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Practice Update

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FEBRUARY 2010

ATO comes down hard on monies owed to 'bucket' companies

Editor: By way of background, for many years now the Tax Office has accepted that trusts could make distributions to private companies but not actually have to pay the amount. These were called unpaid present entitlements.

These amounts were taxed in the hands of the company and the trustee was able to continue to use the funds for the benefit of all the beneficiaries.

The Tax Office has now reversed that longstanding view and issued a draft ruling that many see, at the very least, as contentious.

New draft ruling

The new draft ruling means that, generally speaking, where a trust does not physically pay out a distribution to a private company, the Tax Office will deem that a loan has been provided by the private company to the trust.

Where that occurs, the amount owing under the 'newly created loan' may be treated as a dividend to the shareholders of the company.

"Carve-out" for existing unpaid distributions

However, distributions made before 16 December 2009 are not affected by the ATO's new interpretation, and will therefore not generally be treated as loans (or dividends).

Editor: We have not gone into the technical side of this issue which is quite complicated to the uninitiated.

However, while we will be in contact with clients over the next short while, we recommend that any clients

who may be concerned with how this draft ruling could affect them should contact our office.

For what it's worth, this is a draft ruling and it is possible, but not likely, that the ATO will change its view. In addition, the Tax Office's position has yet to be tested in Court.

Declare offshore income or wear the consequences

The Tax Commissioner has announced that the net is closing in on tax havens and has made a new offer for people who may not have declared all income from offshore activities.

"This is a chance for people with undeclared income, for example interest earned offshore, to contact the Tax Office and sort out their affairs. The offer is open until 30 June 2010."

The Tax Office made a similar offer in 2007 which produced more than 3,000 disclosures with a total of over \$306 million in omitted income.

Compared to 2007, the new offer increases the shortfall penalty from 5% to 10% where a person's additional income from offshore activities is more than \$20,000 in a tax year.

Those with additional taxable income of \$20,000 or less in a tax year will not have to pay a shortfall penalty for that year.

People can now approach the Tax Office anonymously for an indication of whether it would initiate an investigation to determine whether there is a potential breach of the criminal law.

Defamation payout not assessable

The Full Federal Court has held that damages awarded to a company and calculated on a 'lost profits basis' were not assessable.

The taxpayer company was awarded for \$844,624 in damages against the defendant for publishing false and misleading statements as to the nature and quality of laser eye surgery services provided.

The Court held that even though the damages were based on the anticipated net income that the taxpayer had lost from surgical procedures not performed as a result of the defamatory publications, the damage was to the corporation's reputation which is part of what enables it to earn money.

An injury to that reputation diminishes its capacity to earn because it reduces the corporation's ability to induce others to do business with it.

The Court said that an award of damages for that injury is therefore no different from an award for the loss of an arm or any other injury impairing earning capacity.

Five new Tax Alerts

In a rush of blood to the head, the ATO has issued five tax alerts on 'dodgy' arrangements.

- Life insurance bonds issued by tax haven entities – the alert warns taxpayers to be cautious about investing in life insurance policies issued from insurance companies based in tax havens, such as Vanuatu.
- Offshore super trust arrangements – trust structures that masquerade as superannuation funds to avoid tax on money shifted into Australia.
- Sham mortgage arrangements – promoted as 'mortgage management plans' which promise to help home owners repay their home loan sooner and claim tax deductions to which they are not entitled.
- R&D schemes – this alert warns people to be cautious of investment schemes that abuse the research and development (R&D) tax offset.
- 'Option' arrangements – that attempt to artificially create up-front deductions whereby an employer makes a 'deductible' cash contribution to a trust which then pays it back to acquire options from the employer.

ATO appeals case – education expenses/Youth Allowance

Editor: Towards the end of 2009, in what is seen as a landmark decision, the Full Federal Court held that a taxpayer, who received a Youth Allowance as a university student, was entitled to a tax deduction for her education expenses.

The Tax Office has now advised that it has sought special leave to appeal against this decision (the Anstis case) in the High Court.

Until the matter is resolved by the High Court, the Tax Office will continue to apply its view that education expenses are not deductible for tax purposes against various Commonwealth educational assistance schemes.

Goods taken from stock for private use

The Tax Office has issued a new tax determination which estimates of the value of goods taken from trading stock for private use by taxpayers in certain industries for the 2009/10 income year.

Editor: Clients who may be able to justify a lower value for goods taken from stock than that shown in the schedule should speak to us.

The Schedule for the 2009/10 income year is:

Type of Business	Adult/child over 16 \$	Child 4-16 years \$
Bakery	1,130	565
Butcher	760	380
Restaurant/cafe (licensed)	3,860	1,540
Restaurant/cafe (unlicensed)	3,080	1,540
Caterer	3,330	1,665
Delicatessen	3,080	1,540
Fruiterer/greengrocer	810	405
Takeaway food shop	2,920	1,460
Mixed business (includes milk bar, general store and convenience store)	3,680	1,840

Please Note: Many of the comments in this publication are general in nature and anyone intending to apply the information to practical circumstances should seek professional advice to independently verify their interpretation and the information's applicability to their particular circumstances.