NEWSFLASH

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BAN TACS Accountants Pty Ltd

BAN TACS Accountants Pty Ltd is a CPA Practice

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Queensland

Gold Coast ***PNA***
Phone : (02) 6736 5383
E-mail: goldcoast@bantacs.com.au

Mackay ***CA***
Phone: (07) 4957 8340
E-mail: mackay@bantacs.com.au

Ningi ***CPA***
Phone: (07) 5497 6777
E-mail: ningi@bantacs.com.au

Stanthorpe ***PNA***
Phone: (07) 4681 4288
E-mail: stanthorpe@bantacs.com.au

Toowoomba ***CPA***
Phone: (07) 4638 2022
E-mail: toowoomba@bantacs.com.au

New South Wales

Burwood ***CPA***
Phone: 1300 367 688
E-mail: burwood@bantacs.com.au

Central Coast ***MNIA***
Phone: (02) 4390 8512
E-mail: centralcoast@bantacs.com.au

Tenterfield ***PNA***
Phone: (02) 6736 5383
E-mail: tenterfield@bantacs.com.au

Victoria

Geelong ***CPA***
Phone: (03) 5222 6962
E-mail: geelong@bantacs.com.au

Melbourne ***CPA***
Phone: (03) 5222 6962
E-mail: melbourne@bantacs.com.au

South Australia

Adelaide ***CPA***
Phone: (08) 8352 7588
E-mail: adelaide@bantacs.com.au

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Welcome to the BAN TACS News Flash. Our aim is to provide short but succinct updates on all tax issues

Don't Lose the Benefits of Your Farm Management Deposit

Recently enacted legislation will allow primary producers affected by natural disasters access to their farm management deposits within 12 months of making those deposits, without the loss of any tax concessions.

The changes are intended to provide the same relief to primary producers affected by natural disaster as that which is currently available to primary producers affected by severe drought and other exceptional circumstances.

These changes will undoubtedly be good news for many farmers but they won't provide relief from ongoing confusion and red tape surrounding the creation and use of FMD's. In recent months I have seen an increasing number of clients provided with inaccurate and inappropriate advice from organizations not qualified to provide accounting or taxation guidance.

Getting back to basics. To qualify for the benefits of a FMD you must be a primary producer. To fulfil the ATO's definition of primary production you must: cultivate or propagate plants or fungi; maintain animals for the purpose of selling them or their bodily produce; manufacture dairy products from raw materials; plant or tend trees that are intended to be felled; fell trees in a plantation, transport trees felled in a plantation; or conduct operations directly related to the taking of fish or the taking or cultivation of pearls. If you comply with this definition and you have agreed with your accountant that a FMD is appropriate for your circumstances select your financial institution carefully. Make sure you are dealing with someone who can clearly articulate to you the rules that apply to FMD's. When you receive your paperwork take the time to double check that the account has been correctly labelled and reported as a Farm Management Deposit.

As always maintain good records and in particular track any changes to account numbers which may occur as the result of reinvestment of funds.

This article was provided by Lyn Gower, third generation farmer and owner of our Tenterfield, Stanthorpe and Gold Coast offices.

More on Real Estate Contract Clauses

Following on from Newsflash 261 where we examined the nightmare a GST clause can cause we now look at vacant possession and a going concern clause which can be equally as catastrophic, so never ever sign a contract without getting advice.

Going Concern:

If the sale of a commercial property qualifies as the sale of a going concern the seller will not have to pay the ATO any GST when they sell the property. The trouble with property is its market value seems to ignore the GST component. This means that the seller may well get the same price for the property whether they charge GST or not, the difference being whether they have to send 1/11th of the selling price off to the ATO, So sellers are always on the lookout for a way to avoid this. A going concern clause, is a dream come true for a seller of a commercial property. It pushes the GST obligation onto the unsuspecting buyer who has already paid full market value for the property.

A going concern clause only ever has a good outcome for the buyer if they just can't afford the funds up front to pay the GST and then wait for the ATO to refund it. Before a going concern clause can apply both the buyer and seller must be registered for GST. If the contract was subject to GST then the buyer would be entitled to claim it all back from the ATO anyway.

Say the market value of a property is $550,000 if the contract is subject to GST then the seller would have to send off $50,000 to the ATO and only end up with $500,000 in the hand. The buyer may hand over $550,000 but in the next BAS he or she will get $50,000 back as an GST input credit so is really only out of pocket $500,000. This means that if the sale is going to be subject to the going concern provisions the property should really change hands for $500,000. I don't like your chances of talking the seller into that when they know the valuation is $550,000. So just don't agree to the going concern clause, register for GST and pay the full $550,000.

The main reason you don't want to agree to a going concern clause is because if you ever de-register for GST or stop using the property in a business, for example as per last edition, the purchaser was eventually going to turn the professional offices back into a house, then you have to pay back the "notional" GST input credit you received. In the example above, that means effectively paying another $50,000 for the property. Notional, because you didn't actually receive it, it was just that the seller didn't have to pay it to the ATO, but the law is like this because the going concern exemption from GST is intended to make the property cheaper by the value of the GST. This is something that does not always happen unless the purchaser is well informed and a very good negotiator.

All this may lead you to decide to sell the property and cut your losses. That won't get you out of it either. Let's assume you decide this rather quickly so the property is still only worth $550,000 but what if your purchaser is not as gullible as you were? If the purchaser does not agree to use the going concern exemption (and they only should if you sell it below market value) you are going to give the ATO $50,000 of your sale proceeds even though you may still owe the bank the $550,000 you paid for it.

Vacant Possession:

This is a much more straight forward problem. It is only an issue if you intend to use the property as your home. If you don't move into the home as soon as practical after settlement then you will not be able to begin to cover the property with your main residence exemption until you actually move in. Sure it may be only a short time before the tenant moves out. It is not the portion of the gain that you will pay tax on that is the problem. It is the fact that you will need to keep records for the whole time you own the property in order to be able to calculate the whole gain to apply that small percentage to.

Directors' Liability for Unpaid Super and PAYG

Directors of a company can very quickly become personally liable for any superannuation that the company has not paid or any amounts of PAYG that it has withheld from wages but not paid to the ATO.

If 3 months have lapsed since the PAYG was due to be paid to the ATO, the ATO can simply serve a penalty notice on the directors and make them personally liable.

In the case of the superannuation guarantee, these payments must be paid into a superannuation fund before the 28th day after the end of the relevant quarter. If they are not paid by that date then the company must lodge and pay the superannuation guarantee charge within another 28 days ie 56 days after the end of the quarter. If this is not done then the company directors are personally liable.

Capitalising Interest Update

Well the plot is thickening and we are certainly no closer to some clear guidelines. The following is an extract from a letter we received from the ATO in relation to some questions we asked about borrowing to pay rental property expenses. While it gives two examples of when Part IVA would not apply, they are so extreme that you can see it is their intention to push Part IVA as far and wide as they can.

"When taxation considerations constitute at least a substantial purpose of a taxpayer, it is practically inevitable that Part IVA must be considered and cannot simply be ruled out or in.
However, I offer the following observation. There appeared to be a theme to some of your questions; they dealt with an unexpected change in circumstances. In determining whether there is a scheme to which Part IVA applies it will often be necessary to consider whether there has been an unexpected substantial change in the taxpayer's financial situation.
For example:

- If a taxpayer has an unexpected illness that means that they can no longer use their salary to pay the difference between the interest on their investment loan and the rent from the investment property, then the taking out of a line of credit to fund this difference would generally be viewed as weighing against there being a scheme to which Part IVA applied, particularly if the use of the line of credit ceased once the taxpayer went back to work; or

- if it was necessary for a taxpayer to make unexpected repairs to their rental property which they were unable to fund from non-loan sources, then the taking out of a line of credit to fund the repairs would generally be viewed as weighing against there being a scheme to which Part IVA applied."

Surprise, surprise the ATO officer who wrote this letter has requested that I do not identify him. I will say he is very high up at the ATO so this needs to be taken very seriously.

Am I over reacting or does the above say that the ATO will apply Part IVA to deny an interest tax deduction when money has been borrowed to undertake repairs that the taxpayer should have known would need doing or even if they were unexpected but the taxpayer had other funds available (you know that money you keep aside to save up to pay your annual bills or as a safety against unexpected medical expenses). Your emergency savings must be used to fund the unexpected repairs because the ATO will use Part IVA to claim that a choice to borrow the money instead is a scheme with the dominant purpose of a tax benefit. Further, if you have no income because you are ill then you are allowed to borrow the difference between the rent and the interest on your investment property but only until you go back to work then propping up the rental property must come first, no consideration of any other more important bills.

Hart's case made it clear that it was ok to borrow to pay deductible expenses when you were having trouble meeting your commitments there was no mention of supporting investments before other more personal needs. This concept is also backed by case law and rulings. Part IVA is only supposed to apply when the dominant purpose of the arrangement is to gain a tax benefit. In the above this has been reduced to "substantial purpose".

It is time to go back to the courts or someone at the ATO makes them more accountable for their opinions. The ATO does not make the laws they must play by the rules like the rest of us and cannot just dream up their opinions, they must have a basis of law. To apply Part IVA in the case of a 'substantial purpose' would mean that choosing to walk into a newsagency and buy an invoice book then ask for a receipt thus showing an intention to claim it as a tax deduction could be considered a scheme caught by Part IVA. Fortunately the law says dominant not substantial!

If you would like to read the rest of this letter go to
www.bantacs.com.au/docs/Latest-word-from-the-ATO-on-Interest-Deductions.pdf

If you would like to read the minutes of the meeting we had with them where these and other questions were raised go to: www.bantacs.com.au/docs/Minutes-from-GAAR-Panel-Meeting.pdf

If you think it is going too far for the ATO to say that you are not allowed to claim a deduction for borrowings to pay interest on your rental property, repairs (possibly renovations) rates and insurance unless you have no other income at all (no consideration for your living expenses) and do not have any savings then please join the NTAA's who provide excellent membership benefits at a very low $295 pa and most importantly have a fighting fund. Also send a copy of this to your local Federal member.

$5,000 For Building a New Home In NSW

A $5,000 grant is available to buyers of new homes, whether off the plan or newly built, with a value up to $650,000 and to buyers of vacant land that is intended to be the site of a new home valued up to $450,000.

This is not just for buying your own home, it can apply to investors too. For more information go to www.osr.nsw.gov.au/benefits/grant_scheme/

Winning Property Tax Strategies – The Book

Once again a brilliant combination of Noel Whittaker's easy reading style with Julia Hartman's mind numbing attention to detail. Lots and lots of new stuff, plus updated basics for the first time reader, so it is much bigger, 300 pages but still the same price.

New chapters including young investors, SMSFs, renovators, granny flats, investment and budgeting strategies, fires and floods, mass marketing spruikers, commercial properties, subdividing and development.

You can also purchase it online by going to www.bantacs.com.au/book_winning-property-tax-strategies.php The cost is still a low low $29.95 plus $5.95 postage – tax deductible of course!

New and Improved Number Cruncher

A new number cruncher is available in the shopping section of our web site www.bantacs.com.au/shopping_property_breakeven.php It will calculate how much a negatively geared rental property will cost you to hold on an annual basis after taking into account the tax refund it will generate. The calculator then goes one step further to calculate how much capital growth is required (after considering CGT) to breakeven ie recover this holding cost. This is the calculator mentioned in the annexure of Winning Property Tax Strategies.

It is a simple easy to use XL spread sheet that lays everything out so you can understand how the conclusion is reached.

An excellent tool for comparing properties in different areas breaking the numbers down to a percentage of capital growth required so that all you need to decide is which property is more likely to reach their percentage.

Infinite life, simply download on line for $27.95

Ask BAN TACS

For $59.95 at www.bantacs.com.au/QandA/index.php 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.

Where is Julia?

At home in South East Queensland hopefully until the middle of the year except for a short trip to Sydney.

What Is New on www.bantacs.com.au

Want more? Please go to www.bantacs.com.au/publications.php for back issues of newsflash or download our free booklets where past newsflash articles are collated according to their topic.

With the Forum, www.bantacs.com.au/forum, and the Ask BAN TACS Notice Board, www.bantacs.com.au/QandA/index.php?section=browse, the information on the site changes daily but here is a list of significant changes in the past couple of weeks:

Askbantacs – One askbantacser has very kindly allowed their question to be posted on the Ask Bantacs Notice Board http://www.bantacs.com.au/QandA/index.php?xq=435 is about all the CGT problems associated with putting a granny flat in your back yard.