

m2.9C Specific Deduction Provision

Division 25 (Misc. Ded)	s25-5	Managing Tax Affairs/Tax Compliance (not directly related to assessable income)
	s25-10	Repair of Non-Captial Nature
	s25-20	Lease establishment Costs (asso with CAPEX)
	s25-25	Borrowing Cost (asso with CAPEX)
Division 28 (Car)	s.28-15	Method 1: Cents per KM
		Method 2: Log Book
Divison 30 (Gifts/Donat-ions)	s.30-15	*must be endorsed by the Commissioner (registered charity
	Key reqt:	(1)deductible gift recipient (2) gift amt >/+\$2 (3)no material benefit received in return
Division 36		
> Tax Loses of Prior Yrs	s.36.10	Current year surplus deductions Less Net Exempt Income
> Future Year Deduction	s.36-15	1. Apply CY deduction first 2. Appy carry-forward tax loses - after reducing by any Net Exempt Income from CY

m2.10C Specific Deduction Limit/Deny

Division 26	s.26-5	1.Fines and Penalties excluded
	s.26-10	3. Employee leave deferred
	s.26-35	2. Payments to related reduced
Division 32	s.32.5	No Deduction for Entertainment
Division 32	s.32-10	Ent. re: Bus Discussion ► Cannot Deduct
*Exception relating to Entertainment	s.32-20	Can deduct - FBT provisions



m2.10C Specific Deduction Limit/Deny (cont)

*Exception relating to Entertainment	subdiv 32B	Can deduct - table of Exceptions eg seminar, ent. industry exp, employer exp (in-house dining)
Division 35		Non-Commercial Business Losses
Division 820		Thin Capitalisation
Division 328		Prepayments for Services (and s.82KZMD ITAA36)

m2.10C.H Non-Comm'l Bus Losses - Div.35

1. Assessable Income Test	s.35-30	Assessable Income(incl. cap gains & bal. adjmnts) of atleast \$20k
2. Profit Test	s.35-35	Business has a profit in 3 out of past 5 years (incl CY)
3. Real Property Test	s.35-40	Value of real property used in the business has a total reduced cost base of \$500k. Excl dwelling (private use)
4. Other Assets Test	s.35-45	Value of depreciating assets, trading stocks, leased assets & int'l property excl. real property, car, motor cycles used on a continuity basis was at least \$100k

Step 1. Look at assessable Income and Other Income

Step 2 . Losses can be offset in the CY if ANY ONE of the four test above are met:

Step 3 Commissioner discretion

m2.10C.H Commerciality Test

Assessable Income Test	sec 35-30	AI from business including capital gain and balancing adjustment, is at least \$20k
------------------------	-----------	--



By ranele15

cheatography.com/ranele15/

Not published yet.

Last updated 7th October, 2023.

Page 2 of 18.

Sponsored by **Readable.com**

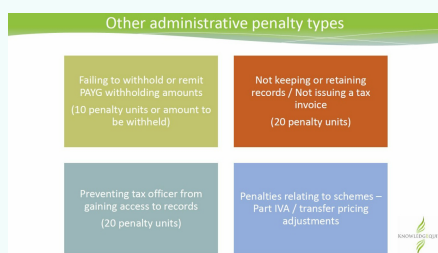
Measure your website readability!

<https://readable.com>

m2.10C.H Commerciality Test (cont)

Profit Test	sec 35-35	Bus activity resulted in profit in atleast 3 of the past 5 years incl CY
Real Property Test	sec 35-40	Real Property or Interest in RP, used in carrying on the business = Reduced Cost Base of \$500k or more . Excludes dwelling and its adjacent land that is mainly used for private purpose.
Other Assets Test	sec 35 - 45	Depreciating Assets, trading stock, leased assets and Intellectual property of business are valued at least \$100k . Excludes cars, motorcycle or similar vehicles.

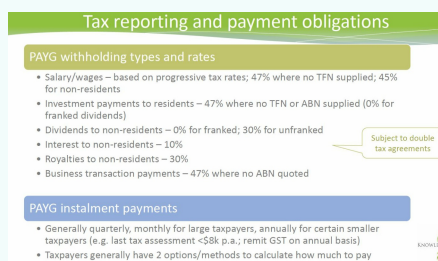
m1.1 Other Administrative Penalty Types



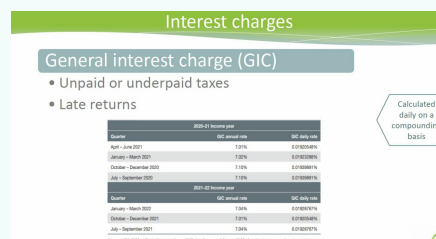
m1.10 PENALTY CATEGORY

Failure to Lodge on Time or In Approved Form	* Taxation Administration Act 1953 s.1 div. 286 * Penalty Units (\$222 from 01/07/2020)
False or Misleading Statement	* Taxation Administration Act 1953 s.1 div. 284 Base Penalty plus Adjustment

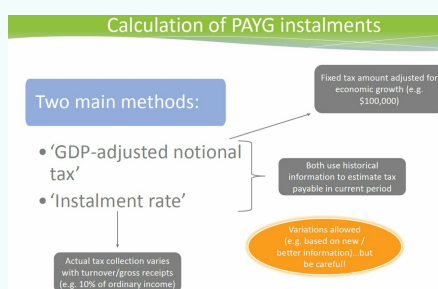
m1.9 PAYG Withholding & Installment Payment



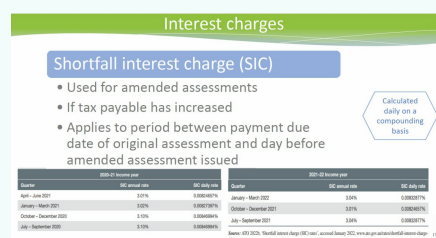
m1.10 GIC - General Interest Charge



m1.9 PAYG Instalment Calculation



m1.10 SIC (Shortfall Interest Charge)



m1.10 SIZE OF PENALTY_Failure Lodge

Size of penalty – failure to lodge

Entity	Penalty
Small	Base penalty 1 penalty unit per 28 day period or part thereof Limit 5 penalty units
Medium (\$1m-\$20m income / GST turnover)	Twice the base penalty
Large (>\$20m income / GST turnover)	Five times the base penalty

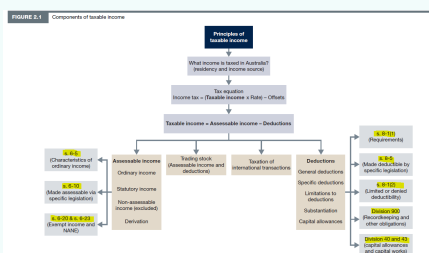
m1.10 PENALTY IN RELATION TO STATEMENTS

Penalty in relation to statements

Behaviour	BASE PENALTY if no shortfall (penalty units)	BASE PENALTY as percentage of shortfall	Shortfall adjustment (increase in base penalty amount)	Voluntary disclosure before assessment (adjustment to base penalty)	Voluntary disclosure during assessment (adjustment to base penalty)
Lack of reasonable care	20	25%	+ 20%	+ 50%	+ 20%
Recklessness	40	50%	+ 20%	+ 50%	+ 20%
Intentional disregard	60	75%	+ 20%	+ 50%	+ 20%
Lack of reasonably arguable position (para 30(1)(a))	25%	+ 20%	+ 50%	+ 20%	
Failure to make a statement	75%	+ 20%	None	None	None

Reduced to nil if shortfall < \$5,000

m2.0A - PRINCIPLE OF TAXABLE INCOME



m2.1A Residency for Individual

Residency for individuals

Section 6(1) ITAA36 – “Resident”

1. A person who is actually residing here within the normal meaning (behaving like a resident);
2. A person who is absent but has retained their Australian domicile and has not established a permanent place of abode in another country;
3. A person who has been present for more than half the income year and cannot satisfy the Commissioner that their usual place of abode is overseas and they do not intend to take up residence;
4. A person who is a member of a Commonwealth Government superannuation scheme (or their spouse/child under 16).

m2.2A Residency for Companies

Residency for companies

Section 6(1) ITAA36 – “Resident”

- Incorporated in Australia; or
- Carries on a business in Australia AND either:
 - Central management and control in Australia; or
 - Voting power controlled by Australian resident shareholders

Person listed or entitled to be listed on the register.
Not necessarily the ultimate owner or beneficiary.

m2.3A Source of Income

Source of income

Generally:

- Salary and wages = place of performance of services
- Income from immovable property = location of property

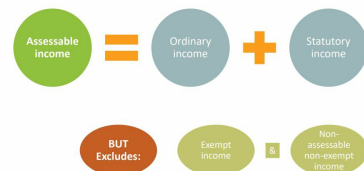
Other types of income depend upon facts and their relative importance

- Business income = place of contract/performance
- Interest = where obligation to pay arises / location of bank account
- Dividends = where profits arose
- Royalties = location of IP / outbound royalties have an Australian source

m2.4B - Assessable Income

Assessable income

Division 6 ITAA97: Assessable income



NOT Assessable Income - [ITAA97 s6.15]

1. Not Ordinary Income [ITAA97 s6-5] and Statutory Income [ITAA97 s6-10]
2. Exempt Income [ITAA97 s6-20]
3. NANE - non assessable and non-exempt income [ITAA97 s6-23]

m2.4A Characteristic of Ordinary Income

Characteristics of ordinary income

Comes to the recipient beneficially

- Income actually received or applied for the benefit of the taxpayer (doctrine of constructive receipt)
- Does not include unrealised gains

Cash or convertible into cash

- Barter transactions

Periodicity, recurrence and regularity

- Lump sums less likely to be ordinary income (but can be...)
- Income from business, property and personal exertion will generally be income even if received irregularly

Does not include capital amounts

Usually connected with a source:

- ACTIVE - e.g. Personal or Business Services
- PASSIVE - e.g. Income as returns on property /investment

m2.4B Characteristic of Ordinary Income

Characteristics of ordinary income

Compensation payments take on character of item/amount replaced

- Compensation for loss of wages / earnings / stock / minor contract = ordinary income even if a lump sum
- Compensation for loss of a capital asset / profit-making structure / key contract is not generally ordinary income even if paid in instalments

Does not include windfall gains

- Unless taxpayer is carrying on a business of gambling

Other

- Principle of mutuality – cannot derive income by dealing with yourself
- Includes illegal income
- Must be characterised as income in the hands of recipient (not the payer)
- Gifts – reward for services or for personal relationship?

m2.4B Compensation

Compensation

Event	Probable tax consequences
Loss of profits/trading stock	Income (revenue account) s. 70-115
Income replacement	Income (revenue account) s. 15-30
Loss of contract/agency	
• Ordinary business	Income (revenue account) – likely if business survives
• Business structure	Capital – if business operations cease as a result
• Special arrangements	Capital
• Severe restrictions	Capital
• Long period	Capital
Restrictive covenant	Capital

Questions of whether Revenue or Capital Compensation?

- Affects the underlying business structure?
- Normal trading risk for the type of business?
- Incidental to carrying on ordinary business?

m2.5B Statutory Income Provisions

Legislation – statutory income

INCOME TAX ASSESSMENT ACT 1997

PART 2-1-ASSESSABLE INCOME

DIVISION 15- SOME ITEMS OF ASSESSABLE INCOME

15.1 What this Division is about

15.2 Allowances and other things provided in respect of employment or services

15.3 Allowances and other things provided in respect of employment or services

15.4 Allowances and other things provided in respect of employment or services

15.5 Allowances and other things provided in respect of employment or services

15.6 Allowances and other things provided in respect of employment or services

15.7 Allowances and other things provided in respect of employment or services

15.8 Allowances and other things provided in respect of employment or services

15.9 Allowances and other things provided in respect of employment or services

15.10 Allowances and other things provided in respect of employment or services

15.11 Allowances and other things provided in respect of employment or services

15.12 Allowances and other things provided in respect of employment or services

15.13 Allowances and other things provided in respect of employment or services

15.14 Allowances and other things provided in respect of employment or services

15.15 Allowances and other things provided in respect of employment or services

15.16 Allowances and other things provided in respect of employment or services

15.17 Allowances and other things provided in respect of employment or services

15.18 Allowances and other things provided in respect of employment or services

15.19 Allowances and other things provided in respect of employment or services

15.20 Allowances and other things provided in respect of employment or services

15.21 Allowances and other things provided in respect of employment or services

15.22 Allowances and other things provided in respect of employment or services

15.23 Allowances and other things provided in respect of employment or services

15.24 Allowances and other things provided in respect of employment or services

15.25 Allowances and other things provided in respect of employment or services

15.26 Allowances and other things provided in respect of employment or services

15.27 Allowances and other things provided in respect of employment or services

15.28 Allowances and other things provided in respect of employment or services

15.29 Allowances and other things provided in respect of employment or services

15.30 Allowances and other things provided in respect of employment or services

15.31 Allowances and other things provided in respect of employment or services

15.32 Allowances and other things provided in respect of employment or services

15.33 Allowances and other things provided in respect of employment or services

15.34 Allowances and other things provided in respect of employment or services

15.35 Allowances and other things provided in respect of employment or services

15.36 Allowances and other things provided in respect of employment or services

15.37 Allowances and other things provided in respect of employment or services

15.38 Allowances and other things provided in respect of employment or services

15.39 Allowances and other things provided in respect of employment or services

15.40 Allowances and other things provided in respect of employment or services

15.41 Allowances and other things provided in respect of employment or services

15.42 Allowances and other things provided in respect of employment or services

15.43 Allowances and other things provided in respect of employment or services

15.44 Allowances and other things provided in respect of employment or services

15.45 Allowances and other things provided in respect of employment or services

15.46 Allowances and other things provided in respect of employment or services

15.47 Allowances and other things provided in respect of employment or services

15.48 Allowances and other things provided in respect of employment or services

15.49 Allowances and other things provided in respect of employment or services

15.50 Allowances and other things provided in respect of employment or services

15.51 Allowances and other things provided in respect of employment or services

15.52 Allowances and other things provided in respect of employment or services

15.53 Allowances and other things provided in respect of employment or services

15.54 Allowances and other things provided in respect of employment or services

15.55 Allowances and other things provided in respect of employment or services

15.56 Allowances and other things provided in respect of employment or services

15.57 Allowances and other things provided in respect of employment or services

15.58 Allowances and other things provided in respect of employment or services

15.59 Allowances and other things provided in respect of employment or services

15.60 Allowances and other things provided in respect of employment or services

15.61 Allowances and other things provided in respect of employment or services

15.62 Allowances and other things provided in respect of employment or services

15.63 Allowances and other things provided in respect of employment or services

15.64 Allowances and other things provided in respect of employment or services

15.65 Allowances and other things provided in respect of employment or services

15.66 Allowances and other things provided in respect of employment or services

15.67 Allowances and other things provided in respect of employment or services

15.68 Allowances and other things provided in respect of employment or services

15.69 Allowances and other things provided in respect of employment or services

15.70 Allowances and other things provided in respect of employment or services

15.71 Allowances and other things provided in respect of employment or services

15.72 Allowances and other things provided in respect of employment or services

15.73 Allowances and other things provided in respect of employment or services

15.74 Allowances and other things provided in respect of employment or services

15.75 Allowances and other things provided in respect of employment or services

15.76 Allowances and other things provided in respect of employment or services

15.77 Allowances and other things provided in respect of employment or services

15.78 Allowances and other things provided in respect of employment or services

15.79 Allowances and other things provided in respect of employment or services

15.80 Allowances and other things provided in respect of employment or services

15.81 Allowances and other things provided in respect of employment or services

15.82 Allowances and other things provided in respect of employment or services

15.83 Allowances and other things provided in respect of employment or services

15.84 Allowances and other things provided in respect of employment or services

15.85 Allowances and other things provided in respect of employment or services

15.86 Allowances and other things provided in respect of employment or services

15.87 Allowances and other things provided in respect of employment or services

15.88 Allowances and other things provided in respect of employment or services

15.89 Allowances and other things provided in respect of employment or services

15.90 Allowances and other things provided in respect of employment or services

15.91 Allowances and other things provided in respect of employment or services

15.92 Allowances and other things provided in respect of employment or services

15.93 Allowances and other things provided in respect of employment or services

15.94 Allowances and other things provided in respect of employment or services

15.95 Allowances and other things provided in respect of employment or services

15.96 Allowances and other things provided in respect of employment or services

15.97 Allowances and other things provided in respect of employment or services

15.98 Allowances and other things provided in respect of employment or services

15.99 Allowances and other things provided in respect of employment or services

16.00 Allowances and other things provided in respect of employment or services

- Specific amounts made assessable by the Act
- ITAA97 s6-10(1) - assessable income which includes amounts that are not ordinary income
- ITAA97 s.6-10(2) amount not ordinary income but included in AI by provision of assessable income

e.g. Net Capital Gains / Forex Gains / Insurance Bonuses

m2.6B Non Cash Business Benefits

Non-cash business benefits

Non-cash, non-convertible benefits are not ordinary income

- FC of T v Cooke and Sherden (holiday provided by supplier)

Statutory assessing provisions

- Non-cash business benefits – s.21A ITAA36

- Non-cash benefits from rendering services – s.15-2 ITAA97 (captured by FBT for employee relationships)

Case 1: Not Cash or Convertible into Cash > Generally NOT an OI > Arise from business relationship [s21A applies] > No exception applies (no entertainment provided by the client) > ARM's LENGHT VALUE (\$2,000) - INCLUDED IN ASSESSABLE INCOME

Case 2 ; Not Cash or Convertible into Cash > Generally NOT an OI > Arise from business relationship [s21A applies] > EXCEPTION applies [s.21A] - non deductible entertainment expense of supplier > Value of Non Cash Business Benefit is REDUCED TO NIL

m2.6B Exempt Income

Exempt income

Section 6-20

- An amount of ordinary income or statutory income is *exempt income* if it is made exempt from income tax by a provision of this Act.
- Ordinary income is also exempt income to the extent this Act excludes it (expressly or by implication) from being assessable income.

Exempt income is not assessable

- Exempt bodies – e.g. registered charities
- Specifically exempted – e.g. welfare, ADF allowances

Exempt income may have still have direct tax impact:

- No deductions allowed in deriving exempt income
- May reduce deduction allowable for overall tax loss
- Disposal of asset used to produce exempt income does not lead to a capital gain/loss

Tax

m2.6B NANE

Non-assessable non-exempt income

Section 6-23

- An amount of ordinary income or statutory income is *non-assessable non-exempt income* if a provision of this Act or another Commonwealth law states that it is not assessable and it is not exempt income.

e.g GST

Quiz: A registered charity sells donated goods thru opshop for \$110 incl GST.

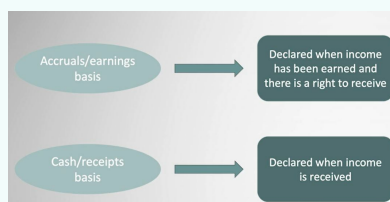
- * \$100 - Exempt income (registered charity) s.50-5
- * \$10 GST - NANE s.17-5(a)

Foreign investors will not be entitled to any franking credits on the FRANKED Dividends.

*wtax on franked dividends is Zero.

Dividends and Interest Income subject to WTAX, the net amount is now NANE [ITAA36 s128D]

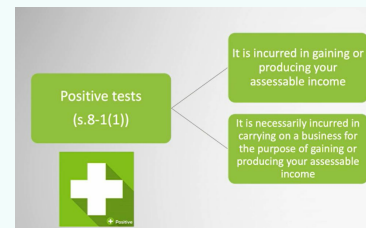
m2.7B Derivation



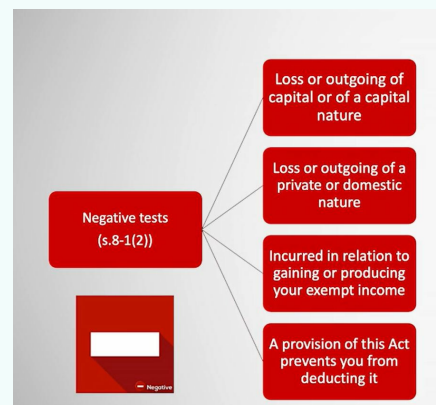
CASH basis - Passive Income (rent, interest, dividends) & Salary and wages

ACCRUAL basis - Business Income (large scale transactions & invoice issuance)

m2.8C General Deduction - Positive Limb



m2.8C - General Deduction - Negative Limb



m2.9C - Specific Deduction Provisions (sec 8-5)

Specific deduction provisions

- Div. 25 - miscellaneous deductions
- Div. 28 - cars
- Div. 30 - gifts & donations
- Div. 36 - tax losses of prior years
- Div. 40 - capital allowances
- Div. 43 - capital works

m2.10C - Specific Limitation to Deduction

Provisions that limit or deny

- Div. 26 - miscellaneous
- Div. 32 - entertainment
- Div. 35 - non-commercial business losses
- Div. 820 - thin capitalisation
- Div. 328 - prepayments for services [and s.82KZMD ITAA36]

m2.10C. - Loss Recoupment Rules - COT Period

Continuity of ownership test (COT)

- Strict test for private companies
- Same persons (individuals or through interposed entities)
- Own the same shares
- > 50% of the voting/distribution rights
- Throughout the 'ownership test period'

Tax Losses: start of loss year to end of recoupment year

Capital Losses: start of loss year to end of recoupment year

Bad debts: day the debt incurred to end of claim year

m2.10C. - Company Losses Key Element

1. Calculation of tax loss

Tax loss:

Deductions > [Assessable income + Net exempt income]

Ineligible deductions:

- Personal contributions to superannuation (s.290-150 ITAA97)
- Pensions, gratuities or retiring allowances (s.25-50 ITAA97)
- Gifts and contributions (Division 30 ITAA97)
- Conservation covenants (Division 31 ITAA97)

m2.10C. COT Addl Rules & Exceptions

Additional rules and exceptions:

- Same share ownership can still apply after share splits/consolidations
- Same share ownership can still apply after death
- Partial deductions permitted if COT satisfied for only part of the year
- Schemes to meet the COT to recoup tax losses can be disregarded
- Companies with unequal share rights can apply amended tests

m2.10C. - Synthesize Tax Loss

1. Calculation of tax loss

Synthesised tax loss:

- Gross tax payable = \$50,000
- Franking credit offset = (\$70,000)
- Franking credit excess = (\$20,000)

- Tax loss = Franking credit excess / Company's tax rate
- Tax loss = (\$20,000) / 27.5% = (\$72,727)

m2.10C. - WH Company & Div 166 Company

Widely held companies:

- Listed companies
- Unlisted companies with > 50 members (except where ≤ 20 people hold ≥ 75% of rights)

Eligible Division 166 companies:

- Widely held companies
- Superannuation funds
- Approved deposit funds (ADFs)
- Managed investment schemes
- Non-profit companies and charities

m2.10C. COT - WH Company & Div 166 Company

Simplified continuity of ownership test:

- 'Substantial' continuity of ownership
- Unbroken continuity throughout ownership test period not required
- > 50% of the rights satisfied at certain 'test times'

Test times:

- End of each tax year
- After certain corporate changes (e.g. takeovers, new share issuances)

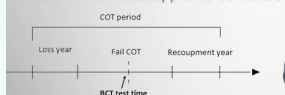
Ultimate ownership tracing:

- Not required to trace through ownership interests being < 10% of rights
- Wider range of entities deemed to be beneficial owners

m2.10C. Loss Recoupment Rules - BCT

Business continuity test (BCT)

- BCT irrelevant if COT is satisfied
- Test time is immediately prior to COT failure



BCT is done immediately after COT FAILED, which means, it is not the business of the last year is tested, only the business carried on immediately prior to the change of ownership

BCT is fulfilled if passed this 2 tests - Same & Similar Continuity Test

m2.10C. BCT SBT - Same Business Test

General SBT rules and principles:

- Must have carried on the same business for the full BCT period
- No new business or transactions:
 - can contribute to assessable income
 - can be commenced for the purpose of meeting the SBT
- The business must be the same business, not the same kind of business
- How the business is conducted is more relevant than who manages the business
- The internal operations and production should be the same; and
- The end use of the products or services should be the same.

m2.10C. BCT - Similar Business Test

Similar business test

- Operates in comparable way to SBT
- Removes the negative limbs relating to innovation and business development
- New business/transactions must be similar and be an extension or continuation of previous business activities

Similar business test factor:

1. Similarity between **assets** of former and new business.
2. Similarity between **activities** of former and new business.
3. Similarity of **identity** between old and new business
4. To what **extent** did a new **business evolve** from developments in old one?

m2.10C. Utilisation of Available Losses

Loss recoupment satisfied [COR or BCT] > can NOW Carry forward and utilise losses

First apply against net Exempt Income > Requirement

Apply any Remaining Tax Losses > Choice

Loss Deduction Rules:

- * Oldest available losses must be utilized first
- * No deduction can be made where excess franking credits exist
- * Deduction of losses cannot result in excess franking offsets.

m2.10C. Temp Loss Carry Back Tax Offset

Temporary loss carry back for companies

Carry back of tax losses to generate a refundable tax offset (Division 160)

- Company must carry on business and have aggregated turnover of less than \$5 billion in loss year
- Tax loss in 2019/20, 2020/21 or 2021/22 can be carried back to 2018/19, 2019/20 or 2020/21
- Loss carry back generates a refundable tax offset which cannot exceed the company's franking account balance at the end of the loss year

m2.10C.Temp Loss Carry Back Tax Offset - Case

Temporary loss carry back for companies

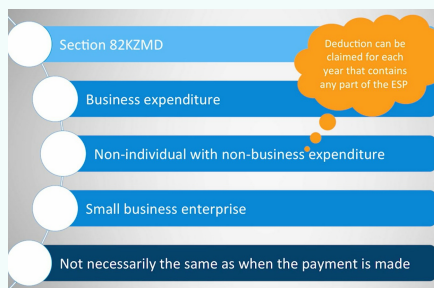
The financial records of Company A (tax rate of 30%) show the following:

	2020/21	2019/20	2018/19
Tax loss	(\$900 000)	-	-
Net exempt income	-	-	\$5 000
Taxable income	-	\$700 000	\$400 000
Tax paid (@30%)	-	\$210 000	\$120 000
Closing franking account balance	\$280 000	-	-
Loss carry back	(\$495 000)	(\$405 000)	-

Loss carry back tax offset for 2020/21:

- 2018/19: $(\$405\ 000 - \$5\ 000) \times 30\% = \$120\ 000$
- 2019/20: $\$495\ 000 \times 30\% = \$148\ 500$
- Total tax offset = $\$120\ 000 + \$148\ 500 = \$268\ 500$
(less than franking account balance in 2020/21 so not restricted)

m2.10C.G Prepayment - ITAA36 Prt III Sub.H



ESP - Eligible Service Period

* A loss or outgoing from an advance payment is usually incurred for s.8-1 purposes when paid (TR 97/7).

* Court have rarely applied the accounting principle matching principles.

* Exception for finance and insurance companies issuing discounted bills [Coles Myer Finance Ltd v FC of T]

m2.10C.G Prepayment - s. 82KZL Exclusion

Section 82KZL provides excluded expenditure from the prepayment deferral rules

Under this section, the rules do not apply to:

- Amounts less than \$1,000,
- Payment of salary and wages, or
- Capital expenditure.

82KZL ► falls under sec 8-1 (Gen. Deduction)

SBE who have NOT CHOSEN to apply s. 82KZMD
INDIVIDUALS with non-business expenditures

Full Deductions if: (1) Expenditure relates to ESP =< 12 months (no greater than 12 mths); and

(2) Ends by 30 June of the ff income year

Prorata if: ESP > 12 months

► Period in a year / ESP

eg George Ind, with passive rental income

m2.10C.H Non-Commcl Bus. Loss - Div. 35

Taxable income is less than \$250,000 and passes ONE of the four tests:

- Assessable income test
- Profits test
- Real property test
- Other assets test

Division 35 purpose - quarantine tax losses from non-commercial activity to prevent deductibility against unrelated assessable income (individual income).

Rules: 1. Carried Forward & 2. Deducted from any future income from that activity.

Applied to: (1) Individuals conducting a business (2) Sole Trader or Partner

Does Not Apply To: (1) Passive Investment Income (2) Hobbies**

m2.10C.I Thin Capital'n > Debt:Equity Ratio

The maximum allowable debt will be the greater of:

- Safe harbour debt amount
- Arm's length debt amount
- Worldwide gearing debt amount (noting that some entities may not be eligible to use this method)

Outward investor takes priority if also an inward investor (Foreign Controlled)

Debt attributed to foreign permanent establishment is excluded from adjusted average debt

Only Australian operations are subject to thin capitalisation rules

Debt Deduction (Interest & Finance chargers) against Assessable Income in Australia

m2.10C.I Thin Capitalisation-Safe Harbour

Calculate safe harbour debt amount (s.820-205)		
Average value Australian assets	$(\$50m + \$52m)/2 + (\$5m + \$5m)/2$	\$56m
Subtract associate entity debt	\$0 associate entity debt	(\$0m)
Subtract non-debt Australian liabilities	\$1m leave provisions	(\$1m)
Net Australian assets funded by debt and equity		\$55m
Safe harbour debt amount	$\$55m \times 60\%$	\$33m

m2.10C.I Thin Capital'n-Safe Harbour

Excess debt = Adjusted average debt – Maximum allowable debt*
 = \$40m – \$33m
 = \$7m

* Maximum allowable debt is the safe harbour debt amount in this example

Deduction disallowed = Debt deductions × (Excess debt / Average debt*)
 = \$3m × (\$7m / \$40m)
 = \$0.525m

* Average debt figure does not deduct loans to associates and controlled foreign entities

Allowed debt deduction = Debt deduction – Deduction disallowed
 = \$3m – \$0.525m
 = \$2.475m

Assets : Au Property 20x6 (\$50m) 20x7 (\$52m)

Au Plant 20x6 (\$5m) 20x7 (\$5m)

Liability: Bank loan 20x6 (\$40m) 20x7 (\$40m)

Leave Prov 20x6 (\$1m) 20x7 (\$1m)

Interest Expense - \$3mil

m2.10C.I Thin Capitalisation-Exceptions



Exception means **THIN CAPITALISATION DO NOT APPLY**

m2.10C.I Thin Capitalisation - Definition

Inward Investor	Foreign investor with Au Branch
Inward Investor	Foreign Controlled Resident Entity
Outward investor; not Foreign Controlled	Resident Co. with single overseas branch

m2.11C Substantiation - Work Expenses (900-B)

Work Expenses (900-B)

- Substantiation is generally required for work expenses
- Work expense (s.900-30): Loss or outgoing incurred to produce wages (*not* business income)
- If total work expense deductions < \$300, then no substantiation required (s.900-35) – reasonable explanation for each expense is sufficient
- If total laundry expenses < \$150, no substantiation required
- Travel > 6 nights: also keep a travel diary
 - Domestic:** no diary or substantiation required if 'reasonable' expenses are covered by travel allowance
 - International:** no substantiation of non-accommodation expenditures required if 'reasonable' expenses are covered by travel allowance; accommodation expenses must still be substantiated

m2.6C Substantiation-Car Expense (900-C)

Car Expenses (900-C)

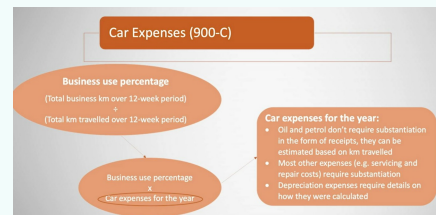
Cents per km method (s.28-25):

- Business kms x Prescribed rate
- Business kms = travelled in the course of earning income or between workplaces
- 2019-20 = 68c/km | 2020-21 = 72c/km
- Reasonable estimate; no substantiation
- Maximum of 5,000 business kms

Logbook method (s.28-90):

- Taxpayer must keep a logbook that records, for a 12-week period, the following details about every journey:
 - Work or private journey
 - Start and finish odometer reading
 - Total kilometers travelled

m2.6C Substantiation -Car Expense (900-C)



m2.6C Substantiation - Bus Travel Exp (900-D)

Business Travel Expenses (900-D)

- Travel expenses not related to producing heavy (e.g. for self-employed person's travels (s.900-95))
- As well as normal substantiation requirements, travel diary required if > 6 days away from home
- Work commenced receipt is an alternative for substantiating fuel or oil expenses
- Travel > 6 nights: also keep a travel diary
 - Domestic:** no diary or substantiation required if 'reasonable' expenses are covered by travel allowance
 - International:** no substantiation of non-accommodation expenditures required if 'reasonable' expenses are covered by travel allowance; accommodation expenses must still be substantiated

- **NO Allowance - ALL Expense** must be substantiated
- If substantiation is required and no receipt is received from supplier - taxpayer can create the invoice only when: (1) Expense =<\$10 and (2) Max. =<\$200 p.a.
- Can use bank statement if no date in the receipt
- If nature of the expense not stated, taxpayer can enter details

m2.14D Depreciation Flowchart

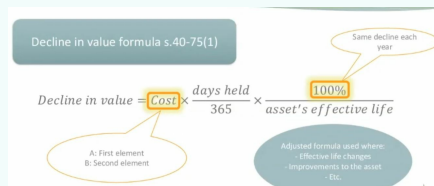


m2.14 Rental Properties Allowable Ded.

Rental properties

- Not a business, therefore:
 - No small business entity concessions
 - No COVID-19 depreciation concessions
- Can use:
 - Immediate deduction for assets costing ≤ \$300
 - Low value pool
 - Prime cost / diminishing value depreciation
 - Capital works deductions
- From 1 July 2017, no deductions for second-hand depreciating assets (s. 40-27):
 - purchased after 9 May 2017
 - used for a private purpose in 2016/17

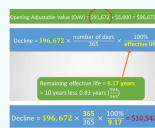
m2.14 s.40-75(1) - Prime Cost Method-



Straight Line Depreciation

First Year with second element

m2.14 s.40-75(1) - Prime Cost Method - Change



Change Year

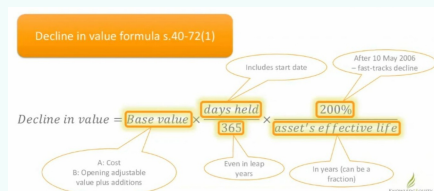
* Must adjust the formula in s.40-75(1) and it occurs in 2 situations:

1. Recalculate effective life; or
2. Include a 2nd element cost amount in a year after the installation year..

Effective Life = 9.17years

= 10 years - 0.83 years (304/365)

m2.14 s.40-72 - Diminishing Value Method



Can be used on Assets held post 9th May 2006

Diminishing Value Method Not Eligible for intangible assets (**except** for Copyright)

First Year ► Base Value = Asset's Cost

Sub Years ► Base Value = Opening Adjustable Value + New Second Element Costs

m2.14 s.40-72 Diminishing-Value Method

Most intangible assets are not eligible for DVM.

Tangible Asset (not acquired from associate) second-hand auction subject to DVM.

Tangible Asset (acquired from associate) so long that taxpayer is using DVM - continue using same method.

Second element costs are not depreciated separately but form part of the base value.

Any changes to the effective life during a year affects the calculation for that entire year onwards – that is, that there is no pro-rata decline calculation for part of the year.

Key Notes

m2.14 s40-72 Diminishing Value - Change



Sub Year ► **Base Value** = Opening Adjustable Value + New Second Element Costs

= \$83,343 + \$5,000

= \$88,343

For a Change of Effective Life = **Calculated for the Entire Year**, No prorata decline calculation for part of the year

m2.14 Depreciation Choice of Method

Once you have elected to use a method then you cannot change

You cannot choose if:

- Relates to intangibles (other than copyright) – use prime cost
- You acquire an asset from an associate – use their previous method
- Asset is allocated to the low value pool – use the pool method

m2.14D Non-SBEs - Assets of \$300< s.40-80

An immediate deduction is available for non-business depreciating assets instead of calculating decline in value, s.40-80

- Cost less than or equal to \$300; and
- Asset predominantly used for earning assessable income that is not income from carrying on a business; and
- Is not part of a set of assets where total costs are greater than \$300; and
- Total with any substantially identical assets is not greater than \$300.

m2.14 Non-SBEs Low Value Asset Pool

Low-Cost Assets (addon)	s. 40-425(2)	cost < \$1,000.00	(18.75%) 1st yr of available-for-use
Low-Value Assets	s. 40-425(5)	opening adjustable value (OAV) < \$1,000; more than \$300.00	(37.50%) previously depreciated while the opening adjustable value (OAV)

*Low-Value Assets - assets subjected to Diminishing Value and later on the balance is <\$1,000.00

Pool Decline in Value (opening adjusted value) + Allocated Asset Decline in Value (newly add-on)

Balancing Adjustment -(sec 40-445) subtract the taxable used % of the termination value from the closing balance. Pool Value cannot go below **ZERO** and the balance goes to Assessable Income.

m2.14D Non-SBEs Low Value Pool - Exercise

Low-value pool – Exercise			
Solution:			
Pool Opening Adjustable Value (OAV)	\$20,000		
Add taxable proportion of low-cost assets allocated	\$640	\$800 × 80%	
Add taxable proportion of low-value assets allocated	\$640	\$800 × 80%	
Add taxable proportion of second element costs	\$0		
Less decline in value of OAV	(\$7,500)	\$20,000 × 37.5%	
Less decline in value of low-cost assets allocated	(\$120)	\$640 × 18.75%	
Less decline in value of low-value assets allocated	(\$240)	\$640 × 37.5%	
Less decline in value of second element costs	\$0		
Less taxable proportion of asset sold (50%)	(\$100)	\$200 × 50%	
Closing pool balance	\$13,320		

Case:

Pool opening adjustable value (OAV) is \$20,000.

\$800 low-cost asset and low-value asset with OAV of \$800 added to pool, both with 80% taxable purpose.

No second element costs incurred in the year.

One pooled asset used 50% for a taxable purpose sold this year for \$200.

m2.14D Non-SBEs Low-Value Asset Pool

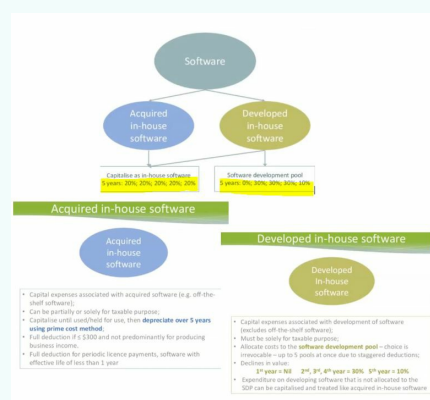
Key Notes:

Remember that low-cost or low-value assets can be allocated to the pool.

In the year in which they are added, the decline in value is calculated using a rate of 18.75% for low-cost assets and 37.5% for low-value assets.

Any second element costs to either of these assets declines at 18.75% in that year of entry. In subsequent years, the pool decline is calculated using a rate of 37.5% on the opening pool balance.

m2.14D Software Development Pool



Intangibles Effective Life

* In-house software = 5 years

* Registered design = 15 years

Acquired asset from associates - use the same

m2.14D Non-SBEs Balancing Adjustment

Balancing adjustment event

- Stop holding a depreciating asset (e.g. disposal, theft)
- Stop using or having installed and never intend to use again
- Not used a depreciating asset and decides never to use
- Change in composition of a partnership holding an asset

(Subd 40-D)

Assessable Income = Termination Value > Adjustable Value

Deduction = Termination Value < Adjustable Value

*Reduced for any non-taxable use of asset

Termination Value s40-300

1. Generally, what you receive in respect of the event (sales proceed or insurance claim)
2. Can be deemed market value (when not dealing at arm's length)

m2.14D Non-SBE- Relief Involuntary Disposal

Relief for involuntary disposal

- Available where depreciating assets cease to be held due to being lost, destroyed, or compulsorily acquired
- Taxpayer can choose:
 - Include a balancing adjustment in assessable income; or
 - Apply some or all of the balancing adjustment as a reduction in the cost of a replacement asset
- Relief only available where replacement asset:
 - Is acquired within certain time frames (i.e. 1 year prior/after)
 - Is held/used/installed ready for use, wholly for a taxable purpose, by the end of the year of expenditure and an amount can be deducted for it

Rollover Relief

- * Available where depreciating assets are transferred bet certain related entities (and CGT rollover relief is available)
- * Rollover relief simply ignores a balancing adjustment (deferred)
- * The tax attributes are transferred to another entity along with the asset.

m2.14D Non-SBEs Rollover Relief

Rollover relief

- Available where depreciating assets are transferred between certain related entities (and CGT rollover relief is available)
- Rollover relief simply ignores a balancing adjustment (deferred)
- The tax attributes are transferred to another entity along with the asset

m2.15D Temporary Full Expensing - Covid19

Temporary Full Expensing

- Allows full write-off for eligible assets first held at or after Budget Time 6 October 2020
- 'Temporary' means it does not apply to assets first used or installed for taxable purposes after 30 June 2023
- For asset eligibility and exclusion rules, see temporary full expensing
- Aggregated turnover < \$5 billion (<\$50 million for second-hand assets)
- Immediate deduction of business portion
- Only applies for assets first held and used (or installed ready for use) from 6 October 2020
- Can choose to opt out on an asset-by-asset basis using simplified depreciation
- Deduction of small business pool balance at 31 2021, 30 June 2022 (now also extended so the deduct pool as at 30 June 2023).

m2.16D Project Pool Expenditure



m2.17D Non-SBE Blackhole Expenditure

Blackhole Expenditure

- Some business capital expenditure was neither deductible, depreciable, nor included in cost base of a CGT asset.
- In a "blackhole" for tax purposes – no way of "claiming"
- Some costs may be deductible (s 40-880(2)):



s40-880(2)

m2.17D SBEs - Blackhole Expenditures

Special capital allowances

Start-up Expenditure

- Available to SBEs (note aggregated turnover threshold for this is \$50 million rather than \$10 million) and certain non-businesses
- Capital expenditure related to a **proposed business**
- Must be for:
 - Professional advice or services (e.g. on structure or operation); or
 - Tax, charge or fee paid to government agency for establishment

Small business startup costs
(deduct in year incurred)



Normally Blackhole Expenditures is spread over 5 years.

SBE start-up costs can deduct in year incurred.

m2.18 SBEs - Capital Allowances (optional)

Simplified Asset Pooling

Immediate Write-Off for Low-Cost Assets

cost threshold - asset costing **less than \$150k**

Temporary Full Expensing (TFE) - 06 Oct 2020 7:30pm

Covid19 temporary measure- to be fully written off irrespective of its balance (2020-21, 2021-22 & 2022-23)

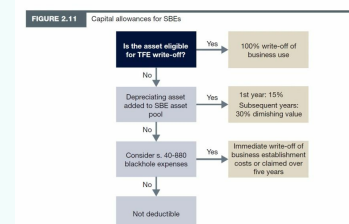
Requirements:

- * it carries on a business that year; and
- * its aggregated **turnover is less than \$10 million**.

Relevant Considerations:

- * What is the taxable use percentage for the relevant assets?
- * Does the taxpayer have existing assets that have previously been depreciated?
- * Are new assets at or below the threshold for immediate write-off
- * What are the permitted rates of decline for pooled assets?

m2.18D SBE Cap Allow - Diagram



m2.18 SBE Capital Allowances

Low cost asset not initially pooled
Adjustable value = zero (after cost is deducted)
Second element cost in future year < \$150,000
Immediate deductions allowed (for first 12 months)

Asset	Cost	Residual value at 12 months	Decline rate
Asset 1	\$150,000	\$90,000	57.5%
Asset 2	\$25,000	Nil	Nil

However, addition is more than the threshold ► SBE Pool

Asset	Cost	Residual value at 12 months	Decline rate
Asset 1	\$150,000	\$90,000	57.5%
Asset 2	\$25,000	Nil	Nil

Future cost additions < \$150,000
\$25,000 < \$150,000 < \$150,000
No additional cost to the SBE Pool

m2.18 SBE Capital Allowance - Close Pool Balance

Opening pool balance	
ADD TP% allocated assets	
ADD TP% cost additions	
LESS TP% termination value	
LESS decline 30% of pool opening balance	
LESS decline 57.5% of allocated asset values	
LESS decline 15% of allocated cost additions	
EQUALS closing pool balance	

If acquired post 12 March 2020 and first used/installed ready for use (for a taxable purpose) between 12 March 2020 and 1 July 2021 (normally 15% for other periods)

* if the Terminated Value puts the Closing balance to Zero = the excess will be included in Assessable Income

* If the Closing Pool Balance is < the instant asset write-off threshold (\$150k) ► Immediate Deduction

m2.18 SBE Capital Allow - First Elect for SBE Pool

Rates:

- 15% - used for assets in the **first year** they are allocated
- 30% - decline rate for **pool opening balance**
- 18.75% - low-value pool decline rate when low-cost assets are **initially pooled**.
- 37.5% - 30% - low value pool rate applied to the **previous year's closing pool**

m2.18D Capital Allow - SBE First Elect

Item	Cost	Rate	Allowance	Balance
Initial pool	100,000	15%	15,000	85,000
Subsequent pool	100,000	18.75%	18,750	66,250
Subsequent pool	100,000	37.5%	37,500	28,750

m2.19 Capital Works (ITAA97 Div 43)

Buildings or extensions including alterations or improvements to the building

Alterations and improvements to leased buildings including shop fittings

Driveways, fences and retaining walls

Earthworks

Div 43 - Capital Works - Generally - **SUBJECT** from CGT

Div 40 - Capital Allowances ► **EXEMPT** from CGT (if fully used for taxable purposes)

m2.19 Capital Works - Formula

Formula	Result
$\text{Deduction} = \text{Cost} \times \text{Rate} \times \text{Years}$	100,000 × 15% × 10 = 150,000

Deduction Rate is based on the **date construction commenced** but

Deductions are **only available** from the *Date Construction was **completed** (assuming the asset is used for income producing or R&D)

m2.19D Rate of Deduct - Capital Works

Rate determined by date construction started	Rate
e.g. begun after 26 Feb 1992	2.5%
• 2.5% basic entitlement (i.e. over 40 years)	2.5%
• Residential and non-residential, income-producing buildings	2.5%
• R&D buildings	2.5%
• Structural improvements	2.5%
• 4% entitlement (i.e. over 25 years) for:	4%
• Short-term traveller accommodation	4%
• Buildings used for industrial activities	4%

m2.21E Trading Stock - Adjustment s.70-35

Trading stock deducted for tax purposes when **purchased**

Cost of Goods Sold expense **reduces** net profit

Add-back accounting-based COGS for tax purposes

Stock **Closing** > Opening ► Adjusted to **Assessable Income**
 Stock Closing < Opening ► Adjusted to **Deductions**

Stock On Hand Valuation on each item/per item:

1. at cost
2. at market selling value
3. at replacement value

m2.21E Trading Stock - Exercise

DVD Players: Technological advances; Sales fallen considerably; Reduce sale price to \$100

Item	Qty	Cost (ea)	Replacement price (ea)	Market selling price (ea)	Closing value (total)
Tablets	30	\$200	\$200	\$400	\$6,000
Televisions	20	\$750	\$750	\$1,400	\$14,000
DVD Players	15	\$1,500	\$1,500	\$100	\$1,500
				Closing value	\$21,500

BUT: Obsolete stock provision (s.70-50)
 Can be written down to lower value – must be 'reasonable'



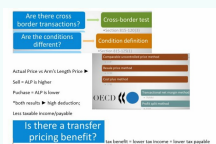
m2.24E Trading Stock - Special Rule

Issue	Treatment
Disposal not in the ordinary course of trading – donations, gifts to family / friends, sale of business	• Include market value at date of disposal in assessable income
Notional disposal of trading stock – change in constitution of a partnership	• Include market value at date of change in assessable income • Election can be made to use trading stock value in certain circumstances
Cease to hold item but still own it – take for own personal use	• Include cost price at the date of transfer in assessable income
Stock lost or destroyed	• Include compensation in assessable income.
Death of owner	• Include market value in assessable income • Election can be made in certain circumstances

m2.24E Trading Stock - SBE Concession

Eligibility	Concessions
Carry on business	No stock take of each item
<\$50m aggregated turnover	No individual valuation
Stock value variation ≤ \$5k	Balance changes not in TI

m2.25E International Transactions Process



if there's a transfer price benefit, the Commissioner will substitute the arm's length price for tax purposes:

1. taxable income - income tax
2. capital gains/losses - that attracts CGT

m2.26 Double Tax Arrangement - DTA

DTA, Tax convention, Double tax treaty
• Bilateral agreement between two countries • Provides obligations to apply tax laws in accordance with negotiated terms • Purpose: "the avoidance of double taxation and prevention of fiscal evasion with respect to taxes on income" • DTAs override other provisions in domestic taxation law
How double taxation arises
1. One country taxes income based on residence of recipient, while another taxes income based on its source 2. Taxpayer may meet the residency requirement of two jurisdictions
Two key principles of DTAs
1. Taxing rights are based on the country of residence 2. Other income taxed based on source (if double taxation arises, then tax credit granted by resident country)

m2.27E Withholding Tax Regime

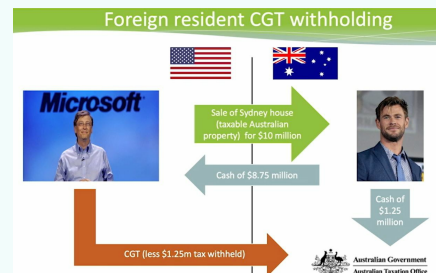
Key elements

- Flat rate withheld by the payer and remitted to the ATO
- Excluded from assessable income of non-resident (NANE income)

Withholding tax rates

- Dividends: 30% (15% DTA rate), no withholding on franked dividends
- Interest: 10% (10% DTA rate)
- Royalties: 30% (10% DTA rate)
- Capital gains: 12.5% (contract price ≥ \$750k) if foreign resident seller

m2.27E Foreign Resident CGT Withholding - Exercise



Rates Applied:

*Capital Gains = **12.5%** (contract price ≥ \$750k) if foreign resident seller

m2.29E Foreign Currency Conversion

1. Conversion of foreign currency

Core rule: Amount of foreign currency to be translated to AUD (s.960-50)

- Australian income tax liability to be calculated in a common unit of account
- Applies to ordinary income, expenses, obligations, liabilities, valuations, etc
- Specific times of conversion, depending on type of amount
 - E.g. Ordinary income: earlier of time of derivation, or receipt
 - E.g. General deduction: earlier of time deduction incurred, or paid
- Exchange rates published by Reserve Bank of Australia or (prior to 1 January 2020) ATO.
- Some permitted modifications:
 - E.g. Same as per audited financial report, daily rates or average rates (if appropriate)

m2.29E Forex REalisation Event (s.775)

5 MAIN TYPE OF FRE (FOREX REALISATION EVENTS):

1. FRE 1 – when you dispose of FX, or a right to receive FX, to another entity.
2. FRE 2 – when you cease to have a **right** to receive FX (otherwise than through disposal to another entity).
3. FRE 3 – when you cease to have an obligation to receive FX.
4. FRE 4 – when you cease to have an **obligation** to pay FX.
5. FRE 5 – when you cease to have a right to pay FX.

s775 - Forex Realisation is under a Revenue Account:

1. Forex **Gain** ► **Assessable Income**
2. Forex **Loss** ► **Deductions**

m2.29E Forex Tax Treatment - FRE

Foreign exchange realisation event (FRE)	Examples
FRE 1 – Disposal of foreign currency or right to receive foreign currency (s.775-40)	• Taxpayer converts amount of foreign currency into Australian dollars (CGT Event A1)
FRE 2 – Ceasing to have a right to receive foreign currency (s.775-45)	• Taxpayer receives repayment of foreign currency-denominated loan • Taxpayer receives foreign currency payment from trade debtor
FRE 3 – Ceasing to have an obligation to receive foreign currency (s.775-50)	• Taxpayer closes out a derivatives contract
FRE 4 – Ceasing to have an obligation to pay foreign currency (s.775-55)	• Taxpayer repays a foreign currency-denominated borrowing • Taxpayer makes foreign currency payment to trade creditor
FRE 5 – Ceasing to have a right to pay foreign currency (s.775-60)	• Taxpayer exercises an option contract

m2.29E Forex Realisation Event - #02

Sales income	GBP 1,000 / 0.47
(derived when invoiced)	= AUD 2,127
Amount received	GBP 1,000 / 0.45
	= AUD 2,222
Forex Realisation Event 2	AUD 2,222 – AUD 2,127
	FRE 2 Gain = AUD 95
	Assessable income (s.775-15)

Events arise from:

1. the **Right** expires - e.g., withdrawal from the foreign currency-denominated account
2. the **Right to Receive** is extinguished. cash is received from overseas debtor under sales contract denominated in foreign currency.

m2.29E Forex Realisation Event - #04

Stock purchase deduction	USD 1,000 / 0.65
(debt incurred per s.8-1)	= AUD 1,538
Amount paid	USD 1,000 / 0.70
	= AUD 1,428
Forex Realisation Event 4	AUD 1,538 – AUD 1,428
	FRE 4 Gain = AUD 110
	Assessable income (s.775-15)

Event Sample:

1. the **Obligation** expires
2. the Forex currency is **Paid** e.g. Obligation to pay is extinguished.

m2.29E Exception to Div 775

Short-term forex gains and losses on the acquisition of capital assets are an exception to the Division 775 rules and the gain instead will reduce the cost base (and reduced cost base) of the capital asset. For non-depreciating capital assets, this is the case when the time between the date of acquisition and the due date for payment is less than 12 months.

