NEWSFLASH

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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

In the last issue I pointed out the extra opportunities offered by salary sacrifice now that the concessional cap has been increased to $35,000 for people aged 60 and over.

Let's think about a person aged 60 who still owes $100, 000 on his home – he would like it to be paid off in five years when he retires at age 65.

Option One is to repay $1933 a month ($23,196 a year) which will have the loan paid off in five years if the rate remains a 6%. The cost to his salary package will be $3143 a month ($37,716 a year) in pre-tax dollars. After five years his home loan would be paid off at a total cost of $188,580 in pre-tax dollars.

Option Two is to leave the loan on an interest only basis and salary sacrificed an additional $25,288 a year to super. After deduction of the entry tax of 15%, he would have an additional $21,495 a year going into super. If his fund earned 9% per annum, these contributions would put an extra $135,000 in his fund.

The interest only cost would be $6000 a year in after tax dollars or $9756 in pre-tax dollars.

At the end of the five years, with Option Two, his total contribution in pre-tax dollars would be $175,220 which is a saving of $13,360 over Option One. Furthermore, after withdrawing $100,000 tax free from his super to pay off his loan, he'd have a bonus of $35,000 left over. Obviously the second option is much better than the first.

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.

Solicitors Corner – Life Tenancy

This new section has come into newsflash after discussions with a solicitor. It will include various articles on areas where our professions overlap. We will welcome any contributions from solicitors, please do not hesitate.

TR 2006/14 www.law.ato.gov.au/atolaw/view.htm?DocID=txr/tr200614/nat/ato/00001 is the ATO ruling on life tenancy. It is so difficult to follow and appears to contradict itself that we suggest taxpayers get a ruling from the ATO before relying on it.

Life tenancies are usually created in a will, giving the beneficiary (Life Tenant) the right to live in a property or to receive income from an investment. Once the tenant dies ownership of the asset transfers to the remainderman, another beneficiary of the will. This arrangement is common when a parent remarries, they leave their new spouse a life tenancy in the family home with the deceased's children being the remaindermen.

A problem arises if the life tenant decides they would like to move or give up their rights. This can be seen as a disposal of an asset at market value to the remaindermen, for CGT purposes. The value of the asset would be the rent or in the case of shares the expected dividend multiplied by the life tenants life expectancy. The life tenant could be trapped by in a home that is no longer suited to their needs because they cannot afford the CGT.

SMSF Borrowing

The ATO is warning taxpayers that they are aware that some trustees are signing contracts to buy an investment property for a SMSF before the bare trust (security or holding trust) comes into existence. When a SMSF borrows it cannot use its current assets as security, only the asset being purchased and then only if it is held in a bare trust rather than directly in the name of the SMSF.

There is just too much involved in these arrangements to take the risk that the ATO could unwind the whole transaction. Accordingly, it is important to first obtain a lender before you seriously look to buy a property. Setting up a bare trust off the shelf could be costly. Your eventually lender may not be happy with the deed and will charge you to have their solicitor review it. It is usually cheaper to just go along with whatever bare trust deed your lender recommends, hence the need to choose your lender first.

Expats Watch Out!

The ATO certainly has Australian Residents working overseas in their sights and they are winning a lot of cases lately. Even if you have not lived in Australia for years, if you have a home here they will want to tax your overseas income. If your spouse and children live here while you work overseas you have no chance at all. You will be considered a resident of Australia for tax purposes so the wages you earn overseas will be taxed by Australia, even though they are probably also taxed overseas. The only concession is that the ATO will give you a tax credit for the tax you paid overseas, if you can prove it, but you will not be entitled to a refund of any overseas tax.

The latest case is Pillay v FCT 2013 AATA 447, where Dr Pillay had lived and worked in East Timor since 2006. The AAT found that he still had a continuity of association with Australia because he maintained a house here and had an Australia bank account. This was enough to prove he "resided" here so all the income he had earned while living overseas was taxable in Australia.

Qld Workcover

When you are totalling your wages for your work cover form consider excluding directors wages if you are operating as a company or trust with a company trustee and the directors have income insurance. Directors are not required to be covered in your work cover policy and generally income insurance will provide better cover.
www.workcoverqld.com.au/insurance/cover-provided-by-your-policy/who-is-covered

Individual Tax Rates

There is now little difference between the tax rate of a low income earner and an medium high income earner. The following figures include a 2% Medicare levy, this could vary depending on your particular circumstances.

Once you earn over $18,200 you hit the 21% tax rate until your income reaches $37,000. It is at this point that the low income tax offset starts to shade out so your tax rate jumps to 36%. If you earn under $180,000 the highest rate of tax you will pay is 39%. The 3% difference is $300 for every $10,000.

Such a small difference in tax rates should be considered rather than a blanket approach of directing all the losses to the high income earner and all the income to the low income earner. For example let's say H earns $170,000 a year and L earns $45,000 per year, they are considering buying a rental property that will be negatively geared for 13 years. Starting out with a $10,000 loss in the first year but each year that loss decreases by $1,000 due to reducing depreciation and increasing rents. In the 13th year they sell for a $100,000 taxable gain which becomes $50,000 after the CGT discount. Who's name should they buy in? In the 13 years their incomes may increase with inflation but we will assume that the tax thresholds move at the same rate so their marginal tax rate does not change.

Year	Effect on Taxable Income, of Property	High Income Earner Tax Consequence	Low Income Earner Tax Consequence
1	$10,000 Loss	$3,900 Refund	$3,300 Refund
2	$ 9,000 Loss	$3,510 Refund	$3,090 Refund
3	$ 8,000 Loss	$3,120 Refund	$2,880 Refund
4	$ 7,000 Loss	$2,730 Refund	$2,520 Refund
5	$ 6,000 Loss	$2,340 Refund	$2,160 Refund
6	$ 5,000 Loss	$1,950 Refund	$1,800 Refund
7	$ 4,000 Loss	$1,560 Refund	$1,440 Refund
8	$ 3,000 Loss	$1,170 Refund	$1,080 Refund
9	$ 2,000 Loss	$ 780 Refund	$ 720 Refund
10	$ 1,000 Loss	$ 390 Refund	$ 360 Refund
11	Breakeven		
12	$1,000 Profit	$ 390 Tax Payable	$ 360 Tax Payable
13	$50,000 Taxable Gain	$22,700 Tax Payable	$18,250 Tax Payable
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Net Tax Bill for the 13 years		$14,900	$11,050

L's net tax result over the period is less because at $45,000 a year there was plenty of room to absorb the capital gain at the lower tax rate where as $40,000 of the capital in H's name was taxed at the maximum tax rate of 47%.

Well, you might ask why over a period of 13 years a negatively geared property doesn't actually reduce tax. That is because the capital growth actually exceeded the loss while it was negatively geared. Remember that is the plan when you buy an investment property, its capital growth must recover your losses. The plan is to be retired and in a lower tax bracket when you sell. If both H & L were retired and both in the same tax bracket when the property is sold the CGT can be ignored but even then with, 10 years negative return and only one year positive the tax advantage of holding the property in the high income earners name is only $2,070 ($21,060-$18,990) which will slowly be eroded over the future profitable years, before they retire, if they continue to hold the property.

Of course a crystal ball is the only way you can be sure you are making the right choice but when it comes to spending money to redirect the tax result it may not be worth the effort, the point of this article is just don't assume, do the numbers. Here are a few examples of when it may not be worth working your circumstances to minimise the tax of the high income earner.

1) Paying stamp duty to change the title on a property
2) Setting up a trust so you can choose who receives the income or capital gain
3) Salary sacrificing into super up to the high income earner's cap. Once that is reached consider salary sacrificing from the low income earner's wage too.

4) Suffering the inconvenience of holding the property in one name when a joint tenancy would suite you better ie estate planning

Seminar

How To Claim Your Trip Around Australia As A Tax Deduction – Speaker Julia Hartman
3pm Sunday 25th August, 2013 at Bucasia Caravan Park Mackay www.bucasiabeach.com.au/contact-us-2/
Come and join us by the swimming pool on the water front to talk about all things travelling and working around Australia. A local chef will be providing free samples so bring a beer and enjoy the afternoon even if you are not a travelling worker. If you require any further information ring Julia on 0428381864.

Where is Julia?

In sunny Mackay until around the end of October. I will go to Townsville for a week towards the end of September.

Ask BAN TACS

For $69.95 at Ask BAN TACS, www.bantacs.com.au/ask-bantacs.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.

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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With the **BAN TACS Forum**, www.bantacs.com.au/forum_introduction.php, and the **Ask BAN TACS Notice Board**, www.bantacs.com.au/ask-browse.php, the information is changing all the time.
This fortnight 2 very generous askbantacsers have allowed their question and answer to be placed on the notice board.
www.bantacs.com.au/QandA/index.php?xq=475 Deals with selling your home in another country after you become a resident of Australia for tax purposes
www.bantacs.com.au/QandA/index.php?xq=477 discusses the options available to a couple who wish to build their retirement home long before they will move into it and cover it with their main residence exemption.

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.