

## CLIENT ALERT

November 2006

### Tax News, Views and Clues

#### Valuing Trading Stock in Retail and Wholesale Industries

The Tax Office has recently released Taxation Ruling TR 2006/8, which applies to taxpayers who elect to value their trading stock on hand at the end of an income year at 'cost' for the purposes of section 70–45 of the *Income Tax Assessment Act 1997* (ITAA 1997).

The ruling provides that when this election is made, the cost of each item of trading stock will include all direct and indirect expenditure incurred in relation to making the item available for sale.

This valuation method is usually known as absorption costing and requires that costs incurred in the normal operation of a business (such as freight or insurance) be included in the final stock value amount.

#### Carrying on a Business From Home

The Tax Office has recently released a guide for taxpayers who carry on a business from their home.

The guide discusses the taxpayer's obligations and other issues that need to be considered when operating a business from home.

Some of these issues include:

- the implications of operating a hobby business as opposed to a business (for profit);
- choosing the right structure to operate within; and
- registration obligations of the taxpayer.

The full guide is available on the ATO's website at:  
<[www.ato.gov.au/print.asp?doc=/content/43191.htm](http://www.ato.gov.au/print.asp?doc=/content/43191.htm)>.

#### AAT Hears GST Anti-avoidance Case

In a recent decision (*VCE and FCT* [2006] AATA 821), the Administrative Appeals Tribunal (AAT) handed down its first case in relation to the anti-avoidance provisions in Division 165 of the *A New Tax System (Good and Services Tax) Act 1999* (the GST Act).

The taxpayer, VCE, entered into an agreement to acquire a commercial property from its sole director for the sum of \$770,000 (GST inclusive).

The purchase price was payable in instalments, the first instalment being for \$550, with the final payment of \$727,450 being payable in June 2018. As VCE registered to account for GST on a non-cash basis it lodged a BAS showing a

capital purchase of \$770,000 and claiming input tax credits of \$70,000. On the other hand, the vendor, who was registered to account for GST on a cash basis, declared GST of \$50, being the GST on the deposit of \$550.

The issues considered by the AAT were:

- whether the anti-avoidance provisions in Division 165 of the GST Act disallow the input tax credit of \$70,000 claimed by the taxpayer (VCE); and
- if so, whether the penalty on the shortfall amount of \$70,000 was properly imposed at the rate of 50%.

The AAT affirmed the Commissioner's decision to prohibit input tax credits totaling \$70,000 claimed by the taxpayer and to impose a penalty of \$35,000.

#### Shorter Review Period: For Loss or Nil Tax Liability

The *Tax Laws Amendment (Improvements to Self Assessment) Act (No. 2) 2005* introduces changes adjusting the amendment period for loss and nil liability assessments.

Previously, when a taxpayer lodged a nil tax liability return, the taxpayer would have an unlimited period of review.

However, the amending legislation changes the amendment period for loss and nil liability assessments to the same as positive liabilities. This period will be either two or four years, depending on the complexity of the taxpayer's affairs.

For income tax returns lodged for the 2004/05 year that include relevant loss information about earlier loss years, the Tax Office will have six years from lodgment of the return to issue an assessment for those years, as part of the transitional provisions to the amending legislation.

This limited period of revision will only apply if the 2004/05 income tax return disclosed the relevant loss information for earlier losses. If this information has not been provided, the loss returns for the earlier years will continue to be subject to an unlimited period of review.

## Common Errors in Trust Tax Returns

The Tax Office has recently identified some errors commonly made in trust tax returns. These errors include:

- **Tax losses carried forward**  
Carried-forward losses are not allowable if there is income at item 21.
- **Zeros in trust return labels**  
Zeros are not necessary and should not be added as this will slow the return process.
- **Non-taxable**  
The Tax Office will not issue a notice of assessment for both original and amended assessments if

a trust is assessed as non-taxable.

- **Date of birth**  
If the beneficiary is not a person, the date of birth label should not be completed.
  - **Assessment calculation codes (V codes)**  
Taxpayers and tax agents to choose the correct V code for every beneficiary in the statement of distribution.
  - **Non-resident and minor beneficiaries**  
Income will be raised as an assessment payable by the trust.
  - **Non-resident beneficiaries' additional information**  
Label K is to be completed by all taxpayers to inform the Tax Office of income that is assessable.
- **TIP:** when lodging trust returns, ensure they have been closely reviewed by your tax advisor.

## Compensation Payment Assessable as Ordinary Income

In a recent decision the AAT held that payments made in respect of a taxpayer's injury at work were assessable as income.

The taxpayer sustained various injuries at work and, as a result, ceased manual labouring. His work contract was terminated shortly afterwards, as it was deemed he was no longer fit to return to active work.

The taxpayer commenced litigation with regard to the injuries sustained at work and was awarded various amounts of compensation, including two sums of aggregated arrears

payments to compensate for weekly earnings.

The Commissioner assessed these sums as ordinary income.

The taxpayer appealed the amended assessment. However the AAT held that the two amounts were payments of ordinary income and the Commissioner's assessment was upheld.

## Superannuation Contributions Not Deductible

In a recent decision, the AAT held that contributions made by a taxpayer to a complying superannuation fund were not deductible.

The taxpayer originally enquired about making contributions to her employer's superannuation fund by way of salary sacrifice and was advised by her solicitor that this was not possible.

Taking the advice of her solicitor, the taxpayer made contributions to a company that she owned, for her own benefit. The contributions made to this company were claimed as allowable deductions.

The Commissioner disallowed the taxpayer deductions and issued amended assessments with regard to the contributions.

In addition, the contribution amounts were completely excluded from the assessable income of the fund.

The AAT upheld the Commissioner's decision to disallow the deduction on the grounds that the contributor and fund member are ultimately the same person.

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.