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Christmas cheer – with no FBT fear

With the year steadily making its way towards the festive period, businesses that are turning their attention to end-of-year celebrations will need to keep in mind the tax implications of throwing a Christmas party or handing over gifts to staff. Of course there's nothing wrong with getting into the yuletide spirit, but business owners should make sure that while doing so, adverse tax outcomes are minimised.

As with any benefit that a business provides to staff that is outside the safe definition of "salary", the question of whether it is a (taxable) fringe benefit or not will need to be addressed.

The Tax Office states that there are no different FBT rules that apply to Christmas entertainment, which can certainly come under the "minor benefits" umbrella. A minor benefit will be FBT-exempt where, broadly, the benefit is less than $300 per person and provided on an infrequent and irregular basis.

The FBT law allows however (perhaps getting into the spirit of the season) for the minor benefits threshold to apply to each benefit provided, not to a total value of "associated benefits".

So if, as a generous employer, you put on a barbecue **and** hand out gifts, the meal and the gift are considered separately for FBT purposes. If each is less than $300, they are both generally FBT-free.

It is worth noting however that as such minor benefits are exempt from FBT, a business cannot then claim such expenses as a tax deduction, nor can claims be made for any goods and services tax (GST) credits that arise from making these "supplies".

Where such costs do fall under the FBT regime, an employer's liability is calculated at 46.5% of the grossed-up "taxable value" (or 47% after April 1, 2014, as an effect of the Medicare levy increase) of the benefit provided. Determining the value (for FBT liability calculations) of "entertainment" expenses can be through the "actual" expenses method (which is the default option) or a business can elect for two other options:

- The "50/50 split" method — where the taxable value is equal to half of the total food and drink expenditure relating to employees and their associates as well as third parties (eg clients)
- The "12 week register" method — based on the percentage of food and drink entertainment through a register that is maintained for a representative period (in this case, as the name suggests, 12 weeks).

In a practical sense, the 50/50 split method can avoid additional administration, however the latter

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About this newsletter

Welcome to South East Access' client information newsletter, your monthly tax and super update keeping you on top of the issues, news and changes you need to know. Should you require further information on any of the topics covered, please contact us via the details below.

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Also in this issue:

Volunteering and tax 2
Top 10 SMSF compliance mistakes 4
Tips to avoid common fuel tax credit errors 5
Beware, non-lodging SMSFs 5
ATO reviewing dependant tax offset claims 6
Carry-forward tax loss warning 6
ATO: wrong call on your tax assessment? 7
Trusts 101 8

Christmas cheer – with no FBT fear (cont)

may be preferred where third party entertaining predominantly exceeds staff entertainment. Consult this office for the best option for your situation.

Note that expenditure in relation to meal entertainment is specifically excluded from having to be reported on an employee's payment summary as a "reportable fringe benefit".

Minimising your Christmas party FBT impost

Structuring your Christmas celebrations in a way that makes sure you play Santa under the "minor benefits" banner will be well worthwhile.

The safest option for a business to steer clear of FBT liabilities would be to hold the Christmas party on the business premises on a working day, as providing meal entertainment to employees (and also bona fide clients) will be FBT free.

If partners and families of employees attend (known as "associates") their FBT-free status is maintained if the benefit provided to each person is less than the minor benefits limit of $300.

And if the party is held off-premises, and everyone attends the work function at a pub or restaurant, the $300 limit applies to both employees and associates, with anything over subject to a liability based on a taxable value calculated by one of the methods referred to above.

If entertainment is held off-premises, here is an added cautionary tip regarding the FBT implications for travel expenses such as staff taking taxis. For an employer thinking of paying for this travel option, the important consideration in regard to this will be venue.

If the taxi travel is from home to an entertainment venue (that is not the workplace) and home again, the FBT law will include the cost of the ride as part of the entertainment and deem that it is to be included in the cost-per-head total (that is, it counts towards the $300 minor benefit limit).

But if the cab drives from home to a function held at the workplace, and/or from the workplace back to home after the festivities, the taxi fare is exempt from FBT. ■

What you need to know about volunteering & tax

The worryingly early start to Australia's bushfire season in New South Wales means scores of local volunteers are standing on the frontline, battling and protecting residents from the devastating fires. This raises the important practical question – do payments to volunteers constitute assessable income and are their expenses tax deductible?

There is no legal definition of "volunteer" for tax purposes, although it typically means someone who enters into any service of their own free will, or who offers to perform a service or undertaking.

A genuine volunteer does not work under a contractual obligation for remuneration, and would not be an employee or an independent contractor (on a related note, refer to our article 'Employee or contractor? Some common myths' in the July 2013 Monthly Client Newsletter to learn more about the differences between an employee and an independent contractor).

Volunteers can be paid in cash, given non-cash benefits or a combination of both – payments include honorariums, reimbursements and allowances. Generally, receipts which are earned, expected, relied upon and have an element of periodicity, recurrence or regularity are treated as assessable income.

Conversely, where a person's activities are a pastime or hobby – rather than income producing – money and other benefits received from those activities are not assessable income. A volunteer payment that is not assessable income will be likely to possess many of the following characteristics:

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- the payment is to meet incurred or anticipated expenses
- the payment has no connection to the volunteer's income-producing activities or services
- the payment is not received as remuneration or as a consequence of employment
- the payment is not relied upon or expected by the volunteer for day-to-day living
- the payment is not legally required or expected
- there is no obligation on the part of the payer to make the payment, and
- the payment is a token amount compared to the services provided or expenses incurred by the volunteer.

The case studies below shed light on whether honorariums, reimbursements and allowances constitute assessable income.

Is an honorarium assessable income?

An honorarium is either an honorary reward for voluntary services, or a fee for professional services voluntarily rendered, and can be paid in money or property.

Case study: Alex works as a computer programmer at the local city council and volunteers as a referee for the local rugby union. This year he organised an accreditation course for new referees. He applied for a grant, arranged advertising, assembled course materials, and booked venues. Alex is awarded an honorarium of $100 for his efforts. No, the honorarium is not assessable income as honorary rewards for voluntary services are not assessable as income and related expenses are not deductible.

Case study: Mindy has a graphic design business and volunteers at the local art gallery. Mindy prepares the gallery's annual report using her business's software and equipment. At the gallery's annual general meeting, Mindy is awarded an honorarium of $800 in appreciation of her services. Yes, this honorarium constitutes assessable income because it is a reward for services connected to her income-producing activities.

Is a reimbursement assessable income?

A reimbursement is precise compensation, in part or full, for an expense already incurred, even if the expense has not yet been paid. A payment is more likely to be a reimbursement where the recipient is required to substantiate expenses and/or refund unspent amounts.

Case study: Matthew is an electrical contractor. He volunteers to mow the yard of a local not-for-profit childcare centre. Matthew purchases a $15 spare part for the centre's mower. The childcare centre reimburses Matthew for the cost of the spare part. No, the $15 reimbursement is not assessable income because Matthew has not made the payment in the course of his enterprise as an electrician.

Case study: Rose is a gardener. She volunteers to prune the shrubs of a local nursing home and uses materials from her business's trading stock. Yes, any reimbursement she receives for the cost of the materials is assessable income because the supplies were made in the course of her enterprise.

Is an allowance assessable income?

An allowance is a definite predetermined amount to cover an estimated expense. It is paid even if the recipient does not spend the full amount.

Case study: Markus volunteers as a telephone counsellor for a crisis centre. He is rostered on night shifts during the week and is occasionally called in on weekends. When Markus works weekends, the centre pays him an allowance of $150. The allowance is paid to acknowledge Markus's extra efforts and to compensate him for additional costs incurred. Yes, these payments to Markus are considered assessable income because he received the allowance with no regard to actual expenses and there is no requirement to repay unspent money.

Expenses incurred by volunteers

Moving on to the tax deductibility of volunteer expenses, a volunteer may be entitled to claim expenses incurred in gaining or producing assessable income – except where the expenses are of a capital, private or domestic nature. For instance, expenditure on items such as travel, uniforms or safety equipment could be deductible, but expenses incurred for private and income-producing purposes must be apportioned

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What you need to know about volunteering and tax (cont)

– with only the income-producing portion of the expense being tax deductible.

Case study: Rupert operates a commercial fishing trawler and uses navigational charts in his business. He also volunteers as an unpaid training officer at the volunteer coastguard. Rupert purchases two identical sets of navigational charts – one for his business, the other as a training aid in coastguard courses. Yes, Rupert can claim the part incurred in gaining or producing assessable income – in this case, half the total cost.

It is also common for volunteers to donate money, goods and time to not-for-profit organisations. To be tax deductible, a gift must comply with relevant gift conditions, and:

- be made voluntarily
- be made to a deductible gift recipient, and
- be in the form of money ($2 or more) or certain types of property.

Donors can claim deductions for most, but not all, gifts they make to registered deductible gift recipients. For instance, a gift of a service, including a volunteer's time, is not deductible as no money or property is transferred to the deductible gift recipient. However, individuals may be entitled to a tax deduction for contributions made at fundraising events, including dinners and charity auctions.

Case study: Eunice buys a clock at a charity auction for $200. No, this is not a gift even if Eunice has paid a lot more than the value of the clock. Payments that are not gifts include those to school building funds as an alternative to an increase in school fees and purchases of raffle or art union tickets, chocolates and pens.

Case study: Clement receives a lapel badge for his donation to a deductible gift recipient. As the lapel badge is not a material benefit or an advantage, the donation is a gift.

Consult this office for more information on which volunteer payments are considered assessable income and which expenses are typically tax deductible. ■

Top 10 SMSF compliance mistakes

The Tax Office has published a list of the top 10 types of compliance mistakes made by SMSF trustees. The data from which the list is taken is based on the type of contraventions reported by approved SMSF auditors since 2005 (when compulsory contravention reporting started) up to June 30, 2012.

The top 10 contravention types in percentage terms are as follows:

Contravention type	Incidence %	Proportion of assets %
Loan to members/ financial assistance	20.9%	14.4%
Dealing with in-house assets	18.3%	27.2%
Administrative contraventions	12.0%	1.8%
Separation of assets	12.9%	26.2%
Operating standards	8.3%	6.5%
Borrowings	8.0%	7.8%
Sole purpose	7.8%	5.7%
Investments at arm's length	7.5%	7.4%
Other	2.8%	0.7%
Acquisition of assets from related parties	1.5%	2.3%

Of the top 10, three types of contravention represent more than two-thirds of the proportion of asset values (67.8%). These are, in order of asset value proportion:

- in-house assets
- separation of assets
- loans to members/financial assistance.

The Tax Office has a number of options when dealing with SMSF compliance issues, including making the fund non-complying for taxation purposes, imposing civil penalties (or perhaps criminal penalties for more serious breaches), and possibly disqualifying a trustee.

As well, the Tax Office can issue rectification and education directions for contraventions, and an administrative penalty (which must be paid personally by the trustee or the director of the trustee company and cannot be paid or reimbursed by the SMSF). ■

Five tips to avoid common fuel tax credit mistakes

The Tax Office has issued advice regarding fuel tax credits after it noticed some errors creeping into recent activity statements — also reminding businesses that rates can change regularly (and have done so recently) and that this can be a common source of the mistakes being made.

For those businesses eligible to claim fuel tax credits, remember as well that from July 1, 2013, rates used in calculations should be those that applied when the fuel was acquired. However one exception is fuel used in heavy vehicles travelling on a public road, where the correct rate will be that which was in effect at the beginning of the tax period covered by the business activity statement (BAS).

The following tips can help you get your claim right, but of course ask for our guidance to follow these tips correctly or should other questions arise.

Use the right rates. As mentioned, fuel tax credit rates can change on a regular basis, so it's important to make sure you use the correct rate. A good habit to get into would be to check up on the rates, or ask us to, before lodging each BAS.

Ensure that your fuel is the right sort. Fuel type and usage will influence your eligibility, as there are some exceptions to what you can claim. A common mistake is to claim fuel tax credits for fuel you use for private purposes or for travelling on a public road in vehicles with a gross vehicle mass (GVM) of 4.5 tonnes or less.

Keep those records. Make sure that accurate records are kept of fuel purchases and how that fuel is used in your business. This is even more important now that fuel tax credit rates are apt to change on a regular basis. Your records should show:

- the date the fuel was acquired
- the type of fuel you acquired
- the quantity of fuel
- how you apportioned the fuel for different activities, and
- the business activities you use it in, such as if it is for on-road or off-road activities.

Do your sums and check them. Make sure you use the quantity of fuel when calculating your fuel tax credits. The Tax Office said a common mistake is claiming fuel tax credits based on the cost of the fuel instead of the quantity of fuel multiplied by the relevant rate.

Work out your fuel tax credits using this formula:

Quantity of eligible fuel x Correct fuel tax credit rate = Fuel tax credits

Write this amount, in whole dollars, at label 7D on your BAS (and it's a good idea to keep records of your calculations).

Read over your contracts. The wording of contracts that involve supplying fuel can affect who can claim credits. If a contract has not been reviewed for some time, check that provisions dealing with fuel supply or use reflect the current regime — or have us read over your contracts for you. ■

Beware, non-lodging SMSFs

Word on the street is that the Tax Office has taken additional steps to engage with self-managed superannuation fund (SMSF) trustees to bring their lodgement obligations up-to-date. Over the past few months, the Tax Office has been writing directly to SMSF trustees with two or more lodgement obligations overdue, advising them that they will remove their regulation details from the Super Fund Register until they bring their lodgements up-to-date – or in the case of non-operating funds, wind up the fund.

If you are affected, consult this office for help on how to:

- review your requirement to lodge, and
- bring your lodgements up-to-date. ■

Tax Office reviewing dependant tax offset claims

The Tax Office has stopped all tax returns with a Dependant (Invalid and Carer) Tax Offset claim and is reviewing them, following an unexpected upsurge in the number of individuals that have made claims for the new tax offset.

The new Dependant (Invalid and Carer) Tax Offset is only available to individuals who maintain a dependant who is genuinely unable to work due to invalidity or carer obligations. However more than 41,000 taxpayers have made claims, prompting the Tax Office to review all tax returns and follow up on any notices of assessment that have already issued.

The Tax Office initially expected that very few individuals would be eligible to receive the new tax offset under legislation that came into effect for the 2012-13 tax year.

Under the legislation, the following eight dependency tax offsets below were consolidated into a single, streamlined and non-refundable tax offset: invalid spouse tax offset, carer spouse tax offset, housekeeper tax offset, housekeeper (with child) tax offset, child-housekeeper tax offset, child-housekeeper (with child) tax offset, invalid relative tax offset, and parent/parent-in-law tax offsets.

Individuals who were eligible to claim more than one tax offset amount in respect of multiple dependants are still be able to do so. However, individuals who received the zone or overseas forces or overseas civilians tax offsets are not entitled to claim the new offset, but can still claim any or all of the other eight offsets at T5 Zone or overseas forces.

Unless an individual is eligible for a zone or overseas tax offset, they are no longer able to claim offsets for a spouse born on or after July 1, 1952, a parent, a parent-in-law, or an invalid relative.

Consult this office to check if your claim for the Dependant (Invalid and Carer) Tax Offset is valid. ■

Did you know… CARRY-FORWARD TAX LOSSES

Got a carry-forward tax loss burning a hole in your business's pocket? Don't get too creative if you've thought how handy it would be to absorb that loss as a tax deduction for a future income year.

Tax law has measures in place to ensure such deductions are limited to those businesses that are legitimately eligible — such as the continuity of ownership and the same business tests. But there is another "integrity" measure that may result in a denial of a claim for losses which business owners should keep in mind.

The Tax Office has the discretion to disallow the deduction of a tax loss if, during the relevant income year, the business attempting to make such a claim earned assessable income (or realised a capital gain) that *would not have been derived* had the loss been unavailable as a deduction (our emphasis).

There is some balance to the rules in that the Commissioner is "prevented" from disallowing the deduction should "continuing shareholders" stand to benefit from the relevant income. However there is still a fair amount of discretion left to the Commissioner in how the rules are applied.

In other words (and of course circumstances of the business or businesses involved will have an influence), a business can mitigate the risk that the Tax Office will exercise this discretion to disallow a tax loss deduction by making sure that either (or preferably both) of the following contentions are supported:

- that the business would have derived the income or realised the capital gain regardless of the tax loss being available
- that continuing shareholders will benefit from the above in a fair and reasonable manner with regard to their rights and interests.

Ask this office for further direction should any of the above be relevant to your business. ■

Has the ATO made a wrong call on your tax assessment? Here's what to do

If you believe your tax assessment is incorrect, the first step should be to go over your tax return or activity statement to check details against your notice of assessment. If you still believe the assessment is wrong, or if you have extra information that may change it, an amendment can be sought from the Tax Office (which we can help you with).

But if the Tax Office disagrees that there is a mistake, you can lodge an objection to that decision. You can also object if it amends an assessment and has taken a different stance to you (for example, you wanted to include a deduction but were allowed only part of it).

The Tax Office requests that objections be in writing (you can use one of its forms, which we can provide, or ask us to write an objection for you), detailing all the reasons you think a decision is incorrect. This should include, where relevant, references to legislation, rulings or case law. It will also be necessary to include any supporting documents and information that relates to the decision.

The Tax Office will generally review its original decision, and says these reviews will be carried out by a tax officer who was not involved in the original decision. It will then let you know the outcome in writing (referred to as an "objection decision"), either directly or via this office. However if you're still not satisfied, the next step is to ask for an independent external review of the Tax Office's actions and its decisions about your tax affairs.

Tax laws specifically give you the right to go to the Administrative Appeals Tribunal (the tribunal) or the Federal Court of Australia for a review of some of the Tax Office's actions or decisions. When the Tax Office lets you know its decision, it should also explain how these options differ and how to access each. You generally have 60 days from the date of this decision notice to seek a tribunal or court review.

When taking the tribunal or court option

The burden of proof in the taxpayer's lap, so you will need to go into the tribunal or court being able to prove that the tax assessment is excessive – or, more pertinently, that your idea of the tax outcome is the correct one – and support this with evidence, documents, and sound technical analysis.

The tribunal is less formal than a court hearing, but it can confirm, vary or set aside the Tax Office decision. You can appear yourself or be represented, and there is an application fee, which is refunded if the hearing goes your way.

Under the umbrella of the tribunal is the Small Taxation Claims Tribunal, which provides a quicker and cheaper review if the amount of tax in dispute is less than $5,000. Either way, if you are not satisfied with the tribunal's decision you can appeal to the Federal Court.

However once at the Federal Court, procedures get much more formal. You will generally need legal representation and there are a lot more fees (filing fee, "setting down" fee and daily hearing fee, for example).

After this level of intervention, the next steps up the legal ladder are the Full Federal Court and then the High Court – but these are rare options for most taxpayers, and these courts won't grant every appeal that is requested.

Taking one for the team

If you think what you've been through can help level the tax playing field for the rest of the nation's taxpayers, it could be possible to apply to have your case funded under the "test case litigation program".

This operates alongside all the other dispute resolution protocols, and can reimburse some or even all of your legal costs if it is decided that your case has important implications for the wider community and the administration of the tax system.

It may be, for example, that your case happens to involve a particular area of tax law in which there is uncertainty and that has not been tested in the courts before – and that the public interest will be served by seeing it go through the courts. Applicants are reviewed by an independent panel of legal and accounting professionals and senior tax officers.

See our office if you think any of the above applies to your tax affairs. ■

Trusts 101: What are they, and how do they work?

One of the big motivations for considering using a trust will be to protect assets. Property and other assets can be moved into a trust for protection from creditors, to maintain an estate until a beneficiary becomes old enough to have legal possession, or isolate valuable assets from a trading company that may be more exposed to litigation, for example.

Trusts, if set up in the right way, can help you legally minimise some tax liabilities. But it is a tricky area, and the taxman is always on the lookout to close perceived loopholes or an over-enthusiastic stretching of the scope for reducing tax. Specialised advice will go a long way.

The word used to name these types of arrangements – "trust" – is appropriate. A trust is a structure that separates control and legal ownership from beneficial ownership; so that at least one person and/or company agrees to hold and manage assets or property in a way that will benefit someone else (the beneficiary). A trust therefore is a formal structure for an obligation, where "beneficiaries" place their trust (in the sense of "confidence") in the controller or holder of assets (called the "trustee"; again appropriate, as the receiver of their trust) to manage those assets for their eventual benefit.

You could almost liken a trust to a private jet. The jet is put under the control of a pilot, who is also the owner (the trustee) to fly the jet while carrying the passengers (beneficiaries) to a destination (when the trust ends, or is "vested") where the cargo or luggage (assets and property) is unloaded and given to the passengers again. During the flight, the luggage and cargo is maintained in the best condition possible and the passengers may occasionally be offered food and drinks if the ticket contract allows it (the beneficiaries may be paid distributions from the trust). The pilot may also off-load some cargo at stopovers along the way.

Separate control from beneficial ownership

The structure of a trust allows a business or asset to be put into the hands of a third party (trustee) who is given legal control and has a duty to operate that business or manage these assets to benefit someone else (beneficiaries). This is known as a "fiduciary duty".

There are various types of trusts. You can have a fixed trust, discretionary trust, hybrid trust, unit trust and many more, each with unique characteristics. A deceased estate is also a trust, being property and assets that are held and managed by the executor (the trustee) for those who will inherit them. Ask this office for more complete run-downs of each trust type.

Trusts can exist even without explicit intention by the parties to create a trust – it is the existence of the necessary relationship (like the deceased estate example) that forms a trust, not formalities. Having said that, modern trusts are generally governed by written trust deeds, that spell out how it is set up and the rules for its maintenance, the rights and obligations of all parties, and also how income from the trust's assets is "distributed".

Distributions and tax

A trust calculates its annual taxable income under the usual tax laws and then the trustee distributes and/or retains the income. Income that is distributed to beneficiaries will be treated as though the beneficiaries earned it directly and will be taxable at their own marginal rates. On the flip side, the trustee has to pay tax (on behalf of the trust) on any taxable income that is not distributed. Undistributed income is taxed at the top rate (including Medicare levy); currently 46.5% (but will be 47% from July 1, 2014, when the Medicare levy goes up). There are some cases where the trustee pays tax on behalf of a beneficiary, such as a child or a foreign resident.

When the trustee decides whether and how much to distribute to each beneficiary, the trustee should take into account each beneficiary's financial, taxation and personal circumstances and distribute income in the way that best serves everyone. Of course, the trustee is restricted by the terms of the trust deed.

"Ownership" conundrums

Another spur for trust use may occur if means or asset tests for government benefits are likely to figure in your financial future. Trusts can help here with the re-allocation of legal ownership without completely letting go of enjoying the benefits of the asset.

The other side of asset protection is a consideration for inheritance. If a prime asset is "owned" by a trust, like for instance a house with pristine beach front, and the trust deed is specific in terms of selling and/or maintaining the beach house, future generations of the family will be able to enjoy the same asset and not have it sold off by some initial inheriting spendthrift relative.

There are many more variations not covered here, and much more regulation and considerations than can be covered in this newsletter. The area of trusts is a complex one, and anyone considering setting up their own trust is well advised to seek expert advice. ■