



ADA GROUP NEWS

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Welcome

In our second newsletter we cover a couple of important areas relating to the Tax Office's compliance program, electing annual GST reporting and a recent decision by the Administrative Appeals Tribunal about Personal Service Business.

We also feature our first client profile, Vuletic Hairdressing and provide some further information on the training organisation MEGT.

Finally, thank you for the positive feedback about this newsletter which will now be published quarterly. We welcome any feedback or suggestions.

Debt/equity exemption extended

The Government recently introduced a "debt/ equity" regime, which basically sets out rules to determine whether money injected into a private company (e.g. by a shareholder) should be treated as a loan or as share capital.

These rules, among other things, affect the treatment of repayments relating to such money (so that interest on a "loan", for example, may instead be treated as a payment of a nondeductible dividend, rather than deductible interest).

Due to concerns about compliance costs, the Government had previously announced:

- a transitional arrangement, exempting "at-call" loans to private companies from the rules until 30 June 2005; and
- an exemption from the debt/equity rules for some smaller private companies.

This exemption will now be extended, so that the new rules won't apply to companies with an annual turnover of less than **\$20 million** (as opposed to the previous carve-out, which basically applied to companies with CGT assets with a net value of \$5 million or less).

This means that companies satisfying the carve-out can effectively ignore the debt/equity rules.

Other amendments will also be introduced to reduce compliance costs associated with the debt/equity provisions.

The amendments take effect from 1 July 2005.

ATO's Compliance program

The Tax Office will be visiting 11,000 businesses unannounced to check their identification and registration details. Targets for this special treatment are generally:

- the property, building and construction industries;
- restaurants, cafes and takeaway food outlets;
- the motor vehicle wholesaling and retailing industry;
- licensed hotels and registered clubs;
- the adult industry;
- bartering;
- horse racing;
- fishing; and
- tourism.

Industry norms – an example of how the ATO puts them to use

As part of its ongoing audit programs, the Tax Office has advised that they use a range of industry norms and ratios that they collect from all activity statements for particular industries. This gives them their 'normal' boundaries for different industry groups.

For example, they calculate:

- average 'expenses as a percentage of total sales'; and
- 'wages as a percentage of total sales'

and identify businesses that are operating outside these norms or ratios.

How they try and target cash avoiders

They also use industry information to determine if the level of income being reported is reasonable. For example, industry information indicates that an average of 110 cups of coffee can be made from a kilogram of coffee beans.

This can be used with other information obtained from a cafe to calculate income from coffee sales compared to total income declared. Similar approaches may be used in other industries.

They say they realise that not all businesses outside the industry norm are doing the wrong thing and (they say) they take the individual circumstances of each business into account.

Benchmark interest rate for Div 7A

The benchmark interest rate for an entity with an income year commencing 1 July 2005 is 7.30% p.a. for:

- private company loans made (or deemed to have been made) after 3 December 1997 and before 1 July 2005; and
- trustee loans made after 11 December 2002 and before 1 July 2005.

This rate is used to:

- determine if a loan made in the 2004/05 income year is deemed to be a dividend; and
- calculate the amount of the minimum yearly repayment for the 2005/06 income year on an amalgamated loan taken to have been made prior to 1 July 2005.

GST on long-term non-reviewable contracts

Long-term non-reviewable contracts that were GST-free during the initial transitional period cease to be GST-free after 30 June 2005.

From 1 July 2005, there are three ways to account for GST on a long-term non-reviewable contract:

- the supplier pays the GST on a revised contract price, as agreed with the recipient;
- the supplier pays the GST on the existing contract price; or
- the recipient (even if not registered for the GST) pays the Tax Office the GST on the existing contract price.

Suppliers or registered recipients liable to pay the GST will account for it on their usual activity statements. Unregistered recipients will be subject to the same reporting and payment obligations as GST registered recipients.

Editor: Please contact this office if you think you may be affected by these changes.

Electing annual GST reporting

Taxpayers may be eligible to elect to report and pay (or claim) GST annually if:

- they are not **required** to be registered for GST (i.e., their turnover is below the relevant threshold and they are registered voluntarily);
- they have not elected to pay GST by instalment amounts; and
- they have not previously been offered the annual reporting option.

In addition, taxpayers who have reported nil amounts for GST on activity statements they have lodged may wish to consider canceling their GST registration or may choose to elect annual GST reporting.

If you think you may be eligible to report and pay GST annually, and would like to take advantage of this option, contact this office.

Car depreciation limit for 2005/06

The car limit for the 2005/06 financial year is \$57,009 (which is the same as that which applied in the 2004/05 financial year). The car limit of \$57,009 is used to calculate Car depreciation limit for 2005/06

Note that this amount is also used to determine the luxury car tax threshold, at which point luxury car tax becomes payable.

Company not involved in a contract, so not a Personal Service Business

The following case serves as a warning to make sure that your documentation is always in order – especially the names of the actual parties to a contract.

The AAT has upheld a decision by the Commissioner of Taxation to refuse to consider a company to be a Personal Services Business (PSB), because the main service contract was with the director of the company (as an individual) and not with the service company.

Other individual letters of engagement, although addressed to the company, were offered under, and referred back to, the general terms of the main contract.

The Tribunal found that the contract was in fact between the director and the client (and not between the company and the client) and that the director derived the relevant income.

Therefore, since it was the director that carried on the relevant business and not the company, the Commissioner was not in a position to be able to issue a PSB Determination.

However, the AAT also found that, even if the company had been involved in the contract, it was still not carrying on a PSB, as it did not meet any of the relevant tests.

Planning opportunity: joint low interest loans

The Tax Office has recently confirmed the existence of a planning opportunity for couples who own rental properties jointly, especially where one member of the couple has a much higher income than the other member.

A recent Interpretative Decision states that, where an employer provides a low interest loan jointly to an employee and their spouse, and the loan is used to jointly acquire an income producing property, the loan is not subject to any fringe benefits tax (FBT) due to the application of the 'otherwise deductible rule'.

This is because the loan is deemed to be provided to the employee alone and since the interest payments on the loan would be 'otherwise deductible' to the employee, no FBT is payable on the loan.

This means that the employee and the spouse can share the income of the property jointly, but the employee can effectively claim all of the deductions.

The implications of this ID should not just be limited to where the employee obtains the loan from the employer, but also where an employee salary packages a loan obtained from a third party lender. Please contact this office if you would like to discuss how you can utilise this planning opportunity.

Training and Recruitment

MEGT started in the eastern region of Melbourne as a Group Training provider, working with host businesses requiring apprentices and trainees. We have now been operating in the training and employment arena for over 20 years. MEGT now has 32 offices located in most states of Australia.

MEGT understand that employers need and want choices in training and employing staff to support the changing needs of their particular industry.

MEGT's Divisions include; • Registered Training Organisation • Group Training • New Apprenticeships Centre • Employment Services

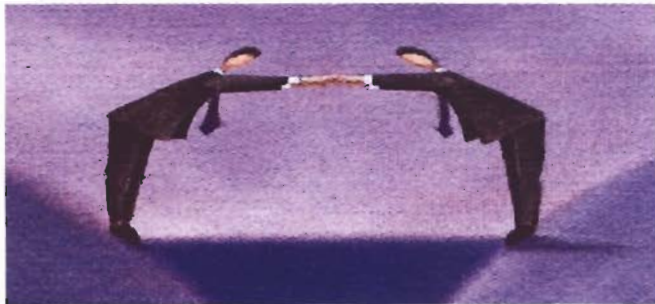
MEGT

- provides more employment and training options to suit different employers' needs
- has more local offices with local area knowledge and personal support
- provides better support with industry specific staff
- has more technological facilities and infrastructure to provide you with faster access to critical information

That's why MEGT is big enough to support you, yet small enough to know you.

Whatever your interest, from business to carpentry or warehousing, MEGT can help.

For all enquiries on how we can assist you, please call Rhonda Ryan on 9871-5524



Client Profile

VULETIC HAIRDRESSING

Pamela Vuletic of Vuletic hairdressing is a young businesswoman who loves a challenge. After years of working for someone else, she decided to make the leap and open up her own hairdressing business in the shopping strip of Toorak Road, South Yarra, where she is competing against over one hundred hairdressing salons.

Pamela is enjoying the challenge of building up her business which she has done by offering great service along with a competitive price strategy. She is also finding that as she becomes well known in the area, she is building up her regular client base and getting referrals.

For quality service contact Pamela at:

**Vuletic Hairdressing
Shop 7, 177 Toorak Rd. South Yarra
ph:9827 7717**

"LowDoc" loans targeted

The Tax Office commenced a project last year that investigated people using low documentation (LowDoc) loans on the basis that many people using these products may have either understated their income or failed to lodge income tax returns.

This year the Tax Office will systematically:

- check the lodgment status of people obtaining LowDoc loans;
- review the income disclosed in the returns lodged by people obtaining LowDoc loans; and
- match the information provided to insurance companies where the LowDoc loans require mortgage insurance.

The Tax Office will also continue to concentrate on identifying high-risk brokers so that it can review whether they and their clients are complying with their tax obligations.

No deduction for fees paid to a psychologist

The AAT has held that fees paid to a psychologist by a nurse who worked in an extremely stressful work environment were not deductible because treatment for physical or mental health is inherently private in nature (even though it helped him progress in his career).

Furthermore, the fees were not rebatable medical expenses as the psychologist was not a legally qualified medical practitioner.

Unfortunately for the taxpayer, the Tribunal made the point that all that may have been required for him to receive the rebate was to arrange for his general practitioner to formally refer him for psychotherapy

Small donations to Tsunami appeal 'bucket collections'

Ordinarily, an individual who makes a monetary gift or donation of \$2 or more to a deductible gift recipient is allowed a deduction for the amount of the donation provided they can produce supporting documentary evidence, such as a receipt.

However, many people made donations of spare change to "bucket collections" for the Boxing Day 2004 Tsunami disaster and would not have obtained receipts.

Recognising this, the ATO will allow taxpayers to claim a deduction of up to \$10 where they made one or more small cash donations (each of \$2 or more) to "bucket collections" conducted by deductible gift recipients collecting for the Tsunami appeals, even though they have not obtained receipts or other evidence.