

Tax News, Views and Clues

Assessability of Property Distributions by Companies

The Tax Office has issued a taxation ruling which deals with distributions of property from a company to its shareholders.

The ruling provides that where the money value of the distributed property exceeds the amount debited to a share capital account of the company, the excess constitutes a dividend to be included in the assessable income of the shareholder to the extent that it is paid out of profits derived by the company.

➤ **TIP:** The Tax Office considers that, provided the market value of the property exceeds the total liabilities and share capital of the company, the excess will generally be paid out of profits, regardless of the accounting treatment by the company. A dividend would therefore arise.

For example, where the excess amount is debited to an account or reserve that is not a share capital account, the excess may still be included in the shareholder's assessable income regardless of whether it is described as a 'profit and loss' account in the company's accounts.

Attribution of Personal Services Income

The Tax Office has released a new ruling outlining its views on the specific application of personal services income (PSI) measures in certain circumstances.

Broadly, these measures prevent individuals from reducing their tax by alienating their PSI to an associated entity in order to facilitate income splitting, access to the corporate tax rate or to claim business deductions.

Where the PSI measures apply, PSI is included in the assessable income of the relevant individual notwithstanding that it may have been derived by a private company or trust. However, if the income is from conducting a personal services business, the PSI rules do not apply.

The ruling covers the following:

- how the PSI rules apply;
- how amounts distributed from a PSI entity are not taxed twice; and
- how the PSI rules will apply to transactions between entities in certain circumstances.

➤ **TIP:** There are certain tests for determining whether a personal services business is being conducted in which case the PSI rules will not apply. There is a personal services business if one of the conditions below apply:

1. The 'results test' is satisfied. This test is based on the criteria for distinguishing independent contractors from employees. Please refer to the article below.
2. Less than 80% of the PSI is from one source and one of the following additional tests are satisfied:
 - an unrelated clients test — services are provided to two or more unrelated clients as a result of offers to the public;
 - employment test — other entities are engaged to perform at least 20% of the principal work; or
 - business premises test — the entity has exclusive use of separate premises in deriving its PSI.
3. A personal services business determination is obtained from the Commissioner.

Please contact us for further information.

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Dismissal Settlement Amount an ETP

The Federal Court has rejected a taxpayer's claim that a settlement amount received following an unfair dismissal action was a payment for personal injury or a bona fide redundancy payment. Rather, the Court held that the payment was an ordinary eligible termination payment (ETP).

An ETP is a lump sum payment received in consequence of the termination of employment. It can consist of several components. Where an ETP includes a bona fide redundancy amount, the payment is tax free up to a certain limit. The tax-free amount for 2002/03 is \$5,623 plus \$2,812 for each year of completed service with the relevant employer. Amounts in excess of this limit are assessable as ordinary ETPs.

The Court agreed in this case that the settlement amount had been received in consequence of the taxpayer's termination. However, it was not satisfied that the termination was the result of a bona fide redundancy. Instead it concluded that the amount represented statutory compensation for an unjust termination and therefore no part of it was exempt from tax as a bona fide redundancy payment.

The Court also rejected that any part of the termination payment was for personal injury. According to the Court, personal injury encompasses injury or disease of a physical or psychological nature. However, in this case, it did not extend to the anxiety and depression suffered by the taxpayer.

As a result, the full settlement amount received by the taxpayer was assessable as an ETP.

Employee v. Contractor

Whether a person is an employee or a contractor can be a difficult question to answer. An employer/employee relationship is more commonly referred to as a contract of services, whilst a contract for services typifies the relationship between a principal (recipient of services) and a contractor (provider of services).

The answer to the question will impact not only income tax, but also GST, superannuation, workers compensation and payroll tax.

Over time certain indicia have emerged to assist in determining whether a person is an employee or a contractor including, for example, the ability of an employer to direct performance, the ability of the service provider to subcontract the work, the existence of entrepreneurial risk for the service provider and the issue of who provides the necessary tools and/or equipment.

Overall, and perhaps most importantly, it's a question of whether the individual is engaged to produce a result, or to work as directed.

➤ **TIP:** Due to the complexity in some cases, and the important tax implications, we suggest that advice be sought where the issue is unclear.

ASIC: Annual Returns No Longer Required

From 1 July 2003, reforms to the Corporations Act will mean that companies are no longer required to lodge an annual return with ASIC where no changes are required to their company details.

Under the reforms, companies will be sent their company details by ASIC for review annually (generally within two weeks of the anniversary of registration).

If changes are required, companies can lodge a new form 484 (Change to company details) via the ASIC web site, via registered agents or in paper form.

The reform will also involve the replacement of the annual return fee with an annual review fee. ASIC will be introducing more payment options.

Medical Expenses Tax Offset

The medical expense tax offset threshold for the 2002/03 income year is \$1,500 (previously \$1,250).

Accordingly, taxpayers will be entitled to claim as a deduction 20% of net medical expenses above \$1,500.

Contact us for further information.

General Interest Charge: July-Sept 2003

The Tax Office has announced that the general interest charge (GIC) rate for September 2003 quarter is 11.78%, up from 11.75% for the previous quarter.

Common BAS Mistakes

With increasing GST audit activity, small businesses should take particular care when preparing their BAS form to avoid the scrutiny of the Tax Office.

Common mistakes to avoid include:

- failing to report GST on asset sales and intercompany transactions;
- omitting cash transactions when calculating GST liability;
- claiming input tax credits for purchases from suppliers who are not registered for GST; and
- failing to report GST on non-monetary transactions such as contra-deals.

Important: This is not advice. Clients should not act solely on the basis of the material contained in this Bulletin. Items herein are general comments only and do not constitute or convey advice per se. Also, changes in legislation may occur quickly. We therefore recommend that our formal advice be sought before acting in any of the areas. The Bulletin is issued as a helpful guide to clients and for their private information. Therefore it should be regarded as confidential and not be made available to any person without our prior approval.