Lusi & Company
Corporate Accountants & Business Advisers

Client Information Newsletter
- Tax & Super

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Three-quarter FBT year compliance check-up

As the FBT year runs from 1 April to 31 March, the months of October to December mark the "third quarter" of the FBT year, and so, as an early fix before year's end, here is an overview of the FBT elements that can attract the ATO's attention.

This can be a timely period for a compliance check-up, so that employers who provide fringe benefits to staff can have better assurance they are not going to be tapped on the shoulder. This may still leave time for a fix-up (if possible) before the FBT year winds up, but certainly might help steer you clear of obstacles for the next FBT year.

FBT topics that can benefit from a clean-up include (but are not limited to) issues with living away from home allowances, car parking fringe benefits, employer-provided vehicles, employee contributions, employer rebates and of course the non-lodgement of FBT returns.

continued ⇨

About this newsletter

Welcome to our monthly newsletter. Should you require professional advice on any matters contained in this newsletter, our team of Accountants are here to assist.

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Three-quarter FBT year compliance check-up *continued*

Living-away-from-home allowance (LAFHA)

LAFHA is an allowance an employer pays to employees to compensate for additional expenses incurred and any disadvantages suffered because the employee's duties of employment require them to live away from their normal residence.

The taxable value of the LAFHA benefit may be reduced by the exempt accommodation and food components of the allowance (ask us for these).

Errors that will attract the ATO's attention include:

- claiming reductions for ineligible employees
- failing to obtain required declarations from employees
- claiming a reduction in the taxable value of the LAFHA benefit for exempt accommodation and food components in invalid circumstances
- failing to substantiate expenses relating to accommodation and, where required, food or drink.

Car parking valuations

The ATO will focus on the validity of valuations provided in relation to car parking fringe benefits. The common errors that attract its attention include:

- market valuations that are significantly less than the fees charged for parking within a one kilometre radius of the premises on which the car is parked
- the use of rates paid where the parking facility is not readily identifiable as a commercial parking station
- rates charged for monthly parking on properties purchased for future development that do not have any car park infrastructure
- insufficient evidence to support the rates used as the lowest fee charged for all day parking by a commercial parking station.

Provided motor vehicles

Another area of focus will be on situations where an employer-provided motor vehicle is used, or available, for private travel of employees. The ATO says this constitutes a fringe benefit and needs to be declared on the FBT return. The ATO says there has been demonstrated inconsistency in the application of exemptions, leading to additional compliance costs, especially where private travel is relatively low.

A change has been made to the rules that will apply from the 2019 FBT year onwards. "Private use" will be defined as any diversion in travel that "adds no more than two kilometres to the ordinary length of that trip". Also that "for journeys undertaken for a wholly private purpose (other than travel between home and place of work), the employee does not use the vehicle to travel more than 1,000 kilometres in total, and a return journey that exceeds 200 kilometres".

Employee contributions

A red flag is also raised in situations where no employee contributions have been paid (which reduces the FBT liability for the employer) yet there are significant motor vehicle expenses included in the entity's income tax return, and no vehicle expenses accounted for in an FBT return (or no FBT return lodged).

The ATO is also keen to ensure that the employer does not:

- fail to report these contributions as income on their income tax return
- incorrectly overstate employee contributions on their fringe benefits tax return to reduce the taxable value of benefits provided.

Employer rebates

Another hot spot for the ATO is whether a fringe benefits tax rebate can be claimed. A taxpayer must be a rebatable employer to claim a fringe benefits tax rebate, but the ATO has found that some ineligible employers incorrectly claim this rebate.

Non-lodgement, no declarations

Of course non-lodgement of fringe benefits tax returns is of concern to the ATO. Employers that provide fringe benefits must lodge an FBT return unless the taxable value of all benefits has been reduced to nil.

Common errors that attract ATO attention include:

- failure to identify fringe benefits provided
- incorrect calculation of benefit values or reduction amounts
- lack of declarations for expense payment benefits such as telephone, internet connection or power, or recurring declarations for same. ■

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How much do we need to retire?

The question of how much a person needs to have saved before confidently launching into their retirement years very much requires an individual answer. Each one of us lucky enough to reach the brink of those golden years will feel a lot better doing so with some assurance that we've squirrelled enough away to be comfortable in retirement.

The answer to the above question is made all the more complicated by several unknown factors, as no-one knows, for example, how long they will live or what medical necessities could surface to strain the coffers.

Some guidance is available however from Super Guru, a website run by the non-profit Association of Superannuation Funds of Australia (ASFA). Super Guru releases a "retirement standard" every quarter. This is a benchmark for the annual budget needed by Australian individuals and couples to fund either a "comfortable" or "modest" standard of living in their post-work years.

The updated quarterly figures reflect inflation and provide an objective outline of the budgets that singles and couples would need to spend to support their chosen lifestyle.

Super Guru's release of figures up to 30 June 2018 shows that the super accumulation balances needed for a "comfortable" retirement are $545,000 for singles and $640,000 for couples. In annual pension payout terms, this equals $42,953 and $60,604 respectively. Details of what these amounts mean for spending capacity are shown in the table on the following page.

By way of comparison, note that the government Age Pension base rate (before payment of supplements) is $21,222 for singles and $31,995 for a couple. "The Age Pension is designed to provide a 'safety net' for those who do not have enough superannuation or other financial resources to provide an adequate retirement income. So the Age Pension works in conjunction with superannuation," Super Guru says. "Most people – women in particular – will continue to be eligible for a full or part Age Pension, supplemented by whatever superannuation benefits they receive."

ASFA notes that as people age, their spending requirements also change. It estimates the net impact of the various factors at play mean that by age 85 annual budgets would reduce by around $1,000 a year for "modest" lifestyles, and $5,000 a year for "comfortable" lifestyles.

As far as measuring what these different lifestyles entails, Super Guru has produced the following comparison table (and includes a retiree taking the Age Pension only — see overleaf).

continued overleaf ⇨

How much do we need to retire? *continued*

ASFA's estimate for retirement savings

	Comfortable lifestyle	Modest lifestyle	Age pension
Single	$42,953 a year	$27,425 a year	$21,222 a year
Couple	$60,604 a year	$39,442 a year	$31,995 a year
	Replace kitchen and bathroom over 20 years	No budget for home improvements. Can do repairs but can't replace kitchen or bathroom	No budget to fix home problems like a leaky roof
	Better quality and larger number of household items and appliances and higher cost hairdressing	Limited number of household items and appliances and budget haircuts	Less frequent hair cuts or getting a friend to cut your hair
	Can run air conditioning	Need to watch utility costs	Less heating in winter
r	Restaurant dining, good range & quality of food	Take out and occasional cheap restaurants	Only club special meals or inexpensive takeaway
w	Fast internet connection, big data allowance and large talk and text allowance	Limited talk and text, modest internet data allowance	Very basic phone and internet package
G	Good clothes	Reasonable clothes	Basic clothes
t	Domestic and occasional overseas holidays	One holiday in Australia or a few short breaks	Even shorter breaks or day trips in your own city
	Top level private health insurance	Basic private health insurance, limited gap payments	No private health insurance
	Owning a reasonable car	Owning a cheaper more basic car	No car or if you have a car it will be a struggle to afford repairs
	Take part in a range of regular leisure activities	One leisure activity infrequently, some trips to the cinema or the like	Only taking part in no cost or very low cost leisure activities. Rare trips to the cinema

The work Christmas party

It's not quite Christmas time yet, but most businesses will be in the process of thinking ahead to the yuletide festivities, if not already into well-advanced planning. One of the perennial questions is if and how fringe benefits tax applies to these activities.

There is no separate fringe benefits tax (FBT) category for Christmas parties and you may encounter many different circumstances when providing these events to your staff. Fringe benefits provided by you, an associate, or under an arrangement with a third party to any current employees, past and future employees and their associates (spouses and children), may attract FBT.

While such social functions may result in FBT, income tax and GST outcomes, these are covered under the existing relevant legislation. The provision of "entertainment" at Christmas therefore mirrors the tax treatment such benefits will receive at other times of the year.

The cost of providing a Christmas party is income tax deductible only to the extent that it is subject to FBT. Therefore, any costs that are exempt from FBT — that is, exempt minor benefits and exempt property benefits (more below) — cannot be claimed as an income tax deduction. Note that the costs of entertaining clients are not subject to FBT and provide no income tax deductions nor GST credits.

There is what is known as a property benefit exemption where costs (such as food and drink) associated with Christmas parties are exempt from FBT if they are provided on a working day on your business premises and consumed by employees. The property benefit exemption is only available for employees, not associates.

There is also the minor benefits exemption. Broadly, a minor benefit is one where it:

- has a notional taxable value of less than $300 (inclusive of GST)
- is provided on an "infrequent" or "irregular" basis, and
- is not a reward for services.

Note that other benefits (such as gifts) provided at a Christmas party may be considered as separate minor benefits in addition to meals provided (referred to as an "associated benefit"). In such cases, the $300 threshold generally applies separately to each benefit provided.

Entertainment benefits

Say for example a company holds a Christmas lunch on its business premises on a working day. Employees, their partners and clients attend. Food and drink is provided at the party and the company provides taxi travel home from the party. The cost per head is $125.

Providing a party for employees, associates and clients is entertainment, because the purpose of the function is for people attending to enjoy themselves. There can be exemptions for this, but these may vary according to the recipient.

Employees: Does an exemption apply?

- Food and drink: The food or drink provided to employees is exempt from FBT because it is provided and consumed on a working day on the business premises.
- Taxi travel: The taxi travel is exempt from FBT because there is a specific FBT exemption for taxi travel provided to an employee directly to or from the workplace.

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The work Christmas party *continued*

Associates/clients: Does an exemption apply?

- Food, drink and taxi travel: The food, drink and taxi travel provided to the employees' partners (associates) is exempt from FBT because of the minor benefits exemption.
- Clients food drink and taxi travel: There is no FBT on benefits provided to clients

Note that the employer could not claim an income tax deduction or GST credits for the food, drink or taxi travel provided for employees, associates or clients (although there is some scope using the "50/50 split method" — ask us about this possibility).

For taxi travel to or from a Christmas function, employers should be mindful that:

- where the employer pays for an employee's taxi travel home from the Christmas party and the party is held on the business premises, no FBT will apply.
- where the party is held off premises and the employer pays for a taxi to the venue and then also pays for the employee to take a taxi home, only the first trip will be FBT exempt. The second trip may be exempt under the minor benefits exemption if the employer has adopted to value its meal entertainment on an actual basis.
- the exemption does not apply to taxi travel provided to "associates" of employees (for example family members).

If other forms of transportation are provided to or from the venue, such as bus travel, then such costs will form part of the total entertainment expenditure and be subject to FBT. A minor benefit exemption for this benefit may be available if the threshold is not breached.

What's under the tree?

Gifts provided to employees or their associates will typically constitute a property fringe benefit and therefore are subject to FBT unless the minor benefit exemption applies. Gifts, and indeed all benefits associated with the Christmas function, should be considered separately to the Christmas party in light of the minor benefits exemption.

For example, the cost of gifts such as bottles of wine and hampers given at the function should be looked at separately to determine if the minor benefits exemption applies to these benefits. Gifts provided to clients are outside of the FBT rules (but may be deductible, see below — also note that deductibility may still apply even if the gift is a "minor benefit").

The income tax deductibility and entitlement to input tax credits (ITC) for the cost of the gifts depends on whether they are considered to be "entertainment". For example, an unopened bottle of spirits is deemed to be a property benefit (the entertainment starts after the cap is unscrewed). Again, in most cases the entitlement to an ITC for expenses incurred for the employer mirrors the income tax implications — so an ITC is only available to the extent that the expense incurred is deductible.

Regarding a business providing a gift a client, even a former client, the ATO confirms that such outgoings are generally deductible as they are being made for the purposes of producing future assessable income. However, the outgoing is not deductible where it is of a capital nature, relates to the gaining of exempt or non-assessable non-exempt income, or some other provision of the income tax law prevents it from being deductible. ■

i Note that an employer cannot claim an income tax deduction or GST credits for the food, drink or taxi travel provided for employees, associates or clients.

Renting out part or all of your home

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If you rent out part or all of your home, the rent money you receive is generally regarded as assessable income. This means:

- you must declare your rental income in your income tax return, and you can claim deductions for the associated expenses
- you may not be entitled to the full main residence exemption from capital gains tax (CGT), which means you'll have to pay CGT on part of any capital gain made when you sell your home.

Goods and services tax (GST) doesn't apply to residential rents, so you're not liable for GST on the rent you charge, but also you can't claim GST credits for associated costs.

INCOME AND EXPENSES

If you rent out part or all of your home at normal commercial rates, the tax treatment of income and expenses is the same as for any residential rental property. This means you must include the rental income in your income tax return, and you can claim income tax deductions for associated expenses, such as the interest on your home loan.

If you are only renting part of your home, for example a single room, you can only claim expenses related to renting out that part of the house. This means you cannot claim the total amount of the expenses – you need to apportion the expenses.

As a general guide, you should apportion expenses on a floor-area basis based on the area solely occupied by the renter (user), and add that to a reasonable amount based on their access to common areas.

You can only claim expenses for when the room was rented. If you use the room in any capacity, for example for storage or as an office when you do not have guests staying, then the ATO will generally not allow deductions for expenses when the room is not occupied.

If you rent out part or all of your home at less than normal commercial rates – mates rates for example, or to a relative – this may limit the deductions you can claim.

Note that payments from a family member for board or lodging are considered to be domestic arrangements and are not rental income. In these situations, you also can't claim income tax deductions.

CAPITAL GAINS TAX

Generally, you don't pay CGT if you sell the home you live in (under the main residence exemption).

However, if you've used any part of your home to produce income – for example, by renting out part or all of it – you're generally not entitled to the full exemption.

To work out the capital gain that is not exempt, you need to take into account a number of factors, including but not limited to:

- proportion of the floor area that is set aside to produce income
- period you use it for this purpose
- whether you're eligible for what the ATO calls the "absence" rule (ask us about this).

You can ask for our help to work out the proportion of your capital gain that is exempt from capital gains tax. ■

Carrying on a business through your SMSF

Under the regulations, self-managed super funds (SMSFs) are not prohibited from carrying on a business, however the business must be:

- allowed under the SMSF's trust deed, and
- operated for the sole purpose of providing retirement benefits for fund members.

Note however that the rules governing SMSFs prohibit or limit some activities available to other businesses, such as entering into credit arrangements or having overdrafts.

If the trustee of an SMSF carries on a business, generally the ATO will examine the activities closely to ensure the "sole purpose test" is not breached. Broadly, what this means is that your fund needs to be maintained for the sole purpose of providing retirement benefits to your members, or to their dependants if a member dies before retirement.

Cases that attract the ATO's attention include those where:

- the trustee employs a family member (the ATO will look at things such as the stated rationale for employing the family member and the salary or wages paid)
- the "business" is an activity commonly carried out as a hobby or pastime
- the business carried on by the fund has links to associated trading entities
- there are indications the fund's business assets are available for the private use and benefit of the trustee or related parties.

OTHER REGULATORY PROVISIONS

As the fund's trustee, you will need to ensure that a business conducted through your SMSF complies with investment rules and restrictions applying to SMSFs.

Your investment strategy – the nature of the business activities and the way they are conducted must be in accordance with the SMSF's investment strategy.

Restrictions on investments – all investments by your SMSF must be made on a commercial "arm's length" basis. If you don't comply with the investment restrictions, penalties could apply.

Loans and financial assistance – the business activities must not involve:

- selling an SMSF asset for less than its market value to a member or relative of a member
- purchasing an asset for greater than its market value from a member or relative of a member
- acquiring services in excess of what the SMSF requires from a member or relative of a member
- paying an inflated price for services acquired from a member or relative of a member.

Acquiring assets from related parties – purchasing assets (such as plant and equipment) for use *in business* activities from a member or other related party could contravene the related party acquisition rules. These dictate that your fund can't acquire an asset from a related party unless it is acquired at market value and is:

- a listed security (for example, shares, units or bonds listed on an approved stock exchange)
- business real property
- an "in-house asset" (loan or investment in a related party, or asset leased to same), provided the market value of your fund's in-house assets does not exceed 5% of the total market value of your fund's assets
- an asset specifically excluded from being an in-house asset.

Borrowing – drawing on a bank overdraft or margin lending account to fund the business activities could contravene the borrowing restrictions. Borrowing money and placing a mortgage on an asset would contravene the borrowing and charge-over assets restrictions.

Arm's length dealings – employing a member, or relative of a member, in the business at a salary higher than an arm's length rate could contravene the arm's length provisions.

Collectables and personal use assets – these type of assets owned by the SMSF can't be displayed at the business premises. ■