Practice Update

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SEPTEMBER 2008

ATO's Compliance Program: 2008/09

The Tax Commissioner, Michael D'Ascenzo, has released the ATO's Compliance program for 2008/09, which lets the community know where they will focus their attention and the action they will take in the coming year, "so people know which areas of risk they should avoid".

The ATO will focus on (among other things):

- income tax;
- tax havens;
- dodgy tax schemes;
- wealthy individuals; and
- the cash economy.

Their priorities for individual taxpayers include:

- a focus on capital gains from the sale of property, shares and other assets;
- expanding their review of the activities of senior executives and directors; and
- monitoring work-related expense claims, particularly out-of-pattern claims for self-education, car and travel expenses.

More industry benchmarks, data matching, and cash economy audits

The Commissioner also advised that the ATO will:

- work with more industries to develop benchmarks (these benchmarks allow taxpayers to compare their performance to the rest of their industry and check that their tax records reflect their business practices);
- increase their data matching to more effectively identify and target people who may have under-reported income or over-claimed expenses; and
- undertake more than 5,000 cash economy audits or reviews.

Resident minors' 2008/09 tax-free threshold

The increase in the low-income tax offset to $1,200 in 2008/09 (from $750 in 2007/08) effectively means that minors (i.e., persons under the age of 18) can receive $2,666 tax-free in the 2008/09 year (e.g., distributions from discretionary trusts).

The table below shows that, without the offset, once a minor's income exceeds $1,308, the entire amount of 'unearned income' is taxed at 45%. *Note that this does not apply to some receipts, e.g., salary and wages.*

However, applying the low-income tax offset of $1,200 means that no income tax will be payable unless the minor's taxable income exceeds $2,666, i.e., $1,200 divided by 0.45 = $2,666.66

2008/09 Resident Minors' Rates of Tax Unearned Income (Div.6AA)

Div.6AA Income $	Tax payable $
0 – 416	Nil
417 – 1,307	66% of excess over $416
1,308+	45% of the entire amount

'In-house' computer software – four year effective life

Editor: The Government announced in the Budget that it would be increasing the period over which taxpayers write off depreciable in-house software for tax purposes from 2.5 years to 4 years.

Although the legislation implementing this change has only recently become law, the new effective life applies to software that the taxpayer acquired under a contract entered into on or after 7:30 pm on 13 May 2008, or which the taxpayer otherwise started developing or holding on or after that time.

Expenditure on 'in-house computer software' is a taxpayer's expenditure on acquiring, developing or having someone else develop computer software which is mainly used by the taxpayer.

This could include off-the-shelf software acquired for use by the taxpayer.

Expenditure on 'in-house computer software' will continue to be depreciated on a straight line basis.

Self Managed Super Funds (SMSFs): Investment rules

The ATO has recently released two rulings, which consider some of the important investment rules that set out how the ATO expects SMSF trustees will use superannuation money.

Editor: Because the superannuation laws allow for very concessional tax treatment of money invested in a superannuation environment, there are very strict rules about what trustees can and can't do.

Two of these investment rules are:

- The **'sole purpose test'** (i.e., basically, the SMSF must be run solely to provide benefits on members retirement or death); and
- The prohibition on SMSFs using fund resources to provide **financial assistance** to a member, or a relative of a member.

The rulings provide a number of examples regarding these two investment rules, three of which are reproduced below.

Example 1 – Separately negotiated benefit: more than an incidental benefit
An SMSF trustee invests in a non-related company that owns a block of holiday apartments at a popular tourist destination.

The members of the SMSF holiday in this area every year and prior to making the investment owned a separate holiday house nearby.

The trustee, when undertaking the investment, negotiated for members of the SMSF to be able to stay at the apartments for free. This is not a standard feature of the investment.

In return, the SMSF was required to accept a reduction in dividends payable by the company.

The members of the SMSF sell their holiday house immediately after the SMSF makes the holiday apartment investment.

The separate negotiation of the benefit, which materially affects the return on the SMSF's investment, demonstrates that the benefit is purposeful and not incidental.

The facts reveal that the SMSF is being maintained for a purpose of providing benefits other than those specified by the superannuation law and, therefore, indicate a contravention of the **sole purpose test**.

Example 2 – Selling an asset for less than market value
Robert is a trustee and member of an SMSF. The SMSF's portfolio of assets includes a block of land located in an inner city suburb where land values have risen significantly in recent years.

Robert sells the asset to his son for $210,000. Two months prior to the sale, the block of land was independently valued at $300,000.

The sale of the land by Robert to his son for less than market value contravenes the **prohibition on SMSFs providing financial assistance to a relative of a member** (*Editor: And probably the sole purpose test, as well*).

Example 3 – Purchase of an asset by an SMSF for greater than market value
Andrew is a member and trustee of an SMSF. Andrew needs to raise $100,000 for personal reasons.

He owns a block of land that qualifies as business real property and has been independently appraised as having a market value of $80,000.

As trustee of the SMSF, Andrew agrees for the SMSF to purchase the land for $100,000.

The purchase of the land by Andrew as trustee of the SMSF for greater than its market value is the giving of financial assistance to himself (a member) and therefore contravenes the superannuation law.