

## Practice Update

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and contact this office  
if you have any queries

JANUARY/FEBRUARY 2008

### Election 2007 wrap-up

For the first time in 11 years, we've had an election that has resulted in a change of Government at the Federal level.

The calling of the election meant that all legislation that had not passed both Houses of Parliament at that time lapsed, and will have to be introduced again (if the new Government wants to).

Having a new Government means we can expect new policies, although it appears that the Labor Government intends to continue the previous Government's gradual reduction of tax rates (and increases in the thresholds).

Parliament is not due to sit until 12 February 2008, so we will keep you updated on any developments.

### Mum and Dad investors getting unfairly hit with GST!

*Editor: The GST law is basically designed so that the supplier (i.e., the person selling the goods or services) is required to calculate the GST and send it off to the ATO; in most cases, the purchaser doesn't have any direct GST liability.*

*However, in some circumstances, a purchaser who is registered for GST may have an "increasing adjustment" (which basically hits them with a GST bill) if they acquire something GST-free, but then don't use it in the specified way.*

*This little-known part of the GST law is affecting many Mum and Dad investors in coastal units and apartments.*

### How property investors are unfairly caught

The ATO says that it is starting to see an increasing number of instances similar to the following:

- a developer builds a high rise holiday complex at a popular coastal holiday destination;
- they then rent out the units to the public under a lease arrangement; and then
- sell the units to individual 'Mum and Dad' type investors who will also lease out their "new" apartment.

Now, the tax problem starts because both the developer and investor are leasing the property, so it can initially be transferred GST-free under something called the "going concern" provision.

This is all legitimate from the developer's point of view, and may sound good to "Mum and Dad".

### The GST consequences down the track

The real problem though is that when Mum and Dad continue to rent out the property, they won't be charging GST to the tenants because the premises are residential.

As they are more or less removed from the GST system, the Act says that **they** will basically have to pay 10% GST on the purchase price to the ATO. This is called an "increasing adjustment".

### The ATO's approach

The Tax Office has recently seen instances where vendors are requiring purchasers to register for GST prior to settlement, on the pretext that if they

are registered they won't have to pay the GST on the new residential premises.

What, of course, isn't disclosed is the increasing adjustment.

The vendor is in the clear, so the ATO has no choice but to pursue the purchaser.

According to the ATO, it's a "classic case of buyer beware", and they recommend that all parties to a contract should seek independent legal advice to protect their interests before signing it.

*Editor: There are many traps in buying property (and other assets) and this serves as a timely reminder for our clients to contact us to discuss any possible tax consequences **before** entering into any contract.*

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### **SMSFs and compliance in 2008**

The ATO has advised that this year's self-managed superannuation fund (SMSF) compliance program will largely focus on risks but is also designed to help SMSFs to prepare for the future.

It will be expanded to cover 2.9% of the total number of SMSFs; effectively an additional 6,600 audits and reviews above last year.

#### **Loans**

The ATO has already completed a number of cases in the loans area, which were selected on the basis that 80% or more of fund assets had been lent out to other parties.

In just over 200 cases completed to date, the majority (74%) were loans made to unrelated third parties over an established loan term and with a written loan agreement in place.

However, the ATO will be taking a closer look at cases where loans are unsecured, or where repayments are not being made, or where loans are not conducted at arm's length.

#### **Other compliance issues**

The ATO will also be looking at transfers of assets into SMSFs, particularly where CGT may have been avoided, and other breaches of the SMSF investment rules.

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### **SMSFs and instalment warrants**

*Editor: The investment laws were recently changed to allow SMSFs to borrow to invest in instalment warrants and similar products (before this change, because instalment warrants involve a borrowing,*

*SMSFs could not technically invest in them without breaching the law).*

*Note(\*): An instalment warrant is basically an agreement that enables someone to purchase an asset over time.*

*The ATO has set out how it will treat investments in these products before the measure became law.*

The ATO recognises that SMSFs may have invested in instalment warrants prior to the law being changed, and has advised that:

- If an SMSF invested in an instalment warrant before 24 September 2007, which is allowed by the new law, the ATO will not make the fund a non-complying fund solely on the basis of this investment.
- However, if such an investment **breaches** the new law, the ATO will decide on a case-by-case basis what the fund must do to become compliant.

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### **Commissioner agrees: No FBT on repayment of a loan**

In a strange turn of events, the ATO has admitted that it was wrong in an important FBT appeal case, just before the appeal was heard by the Full Federal Court.

The ATO agreed with the taxpayer (and the Court also confirmed) that, when a taxpayer company repaid loans to its shareholders (who were also employees) by paying certain private expenses on their behalf, it was not liable to FBT.

However, the case does highlight the importance of having such loans (and their terms, such as allowing the company to pay for the lender's private expenses) in writing.

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### **Beware of another tax refund email scam**

The Tax Office is again warning people about a fraudulent email being circulated that claims to offer a refund from the Tax Office.

The email asks people to click on a link which redirects them to a bogus website that looks similar to the Tax Office website and asks for credit card and personal details.

If people have done this, they should contact their credit card provider as soon as possible and report a possible compromise.

<p>Please Note: Many of the comments in this publication are general in nature and anyone intending to apply the information to practical circumstances should seek professional advice to independently verify their interpretation and the information's applicability to their particular circumstances.</p>
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