NEWSFLASH

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BAN TACS National Accountants Group

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Issue Number: 316 **Pages: 4** **Date: 15th January, 2017**

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

Happy New Year - Update

If the recent increase in sales of our book Winning Property Tax Strategies http://www.bantacs.com.au/shop-2/bookwinning-property-tax-strategies/ is anything to go by there were a lot of New Year resolutions to invest in property. Please make sure you read our pre-purchase booklets before you start looking for a property http://www.bantacs.com.au/booklets/Before_You_Buy_A_Rental_Property.pdf and http://www.bantacs.com.au/booklets/Buying_A_Rental_Property.pdf

We also have a Facebook page with daily property posts https://www.facebook.com/BANTACSpropertypage/ and if all that reading is too much, watch our webinars http://www.bantacs.com.au/media-library/webinars/ If you would like a property related topic discussed in our Facebook forum please email your suggestion to facebook@bantacs.com.au

This edition of newsflash is a bumper issue for property investors! Please make sure you share it with your friends. There is just so much important stuff. In particular the changes to NSW stamp duty and land tax that require your urgent action if you hold a NSW property in a discretionary trust. As always our headings are designed to let you know whether the article is relevant to you. Accordingly, the issues with discretionary trusts and NSW property are broken into 3 articles so you only need to read what could affect you.

We are also excited to announce that we have some new offices coming on board over the next couple of months. If you are an Accounting firm or want to start one up and you are considering joining the BAN TACS group, now is the time to catch the wave of promotions we will be doing to announce our new offices. To find out more about what the BAN TACS group has to offer go to http://www.bantacs.com.au/aboutus/practice-opportunitites/

Our Brisbane office has moved so please make sure you check the address before coming in for your appointment http://www.bantacs.com.au/aboutus/locations/brisbane-office/

Owning A Property In NSW In A Discretionary Trust

If you are considering buying a property in a discretionary trust in NSW, you will need to use a very carefully worded trust deed. The definition of beneficiary in the deed will need to be narrower than is usually the case.

The NSW Office of State Revenue has increased the percentage rate of stamp duty payable on a property purchased in NSW if the purchaser is a foreign resident. The rub is that its new definition of foreign resident, that was only released 5 days before Christmas, **includes any trust that has a foreign resident beneficiary**! The ruling, available at http://www.osr.nsw.gov.au/info/legislation/rulings/general/g009 states at paragraph 23:

> *For a discretionary trust, each beneficiary that the trustee has discretion to distribute the income or property to is deemed to have the maximum percentage interest in the income or property that the trustee may exercise a discretion to distribute to them. This includes all beneficiaries of the discretionary trust, not only beneficiaries who are takers in default. The beneficiaries also do not need to be specifically named by the discretionary trust. If any beneficiary is a foreign person, the trustee of the trust will be deemed to be a foreign person.*

This is likely to catch most current discretionary trusts as non-residents for NSW stamp duty purposes, and applies retrospectively back to 21st June 2016. It is a question of where the property is located, not which state the trust was formed in.

Traditionally, discretionary trust deeds make their list of beneficiaries as wide as possible; you would normally expect all your family members to be included. So, if you have a relative who is not an Australian citizen and is overseas when you use a standard discretionary trust deed to buy a property, you could be up for the extra stamp duty applicable to "foreign residents" on the full purchase price of the property!

Note an **Australian citizen** living overseas is not caught here, but there are many people living in Australia permanently that do not have citizenship, including New Zealanders.

What to do? Preferably set up a new discretionary trust for the purchase. Usually it is better to have a separate trust for each property, for asset protection purposes anyway. Don't use an off-the-shelf trust deed; you need to make sure your new trust deed has a much more limited definition of beneficiary. It is necessary to narrow down the definition of beneficiaries to those that either don't exists ie your children's future spouses or people who are Australian citizens. It is a question of being potentially entitled to the profits of the trust so a clause limiting beneficiaries to Australian citizens as per example 5 in the state revenue office's ruling may work. You have a big problem if you want someone overseas who is not an Australian Citizen to be a beneficiary of the trust.

If you must use an existing discretionary trust then you will need to make a variation to the deed to limit the beneficiaries. The trap here is you could trigger a resettlement of the trust for tax purposes. If the trust already has assets in it and a resettlement is triggered, those assets will be deemed to have been sold for market value at that time. This means Capital Gains Tax will be payable if there has been a capital gain since purchase. You will need to get advice to be sure that changing the beneficiaries will not trigger a resettlement. In TD 2012/21 the simple changing of the beneficiaries didn't
http://law.ato.gov.au/atolaw/view.htm?docid=%22TXD%2FTD201221%2FNAT%2FATO%2F00001%22
Nevertheless, it is far safer to just set up a new trust with a carefully worded beneficiary clause, if at all possible.

Property Development Through Your SMSF

The first problem is that you can't borrow to undertake a development through your SMSF and you can't develop a property that is already security for a loan.

If you have the cash flow to get past that major hurdle then you might be concerned that your development is so business-like, that a SMSF is prohibited from undertaking it. This is an old fashion notion, that SMSFs are not allowed to be involved in a business. It stems from the law that the superannuation fund must act with the sole purpose of providing for your retirement or your family in the event of your death.

SMSFs are certainly allowed to operate a business reference QC 42474 but you need to be careful that the operation of that business does not breach any of the other rules relating to SMSFs such as borrowing restrictions. For more information go to https://www.ato.gov.au/Super/Self-managed-super-funds/Investing/Carrying-on-a-business-in-an-SMSF/

Land Tax NSW Now Higher For Most Discretionary Trusts

In NSW, residential property owned by foreign residents is subject to a higher rate of land tax and there is no threshold value below which land tax is not applicable. Just before Christmas the definition of foreign resident in NSW was changed. For the 2017 land tax year most discretionary trusts will be caught as foreign residents because they normally have a very wide definition of beneficiary. If just one beneficiary is not a resident of Australia then the whole trust is treated as a foreign resident. The foreign beneficiary does not have to be specifically named. It can be implied by reference to family groupings ie a cousin that is not resident of Australia. **Note:** all Australian citizens will be considered residents of Australia, even if they are living overseas.

If you have a discretionary trust that owns property in NSW, it is time to talk to your solicitor about changing the deed to limiting its possible beneficiaries.

Make sure the solicitor is aware of TD 2012/21, who ensures that the changes do not result in a resettlement of the trust. If a resettlement is triggered, the trust is deemed to have sold all its assets at market value, so you will be up for CGT on all the growth to date with no sale proceeds to pay the tax. The solicitor should read this ruling from the NSW start revenue office http://www.osr.nsw.gov.au/info/legislation/rulings/general/g009 and consider a clause like example 5, where the trustee is prohibited from distributing income or assets to a foreign resident.

Can You Claim Interest On A Loan To Pay Tax?

The short answer is **No**; you can't claim the interest on a loan to pay your personal income tax. Reference ID 2002/607.

Section 25-5 (1) (c) of ITAA 1997 says you can claim a tax deduction for shortfall interest and general interest charged by the ATO. Shortfall interest is currently 4.76% pa and applies when you or the ATO amend a tax return to increase your tax liability.

If you don't pay your tax on time then the general interest charge applies which is currently 8.76% pa. If you can borrow at housing loan interest rates, you are still probably better of going without the tax deduction and borrowing to pay the debt.

Note this is all about personal income tax not company tax where there could be an argument that the borrowings are part of the business cashflow.

Owning NSW Property When Not an Australian Citizen

As discussed above, the NSW Office of State Revenue has introduced a foreign resident surcharge, effectively an additional rate of stamp duty or land tax for "foreign residents" who own or are buying residential property in NSW. Australian citizens even if living overseas are not considered "foreign residents" under any circumstances. We have plenty of people in Australia who were born overseas that have not taken citizenship yet have lived here most of their lives. New Zealanders in particular used to travel to and from Australia without the need for a visa.

You are not considered a "foreign resident" for NSW stamp duty and land tax purposes if you are "ordinarily a resident of Australia", but if you do not have Australian citizenship there are a few hoops you have to jump through first. The first rule to be "ordinarily a resident" is that you must have a right to live in Australia that is not subject to any time limitations. This means that people here on a spouse visa, work visa, temporary entry visa, visitor visa, bridging visa or business visa will be treated as "foreign residents" for the purposes of NSW stamp duty and land tax. For example, temporary residents on a 457 visa get many concessions including the main residence exemption for capital gains tax purposes but will still be caught out for land tax on that home if it is in NSW because "foreign residents" are not entitled to the main residence exemption for NSW land tax purposes.

"Foreign residents" are not allowed the main residents exemption from land tax and are not given a threshold where they are only taxed on property above that value. This means if you are the Australian member of a couple and your spouse is here on a spouse visa, if you buy a home in NSW it should only be in your name. If you already have a home together in NSW expect a land tax bill until your spouse gets permanent residency.

Now if you pass the first test in that you have a visa that allows you to stay in Australia as long as you like, or you are legally here for an unlimited period but came before visas were necessary, the catch is you are still not an Australian citizen. This means that you need to actually be in Australia to qualify as "ordinarily residing". The requirement is that you must be in Australia for at least 200 days in the 12 months before you are due to pay the stamp duty or land tax bill.

The next problem is, even if you can skirt around not being caught as a "foreign resident" yourself, is using a discretionary trust to buy property in NSW. If you or your parents were not born in Australia there is a very good chance that you have family members who are "foreign residents". If a discretionary trust buys residential property in NSW and it has a beneficiary that is a "foreign resident" then the trust is deemed to be a "foreign resident" and all of its NSW property is subject to the extra tax. The beneficiary doesn't even have to be named just implied. Most discretionary trust deeds have a wide definition of beneficiary. So you might have been born in Australia but your parents were born overseas yet lived in Australia all your life. If they have not taken up citizenship and they travel overseas for more than 5 months then if your trust deed has a beneficiary clause along the lines of you, your spouse, your children, your parents etc the trust will be considered 100% a "foreign resident".

The problem with discretionary trusts can be avoided by putting a clause in the deed that prohibits the distribution of income or assets to beneficiaries who are foreign residents for NSW stamp duty and land tax purposes. This means you need to see a solicitor about changing your deed or if you are setting up a new trust you need to make sure the deed is up with the latest as this problem only arose on 20th December, 2016 so don't expect any of the off-the-shelf deeds to have anything on this yet.

Ideally your discretionary trust deed should have a clause like example 5 in the NSW State Revenue office's ruling http://www.osr.nsw.gov.au/info/legislation/rulings/general/g009

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For daily property information and a bit of fun like us on https://www.facebook.com/BANTACSpropertypage/

Askbantacs Free Notice Board

For $79.95 at Ask BAN TACS you can have your questions regarding Capital Gains Tax, Rental Properties and Work Related Expenses answered by Julia. They will include ATO references to support the conclusion, answers are generally 300 to 700 words long depending on the complexity.

First check the Notice Board. Your question may have already been answered at someone else's expense.

How to Make Sure Your Next Property Is a Good Investment

- Do you really know how much the property is going to cost you to hold?
- What name should the property be purchased in?
- Will this property fit your investment strategy and goals?
- What does the contract say about GST?
- How does the price compare with similar sales in the area?
- If it is negatively geared, how much capital growth is required before you breakeven?
- Do you know what records you need to keep and how?
- Are your financing arrangements maximising your tax deductions?
- What happens if interest rates rise?

......and the list goes on!

To ensure you don't make a costly mistake with your next purchase, contact us http://bantacs.com.au/Bantacs_pipkit.php

Note: If you are an experienced property investor we understand you might not need all of these services; please feel free to discuss exactly what you need with your local BAN TACS Accountant