



## Extend the festive cheer (but in a tax- efficient way)

The festive season is here again. As with other years it is always brimming with the spirit of giving. The list of practical ways in which Australians spread goodwill is as endless as a Christmas wreath. The ATO also gets into the spirit of the season, but of course feels required to set some limits.

### About this newsletter

Welcome to Taxplanners monthly newsletter update. We hope you find the content informative. If you would like to discuss how any of the content could affect you, your business or retirement savings, please do not hesitate to contact us on the details below.

**T: 1300 000 TAX (1300 000 829)**

**E: [info@taxplanners.com.au](mailto:info@taxplanners.com.au)**

Content in partnership with **Taxpayers AUSTRALIA INC**

### When are donations deductible?

A charitable donation is only tax deductible if it meets the requirements in the relevant legislation. In brief, the rules allow a taxpayer to claim a deduction for a “gift” or for a “contribution” that satisfies certain conditions. While the deductibility criteria do vary, the common requirement across all types is that the recipient must be a “deductible gift recipient” (DGR).

A DGR is a non-profit entity that is legally entitled to receive tax-deductible donations. A DGR must be explicitly registered (or legislated) as such.

Extending the festive cheer *cont***Common donations**

Common of methods of giving include donating cash, being involved in fund raising events, taking part in a workplace giving program, donating goods, volunteering or offering professional services for free.

As noted, different conditions apply depending on the donation type – for example, some gifts must be over \$2 in value, in other cases, there is a need to obtain a valuation (if goods are provided) and/or be purchased within the past 12 months.

Consider these examples:

**Donating cash**

Stephen's son attends the local school. The school has launched a Christmas appeal for donations to fund a renovation. The school as a whole is not a DGR.

Stephen donates \$500 in cash to the school's building fund. However the building fund itself is endorsed as a DGR, so Stephen can deduct his gift of \$500.

Stephen also donates \$50 to his son's school cricket team for new equipment. The cricket team is not a DGR (and neither is the school), so Stephen cannot deduct his gift of \$50.

**Donating goods**

Rosanna buys a new washing machine at the Boxing Day sales. Rosanna decides to donate her old washing machine, which she purchased four years ago, to a large charity (a DGR).

From online listings of similar secondhand washing machines, she estimates that her old machine is worth approximately \$300.

Rosanna cannot deduct the \$300 market value of the gift. It does not meet any of the alternative deductibility conditions, which are that:

- it is a gift of cash, or
- it was purchased within the last 12 months, or
- Rosanna can obtain an ATO valuation of more than \$5,000.

**Volunteering**

Marcus takes a week off work for Christmas and New Year. During that week, he spends each morning volunteering at a soup kitchen operated by a DGR. He drives to and from the soup kitchen. He

pays for petrol for the week and for parking each morning.

Marcus cannot deduct his expenditures on petrol and parking. The payments are not gifts of cash or property that is actually given to the DGR, even though the expenditures enable him to fulfil his volunteer duties.

Marcus observes that the kitchen has insufficient cooking pots. He purchases a new boxed set of pots for \$200 and donates it to the DGR's representative at the soup kitchen the next day. The market value of each individual piece is more than \$2.

Marcus can deduct \$200 for his gift of boxed cooking pots that he makes to the DGR. It was purchased within the last 12 months and the value is not less than \$2 (whether considered as a set or as individual items).

**Offering professional services for free**

Owen is an IT contractor operating as a sole trader. He hears about a local charity (a DGR) that is replacing its outdated computer systems.

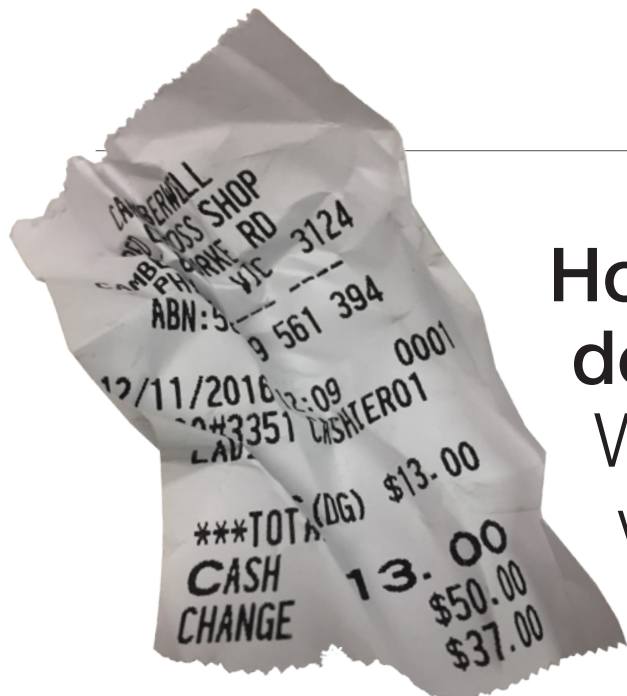
Owen helps the charity with its project during his Christmas break, using his IT expertise. He does not charge the charity any fees for his services. His contracting business receives no advertising, recognition or other benefit from his volunteer work.

Owen uses the same specialised skills and knowledge in his paid contract work. He estimates that his donated services would have earned him about \$2,000 in contract income had he undertaken an equivalent project for a paying client.

However Owen cannot deduct the notional foregone income of \$2,000 as a gift under tax legislation. The \$2,000 is neither cash nor property that Owen gives to the DGR.

As a sole trader, Owen wonders whether he can claim the \$2,000 as a business deduction, since it represents the market value of his professional skills that he uses in his ordinary business activities. However he cannot make such a deduction as the \$2,000 is a notional loss only; it is not expenditure that Owen actually incurred.

Even if Owen did incur expenditures in his volunteer work (such as purchasing consumables), he would still be unable to claim the amounts. There is no connection between the expenditures and either the derivation of his assessable income or the carrying on of his business. ■



# Home office deductions: What substantiation will the ATO accept?

Home office expense claims are subject to the same general substantiation requirements as other deductions – that is, it is a requirement that records should be kept for at least five years.

But in practice, full compliance with the substantiation rules may be difficult. It may be simple to keep a receipt for a printer purchased for a home business, but not so easy to prove the deductible proportion of a specific utilities bill. So the ATO has provided some administrative guidelines to ease this burden.

## Proving business use proportion

The ATO will generally accept these three methods of calculating the business use proportion for a particular expense (in order of preference):

- Explicit evidence of business use – such as an itemised phone bill.
- Records of representative periods of use – such as a diary record spanning a four-week period (see below for details).
- A “reasonable estimate” – the ATO does not define this term, but the taxpayer must be able to demonstrate that such a component was “reasonably likely” under the circumstances.

## More about four-week representative records

### Claims exceeding \$50

The ATO requires a taxpayer to keep records for a four-week representative period in each income year in order to claim a deduction of more than \$50. The taxpayer can choose to keep records for longer than four weeks or to base their deduction on itemised bills (see above) for the entire year for a more accurate deduction.

The four-week record is merely the minimum amount of record-keeping that the ATO will accept. It is not a legal requirement to produce a time-limited representative record like the 12 week log book for car expense deductions. Remember to adjust the deduction for periods of leave taken.

According to one of its fact sheets, the ATO will look favourably upon evidence that the employer expects the taxpayer to work at home or make work-related calls. But be aware that employer expectation is not a legal requirement. Under legislation and taking into account common law covering work-related expenses, it is enough that the expenditure is incurred in the course of producing assessable income and is not private, domestic or capital in nature.

### Claims that are less than \$50

Claims of \$50 or less are not generally subject to substantiation checks (although it is not explicitly stated). This however only affects the substantiation of the amount, and does not change the fact that the relevant expense still has to be deductible under law.

Therefore it would be prudent for the taxpayer to be able to show that they had a reasonable basis for making the claim (for example, to keep evidence that some work was done at home during the year).

## Shared expenses

According to the ATO, an invoice in the name of one person is acceptable as evidence of incurred expenditure for more than one person. This may be relevant where spouses or rental accommodation housemates each do home-based work, using shared utilities.

If you need any assistance with the rules in relation to substantiation, contact this office. ■





# SMSFs need to prepare for the new transfer balance cap

Recent legislation introduced several superannuation rule changes. Among them is a new “transfer balance account”, which each recipient of a superannuation pension will be required to have. In other words, individuals receiving superannuation income stream benefits will need to keep such a transfer balance account.

The use of “accounts” for tax law purposes is not new. The best example, and a useful analogy, is the franking account that each company has. The franking account is used to track income tax paid by the company so that the company can pass to its shareholders the benefit of franking credits when a distribution is made. It does not actually record anything for accounting purposes, but merely tracks an income tax attribute (which is why it does not appear on any financial statements).

## Is there a limit?

Each individual receiving superannuation pensions will have a transfer balance account, which in general will be created when they start an account-based pension with all or part of their accumulated superannuation balance. But an important additional condition is that there is to be a cap placed on the total amount with which a pension can be commenced, with the cap for 2017-18 set at \$1.6 million (it will be indexed for later years). The start date for these new measures is July 1, 2017.

## Why the cap?

The ultimate purpose of introducing the transfer balance account cap is to limit the total amount of an individual's superannuation interests that receive an earnings tax exemption. While the transfer balance account mostly tracks how much superannuation savings an individual transferred into the retirement phase, it does not limit total transfers to the retirement phase. The transfer balance cap is used for this purpose.

However, the cap applies towards net transfers to the retirement phase and is not affected by earnings, losses or drawdowns that occur within the retirement phase. Note also that indexation of an individual's transfer balance cap is done on a proportional basis – only an unused portion of the transfer balance cap is indexed.

## What happens if the cap is breached?

In cases where there are excess funds above the cap placed into pension phase, the amount of excess will be required to be removed. Not only this, but notional earnings made on this amount will be taxed — at a rate of 15% for the first instance of a breach of the cap, but at 30% for subsequent breaches. Moreover, notional earnings are to be taxable regardless of whether the individual has rectified their breach and removed the notional earnings amount from the retirement phase. Contact this office if you would like to know more. ■



## Shopping for a “luxury” car?

## Beware of the luxury car tax

**Y**ou can judge whether a car is luxury or not, according to the government, if it costs more than \$64,132 for 2016-17. It's not an over-the-top price tag if you're considering true luxury, but it's enough to cop an extra tax.

### WHAT YOU NEED TO KNOW

The luxury car tax (LCT) kicks in after that threshold is reached, is been set at a rate of 33%, and applies to the amount that exceeds the \$64,132 threshold.

From a typical car buyer's point of view, where the tax is payable it will already be factored into the price quoted by a dealership or car yard.

Before the goods and services tax era (from July 1, 2000) luxury cars were slugged with a 45% wholesale sales tax. The luxury car tax that replaced it was set at 25%, but has been 33% since July 1, 2008.

The tax is in addition to GST, and that price threshold includes GST but not charges such as stamp duty or compulsory insurance. And the amount of tax is calculated only on the vehicle's value over the threshold, not the GST portion of it (that is, there's no tax on top of a tax).

It also applies only to those registered for GST, so private sales are generally not covered (although it can still apply if you import a luxury car). It's important to note that

businesses acquiring a luxury car will be restricted in their claim for GST credits to the luxury car threshold, so if the car costs more than \$57,581 for 2016-17 (which is the figure used for luxury car depreciation purposes), GST credits are not available in respect of the excess. In other words, the maximum GST credit you could claim will be \$5,235.

### ANY EXCLUSIONS?

Yes there are. Generally speaking, vehicles not included are emergency vehicles, trucks or vans that carry more than two tonnes, and passenger carrying vehicles such as buses. Cars that are specially fitted out to transport disabled people are generally excluded (if the vehicle is supplied inclusive of GST).

Cars that are more than two years old escape the tax, so in general the LCT applies to mostly new vehicles – a second hand luxury car which has had some depreciation may therefore be a good buy.

Fuel-efficient cars (that is, those that burn less than seven litres of fuel per 100 kilometres) are given a break. As long as the fuel-efficient vehicle costs less than \$75,526 (for 2016-17), there's no LCT to pay.

So keep this tax in the back of your mind when you shop for your next set of wheels. ■

# Does your SMSF need a valuation?

The rules around the valuation of assets held under an SMSF have seen a lot of changes over the years. The requirement to consider valuing SMSF assets at market value when preparing the annual financial statements of the fund was one of the most significant and controversial of these changes.

The use of market value accounting for financial statements is regarded as a good practice, but was not imposed on SMSF trustees as a legal requirement.

Since 7 August 2012, a mandatory requirement by regulation came into force, and now aligns SMSFs with accounting principles. Consequently, for the 2012-13 and later financial years, SMSF trustees are required to use market values for the purpose of preparing year-end financial accounts and statements.

## WHY ASSETS NEED TO BE VALUED AT MARKET VALUE

Asset valuation is one of the most significant matters SMSF trustees need to address to confirm compliance with all relevant laws and regulations.

In light of the SIS Act and SIS regulations, a market valuation is required for:

- preparing the annual financial accounts and statements of the fund
- acquiring assets from a related party of the fund
- investments made and maintained on an arm's length basis
- determining the value of assets that support a member's super pension;
  - when an accumulation fund has underlying assets that commence to provide for a pension, the assets must be valued at their market value on the commencement day of the pension
  - for ongoing pensions, the assets must be valued at their market value on 1 July of the financial year in which the pension is paid
- determining the market value of an SMSF's "in-house" assets as a percentage of the value of all assets in the fund;
  - SMSF trustees must not invest in in-house assets that cause the total in-house assets to exceed 5% of the market value of the fund's assets at the time of investment

- if an SMSF held in-house assets, all fund assets must be valued at their market value on 30 June of the income year the in-house asset(s) are held in order to ascertain if a breach of the in-house asset rules has occurred

- selling certain collectibles or personal-use assets to a related party of the fund.

## REASONS FOR MANDATORY VALUATIONS

The ATO was justifiably concerned about a lack of compulsory market valuations of assets.

Failure to record accurate market values of all fund assets, especially of the non-current assets, can have a significant impact on members' balances and may lead to a trustee inadvertently breaching certain provisions.

In cases where a trustee has under- or overstated fund balances, it will be difficult to:

- identify the resources that the fund has available for payment of benefits;
  - for example, an overstated pension balance for a member in the transition-to-retirement phase can lead to situations in which the member takes out more than the allowable maximum limit of 10% of the pension balance. Alternatively, when the market value of fund assets is understated in records, there is the potential for members in transition-to-retirement or pension phase to withdraw less than the minimum amount set in place by the regulations
  - if a member were to leave the fund, an inaccurate valuation can cause an incorrect member balance to be shown in the fund's records, which can lead to the trustee paying or transferring out less or more than the required amount
- determine whether the mix of investments in the fund is in accordance with the investment strategy and adjust the investment mix around the benchmark weighting within the ranges nominated in the fund's investment strategy
- ascertain whether the market value of the SMSF's "in-house" assets exceeds 5% of the value of total assets held by the fund.

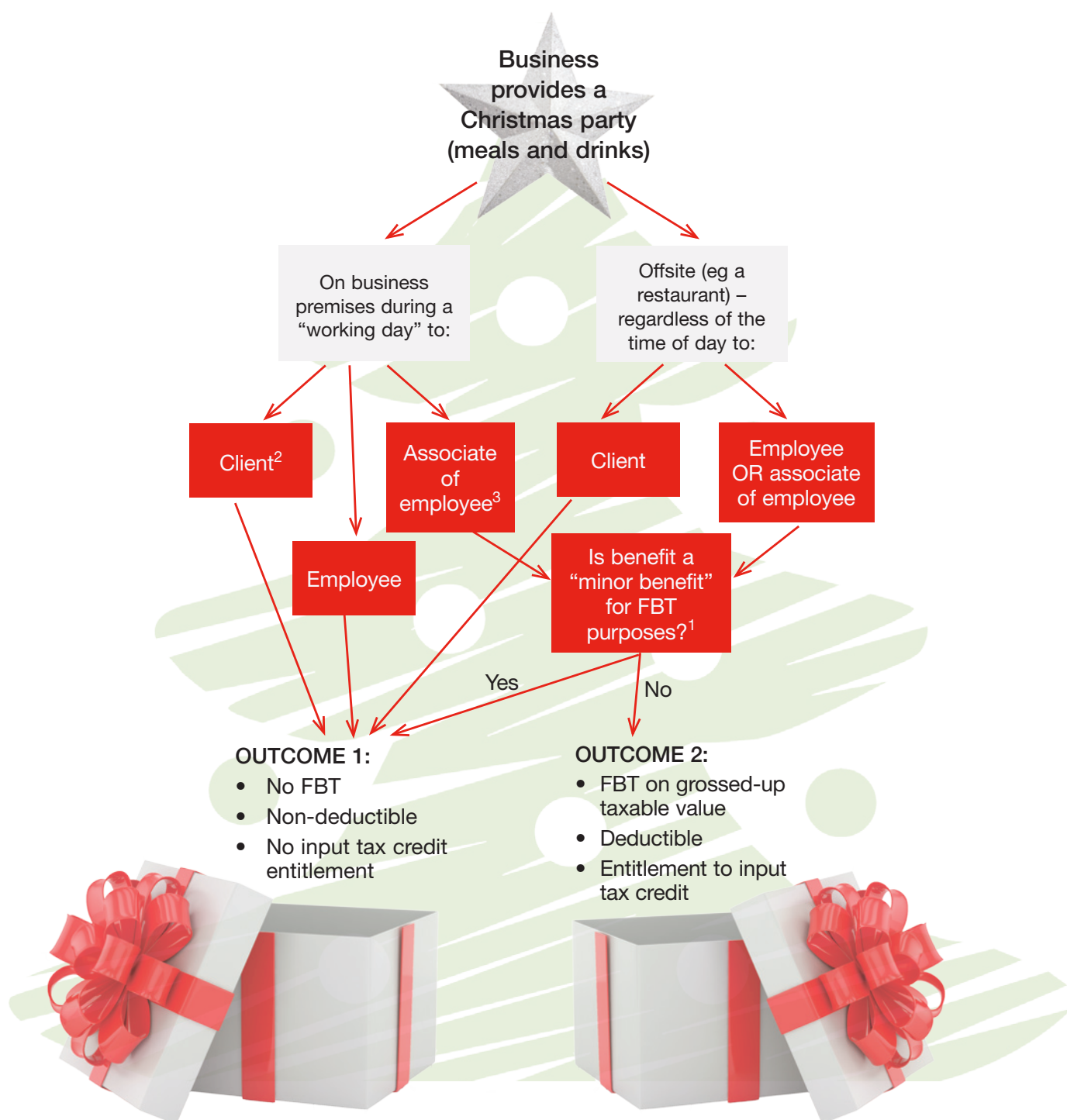
The ATO requires all assets held under a SMSF to be valued at their market value for all valuation purposes.

Contact this office if you require further information. ■



# Christmas party decision tree

This flowchart will help businesses work out the general tax implications of the year-end Christmas party.



1: Minor benefit exemption must be less than \$300 per benefit, provided on an irregular and infrequent basis, and satisfy other relevant conditions.

2: Income tax treatment for entertainment expenses determined under tax law.

3: An associate of an employee is widely defined. It normally includes family members.

NOTE: This flowchart does not apply if you use the 50/50 split or 12 week register in calculating FBT for meal entertainment.

# Christmas party: Examples from the ATO

## EXAMPLE 1

A small manufacturing company decides to have a party on its business premises on a working day before Christmas. The company provides food, beer and wine.

The implications for the employer in this situation would be as follows.

If...	Then...
current employees only attend	there are no FBT implications as it is an exempt property benefit.
current employees and their associates attend at a cost of \$180 per head	<ul style="list-style-type: none"> <li>for employees – there are no FBT implications as it is an exempt property benefit, and the minor benefit exemption could also apply, and</li> <li>for associates – there are no FBT implications as the minor benefit exemption applies.</li> </ul>
current employees, their associates and some clients attend at a cost of \$365 per head	<ul style="list-style-type: none"> <li>for employees – there are no FBT implications as it is an exempt property benefit</li> <li>for associates – a taxable fringe benefit will arise as the value is equal to or more than \$300, and</li> <li>for clients – there is no FBT payable and no income tax deduction.</li> </ul>

## EXAMPLE 2

Another company decides to hold its Christmas party function at a restaurant on a working day before Christmas and provides meals, drinks and entertainment.

The implications for the employer in this situation would be as follows.

If...	Then...
current employees only attend at a cost of \$195 per head	there are no FBT implications as the minor benefits exemption applies.
current employees and their associates attend at a cost of \$180 per head	there are no FBT implications as the minor benefits exemption applies.
current employees, their associates and clients attend at a cost of \$365 per head	<ul style="list-style-type: none"> <li>for employees – a taxable fringe benefit will arise</li> <li>for associates – a taxable fringe benefit will arise, and</li> <li>for clients – there is no FBT payable and the cost of providing the entertainment is not income tax deductible.</li> </ul>



This is a complex area of tax law, so please contact us for further guidance.

This information has been prepared without taking into account your objectives, financial situation or needs. Because of this, you should, before acting on this information, consider its appropriateness, having regard to your objectives, financial situation or needs. Liability limited by a scheme approved under professional standards legislation.