpayer's adjusted fringe benefits for the year.

A taxpayer's rebate income will be applied in determining eligibility for the following offsets:

- SATO;
- pensioner tax offset; and
- trustee offset under s 160AAAB of ITAA 1936.

Income for surcharge purposes

The Bill will insert into s 995-1 of ITAA 1997 a new definition of 'income for surcharge purposes'. This new definition will be used to determine an individual's liability for the Medicare levy surcharge.

A taxpayer's income for surcharge purposes is defined as the sum of the following:

- the taxpayer's taxable income for the income year (disregarding s 271-105(1) of Sch 2F to ITAA 1936);
- the taxpayer's reportable fringe benefits total (if any) (as defined in s 136 of the FBTAA) for the income year;
- the taxpayer's reportable superannuation contributions for the income year;
- the taxpayer's total net investment loss for the income year; and
- less the tax offset available to the taxpayer under s 301-20 of ITAA 1997 (tax treatment of superannuation lump sum for individuals aged 60 and under) for the income year.

Date of effect

These amendments will commence the day after the Bill receives Royal Assent and will apply to the 2009/10 income year and later income years.

Amendment of income tests

The Bill will amend the income tests across various Acts to include reportable superannuation contributions, RESC and total net investment losses where appropriate.

The Acts and the programs which will be affected by the amendments, include:

Act	Program	Income test to include
A New Tax System (Family Assistance) Act 1999	Child Care Benefit Family Tax Benefit Part A and B Baby Bonus	a person's total net investment loss and reportable superannuation contribution in determining eligibility for the payments
Child Support (Assessment) Act 1989	Child support	a parent's total net investment loss and reportable superannuation contributions in the definition of 'adjusted taxable income'
Higher Education Support Act 2003	Higher Education Loan Program	an individual's total net investment loss and reportable superannuation contributions in the definition of 'repayment income'
ITAA 1936	SATO Tax offset for trustees	an individual's rebate income instead of the current total income
ITAA 1997	Deduction for personal superannuation contributions	a taxpayer's RESC in the income base that is used to determine whether personal superannuation contributions are deductible[1]
	Mature age worker tax offset	a taxpayer's RESC in the definition of 'net income from working'
	Spouse superannuation contributions tax offset	a taxpayer's spouse RESC[2] when determining the taxpayer's eligibility for the offset
	Tax offsets for Medicare levy surcharge (lump sum payments in arrears)	an individual's reportable superannuation contributions and total net investment losses
Social Security Act 1991	Commonwealth Seniors Health Card (CSHC)	an individual's total net investment losses to determine eligibility for the CSHC
	Student Financial Supplement Scheme	an individual's reportable superannuation contributions and total net investment losses
Student Assistance Act 1973	Student Financial Supplement Scheme	an individual's reportable superannuation contributions and total net investment losses in the definition of 'repayment income'
Superannuation (Government Co-contribution for Low Income Earners) Act 2003	Government superannuation co-contribution scheme	a person's RECS when determining eligibility for the co-contribution[3]
Veterans' Entitlement Act 1986	CSHC	an individual's total net investment losses in determining eligibility for the CSHC

1. The amendments will not add a taxpayer's 'reportable superannuation contributions' or 'total net investment losses' to income as the income base is assessable income which is the taxpayer's gross income before deductions applied.

2. The amendments means that a spouse's assessable income, reportable fringe benefits (if any) and RESC will need to be less than $13,800 per annum for a taxpayer to be eligible for the offset.
3. The amendments will not add a taxpayer's 'reportable superannuation contributions' or 'total net investment losses' to income as the income base is assessable income which is the individual's gross income before deductions are applied.

Date of effect

These amendments will commence the day after the Bill receives Royal Assent. Generally, the amendments will apply to the 2009/10 income year and later income years.

GST and Uncommercial Property Arrangements

The Tax Office has released two Taxpayer Alerts which relate to GST and uncommercial property arrangements as discussed below.

Taxpayer Alert TA 2009/4

This Alert describes an arrangement that purportedly allows a land owner to register for GST as late as possible to minimise its GST payable under the margin scheme, but still claim a full input tax credit (ITC) on its acquisition of construction services from an associate.

Description of arrangement

The Tax Office says that the Alert applies to arrangements having some or all of the following features:

1. An unregistered entity (the land owner) acquires land prior to 1 July 2000.
2. The land owner engages a GST-registered associate to construct and market residential premises.
3. The associate engages a builder to construct the residential premises, provides payment for the construction services and claims ITCs on these acquisitions.
4. The associate on-supplies these services to the land owner but does not require progress payments for the services.
5. The land owner registers for GST and receives an invoice from its associate, just prior to the sale of the premises.
6. The land owner claims a full ITC on its acquisition of the services from its associate.
7. The land owner calculates its GST payable on the sale of the premises under the margin scheme using a valuation of the land at the date of its GST registration.

Tax Office views

The Tax Office says that arrangements as described above could give rise to taxation issues, including whether:

- the land owner is entitled to a full ITC under Div 11 of the *A New Tax System (Goods and Services Tax) Act 1999* (the GST Act) on its acquisition of the services from its associate;
- the land owner is required under Divs 23 and 188 of the GST Act to be registered at a point earlier than the date its registration takes effect;
- any act or payment by the land owner causes an associate's GST to be attributable in accordance with s 29-5 of the GST Act to a tax period prior to the tax period to which the associate treats its GST as being attributable;
- any act or payment by the land owner causes any ITC that the land owner is entitled to, to be unattributable under s 29-10 of the GST Act because the act or payment occurs at a time when the land owner is not registered or required to be registered for GST;

- the GST payable by the land owner on its sale of the residential premises is calculated correctly under the margin scheme in Div 75 of the GST Act; and
- the anti-avoidance provisions of Div 165 of the GST Act apply, as the arrangement appears artificial and contrived in its design and execution.

Taxpayer Alert TA 2009/5

This Alert describes an arrangement in which an entity uses an associate in an attempt to secure ITCs on the construction of residential premises for lease and defer the corresponding GST liability, in some cases indefinitely.

Description of arrangement

The Tax Office says that the Alert applies to arrangements having some or all of the following features:

1. A land owner, who may or may not be registered for GST, plans to construct residential premises to lease to third parties.
2. The land owner engages its associate to construct the residential premises.
3. The associate either undertakes the construction or engages an arm's length builder, and claims ITCs on its acquisitions.
4. The associate does not seek progress payments from, nor issues an invoice to, the land owner until the premises are ultimately sold.
5. The land owner leases the completed residential premises to third parties (an input taxed supply).
6. The associate only remits GST upon the sale of the residential premises by the land owner.

Tax Office views

The Tax Office says that arrangements as described above could give rise to taxation issues, including whether:

- the associate is carrying on an enterprise under s 9-20 of the GST Act;
- the associate is entitled to input tax credits under Div 11 of the GST Act on the acquisitions it makes in constructing, or arranging the construction of, the residential premises;
- any act or payment by the land owner causes the associate's GST to be attributable in accordance with s 29-5 to a tax period at a point earlier than the sale of the residential premises;
- Division 72 of the GST Act, which covers supplies to associates for no or inadequate consideration, applies to the supply by the associate to the land owner; and
- the anti-avoidance provisions in Div 165 apply, as the arrangement appears artificial and contrived in its design and execution.

Definition of associate

The term 'associate' is defined in s 195-1 of the GST Act which in turns refer to s 318 of ITAA 1936.

Under s 318, the categories of persons and entities that are associates of another person or entity (P) include:

- if P is a natural person, a relative — 'relative' means a parent, grandparent, brother, sister, uncle, aunt, nephew, niece, lineal descendant, adopted child of P or of her or his spouse, the spouse of P and the spouse of a relative;
- a partner (whether P is a natural person, corporation or partnership), the spouse or child of a partner (where the partner is a natural person) or a partnership in which P is a partner (except where P is a partnership);
- if P is a partnership, the associate of any partner;
- if P is a company, a person or entity where P is sufficiently influenced by that person or entity;

- if P is a company, a person or entity that (together with any of their associates) controls more than 50% of the maximum number of votes that may be cast at a general meeting of the company, or any associate of that person or entity;
- a company that is sufficiently influenced by P (whether a natural person or a corporation) and/or P's associate(s);
- a company where more than 50% of the maximum number of votes that may be cast at a general meeting of the company is controlled by P (whether a natural person or a corporation) and/or P's associates;
- the trustee of a trust where P (whether a natural person or a corporation) or any associate of P benefits, or is capable of benefiting, under the trust, whether directly or indirectly through interposed entities; or
- if P is a trustee, any person who benefits, or is capable of benefiting, under the trust, whether directly or indirectly through interposed entities and any associate of such a person (whether a natural person or a corporation).

A company is 'sufficiently influenced' by another person or entity if the company, or its directors, are accustomed or under an obligation (formal or informal), or might reasonably be expected, to act in accordance with the directions, instructions or wishes of the person or entity (however those directions, instructions or wishes are communicated).

GST anti-avoidance provisions

The GST anti-avoidance provisions contained in Div 165 are aimed at artificial or contrived schemes which give entities GST benefits. The definition of a GST benefit is contained in s 165-10 to include schemes that:

- reduce the GST liability of an entity;
- increase the amount of input taxed credits (ITC) refund; or
- alter the timing of payment of GST or refunds.

A scheme is defined as any arrangement, agreement, understanding, promise or undertaking regardless of whether the scheme is express or implied and enforceable by proceedings. A scheme can also include any plan, proposal, action, course of action or course of conduct, whether unilateral or otherwise.

It is important to note that an entity can be deemed to obtain a GST benefit from a scheme even if the entity had no economic alternative but to be entered into or carried out the scheme (or part of the scheme).

Generally, the GST anti-avoidance provisions operate if an entity obtains a GST benefit from a scheme and the benefit is not attributable to the making of a choice, election, application or agreement that is expressly provided for by the GST law: see s 165-5(1).

The general rule as to when the GST anti-avoidance provisions would operate was amended by Tax Laws Amendment (2008 Measures No 5) Bill 2008, which received Royal Assent on 9 December 2008. Broadly, the Bill inserted s 165-5(3) which states that if a GST benefit is attributable to the making of a choice, election, application or agreement, then consideration needs to be given to the purpose of creating any circumstance or state of affairs which enables the choice, election, application or agreement.

Legal status of Taxpayer Alerts

An Alert is only intended to be an early warning of a tax planning arrangement that the Tax Office has under risk assessment. However, it is expected that a GST Ruling or GST Determination will be issued by the Tax Office following the release of the Alert.

Taxpayers who have entered into or are contemplating entering into an arrangement similar to that described in the Alert can seek a formal determination of the Tax Office's position through a private ruling.

Personal Services Income Case

The AAT has found that a company was not conducting a personal services business (PSB). Accordingly, the income of the company should be included in the taxpayer's assessable income: *[2009] AATA 87, Re Taneja and FCT*.

Background

The taxpayer was a computer systems analyst, and was one of the directors of the company. For the income years 2002 to 2005, the company derived income through the provision of the taxpayer's personal efforts or skills. The taxpayer contended that the company satisfied the 'results test' contained in s 87-18 of ITAA 1997 and was therefore a PSB for the relevant income years on the following basis:

- the company's contract must be producing a result if the Commissioner accepted for the purposes of s 87-18(3)(c) that the company was liable for the cost of rectifying any defects in the work performed;
- the reliance on a doorstop interview given by the former Treasurer, Mr Peter Costello, on 9 July 2001 in which Mr Costello announced proposed amendments to the Personal Service Income (PSI) regime;
- the operation of s 87-18(3)(a) was subjected to s 87-18(4), that is the 'custom and practice' of the industry must be considered when applying the results test; and
- the company, under general law, was an independent contractor and therefore the PSI regime could not apply to him or the company's circumstances.

Decision

The Tribunal rejected the taxpayer's contention. It said that the salient issue was whether the company earned income 'for producing a result'. If yes, the company would satisfy the results test and be deemed a PSB.

The Tribunal said that each subsection in s 87-13 had independent operation based on the Federal Court's decision in *IRG Technical Services Pty Ltd & Anor v DCT* (2007) 69 ATR 433. It also said that the requirements of s 87-13 were cumulative and must all be satisfied for the results test to be met.

In response to the taxpayer's reliance on the doorstop interview, the Tribunal said that it was 'unwise to place too much reliance on what a Minister says in a doorstop interview'. It noted that in the same interview, the then Treasurer set out the three criteria for the results test. Therefore, it rejected the taxpayer's submission 'to elevate the contents of the interview to a status equivalent to, or perhaps even above, that of the Explanatory Memorandum'.

The Tribunal agreed with the Commissioner that the principal purpose of s 87-14(4) was to 'act as a safety net for those individuals or entities who cannot point to a written agreement to establish that they have been paid "for producing a result"'. It said that a reliance on the custom and practice of an industry where a written agreement specifying that an individual was entitled to payment for doing something that did not amount to producing a result would remove the criterion in s 87-18(3)(a), which would be against the intention of the legislation.

The Tribunal said that an entity could still be subject to the PSI regime, albeit the entity might satisfy the description of an independent contractor.

The Tribunal examined agreements that the company entered into with its clients. It noted that nothing in the agreements suggested the company was being paid to produce a result. Its view was that the company 'was being paid for the time that it spent, through the taxpayer, doing what the client asked of it'.

The Tribunal considered whether the company would have satisfied the other three personal services business test (the unrelated clients test, the employment test, and the business premises test) for the 2003 income year. It found that the company did not satisfy the other tests. (The Tribunal noted that it was not necessary to apply the other tests in relation to the other years of income because the company failed the 80% rule in those years.)

In conclusion, the Tribunal found that the company did not conduct a PSB in any of the relevant years. However, the Tribunal noted that the issues of the deductibility of some expenditure and additional tax payable remained to be determined. Therefore, the Tribunal remitted the matter to the Commissioner for further consideration.

Results test — s 87-18(3) of ITAA 1997

Where an individual generates PSI through a personal services entity (company, trust or partnership), s 87-18(3) states:

'A personal services entity meets the results test in an income year if, in relation to at least 75% of the personal services income of one or more individuals that is included in the personal services entity's ordinary income or statutory income during the income year:

a) the income is for producing a result; and

b) the personal services entity is required to supply the plant and equipment, or tools of trade, needed to perform the work from which the personal services entity produces the result; and

c) the personal services entity is, or would be, liable for the cost of rectifying any defect in the work performed.'

Taxation Ruling TR 2001/8 provides the Tax Office's interpretation of the results test. The ruling states that the results test is based on the traditional criteria for distinguishing independent contractors from employees. The table below, which is extracted from TR 2001/8, states the factors that are relevant in making the distinction:

Factor	**Explanation**
The contractual obligations	An independent contractor enters into a contract for a specific task or specific tasks
How the work is performed	The independent contractor maintains a high level of discretion and flexibility as to how the work is performed. However, the contract may contain precise terms as to materials used and methods of performance and still be one for a result.
Risk	An independent contractor stands to make a profit or loss on the task. They bear the commercial risk. The independent contractor bears the responsibility and liability for any poor workmanship or injury sustained in performance of the task. Often an independent contractor would carry their own insurance and indemnity policies.
Tools and equipment	An independent contractor provides the asset, equipment and tools, if any, necessary for the work.
Hours of work and place of work	An independent contractor may set their own hours of work, or place of work, depending on the contract or the nature of the work.
Leave and other entitlements	A contract for a result usually does not contain leave provisions, or allowances.
Payment	Payment to an independent contractor is often based upon performance of the contract rather than being paid a hourly rate, piece rates or award rates.
Expenses	An independent contractor usually incurs their own expenses.
Appointment	An independent contractor is likely to advertise their services to the public at large, and the contract for a result is often the direct result of this activity.
Termination	An independent contractor is contracted to complete a set task. The payer may only terminate the contract without penalty where the worker has not fulfilled the conditions of the contract. The contract usually contains terms dealing with defaults made by either party.
Delegation	An independent contractor may delegate all or some of the tasks to another person, and may employ other persons.

Directors beware

The Federal Court has held that six payments made by a company prior to a Deputy Commissioner of Taxation filing an application for the winding up of the company on the ground of insolvency were voidable transactions pursuant to s 588FE of the *Corporations Act 2001*: *Hurricane Formwork Pty Ltd (in liq) v FCT* [2009] FCA 33.

The payments were made between May 2005 and June 2005. Based on an examination of the company's financial statements for the income years ended 30 June 2002, 2003, 2004 and 2005, the liquidator formed the opinion that the company was insolvent at the time the payments were made. The liquidator's opinion was reiterated in an affidavit. The Court gave regard to the affidavit and was satisfied that the company was insolvent at the time the payments were made. In doing so, the Court ordered the Commissioner to repay the company an amount equal to the payments pursuant to s 588FF of the Corporations Act.

Having made an order under s 588FF, the Court was satisfied an amount of the payments which related to the company's PAYG withholding obligations fell within the scope of s 588FGA of the Corporations Act. Therefore, the Court also ordered that the directors of the company (at the time the payments) to indemnify the Commissioner, an amount equal to the PAYG withholding obligations, in respect of any loss or damage resulting from the s 588FF order.

Corporations Act

Broadly, s 588FF gives a court the ability to set aside voidable transactions, which are prescribed in s 588FE, provided that the transaction was entered into within a particular time prior to the appointment of a company's liquidator.

Upon an application by a company's liquidator, a court may make one or more orders if it is satisfied that a transaction of the company is voidable because of s 588FE. These orders include:

- an order directing a person to pay to the company an amount equal to some or all of the money that the company has paid under the transaction;
- an order directing a person to transfer to the company property that the company has transferred;
- an order requiring a person to pay to the company an amount that fairly represents some or all of the benefit that the person has received because of the transaction; and
- an order releasing or discharging (wholly or partly) a debt incurred, or a security or guarantee given, by the company under or in connection with the transaction.

Where a court makes an order under s 588FF against the Commissioner, each person who was a director of a company when a payment was made may be liable to indemnify the Commissioner in respect of any loss or damage resulting from the order if the payment of a type prescribed in s 588FGA(1). The prescribed payments include:

- a payment paid under a liability created by notice under s 222AHA of ITAA 1936; and
- a payment paid under Subdiv 16-B of the *Taxation Administration Act 1953* (which relates to PAYG withholding).

A director can rely on the defences to s 588FGA contained in 588FGB, which are similar to the defences of insolvent trading contained in s 588H. It is important to note that while the director can rely on the defences, these defences must be proven in a court. These defences include:

- the director had reasonable grounds to expect, and did expect, that the company was solvent at the time of making a payment and would remain solvent even if it made the payment;
- the director had reasonable grounds to believe, and did believe, on the basis of information provided by a competent and reliable person that the company was solvent at the time of making a payment and would remain solvent even if it made the payment;
- the director because of illness or for some other good reason did not partake in the management of the company at the payment time;
- the director had taken all reasonable steps to prevent the company from making the payment or there were no such steps the director could have taken.

In ascertaining whether the director took a reasonable course of action to prevent the payment, a court will have given regard to the following matters (but not limited to):

- any action the director took to appointing an administrator for the company; and
- when that action was that; and
- the results of that action.

‘Blackhole’ Expenses

In ATO ID 2009/6, the Tax Office expresses the view that a taxpayer cannot deduct, under s 40-880 of ITAA 1997 (commonly referred to as ‘blackhole’ expenses), the balance of any undeducted qualifying expenditure for an income year in which it stops carrying on the business to which the expenditure relates.

Facts

During the 2005/06 income year, a corporate taxpayer incurred capital expenditure that qualified for a deduction under s 40-880. This section allows a taxpayer to deduct 20% of qualifying expenditure over a period of five years.

However, the taxpayer ceased its business to which the expenditure related to during the 2008/09 income year. The taxpayer proposed that the business be wound up in the income year.

Reasons for decision

Based on an interpretation of s 40-880, the Commissioner’s view is that there is no basis in the section to allow a deduction for an amount greater than 20% of the qualifying expenditure for any income year or to alter the timing of that deduction.

Therefore, if a taxpayer winds up its business during an income year, it will be unable to claim a deduction for any unused deductions in subsequent income years as the taxpayer that incurred the qualifying expenditure will not exist for any part of those income years.

Business related deductions

Section 40-880 of ITAA 1997 provides a systematic treatment for certain business expenditure of a capital nature (commonly referred to as ‘blackhole’ expenses) incurred on or after 1 July 2005. Broadly, expenditure relating to the establishing, expanding or ceasing will qualify for a deduction under this section, provided:

- it is not taken into account in some way elsewhere in the tax law; and
- it is not expressly made non-deductible (other than because the expenditure is of a capital nature).

The expenditure is deductible on a straight-line basis over five years, that is, 20% of the expenditure each year.

However, the section is silent on whether a taxpayer is able to bring forward any undeducted expenditure when the taxpayer winds up its business. The section is also silent on whether the taxpayer is able to ‘bank’ any unused deductions to a future income year when it recommences business. The Commissioner’s views in ATO ID 2009/6 indicate that any unused deductions will be lost if the taxpayer winds up its business.

An alternative argument is that a taxpayer can choose to cease its business but not formally wind up until any s 40-880 deductions are claimed. However, if the taxpayer is not deriving any assessable income, the deductions are carried forward as losses. Therefore, the deductions are still ‘lost’. Note that any s 40-880 deductions are not transferred, ie the deductions remain with the taxpayer.

Pension Drawdown Relief

In an announcement released by the Treasurer and the Minister for Superannuation and Corporate Law, they announced that the Government will temporarily suspend the minimum drawdown requirements for account-based annuities and pensions for the second half of the 2008/09 income year (ie 1 January 2009 to 30 June 2009).

According to the announcement, the measure responds to concerns that meeting the minimum drawdown amount in 2008/09 will mean having to sell investments assets and realise losses in a depressed market. The measure will also respond to concerns that the minimum drawdown requirement was set based on asset values as at 1 July 2008, when equity values were higher.

The Minister said the temporary suspension will occur through a 50% reduction in the minimum payment amount for 2008/09. For those people who have already taken half of the current minimum payment for 2008/09, the annual nature of the minimum payment rules means that a further payment will not be required until the end of the 2009/10 year. The temporary suspension of the minimum payment requirement will apply to:

- account-based annuities and pensions;
- allocated annuities and pensions;
- account-based and allocated pensions payable from retirement saving accounts; and
- market-linked (term allocated) annuities and pensions.

The relief is also available to individuals who are receiving a transition to retirement pensions, provided the pensions are paid through one of the pension products stated above.

Minimum standards for pensions and annuities

Since 1 July 2007, new minimum standards apply for private superannuation pensions and annuities under the Superannuation Industry (Supervision) Regulations 1994 (the SIS Regs). Under the new standards set out in subregs 1.05(11A), 1.06(9A) and Sch 7 of the SIS Regs, pensions and annuities effectively fall into two classes:

- account-based income streams — those where there is an account balance attributable to the recipient; and
- non-account based income streams — those where there is no attributable balance (eg traditional lifetime and life expectancy income streams generally offered by life insurance companies). However, this category can no longer commence from a self-managed superannuation fund.

Broadly, the new minimum standards for account-based pensions and annuities require:

- payments of a minimum amount to be made at least annually: reg 1.07D of the SIS Regs;
- no provision to be made for an amount to be left over when the pension ceases; and
- the pension can only be transferred on the death of the pensioner (primary or reversionary as the case may be) to one of their dependants or cashed as a lump sum to the pensioner's estate.

Minimum payment rules

Account-based pensions and annuities must meet the minimum payment rules set down in Sch 7 of the SIS Regs. The payment rules specify minimum annual limits only. No maximum annual payments apply, except for transition to retirement pensions. Transition to retirement pensions have a maximum annual payment limit of 10% of the account balance at the start of each financial year (until a 'nil' cashing restriction is satisfied: reg 6.01(2) and Sch 1 of the SIS Regs).

Note that if the commencement day of a pension is on or after 1 June in a financial year, no payment is required to be made for that financial year.

Non account-based products can be assessed against the minimum payment rules in Sch 7 or, alternatively, against a set of defined criteria set out in SIS regs 1.05(11A)(b)(ii) and 1.06(9A)(b)(ii). Lifetime pensions and annuities which meet the standards of existing subregs 1.05(2) or 1.06(2) are also deemed to meet the new standards.

The provisions relating to annuities and pensions which commenced before 20 September 2007 are maintained in the regs 1.05(1A) and 1.06(1A) of the SIS Regs. Furthermore, annuities and pensions which commenced in the period between 1 July 2007 and 20 September 2007 are able to meet either the new standards or the existing standards.

The new provisions also clarify that the meaning of 'annuity' or 'pension' includes a complying life expectancy or market-linked income stream (MLIS) that commenced on or after 20 September 2007 from the commutation of another complying income stream, provided the new income stream also meets the new standards.

In addition, where a pension or annuity recipient dies on or after 1 July 2007, the ability to transfer the income stream to another person is prevented where the person is ineligible to be paid a benefit in that form under 6.21(2A) of the SIS Regs, eg a non-dependant of the deceased pensioner.

Minimum annual payment amounts

For a pension or annuity with an account balance attributable to the beneficiary, the minimum annual payment amount (or drawdown amount) is calculated according to the formula in Sch 7 to the SIS regs (rounded to the nearest $10):

account balance x percentage factor

The ‘account balance’ means the value of the pension or annuity on 1 July in the financial year in which the payment is made (or the commencement day if the pension or annuity commenced in that year). If the amount of the pension account balance is less than the withdrawal benefit to which the beneficiary would be entitled if the pension were to be fully commuted, the account balance is the amount of the withdrawal benefit. For non account-based products, the purchase price (total amount paid as consideration) is used instead of the account balance.

The ‘percentage factor’ is specified in the table to Sch 7 of the SIS Regs (see below) according to the age of the beneficiary on 1 July in the financial year in which the payment is made (or on the commencement day if the pension or annuity commenced in that year). In the year of first commencement of the pension or annuity (on a day other than 1 July), the percentage factor must be applied proportionately to the number of days in the financial year that include and follow the commencement day.

Age of beneficiary	Minimum annual drawdown (%)
0–64	4
65–74	5
75–79	6
80–84	7
85–89	9
90–94	11
95+	14

Thomson Reuters example

Joe was aged 61 as at 1 July 2008. Therefore, his minimum annual drawdown percentage for the 2008/09 income year is 4%.

Joe’s account-based pension had an asset value of $250,000 at the start of the 2008/09 income year.

Scenario 1

On 10 October 2008, Joe withdrew $10,000 from his pension. As the amount withdrawn was the minimum annual drawdown required ($250,000 x 4%), he is not affected by the Government’s announcement.

Scenario 2

Joe draws his pension on a monthly basis. As at 1 January 2009, he has withdrawn 50% of the required minimum annual drawdown amount. Therefore, Joe can choose not to draw a pension for the second half of the 2008/09 income year because of the temporary suspension measure.

Scenario 3

Joe draws his pension on an annual basis, which occurs on 30 June. The temporary suspension measure means that he has the option of drawing $5,000 from his pension (which is 50% of the minimum drawdown requirement) instead of $10,000.

FBT and Victorian Bushfires Appeal

In a media release, the Assistant Treasurer announced that the Government will amend the FBT law from the beginning of the 2008/09 FBT year (ie from 1 April 2008) to ensure that donations to the Victorian bushfires appeal made under salary sacrificing arrangements do not result in an employer incurring an FBT liability.

The Assistant Treasurer said that to facilitate the collection of donations to those affected by the 2009 Victorian bushfires, a number of employers have entered into salary sacrificing arrangements with their employees. He said these arrangements may result in a potential FBT liability under the current FBT provisions. In contrast, donations collected through an employer's Workplace Giving arrangement are made from an employee's post-tax dollars and do not result in an FBT liability.

FBT implications

Potentially, an FBT liability arises because of the operation of s 148(2) of the *Fringe Benefits Assessment Act 1986* (the FBTAA). Broadly, the subsection states that the FBTAA may apply to the provision of a benefit where the benefit is provided to a third party, that is, the recipient of the benefit is neither an employee of the employer nor an associate of the employee. This is achieved by deeming the third party as an associate.

It is important to note that if an employee who enters into an effective salary sacrifice arrangement to facilitate donations to the Victorian bushfires (or be it any charity organisation) the employee may be denied a tax deduction for the donations. This is because an employer will be entitled to a deduction under s 8-1 of ITAA 1997 for the total outlay the employer incurs for providing the donations.

In addition, s 8-1 states that a loss or an outgoing is deductible to the extent that it is incurred in gaining or producing a taxpayer's assessable income, or in carrying on a business for the purposes, provided that the loss or outgoing is not private or capital in nature, relates to the deriving of exempt income or a provision of the legislation denies the deduction.

Tax Practice Update

Tax Laws Amendment (2008 Measures No 6) Bill 2008

The Tax Laws Amendment (2008 Measures No 6) Bill 2008 was passed by the House of Representatives on 25 February 2009 with several Government amendments designed to provide assistance to individuals and communities affected by the Victorian bushfires and North Queensland floods. In brief, the amendments made to the Bill:

- amend ITAA 1936 and ITAA 1997 to make the income recovery subsidy exempt from income tax, and to ensure the subsidy is not included in separate net income for the purposes of calculating an entitlement to certain tax offsets — applies to the 2008/09 income year;
- amend ITAA 1997 to provide that the Treasurer may declare an event as a disaster for the purposes of establishing Australian disaster relief funds. The declaration of a disaster by the Treasurer will allow Australian disaster relief funds to receive tax deductible donations, and provide money for the relief of people in Australia in distress as a result of the disaster — applies to the 2008/09 income year and later income years;
- specifically list the 2009 Victorian Bushfire Appeal Trust Account as a deductible gift recipient in Div 30 of ITAA 1997 — also applies to the 2008/09 income year and later income years.

As originally introduced on 3 December 2008, the Bill contains amendments concerning:

- CGT provisions relating to roll-overs for corporate restructures in Subdivision 124-M of ITAA 1997;
- collection provisions in Division 263 of Schedule 1 to the *Taxation Administration Act 1953*;
- late payment offset for superannuation guarantee contributions in section 23A of the *Superannuation Guarantee (Administration) Act 1992*; and
- technical corrections to taxation laws, which include the *A New Tax System (Goods and Services Tax) Act 1999* and the *Fringe Benefits Tax Assessment Act 1986*.

At the time of publication, the Bill is awaiting Royal Assent.

Draft legislation — temporary investment allowance

Treasury has released draft legislation and a draft Explanatory Memorandum on the proposed Small Business and General Business Tax Break. The tax break was first announced by the Government in its Nation Building and Job Plans released on 3 February 2009. The tax break is not in addition to the proposed temporary investment allowance, which was announced by the Government in December 2008, but rather subsumes the allowance.

Broadly, the tax break will amend the income tax law to provide a temporary bonus deduction for new, tangible depreciating assets and new expenditure on existing assets. This will be achieved by inserting a new Div 41 into ITAA 1997.

Taxpayers will be able to claim a bonus deduction at either a rate of 10% or 30%, provided the conditions of the tax break are satisfied. The conditions are:

- the investment must occur between 13 December 2008 and 31 December 2009 (inclusive);
- the investment must be for eligible assets;
- the expenditure on the investment meets the new investment threshold;
- the assets must be used in Australia; and
- the time at which the assets start to be used and/or the economic benefit of the improvement to an asset is realised before 31 December 2010.

The tax break is in addition to the depreciation deductions available under the capital allowance provisions of Div 40 of ITAA 1997.

Investment time

One of the eligibility requirements of the tax break is that the investment must occur between 13 December 2008 and 31 December 2009 (inclusive). To this extent, the draft legislation introduces the concept of an 'investment time', which is when an investment is considered to have been made.

If an amount is included in an asset's first element of cost (worked out at the time the taxpayer begins to hold the asset), the investment will be the point the taxpayer has:

- entered into a contract to start or hold the asset; or
- started to construct the asset; or
- started to hold the asset in some other way.

If an amount is included in an asset's second element of cost (because the amount relates to an economic benefit that contributes to bringing the asset to its new condition and/or location), the investment time will be the point in time the taxpayer has entered into a contract for that economic benefit or commenced construction of that economic benefit.

An integrity rule will be introduced to ensure that the taxpayers cannot circumvent the investment time requirement by 'refreshing' a contract entered into on or before 12 December 2008.

Eligible assets

The bonus deduction is available for new investment in tangible depreciating assets for which a deduction is available under Subdiv 40-B. Alternatively, the bonus deduction is also available on new expenditure on existing assets.

An asset is 'new' for the purposes of the bonus deduction if the asset has never been installed ready-for-use before either by a taxpayer or another entity for any purposes, anywhere prior to 12 December 2008. Therefore, second-hand assets are not eligible for the bonus deduction.

However, an asset will still be considered to be 'new' if it has only been used for the purposes of reasonable testing and trialling (by any entity). The example below is adapted from the draft Explanatory Memorandum.

> *On 20 March 2009, Gladys acquires a car to use in her mobile computer repair business. She uses the '12% of original cost' method to work out her car expenses deductions for the 2008/09 income*

year. The car was a 'demonstrator' vehicle. Providing any prior use of the car only amounted to reasonable testing and trialling, the car will still be considered to be 'new' for the purposes of the bonus deduction.

The term 'depreciating asset' is defined in s 40-30. Land, trading stock and intangibles are excluded from the definition of a depreciating asset and therefore not eligible for the bonus deduction.

Note that while s 40-30 rules some intangible asset back into the definition of a depreciating asset, those exceptions do not apply to the bonus deduction. That is, all intangible assets are ineligible. By way of example, software will be excluded because it is an intangible asset.

Taxpayers claiming deductions for assets under the following subdivisions will not be entitled to claim the bonus deduction:

- Subdiv 40-F (depreciating assets involved in primary production such as water conservation facilities and horticultural plants);
- Subdiv 40-G (capital expenditure of primary producers and other landlords); and
- Subdiv 40-J (capital expenditure for the establishment of carbon sink forests).

Research and development

Tangible assets used exclusively for research and development (R&D) purposes may be eligible for the bonus deduction, albeit the assets receive deductions under the R&D provisions contained in ITAA 1936.

Cars

Cars will be eligible for the tax break, provided taxpayers are using the following methods in determining their car expenses:

- 'one-third of actual expenses' method;
- '12% of original value' method; and
- log book method.

Taxpayers who use the 'cents-per-kilometre' method will be precluded from claiming the bonus deduction. The amount of bonus deduction will be limited to the car cost limit ($57,180 for 2008/09).

[***Thomson Reuters note***: Taxpayers who lease luxury cars will be able to claim the bonus deduction because Item 1 in s 40-40 states that it is a lessee who is the holder of a luxury car. That is, the lessee is the entity eligible to claim a deduction for depreciation on the car.]

Small business entities

Small business entities will be eligible for the bonus deduction notwithstanding that the entities elect to use the capital allowance concessions contained in Subdiv 328-D of ITAA 1997. It is the fact that an asset is one for which a deduction is available under the core provisions of Div 40 that matters, that is, regardless of whether an entity 'opts out' of Div 40 for capital allowance purposes.

Lease assets

Eligible assets held under a lease will still qualify for the bonus deduction. The bonus deduction will be claimed by the entity that is entitled to claim a capital allowance deduction on an eligible asset.

Note that s 40-40 identifies the circumstances under which an entity can become a holder of a depreciating asset.

New investment threshold

The 'new investment threshold' will depend on whether a taxpayer is a small business entity or a general business:

- for a small business entity, the threshold is $1,000 or more; and
- for a general business, the threshold is $10,000 or more.

The investment threshold operates on a per asset basis. That is, investments in different assets cannot be amalgamated for the purpose of meeting the threshold. However, multiple amounts (which are referred to as 'recognised new investment amounts') in relation to a same asset can be combined for the purposes of meeting the threshold.

For an amount to be a recognised new investment amount in an income year, the amount needs to be included in an asset's cost base between 13 December 2008 and 31 December 2009 (inclusive). The asset's cost base is defined in Subdiv 40-C and consists of two elements. The first element is worked out at the time a taxpayer begins to hold the asset which is generally the amounts that the taxpayer has paid. The second element is amounts that the taxpayer has paid to bring the asset to its present condition.

The following example, which is modified from the draft Explanatory Memorandum, explains how a taxpayer calculates the recognised new investment amount.

> *Gail, a small business entity, decided to purchase a new oven to improve the energy efficiency of her cafe's kitchen. She enters into a contract with the supplier of the oven on 10 August 2009 for $4,500, which does not include installation. The $4,500 is included in the asset's first element of cost.*
>
> *An electrician charges Gail $500 to install the oven on 17 August 2009. Because Gail has already started to hold the asset, the installation cost is included in the asset's second element of cost. Once installed, Gail's oven has a total cost of $5,000.*

In determining whether the investment threshold has been met, taxpayers are required to compare the amount of their recognised new investment amounts for an asset for an income year against the relevant threshold. An amount can be a recognised new investment amount in more than one year, provided the bonus deduction has not been previously claimed for that amount. The effect of this is that recognised investment amounts below the threshold can be carried over to the following income year.

New expenditure on existing assets

The bonus deduction also applies to new expenditure on assets acquired prior to 13 December 2008, provide that expenditure is of a capital nature. New expenditure incurred on existing assets are treated in the same manner as amounts relating to investment in new assets.

However, if new expenditure on an existing asset results in a new asset being created (for eg, the asset is split into two or more assets), an amount included in the first element of cost for the new asset created will not be eligible for the bonus deduction where the amount was for an investment made before 13 December 2008 or where the bonus deduction had already been claimed on that amount.

Rate of tax bonus

The income year that the bonus deduction can be claimed and the rate to be used in calculating a taxpayer's deduction will depend on when the new investment is undertaken and when the new or modified asset is put to use.

The bonus deduction is to be claimed by the holder of the asset as determined by s 40-40.

The table below modified from the draft Explanatory Memorandum summarises the key dates relating to the different rates at which the tax break could be claimed, if all conditions are met.

Installed by	**New investment by**	
	30 June 2009	**31 Dec 2009**
30 June 2009	30% in 2008/09	
30 June 2010	30% in 2009/10	10% in 2009/10
31 December 2010	10% in 2010/11	10% in 2010/11

A taxpayer will not be required to apportion the bonus deduction between the business and non-business uses of an eligible asset. However, the taxpayer must be able to demonstrate that at the time it started to use the asset or had it installed ready for use, the asset was to be used in Australia and for the principal purpose of carrying on its business (the 'purpose test').

The bonus deduction will not be clawed back for any subsequent non-business use of the asset or if the asset is subsequently disposed of provided that the purpose test was genuinely satisfied at the time the taxpayer started to use the asset or had it installed ready for use. (Note that neither the draft legislation nor the draft Explanatory Memorandum provide any guidance on how the purpose test can be satisfied, including the definition of principal purpose.)