NEWSFLASH

Visit us at www.bantacs.com.au

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BAN TACS Accountants Pty Ltd

BAN TACS Accountants Pty Ltd is a CPA Practice

Issue Number: 266 Pages: 4 Date: 1st April, 2013

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

Column by Noel Whittaker

The age pension for singles is about to increase by $35.80 fortnight – couples will see an increase of $27 a fortnight per person. This means it is timely for anybody nearing retirement to understand the way the pension is assessed.

Applicants are assessed under an asset and an income test and the one that gives the least pension is the one used. The family home is not counted, while chattels such as furniture, car and boat are valued at second-hand value, not replacement value. This puts a figure of $5,000 on most people's furniture.

The asset cut-off points for a homeowner couple are currently $1,050,000 and for a single pensioner $707,750. The income test cut-off points are $67,537 per annum for a couple and $44,127 for a single.

Financial assets are deemed to be earning 2.5% for the first $75,600 ($45,400 for singles), and 4% on the balance. For example, if a couple had $300,000 of financial assets their deemed income would be $10,866 a year being 2.5% on $75,600 ($1,890) and 4% on $224,400 ($8,976). These include interest bearing deposits, debentures, shares, share trusts, and friendly society and insurance bonds. However, it does not include property, and money in account-based pensions.

Your superannuation is not counted until you reach pensionable age. We often encounter situations where the husband may be 65 or more and where the wife less than 60. Wherever possible we encourage as much superannuation as possible to be held in the wife's name, as it is not counted by Centrelink, and this enables the husband to maximise his pension.

Unfortunately, many people in their late fifties do not understand these rules and start an account-based pension when they should have simply relied on withdrawals from their superannuation. As soon as they start the account-based pension, its value counts for the asset test even if they have not reached pensionable age and they often render themselves ineligible for Newstart.

Noel Whittaker is the author of Making Money Made Simple and numerous other books on personal finance. His advice is general in nature and readers should seek their own professional advice before making any financial decisions. Email: noelwhit@gmail.com.

Latest Changes to Superannuation

Currently if a superannuation fund is in pension phase any income on its investments are tax free and it remains tax free when paid out to members. Starting on 1st July, 2014 the government will claw back some of this tax concession for the big end of town. When the superannuation fund earnings of an individual member exceed $100,000 in a financial year the excess will be taxed at 15%. The $100,000 threshold will be index to CPI increase in $10,000 intervals. The tax will not apply to capital gains on assets purchased before 5th April, 2013 for 10 years ie 2024. It is estimated this will only affect 16,000 superannuation fund members. There will be no further taxing of this excess when it is paid to the member over 60 years of age.

Stay tuned for more detail as it becomes available but it would seem that members in this situation should take advantage of the ability to split their superannuation with their spouse. Before you start thinking that this is a reason why you should not invest in superannuation consider that once the fund is in pension phase the member is entitled to take the money out so at worse they will be in the position they would have been in if they had not utilised superannuation but during the accumulation stage and to date they have received tax concessions. But they will not take their money out of the superannuation fund because it is still a tax haven for them, just a little less so.

From 1 July 2013 the concessional superannuation contributions cap will increase from $25,000 to $35,000 for people over 60 years of age

From 1 July 2014 the concessional superannuation contributions cap will increase from $25,000 to $35,000 for people over 50 years of age

Taxpayers who have exceeded their contribution cap, from 1st July, 2013, will have the option of withdrawing the excess from the fund to be taxed at their marginal tax rate plus a shortfall interest charge.

Note all of the above is proposed, not legislation yet. The following has been passed.

From 1 July 2012, individuals with income greater than $300,000 had the tax concession on their contributions reduced from 30% to 15%. As people on $300,000 a year are in the 45% tax bracket this means their superannuation will be taxed at 30% (45% - 15%)

The definition of 'income' for the purpose of this measure will include taxable income, reportable employer superannuation contributions, adjusted fringe benefits, total net investment loss, target foreign income, tax-free government pensions and benefits, less child support.

CGT Consequences of Depreciation

Building Depreciation:

If you purchased you property after the 13th May, 1997 then any building depreciation that you could have claimed against your income must also reduce your cost base for CGT purposes. Generally, choosing not to claim the depreciation will not help you avoid the add back for CGT purposes. The legislation refers to depreciation that you were entitled to claim, not whether you claimed it or not.

There is a small window of opportunity here if you have not claimed building depreciation and do not know the amount that you would qualify to claim. It is intended to prevent people having to obtain a quantity surveyors report just to calculate their CGT when they have not had the benefit of the tax deductions over the years.

PLSA 2006/1 states that if you have no other way of obtaining the original building costs than paying for a quantity surveyors report and you have never claimed building depreciation in your tax return then you do not have to reduce your cost base.

TD 2005/47 addresses the situation where you do know the building costs ie you were the original owner, yet you have not claimed depreciation at all. In this case you only have to increase your cost base by the depreciation you could claim if you amended your tax returns. This limits your add back to the number of years you would be allowed to amend your tax return to claim the missed depreciation. Taxpayers with simple tax returns are only supposed to be able to amend back two years so you would only need to increase the cost base by two years depreciation. Note that the two years is from the assessment date. In a recent case the ATO was successful in arguing that in most cases a 4 year limit applies because beneficiaries of trusts have a 4 year limit and most trust deeds have such a wide definition of beneficiary that just about anyone could be caught. It is not necessary that they receive a distribution from the trust, it is enough that they technically could. As a result of this case the government's reduction of the amendment period for average tax payers to 2 years has been completely circumvented by the ATO.

Depreciation of Plant and Equipment:

It may surprise some readers to find out that there is no CGT on plant and equipment. It is subject to normal income tax ie no 50% CGT discount. If you have been using the ATO rates for your depreciation the ATO will generally accept that the original purchase price of your plant and equipment is the same as the start figures in your depreciation schedule and that the value of the plant and equipment on sale is the same as the balance of unclaimed depreciation in the schedule, so there are no tax consequences.

But this means that the first element of your cost base on an investment property, for CGT purposes, is the purchase price less the start value of the plant and equipment. Further, the sale price included in the CGT calculation is the sale proceeds less the remaining unclaimed depreciation in the schedule. Note if there was a period where the depreciation was not claimed ie the property was used for private purposes, the balance in the depreciation schedule should still have been reduced.

Draft Legislation on 50% CGT Discount for Non-Residents

While this legislation is only a draft, so may not make it through Parliament in its current form, it is not looking good for Australians working overseas with investment properties in Australia.

From 8th May, 2012 non-residents for tax purposes and temporary residents (ie 457 visa) will not be entitled to the 50% CGT discount. This will even apply to Australian citizens who may work overseas for a while. The draft legislation provides for an apportionment of the 50% discount based on the number of days you are a resident of Australia compared with the number of days you are not.

How the Capital Gains Tax Discount is Calculated

You will need a market valuation of the property as at 8th May, 2012. Valuers can work out the value back then by considering sales at that date, so don't rush but on the other hand don't leave it too long or at least take photos now so the valuer can consider any deterioration since May 2012.

When you eventually sell the property the formula starts with the gain up to the market value at 8th May, 2012 and checks whether this is less than the gain for the whole period. Initially this will be quite likely because the selling costs will reduce the total gain but not the gain before 8th May 2012. If there is no real gain since 8th May, 2012 then the full 50% CGT discount will apply.

The capital gain that relates to the period after 8th May, 2012 is calculated by deducting from the total capital gain, the capital gain made up until 8th May, 2012. The amount of 50% CGT discount you qualify for on the gain applicable to the period after 8th May, 2012 is relative to the number of days you were a resident to the number you are not. But it gets more complicated than that because the formula needs to come up with a percentage that applies to the whole gain apportioning between the pre and post gain figures. So it takes into account the pre 8th May, 2012 days at 50% discount and the post days at the ratio of resident to non-resident days and then apportions this over each period's relative gains. So let's assume the property made a $200,000 capital gain pre 8th May, 2012 and a total capital gain of $300,000. Also assume you owned the property for 1,000 days before 8th May, 2012 and the date you sell the property is 1,000 days after the 8th May, 2012 but for 500 of those days you were a resident. You will be entitled to a 41.667% CGT discount on the total gain over the whole period of ownership:

$200,000 pre gain + ($100,000 post gain x 500 resident days/ 1000 post 8th May 2012 days)

$600,000 twice the total gain

Well that is the formula, another way of looking at it is that two thirds of the gain was made pre May 2012 when the 50% discount applied and one third afterwards when the owner was only a resident for half the time. Two lots of 50% and one of 25% equals 125% divided by 3 to average them out is 41.667%.

If you do not have a valuation then you will lose the 50% CGT discount for the pre 8th May, 2012 period. The discount percentage is apportioned by reference to the days you were an Australian resident after 8 May 2012 as a proportion of the total time that the asset was held.

Temporary Residents

Taxpayers on a 457 visa will be treated as a non-resident for capital gains tax purposes though they will be entitled to the main residence exemption.

Changing Residency

Unfortunately it is not a question of your residency status when you sell the property. The whole period of ownership since 9th May, 2012 is examined with the 50% CGT discount only applying on a pro rata basis to the days you were a resident.

Main Residence Exemption

It is only the 50% CGT discount that is affected, not the main residence exemption. This means that temporary residents can still protect their Australian home from CGT. Note temporary residents are not subject to CGT in Australia on any gains they make on their overseas assets.

Section 118-145 (6 year rule) will not change. It contains an example of how a resident of Australia can leave and become a resident of another country for tax purposes but still continue to cover their home with their main residence exemption. As long as the main residence exemption fully covers the property there is no need to look at the 50% CGT discount. This means that an Australian citizen could continue to own their home here, completely protected by their main residence exemption, while they work overseas, providing it only produces income for a period of 6 years or less. If it is not earning income it can continue to be covered indefinitely.

Donations to School Building Funds

To claim a tax deduction for donations to a school building fund the payment must be voluntary. So a "donation" that is part of the school's fees would not qualify.

Further, it must be to a public fund whose sole purpose is to provide money for the acquisition, construction or maintenance of a building used as a school by a government, public authority or a non profit organisation. TR 2013/2 provides much more detail.

Off The Plan Apartments

Stacks the Law Firm have created a useful check list of 12 pitfalls of buying off the plan. The article is available at

http://www.stacklaw.com.au/web/page/top-12-pitfalls-in-buying-property-off-the-plan/news/3028

Where is Julia?

Back home in South East Queensland until the cold of the winter drives her further north.

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!

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For $59.95 at Ask Bantacs, 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.

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