

Tax News, Views and Clues

Tax-effective Investment Scheme

In a recent Federal Court decision, a taxpayer was disallowed deductions arising from a sandalwood plantation investment scheme on the basis that the general anti-avoidance rules in Part IVA of the *Income Tax Assessment Act 1936* applied.

As part of the scheme, the taxpayer was required to make payments to the promoter totalling \$80,000 for the purchase of seedlings.

The taxpayer claimed deductions for \$80,000, which generated tax refunds that funded two initial cash payments to the promoter of \$14,000 each. The balance of the \$80,000 investment was to be paid on completion of the project.

The Court found that \$3,000 was a reasonable purchase price for the seedlings, not \$80,000.

The Court noted that the promotion of the tax-effectiveness of the project had a significant influence on the taxpayer's decision to participate in the scheme, especially as the tax refunds were to fund the initial payments and the taxpayer would incur no real cash outgoing.

The Court held that Part IVA applied to the seedling purchase and that the dominant intention of the taxpayer was to obtain a tax benefit. Consequently, the deductions were denied.

➤ **CAUTION:** Although the scheme in this case did not come with an ATO product ruling, investment schemes of this type often do. An investor can rely on a product ruling to determine whether or not a tax deduction from an investment is available. However, a product ruling only applies if the promoter implements the arrangement in the manner specified in the product ruling. Investors may seek assurance from the promoter that this has been done.

Shareholder Loan Reviews

The Tax Office has announced that it will review loan arrangements between private companies and their shareholders (or associates), checking for compliance with Division 7A of the *Income Tax Assessment Act 1936*.

Loans that do not comply with Division 7A may be deemed to be taxable dividends for shareholders and result in losses of company franking credits.

It is understood that the Tax Office will initially send letters to selected private companies asking them for the following information:

- the names and addresses of all shareholders;
- copies of company loan accounts;
- copies of loan agreements;
- calculations of interest charged on each loan;
- details of repayments made;
- copies of financial statements; and
- other particulars of loan transactions.

We will keep you informed of further developments.

Strata Titling of Residential Property

The Tax Office has recently changed its view on whether the strata titling of a residential property makes the strata-titled property 'new residential premises'.

The Tax Office previously held that the strata titling of existing residential properties, notably residential apartments, turned them into new residential premises.

This meant that the subsequent sale of a newly strata-titled unit by an entity registered for GST would be a taxable supply and the vendor would pay 1/11th of the sale price in GST — if this could not be passed on to the purchaser.

The Tax Office now acknowledges that the strata titling of residential premises does not in itself create new residential premises.

The effect of this change is that, generally, the sale of a strata-titled residential property by an entity registered for GST will be an input taxed supply and no GST liability will apply.

Partnership Capital Gains

The Tax Office has issued an interpretive decision (ID) confirming that the capital gains tax laws apply when a partner contributes an interest in land to the capital of a partnership.

The ID covers situations in which two individuals acquire one block of land and subsequently contribute the land to a partnership of four individuals (including themselves).

The ID notes that when a partner contributes assets into a partnership, the partner disposes of part of their interest in the property to the new partners. Consequently, the landowners must determine whether a capital gain or loss has arisen on the disposal.

- **TIP:** When there is a partial disposal of an interest in an asset, the cost base of the asset must be apportioned.

Contact our office for assistance.

Commissioner Loses Part IVA Case

In a recent case, the Full Federal Court held that the Part IVA

general anti-avoidance rules did not apply to an investment arrangement entered into by a taxpayer, because the deductions she claimed were not allowable under the general deduction provisions.

The taxpayer invested in a cattle-breeding project and paid for management services, lease payments and interest. She claimed deductions for these payments in her 1995 and 1996 income tax returns; these deductions were later disallowed by the Commissioner, who argued that Part IVA applied.

The Court held that the amounts were capital in nature and hence not deductible, and that accordingly Part IVA could not apply.

Although the payments were capital in nature and not deductible, the Commissioner was out of time in amending the 1995 assessment. Accordingly, the taxpayer was successful in claiming the deductions.

Dividend and Interest Statement

Companies must lodge a statement showing details of any dividends and interest paid during the financial year that ended on 30 June 2002.

Companies with a 30 June 2002 year end must lodge the statement by the due date for lodgement of their tax return (but not later than 15 May 2003).

Companies with an approved substituted accounting period must lodge the statement by 31 October 2002 or the due date for lodgement of their tax return, whichever is later.

Companies do not need to report interest paid to financial institutions or to the Tax Office (e.g. general interest charge).

- **TIP:** The Tax Office has released a sample dividend and interest statement, which details the information that must be provided in the statement. Taxpayers may view the sample statement on the ATO's web site.

Who's Watching the Tax Office?

The Federal Government has introduced a new Bill into Parliament which aims to establish an independent statutory office of Inspector-General of Taxation.

The Inspector-General of Taxation would have the authority to:

- conduct reviews of the tax administration system, invite submissions from the public, and advise the Government on ways the tax system can be improved; and
- demand documents and take evidence from tax officials.

Calls for Changes to Enhance R&D

The Federal Government has been asked by the Federation of Australian Scientific and Technological Societies to revise the eligibility requirements for businesses wanting to use R&D tax concessions and also to expand the concessions which currently exist.

In particular, the Government has been asked to:

- provide better incentives for companies to conduct R&D by having a sliding scale of deductions for increased levels of R&D;
- reduce CGT rates for long-term venture capital investments; and
- allow trusts to use R&D concessions.

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. This firm respects your privacy. You have received this communication because your details are currently included on our mailing list. If you wish to be removed from our mailing list and receive no further communications of this nature in the future, please contact our office.