

NEWSFLASH BOOKLET

GOODS AND SERVICES TAX (GST)

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Important

This booklet is simply a collection of Newsflash articles relevant to GST. The articles are transferred from Newsflash into this booklet so it is best read from the back page forwards to ensure you are reading the latest article on the topic first. Note that the information contained in this booklet is not updated regularly so it is important that you seek professional advice before acting on it.

Basic Mechanics of GST

All businesses with a turnover greater than \$50,000 must register for GST unless they are “Input Taxed” i.e. domestic rental properties. Even exempt businesses need to register in order to claim back their input credits. All businesses that are not exempt and are registered for GST must charge GST to all customers even if the customers are exempt from GST. The only exemptions from charging GST are on exempt goods not exempt customers, with the exception of disabled vehicles and the parts for these vehicles. All businesses registered for GST can claim an input credit for GST paid on inputs to their business.

Note unlike sales tax there are no exemptions, only input credits. No one can ask you to sell them goods or services exempt from GST unless those goods or services are exempt themselves. Exempt entities have to claim their GST back from the ATO, not buy goods or services without GST. Unlike sales tax, the tax is not to be added on at the end of the invoice. Each price stated must be GST inclusive.

Definitions

Input Taxed – GST is paid on all expenses unless they are an exempt expense such as food. But no credit can be claimed for the GST paid. No GST is charged on sales or income. Examples: domestic rental properties and bank transactions.

GST Free – GST is not charged to customers but an input credit can be claimed on inputs where GST has been paid. Must register for GST and perform basically the same paperwork tasks as normal businesses. Examples medical services, childcare and exports.

GST and Domestic Rental Properties

Properties rented to households will be input taxed. This means that the rent does not need to be increased to include GST. But an input credit cannot be claimed for the GST paid on expenses relating to the property. In particular, building materials that were exempt from sales tax, but now will be subject to GST, will increase. As a result the costs of maintaining a rental property are expected to increase. Further, the GST will increase the cost of new houses, eventually increasing the value of established homes. Landlords expecting to make the same percentage return as they were before GST may increase rents. The increased price of housing may also push more people into the rental market and so increase demand for an item now more costly to supply. In summary, increased maintenance costs, replacement costs and demand will have at least some upward pressure on rents.

Miscellaneous GST Information

You will need an ABN to register for PAYG regardless of whether you choose to be registered for GST. In other words if you pay employees or sub contractors you will need to complete an ABN application form. According to the ATO, you will have to fill in the same details as required on the GST business activity statement if you are registered for PAYG. Of course subcontractors need an ABN as well.

Regarding Real Estate for GST purposes the transaction date is the date the property actually changes hands not the date of signing the original contract as is the case for CGT.

GST & Employee's out of Pockets

Only businesses registered for GST can claim an input credit for GST paid on expenses. If an employee pays for a work related expense the benefit of the input credit is lost unless the employer reimburses the employee for the expense. After 30th June 2000, instead of paying employees a tool allowance, they will have 10% more to spend if the tools are actually purchased by the employer either directly or by reimbursing the employee.

Note - Employees should be advised of the details required to claim an input credit - they will need to have these on the receipt for which they are seeking reimbursement. GST R2000/17 paragraphs 73 & 74 allows the receipt to show the employees name not the employers.

To ensure the reimbursement does not create an FBT liability, reimburse employees only for expenses that would otherwise be deductible in their personal income tax return.

Threshold Changes

You are required to lodge your business activity statement electronically and monthly only if your annual turnover exceeds \$20 million. You can elect to lodge electronically and /or monthly if you annual turnover is less than \$20 million.

You can account for GST on a cash basis (rather than accruals) if your annual turnover is less than \$1 million. You can also use a cash basis if your annual turnover is more than \$1 million and you are accounting on a cash basis for income tax purposes.

Taxi Drivers and GST

Page 7 of the Australian Taxi Industry Association's GST Manual states that taxi drivers in a bailment arrangement are the ones who must forward one eleventh of the total fares taken, during his shift, to the ATO as GST collected. This means that the percentage used to split income between the taxi driver and the cab owner will need to change. The following is an example of how the GST will affect the split. In this example the owner pays fuel and all other costs of the vehicle. The split is 45% to the driver and 55% to the owner.

Assuming takings of \$100 prior to GST	ATO	Driver	Owner
The old way the \$100 would be split 55% to the owner and 45% to the driver i.e.		45.00	55.00
After GST, takings for the same amount of travel will be close to \$110. The price increase should not be a full 10% because input credits will be claimable on expenses such as fuel. Petrol and Diesel should stay the same price at the bowser as the government will adjust excise to ensure this, but LPG will increase with GST. One eleventh of the fuel bill will be reimbursed through the GST system. There is an argument that the party paying for the fuel, in this case the owner, should now receive a lower portion of the total takings. For the sake of the exercise I will assume the percentages stay the same. That is that the Owner still expects to get 55% of the actual fares after GST has been remitted to the ATO and the Driver 45%. Also, for the point of proving the percentages work out the same I will assume a full 10% increase in fares. Therefore takings after GST will be \$110. According to page 7 of the manual one eleventh of this i.e. \$10 will be sent to the ATO as GST.	10.00		
The owner will still receive 55% of the total fares which is \$60.50, but as this is income to the owner, the owner must send one eleventh, namely \$5.50 to the ATO as GST.	5.50		55.00
As the driver has paid \$60.50 to the owner he will be able to claim an input tax credit of this amount from the ATO. After all these transactions the driver still holds: \$110.00 – 10.00 – 60.50 + 5.50 =		(5.50) 45.00	
The result is the same dollar value as before GST except that the consumer has paid 10% which went to the ATO.	10.00	45.00	55.00

But what if fares go up by only 8%?

This could happen because the costs of fuel, parts and vehicles will decrease as a result of the GST, especially after input credits are claimed. Note the labour portion of repairs will probably increase, but not by more than the input tax credit. Diesel and Petrol should be one eleventh cheaper after claiming the input credit, but LPG

will probably reduce by a small amount only after the input credit. Working through the same circumstances above, but with only an increase of 8%, the figures change as follows:

Assuming takings of \$100 prior to GST	ATO	Driver	Owner
Prior to GST \$100 Fare		45.00	55.00
After GST same amount of travel results in \$108. The driver must remit one eleventh of this to the ATO:	9.82		
The Owner then receives 55% of the gross takings \$59.40 but has to remit one eleventh to the ATO:	5.40		54.00
The reduction in income is probably less than the savings on operating costs. The driver can claim the input credit back so he is left with $\$108 - 9.82 - 59.40 + 5.40 =$		(5.40) 44.18	
Driver's income is reduced but as in this case the Owner bears 99.9% of the costs, the owner is the only one to benefit from the costs savings.	9.82	44.18	54.00

In this case it is extremely unfair as the driver who pays the GST is not the one who benefits from the reduction in vehicle operating costs because in this case the owner pays all costs including fuel. The 45:55 split will have to be renegotiated but this cannot be done accurately until the increase in fares is known and we have an idea of the changes in operating costs. Fortunately, because in this particular agreement the owner bears 99.9% of the costs a formula can be applied to working out the driver's share. Note this will be fair only if the fare increase as a result of the GST truly reflects the costs savings.

If fares increase by 8% the driver should still get \$45 out of every \$108 collected. Worked through as above:

Assuming takings of \$100 prior to GST	ATO	Driver	Owner
8% Increase in Fares Driver's Percentage 45.85%			
\$108 in fares the driver has to send one eleventh to the ATO as GST:	9.82		
The driver then gives the owner $100\% - 45.85\% = 54.15\%$ Of the \$108 = \$58.48 but the owner must pay one eleventh to the ATO as GST:	5.32		53.16
The Driver can claim the input credit back on the Money paid to the Owner:	(5.32)		
The Driver then ends up with $\$108 - 9.82 - 58.48 + 5.32:$	9.82	45.02	53.16

The Owner is getting less than previously but if the Industry correctly sets the increase in fares then there should be a corresponding reduction in his costs.

Assuming takings of \$100 prior to GST	ATO	Driver	Owner
7% Increase in Fares Driver's Percentage 46.27%			
\$107 in fares the driver has to send one eleventh to the ATO as GST:	9.72		
The driver then gives the owner $100\% - 46.27\% = 53.73\%$ Of the \$107 = \$57.49 but the owner must pay one eleventh to the ATO as GST:	5.23		52.26
The Driver can claim the input credit back on the money paid to the Owner:	(5.23)		
The Driver then ends up with $\$107 - 9.72 - 57.49 + 5.23:$	9.72	45.02	52.26

Note for each 1% change in the percentage increase in the fare the drivers percentage share needs to be adjusted by .43% but you should work through the above to be sure as this figure will be a bit out over a few percentage points change in the fares.

If you use Cab-charge or the driver pays some of the operating cost the above is not suitable to your circumstances.

GST Applies When Selling Equipment etc.

A business must remit 1/11th of any income from a taxable supply. A taxable supply is any item not GST free or input taxed. Examples of GST free items are exports, medical supplies, basic food, plain milk and water.

Examples of input taxed items are interest and dividends. So if the business receives income from any item other than these, GST probably applies even though the sale might not be within the normal trading practices of the business. For example 1/11th of the price received for the sale of a business vehicle must be remitted to the ATO as GST. This is so even if the vehicle has been depreciated, purchased before 1st July 2000 or purchased brand new in 2000/2001 and no input credit was claimable on the purchase. The above also applies to a business selling off some of its plant.

Please note the above refers to income not funds received by way of a loan. There are special rules regarding the sale of a business. These special rules apply to Goodwill, Plant, Motor Vehicles and Business Premises sold as part a business that is a going concern. It is important to consult an accountant before signing any contract to sell a business without paying GST as the special rules have a few traps.

GST Free Supplies

The following is the most current list available of items that are GST free. Note this is not by any means final.

Hospital Services, such as:

- ◆ Public and private hospital treatment
- ◆ Hospital-in-the-home services
- ◆ Hospital outreach services
- ◆ Hospital services that are contracted out

Food and Drink:

- ◆ Meat but not crackling
- ◆ Baked Beans
- ◆ Cheese-topped bread
- ◆ Damper
- ◆ Fruit loaves, plain
- ◆ Gluten-free bread
- ◆ Hamburger buns
- ◆ Lavash bread
- ◆ Lebanese bread
- ◆ Pita bread
- ◆ Plain bread and rolls
- ◆ Plain focaccia
- ◆ Pumpkin bread
- ◆ Sesame seed or poppy seed rolls
- ◆ Sour dough or rye bread
- ◆ Unleavened bread
- ◆ Yeast-free bread
- ◆ Breakfast cereals that are not separately wrapped
- ◆ Cake mixes
- ◆ Candied peel
- ◆ Cheese
- ◆ Fresh or frozen chicken
- ◆ Condiments
- ◆ Cooking fats and oils
- ◆ Crabs (dead or alive)
- ◆ Eggs
- ◆ Fish
- ◆ Fish fingers
- ◆ Flavourings
- ◆ Frozen whole fruit
- ◆ Infant or invalid rusks
- ◆ Irish stew, tinned
- ◆ Lobsters (dead or alive)
- ◆ Meat products
- ◆ Raw nuts
- ◆ Unshelled nuts
- ◆ Oysters (dead or alive)
- ◆ Uncooked pasta
- ◆ Frozen vegetables
- ◆ Seasoning
- ◆ Soup
- ◆ Spaghetti
- ◆ Spices
- ◆ Sugar
- ◆ Sweeteners
- ◆ Vegetables
- ◆ Chicory
- ◆ Coffee
- ◆ Cordials at least 90% fruit juice
- ◆ Carbonated 100% pure fruit juices
- ◆ Non-carbonated 90% pure juices
- ◆ Infant or invalid beverages
- ◆ Tortillas
- ◆ Lactose
- ◆ Malt
- ◆ Milk products (unless listed)
- ◆ Non-carbonated pure water
- ◆ Rice milk
- ◆ Soy milk
- ◆ All teas

- ◆ Fruit
- ◆ Unprocessed goat milk
- ◆ Hamburger patties sold in packets
- ◆ Carbonated 100% vegetable juice
- ◆ Fresh or dried herbs

Health and Medical:

- ◆ Services of a medical practitioner or pathologist.

Services of Allied Health Practitioners, these include:

- ◆ Aboriginal or Torres Strait Islander health services
- ◆ Acupuncture
- ◆ Audiology, eudiometry
- ◆ Chiropody
- ◆ Naturopathy
- ◆ Occupational therapy
- ◆ Osteopathy
- ◆ Pharmacy
- ◆ Physiotherapy
- ◆ Speech pathology
- ◆ Residential, Community Care and Specialist Disability Services.
- ◆ Social work
- ◆ Chiropractic
- ◆ Dental
- ◆ Dietary
- ◆ Herbal Medicine
- ◆ Nursing
- ◆ Optometry
- ◆ Paramedical
- ◆ Psychology
- ◆ Podiatry
- ◆ Speech therapy

Medical aids and Appliances

Drugs, Medicines and Health Goods, where:

- ◆ They are supplied on prescription and supply without prescription is restricted.
- ◆ They qualify as pharmaceutical benefits and are sold on prescription.
- ◆ They can only be supplied by a medical practitioner, dental practitioner or pharmacist (eg. Ventolin), or by other legally permitted people. (eg. optometrists or chiropodists)
- ◆ They qualify as Schedule 2 (S2) drugs or medicines such as aspirin or paracetamol (or would if they were in different packet sizes), medicated cough medicines, antifungal treatments, and smoking cessation treatments such as Nicorettes.
- ◆ They are supplied under special arrangements that enable non-approved goods to be used by people with life-threatening or other serious conditions.

Health Insurance.

What Food is GST Free?

The Tax Reform Web site at www.taxreform.ato.gov.au is constantly updating the information available on what and when food will be subject to GST.

GST Titbits to Push You Over the Edge

If you charge your customers a fee on their **over due account** you will have to remit 1/11th to the ATO as GST unless that charge is considered interest which is a financial supply and input taxed. Accordingly, you will not have to remit GST and you will not suffer all the administration problems of providing an input taxed supply because you should be under the threshold. The threshold is \$50,000 in input credits relating to the financial supply or if the input credits relating to the provision of the financial supply exceed 10% of your total input credits. If you intend to charge interest on overdue accounts, please check that you are legally entitled to do so. On the other side of the fence, if one of your suppliers charges you a fee for late payment of their account you can claim an input credit for 1/11th, but if it is an interest charge then no input credit is available.

Fisherman/woman don't separate the eggs from the fish. Caviar is subject to GST but fish are not. The ATO considers Caviar to become Caviar the minute it leaves the fish even if it has not been salted. So a fish

containing eggs is GST free. But the eggs no longer attached to the fish are subject to GST so 1/11th of the price you receive must be remitted to the ATO.

Businesses who are accounting for GST on an accruals basis i.e. their **turnover is greater than one million** will have to pay the GST on the whole contract price in the period they receive the deposit. Accordingly, they should consider increasing the deposit they require by another 10% of the total contract price.

GST is payable on **employee contributions for fringe benefits**. If an employee pays a cash contribution towards a benefit provided by his or her employer, the employer must remit 1/11th of the amount received to the ATO as GST. If the employee makes a contribution by a method other than cash (i.e. puts petrol in the car) the employer does not have to remit any GST. This all works out in the wash as the employee is unable to claim an input credit for the GST in the fuel price he or she paid and cannot pass this input credit on to his or her employer.

Joint Owners of Commercial Property

Firstly, make sure you have an ABN before 1st July, 2000 or your tenants will be holding back 48.5% of their rent and sending it to the ATO. Registering for an ABN does not automatically require you to remit 1/11th of the rent you receive to the ATO as GST. This is only necessary if the rental income is greater than \$50,000 per annum. If you are not registered for GST you will not be able to claim input credits but this is a small price to pay for not losing 1/11th of your income. Your tenants may want you to be registered for GST so they can claim an input credit for 1/11th of the rent they pay. If your tenants are only very small businesses that are not registered to charge GST and so claim input credits, they will not care whether you are registered but may expect their rent to be cheaper.

Joint Owners of Commercial Property are not normally required to lodge a partnership income tax return, so they do not have a partnership tax file number. However, they will be required to have a partnership ABN. A normal application for a partnership ABN form can be used just write “no TFN necessary” where it asks for the partnership TFN. The individual owner’s TFNs can be entered at the back of the form. Note you will not be able to lodge the application over the internet. If the rent received from the commercial property is less than \$50,000 there is no requirement to charge GST, but of course input credits will not be claimable on the GST paid on repairs etc. Note the \$50,000 threshold looks only at the joint income from the commercial property not each individual owner’s turnover in their own right. So, one of the owners may be registered for GST in their own business because the turnover is more than \$50,000. This would not affect the commercial property because for taxation purposes it is a completely separate entity from the owner’s. There are no compulsory grouping provisions in the GST so each entity tests the \$50,000 threshold individually. For example, A & B jointly own a commercial property that produces \$35,000 in rental income per year. A & B do not have to charge GST as they are under the threshold. B the buys a commercial property with C that returns \$40,000 in rental income per year. Then B also buys a commercial property with D that produces annual rental income of \$30,000. Now, assuming B has a 50% interest in all properties, B’s combined rental income is \$52,500 and the GST threshold is \$50,000. Nevertheless, B does not have to charge GST because for GST purposes he is not the owner of the properties - each individual partnership is and individually the partnerships do not exceed the threshold. Caution, there are anti avoidance provisions that would probably catch an intentional transfer of properties for this purpose but they would not catch a simple purchase of a property. So while you can’t rearrange your properties to avoid GST you can consider these provisions when deciding what name to purchase your next property in.

If the rent does include GST, a “tax invoice” must be received by the tenant in order for him or her to claim an input tax credit. Refer Newsflash 9 for details of the information to be included in a tax invoice. According to GSTR1999/D10 (which is a draft ruling only) one invoice can cover multiple payments but, if the amount varies, a schedule must be attached showing the amount for each supply. A lease can be used as a tax invoice if it has the correct details, states that the parties intend the lease to be a tax invoice and a new document is created if the amount of the rent changes.

Voluntary Agreements

The ATO fact sheet NAT3063 states the following:

- 1) A voluntary agreement must be in writing and must be for the services of an individual who has an ABN.
- 2) The agreement can be terminated by either party advising the other in writing.

- 3) Providing the person who is receiving the services would normally be entitled to a full input credit for these services, the person supplying the services does not charge GST to the person receiving the services. The person receiving the services does not receive an input credit for services provided under a voluntary agreement. So you would expect to be charged 1/11th less than suppliers for whom you can claim an input credit.
- 4) The person who provides the service should be registered for GST as they can claim an input credit for any items they buy in relation to their business but do not have to charge GST to the person receiving the service under a voluntary agreement. **But** if the service provider is also providing services to the public and their total turnover is under \$50,000 it will probably not be in their interest to register for GST.
- 5) Basically, the rate of tax to be withheld is either 20% or the amount shown as the instalment rate at T2 on the subcontractor's BAS. Note the ATO has released a voluntary agreement form that can be used but it is not compulsory.
- 6) Appropriate records must be kept by the payer for each individual subcontractor, as a payment summary must be prepared at the end of the year.

Ice

The ATO has finally ruled that ice will be subject to GST. But if supplied as part of an item that is normally GST free and there is no extra charge for the ice then no GST needs to be charged. For example a fisherman packing his fish in ice to take to the markets. He is only paid for the fish and fish are GST free so the whole transaction is GST free. Note the fisherman would have paid GST when he bought the ice. He can still claim this back as an input credit.

For details of the ruling on ice and other mind-numbing issues such as the definition of pudding visit the Tax Reform web site at www.taxreform.ato.gov.au/ind_partner/food/issues.html

Domestic Rental Properties – Paying an Invoice

In media release Nat 2000/50 the Commissioner of Taxation announced that owners of domestic rental properties will not need to have an ABN even if their tenants use part of the premises for business purposes. Landlords don't even have to have an ABN if they are renting the property to a business that is providing the accommodation to their employees i.e. The Defence Force.

The letting of domestic rental properties does fall within the definition of an enterprise. This means owners are entitled to an ABN but there should never be a need for them to have one. This also means landlords have the same responsibilities under the ABN withholding provisions as other businesses. A landlord must withhold 48.5% of a payment for rental property expenses if the invoice does not contain an ABN.

Small Food Retailers

GSTD 2000/D2 is only a draft ruling but as 1st July, 2000 is fast approaching it is the best we can do at the moment. This ruling addresses the problems faced by takeaway food stores selling a piece of fruit or bottled water. These are some of the items that are GST free if consumed off the premises but subject to GST if the customer consumes them before leaving. These items can now be supplied GST free if the method of the suppliers operations are such that it is not clear at the time of purchase where the item will be consumed, provided the item is served in its original take away container (i.e. unopened bottle), not served at a table or any other way that indicates it is expected to be consumed on the premises.

GSTD 2000/D3 is also a draft ruling that allows basic "normal" packaging of GST free items (i.e. bottle) to also be supplied GST free. This includes as GST free basic necessities such as straws, spoons etc if no extra charge is made for them. There is a problem if the purchase includes a promotional glass or recipe etc. The whole supply can only be GST free when no charge is made for these items and the total cost price of all the non GST free supply is the lesser of \$3 or 20% of the wholesale value of the total supply.

As outlined in Newsflash 8 there are three concessions for small food retailers that do not have a till capable of separating GST Free items. They are the business norms method, snapshot method and stock purchases method. The Commissioner has released his percentages for the business norms method - they are as follows:

Type of Shop	Sales GST free	Purchases GST free
<i>Continental Delicatessens</i> (that don't sell hot foods or prepared meals)	85%	90%

<i>Cake Shops</i>	2%	95%
<i>Health food shops</i> (that don't convert GST-free Food into taxable food)	35%	35%
<i>Fish shops</i> (that sell fresh fish and some cooked fish)	35%	98%
<i>Pharmacies</i> (with both taxable and GST free Food sales)		
- Dispensary: non-claimable	98%	0%
- Over the counter	47.5%	2%
<i>Hot Bread Shops</i>	50%	75%
<i>Convenience stores which:</i>		
- Prepare takeaways	22.5%	30%
- Don't prepare takeaways	30%	30%
<i>Rural convenience stores</i> (that may sell fuel or have an Australian Post agency):		
- Converters	22.5%	30%
- Non-converters	30%	30%

Note a rural convenience store may be a converter if it prepares takeaway or hot foods. For example, it may convert GST free bread and filling into sandwiches, or GST free potatoes and fish into taxable fish and chips.

The tax office has produced a booklet titled "simplified GST Accounting Methods for Food Retailers" which is available by calling 13 24 78 or at www.taxreform.ato.gov.au.

Apportionment of Input Credits for Motor Vehicle Expenses

GSTB2000/2 explains how to apportion the input credits on motor vehicle expenses. The percentage or number of kilometres etc that you calculate for income tax purposes is not necessarily the same for GST purposes. Under GST, an input credit can be claimed only for the use (however apportioned) relating to a GST registered business. Therefore, if your estimate for income tax purposes includes travel for work as an employee or an activity that is input taxed, such as a domestic rental property, an input credit is not claimable for that portion.

While the following methods refer to the methods used for income tax purposes, it is not necessary to use the same method for both GST and income tax purposes.

Under 5,000km pa for a GST Registered Business:

Formula Method - The GST Registered Business Kilometres and the total kilometres can be estimated from odometer readings, service records or any other reasonable basis. The portion of the GST input credit that can be claimed is calculated by either of the following:

$$\frac{\text{Reasonable estimate of GST registered business kilometres}}{\text{Reasonable estimate of total kilometres}}$$

or

Set rate method

Reasonable estimate of GST Business Kilometres per year	Percentage of input credit that can be claimed
0 – 1250	5%
1251 – 2500	10%
2501 – 3750	15%
3751 – 5000	20%

Over 5,000km pa for a GST Registered Business:

33.33% or the percentage shown in a log book (prepared in accordance with the income tax law requirements) after removing travel regarding employment or a domestic rental property.

An input credit is available for the purchase of a second hand car after 1-7-2k and a new car after 1-5-2001. This is claimable in the first quarter after purchase but an adjustment may be necessary in later quarters if the percentage claimable changes. This would not normally apply to other motor vehicle expenses as the threshold for an expense to be subject to an adjustment is \$1,100 (including GST) for each individual expense.

Unlike the Income Tax Legislation under the GST estimates of expenses cannot be used to claim back an input credit. Estimates can be used only to work out the business percentage. To claim an input credit a tax invoice must be obtained (refer Newsflash 9 second page) for all expenses including the private portion. **This means all clients registered for GST must keep all their fuel receipts all year.**

If the business operates as a partnership, trust or company and the vehicle is personally owned an input credit is not claimable unless the partnership, trust or company reimburses the owner for the expense.

Wages, Commissions, Voluntary Agreements & the BAS

Voluntary Agreements – The gross amount is included at W1 and the tax withheld at W2. These amounts do not appear in any of the G boxes. Refer BAS Instruction book page 107.

Wages – This includes bonuses, leave payments, commissions, allowances etc paid to employees. Include the gross amount at W1 and the tax withheld at W2. This amount does not appear in any of the G boxes. Refer BAS Instruction book pages 107 and 50.

ABN Quoted but not registered for GST – If using the shortened BAS form described above you need only include this amount in G11 as G14 is not required to be filled out in the shortened version. But note it is not included in the calculation for G20. When entering this in Quickbooks the tax code will be NCF. Refer BAS Instruction book pages 50 and 55.

Registered for GST and Quoting ABN – Include the GST inclusive amount at G11. This amount is included in the calculation for G20. The QuickBooks tax code is NCG. Refer BAS Instruction book page 50.

Supplies on Which no Input Tax Credit can be Claimed

Newsflash 9 outlines the requirements of a tax invoice, which is a prerequisite of being able to claim a credit. The following is an updated but still incomplete list of supplies on which no GST input credits can be claimed. For those paying the following expenses care should be taken to ensure you do not attempt to claim an input credit for them:

All items classified as input taxed or GST free, many of which are listed below.

- Expenditure over \$55 where no taxed invoice has been kept
- Life Insurance
- The stamp duty portion of all insurance policies
- Residential Rent – even if part of the premises are used for business providing the actual premises are of a domestic nature.
- A piece of Real Estate acquired where the vendor used the margin scheme
- Acquisition of residential premises
- Precious Metals and subsequent supplies
- Sale of existing business by shares
- Sale of existing residence
- Financial supplies i.e. bank fees and interest on loans but not merchant fees.
- Basic Foods as per ATO web site - a 29 page list.
- Payments made under a Voluntary Agreement.
- The private portion of any expense.
- In relation to any item that is not tax deductible
- Salary, wages and allowances
- Superannuation
- Entertainment
- Fines and Penalties

- Any expenses associated with domestic rental properties i.e. this goes as far as having to apportion motor vehicle expenses.
- Most Federal and State Government Fees: i.e. Rates, Occupational Health & Safety – Licences to operate plant, Income Tax, Fringe Benefits Tax, Wool Tax, Medicare Levy, Various ASIC Fees, Primary Industry Levies, Drivers' & Boat Licences, Various Court Fees, Tax Agent Registration Fees and Pay-roll tax. In other words when dealing with a government department it is important to check whether GST is included in the price paid.

Super Contributions for Employees & the BAS

No input credit is allowed for superannuation contributions made by employers for their employees because GST is not charged on superannuation. Normally when an expense has no GST in the price the amount is included at G11 and then deducted at G14 on the BAS. This is not the case with superannuation. It is neither included at G11 nor G14. Superannuation Contributions are totally excluded from the BAS. Refer Newsletter No. 4 of the Primary Production Industry Partnership.

Cash Basis BAS Rules

Refer GSTR2000/23. Despite being on a cash basis the BAS is not governed by when amounts appear on the bank statements. When a payment is received by cheque the payee includes the amount in their BAS when the cheque is received. The payer includes the payment when the cheque is posted or handed over. When payment is made by credit card the payment is recorded in the BAS by both the Payee and Payer when the slip is signed or details are given over the phone. When payment is received via an agency (i.e. commercial rental property) the NTAAs have a ruling stating that the amount is included in the Principal's (Landlord's) BAS when the Agent notifies the Principal of the payment being received.

Telstra Advertising Fees

Telstra have been asking customers to pay the GST up front. If you report GST on an accruals basis then you can claim the whole input credit when making the first payment but you will have to bring the whole amount of the debt into account. For example, assuming GST of \$100 plus 4 quarterly instalments of \$250 each, in QuickBooks bill entry the cheque amount for the first payment i.e. GST up front plus first quarterly instalment, would be \$350:

Account	Tax Code	Net Amount	Tax Amount
Advertising	NCG	1,000.00	100.00
Accounts Payable		-750.00	

If you report GST on a cash basis you will not be able to claim the full input credit for the up front payment until the whole amount is paid as under section 29-5 you can claim an input credit of only 1/11th of the amount paid each time. Therefore the entry for the same \$350 on a cash basis would be:

Account	Tax Code	Net Amount	Tax Amount
Advertising	NCG	318.18	31.82

Finer Points for BAS

Be careful not to claim an input credit for supplies from suppliers who are not registered for GST (i.e. because their turnover is under \$50,000). It is also not necessary to include these payments in G11 and probably more practical not to if using the concessions on the G items mentioned in the first article of this Newsflash. If using QuickBooks, use the NCF tax code.

Don't pay GST or include in G1 any money received after 30th June 2000 if the service or goods were supplied before or on that date. This is so even if you are reporting for GST on a cash basis. Don't claim an input credit for payments made for goods or services supplied before or on 30th June 2000. It is not necessary to include these amounts at G11 or G10 but, if you do, make sure they are also included at G14 or removed before you calculate your input credit if you are using the abridged BAS mentioned in the first article of this Newsflash.

Lay-bys claimed after 30th June 2000 are subject to GST on the full original price of the goods.

Working out Your Workcover Payment

It has come to our attention that it can be very confusing when trying to work out the GST component of a Workcover Policy. A quick call to Workcover has resolved this problem.

GST is charged as listed below. The amount at (2) needs to be divided by 1.05 to remove the stamp duty component of the credit as stamp duty is added on after GST.

To record this transaction in Quickbooks you must first enter a bill for 1,3 & 4, (it is best to enter each component to save confusion if you need to look back at a later date)

Bill

Account	Tax	Amount	Tax Amount
Insurance	NCG	2281.01	228.10 Assessed premium for 1999/2000
Insurance	NCG	2419.20	241.92 Plus Provisional Premium for 1999/2000
Insurance	NCG	89.37	8.93 Plus Late Payments (if any)
Insurance	PLR	167.25	0.00 Stamp Duty not shown at G11
		4789.58	478.95 = Total Bill \$5,268.53

then a credit for 2. Note that the credit for 2 needs to be split into two lines:

Account	Tax	Amount	Tax Amount
Insurance	NCG	1659.41	165.94 Provisional Premium for 1999/2000
Insurance	PLR	82.97	Stamp Duty not shown at G11
		1742.38	165.94 = Total Credit 1908.32(including GST)

You then use pay bills function to make payment and apply credit.

Assessed Premium for 1999/2000 - 10% GST

1. Less Provisional Premium for 1999/2000 – divide by 1.05 to remove stamp duty – then 10% GST
2. Plus Provisional Premium for 1999/2000 – 10% GST
3. Plus Late Payments (if any) – 10% GST

QuickBooks BAS Worksheet

The following are internal notes generated at a meeting we had to discuss a simple reconcilable method of preparing a BAS that would suit most of our clients. Note this is not for clients who make input taxed supplies. The following assumes that your BAS is prepared on a cash basis but is easily adaptable to accruals. Note certain expenses are not included in the BAS at all, they are not even put in at G11 and reversed out at G14. These expenses include insurance excess, wages, superannuation and the stamp duty.

Object: To complete G1,G2,G3,G9,G10,G11,G12,G14&G20 of the BAS

Procedure:

- 1) Check that all items (the codes for transactions on the invoice) are allocated to income accounts
- 2) Check that all expenses, cost of goods sold and income entries have one of the following codes in the tax code column:

- PLR Profit and Loss Reconciliation** -All amounts that do not go in any of the following but are expenses, cost of goods sold or income.
- QFA Questions for Accountant** – If unsure of which tax code to apply or whether a tax code is necessary, put QFA as the tax code so we will know which ones to check.
- NCG Non Capital Acquisitions with GST** – Expenses or cost of goods sold with GST included in the price. These amounts go in G11.
- NCF Non Capital Acquisitions with No GST** – Expenses or cost of goods sold where GST is not included in the price. These amounts go in G11 and G14.
- CAF Capital Acquisitions with No GST** – This is for expenditure of more than \$1,000 on plant and equipment, that is items that are used but not used up in the business, but only when there is no GST included in the price i.e. a compressor bought at a garage sale. These amounts go in G10 and G14. Note special rules apply to Hire Purchase acquisitions if reporting on a cash basis.

- CAG** **Capital Acquisitions with GST** – This is for expenditure of more than \$1,000 on plant and equipment, that is items that are used but not used up in the business. These amounts go in G10. Note special rules apply to Hire Purchase acquisitions if reporting on a cash basis.
- GST** **Income on which GST is Payable** – These amounts go in G1. Mostly this would be sales but if any business equipment is sold (including a motor vehicle used even just partly in the business) this must also be included here.
- FRE** **Income on which No GST is Payable** – These amounts go in G1 and G3. This applies if you supply goods that are GST free such as basic food.
- INT** **Interest Income** – This amount is included at G1 but removed again at G4.
- CAP** **Sale of Capital Items** – This code is only to be used when you sell capital items i.e. equipment and vehicles. The total amount received from the sale must be included at G1. But as this sale is a capital item the proceeds of the sale will appear in the balance sheet so just like CAG and CAF amounts coded to CAP are not included when reconciling to the Cash Gross profit. It is advisable that you seek an accountant's advice when preparing your first BAS where you have sold a capital item.
- BLANK** Can only be used for payments that are not capital acquisitions or are not income, expenses or cost of goods sold. e.g. drawings
- 3) To ensure no GST or input credits are missed it is necessary to reconcile the total of all GSTs, FREs, INTs and PLRs on income, with the income total on your Profit and Loss Report. All NCG's, NCF's and PLR's on expenses should balance with the total of your cost of goods sold and total expenses. Ensure that the Balance Sheet balances and reconciles to the profit and loss statement. If the above accounts don't balance check that sales have not been entered using the make deposits function as it does not allow entry of tax codes. *Note that you need to make sure your reports are customised to cash and gross for Cash GST accounting method or accrual and gross for non-cash (Accrual) GST accounting method.*
 - 4) Look at Fixed Assets for any capital transactions that will effect the BAS, these should have been coded to CAG or CAF or CAP.
 - 5) Look at Hire Purchase repayments and claim GST on principal portion only if applicable. This is applicable if reporting on a cash basis and the contract specifies what interest is charged.
 - 6) Check for a claim for sales tax paid on trading stock.
 - 7) To bring into account amounts received after 30-6-2k for pre GST invoices. Create an accounts receivable report and make certain that each outstanding invoice has a PLR tax code.
 - 8) Check accounts payable at 30-6-2k to ensure they are all coded PLR.
 - 9) Look at Insurance to check stamp duty has been removed before GST calculated.
 - 10) Check detailed tax liability report to insure GST is always 10%.
 - 11) In the first BAS include any GST paid before 30-6-2k i.e. insurance premiums, annual subscriptions etc.
 - 12) Check that all combined private and business expenses have been apportioned.

Income Activity Statement – T1

T1 is not necessarily the same as G1. T1 usually includes income from business on an accruals basis yet in most cases G1 includes business income on a cash basis. Note you can elect to measure T1 on a cash basis.

A simplified definition of income measured on a cash basis is all the actual cash, cheques and credit card transactions received in relation to the business during the period. Income measured on an accruals basis is the total of all invoices dated within the period but does not include loans to the business.

The business income included at T1 is only sales in the normal course of the business so (unlike G1) it does not include the proceeds from sale of equipment and motor vehicles. Further G1 is the GST inclusive value of sales whereas T1 is the net amount after deducting GST. But it does include the proceeds of the sales tax credit for trading stock. If any income has been subject to the ABN withholding rate of 48.5% the full gross amount must be included as T1 not just the net amount received. If you are a sole trader you also need to include income from outside the business such as interest, gross rent, dividends, royalties, your share of any other trust or partnership income. If you are a partner your share of income from the partnership is subject to the formula above "Partnership PAYG Instalment Rates" but, after calculating that amount, you must also include at T1 interest etc the same as sole traders. If you are a beneficiary of a trust get an accountant to calculate your T1.

Employee Contributions for FBT and the BAS

On the 21st May, 2001 the Commissioner released GSTR 2001/3 which deals with employee contributions towards fringe benefits, being subject to GST. Unless the employee makes the contribution by way of paying the actual expenses associated with the benefit (such as fuel) and no input credit has been claimed on those expenses the taxable employee contribution is to appear in the BAS in the quarter in which it is received if the BAS is on a Cash basis. According to GSTR 2000/D17 paragraph 24, if the BAS is on an accruals or non cash basis all of the employee contribution is included in the BAS in which the first amount is received or when a bill is issued to an employee unless the full amount is not known then only the amount received is included.

While the ruling doesn't address this I believe the legislation supports that the full amount of the contribution should be included when the supply is made if this is the first thing to happen and you are reporting on a non-cash basis. As the last FBT year started before the GST was introduced an amount paid for a benefit received over this particular FBT year 1st April 2000 to 31st March 2001 should be amortised over the period the benefit was provided to see if there is a pre GST portion on which no GST will be payable.

Unfortunately the ruling only looks at the limited circumstances of employees who are not owners of the company. Many of our clients own companies or trusts of which they are employees. They don't pay fringe benefits tax because they make employee contributions to cancel out the benefit. Many clients may not even be fully aware of this because until now the entry has been made by journal entry by the accountant when the tax return is done. This is permitted to be done retrospectively under ruling MT2050. GSTR2001/3 accepts that the employee can make a contribution after the end of the FBT year and have it apply to that year. So in order to be technically correct the journal, when made should not be back dated as it has been in the past but dated the date it is made. This way it can be correctly recorded in the BAS for the period when the accountant is doing the work. Just make sure you get this information for your BAS. We have written to the ATO to confirm that this is the right approach but many clients will have to act before we are likely to get a reply, so we have had the above approach confirmed by the NTAA.

The above probably applies to you if your vehicle is owned by a trust or company and you are not in the maximum tax bracket, or if an employee makes contributions to you.

In Short, What to do Now?

If you have employees who make actual contributions during the year and you prepare your BAS on a cash basis you will have to enter these amounts on the BAS for each period they are received. If you prepare your BAS on a non-cash accruals basis you have to include all the future payments when the first one is received or you issue a bill or the goods are supplied unless the total amount is uncertain. This should not be a problem if the contribution is for goods as they have been supplied so the amount should have been set. The problem arises when a car is provided on an ongoing basis. There seems to be a good argument here that the total amount is not certain so the contribution only needs to be included when it is received or the journal entry made. In the latter case where you are at risk of missing this one off entry as it does not go through the cashbook. So if you are preparing your own BAS don't forget to ask your accountant for this amount when the business income tax return is done.

Some employees will be making an annual contribution in the June quarter as in most cases this is the quarter when the liability is calculated for the FBT return. The fringe benefit calculation for motor vehicles based on the formula method is reasonably simple. So once shown by your accountant you should be able to do it yourself in future years. But note when the car has been held for more than 4 years, at the beginning of the FBT year, the cost base in the formula is reduced to 2/3rds of the original cost. If you are accounting for the car on a log book basis the fringe benefit calculation is much more complex.

BAS Audits

The following are extracts from a checklist of questions used by the ATO during an audit:

- 1) Confirm that the amounts at G10 and G11 reconcile with the accounting records. *This should be a fun exercise considering the stamp duty is not included in G11 but is in the accounts, the same applies to insurance excesses and wages. The difference between G10 and G11 will be even more fun as capital assets are over \$1000 in the BAS but over \$300 in the accounts.*
- 2) Reconcile G10 to the asset register and check the actual asset.
- 3) Check that goods for own use are taken into account.

Selling Motor Vehicles and Plant and the GST

In Newsflash 10 we warned how if you claim an input credit or a tax deduction for any durable item that was partially business and partially private, you would have to pay a full 1/11th of the selling price in GST regardless of how small the business percentage you claimed was. TLAB 8 has rectified this disparity. The GST on the sale is now apportioned the same as the claim for input credits. This amendment to the law has been made retrospective to apply from 1st July, 2000. Accordingly, some clients may need to amend their BAS. The full amount of the GST on sale is included on the output side of the BAS but an adjustment for the private portion is included in the input side of the BAS.

Note there are exceptions as the availability of this concession. The above will not apply if any of the following apply to the vehicle or plant:

If there was no input tax credit entitlement on the original purchase price of the car. For example if it was purchased new before 22nd May, 2001 or second hand before 1st July, 2000 or was purchased when the owner was not registered for GST.

The seller of the vehicle or plant did not charge GST. For example a private sale.

Thresholds – GST Inclusive or GST Exclusive

The Minor Fringe Benefit limit of \$100 is the GST inclusive price. The value of all fringe benefits is the GST inclusive price.

The \$300 plant and equipment limit regarding immediate write off of the expense is the GST inclusive price.

The \$1,000 threshold for taxpayers in the simplified tax system to be able to write off the purchase price of an asset is GST exclusive.

To switch to the Simplified Tax System you must have an average income of under \$1million per year. This amount is GST exclusive.

Prepayments are still fully deductible to all taxpayers if the amount is under \$1,000 (GST Inclusive),

The \$20,000 income threshold (section 35-30) to allow the offset of a business loss against other income is the total sales after removing the GST. Note also the \$20,000 total sales is per partnership not per partner providing all the partners are individuals (section 35-25).

Thankfully our Government has tax simplification as a priority.

The New BAS

You have probably noticed that the new look BAS has replaced the word acquisitions with purchases and supplies with sales. This does not mean the definition of what is to be included in the boxes has changed. To quote the BAS Basics Guide for June 2001:

The labels on the form and calculation sheet still mean the same things. G1 is still G1 and 1A is still 1A.

You should still refer to the BAS Instructions for the definitions of, and detail on, each label.

The worksheet that is available to support the new look BAS has the same boxes as the old BAS. Therefore you are still required to include in G1, G11 & G10 items that do not include GST and then remove them before calculating the GST. Further as the definition of what actually goes in the box has not changed items that do not fit the description of sales or purchases are still included as they have been in the past. For example interest income is included in G1 but removed before you calculate the GST as no GST is payable on interest.

Note if you opt to pay your GST on an estimate you are must continue to use this method for the rest of the financial year. So if you chose option 3, to pay the GST installment amount, in the March BAS you must do the same in the June BAS. If you did not choose option 3 in the March quarter you cannot switch to it in the June quarter unless the addition of your last two GST payments results in you paying GST not receiving a refund.

Motor Vehicle Purchases & GST

Please make sure when purchasing a motor vehicle that you obtain a Tax Invoice if you wish to claim back the GST for business purposes. The Purchase Contract does not constitute a Tax Invoice.

GST Audit Warning

The ATO have begun their public awareness audits. Some auditors are not as aware as others and they can be very forceful in their opinions. The following are some examples.

Invoices over \$1,000 are required to show the purchaser's name and address or name and ABN. Directors and employees sometimes get these invoices in their own names. We have experienced an ATO auditor claiming that the invoice is not a correct tax invoice because it shows the employee's name not the company or trust name. This interpretation by the ATO is not correct in fact it contradicts their ruling GSTR 2000/17 at paragraphs 73 and 74 so don't be bullied. The ruling states:

Division 111 has special rules covering the situation where you reimburse an employee, an officer of a company or a partner for an expense they incur for an acquisition directly related to that position. Providing the requirements of the Division are met, the reimbursement is treated as consideration for an acquisition you (or the company) make from that person. You (or the company) may claim the input tax credit for a creditable acquisition if you hold the tax invoice that was issued to the person you (or the company) reimbursed. The tax invoice may identify that person and not you (or the company) as the recipient of the taxable supply.

A Family Day Care provider came to us after she felt that an ATO auditor was over the top in disallowing claims for food and a pet dog. We used the day care manual that encourages party foods and the use of pets to entertain children as evidence that these items were acceptable business expenses.

The ATO has been particularly fussy about when an account has been paid. As most BASs are prepared on a cash basis this is relevant but hardly important as one quarter or the other you still end up being entitled to the claim. Nevertheless, if an expense is paid in cash it is difficult to argue that the invoice has actually been paid. We have even experienced an auditor not being satisfied with a receipt as proof that the account had been paid because it had been paid in cash so there was no record on the bank statement. There is not a lot you can do to protect yourself here other than telling them you will see them in court knowing they would never get ATO support to fight such a silly case. It is worth writing on an invoice how it was paid and on what date.

ATO auditors are checking bank statements and arguing that income should be included in the period it is deposited and expenses when the cheque is presented. This is not correct, the definition of cash basis considers income to be received when the cheque or cash is received not when it is banked. Expenses are incurred when the cheque or cash leaves your possession. Refer GSTR 2000/23 which states at paragraphs 17 and 18:

When a payment is made by tendering Australian currency, consideration is both provided and received when the payment is tendered. When payment is made by way of cheque, the recipient of the supply provides consideration when the cheque is either handed or posted to the supplier. Consideration is received by the supplier when the cheque is received, not when it is banked, or cleared.

An auditor has even complained that a typical tax invoice issued over the counter is not evidence that the account has been paid. So if you are paying in cash it is worth keeping the cash register tape if possible or getting the cashier to sign the invoice as paid in full. Again this is just harassment by the ATO and they would not win a court case but it is better to avoid the fight.

If you have experienced a GST audit and been told something that you have trouble swallowing please let us know so we can research it and print the result to help others. Note the books issued by the ATO are only the ATO's interpretation of the legislation, which we have, on many occasions, found to be incorrect. In fact they are alarmingly misleading. Don't be bullied!

BAS Warning

Please do not go back and change any data for that quarter after your BAS has been completed. If you need to change an invoice, issue a credit note in the current quarter and a new invoice. The same with any expenses. Never date anything a date within a quarter for which a BAS has been completed.

Latest Changes to BAS by ATO

The ATO has issued a newsletter called BAS Basics in which they make a few concessions. A summary of these changes are listed below:

They give more publicity to the Accounts method of preparing the BAS. This method has been available since 1st July, 2000. All clients who have been shown how to prepare the BAS by this firm are already using this method.

If your annual turnover is less than \$1 million and you don't record your capital acquisitions separately, only capital acquisitions costing more than \$1,000 need to be included in G10. Please note that for income tax purposes until 1st July, 2001 only capital acquisitions costing less than \$300 can be considered non capital acquisitions but anything over this amount must still be included in the depreciation schedule as a capital acquisition. Accordingly, in order to avoid problems with your income tax return we recommend that you continue to segregate capital investments at the \$300 threshold until 1st July, 2001. For GST purposes you will still be allowed the full input credit anyway - it is only a question of into which box you put the item on the BAS.

The amounts you show at G1, G2, G3, G10, G11 & G14 can now be either GST inclusive or exclusive.

The amounts shown at 1A and 1B on the front of the BAS no longer need to reconcile to the amounts shown in the G boxes. Makes you wonder why you now need to fill out the G boxes.

Understanding the GST Attribution Rules

Basically subdivision 29-5 to 29-10 of the GST legislation states that if you report for GST on an accruals (non-cash) basis you account for GST or claim input credits in the period any payment is received or made or, if earlier, when an invoice is created or received. Note under the accruals method if it is the payment of an amount that comes first the whole amount of the contract is accounted for in that period even if it is only a part payment. The reverse is true if you report for GST on a cash basis. That is, you can only claim an input credit for amounts actually paid and you need only pay GST on amounts actually received. Some examples of areas when this could become a problem are considered below. Check that you understand which reporting method applies to you.

Accruals Reporting:

If a customer pays you a deposit the whole contract is included in the GST period the deposit is paid. So make sure your deposit is more than 10% as you will be sending 1/11th of the whole contract price to the ATO probably before you get the next installment from your customer.

Cash Reporting:

When using a loan or hire purchase to acquire equipment you are considered to be borrowing the money and have fully paid for the goods. So an up front input credit can be claimed on the whole amount of the purchase. Note not the total amount of the repayments as these include interest. The repayments on the loan are simply paying back your debt plus interest the latter being a financial supply (no input credit available). But if you want to be totally correct in your BAS you should calculate the interest portion of each repayment (usually on a reducing balance method). Put the interest portion in at G11 on the BAS and remove it again at G14.

If you buy the equipment under interest free terms but do enter into a finance arrangement then you can claim the purchase price of the goods up front and there is no need for further entries as no interest applies.

If a supplier simply lets you pay off the equipment over a period of time and no separate finance agreement has been entered into you can claim an input credit only for the amount you have paid in that period.

The Latest Concessions Regarding the BAS

Due to the backlash the Howard government is facing regarding the burden it has placed on businesses with the BAS, it has made the following concessions. Note businesses with a turnover of more than \$20 million are not addressed here:

- 1) Businesses with a turnover of \$2 million or less will have the option of lodging an annual BAS but still be required to pay their GST quarterly. The payment will be the amount they paid for the December Quarter. For the 2001/2002 financial year the December quarter will still be used, until the annual BAS has been lodged, but an uplift factor for any changes in the Gross Domestic Product will be added to payments made for periods after 30th June 2001. The annual return has to be lodged when the income tax return is lodged or by 28th February 2002 if earlier. The annual return will include Total Sales (G1), Exports (G2), Other GST-Free (G3), GST Payable (1A & 1B), Capital Purchases (G10) and Other Purchases (G11). You will be notified by the ATO of the amount you are required to pay each quarter and you can vary this amount if necessary. But if you do apply for a variation and the total GST paid by the 4th quarter is less than 85% of the actual GST for the year, interest charges will apply. Note the simplified instalment method is only a method of payment so if you use this method you will not be able to collect any net refunds for a quarter

until the end of the year when lodging the annual return. Therefore this method should not be used for GST-free suppliers, exporters, if your GST liability is erratic or if you intend making a large capital acquisition.

- 2) The BAS form will be simplified for businesses with a turnover of less than \$20 million but over \$2 million that cannot take advantage of 1) above and who lodge quarterly. The quarterly form will only require Total Sales (G1), GST Collected (1A) and GST Paid (1B) to be completed regarding the GST, note other taxes may apply. But they will also be required to lodge an annual return showing exports (G2), Other GST-free Sales (G3), Capital Purchases (G10) and Other Purchases (G11). You can avoid lodging the annual return by providing this additional information each quarter. This would effectively mean that you continue on the way we have shown you except that we have advised that you complete the box for acquisitions that do not include GST (G14) so that your G11 & G10 reconcile to 1B.
- 3) For all future years the December BAS will not be due until 28th February. This is later than the due date they allowed this year so if you received a late lodgment fine it is worth applying for it to be remitted.
- 4) All other quarterly GST payment deadlines will now be 4 weeks after the end of the quarter except for the quarter ending the 31st December which will be due by the 28th February. Note monthly remitters will still be required to pay their GST 21 days after the end of the month for every month.
- 5) Monthly statements will only contain 7 GST boxes: Total Sales (G1), GST collected (1A), GST paid (1B), Exports (G2), Other GST-free sales (G3), Capital Purchases (G10) and Other Purchases (G11). This would effectively mean that you continue on the way we have shown you except that we have advised that you complete the box for acquisitions that do not include GST (G14) so that your G11 & G10 reconcile to 1B
- 6) New businesses will have to report as per 2) above (over \$2 million but under \$20million) for the first 2 quarters before they will be allowed to use the instalment method adjusted for GDP as per 1) above.
- 7) Business taxpayers with a turnover of under \$1 million, who are registered for GST, will be given the option of reverting to the old provisional tax method of the ATO advising them of the amount they have to pay which will be based on the previous year, rather than paying their income tax at their PAYG instalment rate. But quarterly payments will still be applicable unless their total tax due is under \$250. This includes Sole Traders, Partners, Companies and Superannuation Funds.

I believe the ability to pay GST based on a predetermined rate set by the ATO is too late to help most of our clients as they have finally managed to accommodate the GST. I recommend that these clients continue to do a quarterly BAS because they have already gone through the tears and expense of setting themselves up. So they should at least take the advantage of knowing their true liability. At least they won't be in for a shock at the end of the year or pay too much GST and stretch their overdraft. This will also save them having to complete an annual BAS. We will still be preparing ours quarterly. On the other hand clients that still require our assistance to prepare their BAS may want to consider an annual BAS to save accounting fees especially if their GST liability is not likely to be large anyway.

Reminder about Increased Late Lodgement Penalties

Since the 1st July 2000 the ATO has had the power to fine taxpayer \$110 for every 28 days you are late in reporting your tax obligations.

ATO Written GST Advice Wrong 22% of the Time

As part of the ATO's 2000/2001 Annual Report the quality of its written advice on GST was reviewed. It was discovered that 22% of the time this advice was incorrect. Just imagine how inaccurate their verbal advice has been.

When Ceasing to be Registered for GST

Division 138 of the A New Tax System (Goods and Services Tax) Act 1999 covers a taxpayer's responsibilities when a business ceases or just ceases to be registered for GST.

Division 138 Subsection 5 states that you must make an adjustment for any assets the business has been using and are still held at the date of ceasing GST registration. If when you purchased that asset you claimed an input credit and the adjustment period for that asset has not yet expired. The adjustment period is determined by the original cost of the asset to you (Section 129-20). If the asset cost you \$5,000 or less (GST exclusive) your adjustment period extends up to the fourth 30th June after the original input credit was claimed for the item. If

the asset cost more than \$5,000 but less than \$500,000 (GST exclusive) the adjustment period extends up to the seventh 30th June after the original input credit was claimed for the item. If the asset cost more than \$500,000 (GST exclusive) the adjustment period extends up to the twelfth 30th June after the original input credit was claimed for the item. The amount of the adjustment is 1/11th of the market value at time of cancellation or the amount you originally paid if less than the market value. This amount is apportioned if there is some non business use of the asset.

Division 138 Subsection 15 allows an entity registered for GST and accounting on a cash basis to prepare its last BAS, upon cancellation of registration, on an accruals basis. So bringing into account any transactions that may not have yet been paid.

Naturopaths & GST

The services (goods are discussed further on) you provide will be exempt from GST if one of the following applies to you (Reference Section 37-10 GST Act and section 21 Regulations GST Transitions):

The laws of the State or Territory where the service is provided require government permission to provide these services, it is sufficient if you have this permission.

If there is no government control. This section sets out the requirements depending upon whether the practitioner commenced practising before or after 8th July, 1999.

After 8th July, 1999 you need to have a diploma, advanced diploma or degree in the discipline by completing an accredited course of study. To be an accredited course it must be accredited as a higher education course by the authority responsible for the accreditation of higher education courses in the State or Territory in which the course is conducted.

Before 8th July, 1999 there is a choice between the requirements of (i) and having been a member of a national professional association of practitioners in the discipline before 8th July, 1999 and continuing to be.

For the service to be GST free it must be generally accepted, in the profession associated with supplying services of that kind, as being necessary for the appropriate treatment of the recipient of the supply. Reference Section 37-10 (1) (c) GST Act.

For goods supplied as part of Naturopathy, to be GST free they must be consumed during the service (Section 38-10(4)) or be exempt because they are a food (Subdivision 38-A). The ATO issues register states that only Ginger, Cinnamon, Cardamom, Turmeric and Licorice would be exempt as food. They would lose their GST exemption if they are mixed or if supplied in tablet or capsule form. The above seems a very narrow view of the definition of food according to the GST Act includes, among other things:

“food for human consumption (whether or not requiring processing or treatment), ingredients for food for human consumption and goods to be mixed with or added to food for human consumption (including condiments, spices, seasonings, sweetening agents or flavourings.”

I would like to see a professional organisation for Naturopaths challenge the ATO on limiting their interpretation to few items and only when they are not mixed.

To be required to charge GST you must have a turnover of \$50,000 or more of items that, if you were registered for GST, would be subject to it. For Naturopaths that meet the professional requirements of section 21 of the GST Transition Act this means you may only have to count the herbs etc. that you supply to patients, for consumption outside your office, in that \$50,000 so many sole practitioners will be completely free of GST anyway. Note it is very important that you are diligent in reviewing the \$50,000 threshold as the ATO can come along later and take 1/11th of your total turnover from you as GST, if you are wrong in any year. The rule is you must each month consider the last 11 months (for seasonal changes) and the likely outcome of the next 11 months based on the current month's turnover. In most cases as soon as you have a month where your sales that would be subject to GST (if you were registered) exceed \$4,166 you should register. Note: if the majority of your services are exempt from GST it maybe in your best interest to register so you can claim input credits on your expenses

GST Concessions for Land Developers & Rental Car Costs

Land Developers will not be subject to GST on land they give to local government authorities in return for the right to develop an area. For example an in kind contribution of park land. These transactions were caught under the GST legislation so the government has introduced Taxation Laws Amendment Bill (No3) 2002 to correct this. If the bill is accepted by Parliament it will apply retrospectively back to 1st July, 2000.

Rental Car Companies will be entitled to a special credit for the GST they have had to remit to the tax office when they have sold rental cars. Note this credit is reduced if the car was under an eligible short-term lease agreement with the ATO back in the days of sales tax. For a car to qualify for the special credit the following conditions must have been met:

- 1) It must have been sold for the first time during 1st July 2000 and 1st July 2002.
- 2) The car must have been held by the rental company at 1st July 2000
- 3) The car must have been used as a rental car from 1st July, 2000 until sold and have the appropriate third party insurance.
- 4) Sale tax must have been paid by the rental company when the car was first purchased.

The tax credit cannot be claimed until the first BAS you lodge after the Taxation Laws Amendment Bill (No3) 2002 is passed by Parliament, but it will apply to seals of cars dating back to 1st July, 2000.

Tips and GST

The ATO document *The Taxi Industry and the New Tax System* states that tips are not subject to GST. This could apply to other industries as the wording of the document is as follows:

“A genuine tip, paid on a purely voluntary basis by a customer, is not subject to GST. If the tip is not voluntary, for example, a pre-set amount or otherwise defined as a service charge or similar, the amount will be subject to GST. If a voluntary tip is paid with a credit card it is not subject to GST if the amount of the tip is given to the person for whom it was intended.”

30th June 2002 First Adjustment Period for GST

If you are registered for GST and incurred an expense, since 1st July, 2000, that has both a business and private use you have had to estimate an apportionment percentage when claiming the GST back in your BAS. If the amount of the expense is more than \$1,000 (net of GST) you are required to review this apportionment at regular intervals and make an adjustment in your BAS if the ratio of business to private use has changed. Note because of the \$1,000 (net of GST) limit you would probably only think of durable assets but this could include a large motor vehicle repair. The intervals that you are required to review your apportionment are determined by the original cost of the item as follows:

\$1,001 to \$5,000 net of GST -12 months after the first 30th June after the purchase and again 12 months later. For example purchase in July 2000 the first adjustment date is 30th June, 2002 the next adjustment date is 30th June 2003 and no more after that.

\$5,001 to \$500,000 net of GST -12 months after the first 30th June after the purchase and again 12 months later and each year after that for the next 3 years i.e. 5 adjustment periods. For example purchase in October, 2001 the first adjustment date is 30th June, 2003 then 30th June, 2004 then 30th June 2005 then 30th June, 2006 then 30th June, 2007 and no more after that.

\$500,001 or more net of GST - 12 months after the first 30th June after the purchase and again 12 months later and each year after that for the next 8 years.

Note the above is different if you are making financial supplies

Becoming Registered for GST or De-Registering

Registering for GST – Division 60 deals with pre-establishment costs. An input credit can be claimed on items purchased for the business before it is established. The claim cannot be made until the business is registered for GST and has reimbursed the person who incurred the expense on its behalf. A business that is established but not registered for GST i.e. turnover has gone from under \$50,000 to over \$50,000 can only claim the GST back on its trading stock on hand when becoming registered (Division 137). But note you cannot claim the GST back if you were previously registered for GST and held that particular stock when you de-registered.

De-registering for GST – If you cancel your GST registration you must pay back the input credit you have claimed on any assets or stock you still have when you de-register (Division 138). Note if you never paid GST on the item you do not have to pay it back when de-registering. But if you were entitled to claim the GST input credit but didn't you are still caught by this section and will have to pay GST on the item when you de-register. If the item was only partially used for the business then you only have to pay GST on that portion. The amount you pay GST on is the original price you paid or the current market value whichever is the lesser. This does not

apply to any assets for which all the adjustment periods have passed. Refer Newsflash 37 for details of adjustment periods.

GST Pedantics

ID2002/679 – Dietary Services - To be GST free they must be supplied by a member of the Dieticians Association of Australia and to be considered necessary for that particular individual by the dietary profession.

ID2002/687,8,9 – Antenatal/Postnatal Exercise Classes- For these classes to be GST free they must be conducted by a registered physiotherapist after an initial interview is conducted to determine whether the classes are appropriate for the particular client. Further the classes must be generally accepted as necessary by the industry. The actual class may be run by an assistant to the physiotherapist.

ID2002/686 - Farm Managers Residence- Renovations etc are still considered to be input taxed regardless of whether the manager is charged rent or not. In other words the property is considered to be a domestic rental, therefore no GST credits can be claimed on any expenses.

Developers who Decide to Rent out House Built for Resale

Newsflash number 33 outlined the extreme GST consequences if a developer decided to rent out a property before it is sold. The problem arose because no GST input credits are allowed for a property used for domestic rental. The entitlement to input credits was pro rataed on a time basis. As in these sorts of cases about 95% of the time the property was held and it was rented out, only 5% of the GST input credits on the land and building costs are claimable yet full GST (subject to use of the margin scheme) is payable on the sale because it is the first sale of a new home.

In the Property and Construction Industry Partnership Issues Register item number 4 the ATO has now agreed to pro rata the input credits on the basis of income received . The formula for apportioning input credits between the taxable supply of the home and the input taxed supply of rental accommodation is as follows:

Consideration for the taxable supply of the premises

Consideration for the taxable supply of the premises plus rental income

Note the above explains the calculation but spares you the details of how this is dealt with in each adjustment period as these changes do not change the article in Newsflash 37 on adjustment periods.

GST & Expensive Cars

ID 2002/693 may surprise you with its approach to deciding if a car exceeds the car limit which is currently \$55,134. This is not a simple matter of whether this amount is GST inclusive or exclusive. The car limit determines what portion of the cost price of the car can be depreciated. The car limit also determines the maximum amount of GST input credit claimable. Basically the ruling states that the cost of the car is reduced by any input tax credit before the car limit is applied. So if you buy a car in the 2002/03 financial year and it costs more than \$55,134 even if it is used 100% for tax-deductible purposes the maximum input credit you can claim is \$5,012. If a car's cost exceeds \$55,134 to determine whether the purchase price exceeds the cost limit for depreciation purposes deduct \$5,012 from the purchase and then see if it exceeds \$55,134. If it does you can only claim depreciation on \$55,134. To make sense of this formula you have to accept that logics will always loose out to the ATO's passion for double dipping. First you pay GST on a vehicle you use for the business. But unlike other business expenses you are not entitled to claim the full GST credit back. On top of this you are not entitled to claim a tax deduction for this portion of your business expense. This means you are taxed twice on the dollars you use to pay the GST, firstly when they take the GST on purchase and again when you earn the money to pay the GST as in these circumstances it is not considered a tax deduction. Then after all that when you sell the car you must pay the ATO GST on the full selling price multiplied by the percentage of business use of the vehicle.

GST on Winnings and Prizes

GSTR2002/3 states that there is no need to remit GST on trophies, medals or ribbons received as a prize if these have little or no actual value. GST is also not payable by Amateurs such as school children, TV games show contestants and sports people who are not in the "enterprise" of being a sports professional. But if the

person receiving the award, that is of some value, do so as part of their business and that business is registered for GST then they must remit 1/11th of the prize money or market value of the prize to the ATO.

Secret Plans and Clever Tricks

Adjustment periods for any expenditure over \$1,000. This is the amount of each individual item or service. For example GSTR 2000/35 states that each progress payment is for a separate acquisition so it does not matter if the final product is over \$1,000 it is the individual items invoiced that count. There may be an advantage gained here by packaging items into invoices under \$1,000 where ever possible.

Partnership, Cars and GST

The following only applies to partnerships. When a car is sold and it has been used in the business and owned by someone who is registered for GST, GST is payable on the proceeds of the sale. The ATO considers it to have been used in the business if input credits or a tax deduction have been claimed for its expenses.

Assuming the partners themselves are not also registered for GST, a car owned personally by the partners is not going to be subject to GST on its sale. This means of course no input credit can be claimed on its purchase price. But an input credit can still be claimed on expenses associated with the car by the partnership reimbursing the partner for those expenses and then being entitled to the GST input credits. This is available under the GST Act Section 111-5(1)(c). But the expense must be apportioned between business and private use.

In summary by far the most tax efficient way for a partnership to utilize a motor vehicle that is pre GST or purchased in a private sale, is to have it owned by the individual partners who are not registered for GST but reimburse these partners for the business portion of all the expenses.

GST Margin Scheme Update – Sale of Real Estate

Basics:

- The margin scheme can only be used with a house and land or land. If the seller is registered for GST the margin scheme can only be used where the property was owned pre 30th June 2000 or purchased under the margin scheme. Or if the seller, who is registered for GST purchased the property from someone who was not registered for GST
- The margin is the amount of the selling price on which GST is calculated.
- The purchaser of a property under the margin scheme cannot claim any GST input credits back on the purchase price. But if they are registered for GST they can claim GST input credits for further expenditure on the property.

Property Purchased After 30th June 2000:

- If you are selling a property you purchased after 30th June 2000 and the price you paid was calculated under the margin scheme section 75-5 allows you to only charge GST on the difference between the selling price and the cost to you of the asset that was measured under the margin scheme. Note any improvements to the asset after purchase do not reduce the margin. For example a GST registered developer buys land for \$66,000 from someone who is not registered for GST. The developer spends \$100,000 (after claiming back input credits) putting a building on the land and sells the property for \$200,000. If the GST on the sale is calculated under the margin scheme it will be 1/11th of \$134,000 (\$200,000 - \$66,000).
- Note there is one dubious exception to the above ID 2002/30 states that the price you paid for the property, as calculated under section 75-10 (i.e. the portion that is not subject to GST when you sell) includes any adjustments for land tax or council rates you may have paid at settlement. But ID 2002/31 states that this does not include legal fees.
- You cannot use the market value to set the cost under the margin scheme if you purchased the property after 30th June 2000. This is the case even if you did not register for GST until after the purchase.

Property Purchased Before 30th June, 2000:

- If you owned a property before 30th June, 2000 you need to set the amount that is not subject to the margin scheme. This is the value of it at 30th June, 2000 or when you first became registered for GST, whichever is the latter.

- GSTR 2000/21 details how to set the value as at 30th June, 2000 or when you first became registered but note this is only for property held before 30th June, 2000.
- If the property is fully complete the value can be set by a qualified valuer or the amount set by the government for land tax or council rates purposes.
- If the property is being developed at the time you require the valuation you can use a value set by a qualified valuer or use the cost of completion method.
- The cost of completion method determines what percentage of the total costs the costs that have been incorporated into the project at the date of valuation are. It is this percentage of the selling price that is not subject to GST. Note this method can only be used if the property is sold before 1st July, 2005 and owned by you before 1st July, 2000.

Comparing Apples with Apples:

If you are registered for GST and you purchase a property where GST is calculated under the margin scheme you cannot claim an input credit for any of the GST you are charged. So it is important when comparing properties to know whether the margin scheme applies or not. Yet the GST legislation does not compel the vendor to tell you whether they are using the margin scheme. In fact the ATO in ID 2001/393 states that the seller does not have to decide whether to use the margin scheme until the date of settlement. The margin scheme only makes a difference to your cash flow not your final profit. So if you intend turning the property over quickly it doesn't make much difference but if you intend to hold onto the property it is very relevant, for example:

Land purchased for \$66,000 under margin scheme by a developer who is registered for GST and puts a building on it. The house cost \$100,000 (after claiming back input credits on the materials) to build. The whole property is sold for \$200,000 GST inclusive but again under the margin scheme. The developer would have to pay GST of \$12,190 ($\$200,000 - \$66,000 = \$134,000 / 11$). Profit on the deal would be \$21,810 ($\$200,000 - \$66,000 - \$100,000 - \$12,190$). As the sale with the building is under the margin scheme the purchaser will not be entitled to input credits which would be bad if they would have been entitled to otherwise and they intend holding onto the property.

The same scenario as above except that the land was not under the margin scheme but the price was still \$66,000 including GST. The Developer would be able to claim an input credit of \$6,000 but would have to pay GST on 1/11th of the whole of the whole of the selling price of \$200,000 which would be \$18,182. The profit on the deal would now be \$21,818 ($\$200,000 - \$60,000 - \$100,000 - \$18,182$). The purchaser of the property may be able to claim an input credit but the whole scenario above would apply to them unless they intended to hold onto the property.

In short don't be prepared to pay more for a property just because you can get an input credit on it (because it is not subject to the margin scheme) unless you intend keeping the property for a long time.

GST When Purchasing a Business

The purchase of a business can be GST free if the following requirements are met.

- 1) The transfer of the business has some value
- 2) Both the buyer and seller are registered for GST
- 3) All things necessary to continue the operation of the business are transferred.
- 4) The seller carries on the business until the day of transfer.

GSTR 2002/5 goes into the detail of these requirements. In particular point 3 above is a problem (GSTR 2002/5 paras 58 to 70). For example to meet the requirements of transferring all that is necessary to run the business the lease on the business premises (if necessary for the continued operation of the business) must also be transferred. This requirement cannot be satisfied if the seller is behind in the rent and without a lease or does not pay rent (paying outgoings only does not meet the requirement of paying rent).

If the purchase of the business is subject to GST make sure the contract satisfies the tax invoice test on page 49 so you can claim the GST input credit back. Also make sure you are registered for GST on or before the date of the contract.

Whether the contract includes GST or is GST free is neither here nor there if you are registered for GST and if you receive a tax invoice, though it may cause an initial cash flow problem. If you end up paying GST you will be able to claim it back anyway. It is really for the seller to beware.

What to do When the ATO Walks in the Door

The ATO has begun what they call "Walk Ins". Their objective is to find businesses operating outside the PAYG or GST systems by going to an area or a particular industry and checking every business. The typical questions they will ask during these "Walk Ins" is:

- 1) Your ABN?
- 2) Are you registered and charging for GST?
- 3) How many employees do you have?
- 4) Are your Activity Statements (BAS & IAS) up to date?

They will not ask you to prove your answers but will take the information back to their office and check it against the information you have been supplying on your BAS. This will not just catch out those not registered for GST. Imagine if they walk into your premises while you have staff working yet you have not registered for PAYG withholding (deducting tax from employees wages). We have long been advising clients that paying cash wages is not worth the risk and only benefits employees not the employer. These "Walk Ins" are just another reason to be up front with the ATO from the minute you start to employ.

Don't feel pressured to respond to these "Walk Ins" they do not have the right to disrupt your business. If you are busy simply ask them to come back at a more convenient time. The information you provide is voluntary so don't feel obligated but obviously if you don't eventually provide the information they will use their stronger powers to gain all the information they require. You also have a right to have your accountant present when they ask the questions. Clients doing the right thing should not need an accountant to answer the basic questions listed above but if they go further than this and you are concerned, you can halt the whole process until you seek advice.

ATO staff performing the "Walk Ins" have been trained that they must not be intrusive. The ball is in the taxpayer's court, don't be intimidated but realise that you must answer their questions eventually. If you are unsure of the answer you are allowed a lifeline. Call your accountant or arrange for them to come back at a more convenient time.

Of course they will be targeting low compliance areas such as markets and the construction industry.

ATO Hit List of Most Common BAS Mistakes

According to the ATO the following is a list of areas where taxpayers are most likely to make mistakes in their BASs.

- 1) Not remitting to the ATO the GST on the sale of any assets by the business. For example if you update your computer or trade in a vehicle that has been used for the business you must charge GST on the sale and record it in your BAS.
- 2) Taxpayers who purchase an asset under a Hire Purchase agreement and report their GST on a cash basis are not entitled to claim the GST input credit on the purchase up front. They must only claim the GST portion of each payment made under the HP agreement when that actual payment is made.
- 3) As discussed regarding income tax returns in Newsflash 53 the ATO will be using industry averages to compare BASs for abnormalities. Some of these Benchmarks are available on the ATO web site at visit www.ato.gov.au/content/business/downloads
- 4) Not including Barter transactions on the BAS. They must be included even if the net effect is zero.
- 5) No wages declared at W1 – payments of employees or contractors cash in hand.
- 6) Cash transactions missing.
- 7) Inaccurate records.

The ATO will be making an effort to contact new businesses early in the piece to ensure they understand these and other issues.

Financing Equipment or Motor Vehicles

As we are still getting many phone calls on this subject it bares repeating. If you are registered for GST and reporting on a cash basis the advent of GST should make you rethink you financing strategy. If you finance a purchase under hire purchase or lease section 29-10(2) will only allow you to claim the GST input credit back on each repayment over the term of the finance agreement. Whereas a chattel mortgage, personal loan or

splitting your home loan and drawing on it will allow you to claim the GST input credit back at the time of purchase. Strangely enough financial institutions are usually prepared to lend you the full purchase price without allowing for the fact you will get an input credit in the next quarter. Accordingly, these arrangements can initially result in a cash flow injection.

Leases have also lost a lot of ground since deductions for prepayments have been limited for all but those in the simplified tax system. This is the end of reducing a tax bill by going out and leasing a car and making 12 months lease payments in advance, unless you are in the simplified tax system.

GST and Motor Vehicle Registration

From 1st July, 2003 businesses registered for GST can claim an input credit for motor vehicle registration. Just like general insurance there will be a stamp duty component of the price, which is added after the GST. Accordingly, the GST is not exactly 1/11th of the total registration fee. Further if the vehicle is not 100% business use you will have to apportion the GST you claim.

GST and Passing on Credit Card Fees

From the 1st July 2003 business owners will be permitted to charge a surcharge on credit card transactions to cover the extra costs of merchant fees. The surcharge for using a credit card is considered to be part of the price of the goods purchased so is treated for GST purposes the same as the goods purchased. For example if the credit card is used to buy goods that are exempt from GST such as medical services there is no GST payable by the provider on the merchant fee surcharge received. On the other hand if the purchase was for clothing, which is subject to GST then 1/11th of the merchant fee surcharge received must be remitted to the ATO as GST. If the purchase involves both GST inclusive and GST exempt goods the surcharge must be apportioned on the same ratio and 1/11th of the surcharge on the non-GST inclusive goods must be remitted to the ATO.

As you can see this rule is directed at making the seller of the goods and services liable for the GST on the merchant fee. If you are both a supplier of GST exempt goods or services and those subject to GST you really need to display a different percentage merchant fee surcharge depending on whether the item purchased is subject to GST. In reality the distinction will not be made and once again the provider of the goods or services will absorb the cost.

Nasty Sting for Legitimate Business Expenses

You may already be aware that if you are caught by the APSI rules you cannot claim a deduction for payments made to associates unless the work they perform directly relates to the principal work provided to customers or clients. An example of this is if I charged my brother for preparing the income tax return for his tutoring business he would not be able to claim the fee paid to me as a tax deduction, despite the size of my business. Naturally enough I don't charge him. Nevertheless, under GST legislation I am required to remit to the ATO the amount of GST that would have been applicable had I charged him! In an even further development of this double standard the ATO has taken the approach that the rules on payments to associates include payments for goods. Accordingly, if your spouse owns the business from which you purchase your business's stationery and your income is from personal services you cannot claim a deduction for that stationery. The following is an extract from the legislation validating the ATO's approach

SECTION 85-20 Deductions for payments to associates etc.

85-20(1) You cannot deduct under this Act:

(a) any payment you make to your *associate; or

(b) any amount you incur arising from an obligation you have to your associate; to the extent that the payment or amount relates to gaining or producing your *personal services income.

85-20(2) Subsection (1) does not stop you deducting a payment or amount to the extent that it relates to engaging your *associate to perform work that forms part of the principal work for which you gain or produce your *personal services income.

85-20(3) An amount or payment that you cannot deduct because of this section is neither assessable income nor *exempt income of your *associate.

Makes you wonder if any of our highly paid politicians read the legislation before they vote on it, doesn't it.

GST and Chocolate Body Paint

The ATO officer who wrote ID 2004/38 definitely has no life. A Taxpayer wrote to the ATO asking if the Chocolate Body Paint it manufactured was subject to GST. The Taxpayer's argument being that as it was food it should be exempt. The ATO responded by saying that in order to be exempt as food the substance must not only be food but must be used as food. The ATO further went on to cite the fact that a paint brush etc was supplied meant that it was not being sold as food.

My question is, why would a person cover themselves in sticky chocolate if it wasn't in the hope that someone would consume it?

What is the ATO Trying to Tell Us?

The Tax Office's annual report, released last week, clearly shows that the smaller the business on average the more it is struggling with the GST and alarmingly, the higher the relative penalties the ATO is imposing. The report states that audit activity of micro businesses has resulted in \$323 million extra GST collected plus \$15 million in penalties. Audits of small to medium businesses resulted in \$257 million in additional GST plus \$7 million in penalties. Audits of big businesses resulted in \$234 million in extra GST with virtually no penalties. It clearly shows that the smaller the business the less they are able to cope with the GST. This is probably as a result of economies of scale in accounting systems and support staff. The alarming fact is that the average penalty for every dollar a micro business failed to report was 4.6% yet for small to medium businesses it was only 2.7% and big businesses didn't even rate.

GST & Making Supplies Through an Agent

In a normal Principle and Agent arrangement it is the Principle who is responsible for remitting the GST charged on the sale to the ATO. This is the case whether the Tax Invoice is issued by the Agent or the Principle. But if the Agent invoices the customer, the agent must not charge GST unless the Principle is registered for GST.

ATO ruling GSTR 2000/37 states at Paragraph 55 - "the principle is liable for any GST payable on the supplies". This is under a normal Principle and Agent arrangement. This may put the principle in a vulnerable situation if the agent does not provide relevant information about the sale. Section 153-B does allow Principles and Agents to act as separate suppliers and acquirers. That is they can enter into an agreement where the Principle is taken to have made a supply to the agent and the agent is then taken to have made a supply to the third party. Section 153-55 (1) (c) requires both the Principle and the Agent to be registered for GST. GSTR 2000/37 at paragraph 76 reiterates this, specifying that the agreement must be in writing, specifying the suppliers and both parties must be registered for GST. These arrangements together with a the right for the Agent to create a recipient created invoice on behalf of the Principle will not reduce the Agents paperwork but will at least streamline it.

Sell to a Farmer as Opposed to a Developer

A husband and wife purchased a farm in 1988 which they have farmed, in partnership, continuously for the last 15 years. Their combined assets are under \$5 million. They want to know how much tax they will be up for and whether this changes if they sell to a farmer as opposed to a developer. It is expected that they will get a higher price from the developer but wonder whether this will be worth it after tax considerations. The following only addresses the ramifications for the land not the plant and equipment on it.

CGT Considerations

15 Year Exemption: The most attractive CGT concession here is the 15 year exemption. This concession is superior to all other concession if you can qualify as follows:

- 1) Active Asset Test S152 - Used in the business up to just before sale and for at least half of the time it was owned. If the business ceases before the sale the asset must have been used in the business up to the time it ceased (note the ATO is taking a very strict view here it means right up to the last day) and then must be sold within one year of the business ceasing. The property would not be an active asset if it was used to derive rental income.
- 2) The asset must have been owned for at least 15 years.
- 3) Both owners must retire

If they can pass this test the gain is totally CGT free and does not even count towards their RBLs.

Retirement Exemption Combined with 50% CGT Discount and 50% Active Asset Discount:

If they cannot meet the requirements of the 15 year exemption because they are not retiring the next best option is the retirement exemption after utilising the 50% CGT discount and 50% active asset discount. All three of these concessions can be used together but before they are used the capital gain must be offset against any capital losses. In the case of the 15 year exemption they would get to keep any accumulated capital losses to offset against other capital gains. The amount that the retirement exemption applies to counts towards their RBLs.

For example assume the gain on the property was \$100,000 the 50% CGT discount would reduce this to \$50,000 and the 50% active asset discount would further reduce this to \$25,000. Placing the remaining \$25,000 into superannuation would mean that the whole \$100,000 is received tax free. The \$25,000 is not taxed in the hands of the superannuation fund.

Note:

If they could not use the 15 year exemption because they failed the active asset test as per 1) then they will not qualify for the retirement exemption or the 50% active asset discount.

Despite its name the retirement exemption does not require them to retire. They can just put the money into superannuation instead.

Companies and Fixed Trusts are not entitled to the 50% CGT Discount and the use of the 50% Active Asset Discount creates problems when the asset is owned by a Company or Fixed Trust. In Discretionary Trusts the CGT flows through to the beneficiaries so is treated the same as an individual. Fixed Trusts are all trusts that are not discretionary. Fortunately our Readers owned the farm in partnership.

GST Considerations:

If they sell the land while they are registered for GST they will have to charge GST, unless they sell it as a going concern and the purchaser is registered for GST in which case it will be exempt. Whether the purchaser is a farmer or developer, if they are registered for GST it makes no difference as they can claim the GST straight back off the ATO anyway. So the GST will be just added on to the agreed price.

If the purchaser is not registered for GST they need to try to avoid charging GST on the property. If they can drop their annual turnover to under \$50,000 they could de register for GST before they sell it. They could also consider ceasing the business in order to deregister but they must be careful to sell within 12 months in order to keep the active asset concessions. Upon de registration section 138 would require them to pay back some of the GST claimed on equipment for which all the adjustment periods have not expired but this will happen sooner or later. If it is not possible to de register for GST they could utilise the margin scheme to minimise the GST to a purchaser. A purchaser of land purchased under the margin scheme is not entitled to claim back any of the GST included in the purchase price but is entitled to use the margin scheme themselves, if they are registered for GST when they on sell the land.

Conclusion: It makes no difference who they sell the property to as long as it is used in the business up until the time of selling or within 12 months of ceasing business. Careful planning can completely eliminate all CGT and GST. Now that's the way to BAN TACS legally.

Hot House

Things will get a lot hotter in the Hot House once the tax man moves in!

One couple will eventually win the house but it won't be like winning the lottery, they have worked for the prize. In accordance with IT 167 the value of the prize will be income to them. This value has been highly advertised at \$2 million. For GST purposes they would be considered to be an enterprise (MT200/1 & TR2000/14) as they are providing services, paid on the basis of a result and accept the risk. The ATO will score \$181,818 in GST. This leaves \$1,818,182 combined in taxable income for the 2004 tax year. Assuming they already both have jobs with reasonable pay packets the extra \$1,818,182 is going to attract the maximum tax rate of 48.5%. That is \$881,818 in income tax. They will need to find a bank that will lend them \$1,063,636 to pay the tax if they want to keep the house. Basically the tax man will pick up more than half their prize. Worse still the advertising might say the house is worth \$2,000,000 but a lot of that is hype. By the time they realise the trouble they are in and have to sell it to pay the tax bill they may not be able to find a buyer for \$2,000,000 especially when the whole country knows what went on in the construction. So what happens if a year later when they sell it to pay the taxes and they can only realise \$1.6 million? The ATO would have a good

argument to still tax them on the \$2 million, the change in the value since then could be put down to the fickleness of the property market over the year. They now have an asset worth \$1.6million that they, notionally, purchased the year before for \$2 million (IT 2584). If they have lived in it since it was built the capital loss on the sale is private so no tax concessions at all. If they did not live there they can recognise a capital loss but this can only be offset against future capital gains not other income. Let's hope they already have private health insurance because if they don't the income from the house will push them into the Medicare Levy Surcharge which will be \$18,182 on the house income alone plus another 1% on their wages income. To eliminate the surcharge they must have had the insurance from 1st July, 2003 and you can't back date the insurance for the love of money. Still not bad for a few months work \$1.6 million dollars less GST of \$181,818, income tax of \$881,818 and \$18,182 in surcharge leaves them with \$518,182. But the taxman scored \$1,081,818 which is more than twice as much as them.

There is also the fact they have been provided with food and accommodation, and because they are not travelling but have set up a new home (MT2030), this will be a non cash business benefit on which they will also be subject to tax. I cannot quantify how much this would be but they will have to find the cash to pay this as well.

So in a year's time when they realise the mess they are in with the ATO they will need to sell the house for more than \$1,081,818 before they make a cent out of their efforts.

Now that's the real reality!

The Taxman may do even better if they aren't aware of all the traps. What if after living in it they decided to rent it out. Section 118-192 deems the cost base of the house to be the market value at that time. Making the same assumptions as above that is \$1.6 million. After a few years the property's value reaches maybe \$1.9 million and they sell. The taxman would then assess them on a \$300,000 capital gain (ignore commissions etc). They would receive the 50% discount so would only be taxable on \$150,000. Assuming they still had decent jobs this gain would be taxed at 48.5%. The tax man just made another \$72,750, even if they have learned their lesson this time by having private health insurance. So of the \$1.9 million they end up receiving the taxman takes more than half (\$970,000 income tax, \$20,000 surcharge plus \$72,750 CGT) \$1,062,750 and they are left with \$837,250.

GST and the Ambulance Subscription in Electricity Bill

You pay on your businesses electricity bill. As a result Beattie has delivered businesses another ridiculous record keeping burden for the sake of a few dollars. When entering your businesses electricity bill, if you are registered for GST, you will need to enter the Ambulance levy separately. One entry will be for the electricity and coded for GST as GST will be 1/11th of that amount. The levy is then entered separately with no GST code and no input credit claimed. The levy is still tax deductible if the electricity is used for business purposes. If the electricity is only partially used for business purposes it will need to be apportioned.

Suncorp re Nig

Many clients put their GST and tax savings into there mortgage until the BAS is due, when they simply use the redraw facility to draw the money back out. This is fine while the bank honour this agreement. Imagine the dilemma if they won't give you the money back even though you are up to date on your repayments.

We have heard of a case where a married couple jointly owned the home and were jointly liable for the mortgage. One member of the couple died suddenly. The bank was informed as a matter of course. They should not have been concerned because the surviving spouse was the main income earner, could easily afford the repayments on the housing loan and had 47% equity in the house. But no, Suncorp would not allow the GST to be withdrawn to pay the BAS when it was due. Suncorp claimed that as the loan and house were in both names one party can't withdraw. Suncorp demanded that before the surviving spouse can access the extra repayments the house must first be transferred into their name, they must write a letter to Suncorp explaining their circumstances and prove their ability to be able to meet the repayments all over again. Needless to say if the person is going to go through all of this they may as well change banks! The requirements to walk in off the street and apply for a low doc loan are less onerous than that required by Suncorp just to make a redraw.

I am sure the ATO would have been sympathetic to the situation and held off pursuing the debt but it won't stop them charging interest on the outstanding tax. What would the situation have been if the surviving spouse was not the main income earner? It is very concerning that having paid extra off your mortgage as a safety net

may not help you in the event of a spouse's death. We don't believe this should be the case but it may be worth checking with your bank, in writing.

GST and Selling a Business

If a business is sold as a going concern it is exempt from GST providing both the buyer and seller are registered. There are many other conditions including a requirement that all things necessary to carry on the business are included in the contract. Wide statements such as this give the ATO a field day to nit pick. It is the seller who will ultimately have to pay the GST if the ATO decides it is applicable. A clause in the contract saying the purchaser will reimburse the seller if GST applies will not help you if the purchaser does not have the money or has disappeared. The ATO is only interested in getting the seller to pay. We believe it is not worth the risk.

If you charge GST on the sale you just increase the price by the amount of the GST and the purchaser claims it back as an input credit. If cashflow is an issue with the purchaser and they can't afford to wait to lodge their BAS consider offering vendor finance. It is only for a few months at the most.

GST When a Car is Sold

When a car, used in a GST registered business is sold GST must be paid to the ATO. This is the case even if the car has been used in the business for only a few kilometres. The ATO is concentrating on this issue because they realise that many people do not think to remit the GST or do not know how to calculate it.

There are various rules depending on when the car was purchased and what it was used for. So watch out for this one when you are doing your BAS. The relevant section is 132 which apportiones the GST as follows:

Car Purchased Before GST

You must remit 1/11th of the price you receive for the car to the ATO even if it has only done a few kilometres for the business and even though you did not qualify for an input credit when you purchased it.

Cars Purchased After GST and:

Exceeded the Luxury Car Limit – This is the price you originally paid for the car. The limit in 2002 was \$55,134 for 2003 and 2004 the limit is \$57,009 GST inclusive. Even though you were not entitled to the GST credit on the amount above the luxury car limit you must remit a full 1/11th of the selling price to the ATO unless there was some private use of the car and it was purchased after GST was introduced. If this is the case and the car was used 10% for private purposes then 90% of 1/11th of the selling price must be remitted to the ATO as GST.

Used Partially for Private – Take 1/11th of the selling price, multiply this by 100% less the private use percentage. Note private use does not include other income producing purposes such as travel for a rental property.

Partially in Relation to a Rental Property - Use of the vehicle in relation to a rental property is not included in private use and section 132 only allows the GST on sale to be reduced by the private and financial institution use. Accordingly, the GST is calculated as per private use above. That is the 1/11th in GST is only reduced by the private use not the rental property use.

Sold with the Business – Providing the business meets the requirements of a going concern then no GST is payable on the sale anyway. But you are still entitled to a reduction in your GST for the private portion of the notional GST. Lets say the vehicle has been used 20% for private 70% for business and 10% regarding a rental property. If it is sold with the business you are entitled to an input credit (reduction in GST) of 20% of 1/11th of the selling price of the vehicle even though you didn't charge GST.

Did not pay GST when Purchased the Car – An example would be a private sale. If this is the case 1/11th of your selling price must be remitted in GST regardless of private use.

Note if the car is owned by a company or trust then technically there is no private use as the private use is a fringe benefit provided to an employee. The above assumes you are not a financial institution.

Buying a Vehicle

If you are in business and registered for GST you may need to refresh you attitude to buying a car. Many people dislike buying brand new cars feeling they lose value the minute you drive them away from the

dealership. Some also prefer not to buy a car from a dealer at all because it is generally more expensive than buying privately. Quite a bit has changed over the past few years so do your sums first don't just assume a second hand car purchased privately is the best deal. Take a look at the price of new cars. They have now fallen considerably because of the improved buying power of the Australian dollar. People selling a car they purchased new a few years ago expect to recover about 80% of their original purchase price only to find out in some cases that a brand new version of the same car is now 80% of the price they paid. Also if you buy privately it is very likely that the seller is not registered for GST. If you are going to use the vehicle for business and you are registered for GST the ATO will give you back up to 1/11th of the purchase price if you buy from a dealer. Note: if you lease the vehicle you can only claim the GST as you make the lease payments. Don't forget the benefit of the warranty you will get from a dealer.

Recently I nagged a client into seeing a dealer before he paid for a car he had arranged to buy privately. He was always against buying brand new but when he did the numbers on the GST and found the new car price to be so much lower than a few years ago he was even prepared to lose his deposit on the private sale and buy new.

You should refer to Newsflash 96 for more details on how GST effects buying and selling a vehicle. You will only be able to claim a percentage of the GST back on the vehicle if it has some private use unless you operate through a company or a trust. To make the apportionment of GST easier for small business the government has just introduced that you can claim all the GST back at the time you purchase the vehicle and let your accountant work out the actual business portion and adjust your BAS when preparing your tax return later in the year. This concession applies if your business has an annual turnover of less than \$2,000,000 and you purchased the vehicle after 1st October, 2004 for quarterly BASs or after 1st November, 2004 for monthly BASs.

Be careful not to exceed the Luxury Car Limit. If you pay more than \$57,009 GST inclusive for the car in 2004 you are not entitled to claim an input credit or depreciation on any amount over \$57,009. This only applies to cars not trucks and buses.

GST Small Business Concessions Through Parliament

These concession allow small businesses (turnover less \$50,000 or \$100,000 for non profit organisation) and non-profit organisations to opt to report and pay their GST annually. This means instead of struggling with the BAS each quarter themselves they can get their Accountant to do the whole lot when their tax return is being prepared. Great economies of effort. While the bill has only just passed through Parliament (due to the Federal Election) it actually applies to the BAS for the quarter ending December, 2004. Refer section 151. Note this concession does not apply to taxis as it is only available to entities that are not required to be registered for GST because their turnover is under \$50,000 and taxi drivers are required to be registered even if their turnover is less than \$50,000. Yes this is a Clayton concession and can be summed up simply: Hail the Government they have made the GST burden simpler for small business - if you are not required to be registered for GST but do register you will only be require to report annually.

The ATO sent out election forms before the legislation was through Parliament. If you accepted these before 28th February, 2005 Quarterly lodgers or 1st October 2004 monthly lodgers (hey hello to that one person if any that is not required to be registered for GST but is and lodges every month, good to know you exist, there was a reason for all that extra legislation). If you did not accept these offers you will not be able to enter the annual system until 1st July, 2005.

Businesses with a turnover of less than \$2m can also report their GST annually but they will still need to pay their estimated GST quarterly.

Whose Name do you Buy the Car In?

A client recently got caught between a rock and a hard place. Over Christmas she purchased a car. You know the story during that time we close up shop and hide and leave you to your own devices. She purchased it in her name yet her business was operating in a trust. When we did the numbers it made no difference in the future as the best way to claim the vehicle was under a log book anyway. The problem was she wasn't registered for GST and the trust was so she was not entitled to claim the GST back on the purchase of the car. This was quite a few thousand dollars. Even if she now transferred the car over to the trust's name now it

would effectively be a transfer between her and the trust at a huge stamp duty cost. But as she was not registered for GST she could not pass on the GST input credits anyway.

Fortunately GSTR 2000/17 paragraph 73 and 74 state that the tax invoice can be in the name of an employee or officer and still the business can claim the GST back by reimbursing them.

No GST on Prepaid Phone Card

Don't ask why just comply. For no reasoning that I can gain in the legislation, phone cards are not subject to GST. So be very careful with the tax code you use if you have a pre paid mobile. On the bright side at least you don't have the grief of trying to get a tax invoice for the transaction.

Margin Scheme Amendment

On 17th March, 2005 a bill was introduced to Parliament that will require the parties to a contract for the sale of real property to both sign a written agreement on or before settlement, stating that the margin scheme is to apply to the contract. The bill also tidies up areas in the calculation of the margin to ensure that the cost of improvements made after the seller purchased the property are included in the margin.

GST and Subdivisions

An enterprise with a turnover of more than \$50,000 of supplies that are subject to GST must register for GST and as a result remit 1/11th of all its income and capital proceeds to the ATO. Capital proceeds are the amount received for the sale of assets used in the business, income is from rent and regular trading. Capital proceeds are not included in the \$50,000 turnover test.

Section 9-20 defines enterprise to include a business or an adventure or concern in the nature of trade. At paragraph 187 MT 2004/D3 states that the realisation of an investment does not amount to trade. MT 2004/D3 states at paragraph 170 that an adventure or concern may be a one-off transaction that does not amount to a business. So once again we are left with the notion that the mere realisation of an asset is not subject to GST but once it becomes business like it will be. The trouble is the wording of the GST legislation is not the same as that for income tax. MT 2004/D3 at paragraph 153 recognises that the GST definition of enterprise is much wider than the income tax definition of being in business. You could well not be in business for income tax law but still have to register for GST. GST should also be taken very seriously when doing your costing as GST is not a tax on the profit but 1/11th of the selling price which may well be all your profit though you will be allowed input credits.

GST and Sale of Properties Held for Rental

Even holding domestic rental properties is considered an enterprise and qualifies for an ABN but normally landlords don't bother as they are not required to charge GST on rent on residential properties. So even if their turnover is more than \$50,000 it is not for supplies to which GST applies to so they are not required to be registered. The eventual sale of the rental property will turnover more than \$50,000 but this is not included in the \$50,000 test unless they are in the business of selling rental properties. So if you are just a normal investor in domestic rental properties your turnover of GST supplies in the course of your business is never likely to exceed \$50,000. At paragraph 186 of MT 2004/D3 states that the realisation of an investment does not amount to an enterprise in its own right. Even though the sale of the property is for more than \$50,000 it is not part of your turnover so will not force you to be registered for GST. If you are not registered for GST, you will not have to remit GST on the sale of a rental property. If you are registered for GST the sale of a domestic rental property will still not be subject to GST providing it is not considered the sale of a new home. Refer above.

Landlords are required to charge GST on rent for commercial premises if they are registered for GST. They are required to be registered for GST if their rents for the year exceed \$50,000. Now the \$50,000 is in turnover so it doesn't include the sale of capital assets but if you are registered for GST when you sell it you may be required to remit 1/11th of the selling price in GST. If you have built or substantially renovated the rental property within 5 years before you sell, you need to read the above article about new houses.

MT2004/D3 at paragraph 214 points out that an asset purchased as an investment and therefore not subject to GST when it is sold can become subject to GST by being applied to an enterprise in the way it is sold ie subdividing or building on it. If this is the case you need to read the section above of Does GST Apply to the Sale?

GST and New or Substantially Renovated Houses

The first sale of a new house is always subject to GST if the seller is registered for GST. If the house was built with the intention of resale at a profit then the seller must be registered for GST as the sale is part of the business turnover and that would be more than \$50,000. If the house was built to live in or rent out the seller would not be required to be registered for GST so when it is sold GST does not apply simply because the seller is not registered.

No GST on sale means no input credit for building costs. Even if the house hasn't been finished for 12 months at the time of sale you will still qualify for the 50% CGT discount on the profit on sale if you have held the land for more than 12 months. All this is only if you built the house for the purpose of rental not resale at a profit. Reference: Section 40-65 states even if new residential premises are rented for a period prior to first sale the first sale will be a taxable supply. Section 40-75 states that premises are not new if they have been used as residential premises for at least 5 years.

Note if you are builder you will have two things working against you. Firstly, it will be hard to argue that you did not build it for resale refer Case R51 84 ATC 392 where a builder was found to have built a block of flats with the intention to profit on their resale. Even though the flats were not sold until 6 years after they were built. Secondly you own the property in your own name and are in business as a sole trader you are probably already registered for GST, the only way the sale could be excluded from the GST provisions is to argue that it was not purchased in the furtherance of your business. This would be impossible if you have been claiming input credits on the building costs.

Now if you did not build the house for resale at a profit and are not registered or required to be registered for GST you can sell the house without any GST concerns. If you build the house for resale at a profit you are required to be registered for GST. If you did not build for resale at a profit but you are registered for GST and the sale of the property is part of your enterprise even if it is not part of your enterprise's normal turnover, you will have to rent the property out for 5 continuous years or pay GST on 1/11th of the sale price (less if margin scheme applies). Continuity is not broken by short periods between tenants GSTR 2003/3.

Note: if you substantially renovate a property it may be treated as a new property.

If you are caught for GST and have used the property partly for rental and partly for resale at a profit you will be entitled to claim back most of the input credits on the cost of the property but you are subject to GST on the proceeds of the sale. The margin scheme can help here refer below. In the Property and Construction Industry Partnership Issues Register item number 4 the ATO has agreed to pro rata the input credits on the basis of income received. The formula for apportioning input credits between the taxable supply of the home and the input taxed supply of rental accommodation is as follows:

Consideration for the taxable supply of the premises

Consideration for the taxable supply of the premises plus rental income

When Do You Have to Charge GST on Selling a Property?

The main determinate of whether GST is applicable to the sale of the land is whether you are carrying on an enterprise. Section 38 (1) states that an enterprise is an activity or a series of activities done (a) in the form of a business or (b) in the form of a an adventure or concern in the nature of trade. There are further subsections but these are the ones relevant to this booklet. Note by the use of the words "an activity or series of activities" it is clear that one transaction can be an enterprise.

Much of the discussion above is how not to be considered in business so (a) does not concern us but (b) is clearly intended to make GST applicable to transactions that would not normally be caught as a business. MT2004/D3 states at paragraph 169 that "38 (1) (b) covers commercial activities of a trading nature that may or may not amount to activities in the form of a business". At paragraph 170 and 171 MT2004/D3 states "an adventure or concern in the nature of trade may be an occasional or one-off transaction that does not amount to a business but which has the characteristics of a business deal..... trade commonly means operations of a commercial character where goods or services are provided to customers for reward." Paragraph 172 states "The sale of the family home, car and other private assets are not, in the absence of other factors, adventures or concerns in the nature of trade. The fact that the asset is sold at a profit does not, of itself, result in the activity

being commercial in nature.” Paragraph 174 states “ If the property provides either an income or personal enjoyment to the owner it is more likely to be an investment than a trading asset.”

Paragraph 176 says that if an asset is only held for a short time it is likely to be held for trade. Paragraph 178 states that the frequency of similar transactions the greater the likelihood of trade.

Paragraph 187 in addressing the issue that investment assets are not in the nature of trade states. “Examples of investment assets are rental properties, business plant and machinery, the family home, family cars and other private assets.” But note paragraph 188 states that assets can change their character.

Paragraph 206 states “Where land is sold that was purchased with a view to resale at a profit we consider this to be an adventure or concern in the nature of trade. This would be so whether the land was sold as it was when it was purchased or whether it was subdivided before sale. This is because activities of this nature meet the criteria to be an adventure or concern in the nature of trade. The ruling then goes on to give a couple of examples that are based on the intention of the purchaser. In one example the purchaser buys land with the intention of building a duplex and living on one side and selling the other. In this case the sale would be subject to GST.

Paragraph 214 states that land even if not initially purchased for resale at a profit will be subject to GST if the process involved activities such as detailed planning, earthworks, drainage, the provision of access as well as marketing and selling activities. I now reproduce paragraph 215 in its entirety as it is extremely relevant to intending non developers:

“If there is a subdivision of land which is not substantial (as a rule of thumb say less than 10 blocks) and has only required minimal activities to meet council requirements and to sell the subdivided land, we will accept that these activities may not be in the form of an adventure or concern in the nature of trade. Such minimal activities could include:

- Surveying the land;
- Lodging plans with the local council;
- Obtaining the council’s consent for the subdivision;
- The provision of access, drainage, water meters, electricity and telephone to the subdivided blocks of land; and
- Arranging for a real estate agent to market and sell the subdivided land;”

Paragraph 216 points out the rule of thumb cannot apply if you build on the land or you purchased the land originally with the intention of resale at a profit. It also states that major roads or bridgeworks would put the project outside the rule of thumb. Paragraph 217 lumps all previous subdivisions, by the entity, together in the 10 block test.

If for GST purposes your activities do amount to an enterprise it does not necessarily mean you are in business for income tax purposes. The primary determinants are your intention in purchasing the land and the nature of your activities. Refer *Are You Merely Realising An Asset* above. So you could have to register for GST but may still be entitled to the CGT discount. But if under the GST legislation you are considered in the enterprise of selling land and or buildings the sale of any of the blocks is a normal transaction in the furtherance of your enterprise and as the turnover will no doubt exceed \$50,000 so you are required to be registered for GST. If you are registered for GST you must remit 1/11th of the selling price to ATO, though you will be entitled to input credits for GST on the development costs and possibly on the purchase of the land.

Simplified GST for Food Retailers

From 1st October, 2005 supermarkets and convenience stores with a turn over of less than \$2 million and a cash register that separates GST inclusive sales from GST exclusive sales will be allowed to estimate the GST free inputs. The method is only available to Food Retailers who convert 5% or less of their GST free inputs into taxable supplies. An example of this would be using fresh food to produce takeaway food. The conditions mean that very few Food Retailers will qualify. If they do they can apply the percentage of total sales that are GST free sales to their purchases to estimate their GST free purchases. Reference SAM 2005/1.

GST Record Keeping

We thought readers struggling with GST might appreciate the following quote from the Tax IQ Monthly:

“In a Government v. Government farce the Tax Office has announced that it has discovered widespread compliance problems among Government agencies resulting in a series of multi-million dollar penalty adjustments. Apparently Government bodies are unable to cope with their responsibilities under the GST legislation. Government bodies are required to comply with GST requirements in the same way as business and are simply unable to cope. They say that the problems result from a lack of both resources and experienced staff. We wonder if that excuse would work for business?”

Overseas Clients

If you are a non resident and have a rental property in Australia that we prepare the income tax return or provided other accounting services in relation to, you will notice that this year your invoice will include GST. Previously we did not have to charge you GST because our services were exported. On 1st April 2005 the GST legislation was amended to catch these services in the GST net.

Interesting ATO Rulings for Partnerships

GSTA TPP 086 & 87 - A partnership can claim the input credit for a tax invoice in the name of an individual partner or even an employee.

GSTA TPP 089 – If you receive a tax invoice after you have cancelled your registration you are not entitled to an input credit and you cannot claim that input credit before you cancel your registration because you do not have a tax invoice.

Reader's Question – Managed Apartments

A reader was concerned about an announcement in The Australian saying that the government had changed the laws to allow the ATO to retrospectively claw back GST credits legitimately claimed by investors who owned managed apartments.

Before I explain I would like to point out that I am never likely to lift a finger (except maybe the middle one) to help the ATO at the best of times but the Article in The Australian has twisted things a bit. Really the ATO should never have argued the case the way they did in Marana Holdings as it was against their stated opinion in their own ruling.

Instead of implying the ATO was attacking investors the real point of the article should have been that the ATO has no idea how to interpret the tax law. So the idea of taxpayers being responsible, under self assessment, to interpret the law themselves before lodging their tax returns, is the biggest social injustice facing Australia.

Taxpayers who have always organised their affairs according to the ATO's stated opinion in GSTR 2000/20 will not have to pay anything back so I doubt the \$100m claim in the article. When the ATO won its case based on an argument contra to its own ruling, taxpayers started to apply for a GST credit on the purchase of their managed apartments etc. The ATO panicked and decided it liked its first opinion better so now needs to go back and change the legislation to override this case. The ATO will be damned if they do and damned if they don't but hopefully public pressure will mean they give taxpayers the benefit either way.

Having finished my little soap box I will now attempt to explain the concepts in layman's terms but to do this succinctly I will ignore a few of the twists and turns along the way.

This is a classic case of the ATO issuing a ruling saying one thing and then when it goes to court arguing the contra because it suits them at the time. GST law says that residential premises supplied for sale or rent are input taxed (ie GST does not apply to expenses or income) unless it is the first sale of new residential premises. Now to the big question is the definition of residential premises. The GST Act says at section 195-1 defines residential premises as a building occupied as a residence or intended and capable of so being. Section 40 - 65 states that premises used predominately for residential accommodation are input taxed but the input tax concession does not apply to commercial residential premises. This leaves a bit of doubt in regard to motels with self contained units or serviced apartments.

Back when GST started the ATO issued GSTR 2000/20 which stated: "to be used for residential accommodation ... premises do not have to be a home or a permanent place of abode. To be residential premises as defined, a place need only provide sleeping accommodation and the basic facilities for daily living even if for a short term. On this basis when investors bought serviced apartments etc they did not claim the GST back nor charge GST when they sold the property.

The trouble arose when the ATO wanted to collect GST on the sale of a motel that had been converted to apartments. The ATO argued it was the first sale as a residential property. The taxpayer argued no when they purchased it as a motel that was a purchase of residential property so it wasn't the first. The ATO then went to court to effectively argue against the statements contained in GSTR 2000/20.

The court found in Marana Holdings that the accommodation had to be long term to be classed as residential, so serviced apartments and motels would not qualify.

After winning the case the ATO advised the GST subcommittee meeting on 8th March, 2005 that it would review its statements in GSTR 2000/20 but in the meantime they could be relied on. Any subsequent changes would be addressed as an implementation issue. Then on the 27th February, 2006 Peter Dutton announced that the law would be changed to meet the statements in GSTR 2000/20 and that the changes would apply retrospectively from the start of GST.

How does this effect you? If you have a piece of residential accommodation that provides sleeping accommodation and the basic facilities for daily living, whether you rent it long term or short term it is input taxed therefore you cannot claim the GST back on the purchase price nor expenses associated with it and you do not have to include GST in the rent. You do not have to charge GST when you sell it unless you were the one who built it or converted it to residential premises. If you have done anything contrary to the above, when the legislation changes you, in theory will have to amend your BAS return but lets hope some concessions apply. Personally I think it will apply to very few taxpayers as they would have acted on in accordance with the statements in GSTR 2000/20. Those that were quick off the mark to claim the GST back after Marana Holdings are the only ones who will have to worry whether they need to repay it.

Taxi Drivers

Most taxi drivers receive 50% of the fares they take as payment for doing their shift. They are considered to be in business and must register for GST regardless of their turnover. But they do not need to register for GST if they are simply paid wages on an hourly rate.

What we have noticed is that some drivers only include 50% of the fares they receive in their BAS at G1. In fact they should include 100% of the fares as they are the ones dealing with the public and taking the money, reference NAT 11368. The arrangement with the owner of the taxi is one of bailment ie the driver is hiring the taxi from the owner. This means that the owner must give the driver a tax invoice for 50% of the fares which the driver then includes in G11 on his or her BAS. The net result is GST is still only paid on 50% of the fares but it must be by claiming back an input credit for the amount paid to the owner. This means at the time of preparing the Taxi Driver's BAS he or she must have a tax invoice from the owner. If the driver does not he or she will end up paying GST on 100% of the fare.

Another warning to drivers in a bailment situation, you are the one required to give a tax invoice to the passenger with your ABN on it, if the fare is for more than \$82.50. If you do not do this and the passenger is in business they are required to withhold 46.5% of the fare and remit it to the ATO.

GST on Leasehold Improvements

To be entitled to claim a GST input credit on expenditure it must be used for a creditable purpose, this includes making improvements to something you do not own, as long as you use it in your business. An example of this would be the family farm being owned by Mum and Dad but the business of farming being carried out by a family trust that is registered for GST. The trust constructs a hay shed on the property. Once the hay shed is attached to the land it becomes the property of the owner of the land ie Mum and Dad. This does not stop the trust claiming the input credit for the hay shed as it is the trust that will be using the hay shed in its business.

Maybe GST Doesn't Apply to Forfeited Deposits After All

We will no doubt hear much more about this, I doubt the ATO will accept the Federal Court's ruling. A full bench of the Federal court in *Reliance Carpet Company Pty. Ltd v FCT* found that when the person who was going to purchase land off Reliance Carpet Company rescinded on the contract Reliance carpet did not have to remit GST to the ATO, on the deposit it was entitled to keep due to the default of the purchaser.

The Court said that when Reliance Carpet entered into the contract for sale with the purchaser it entered into a contract for the supply of real property. The fact that the supply did not take place did not warrant dissection of the contract to find some other supply. Accordingly Reliance carpet did not have to pay GST on the forfeited deposit because they did not receive the payment for a supply they made.

Do not act on this without further advice.

GST on Deposits

Taxpayers reporting on a cash basis in their BAS only have to remit 1/11th of the actual deposit received. Many taxpayers have been concerned that when they change to an accruals basis they will have to remit 1/11th of the whole contract price upon receiving a deposit. This is true but the ATO has stated that if the deposit is simply a security deposit no GST is payable on it at that time. GST will only be payable when the deposit is forfeited or applied as part of the payment for the goods. This sounds good in theory but check that your accounting system can cope with this.

Latest on Forfeited Deposits – Act Now

In the last edition of Newsflash we discussed *Reliance Carpet Company Pty. Ltd v FCT* where the full bench of the Federal Court found that GST did not apply to forfeited deposits because there was no supply made by the seller who got to keep the deposit.

On the 3rd August the ATO announced that it would appeal this case in the High Court. In the meantime the ATO advises taxpayers wishing to claim back GST they have paid on deposits in the past, that they should apply in writing immediately. The ATO will not pay the GST back until the issue has been resolved by the High Court but any delay in applying could mean that the time limit, within which refunds can be claimed, may expire.

When is it a Hobby for GST Purposes

If you are operating a business you must collect an ABN from every supplier you deal with, if they do not provide you with an ABN you must withhold 46.5% of the invoice amount and remit it to the ATO. The only exception is if the supplier provides you with a declaration that he or she and the activity they are invoicing you for is part of their private recreational pursuit or hobby.

It would be hard to argue that a cleaner is operating as a hobby but not a problem at all if you buy a work of art for reception. MT 2006/1 at paragraphs 365 to 375 outlines when the ATO considers an activity to be a hobby rather than a business. For example a spare time activity or pastime pursued for pleasure or recreation (relaxation, refreshment or enjoyment).

According to the ruling the following are indicators of a hobby rather than a business though any one point is not decisive:

- 1) No intention or future plan to make a profit
- 2) No repetition or regularity of sales
- 3) The activity is not business like in nature.
- 4) Lack of systematic approach
- 5) Small scale operation without the intention of creating a business.
- 6) Not dealing with the public

Considering how much of a buzz Julia gets out of delving into tax law maybe she shouldn't be charging GST and maybe even not paying income tax. After all, what could be more recreational to her than finding a little gap in the rules?

What was once a hobby can become a business without jeopardising the hobby status in the years before the decision was made to go full time.

For GST purposes the person involved in the activity is not required to register until his or her turnover from non hobby activities exceeds \$75,000 but they are required to hold an ABN should the activity be considered a business rather than a hobby.

GST on Selling a Business

While we have covered this topic in detail before, this article is directed at the very small business owner who may not think it worthwhile to get professional advice for a small transaction. Firstly you are wrong as one new client just found out, one little slip up and the ATO get a windfall payment of GST that the legislators never intended them to have.

When GST was introduced it included a concession to help small business. You see if a small business changes hands and both the buyer and seller are registered the GST is just an unnecessary and temporary finance cost. They realised that it was silly to make the purchaser borrow more money just to pay the seller GST when as soon as the buyer put in their BAS they would get it back. In reality small businesses do not have the cash flow to finance the ATO's administration burden.

So the GST legislation included an exemption from GST for businesses sold as a going concern. There were a couple of simple conditions to prevent this being used to sell something other than a business or to prevent the buyer accidentally claiming the GST back. The legislation says at section 38-325:

- (1) The supply of a going concern is GST-free if:
 - (a) the supply is for consideration, and
 - (b) the recipient is registered or required to be registered, and
 - (c) the supplier and the recipient have agreed in writing that the supply is of a going concern.
- (2) A supply of a going concern is a supply under an arrangement under which:
 - (a) the supplier supplies to the recipient all of the things that are necessary for the continued operation of an enterprise; and
 - (b) the supplier carries on, or will carry on, the enterprise until the day of the supply (whether or not as part of a larger enterprise carried on by the supplier).

Pretty straight forward you would think. The trap the do it yourselfers fall into is not having the agreement in writing or not supplying a "going concern".

It is the going concern definition that the ATO is having a field day with. They have a 29 page ruling , GSTR 2002/5 on the issue. This discusses the need to provide a lease on the current business premises, information necessary to continue the business, transfer licences, intellectual property, goodwill, franchise agreement and future bookings or contracts. You also have to be careful of the definition of the actual business you are selling. If it is part of another business you may not qualify as selling all things necessary if you only sell part of the business. Warning, if your staff abandon you just before the sale the ATO may argue that you did not continue to operate the business up until the day of transfer. Further, as you are required to transfer the information necessary to continue the business losing staff may make this impossible.

If you think by reading the ruling you can proceed with confidence you are a better person than me. When I sold a business I didn't even bother trying to meet the ATO's (at the time constantly changing) requirements of a going concern. I simply charged GST and gave the purchaser enough time to pay that it allowed them to lodge their BAS and get it back from the ATO. Solicitors will tell you they just put a clause in the contract that will allow you to recover the GST from the purchaser should the ATO decide GST is payable. The very fact they offer this shows you how little confidence the legal profession has in their ability to decipher what the ATO considers a going concern. I prefer to take the risk over the short term ie until the purchaser lodges their BAS then over the long term living in dread of the ATO questioning the contract.

So if you must (and we are certainly not recommending this) do the contract for the sale yourself. Better to charge GST and give the purchaser a tax invoice so they can claim the GST back. Because the ATO has no qualms about coming along, finding fault and collecting the GST off you even though they know the purchaser has not claimed it. The ATO has turned an attempt by the legislators to make things easier for business into a chance for them to collect tax where it was never intended by making things confusing.

This should not surprise us as they have been doing this sort of thing for over a decade now with the CGT main residence exemption.

ATO Warning About Registering for GST When Buying a Property

The ATO is concerned about developers selling domestic properties cheap to purchasers as long as they register for GST. This can result in the ATO collecting another 10% of the selling price off the purchaser.

Don't be fooled the developer can sell the property to you cheaply because they will not be liable for GST which may be as much as 10% of the purchase price.

The developer sets the property up as a going concern so it can be sold exempt from GST the trouble is once you use the property as a domestic rental you (not the developer) must pay the ATO 10% (not margin scheme) of the purchase price in GST.

According to ATO's Interpretive Decision 2002/710 because the property is being used for a purpose that is only input taxed the owner must, under section 135-5 repay any GST that has been claimed back in the past on the asset. Even though the sale was exempt from GST you are considered to have received the benefit of that GST so you will have to pay it back.

Deregistering for GST

When you de registered for GST you will need to pay back any input credits you had claimed on items for which the adjustment period has not expired? The adjustment periods differ depending on the cost of the item, as follows:

\$1,001 to \$5,000 GST exclusive – *Go forward to the first 30th June after the item was purchased then add another 3 years. If this date has passed then no adjustment is necessary.*

\$5,001 to \$500,000 GST exclusive - *Go forward to the first 30th June after the item was purchased then add another 6 years. If this date has passed then no adjustment is necessary.*

The amount you pay back is $1/11^{\text{th}}$ of the current market value (GST inclusive) or the price you originally paid, whichever is the lesser.

This creates a problem if you are a small business entity using a low value pool. Just another reason never to believe they have simplified things for small business entities because you have to keep the records anyway. You will have to trace back to your documents on the original purchase because your depreciation schedule will not show the individual items in the pool.

If you have been claiming GST on a cash basis your final BAS must be prepared on an accruals basis ie take debtors and creditors into account.

Budget GST Measure for Developers

The budget included a warning that GST law would be tightened to reduce the tax benefits of combining the going concern or non taxable supply exemptions with the margin scheme. This should not take affect until the new law receives royal accent, so there is a bit of time yet. But when it does become law it is important that developers realise if they purchase land from someone who is registered for GST but the sale is not subject to GST they need to find out the original price paid by the vendor because this will be the new purchaser's base for the purposes of the margin scheme.

For those not familiar with the workings of the margin scheme, it is intended to prevent the ATO from collecting tax on a profit that was exempt from GST in the hands of the previous owner. So if for example a developer purchased a property from someone not registered for GST for \$100,000 and then sold it for \$150,000 GST would only be payable on the margin of \$50,000.

This will limit the use of the margin scheme where the developer purchased the property from someone who was registered for GST but GST did not apply to the contract either because it was a non taxable supply or the supply of a going concern. In these cases the base figure for the margin scheme would not actually be the developer's purchase price but the purchase price of the owner before that. That is the developer would have to pay the GST on the profit made by the person selling them the property but strangest of all this would require the vendor to inform the purchaser of the price they originally paid for the property. This means that the margin ie the portion of the developers selling price that would be subject to GST, is the difference between the developer's selling price and the cost price of the property to the person the developer purchased the property from.

GST Draft Ruling on Subdivision and Partitioning Land

The ATO has released GSTR 2008/D3 discussing its opinion on when GST applies to the subdivision and partitioning of land.

A subdivision or strata in itself does not create a GST liability because there is no supply of the land. But the next step, partitioning the land so the joint owners can own a lot or unit individually is where GST could apply. If the arrangement is a joint venture then GST is only likely to apply to the portion that is being transferred by one owner to the other. If it is a common law partnership transferring to the individual partners, GST will apply to the whole transfer but the margin scheme is available.

GST is unlikely to apply if you are not in a profit making arrangement, for example the property is split to build a rental or a home for yourself. This ruling is discussed in detail in the October edition of Australian Property Investor Magazine.

GST and Small Farm/Home Stays

Commercial residential premises are subject to GST. This doesn't just mean that you need to charge your guests or tenants GST it will also mean that when you sell these premises you will have to charge GST if you are still registered for GST. On the up side you can claim the GST back, if applicable on the purchase of the property. The trouble is if you were entitled to claim the GST back on the purchase then if you de register for GST and still have the property, you may have to pay back some of the GST credits.

As you can see it is important to know exactly where you stand. The trouble is it is not all that clear for small B&Bs, farms and home stays. GSTR 2000/20 goes into great detail on the fine line between a normal rental property which is not subject to GST and commercial residential properties such as motels. It seems that if you only have one unit of accommodation and do not provide much in the way of services to your guests you do not have to register for GST because you are just providing a normal domestic rental, this could continue to be the case if you have more than one unit providing they are not in the same complex. But once you get more than one unit on the same property and you are advertising short term accommodation you should consider whether you should be registered for GST. The best way to be sure is to apply to the ATO for a ruling. Note if your turnover is less than \$75,000 you are not required to be registered for GST anyway so you can rest easy until your current month turnover, taking into account seasonal fluctuations, suggests that your turnover will exceed \$75,000 within the next 12 months.

Of course a typical motel like situation would have to be registered for GST if the turnover is more than \$75,000, no need for a ruling to clarify.

Renting Out a House You Built to Sell

There has been much written about this in Newsflash and our How Not To Be A Developer booklet. Basically if you are registered for GST and build a house for resale but then change the purpose by renting the house out you have to pay back the input tax credits on the property. You see a property held for rental is input taxed so no GST credits are available on the cost of building it. If you have been claiming them because you intended to sell the property so will have to charge GST on the sale, then later change your mind or can't sell it. Then using it as a rental property will mean quite a large amount of GST has to be paid back.

Now I imagine you are starting to think that it is not as black and white as that. You may not have changed the purpose at all it is just logical to collect rent for the property while the market is slow. I imagine there were some developers caught between a rock and a hard place. They can't possibly afford to pay back the GST but could really benefit by receiving some rent to help meet the overdraft.

ID 2008/114 examines purpose beyond the current use and recognises a property can still be held for resale while it is rented. The following paragraph from the ID gives a clear guideline as to what would be considered holding a property for resale:

Determining whether or not new residential premises have been actively marketed for sale will require consideration of all the relevant facts and circumstances. Although no single factor by itself is conclusive, the active marketing of new residential premises for sale may encompass activities such as listing the property for sale with a real estate agent or agents, advertising the premises for sale in relevant publications or via Internet advertising websites for real property, arranging 'open for inspection' times and/or showing prospective buyers through the premises. In the case of stratum units,

actual arm's length sales of some of the listed units would be further evidence of active marketing. Listing premises for sale at a price that is significantly above market value may be an indicator that the premises are not being actively marketed for sale.

ID 2008/114 is only an interpretive decision so you cannot hold the ATO to its content unless you are the applicant. Accordingly, if you want to use this interpretation to your advantage you should apply to the ATO for your own ruling quoting ID 2008/114 as a precedent.

By the way you do not have to pay the GST back immediately, even if you are caught. You are only required to consider this issue once a year, when preparing your BAS for 30th June. You do not even have to consider an adjustment to the GST at the first 30th June after the original input credit has been claimed it is not until a full 12 months after the first 30th June that an adjustment must be made. Now if the property has at anytime been used for a rental then some adjustment needs to be made. But it may only be minor. Certainly if the property has now become a rental and it does not meet the available for sale status discussed above then you need to pay back all the GST. On the other hand with a property still available for sale, you only need to pay back a small portion of the GST. This portion is calculated by adding the estimated rent you expect to receive to the expected sale price then look at what percentage the rent is of this. This is the percentage of the GST credits you have to pay back. Yes, very vague but each 30th June you will have to re work this calculation until you sell it (assuming it is sold within 5 years) so eventually the right amount will filter through.

Interestingly the ATO has recently issued a warning to property owners or developers who are registered for GST that their June BAS should have included an adjustment if they are now renting the property out. The warning goes on to encourage readers to fess up and correct their BAS now before they are found out in an audit were the penalty could be as much as 90% of the tax not paid.

GST and Vacant Land

The ATO issued an Addendum to GSTR 2003/3 pointing out that the exemption from GST on domestic properties that are not brand new does not apply to the sale of land cut off from such a property. Even if you are registered for GST you do not have to charge GST on the sale of a house if it is not the first time it has been sold as a residential property. Note if you undertake substantial renovations that affect every room in the house then the next sale of the house will be subject to GST because it is considered new again.

In order to qualify for the concession the house and land have to have been sold previously as a package. Vacant land can never qualify for the concession. This is the case even if there was once a house on the land or the block has been cut off from a house and land. Relocating a home onto land and selling it will still be considered the first sale of the house because it is the first time that piece of land and that house have been sold together.

If you buy a house and land, move the house to one side and subdivide the land GST is not applicable to the sale of the house side because that land and house have previously been sold together but of course GST will apply to the separate sale of the vacant land. On the other hand if you add land to an existing house and land package you will have to charge GST on the sale of that part of the land because that land had never been sold with that house before.

Note if you are not registered for GST and you are not selling the land as part of your actual business activity then even though the sale maybe for more than \$75,000 you are not required to register for GST. The \$75,000 threshold, at which you are required to register for GST, only includes turnover that is subject to GST from normal business operations, even domestic rents are not included in this threshold because they are not subject to GST.

For more detail on GST and property refer our How Not TO Be A Developer Booklet available under the freebies section of our website.

Demolishing a Rental Could Expose it to GST

Before you go picking up that sledge hammer thinking you will get more for your rental property as vacant land have a read of ID 2009/20 and ID 2009/19.

In these examples the owners of both these rental properties were registered for GST because they did some development and held some properties simply as rentals. Subsection 9-30(4) of the GST Act states:

A supply is taken to be a supply that is input taxed if it is a supply of anything (other than new residential premises) that you have used solely in connection with your supplies that are input taxed but are not financial supplies.

Input taxed means you do not have to remit GST on the income you receive. One property had a demountable home on it which the owner sold off separately and the purchaser of the demountable home was required to remove the house at their own cost. In this case the ATO considered that the property had at all times been used solely as a domestic rental and was input taxed so the sale of the vacant land was not subject to GST.

In the other example the owners decided to demolish the property themselves. The ATO considered this to be using the property other than for input taxed supplies so GST applied to the sale of the vacant land.

Of course if they simply left the house on the land, GST would not apply either because it only applies to the first sale of residential property and then only if it has not been used as a rental for a continuous period of more than 5 years. Removing the house changed it from residential property to simply vacant land.

GST on Bank Charges

Late Payment Fees – These fees include GST

Retailer Credit Card Charges - When a retailer charges you a fee for using a credit card GST will apply to the fee if the item you buy is subject to GST. In some cases the fee amount will have to be apportioned between items subject to GST and those that are not.

GST Adjustment Periods

Each 30th June is an adjustment period so you need to consider this for the BAS you are currently preparing. An adjustment is necessary when the ratio of deductible to non deductible use of an item has changed from that on which you originally apportioned the GST. Any invoices under \$1,000 do not have to be considered but don't forget to consider all invoices over \$1,000, for example motor vehicle repairs when the ratio of business to private use of the vehicle has changed.

The number of adjustment periods depends on the GST exclusive amount of the invoice. Invoices for \$1,001 to \$5,000 have two adjustment periods. Invoices for \$5,001 to \$499,999 have 5 adjustment periods and for \$500,000 or more there are 10 adjustment periods.

GST When You Sell a House You Built as a Rental

The following section references are provided to assist readers whose accountants are advising them that they must pay GST if they sell a rental property less than 5 years after they build it.

If you are not already registered for GST you are not required to do so just because you choose to sell a property you built with the intention of holding as a rental. Section 23-5 states that if the annual turnover of supplies you make in the normal course of your enterprise, exceed \$75,000 you must register for GST. Section 185-25 excludes from the calculation of annual turnover the supply of a capital asset. Building the property for rental then selling, is the supply of a capital asset and not included in the annual turnover. Section 118-15 excludes from annual turnover input taxed supplies so any domestic rent received is not included in annual turnover.

What if You Use Two Dwellings As Your Home?

If they are adjacent to each other then you could, in theory, cover them both with your main residence exemption. The trouble is that you would have to sell them both to the same person on the same day to be able to use your main residence exemption on both.

Section 118-192 resets the cost base of a dwelling to its market value at the date it first produces income, if until that date it had always been covered by your main residence exemption. This section is compulsory and the only prerequisite is that the property would have been entitled to your full main residence exemption had it instead been sold at the time it was first rented out.

Now when examining whether it would have been covered up till that date look back over section 180-110 to 118-120 pretending that a sale has actually happened. If a sale had actually happened at that time then the dwelling (residence used as a home by the owner) and adjacent land up to 2 hectares are exempt.

This means that a duplex where both sides are used as a home, or when you subdivide and build a house on the back of your home block where the new house is also used as part of the family home, then both properties qualify for your main residence exemption. If you then move out of both and rent them out the cost base on both is reset to the market value at that time. Now you can sell them to different purchasers and cover one with your main residence exemption under the 6 year rule and the other would be exposed to CGT but only on the difference between the market value when you moved out plus selling costs etc and the selling price, which probably won't be much at all. Section 118-120 talks about adjacent land being included in the main residence exemption so if you own another house in the same street that is also used by the family and is not income producing yet then it would be considered adjacent and the main residence exemption would be available. It is not necessary for both properties to be connected, the section says adjacent not adjoined.

But don't go building a house down the back or a duplex with the intention of utilising this because if you build with the intention of selling then you are going to be up for normal income tax on the profit and GST.

The Margin Scheme When You Develop a Block Where You Didn't Claim Back the GST on Its Purchase

If you are considering developing a block of land to an extent that you are considered to be in business (Refer our How not to be a Developer booklet) then if you haven't claimed GST back on the original purchase of the land, you need to understand the margin scheme.

GST is 1/11th of the price you sell the property for, you will get an input credit for any GST you pay on your development costs. The trap is if you didn't pay GST on a council fee or employed a tradesperson who was not registered for GST you will have to charge GST on the effective value they add to the property even though you did not qualify for an input credit on that cost. So you may sell a property for \$110,000 and have to send \$10,000 off to the ATO this leaves you \$100,000. If you have spent \$60,000 on bringing the property into existence for sale but there was \$5,000 in costs to which GST did not apply then your input credit is only going to be \$5,000 (1/11th of \$55,000) so the net GST you pay on the project is \$5,000 even though your profit is only \$45,000: that is the GST ends up being 1/9th of your profit.

Note the margin scheme can only be used if the original purchase was not subject to GST because the seller was not registered or the supply was under the margin scheme originally, the purchase happened before GST was introduced or the purchase was not a supply subject to GST because it was a residential building but not the first sale since construction. The margin scheme does not apply if GST didn't apply to the original purchase due to one of the exemptions such as going concern applying ie the property was actually a GSTable supply but a special exemption was used to avoid charging the GST. The margin scheme can only be used with a house and land or land.

The margin scheme is intended to minimise the GST when the original purchase did not include GST. The margin scheme cannot be used on any development costs even if no GST has been charged. The idea of the margin scheme is to make sure that the GST you pay on the sale is only on the margin between the selling price and the original purchase price of the property, if you did not have the benefit of claiming input credits on the purchase of the land.

If you buy a property under the margin scheme then you are not allowed to claim any GST back on its purchase but you are also entitled to use the margin scheme when you sell so it all comes out in the wash. . A sale that is subject to the margin scheme must have a written agreement signed by both parties on or before settlement for the sale, stating this.

If you purchased the property before GST was introduced, which was 1st July 2000 then you are entitled to use the margin scheme when you sell it, even if the latter sale is of a unit or portion of the land (references Section 75-15 GST Act). In these circumstances the margin is the difference between the selling price and the market value at either 1st July 2000 or the date you became registered, whichever is the most recent.

From Property Development to Investment Property

Section 70-110 of the 1997 ITAA states that you can stop holding a block of land or building as trading stock and start to hold it as a rental property or for private use even though your original intention when purchasing the block was to develop it.

Until this section was included in the legislation, an item of trading stock was always considered trading stock no matter how long you held it, its character could never change. There are so many precedents still around that back date to before this legislation that many people don't realize it is no longer the case.

All you have to do is simply stop holding it as trading stock and it will be considered to have been acquired by you at that time for its cost. There is a ruling about the GST consequences of a partnership making a supply to its partners but that would be the case if the name on the title was changing. In the case of a partnership between husband and wife who were then going to hold the property together as a rental, all that would be happening is a change of purpose not a change of ownership. The change of purpose will mean GST credits would have to be paid back. Deregistering for GST would also trigger the same paying back of GST credits (section 138). Though it only applies to GST on invoices exceeding \$1,000. Invoices exceeding \$1,000 will have to have their GST paid back if their adjustment periods have not expired. Invoices for \$1,001 to \$5,000 have two adjustment periods. So their adjustment period does not expire until two years after the first 30th June after the BAS in which the GST was claimed. Invoices for \$5,001 to \$499,999 have 5 adjustment periods. Of course the amount of GST you pay back will increase the cost base of the lots to you because the cost currently recorded in the accounts would be the net of GST amount.

GST Adjustment Periods

Each 30th June is an adjustment period, so you need to consider this for the BAS you are currently preparing. An adjustment is necessary when the ratio of deductible to non deductible use of an item has changed from that on which you originally apportioned the GST. Any invoices under \$1,000 do not have to be considered, but don't forget to consider all invoices over \$1,000, for example motor vehicle repairs when the ratio of business to private use of the vehicle has changed.

The number of adjustment periods depends on the GST exclusive amount of the invoice. Invoices for \$1,001 to \$5,000 have two adjustment periods. Invoices for \$5,001 to \$499,999 have 5 adjustment periods and for \$500,000 or more there are 10 adjustment periods.

Some Answers on Selling Solar Power Back to the Grid

A reader has very kindly alerted us to a PBR on this topic. Now PBRs are summaries of private binding ruling applications. Only the person who applied for the ruling can bind the ATO to their word. Nevertheless these rulings are a method of finding out just what the ATO is thinking when there are no other rulings on the subject.

There are thousands upon thousands of these PBRs so if any readers receive an interesting ruling response please don't assume we know about it. We would certainly appreciate hearing about yours.

In PBR 92788 it appears, reading between the lines, that the taxpayer was hoping to negatively gear their solar panel investment, because it talks of claiming interest and being unlikely to make a profit in the near future. The ATO found that tax did not apply to the activity because the panels were on the taxpayer's home rather than in a business environment and the operation was not of the size normal for electricity generation. Further their motive was not business like as it was to offset their electricity consumption and create a renewable energy resource. I wonder if the answer would have been different if they were likely to make a profit. This is a good outcome considering the record keeping involved would not be worth the small amount, if any, tax revenue that would be generated, so let's hope the ATO stick to this opinion.

The PBR specifically states that interest is not deductible. This can be used to address the CGT concerns, that if a home is used to produce income then only part of the main residence exemption is available. The formula for determining the percentage of the gain on the home that is subject to CGT is based on the rules that determine how much of the interest on the loan for the home would be deductible. So as you can see, even if, because the home is actually producing income, it is caught by the CGT provisions, as the PBR states none of the interest is deductible then the percentage of the gain that is taxable is still zero.

What still remains unanswered is the comment on TV by an MP that Centrelink would be taking the income received from selling electricity back to the grid into account when calculating the house owner's entitlement to

the Pension and other benefits. We have had an election since then so hopefully that MP is no longer in Parliament.

Of course the situation is completely different if these panels are on the roof of your business. In this case, if you are registered for GST, you will have to remit 1/11th of what you receive to the ATO as GST. Regardless of whether your business is registered for GST or not the income from its solar panels will be taxable.

2011 Checklist – Before Paying an Invoice

Invoice checklist

You should not have any business expenses over \$75.00 where you do not at least have a record of the supplier's ABN.

Supplier is not registered for GST

If the supplier is not registered for GST then you enter the full amount of the invoice in the relevant expense column but if the invoice is for more than \$75.00 you need to make sure you at least have their ABN.

Supplier is registered for GST

If the supplier is registered for GST then the amount you enter in the relevant expense column is the net of GST amount (usually 10/11ths). This is the case whether you have a tax invoice with the appropriate entries or not. The absence of a valid tax invoice means you do not qualify to claim the GST back but you still do not qualify to claim the GST as an expense! To make the spreadsheet balance it will be necessary to put the GST component of the payment in the column titled 'GST where no tax invoice held'.

If the tax invoice for a GST supply exceeds \$82.50 (GST inclusive) you need to check that the invoice has the appropriate entries to qualify as a valid tax invoice before you qualify to claim a credit for the GST. For supplies over \$82.50 it must be clear that the document is intended to be a "tax or GST invoice" and show how much GST has been charged. It needs to contain the date, supplier's name and ABN. Details are needed of what is supplied, the quantity and price. If the invoice is for \$1,000 or more it must also contain your name or ABN.

Charging GST When Used For Private

Quite often we are asked whether a person who is registered for GST has to charge GST on all taxable supplies they make when the item might not have been intended to be part of their business. Examples would be a carpenter who is registered for GST and built a rental property, as an owner builder. Does he or she have to charge GST if they sell the property. A husband and wife partnership who are registered for GST in a retail outlet but subdivide off their back yard and sell it. A builder who builds his or her own home but later sells it.

It is all a question of whether the sale is in the course and furtherance of a business, which unfortunately again boils down to proving what you were thinking at the time. The 1998 explanatory memorandum to the A New Tax System Act, at paragraph 3.10 went so far to say that even when a car dealer sells his or her own private car GST would not apply.

Of course, in these circumstances you would not claim the GST input credits when you built or subdivided.

GST and Transferring Land Between Co Owners

The catch when you subdivide land, build a duplex or townhouses with a business partner is that, assuming you jointly owned the original property, then all of the lots or units are going to be jointly owned by you both. If you transfer the titles around so that you each own particular properties individually, then you are making a supply to each other and this may well be subject to GST.

The first question is whether the activity is an enterprise and then whether you are in partnership or merely co owners of the property. In technical terms the word partnership in this article and in the relevant ruling GSTR 2009/2 refers to a general law partnership which is a business enterprise. Co owners is referring to something less, i.e. not a profit making motive from selling the property. A non profit making motive, from selling, would be when two people buy and develop so they can have a home or rental property each.

If you are in a general law partnership it is the partnership that is supplying the whole property to you not just the other partner's share. So GST would be payable on the whole value of the property (possibly reduced by the margin scheme). Mere co owners of property would only have to pay GST on the fraction of the property transferred and that is only if they are required to be registered for GST which quite often would not be the case for mere co owners because the property is not part of their normal turnover so their turnover is under the \$75,000 threshold.

It is all about your intentions. That age old question of whether you are merely realising an asset or in business to make a profit. A general law partnership is about a profit making venture. So if you purchased the property to hold as a rental or your home you would not be in a general law partnership as the rent is passive investment income. But if you then go into a business by demolishing the rental and building townhouses you are into a profit making venture and GST would apply if you sold the townhouses rather than continue to hold them as rentals. Selling vacant blocks of land can sometimes be considered merely realising an asset rather than a business but only if your original intention when purchasing the property was not to subdivide. Our how not to be a developer booklet (in the freebies section of the web site) discusses the ATO's jagged line on when it thinks you may have crossed over from merely realising an asset. This topic is also discussed in MT 2006/1.

All we are looking at here is what happens when you are doing **more** than merely realising an asset and you want to take away from the project, properties in your individual names rather than just sell off to the public. Remember the most common outcome would be for the partnership to sell to the public or the co-owners to keep the units for rental or private use. We are now really just looking at the unusual circumstances of when the development is business like ie profit making (must register for GST) ie general law partnership but for some strange reason the partners decide to transfer the properties (or at least some of them) out of the partnership and into their own names. In the particular case that led to this article a solicitor decided to transfer the titles around between the owners before the properties were then on sold to the public.

Let's consider a town house development which is business like with a profit motive, yet the partners will take away a townhouse each and sell the rest to the public. For GST purposes this is a supply by the partnership to the partners so the partnership must charge the partners GST. Note for income tax or CGT purposes the partnership is not even recognised as owning the property, the individual partners are, let's not even go here at this point but it is suffice to say do not apply the GST principals here to any income tax issues.

The GST effect of the partnership being the transferrer is that even though one partner might already have their name on half the title, when the townhouse is transferred to them GST would be payable by the partnership on the value of the whole townhouse (though the margin scheme maybe still used to reduce the GST). This is an important reason why you need to avoid being considered a general law partnership if you don't intend on selling the property.

The very fact that you don't intend on selling supports the fact that there is not a general law partnership anyway. Paragraphs 79 to 85 of GSTR 2009/2 recognise that two people can come together to do a development with different purposes in mind. If in this case you were the one building to sell and the other co owner was building to live in then you really have to look at the one property as two separate assets. The first sale of a new residential property is subject to GST but not any subsequent ones unless it is substantially renovated. So if you received half the property from the other co owner with no GST being charged because they weren't registered then when you sell only half the property is being sold for the first time so only half of it would be subject to GST. The trap is when you transfer your half of the live in co owner's property to them you will have to charge GST because you built that half with the intention of making a profit as part of your enterprise. So in the end the full GST is paid. Half of the value of your unit on the transfer to the other co owner of half of their unit and the other half of the GST is paid (on half the value of your unit) when you sell to the public. You only charge half the GST on this latter sale because only half the unit is being sold for the first time. The other half was sold to you earlier by the other co owner with no GST charged because they did not have a profit making motive so they were not required to be registered for GST.

A joint venture is a different situation to the partnership discussed above though GSTR 2009/2 asserts the transfer should still be a taxable supply despite subsection 51-30 stating that a transfer to joint venturers is not a taxable supply.

Don't forget if you are not already registered for GST and the units are not built to be sold as part of your normal business turnover then their sale will not force you to register from GST because your taxable supplies from your normal turnover are not over \$75,000.

Saving Tax on Your Investment Property – The Book

“Every investment property tax-related question you’ve ever wondered about is answered here and – perhaps more importantly – the ones you didn’t think to ask but should have! For property investors who want to refine their strategy for maximum gain, this resourceful handbook will make a great constant companion.” Eynas Brodie, Editor, Australian Property Investor magazine.

Combining Noel Whittaker’s easy reading style with Julia Hartman’s mind numbing attention to detail was a major challenge but made it to the book stores. You can also purchase it online by going to:

bantacs.com.au/book_savingTax.php. The cost is \$29.95 plus \$5.95 postage – tax deductible of course!

Ask BAN TACS

For \$59.95 at [Ask BAN TACS](http://AskBAN TACS) you can have your questions regarding Capital Gains Tax, Rental Properties and Work Related Expenses answered. We will include ATO references to support our conclusion.

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Disclaimer: Please note in many cases the legislation referred to above has only just passed through parliament. The full effect is not clear yet but it is already necessary to make you aware of the ramifications despite the limited commentary available. On the other side of the coin by the time you read this information it may be out of date. The information is presented in summary form and intended only to draw your attention to issues you should further discuss with your accountant. Please do not act on this information without further consultation. We disclaim any responsibility for actions taken on the above without further advice as to your particular circumstances.