THE ADVANCED DIPLOMA IN INTERNATIONAL TAXATION

June 2021

MODULE 2.01 – AUSTRALIA OPTION

SUGGESTED SOLUTIONS

PART A

Question 1

Mariana is treated as an Australian resident taxpayer for the year ended 30 June 2021 and is accordingly taxed on all assessable including ordinary income, derived directly or indirectly from all sources, whether in or out of Australia, during the income year: per Section 6-5(2) of ITAA 1997. However, an amount is not assessable income for tax purposes if it is exempt income, as it is excluded: Section 6 20 of ITAA 1997. Consultant's fees of $250,000 are fully assessable at marginal rates, after accounting for any allowable deductions, rebates, credits or charges.

A compensation payment is exempt income relates where a "personal injury lump sum" or "personal injury annuity" awarded to the taxpayer and specific conditions are met: Section 54-45 of ITAA 1997. Cases such as Allsop v FCT (1965) 113 CLR 341 and McLaurin v FCT (1961) 104 CLR 381 stand for the principle that an undissected lump sum payment made in settlement of compensation claims, where no part of the payment can be attributed to any particular claim, then the whole sum is on capital account.

A payment for a wrong or injury suffered is also exempt from capital gains tax, where a taxpayer is awarded compensation for any wrong or injury suffered. Broadly to be exempt, a payment must satisfy the conditions of Section 118-37 of ITAA 1997.

Land and property are a CGT asset (Section 108-5 of ITAA 1997) and a disposal of a CGT asset is a CGT event. Any net capital gains from the sale of an investment property in New Zealand is taxable for Australian Tax purposes and included in assessable income. An exception only applies if Mariana is eligible to claim a main residence exemption (section 118-B of ITAA 1997). Rental income derived from New Zealand property is generally assessable income for an Australian resident taxpayer.

Bitcoin is considered as a kind of property for Australian tax purposes (per section 108-5 of ITAA 1997) and hence profits are taxable under the CGT provisions, where it is not being part of a business transaction or trading stock. A discounted capital gain would be included in assessable income (Division 115).

Rental receipts constitutes income according to ordinary concepts, and is assessable for tax purposes in Australia in the year of receipt, notwithstanding it was sourced in New Zealand (section 4-15 of the ITAA 1997).

Question 2

The entities, Aquarius Pty Ltd and Exploro Pty Ltd form a Joint Venture (JV) for tax purposes, which is not a separate legal entity. Whether it is a partnership depends on the tax interpretation in section 995-1(1) of ITAA 1997; which defines a partnership as an association of persons carrying on business or in receipt of ordinary or statutory income jointly, or a limited partnership.

Unlike a partnership an unincorporated JV does not lodge a tax return and each joint venture entity returns its share of net income and claims those expenses that each entity outlays. Neither a joint venture or a partnership pays tax, however the partners pay tax on their share of any income received jointly.

The general tax deductions provisions of section 8-1 ITAA 1997 broadly apply to a mining business Joint Venturers. In addition, there are also specific mining provisions in Division 10 of the ITAA 1997, which allows an alternative deductions claim in an income year where it's reasonable to conclude that mining for minerals or quarrying operations were carried on (section 40-730).

All amounts outlayed by Aquarius Pty Ltd, which are necessarily incurred for carrying on a business, once a business has commenced- are considered deductible expenditure, including wages, rental, marketing and surverys. Equipment may be an item of capital expenditure and depreciable; or allowable under the specialised mining provisions.

Explora Pty Ltd may claim expenses generally or specifically provided for under tax law. Exploration expenses may be deductible under the general provisions. There is however a special category of expenditure that includes activities that are either reasonably incidental to, or closely connected with exploration or prospecting. Expenditure of a revenue or capital nature may qualify for a deduction under subsection 40-730(1) of ITAA 1997. Deductions for exploration and prospecting includes…" geological mapping, geophysical surveys...and systematic search for areas containing minerals and search for quarry materials by drives, shafts, cross-cuts, winzes, rises and drilling." (sub- section 40-730(4)).

The issue under the general provisions of the tax laws for alternate hydrogen technology production is whether it is in the usual course of business, or a new or even separate business. Expenditure must be necessarily incurred in carrying on that business, or it takes on the character of capital expenditure and is not deductible. Expenses on feasibility reports, tax structuring options, and logistics studies suggests it is prior to any actual new business starting up and may have an enduring benefit character.

The next consideration is whether it qualifies as part of integrated mining operations. Any new venture such as hydrogen technology that is not "on" mining operations would be outside the specialised mining provisions of Division 40.

PART B

Question 3

Taxation is levied at individual or entity level for any entity or individual engaged in the carrying on a business.

Sub leasing payments to a Maxine at market rates is considered ordinary and assessable income for taxation purposes and any related expenses are allowable deductions. The definition of 'assessable income' is provided by sections 6-5 of ITAA 1997 to include all ordinary income received directly or indirectly, which includes being paid on behalf or for the benefit of. This means that payments of monthly rental owed to a landlord, but paid by direction to another entity remain assessable to Maxine.

The timing of receipt is dealt with under subsection 6(4) of ITAA to be (4) derived by Maxine as soon as it is …"applied or dealt with in any way", on Maxine's behalf or as directed. The indirect income receipt doesn't affect Maxine'e deduction for the full fixed costs of gas and electricity of $1,000 per month notwithstanding it would be paid on her behalf by Fred.

Legal expenses for lease preparation of rental property would fall for consideration under section 8-1 of the ITAA 1997. However, section 25-5 limits general deductions if they are expressly limited or capital expenditure.

Question 4

Income received from a sub-lessee Fred is considered as income according to ordinary concepts and subject to tax (per section 6-5 of the ITAA 1997). Under this arrangement Maxine does not change her small business status for tax purposes.

Under a legal partnership, each partner may be joint & severally liable for the debts of the partnership and will split the profits to be as taxable income. A partnership is not a legal entity for tax purposes and the partnership share of net profits is returned in the individual tax return.

A company is a separate legal entity and taxed at the entity level.

PART C

Question 5

A business owner is responsible for registering for GST purposes with the ATO if business turnover exceeds the $75,000 threshold or is likely to exceed it. The ATO advises that if you've just started a new business and expect it to earn $75 000 or more in its first year of operation, you should register for GST.

The standard rate of GST is 10%.

Australian client fees of lawyer's enterprise are subject to GST as normal taxable supplies (per section 9-5 of A New Tax System (Goods and Services Tax) Act 1999) ("GST Act"). Overseas client fees should be GST-free as GST export of services (per section 38-190 of GST Act), as non-resident outside Australia and/or use is outside Australia (i.e. items 2 or 3).

Where the lawyer buys a computer costing $1,100, including GST, that GST component is one-eleventh of the sale price, and hence the price is inclusive of a GST ($100) amount paid. Lawyer is able to claim a GST credit of $100 for the GST included in the sale price of the computer, being ..."the amount of the input tax credit for a creditable acquisition is an amount equal to the GST payable on the supply" per section 11-25 of GST Act.

If at the end of the year the GST credits are higher than the amount of GST paid to the ATO, a GST refund is available to be claimed.

Question 6

Gift deductibility is covered in Division 30 of ITAA 1997.

Broadly a gift deduction needs to meets four conditions:

- You make it to a deductible gift recipient (DGR);
- It must truly be a bona fide donation and not a voluntary transfer of money or property where which results in a benefit or advantage;
- It must consist of money or property, which includes financial assets such as shares; and
- The gift donation can be verified by a receipt.

Question 7

The Fringe Benefits Tax Act 1986 brings to account tax on benefits paid to employees and associate.

The relevant provisions for Expense Paid Fringe Benefits are contained in Division 5 of the FBTAA 1986. These apply where a provider (employer) either makes a payment in discharge of an obligation of a recipient employee, or reimburses an amount of expenditure incurred by that recipient then it is taken to be an Expense Paid Fringe Benefit (section 20). Where the energy bills are from a product that the employer provides its termed an in-house expense paid fringe benefit.

The taxable value of the benefit paid by the employer is the amount of the actual payment unless the otherwise deductible rule applies. This occurs where the recipient was otherwise entitled to a once- only deduction for the such expenditure if paid directly (section 24 FBTAA 1986). Household energy costs are unlikely to fall into this deductible category as being private and domestic costs.

The FBT valuation rules differ depending on whether Energyco normally supplies the energy goods on a retail or non-retail basis and whether the goods are identical or merely similar. However, a de minimus rule applies where expenditure is under an allowable limit. There is a tax free threshold for in-house fringe benefits provided to employees during the FBT year, so that aggregate values of the in-house fringe benefits may be reduced by $1,000.

Question 8

Under the Promoter Penalty (PP) regime of Division 290 of ITAA 1997, an entity that obtains a scheme benefit when engaged in prohibited conduct under a tax exploitation scheme; being an arrangement proposal, plan or course of conduct. The scheme will have to be implemented in a way materially different and contrary to a product ruling.

Depending on the facts & circumstances, the ATO may look to the entity to provide an undertaking to rectifying its conduct by recompensing the participants. This is the quickest way to resolve ant dispute. If this is not an option, then more formal sanctions and remedies available to the Commissioner are: Federal Court voluntary undertakings, statutory injunctions or civil penalties.

Defences to an ATO action under the PP regime are that it was caused by a reasonable mistake, such as, that it was reasonably arguable application of the law, or reliance on advice given by the Commissioner's agents or publications (section 290-55).