# client alert | explanatory memorandum

March 2020

**CURRENCY:**

This issue of **Client Alert** takes into account developments up to and including 21 February 2020.

## Super guarantee loophole closed

A superannuation guarantee loophole that allowed employers to use salary sacrificed contributions to make up part of their required super guarantee contributions has been closed. From 1 January 2020, employers must make the full amount of mandatory super guarantee contributions and cannot use salary-sacrificed amounts to reduce those mandatory contributions. Depending on the types of employment agreements between employees and employers, this could mean more money for employees' retirement.

The concept of super guarantee – the requirement for employers to contribute 9.5% of an employee's salary or wages into a nominated super account – should be familiar to everyone, particularly anyone who is an employee, as it makes up the bulk of future retirement income. Employees may also be salary-sacrificing amounts of their salary and wages to put extra into their super.

Before this year, a loophole in the law meant that an employee's salary-sacrificed amounts could be counted towards employer contribution amounts. This allowed a potential reduction in employers' mandated super guarantee contributions – essentially working against the employee's intention to add extra to their super. In addition, employers were able to calculate their super guarantee obligations on the lower, post-sacrifice earnings base.

Depending on the type of employment agreement between an employee and employer, this meant that if the employee salary-sacrificed an amount equal to or more than the super guarantee amount the employer was required to pay, the employer could have chosen to not contribute any non-sacrifice amount and the legal requirements of the super guarantee would still be met. It's important to note that this was not the original intention of the law, and not all employers would make the choice to exploit this loophole; however, where they did, employees who salary-sacrificed could be short-changed and end up with lower super contributions as well as a lower salary overall.

The law has now been changed specifically to close this loophole. From 1 January 2020, amounts that an employee salary-sacrifices to superannuation cannot be used to reduce the employer's super guarantee charge, and do not form part of any late contributions the employer makes that are eligible for offset against the super guarantee charge. To avoid any possible shortfall in their mandatory super guarantee contribution payments, employers must now contribute at least 9.5% of an employee's ordinary time earnings (OTE) base to a complying super fund. The OTE base consists of the employee's OTE *and* any amounts they sacrifice into superannuation that would have been OTE if the salary-sacrifice arrangement wasn't in place.

The following simple example illustrates the effect of the old law versus the new law for an employee with an OTE base of $15,000.

| | **Old law** | **New law** |
|---|---:|---:|
| Employee's OTE | $15,000 | $15,000 |
| Super guarantee entitlement ($15,000 × 9.5%) | $1,425 | $1,425 |
| Salary-sacrifice contribution | $1,000 | $1,000 |
| Minimum compliant employer contribution | $425 | $1,425 |
| Total super contributions<br>(including salary-sacrificed amount) | $1,425 | $2,425 |

*Source: Treasury Laws Amendment (2019 Tax Integrity and Other Measures No 1) Act 2019.*

## ATO tackling international tax evasion

Australian tax residents are taxed in Australia on their worldwide income. While most do the right thing and declare all their income, some try to avoid paying tax by exploiting secrecy provisions and the lack of information-sharing between countries. As the world becomes more interconnected and barriers are broken down, it is inevitable that there are fewer places for the unscrupulous to hide from tax.

With the rise of the global economy and easy flow of money across borders, no country is immune to international tax evasion and money laundering. A recent coordinated effort with Joint Chiefs of Global Tax Enforcement (J5) shows that member countries, including Australia, are doing all they can to protect their tax revenue. This most recent investigation yielded evidence of tax evasion by Australians using an international institution located in Central America.

Tax chiefs from the J5 countries met in Sydney on 17–21 February 2020 to share information about common mechanisms, enablers and structures that are being exploited to commit transnational tax crime. The J5 was initially formed in 2018 to fight global tax evasion and consists of the tax and revenue agencies of Australia, United Kingdom, United States, Canada and the Netherlands. The countries share intelligence on international tax crime as well as money laundering.

The current international investigation started on information obtained by the Netherlands, which led to a series of investigations in multiple countries and concerned an international financial institution located in Central America whose products and services are believed to be facilitating money laundering and tax evasion for customers across the globe.

J5 members believe that through this institution, a number of clients may be using a sophisticated system to conceal and transfer wealth anonymously to evade their tax obligations and launder the proceeds of crime. The enforcement action consisted of evidence, intelligence and information-collecting activities such as search warrants, interviews and subpoenas.

According to the ATO, several hundred Australians are suspected of participating in these arrangements. The ATO is currently proceeding with multiple investigations with support from the Australian Criminal Intelligence Commission (ACIC). In addition, it is encouraging anyone with information about the scheme or other similar arrangements to contact the ATO.

ATO Deputy Commissioner and Australia’s J5 Chief, Will Day, has said, “this multi-agency, multi-country activity should degrade the confidence of anyone who was considering an offshore location as a way to evade tax or launder the proceeds of crime”.

While the J5 is a powerful tool, it is by no means the only one in the ATO’s arsenal. The ATO also has a network of international tax treaties and information exchange agreements with over 100 jurisdictions, and uses them to identify facilitators such as banks, lawyers and financial advisers. Once a pattern has been identified, such as a practitioner with a large number of clients using the same methods to avoid or evade tax, the ATO is likely to look closely at the entire client base.

In recent years over 2,500 exchanges of information have occurred, enabling the ATO to raise additional tax liabilities of $1 billion. The message from the ATO is that anyone with offshore income or assets is better off declaring their interests voluntarily. Those who do so may have administrative penalties and interest charges reduced.

It’s important to keep in mind that holding offshore assets is not just for the wealthy. Australians with migrant backgrounds may not even know they hold offshore assets in some cases, but those assets are still subject to tax law. For example, grandparents or other relatives may start a bank account in an Australian’s name in another country to make contributions celebrating a holiday, birthday or other life event.

*Source: www.ato.gov.au/Media-centre/Media-releases/Global-tax-chiefs-undertake-unprecedented-multi-country-day-of-action-to-tackle-international-tax-evasion/.*

## New measures to combat illegal phoenixing

New laws are now in place to target illegal phoenixing of companies, which by some estimates costs businesses, employees and governments more than $2 billion a year.

While there is no Australian legislative definition of “illegal phoenixing” or “phoenixing activity”, at its core it is understood as the use of serial deliberate insolvency as a business model to avoid paying company debts. To combat this, the new laws target a range of behaviours, including preventing property transfers to defeat creditors, improving accountability of resigning directors, allowing the ATO to collect estimates of anticipated GST liabilities and authorising the ATO to retain tax refunds.

### Property transfer to defeat creditors

New criminal offences and civil penalty provisions will apply to company officers who fail to prevent the company from making “creditor-defeating dispositions”, and to other persons (including pre-insolvency advisers, accountants, lawyers and other business advisers) who facilitate a company making a “creditor-defeating disposition". Liquidators and the Australian Securities and Investments Commission (ASIC) can seek to recover the assets for the company's creditors, and in some cases creditors can recover compensation from a company's officers and other persons responsible for making a "creditor-defeating disposition".

A "creditor-defeating disposition" is defined as disposing of company property for less than its market value (or less than the best price reasonably obtainable) that has the effect of preventing, hindering or significantly delaying the property becoming available to meet the demands of the company's creditors in winding-up. To ensure legitimate businesses aren't affected by this wide definition, safe harbour has been maintained for genuine business restructures and transactions made with creditor or court approval under a deed of company arrangement.

### Accountability of resigning directors

In order to reduce the instances of unscrupulous directors using loopholes to shift the blame, the new laws seek to prevent abandonment of companies by a resigning director or directors, leaving the company without a natural person's oversight. Practically, under the new laws, a director cannot resign or be removed by a resolution of company members if doing so would leave the company without a director (unless the company is being wound up).

In addition, if the resignation of a director is reported to ASIC more than 28 days after the purported resignation, the resignation is deemed to take effect from the day it is reported to ASIC. However, a company or director may apply to ASIC or the Court to give effect to the resignation notwithstanding the delay in reporting the change to ASIC.

### Collection of anticipated GST liabilities

Under the new laws, the ATO can now collect estimates of anticipated GST liabilities, including luxury car tax (LCT) and wine equalisation tax (WET) liabilities. The ATO can also recover director penalties from company directors to collect outstanding GST liabilities (including LCT and WET) and estimates of those liabilities.

### Retaining refunds

The new laws also allow the ATO to retain a refund to a taxpayer where that taxpayer has other outstanding lodgements or needs to provide important information.

*Source: Treasury Laws Amendment (Combating Illegal Phoenixing) Act 2019 (Cth).*

## Insurance payouts: are they taxable?

In recent months, parts of Australia have been battered by a combination of fire and floods. As people try to piece their lives together in the aftermath, insurance payouts can go a long way in helping rebuild homes and replace lost items. However, if you receive an insurance payout in relation to your business, home business or rental property you need to be aware there may be associated tax consequences.

For example, if you rent out your home or a portion of your home on a short stay website, you may be subject to capital gains tax (CGT) if you receive an insurance payout in relation to that home. Businesses that receive an insurance payment may be subject to varying tax consequences depending on what the payment is designed to replace.

Insurance payouts relating to personal property (including household items, furniture, electrical goods, private boats and cars) and your main residence are not taxed. If you keep a home office or run a business from home and you receive an insurance payout in relation to the property being damaged or destroyed, there may be CGT consequences.

Similarly, if you have a rental property or rented out a room of your main residence which later becomes damaged or destroyed and is subject to an insurance payout, you will need to include the insurance payout amount when you work out whether you have a capital gain or loss. This applies even if you were casually renting out a room, your home or (part of) your farm as short-stay accommodation.

For those operating a business, the tax consequences of an insurance payout are even more complicated depending on what the money received is for. For example, destroyed business premises come with CGT consequences, while any insurance amount you receive for repair of damage will need to be included in your assessable income.

If an amount is received in relation to damaged or destroyed trading stock, it must be included as assessable income. For any depreciating assets used in generating assessable income (eg office equipment), you will need to calculate the difference between the amount received from insurance and the asset book value of the asset at the time it was destroyed. Any excess needs to be included as assessable income, while a deduction can be claimed for any losses.

For depreciating assets in the low-value pool, you will need to reduce the closing pool balance by the amount of insurance payment you receive. In addition, the tax treatment will need to be modified if an asset was partly used to produce assessable income and in a low-value pool.

The tax treatment of insurance payments for work cars is similar to that of depreciating assets, except if you used the logbook method for claiming car expenses. If you used the logbook method, the balancing adjustment amount needs to be reduced by the percentage that you used the car for personal use.

Businesses that correctly informed their insurer of their GST status when they took out the insurance don't have to pay GST on insurance payout amounts and may be entitled to GST credits for purchases made with those amounts. Small businesses may also be entitled to CGT concessions.

*Source: www.ato.gov.au/individuals/dealing-with-disasters/damaged-or-destroyed-property/.*

## Australia's independent tax complaints investigator

Do you know who to turn to when you have a complaint about the ATO? Whether you're an individual or business, the Inspector-General of Taxation and Taxation Ombudsman (IGTO) should be your first port of call. The department has two distinct, yet intertwined, functions.

As the Taxation Ombudsman, the IGTO provides all taxpayers with an independent complaints investigation service. One of the main roles of the IGTO is that it must investigate complaints by taxpayers (or their representatives) where a tax official's actions or inactions, decisions or systems have affected them personally. As the Inspector-General of Taxation, it also conducts reviews and provides independent advice and recommendations to government, ATO and other departments.

The difference between the two functions is that the Taxation Ombudsman's investigations and recommendations are likely to be made privately, whereas when the office conducts reviews (not in response to a complaint) as the Inspector-General of Taxation, the investigations and recommendations are public and aimed at improving administration of the tax law.

In the first quarter of 2019–2020 the IGTO received 909 complaints – a 14% increase over the number for the same period in 2018–2019. Of the complaints received so far this year, 82.4% of the complaints received were from self-represented individuals, of whom approximately 10-12% were small business taxpayers. Taxpayers who had a representative were largely represented by a family member or friend, although around a third were represented by an accountant or a tax practitioner.

The top five issues raised in complaints for the quarter remain largely the same as the previous year, covering debt collection, payments to the taxpayer, lodgement and processing, communication, and audit and review. According to the IGTO, issues surrounding debt collection have featured consistently among the complaints lodged since the assumption of the Tax Ombudsman service.

While the IGTO has direct access to ATO officers, records and systems, it cannot investigate how much tax needs to be paid, provide advice regarding structure of tax affairs or assist with decisions made by other government agencies apart from the Tax Practitioners Board. The IGTO can investigate and assist taxpayers with issues including:

- extensions of time to pay;
- the ATO's debt recovery action;
- delays with processing tax returns;
- delays in ATO communication and responses;
- information the ATO has considered regarding taxpayers' matters;
- understanding the ATO's actions and decisions; and
- identifying available options and other relevant agencies that can help.

Taxpayers can approach the IGTO at any stage of their dispute with the ATO, although it is recommended that they first approach the ATO officer/manager assigned to their case, followed by the ATO complaints section, before lodging a formal IGTO complaint.

Complaints can be made online and via phone or post, and services are offered in languages other than English as well as for people who are hearing, sight or speech impaired. The IGTO will require:

- basic personal information including the taxpayer's tax file number (TFN);
- the main facts, relevant dates and supporting documents;
- an explanation of how ATO actions have caused concern and how those actions have affected the taxpayer; and
- information about what the taxpayer or their representative has done to try to resolve the complaint, the result to date, and the desired outcome from the complaint.

*Source: www.igt.gov.au/.*

## ATO scrutiny on car parking fringe benefits

The ATO has started contacting certain employers that provide car parking fringe benefits to their employees to ensure that all fringe benefits tax (FBT) obligations are being met. Generally, car parking fringe benefits arise where the car is:

- parked on the business premises of the entity providing the benefit;
- used by the employee to travel between home and their primary place of employment and is parked in the vicinity of that employment;
- parked for periods totalling more than four hours between 7 am and 7 pm; and
- a commercial parking station located within 1 km of the premises charges more than the car parking threshold amount.

Employers that meet these conditions are providing parking benefits and have a choice of three methods to calculate the taxable value of the benefits: the commercial parking station method, the average cost method and the market value method.

The method currently under ATO scrutiny is the market value method, which states that the taxable value of a car parking benefit is the amount that the recipient could reasonably be expected to have to pay if the provider and the recipient were dealing with each other under arm's length conditions. When using this method, the employer must obtain a valuation report from an independent valuer who has expertise in the valuation of car parking facilities and is at arm's length from the employer.

**TIP:** Specifically, the ATO is looking at employers that have engaged an arm's length valuer as required under the market value method. According to the ATO, it has information that valuers in some instances have prepared reports using a daily rate that doesn't reflect the market value and as such, the taxable value of the benefits is significantly discounted or even reduced to nil.

The ATO notes that just engaging an arm's length valuer does not mean you've met all the requirements for working out the taxable value of the car parking fringe benefits. It is the employer's responsibility to confirm the basis on which the valuation is prepared and examine any valuation that is suspected to be incorrect or considerably reduces FBT liability.

At a minimum, the ATO requires a valuation report to be in English and to detail the following:

- the date of valuation;
- a precise description of the location of the car parking facilities valued;
- the number of car parking spaces valued;
- the value of the car parking spaces based on a daily rate;
- the full name of the valuer and their qualifications;
- the valuer's signature; and
- a declaration stating the valuer is at arm's length from the valuation.

In addition to the valuation report, an employer also needs a declaration relating to each FBT year that includes the number of car parking spaces available to be used by employees, the number of business days, and the daily value of the car parking spaces.

*Source: www.ato.gov.au/Tax-professionals/Newsroom/Your-practice/Valuing-car-parking-fringe-benefits/.*

## Foreign residents and the main residence exemption

Laws limiting foreign residents' ability to claim the capital gains tax (CGT) main residence exemption are now in place. This means that if you're a foreign resident at the time of disposal of the property that was your main residence, you may not be entitled to an exemption and may be liable for tens of thousands in CGT. Some limited exemptions apply for "life events", as well as property purchased before 9 May 2017 and disposed of before 30 June 2020.

The restrictions apply to any person who is not an Australian resident for tax purposes at the time of disposal (ie when the contract is signed to sell the property).

According to the ATO, a person's residency status in earlier income years will not be relevant and there will be no partial CGT main residence exemption. Therefore, not only are current foreign residents affected, but current Australian residents who are thinking of spending extended periods overseas for work or other purposes may also need to factor in this change to any plans related to selling a main residence while overseas.

For current foreign residents, there may still be time to act. You can still claim the CGT main residence exemption if, when the CGT event happens to your property, you were a foreign resident for tax purposes for a continuous period of six years or less and during that time one of the following "life events" happened:

- you, your spouse, or your child under 18 had a terminal medical condition;
- your spouse or your child under 18 died; or
- the CGT event involved the distribution of assets between you and your spouse as a result of your divorce, separation or similar maintenance agreement.

Further, if you purchased your main residence before 7:30 pm (AEST) on 9 May 2017, you may still be entitled to the exemption provided you sell your home on or before 30 June 2020, subject to satisfying other existing requirements for the exemption. If you miss the 30 June window for disposal of the property in 2020, you will not be entitled to the main residence exemption unless one of the listed "life events" occurs within a continuous period of six years of becoming a foreign resident.

Similarly, for properties acquired at or after 7:30 pm (AEST) on 9 May 2017, the CGT main residence exemption will not apply to disposals from that date unless certain "life events" occur within a continuous period of six years of the individual becoming a foreign resident.

It's important to note that these changes apply even if you die – if you're a foreign resident for tax purposes at the time of your death, the same foreign resident restrictions will apply to your legal personal representatives, the trustees and beneficiaries of deceased estates, any surviving joint tenants and special disability trusts.

Since this law change is retrospective, the ATO requires foreign residents who acquired property at or after 7:30 pm (AEST) on 9 May 2017 to review their positions back to the 2016–2017 income year and seek tax return amendments where necessary. Foreign residents who purchased their property before 7:30 pm (AEST) on 9 May 2017 and who then dispose of their property after 30 June 2020 will only need to review their positions to the 2020–2021 income year.

The ATO has said it will not apply shortfall penalties and any interest accrued will be remitted to the base interest rate up to the date of enactment of the law change. Additionally, any interest in excess of the base rate accruing after the date of enactment will be remitted where taxpayers actively seek to amend their assessments within a reasonable timeframe of the law cming into force.

*Source: www.ato.gov.au/general/capital-gains-tax/international-issues/Foreign-residents-and-main-residence-exemption/.*

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